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SUPREME COURT
OF THE STATE OF WASHINGTON

STEVEN AND KAREN DONATELLI, a married couple,

Respondents,

v.

D.R. STRONG CONSULTING ENGINEERS, INC.,

Appellant.

SUPPLEMENTAL BRIEF OF APPELLANT
D.R. STRONG CONSULTING ENGINEERS, INC.

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ORIGINAL

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A. INTRODUCTION

In two landmark decisions, *Eastwood v. Horse Harbor Foundation, Inc.*, 170 Wn.2d 380, 241 P.3d 1256 (2010) and *Affiliated FM Ins. Co. v. LTK Consulting Services, Inc.*, 170 Wn.2d 442, 243 P.3d 521 (2010), this Court replaced the economic loss doctrine, a principle that attempted to differentiate the line between damages in tort and contract, with the independent tort duty doctrine that similarly sought to identify the line of demarcation between damages in tort and contract. In so doing, this Court did not specifically overrule the many prior decisions of the Court and lower courts applying the old economic loss doctrine.

This case offers the Court an opportunity to clarify the reach of the new independent tort duty doctrine and to offer an appropriate articulation of the rule that differentiates damages in tort from damages arising out of a breach of contract. Not every breach of contract should subject a defendant to damages in tort merely because an attorney can portray a breach of contract as a tort claim.

In this case, D.R. Strong Consulting Engineers, Inc. (“Strong”) is a civil engineering and surveying firm. Strong had a contract with developer Steve Donatelli. As in this Court’s decision in *Berschauer/Phillips Const. Co. v. Seattle School District No. 1*, 124 Wn.2d 816, 881 P.2d 986 (1994), *review denied*, 135 Wn.2d 1010 (1998)

the independent tort duty doctrine should not afford the developer a remedy in tort where the contract between Strong and the Donatellis articulated in detail the commercial expectations of those parties in the construction setting and the Donatellis' claim against Strong involves only commercial losses arising out of Strong's performance of its contractually-based services.

B. ISSUE PRESENTED FOR REVIEW

Is a developer's claims against a civil engineer for negligence and negligent misrepresentation barred under the independent tort duty where the contract between the civil engineer and developer clearly articulated the commercial expectations of the parties and only sought recovery for commercial loss, as distinct from personal injury and personal damages, as in this Court's *Berschauer/Phillips* decision?

C. STATEMENT OF THE CASE

Steven and Karen Donatelli owned property in King County they wanted to develop into two short plats (the "Project").¹ The Donatellis signed a written agreement with Strong to perform six phases of civil engineering services for the Project. The agreement, signed by Steven Donatelli, was extensive, describing in detail Strong's work to be

¹ The facts are set forth in detail in *Donatelli v. D.R. Strong Consulting Engineers, Inc.*, 163 Wn. App. 436, 261 P.3d 664 (2011), *review granted*, 173 Wn.2d 1025 (2012). *See also*, CP 2-3.

performed, the likely time required for the work and the fees. CP 21-26. With respect to any costs or delays, the agreement stated that probable construction costs and time were an opinion only, not guaranteed by Strong. CP 23. Moreover, Strong's liability to the Donatellis was addressed in the agreement and limited in scope:

LIMITATIONS OF PROFESSIONAL LIABILITY: DRS' findings, recommendations, specifications, or professional opinions will be presented, within the limits prescribed by the Client, after being prepared in accordance with generally accepted professional engineering and surveying practice. DRS makes no other warranty, either expressed or implied. For any injury or loss on account of any error, omission, or other professional negligence, the Client agrees to limit DRS and/or its professional employees' liability to the Client and to all agents, contractors, and subcontractors arising out of the performance of our professional services, such that the total aggregate liability to all those named shall not exceed \$2,500, or our fee, whichever is greater. In the event the Client does not wish to limit our professional liability to this sum, we shall waive this limitation upon the Client's written request made at the time of the initial authorization on a given project, provided that the Client agrees to pay for this waiver an additional 5% of our total fee or \$500, whichever is greater.

In the event the Client makes a claim against DRS and/or its staff at law or otherwise, for any alleged errors, omission, or other act arising out of the performance of our professional services, and the Client fails to prove such claim or prevail in an adversary proceeding, then the Client will pay all costs incurred by DRS and/or its professional staff in defending itself against the claim, including all attorney's fees.

