

WHO SAID YOU CAN'T HAVE IT ALL? THE PERILS OF IGNORING RISK ALLOCATION IN CASES OF RELATIONAL ECONOMIC LOSS

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Introduction

Since the High Court's decision in *Caltex Oil (Australia) Pty Limited v The Dredge 'Willemstad'*¹ there has been a divergence in many of the Commonwealth jurisdictions as to the preferred approach to recovery in cases of relational economic loss. The principles upon which the courts have allowed or disallowed recovery are not always readily apparent, with several jurisdictions content to place the burden of justification upon the dromedary-like area of policy. But it is far from certain that policy alone can continue to carry such a weight.

While the search for a unifying principle continues, what is often missing in the judicial analysis is an appropriate recognition that the reasoning must support the imposition of a duty of care; not that it should simply justify recovery. It is submitted that a realigning of these considerations is necessary, in order that in the haste to do justice between the parties, a result is not produced which does not account for factors which properly negate the existence of a duty of care, and are ultimately unfair.

Of particular concern is the paucity (and in most cases, a complete absence) of economic considerations in the reasoning.² Many of these cases concern commercial enterprises seeking recovery for relational economic loss in the form of reduced profits or additional expenditure. However, it is not entirely clear why the courts have seemingly divorced fundamental economic considerations from the law of relational economic loss. In the commercial context, the primary consideration which receives little or no recognition is that parties can allocate (contractually or otherwise) their risks long before the day arrives where they suffer economic loss. Viewed thus, it is submitted that such 'losses' are not losses at all; they are materialisations of

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¹ (1976) 136 CLR 529 (*Caltex*).

² B Feldthusen, 'Liability for Pure Economic Loss: Yes, but why?' (1999) 28(1) *University of Western Australia Law Review* 84 at 87.

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anticipated risks which, much like the risk borne by insurance underwriters, occasionally come home to roost.

This paper argues that, fundamentally, allowing recovery for relational economic loss whilst ignoring economic considerations allows an affected party to possess their cake, whilst at the same time reserving the right at some unknown date to eat it, and thereafter to leave the dirty plate in a stranger's kitchen for washing.

To illustrate this, the paper will discuss the following:

- the relevance of risk allocation as a factor in determining the existence of a duty of care;
- the historical development of recovery for relational economic loss;
- the High Court's current approach to novel duty situations; and
- a discussion of recent Australian decisions involving relational or other types of pure economic loss.

The relevance of risk allocation

Most, if not all, parties (including non-commercial parties) actively engage in risk allocation on a daily basis. For example, when an individual purchases a home, the reward is that they have a secure place to live, over which they exercise control. They may also benefit from any increases in value during the period they own the property. However, they also accept the risk that they may have to make repairs to operational items such as water heaters, or structural repairs to roofs, walls or the foundations. Similarly, any reductions in the value of the property will be borne by the home owner.

In any market-driven economy, and barring other vitiating conduct such as fraud or unconscionability, it is difficult to see any reason why it should not be assumed that all of these risks and rewards are properly factored into the price that is paid for the property. As a general rule, people do not offer to pay more for something than they ultimately think it is worth.

In this way, risk is allocated between the parties in the transaction. The buyer no doubt takes into account the age of the house and any of its fixtures when setting their offer. They may even engage a professional to inspect and report on the property to assist them with this task. The further inspection is itself another means of allocating risk. If the inspector provides a glowing report which affects the amount paid for the property, and it later transpires that the report was prepared negligently, any difference between the true value and the amount paid, whilst not recoverable

from the vendor, would still be recoverable from the inspector in negligence or contract.

This is just one example. In the commercial arena, companies often split into a group structure for various reasons. One of these is asset protection. Another might be tax favourability. The rewards for so doing are clear, but, it is submitted, so are the risks.

The risks may not seem quite as obvious as in the house example, but they are certainly still there. For example, if assets are put into a subsidiary, there is a risk that the holding company can no longer obtain credit without the directors giving personal guarantees. The directors know this, but proceed regardless. They proceed in the full knowledge that a change in the corporate structure may ultimately lead to a personal liability for the directors, however, this risk is offset by the potential tax and liability rewards which are conferred through the use of the group structure. It would be unusual in such a case that there should be any sympathy for the directors if ultimately it is the risk of being personally liable which materialises but not the reward. In this context, the risks were all too clear, but they were nonetheless taken.

