Economic Loss Rule—*Commercial Painting Co. v. Weitz Co.*: Tennessee's Abrogation of the Economic Loss Doctrine as Applied to Service Contracts

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I. INTRODUCTION

In its broadest form, the "economic loss rule" stands for the proposition that contracting parties who suffer purely economic damages may not recover in tort.[1] The doctrine reasons that, in cases where there are no personal injuries or property damage, contract law—and not the law of tort—provides the appropriate avenue for recovery.[2]

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1. Jeffrey L. Goodman et al., *A Guide to Understanding the Economic Loss Doctrine*, 67 DRAKE L. REV. 1, 2 (2019).

2. *Id.* at 2–3.

This rule originated in the context of products liability,[3] and it exists to preserve the boundary line between contract and tort law when both theories could ostensibly apply.[4] However, "the economic loss rule" is a bit of a misnomer because there is not one unified rule.[5] Instead, there is widespread disagreement about the contours of the doctrine's application and its numerous exceptions.[6]

In *Commercial Painting Co. v. Weitz Co.*, the Tennessee Supreme Court ("Court") addressed for the first time whether Tennessee should recognize an exception to the economic loss rule for service contracts.[7] *Commercial Painting* centers around a contractual dispute between an established commercial contractor, the Weitz Company, and its drywall subcontractor, Commercial Painting Company, during the construction of a retirement community in Shelby County.[8] Commercial Painting asserted both breach of contract and tort claims, including a claim of intentional misrepresentation, after the Weitz Company failed to inform Commercial Painting that the construction schedule would be compressed.[9] This expedited schedule required Commercial Painting to pay for supplemental manpower to bring the project up to speed.[10] Reversing the Court of Appeals' ruling as to the applicability of the economic loss doctrine, the Court held that the economic loss doctrine "only applies in products liability cases and

3. Danielle Sawaya, Note, *Not Just for Products Liability: Applying the Economic Loss Rule Beyond its Origins*, 83 FORDHAM L. REV. 1073, 1075–76 (2014).

4. Vincent R. Johnson, *The Boundary-Line Function of the Economic Loss Rule*, 66 WASH. & LEE L. REV. 523, 546 (2009).

5. Commercial Painting Co. v. Weitz Co., 676 S.W.3d 527, 545 (Tenn. 2023) (Campbell, J., dissenting).

6. Johnson, *supra* note 4, at 529, 533–34. Two prominent exceptions include those for service contracts and contracts involving intentional torts, such as fraud. *See* Flagstaff Affordable Hous. L.P. v. Design All., Inc., 223 P.3d 664, 673 (Ariz. 2010) (applying the economic loss doctrine to construction defect cases) *and* Milan Supply Chain Sols., Inc. v. Navistar, Inc., 627 S.W.3d 125, 147 (Tenn. 2021) (explaining that "fraudulent inducement claims seeking economic losses are excepted because the duty not to commit fraud exists independent of any contract.").

7. *Commercial Painting*, 676 S.W.3d at 542.

8. *Id.*

9. *Id.* at 529–30.

10. *Id.* at 543.

should not be extended to other claims" because extending the doctrine would risk creating a "confusing morass" of exceptions.[11]

The Court's conclusion, while attempting to preserve the protections of tort law,[12] undermines much of the established contract law. Freedom of contract should apply equally to contracts for goods and services, especially when the parties are sophisticated business entities.[13] Further, the Court's holding leaves in dicta the applicability of the fraud exception to the economic loss rule.[14]

Part II of this Comment explores noteworthy legal decisions that established the modern iterations of the economic loss rule. Part III discusses the essential facts and holding of *Commercial Painting*. Part IV then analyzes the reasoning behind the Court's refusal to extend the economic loss rule to service contracts. Part V evaluates some potential pitfalls of the Court's analysis and their likely impact on the law of contract.