CP 26. Strong's fee was set at \$33,150. CP 23.

King County issued a preliminary approval for the Project in October 2002 valid for five years, CP 28-37, but completion was delayed and the preliminary approval expired in October 2007. CP 2-3. Thereafter, with Strong's assistance, King County issued a new preliminary approval for the Project. CP 46, 93. But in 2008 the financial markets crashed. CP 3. The Donatellis were unable to finish the Project. *Id.* They ran out of money and lost the property to foreclosure. *Id.*

Blaming Strong for the delayed completion and loss of the Project, the Donatellis sued Strong to recover commercial losses that they alleged exceeded \$1,500,000, pleading various claims, including claims for negligence and negligent misrepresentation. CP 5. They alleged commercial loss only; this case does not involve personal injuries to anyone or property damage to the Donatellis' property.

D. SUMMARY OF ARGUMENT

This case affords the Court an opportunity to address the scope of the independent tort duty concept it adopted in *Eastwood* and *Affiliated*.

Washington law, both decisional and statutory, recognizes a difference between the measure of damages in tort and contract. Early decisions addressing the former economic loss doctrine, like *Berschauer/Phillips*, a case analogous to the present case, applied the risk of harm analysis to determine whether commercial loss damages may be sought in

negligence. The Court should reaffirm the principle that risks implicating the safety of persons or property are within the ambit of negligence, while those risks that implicate no more than commercial expectations are within the ambit of the law of contracts.

E. ARGUMENT

(1) Washington Law Has Correctly Recognized That Contract and Tort Serve Distinct Roles

This Court has consistently acknowledged that the law of contracts and torts serve distinct roles in ordering relationships and the claims they spawn, and has consistently declared that the boundary between them should be preserved. The Court noted the distinction between tort and contract damages most recently in *Elcon Constr., Inc. v. Eastern Washington University*, ___ Wn.2d ___, 273 P.3d 965 (2012), referring to the independent duty doctrine as “an analytic tool used by the court to maintain the boundary between torts and contract.” *Id.* at 969.²

(a) Decisions of This Court

In a long line of cases, beginning with *Stuart v. Coldwell Banker Commercial Group, Inc.*, 109 Wn.2d 406, 745 P.2d 1284 (1987), this Court has maintained the distinction between contract and tort recoveries

² The Court there determined that the independent tort duty analysis did not apply to a fraud in the inducement claim. Both the majority and the concurring opinions agreed the plaintiff failed to establish the elements of fraud or the tort of intentional interference with a contractual relationship.

in the construction setting. There, this Court refused to recognize a cause of action for negligent construction against a builder. *Id.* at 417-21. Instead, the Court held that warranty liability governs claims for construction defect. The Court explained that injuries including physical harm invoke “the safety-insurance policy of tort law” which is distinguished from “the expectation-bargain protection policy of warranty law.” *Id.* at 421. The Court reaffirmed that principle and the need for a differentiation between damages in tort and contract in *Atherton Condominium Apartment-Owners Assn. Bd. of Directors v. Blume Development Co.*, 115 Wn.2d 506, 526-27, 799 P.2d 250 (1990).

The Court in *Berschauer/Phillips* recognized the distinction between the law of contract and tort law as well. There, the general contractor brought an action for negligent misrepresentation against the architect and structural engineer, claiming that their inaccurate and incomplete engineering plans caused the general contractor to spend more money and time to complete the construction project than originally believed. This Court employed a risk of harm analysis in concluding that the economic loss doctrine was necessary to “ensure that the allocation of risk and the determination of potential future liability is based on what the parties bargained for in the contract.” 124 Wn.2d at 826. The Court determined to preserve the

fundamental boundary between the law of contracts, which is designed to enforce expectations created by agreement, and the law of torts, which is designed to protect citizens and their property by imposing a duty of reasonable care on others.

Id.