Similarly, in cases of relational economic loss, it is submitted that adherence to an exclusory rule based on an acceptance of risk is justified. However, such a rule should not be based on archaic policy considerations such as indeterminacy. Properly considered, the rule is justified on the principle that parties who accept and allocate risk should not be relieved of the consequences of their risk-taking by the law when their risk matures. To hold otherwise unfairly imposes liability on third parties who do not cause personal or property damage to plaintiffs.

The development of the law in this area shows the difficulties faced by courts in attempting to arrive at a decision which, superficially at least, is fair and just. However, a closer analysis shows that the courts often ignore in their analysis the conduct of plaintiffs who accept or allocate risk. The focus is generally on the tortfeasor and the foreseeability of harm, with scant regard paid to the plaintiff who has generally foreseen their own risk, but chooses to proceed regardless. The irresistible conclusion in some cases is that the liability imposed is often moral, rather than legal, in nature.

The development of recovery for relational economic loss

The first case of any real renown in this area is that of *Cattle v Stockton Waterworks Co.*³ That case involved a plaintiff tradesman who, for a set fee, contracted to make a tunnel under a road which divided a landowner's property. A waterpipe owned by the defendant was incorporated into an embankment which formed part of the road,

³ (1875) LR 10 QB 453.

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and through which the tradesman was required to tunnel. During the works, a leak was discovered in the pipe which flowed into the tunnelling area, causing the works to be delayed. The profits of the tradesman were thereby minimised, as he had agreed upon a set fee with the landowner. The tradesman claimed his diminution in profits as damages from the defendant owners of the water pipes.

In dismissing the plaintiff's claim, the Court relied heavily upon the notion of indeterminacy. The Court reasoned (by analogy) that if the law were to develop in this fashion, it would extend recovery in situations such as the drowned mine in *Rylands v Fletcher* to the mine workers whose wages were minimised by the adjoining landowner's negligence.⁴ It was said that whilst it may lead to imperfect results, 'only the proximate and direct consequences of wrongful acts' should be redressed through the law of negligence.⁵

The decision in *Cattle* clearly predated the later elucidation of the concepts of foreseeability in *Donoghue v Stevenson*,⁶ however, the essence of the reasoning in *Cattle* is likely to conform with an argument that recovery for damage in the nature of that suffered by the plaintiff, whilst foreseeable, would still have been prohibited on the ground that the plaintiff and defendant lacked a requisite level of proximity. Such a view appears to have largely prevailed in Australia up until the High Court's decision in *Caltex*.

However, it is submitted that *Cattle's* case is more easily reconciled with a principle that the tradesman, who was free to contract or not on the terms that were agreeable to both he and the land owner, in agreeing to perform the works for a fixed sum, accepted the risk that foreseeable interferences, such as the burst water pipe, could impact on his economic interests. Knowing these risks, and always having the option of contracting on some other basis, such as for a fixed margin of profit, the tradesman agreed to perform the works.

The risks were thus allocated between the parties to the contract, and it is difficult to see why the defendant should be held to account when one of these risks materialised to the detriment of the tradesman. Viewed thus, the exclusion of the tradesman's claim is supportable for reasons of principle rather than policy. As will be seen below, a policy-based approach invariably leads to anomalous exceptions to an otherwise clear rule.

⁴ Ibid at 457.

⁵ Ibid.

⁶ [1932] AC 562.

A brief note on negligent misstatement

Of significance in the intervening period between the decisions in *Cattle* and *Caltex* was the decision of the House of Lords in *Hedley Byrne & Co Ltd v Heller & Partners Ltd*.⁷ In that case, an information provider was held liable for the negligent provision of credit information to a third party. The basis of liability in that case appears to rest largely on the knowledge by the defendant of the plaintiff's intended use of the information, along with an assumption of responsibility by the defendant in providing that information.

Whether the reasons justifying recovery for economic loss caused by negligent misstatement could be attacked on the same basis as those concerning relational economic loss is now somewhat moot. In Australia at least, the provisions of Part V of the *Trade Practices Act 1974* (Cth) provide a statutory basis for that relief.