II. JUDICIAL HISTORY OF THE ECONOMIC LOSS RULE

The economic loss doctrine is a judicially created rule that developed in response to concerns that products liability and tort law would consume the law of contracts.[15] These two divergent fields of law necessarily impose different remedies because, "[i]n tort law, duties are imposed by law to protect the public from harm, whereas in contract the parties self-impose duties and protect themselves through bargaining."[16] The U.S. Supreme Court first adopted the economic loss doctrine in the products liability context of *E. River S.S. Corp. v. Transamerica Deleval*, holding that Transamerica could not be sued in

11. *Id.* at 533, 542.

12. *Id.* at 540 ("[L]ike the alien in the classic horror film *The Blob*, '[a]t the current pace, the economic loss doctrine may consume much of tort law if left unchecked.'").

13. *Id*. at 550–52 (Campbell, J., dissenting) ("This case merely asks us to treat contracts for services the same as contracts for goods. Because I see no good reason to distinguish between the two, I would hold that the economic-loss doctrine applies here.").

14. *Id.* at 539, 541–42 (majority opinion).

15. Milan Supply Chain Sols., Inc. v. Navistar, Inc., 627 S.W.3d 125, 142 (Tenn. 2021).

16. Long Trail House Condo Ass'n v. Engelberth Constr., Inc., 59 A.3d 752, 756 (Vt. 2012).

tort for the malfunction of a turbine that damaged only itself and caused purely economic harm.[17] The economic loss doctrine has since been adopted in a majority of jurisdictions, but most states have not limited the doctrine to the products liability context in which it originated, leading to a "confusing morass" of exceptions.[18]

In Tennessee, the Court first expressly adopted the economic loss rule in *Lincoln General Insurance v. Detroit Diesel Corp.*, after it was asked to consider whether the "sudden, calamitous event" exception to the economic loss rule applied in Tennessee.[19] Before answering the question, however, the Court officially adopted the economic loss doctrine, noting that the "economic loss doctrine is implicated in products liability cases when a defective product damages itself without causing personal injury or damage to other property."[20]

Later, in *Milan Supply Chain Solutions, Inc. v. Navistar, Inc.*, the Court considered whether to adopt a fraud exception to the economic loss doctrine in cases involving a contract for goods.[21] The

17. E. River S.S. Corp. v. Transamerica Delaval, 476 U.S. 858, 871 (1986) ("[A] manufacturer in a commercial relationship has no duty under either a negligence or strict products-liability theory to prevent a product from injuring itself.").

18. Commercial Painting Co. v. Weitz Co., 676 S.W.3d 527, 533 (Tenn. 2023); *Milan Supply Chain*, 627 S.W.3d at 144 ("Despite its wide acceptance . . . the economic loss doctrine has been aptly described as 'one of the most confusing doctrines in tort law.'").

19. Lincoln Gen. Ins. v. Detroit Diesel Corp., 293 S.W.3d 487, 490 (Tenn. 2009). This case involved a bus catching fire due to an alleged engine defect. The engine fire did not cause personal injury or damage to any property other than the bus itself. Therefore, the Court held that the damage was covered by the economic loss doctrine.

20. *Id.* at 489, 491 ("[T]he remedies available to . . . [the owners of a defective product] should derive from the parties' agreements, not from the law of torts, lest we disrupt the parties' allocation of risk.").

21. Milan Supply Chain Sols., Inc. v. Navistar, Inc., 627 S.W.3d 125, 154 (Tenn. 2021). This case concerns a logistics company (Milan) that agreed to purchase trucks with diesel engines using exhaust gas recirculation ("EGR") technology. Milan was later dissatisfied with the performance of these trucks, but it had previously signed a warranty explicitly stating that "The Company [Navistar] specifically disclaims warranties of merchantability and fitness." *Id.* at 133. The Court found that the economic loss doctrine barred Milan's fraudulent inducement claim because Milan was a sophisticated business entity that contracted around the general warranty of merchantability.