In more recent economic loss doctrine cases, this differentiation between contract and tort damages remained viable. In *Alejandro v. Bull*, 159 Wn.2d 674, 153 P.3d 864 (2007), the purchasers of a home discovered that their house had a defective septic system. They sued the seller of the home claiming that the seller had engaged in fraud and negligent misrepresentation in selling the home with the defective septic system. This Court applied the economic loss doctrine, barring the purchaser's negligence claim because the purchaser's damage was "more properly remediable only in contract." *Id.* at 681.³ This Court noted that the fundamental boundaries of tort and contract were important to ensure the allocation of risk of future liability was based on what the parties bargained for; otherwise, certainty and predictability in allocating risk would decrease and impede future business activity. *Id.* at 682. The Court articulated the economic loss rule as follows:

The key inquiry is the nature of the loss and the manner in which it occurs, i.e., are the losses economic losses, with economic losses distinguished from personal injury or

³ This Court also ruled that plaintiff's fraudulent concealment claim was not precluded by the economic loss rule. *Id.* at 689.

injury to other property. If the claimed loss is an economic loss, and no exception applies to the economic loss rule, then the parties will be limited to contractual remedies.

Id. at 684.⁴

This Court's adoption of the independent tort duty analysis in *Eastwood* and *Affiliated* was also intended to maintain a line of demarcation between contract and tort damages. In *Affiliated*, the Seattle Monorail caught fire and its operator suffered extensive lost revenues. That company sued the engineering firm that provided maintenance services for the Monorail for negligently causing the fire. In *Eastwood*, a horse farm lessor brought an action against the lessee for breach of the lease, waste, and negligence in breaching a duty not to cause damage to the leasehold. This Court in both cases held that the tort-based claims were not barred.

In *Eastwood*, the Court held that plaintiff may bring a tort claim where the tort duty is independent of the contract, abandoning the term "economic loss rule" and renamed this rule the "independent duty doctrine." 170 Wn.2d at 393, 402. The Court further explained that "[t]he term 'economic loss rule' has proven to be a misnomer. It gives the

⁴ The Court defined economic loss as an injury in a contractual relationship "where the parties could or should have allocated the risk of loss, or had the opportunity to do so." 159 Wn.2d at 687. Economic loss occurs when the defendant's action causes the plaintiff to lose money, or something of purely economic value, as opposed to suffering personal injury or injury to other property. *Id.* at 684.

impression that this is a rule of general application and any time there is an economic loss, there can never be recovery in tort.” *Id.* at 388-89. The *Eastwood* court determined the economic loss rule does not bar a plaintiff from bringing a tort claim simply because the injury is an economic loss and the parties have a contractual relationship. *Id.* The Court explained that in the past, when it has held that the economic loss rule applies, “what we have meant is that considerations of common sense, justice, policy, and precedent in a particular set of circumstances led us to the legal conclusion that the defendant did not owe a duty.” *Id.* at 389. As the Court explained, “[a]n injury is remediable in tort if it traces back to the breach of a tort duty arising independently of the terms of the contract.” *Id.* Notwithstanding this transition to the independent tort duty analysis, this Court reiterated its commitment to a line of demarcation between tort and contract recoveries, *Affiliated*, 170 Wn.2d at 451-54, and it expressly did not overrule any of its prior decisions on the economic loss doctrine. *Affiliated*, 170 Wn.2d at 450 n.3.

(b) Legislative Policy

In the product liability setting, this Court chose not to apply the former economic loss doctrine when in *Berg v. General Motors Corp.*, 87 Wn.2d 584, 555 P.2d 818 (1976), the Court permitted a plaintiff to recover in tort for purely commercial loss after a defectively manufactured engine

malfunctioned during a commercial fishing trip. The Legislature, however, overruled *Berg* in 1981 by enacting RCW 7.72.010(6) where it excluded from the definition of harm any direct or consequential economic (commercial) loss under the Uniform Commercial Code. *See also*, RCW 7.72.020(2).

In *Touchet Valley Grain Growers, Inc. v. Opp & Seibold Gen. Const., Inc.*, 119 Wn.2d 334, 831 P.2d 724 (1992), this Court analyzed the proper application of RCW 7.72.010(6). There, claims arose from the catastrophic collapse of a grain storage building; the Court concluded the claims met either of two possible tests: the risk of harm test or the sudden and dangerous test, and upheld a tort claim against a truss supplier. More than simply economic loss was involved; catastrophic property damage had occurred and, while not stated, someone could have easily been seriously injured or killed.

Indeed, the Legislature's limitation of mere economic claims arising from product defect to warranty liability under Uniform Commercial Code was one of the solid reasons for the rule adopted in *Berschauer/Phillips* barring negligence theories of recovery of commercial loss claims in construction cases. *Berschauer/Phillips*, 124 Wn.2d at 822. The Court aptly noted it would be incongruent to deprive an unsophisticated consumer a tort recovery under RCW 7.72 where the

product caused only economic loss damages, yet allow a tort recovery to a sophisticated consumer like a general contractor. *Id.* General contractors, owners, developers and design professionals are sophisticated consumers who are privy to the economic risks associated with their business. They do not need more protection than what the law gives the ordinary consumer.