It is not intended, therefore, to comment further on this area of economic loss, save for the assertion that the underlying economic considerations would apply equally to preclude recovery in cases of negligent misstatement, but for the intervention of the legislature in this area. It is submitted that the economic considerations discussed above provide a unifying principle capable of application across the spectrum of economic loss cases.

Recovery in the pipeline: the decision in *Caltex*

Not until *Caltex* did the issue of recovery for relational economic loss fall to be examined by the High Court. The facts of *Caltex* were relatively straight forward. A dredge was engaged to deepen a shipping channel, in the process of which it damaged an oil pipeline owned by a company called AOR, but used to transport *Caltex*'s petroleum products. The petroleum products were, by contractual agreement, at the risk of AOR while in the pipeline.

AOR recovered for damage to its pipeline and the loss of petroleum products. *Caltex* sought only to recover for the additional costs incurred in transporting its products to and from the AOR terminal in ships or overland, instead of through the pipeline. Its claim was therefore one of pure economic loss.

In examining the decision in *Caltex*, it is important not to divorce the issue of recovery from the existence of a duty of care. While the judgments generally have a sympathetic tone toward the plaintiff's situation, the case should not be seen as giving guidance on when policy dictates that recovery is fair. The search, as in most novel areas of negligence, is for whether a duty of care exists which would allow any recovery at all.

⁷ [1964] AC 465.

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In this respect, Gibbs CJ concluded it was generally the rule that recovery for economic loss was not recoverable where damage was not consequential upon personal or property damage. However, his Honour accepted that there was an exception created where there is knowledge on the part of the defendant that the plaintiff particularly, and not merely an unascertained class, will be likely to suffer harm as a consequence of the defendant's negligence. On the facts of the case, in his Honour's opinion, such a relationship existed which warranted the imposition of a duty of care.⁸

Stephen J fell into the unprincipled (and possibly moralistic) approach of determining whether there existed a rule precluding recovery, rather than the more fundamental question of whether a duty of care was owed. His Honour confined his discussion to whether it was 'just and fair' that the tortfeasor should be liable to the plaintiff, and did not examine the principles upon which it is determined, in any particular case, whether a duty of care should be imposed.⁹

Mason J preferred an approach based on the existence of a duty of care. However, his Honour's reasoning ultimately relied on the need to avoid indeterminacy, which he held could be avoided by a limited application of the notion of foreseeability.¹⁰

Jacobs J said that a duty of care was owed due to the 'physical propinquity' of the property of Caltex and the operation and physical effects of the dredging operation. This 'proximity' meant that any effect on the property of Caltex was foreseeable, such that a duty of care was owed.¹¹

While holding that a duty of care was owed, Murphy J was somewhat more critical of the approach taken by the courts. His Honour specifically adverted to the fact that there was 'no satisfactory general principle governing recovery of economic loss caused by negligence', and highlighted the uncertainty surrounding recovery in cases of economic loss.¹²

It is interesting to note that in *Caltex*, two members of the High Court made direct reference to the contractual provisions which existed between Caltex and AOR, by which the parties sought to contractually allocate portions of their respective risks.¹³ Stephen J noted that:¹⁴

⁸ (1976) 136 CLR 529 at 555.

⁹ *Ibid* at 581.

¹⁰ *Ibid* at 592-3.

¹¹ *Ibid* at 604.

¹² *Ibid* at 605-6.

¹³ *Ibid* at 560 per Stephen J, and at 603-4 per Jacobs J.

¹⁴ *Ibid* at 562.

It was the interruption to the general flow of product through the pipeline, coupled with the fact that, by the terms of cl. 23 of the processing agreement, A.O.R. was not, in the circumstances, liable to Caltex for the failure to supply by pipeline, that cast upon Caltex the substantial financial burdens which represented its economic loss.

Unfortunately, there was little analysis of the effect of these contractual choices on the parties to the litigation. Caltex had, it appears, allocated by contract risks associated with the interruption of its use of the pipeline. The sympathetic tone of the judgments in that case do not appear to give sufficient consideration to the fact that Caltex had, through its contractual dealings, created the very risk for itself which materialised upon the pipeline being damaged. This was discussed only briefly in the judgments. Stephen J said:¹⁵

It is not unimportant to note that in the circumstances of the present case even the exclusory rule would operate to confer a complete right of recovery upon Caltex for its claimed economic loss had the processing agreement contained a clause granting it some possessory right in the pipelines during the currency of the agreement. These considerations make the suggested rule seem a high price to pay for protection against the fear of possibly excessive extension of the right to recover compensation for proved loss.