Milan Court adopted a narrow exception for fraud, which operates to bar an economic loss claim only when the alleged fraud concerns the "quality, reliability, and character of *the goods that are the subject of a contract between sophisticated business entities.*"[22] However, the *Milan* Court notably did not resolve the broader question of whether there may ever be an exception for fraud outside of the products liability context because the product at issue in *Milan* was a defective truck, and there was no service component to the contract.[23] Yet, in reaching its decision, the *Milan* Court relied heavily on *HealthBanc International, LLC v. Synergy Worldwide, Inc.*, which did address non-goods contracts—in this case, a licensing agreement—and held that the "economic loss rule applies to fraudulent inducement claims that overlap completely with a breach of contract claim[,]" even if there are no goods involved.[24]

Other states have explicitly extended the economic loss doctrine to service contracts. The Supreme Court of Nevada held that contract law provides the appropriate remedy when the work of construction contractors is deemed defective.[25] Further, some states have declined

22. *Id.* at 154. (emphasis added).

23. Commercial Painting Co. v. Weitz Co., 676 S.W.3d 527, 532–33 (Tenn. 2023).

24. HealthBanc Int'l, LLC v. Synergy Worldwide, Inc., 435 P.3d 194, 198 (Utah 2018) ("In so holding we do not foreclose the possibility of a fraudulent inducement exception in some other circumstance."). HealthBanc is a product developer who sold a "greens formula" to Synergy, a multi-level marketing distributor. In the royalty agreement, HealthBanc assigned its rights to the greens formula to Synergy, and Synergy agreed to pay HealthBanc a royalty for use of the product. HealthBanc later sued Synergy for failing to pay the royalty agreement on certain sales, and Synergy filed a counterclaim asserting that HealthBanc did not own the greens formula. Synergy's claim alleges both breach of contract and fraudulent inducement on the ground that HealthBanc misrepresented that it "had the exclusive right to use, assign[,] or sell the Specified Greens Formula and its associated intellectual property rights." *Id.* at 195. Because the two claims overlap, the Court held that damages could be assessed under the breach of contract theory.

25. Terracon Consultants W., Inc. v. Mandalay Resort Grp., 206 P.3d 81, 90 (Nev. 2009). Mandalay hired Terracon to prepare a geotechnical report with recommendations for the foundation design of Mandalay's planned resort. Based on Terracon's soil analysis and the projected weight of the building, Terracon predicted a certain amount of soil setting under the resort's foundation. However, the actual amount of soil settling exceeded Terracon's projections and required Mandalay to repair and reinforce the foundation before proceeding with construction. The Court

to make an exception even in the event of fraud; for example, in *Bakke v. Magi-Touch Carpet One Floor and Home, Inc.*, the North Dakota Supreme Court ruled that the remedy for fraud is rescission of the contract and expectation damages.[26] The Court reasoned that fraud and contract claims are mutually exclusive remedies because evidence of fraud terminates a contract from its inception through its recission.[27] Moreover, in *Filak v. George*, the Virginia Supreme Court found that even in cases involving affirmative misrepresentations, tort claims are improper if the breached duty stems from the parties' contractual relationship rather than an independent duty imposed by law.[28] Contract law should govern such disputes because contractual duties are assumed only by the parties' mutual agreement.[29]

III. *COMMERCIAL PAINTING, CO. V. WEITZ CO.*

In *Commercial Painting*, an established construction company, the Weitz Company, and its drywall subcontractor, Commercial Painting, Inc., entered a contract for the outfitting of a retirement

found that the economic loss doctrine applies to bar claims against design professionals when the design defects have caused only economic losses.