Thus, by legislative policy, commercial loss is not recoverable in tort, but rather must be recovered in contract.⁵

The logic of setting a boundary between contract and tort damages remains true today. The law of negligence is well suited to ensure that injured persons are compensated for their personal injuries or property damages. The law of negligence properly invokes safety-insurance policies to spread the cost of such injuries, often by means of insurance.

⁵ It is well-recognized in the treatises on torts that tort law traditionally redresses injuries properly classified as physical harm; while, in contrast, contract law protects expectation interests. W. Prosser, *Torts* § 101 at 665 (4th ed. 1971). In the context of product liability, Prosser said:

Where there is no accident, and no physical damage, and the only loss is a pecuniary one, through the loss of the value or use of the thing sold, or the cost of repairing it, the courts had adhered to the rule that purely economic interests are not entitled to protection against mere negligence...

Id. at 665. This principle has been recognized in the Third *Restatement of Torts* as well. In the *Restatement of Torts* (3d), Liability for Physical and Emotional Harm, physical harm is explicitly a factual predicate to a claim for negligence: "An actor whose negligence is a factual cause of physical harm is subject to liability for any such harm within the scope of liability, unless the court determines that the ordinary duty of reasonable care is inapplicable." *Id.*, section 6 at 67.

On the other hand, claims for defeated commercial expectations are best and properly governed by the contracts in which those expectations were created and the risks and benefits were allocated and priced.

(2) To Establish the Boundary Between Tort and Contract, This Court Should Adopt a Risk of Harm Analysis

The proper focus for this Court in applying the independent tort duty analysis is not the characterization of the cause of action, but the nature of the harm for which redress is sought. Whether the claim advanced by a plaintiff is negligent misrepresentation or tortious interference with a contractual relationship, or breach of contract is less consequential analytically than whether a plaintiff seeks redress for personal injuries and property damages, or commercial loss.

Historically, that is the distinction that has been of moment in drawing the line between contractual and tort damages, as noted by Justice Benjamin Cardozo, then of the New York Court of Appeals, in *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 111 N.E. 1050 (N.Y. 1916). There, he wrote that the law allows for liability of a manufacturer in tort for personal injuries caused by a Buick automobile's defective wooden wheel without privity of contract. Similarly, *Ultramares v. Touche*, 255 N.Y. 170, 174 N.E. 441 (N.Y. 1931) involved liability in negligence for investment losses, Ultramares was an accountant who

prepared a financial statement. He was then sued, not by his client, but by an investor who relied upon his statement. The court rejected the investor's claim for negligence because the accountant owed no duty to third persons to refrain from negligently causing commercial losses.

Justice Roger Traynor, writing for the California Supreme Court, similarly observed the same dichotomy between personal injury and commercial loss. In *Seely v. White Motor*, 63 Cal.2d 9, 403 P.2d 145 (1965), the court held that lost profits in the absence of a personal injury are not recoverable in negligence. The abolition of the rule of privity in product liability law was impelled by "the distinct problem of physical injuries." *Id.* at 15. "Even in actions for negligence, a manufacturer's liability is limited to damages for physical injuries and there is no recovery for economic loss alone." *Id.* at 18.

Thus, the theory of recovery for personal injury should be broad enough to pass the risk of loss to those who can afford to pay, particularly where the injured party is essentially powerless to negotiate the terms of sale. By contrast, the remedies for commercial loss should be defined by the agreement under which the relationship of the parties is created.

This Court first confronted whether to permit the use of negligence law in resolving construction claims in *Stuart*, and the Court applied a risk of harm analysis:

In cases such as the present one where only the defective product is damaged, the court should identify whether the particular injury amounts to economic loss or physical damage. In drawing the distinction, the determinative factor should not be the items for which damages are sought, such as repair costs. Rather, the line between tort and contract must be drawn by analyzing interrelated factors such as the nature of the defect, the type of risk, and the manner in which the injury arose. These factors bear directly on whether the safety-insurance policy of tort law or the expectation-bargain protection policy of warranty law is most applicable to the claim in question.