With respect to his Honour's reasons, the existence of the contractual arrangement is the very reason that the exclusory rule is not a high price to pay. On the contrary, such a rule merely holds a plaintiff to the bargain they have struck for themselves. At least in *Caltex*, it is difficult to see why the defendants should be liable in tort for damages flowing from a risk that the plaintiff had specifically contracted for.

Caltex reviewed: ships that go 'bump' in the night

The High Court's decision in *Caltex* was relied on by the plaintiff in the Privy Council case of *Candlewood Navigation Corp Ltd v Mitsui OSK Lines Ltd (The Mineral Transporter)*.¹⁶ In that case, the defendant's vessel negligently collided with another, causing it damage. The plaintiff was a time charterer of the damaged vessel, and claimed for the losses suffered whilst the damaged vessel was undergoing repair. The plaintiff recovered at first instance. The defendant appealed to the Privy Council.

Although the appeal was from the Supreme Court of New South Wales, the Privy Council chose not to follow the decision in *Caltex*. After quoting the facts of *Caltex*, Lord Fraser of Tullybelton, delivering the advice of the Council, found that while the judgments in the High Court examined the relevant law and its associated problems,

¹⁵ Ibid at 569.

¹⁶ [1985] 3 WLR 381.

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the Privy Councillors were unable to extract a single ratio decidendi which they could apply to the present case.¹⁷

His Lordship then went on to hold that, for reasons of policy, a 'limit or control mechanism has to be imposed upon the liability of a wrongdoer towards those who have suffered economic damage in consequence of his negligence'.¹⁸ This approach to duty of care for claims of pure economic loss by the English Courts became known as the 'Bright Line Rule', in that it provided a definite and ascertainable mark over which the law of negligence would not be allowed to pass.

Ultimately, the Privy Council considered *Caltex* to be an exception to the general rule in *Cattle* that a wrongdoer would not be liable for damage in the nature of economic loss which was not consequential upon damage to person or property.¹⁹ The Privy Council also put *Hedley Byrne* in that same category of exceptions.²⁰

However, it is worth noting the Privy Council's express rejection of the idea that knowledge by a defendant of the existence of a plaintiff as the test for establishing a duty of care. As will be seen below, this test continues to be applied in Australia.

Bangers, but no mash: the decision in Perre

The most recent relational economic loss case considered by the High Court was *Perre v Apand Pty Ltd*.²¹ The case involved a company which grew an experimental crop of potatoes in South Australia. The potatoes were later found to be contaminated with a bacterial wilt, the presence of which prevented any potato so affected, or any produced on any property within 20 kilometres of the affected property, from being imported into Western Australia. The plaintiffs were so affected, and subsequently were unable to sell product into Western Australia, for which they claimed on the basis of economic loss.

The High Court held that the plaintiffs were owed a duty of care. This was so, notwithstanding that what was claimed was pure economic loss; the plaintiffs' land not itself having been actually contaminated. Gleeson CJ held that a duty of care was owed where there is knowledge by the tortfeasor that their acts or omissions may affect the legal rights of another, where the party claiming damage is in no position to protect their own interests.²²

¹⁷ Ibid at 391.

¹⁸ Ibid at 394.

¹⁹ Ibid at 394-5.

²⁰ Ibid at 389.

²¹ (1999) 198 CLR 180.

²² Ibid at 202.

As to the approach to be taken in establishing the existence of a duty of care, McHugh J favoured an incremental approach, without the need to discover a unifying principle.²³ In applying this approach to the present case, his Honour held that a duty exists whenever a defendant should have contemplated the interests of the plaintiff before they pursued their particular course of conduct.²⁴

McHugh J ultimately held that a duty of care was owed on the basis that:

- the loss was reasonably foreseeable;
- the imposition of a duty would not impose indeterminate liability;
- the imposition of a duty would not impose an unreasonable burden on the autonomy of Apand;
- the Perres were vulnerable to the loss from the conduct of Apand; and
- Apand knew that its conduct could cause harm to individuals such as the Perres.²⁵