26. Bakke v. Magi-Touch Carpet One Floor & Home, Inc., 920 N.W.2d 726, 733 (N.D. 2018) ("Fraud, if asserted, terminates the contract at its inception through the rescission."). Bakke entered into a contract for Magi-Touch to install a shower and floor tiles in his home. *Id.* at 729. Bakke alleged the shower door was improperly installed, causing the shower door to implode. *Id.* The Court, finding no fraud, held that the contract relationship covered the property damage. *Id.* at 733. But, if fraud were found, the remedy would be rescission of the contract. *Id.*

27. *Id.*

28. Filak v. George, 594 S.E.2d 610, 613 (Va. 2004) ("[L]osses suffered as a result of the breach of a duty assumed only by agreement, rather than a duty imposed by law, remain the sole province of the law of contracts."). In this case, an insurance agent promised that an insurance policy would cover the "total replacement costs" of an insured house. *Id.* at 611. But, after the house burned down, the plaintiffs only received the "actual cash value" of the house, not the money required to rebuild the home. *Id.* at 612. The court held that constructive fraud is not actionable when the claim alleges negligent performance of contractual duties. *Id.* at 614. ("[W]hen a plaintiff alleges and proves nothing more than disappointed economic expectations, the law of contracts, not the law of torts, provides the remedy for such economic losses.").

29. *Id.* at 614.

community in Shelby County.[30] The parties executed a standard form subcontract agreement, which addressed in detail the scope of the work to be completed, the available remedies in the case of a breach, and the project schedule.[31] The contract specifically provided that Weitz could charge Commercial Painting for the cost of any additional work needed to "'assist [Commercial Painting] in performing its obligations' under the subcontract, including 'supplemental manpower.'"[32] However, Commercial Painting alleged that Weitz made fraudulent misrepresentations by not communicating that the project was significantly behind schedule, requiring the construction schedule to be greatly compressed and supplemental manpower to be hired at Commercial Painting's expense.[33]

Commercial Painting sued Weitz for compensatory and punitive damages, asserting both contract and tort claims, including negligent and intentional misrepresentation.[34] The trial court upheld the viability of Commercial Painting's claims of intentional misrepresentation and found that Commercial Painting was entitled to compensatory and punitive damages against Weitz.[35] The Court of Appeals subsequently reversed the award of punitive damages, finding that the economic loss doctrine applied and precluded Commercial Painting from recovering damages in tort.[36] Instead, the Court said that Commercial Painting should be limited to the remedies it had agreed to in the subcontract, which explicitly excluded damages in tort.[37] Finally, the Tennessee Supreme Court granted Commercial Painting's appeal to decide whether the Court of Appeals erred in extending the economic loss doctrine to the facts of this case.[38]

30. Commercial Painting Co. v. Weitz Co. , 676 S.W.3d 527, 529, 542 (Tenn. 2023).

31. *Id.* at 543 (Campbell, J., dissenting). Specifically, "Commercial Painting 'waive[d] and release[d] [Weitz] from any and all [c]laims for such delay damages, including without limitation [c]laims attributable to breach of contract or tort.'" *Id.*

32. *Id.*

33. *Id.* at 544.

34. *Id.*

35. *Id.*

36. *Id.*

37. *Id.*

38. *Id.* at 544–45.

Finding that the "extension of the economic loss doctrine to services threatens to engulf longstanding common law torts for the inadequate or incompetent performance of professional services," the Court held that the economic loss doctrine only applies in the context of products liability cases and should not be extended to service contracts.[39] The Court also found that:

> Commercial Painting's claim of intentional misrepresentation was not predicated merely on a breach of the contract; it was predicated on the fact . . . that Weitz deliberately made false representations about the timing and amount of work involved in the subcontract "in order to mislead Commercial Painting to obtain an undue advantage over it."[40]

Further, the Court reasoned that parties to a contract, even sophisticated business entities, cannot be expected to anticipate fraud among the potential risks of contracting; therefore, Commercial Painting could not have been expected to factor the risk that Weitz was making false representations into its calculations.[41]

IV. *COMMERCIAL PAINTING* ANALYZED

Today, when contracting in Tennessee, parties are authorized to sue in tort for breach of all service contracts.[42] The majority, relying on its determination that there are already existing safeguards against disproportionate liability in Tennessee, found that the expansion of the

39. *Id.* at 540 (quoting Daniel Rapaport et al., *Tort Killer: The Applicability of the Economic Loss Doctrine to Service Contracts*, 20 ME. B.J. 100, 103 (2005)).