109 Wn.2d at 420-21.

Under a risk of harm analysis, the distinction between negligence and contract is maintained by asking, what interests are at issue? Is the court dealing with the safety-insurance principles necessary to ensure within some boundary that injured persons are compensated for personal injuries caused by unsafe conditions? Or is the court dealing with defeated commercial expectations without personal injury or property damage?

Subsequent to *Stuart*, courts lost sight to an extent of this analysis by focusing instead on the nature of the cause of action pleaded. The expression "economic loss" arose in a context in which there was no personal injury or catastrophic property damage, but over time it came to mean any loss that was economic, including revenue losses arising from a catastrophic fire in which personal injuries were at risk. In *Affiliated*, for

example, the district court applied its conception of the “economic loss” rule to claims arising from a fire on the Seattle monorail that was occupied by tourists. 170 Wn.2d at 446-47. In *Alejandre*, Justice Chambers in his concurrence noted the misnomer in the expression “economic loss” and its concomitant confusion, preferring the more accurate expression “commercial loss.” 159 Wn.2d at 695-96.

The Court of Appeals below applied this Court’s new independent duty analysis to the cause of action, rather than nature of the harm for which redress is sought. It construed “independent duty” to mean that merely because an engineer may owe a duty to his/her clients that the independent tort duty analysis is satisfied: “We conclude that a majority of the supreme court in *Affiliated* held that professional engineers owe a tort duty of reasonable care to their clients. This is consistent with prior Washington law.” *Donatelli v. D.R. Strong Consulting Engineers, Inc.*, 163 Wn. App. 436, 443, 261 P.3d 664 (2011).⁶ The court cited *Jarrard v. Seifert*, 22 Wn. App. 476, 591 P.2d 809 (1979) and *Burg v. Shannon & Wilson, Inc.*, 110 Wn. App. 798, 43 P.3d 526 (2002) for this proposition. *Donatelli*, 163 Wn. App. at 443 n.27. The court did not undertake any

⁶ It would be more accurate to assert that in *Affiliated* all nine members of this Court held the engineer owed a duty of care and seven of those concurring did so because the economic loss rule was not at issue at all. Justice Chambers stated the issue most directly: “This case does not implicate in any way the independent duty doctrine, formerly known as the economic loss rule.” *Affiliated*, 170 Wn.2d at 462.

analysis of the nature of the damage being claimed by the engineer's clients. While it is true that an engineer owes a duty to his/her clients, that is too simple a formulation of the independent tort duty analysis. A more rigorous analysis is required, as the risk of harm approach requires. This Court would not be honoring the necessary line of demarcation between damages in tort and contract if every action pleaded in tort against an engineer that involved only commercial loss allowed recovery of tort damages against an engineer. Nor would it explain the cases left unaffected by this Court's decisions in *Eastwood* and *Affiliated*.

For example, in *Jarrard*, cited by the Court of Appeals below, the claims were in the nature of commercial loss due to a surveyor's error. The Court of Appeals there made its decision without any briefing or any analysis of the distinction between negligence and contract, and its decision came well before this Court ruled in *Stuart* that there was no tort of negligent construction. *Jarrard* also predated this Court's unanimous determination that damages for delay claims in construction cases, economic loss, are not recoverable in *Berschauer/Phillips*.

In *Burg*, the Court of Appeals upheld a summary judgment in favor of the engineering firm because, under the contract between the city and the firm, the firm did not assume any duty to third parties, such as the plaintiff homeowners in that case whose homes were severely damaged by

landslides. The court rejected a claim that the firm negligently failed to warn them of the need for remedial measures to avoid landslides when it was making recommendations to the City of Seattle to avoid such landslides where the firm's contract with the City evidenced no intent to benefit the homeowners or their property.

In *Berschauer/Phillips*, this Court held that the contractor and owner could not sue the architect and engineer for negligence or negligent misrepresentation for delay damages. This Court emphasized that such delay damages are appropriately the subject of risk allocation in contract negotiations between the parties. *Id.* at 826-27.

By contrast, in *Affiliated*, the fire on the Monorail damaged the property of the operator, i.e., the Monorail itself, and it put people's safety at risk. 170 Wn.2d at 452-53.

This case more resembles the fact pattern in *Berschauer/Phillips*.