Of the possible economic considerations, McHugh J held that the ability of a plaintiff to purchase insurance was not relevant to the issue of vulnerability. The reasoning behind this is compelling in that loss spreading, which can occur when an insurer redistributes losses over many premium payments, is not synonymous with economic efficiency.²⁶ Loss spreading is concerned with diffusing the aftermath; risk allocation is about avoiding the explosion altogether. The insurability of any particular loss is relevant to an argument in favour of loss spreading, but it has no bearing on risk allocation. Economic efficiency was, however, seen to be a relevant factor in determining duty.²⁷

Risk allocation has not been altogether ignored by the High Court. In *Perre*, McHugh J, who placed a great deal of reliance on the notion of vulnerability as being relevant to the imposition of a duty of care, said that vulnerability itself depends on what protective action the plaintiff could have taken to protect its own interests.²⁸ He cautioned that where another body of law (such as contract) could deal effectively

²³ Ibid at 216-217.

²⁴ Ibid at 218.

²⁵ Ibid at 231. These factors were applied by the High Court in *Woolcock Street Investments Pty Ltd v CDG Pty Ltd* (2004) 216 CLR 515 and by the Queensland Court of Appeal in *Fortuna Seafoods Pty Ltd as Trustee for the Rowley Family Trust v The Ship 'Eternal Wind'* [2005] QCA 405.

²⁶ Ibid at 230.

²⁷ Ibid.

²⁸ Ibid at 226-7.

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with economic loss, the 'court should be slow to use negligence law to impose a duty of care on a defendant', and that 'developments in negligence should occur in sympathy with the law of contract'.²⁹

Gummow J's approach to the issue of duty of care was to adopt the approach taken by Stephen J in *Caltex* of isolating a number of 'salient features' which combined to establish a relationship such as to justify the imposition of a duty of care.³⁰

Kirby J used *Perre* as an opportunity to showcase the merits of the approach to novel duty situations adopted by the House of Lords in *Caparo Industries Plc v Dickman*.³¹ This approach was rejected by Gleeson CJ in *Perre* and later in the unanimous High Court decision of *Sullivan v Moody*.³²

The decision in *Perre* was something of a high-water mark in the divergence of views within the court on the question of when a duty of care should be imposed. Significantly, this case, and in fact all of the Australian cases discussed above, preceded the High Court's decision in *Sullivan*, in which the court reviewed its approach to the question of duty of care in novel fact situations.

The search for a unifying principle applicable in all novel fact cases had been largely fruitless, such that the basis for imposing a duty of care in cases of pure economic loss was arguably no further advanced by the time of *Perre* than it had been some 23 years earlier in *Caltex*. This situation, to some extent, was resolved in *Sullivan*.

A new approach to duty of care

The facts of *Sullivan* are not important. The case was a vehicle for a unanimous High Court³³ to review its approach to determining the existence of a duty of care in novel fact situations. It had long been recognised that foreseeability of itself was insufficient to impose a duty of care; something more was required.³⁴ In the interval during which both *Caltex* and *Perre* were decided, the key additional factor relied on by the court was proximity. Essentially, a duty would be imposed where, in addition to the defendant and/or their harm being reasonably foreseeable, the parties were in a relationship of proximity (be it physical, temporal or relational) such that the imposition of a duty of care was justified.

²⁹ Ibid.

³⁰ Ibid at 254.

³¹ [1990] 2 AC 605.

³² (2001) 207 CLR 562.

³³ Gleeson CJ, Gaudron, McHugh, Hayne and Callinan JJ.

³⁴ *Jaensch v Coffey* (1984) 155 CLR 549 at 583-5 per Deane J; *Sutherland Shire Council v Heyman* (1985) 157 CLR 424 at 497-8 per Deane J.

In dismissing this approach in *Sullivan*, the Court held that such an approach gave little guidance to assist with determining whether a duty exists in cases that bear no analogy to previously decided cases.³⁵

The court also expressly ruled that the *Caparo* approach was not the law in Australia.³⁶ Ultimately, the court preferred a more incremental approach, accepting that the different classes of cases coming before the courts gave rise to differing problems for ascertaining whether a duty should be imposed.³⁷

It must now be accepted that the High Court will determine any future cases where it is argued that a duty of care should be imposed, by reference to the incremental approach outlined in *Sullivan*. However, as the next cases show, this does not automatically mean that decisions in earlier cases will be of no relevance in determining the duty of care issue.