40. *Id.*

41. *Id.*

42. *Id.*

economic loss rule was not "necessary."[43] However, Tennessee is one of only four jurisdictions to do so.[44]

Legal scholars have raised concerns that the Court's decision is likely to discourage contracting for services in Tennessee because even if a contract purports to exclude recovery of incidental, consequential, or punitive damages, the Court may decide to override the contracting parties' stated intent.[45] This threatens to abrogate the agency of contracting parties. The dissent recognizes this, expressing concerns about the erosion of contract law.[46] Justice Campbell argued that "[b]y altogether refusing to extend the economic-loss doctrine to contracts for services, the majority opinion opens the door to any and all tort claims, including those alleging nothing more than negligent performance of the contract."[47] Moreover, the detailed and comprehensive nature of construction projects makes them especially susceptible to economic risk, and the Court's ruling threatens the industry as parties become less able to effectively allocate risk.[48] Indeed, as the *Terracon* Court noted, "imposing unbounded tort

43. *Id.* at 541 ("[T]he common law of damages, contracts, and torts has developed to adequately equip courts to guard against and reject claims that involve overly speculative, excessive, or unforeseeable losses.").

44. *Id.* at 549 (Campbell, J., dissenting) (noting that Minnesota, Wisconsin, and Florida are the only states that have declined to apply the economic loss doctrine to service contracts).

45. Cannon Allen & John Woods, Feature Story: *A Reversal of Fortune: Tennessee Supreme Court Rules Economic Loss Doctrine Only Applies to Products Liability Cases*, 60 TENN. B.J. 30, 42 (2024) ("[The Court] has made plain that commercial contracts for services that purport to exclude recovery of incidental, consequential and punitive damages may not actually exclude the recovery of such damages . . . .").

46. *Commercial Painting*, 676 S.W.3d at 546–47 (Campbell, J., dissenting).

47. *Id.* at 551.; *see also* Allen & Woods, *supra* note 45, at 31.

48. *Commercial Painting*, 676 S.W.3d at 548 (Campbell, J., dissenting) (quoting City Express, Inc. v. Express Partners, 959 P.2d 836, 839–40 (Haw. 1998) ("Construction projects are characterized by detailed and comprehensive contracts that form the foundation of the industry's operations.")); *see also id.* (quoting Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1, 881 P.2d 986, 992 (Wash. 1994) ("We hold parties to their contracts. If tort and contract remedies were allowed to overlap, certainty and predictability in allocating risk would decrease and impede future business activity. The construction industry in particular would suffer, for it is in this industry that we see most clearly the importance of the precise allocation of risk as secured by contract.")).

liability for pure financial harm could result in 'incentives that are perverse,' such as insurance premiums that are too expensive for the average economic actor to afford."[49]

V. OPINION AND CRITIQUE

Desiring to avoid the confusion that may result from perpetuating a rule with many exceptions, the Court in *Commercial Painting* declined to extend the economic loss rule to service contracts.[50] However, by so doing, the Court further muddled Tennessee contract law by adopting a standard which departs from settled principles of contract law.[51]

Freedom of contract is one of the bedrock principles of contract law.[52] Historically, courts in Tennessee have declined to consider whether contract terms constitute a good bargain when the contract is supported by proper consideration.[53] This is especially true when contracts are formed between sophisticated business entities, which are presumed to have equal bargaining power and experience.[54] However, the Court's holding in *Commercial Painting* implicitly posits that sophisticated business entities are incapable of handling their own affairs.[55]

In *Commercial Painting*, the subcontract specifically included provisions outlining the remedies available in case of a breach, "provid[ing] that, 'in no event' would the general contractor have to pay any special or consequential damages."[56] Allowing Commercial Painting to bypass the contract remedies expressly agreed to at the time of contract formation explicitly undercuts the strength of contracts in

49. Terracon Consultants W., Inc. v. Mandalay Resort Grp., 206 P.3d 81, 88 (Nev. 2009).

50. *Commercial Painting*, 676 S.W.3d at 538.