The Court of Appeals opinion is logical only if the Court had overruled all of the cases limiting construction claims lacking personal injury or catastrophic property damage to the remedies of the contract, which it did not: "our decisions in this case and in *Eastwood* leave intact our prior cases where we have held a tort remedy is not available in a specific set of circumstances." *Affiliated*, 170 Wn.2d at 450 n.3.

A risk of harm analysis will accurately inform practitioners and the lower courts how to determine whether a negligence theory will be permitted. That analysis asks three key questions: What is the nature of the conduct presented by the facts of the case? What is the nature of the risk in the case? How did the injury to the claimant arise? *Stuart*, 109 Wn.2d at 420-21. If the Court applies the risk of harm analysis here, it is clear that the Donatellis' remedy lies in contract and not in tort.

(3) Applying the Risk of Harm Analysis to the Donatellis' Negligence Claims Results in Their Dismissal

The core of the Donatellis' claims involve economic loss due to construction delay; the trial court and Court of Appeals should have barred such recovery in tort based on a risk of harm analysis.

(a) The nature of the conduct

Donatellis' amended complaint alleged that Strong was negligent for failing to complete its work in a timely, competent and cost effective manner. CP 4. The nature of the conduct at issue was tardy performance; no conduct by Strong created a risk of harm to the safety of the Donatellis' person or property.

(b) The type of risk

The Donatellis allege that, as a result of the tardy performance, the local residential real estate market crashed before the Project was

completed and they “lost all of the invested time, money, and effort.” CP 3. The type of risk is commercial loss only; nobody’s person or physical property was damaged. This was a risk that was directly addressed in the contract with Strong with the parties there agreeing on the allocation of risk and a modest fee for Strong. CP 26.

(c) The manner in which the injury arose

The injury arose because Strong allegedly took too long to perform its contracted duties, and the Donatellis were caught short by the financial crisis that erupted in 2008, losing their investment to foreclosure. This was not a traumatic injury to person or property.

All of these factors weigh heavily toward dismissal of the negligence claims. The Donatellis’ remedy, if any, is to be found in the parties’ contract.

F. CONCLUSION

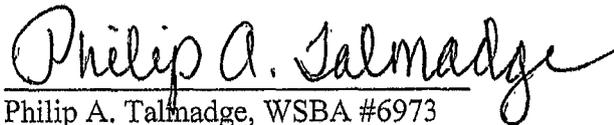
In applying the independent tort duty analysis here, the Court of Appeals erred in concluding that despite the careful articulation of the commercial responsibilities and expectations of Strong and the Donatellis in their contract, the Donatellis were entitled to pursue damages in tort against Strong. As in *Berschauer/Phillips*, the Donatellis’ relief is more appropriately found in the parties’ contract. The Court of Appeals

erroneously focused on the nature of the Donatellis' theory of recovery, rather than the elements of the risk of harm analysis.

This Court should reverse the Court of Appeals and the trial court, and remand the case to the trial court with directions to enter partial summary judgment in favor of Strong, dismissing the Donatellis' claims for tort-based damages against it. Costs on appeal, including reasonable attorney fees, should be awarded to Strong.

DATED at this 9th day of May, 2012.

Respectfully submitted,



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DECLARATION OF SERVICE

On said day below I emailed and put in the U.S. Mail a true and accurate copy of the Supplemental Brief of Appellant D.R. Strong Consulting Engineers, Inc., in Supreme Court Cause No. 86590-6 to the following parties:

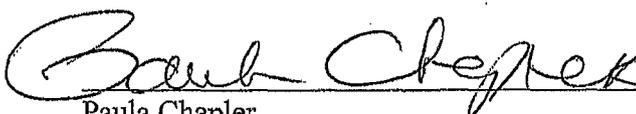
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I declare under penalty of perjury under the laws of the State of Washington and the United States that the foregoing is true and correct.

DATED: May 9, 2012, at Tukwila, Washington.



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Subject: Steven and Karen Donatelli v. D.R. Strong Consulting Engineers, Inc., Cause No. 86590-6

Per Mr. Talmadge's request, please see the attached Supplemental Brief of Appellant D.R. Strong Consulting Engineers, Inc. for filing in the following case:

Case Name: Steven and Karen Donatelli v. D.R. Strong Consulting Engineers, Inc.
Cause No. 86590-6
Attorney: Philip A. Talmadge, WSBA #6973
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Sincerely,

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