Recent Australian decisions

Two recent Australian decisions illustrate the divergence of approaches adopted by the courts in this country, and the inevitable uncertainty that follows an unprincipled approach to this area of negligence. The cases discussed are *Woolcock Street Investments Pty Ltd v CDG Pty Ltd*,³⁸ a decision of the High Court, and *Fortuna Seafoods Pty Ltd as Trustee for the Rowley Family Trust v The Ship 'Eternal Wind'*,³⁹ a decision of the Court of Appeal of Queensland.⁴⁰

Woolcock Street Investments: the foundations begin to crumble

In *Woolcock*, the High Court was again faced with a situation where a party had suffered purely economic loss due to the alleged negligence of another. In that case, a firm of engineers was sued by the subsequent owner of a commercial building, on the basis that the engineers had failed to properly design the foundations of the building which were later found to be defective.

In light of the court's decision in *Sullivan*, the issue of whether a duty of care is owed in this type of claim was discussed by Callinan J as follows:⁴¹

³⁵ (2001) 207 CLR 562 at 578-9.

³⁶ *Ibid* at 579.

³⁷ *Ibid* at 579-580.

³⁸ (2004) 216 CLR 515.

³⁹ [2005] QCA 405.

⁴⁰ Special leave to appeal to the High Court against the decision of the Court of Appeal was declined on 10 March 2006.

⁴¹ (2004) 216 CLR 515 at 593.

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In this area of claims, for economic loss, an evolving area of the law, cases will in practice only be resolved by closely and carefully examining the facts to ascertain whether a sufficiency of factors of a sufficient degree of relevance and importance has been demonstrated. It is better I think to acknowledge and apply that reality than to attempt to state an inflexible principle which is bound, at this stage at least, to fail to meet the justice of the cases which are likely to arise in the future.

The principal factor relied upon in the majority judgments was that of vulnerability, which had previously been outlined as a key consideration by McHugh J in *Perre*. Underlying this was a willingness by the court to treat risk allocation as fundamental to a particular party's vulnerability, which itself was held to be concerned with whether a plaintiff has the ability to protect itself from the consequences of a defendant's negligent conduct, and not merely that the plaintiff was likely to suffer damage if care was not taken.⁴²

The majority found that a duty of care was not owed, principally because it could not be said that the plaintiff was vulnerable to any failure by the defendant to take reasonable care. Risk allocation featured heavily in the court's considerations. In particular, McHugh J held that the owners were in a position to protect themselves from losses arising from defects in the building's construction.⁴³ Importantly, his Honour noted that 'no prudent purchaser would contemplate buying a building without determining whether it has existing or potential construction defects'.⁴⁴ His Honour concluded by saying that where risks are unknown or uncertain, this should be dealt with in an adjustment to the price, by obtaining some form or contractual protection, or by simply walking away.⁴⁵

Each of the majority judges concluded that the plaintiff was not vulnerable, in the sense that they could not have properly protected themselves. Such an approach is preferable to that taken in *Caltex*, however, it is submitted that it should go further.

The approach taken in *Woolcock* achieved an appropriate result, which properly reflected the fact that the risks involved in the purchase of the building must have been contemplated by the plaintiff at the time of purchase. However, it did so without formalising a principled approach for use in all cases of economic loss. This is to be expected, and it would be quite unusual for the High Court to readily abandon reasoning developed (with some difficulty) over the course of 30 years.

⁴² Ibid at 530 per Gleeson CJ, Gummow, Hayne and Heydon JJ.

⁴³ Ibid at 558.

⁴⁴ Ibid.

⁴⁵ Ibid.

However, it is submitted that a principled approach has become both necessary and appropriate. Although McHugh J's reasoning in *Woolcock* was laced heavily with commercial overtones, there is no reason for not applying the same approach to claims for economic loss which do not bear that same commercial flavour. It is not the commerciality of the plaintiff which should ultimately govern whether a party should recover; it is the conscious ability to allocate risk which should be fundamental to the discussion. All parties, commercial or otherwise, have the ability to control their risk, such that a risk-based approach provides a uniform principle applicable across all claims for economic loss.