51. *Id.* at 551 (Campbell, J., dissenting).

52. Milan Supply Chain Sols., Inc. v. Navistar, Inc., 627 S.W.3d 125, 154 (Tenn. 2021) ("'[T]he individual right of freedom of contract is a vital aspect of personal liberty' in Tennessee.") (citing Baugh v. Novak, 340 S.W.3d 372, 382 (Tenn. 2011)).

53. *Milan Supply Chain Sols.*, 627 S.W.3d at 153–54.

54. *Id.* at 154.

55. *Commercial Painting*, 676 S.W.3d at 541.

56. *Id.* at 543 (Campbell, J., dissenting).

Tennessee. It is also likely to increase the risk of contracting in the future, as contracting parties will no longer be able to trust that the Court will uphold the terms of the bargain.[57] Furthermore, the traditional remedy for breach of contract is expectation damages, and parties can increase certainty by including a liquidated damages clause.[58] As a matter of fairness, why should a party benefit from remedies that are better than the ones for which they bargained?

Moreover, service contracts comprise a great percentage of all contracts in Tennessee, and a breached contract will almost always include an economic loss of some kind.[59] If the Court's decision stands, it will greatly impede the proper allocation of risk as service providers will now be compelled to insure themselves against tort damages, which greatly exceed the recovery permitted under the expectation damages of contract law.[60] Instead, the Court should have adopted a rule like the one in *Filak*, which provides that losses suffered as a result of the breach of a duty assumed only by contract—instead of a duty imposed by law—should remain the "province of the law of contracts."[61]

Lastly, as the Court acknowledged, the central issue of this case was fraud and not merely a breach of contract.[62] However, by

57. Allen & Woods, *supra* note 45, at 42 ("The unmistakable ruling is that in a non-product liability context, an aggrieved party to a breach [sic] contract might be able to collect much more than contract damages permitted under the parties' agreement.").

58. *Milan Supply Chain Sols.*, 627 S.W.3d at 155 (quoting HealthBanc Int'lv. Synergy Worldwide, Inc., 435 P.3d 193, 197–98 (Utah 2018)) ("The possibility of liquidated damages seems particularly salient. If the parties to a contract with express warranties are concerned about the insufficiency of expectation damages[,] they can bargain for liquidated damages. And where they fail to do so it seems problematic for a court to make a better contract for them than the one they negotiated—by importing tort remedies into the deal.").

59. *Commercial Painting*, 676 S.W.3d at 551 (Campbell, J., dissenting).

60. *Milan Supply Chain Sols.*, 627 S.W.3d at 143–44 (quoting E. River S.S. Corp. v. Transamerica Delaval Inc., 476 U.S. 858, 874 (1986)) (noting that losses sustained by a commercial user when a product injures itself are typically losses that can be insured against, but "[p]ermitting recovery [in tort] for all foreseeable claims for purely economic loss could make a manufacturer liable for vast sums").

61. Filak v. George, 594 S.E.2d 610, 618 (Va. 2004) ("[W]hen a plaintiff alleges and proves nothing more than disappointed economic expectations, the law of contracts . . . provides the remedy for such economic losses.").

62. *Commercial Painting*, 676 S.W.3d at 539.

decreeing the economic loss rule inapplicable to service contracts writ large, the Court misses a crucial opportunity to settle the question of fraud. Although the Court called into question the narrow fraud exception previously adopted in *Milan*, the Court's view of fraud was left in dicta because its holding only related to the applicability of the economic loss rule to service contracts.[63] Thus, the fraud exception is an open question that desperately needs to be decided because fraud is relevant not just to service contracts but also to contracts for goods.

63. *Id.* ("Contracting parties in Tennessee, including those in the construction industry, should not have to factor into their decision to enter a contract the potential for fraud or another party's dishonesty.").