If such an approach was adopted, it is submitted that claims for relational economic loss will be precluded altogether. Although it has been said that it would be 'unrealistic, if not absurd, to suggest that the High Court would now retreat from the *Caltex* decision and reaffirm the traditional exclusory rule',⁴⁶ it is accepted that an approach based on an acceptance of theories of risk allocation would have this precise effect.

However, this does not automatically mean that the former exclusory rule first outlined in *Cattle* has in any way been reaffirmed. That rule as laid down in *Cattle* and *Candlewood* is little more than an application of policy based on notions of indeterminacy. Once so established, exceptions are easy to find if the issue of indeterminacy can be resolved in any particular case.

A risk allocation approach to these cases would have the effect of excluding claims, however, it does so in a principled way which is not then open to anomalous exceptions. It is submitted that these exceptions often rely on the reasoning which is neither logical nor principled, in seeking to do justice to a party.

The next case is an excellent illustration of the difficulties which underpin the current approach, and the need for a consideration of risk allocation as a primary factor negating the existence of a duty of care in cases of relational economic loss.

Fortuna Seafoods: a fishy result?

Fortuna involved a defendant vessel which collided with a commercial fishing vessel. The fishing vessel was owned by a company associated with the plaintiff. The plaintiff processed and sold fish caught by the associated company. The plaintiff claimed for the losses it suffered in being unable to process and market the catch following the collision. The issue, as in all such cases, was whether the defendant

⁴⁶ K Hogg, 'Relational Loss, the Exclusory Rule and the High Court of Australia' (1995) 3 *Tort Law Review* 26 at 36.

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owed the plaintiff a duty of care so as to sustain an action for damages for negligence.⁴⁷

All members of the Queensland Court of Appeal relied heavily on the defendant's knowledge or means of knowledge of the foreseeable risk as being critical to the question of whether a duty of care should be imposed in the case.⁴⁸ However, such reliance also shows how artificial the tests in *Caltex* have become through their continued application.

The plaintiff in *Fortuna* was part of what the trial judge described as an integrated commercial enterprise, whose association with the holding company whose vessel was damaged included common shareholders and directors, a relationship of trustee and beneficiary and an integrated operation of separate aspects of a common business.⁴⁹

The evidence, however, was that the divided structure which led to the integrated operation was driven by a desire to by-pass the relevant marketing authorities in another State.⁵⁰ Remarkably, such a revelation played no part in the negating the existence of a duty of care. In fact, Dutney J remarked that these factors operated to define a separate ascertainable category of membership.⁵¹

With respect, it is difficult to understand that a company which deliberately sets about altering its structure with the direct intention of avoiding marketing restrictions imposed by a statutory authority, and in so doing increases its actual or potential profitability, should be considered so vulnerable by the courts that it warrants the imposition of a duty of care. The risks involved in so arranging the company's affairs must have been evident at the date the arrangement was entered into. The materialisation of these risks are not, it is submitted, an issue of vulnerability.

The vulnerability of any particular party cannot, and must not, be divorced from that same party's responsibility for the consequences which flow from its own conduct. To find otherwise creates continued uncertainty in this area of law, and unduly rewards parties who accept and/or allocate risk, or otherwise arrange their affairs, over those that do not.

⁴⁷ [2005] QCA 405 at [2] per McMurdo P.

⁴⁸ Ibid at [15] per McMurdo P; at [75]-[76] per Jerrard JA; and at [108] per Dutney J.

⁴⁹ *Fortuna Seafoods Pty Ltd (as Trustee for the Rowley Family Trust) v The Ship 'Eternal Wind'* [2005] QSC 004 at [30].

⁵⁰ [2005] QCA 405 at [9] per McMurdo P; and at [105] per Dutney J.

⁵¹ Ibid at [105].

For example, the parent company in *Fortuna* sought to avoid marketing restrictions. To do this it split its corporate structure. At that point it must have been aware that doing so created the risk that an indirect interference with one of the parent company's ships would have an effect on the plaintiff's economic interests, and that such losses were no longer recoverable by the parent company. Having taken this risk, and in so doing, reaped the benefit of avoiding the statutory restrictions, it seems somewhat incongruous that a court should then step in to provide the plaintiff with a complete indemnity from the consequences of its own risk-taking.

The absurdity of such a divorced approach is evident in the highly artificial reasoning propounded by the majority in *Fortuna*. Having failed to account for the fact that *Fortuna* had accepted a level of risk in exchange for a commercial reward, the question of duty largely came down to whether the defendant had knowledge of the nature of the plaintiff's integrated structure.

Bearing in mind the defendant's ship was Panamanian registered with a Filipino crew,⁵² the findings by the Court of Appeal are somewhat surprising. McMurdo P observed that notwithstanding these difficulties, the master or owner of the Panamanian vessel had the means of knowing that commercial fishing ventures in Australia may consist of a number of companies in an integrated company group with related shareholders with different functions undertaken by the individual companies in the group.⁵³

With respect, such findings are something of a stretch. They discard altogether the risk allocation considerations relied on by the High Court in *Woolcock*, and only serve to uphold the ongoing reliance on anomalous policy considerations such as indeterminacy. Nonetheless, her Honour concluded that *Fortuna's* arrangements were sufficiently notorious within the Australian fishing industry such that it was reasonable to infer that such arrangements were within the means of knowledge of the defendant.⁵⁴

Dutney J also relied upon the supposed 'knowledge' by the defendant of discrete facts concerning the ownership of a private company, saying that although it was not necessary that the defendant have actual knowledge of the arrangements, it was sufficient if it could be inferred that they knew the class to which the plaintiff belonged.⁵⁵

⁵² *The Ship 'Eternal Wind' v Fortuna Seafoods Pty Ltd* [2006] HCA Trans 136 (10 March 2006).

⁵³ [2005] QCA 405 at [16].

⁵⁴ *Ibid* at [17].

⁵⁵ *Ibid* at [108]-[109].

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Jerrard JA (in dissent) was more circumspect. His Honour questioned whether such a class could be ascertained without actual analysis of the documents or facts which established the relationship.⁵⁶

The decision in *Fortuna* highlights the problems which currently beset this area of law in Australia. It is interesting to note the continued unquestioning application of *Caltex* and *Perre*, notwithstanding the decision in *Sullivan*, and its subsequent application in *Woolcock*. It is submitted that a consideration of commercial factors such as risk allocation similar to that discussed by McHugh J in *Woolcock* may have yielded an entirely different result.

When one considers the context of two vessels colliding in open waters, the following passage shows that continued adherence to the current approach can result in findings that border on the absurd:⁵⁷

[110] In this case, there was some further evidence before him but to which the trial judge did not make express reference. This concerned the circularisation of business cards for the business, "Fortuna Australia." This card showed, in addition to the name Fortuna Australia, but in smaller print, the names of both Fishing and Seafoods. It clearly identified them as the operating companies behind the business name. A single address, telephone and facsimile number was provided for Fortuna Australia. The managing director of Fortuna Australia was given as Mike Rowley and his mobile phone number was shown. The card was supplied to prospective purchasers, not only in Australia, but in the United States and Japan and was circulated from late 1996 or early 1997. While this only advances the case a little, it does appear that at least within the markets in which Seafoods operated, which markets were not limited to Australia, the integrated nature of the business and the interrelationship of the two companies was in fact publicly known.

[111] In the absence of any other evidence it was open to the trial judge to conclude that it was within the means of knowledge of the appellant that Fishing was part of an integrated group of related companies which were likely to rely directly on fishing, and, more particularly, on the Melina T, for their incomes. [footnotes omitted]

For present purposes, however, it must be accepted that the approach adopted in *Fortuna* to cases of relational economic loss continues to represent the law in Australia.

⁵⁶ Ibid at [80]

⁵⁷ Ibid at [110]-[111].

Conclusion

The discussion above illustrates that an approach which continues to rely on archaic policy and a desire by the courts to impose what it sees as moral obligations on tortfeasors is destined to founder. The reluctance of courts to consider risk allocation will continue to promote uncertainty in an area of law which is arguably no more settled today than it was 30 years ago when the High Court handed down its decision in *Caltex*.

Conversely, the acceptance of risk allocation as a key factor in determining the existence of a duty of care in cases of relational economic loss would provide a 'bright line', underpinned not by the vagaries of policy, but by the generally accepted principle that no person is immune from the consequences of the risks they take. It remains to be seen if this view will ultimately prevail in Australia.