Armstead v Royal & Sun Alliance Insurance Company Limited: Case Note

A recent decision in a lower court, now possibly on its way to the Court of Appeal, has opened up interesting legal questions on the extent of a negligent party's liability in bailment and tort for damage to hired equipment.

Legal argument in a two day appeal hearing, in front of Recorder Benson KC sitting in the County Court, focused on the extent of a negligent third party's duty of care; whether liquidated damages due under a hire contract by a bailee of hired equipment were recoverable in an action brought by the bailee against a negligent third party, whatever the amount of those liquidated damages; and whether a claim for recovery of such liquidated damages from the negligent third party (who was not a party to the hire contract) amounted to a claim for pure economic loss and / or a claim for recovery of a relational economic loss by the bailee.

The factual matrix may be briefly summarised as follows: Person A negligently damages property that has been hired by Person B. The hire contract provides that Person B is obliged to pay the hire company liquidated damages for the period that the damaged property is unavailable, for example, during repairs. These liquidated damages that Person B is subject to are calculated by reference to the contractual hire rate. The hire company demands payment and Person B seeks payment from Person A of the sums demanded under the hire contract. Is Person A liable for such sums?

So opens up an interesting legal question on the extent of Person A's duty of care and scope of the proprietary fiction in bailment. The decision by Recorder John Benson KC, on appeal in *Armstead v Royal & Sun Alliance Insurance Company Limited*, gives answers to these questions.

The legal analysis of the above situation is in some ways straightforward: (a) Person B was the bailee of the hired property; (b) therefore Person B enjoyed possessory title to the hired property and can claim for the physical damage to it; (b) Person A owed Person B a duty of care; (c) Person A breached that duty of care by negligently damaging the property.

There can be no doubt that Person A is liable to Person B for the physical damage to the property, but what else is Person A liable for?

This note considers three of the key arguments that the Judge in Armstead addressed:

- That the liquidated damages that Person B is subject to are pure economic loss (and a subset of such loss, namely a relational economic loss) to which there is no entitlement.
- That the claim for liquidated damages was based on an expansion of the so called proprietary fiction in bailment and that expansion was unacceptable.
- That Person A had a duty of care to prevent liabilities in contracts agreed by Person B with third parties, or that it was fair just and reasonable for the court to impose such a duty of care on Person A.

The reality of the situation

In the Judges' reasoning can be seen an appreciation for the reality of the claim [28]: The hire company was the entity who had suffered the loss of use of their property. As the Judge observed, the only sensible analysis of this situation is

4 Pump Court, Temple, London, EC4Y 7AN
T: +44 (0)20 7842 5555 F: +44 (0)20 7583 2036
www.4pumpcourt.com

that Person B (the bailee) is claiming for and on behalf of the hire company (the bailor) to compensate them for their loss of use. The contractual mechanism placing liability on the bailee is the link in the chain for such an arrangement.

However, the judge acknowledged [41] – [45], this is a convenient arrangement for a bailor, who can likely expect to recover more when their bailee claims for the contractual sum demanded (being the full hire rate), than if they (the bailor) brought their own claim for loss of use (being at most their loss of profit), something which they would be entitled to do.

Unacceptable expansion

The claim was based on the proprietary fiction in bailment: The Claimant argued that, as bailee, the Claimant had possessory title to the damaged asset, and could sue to recover liquidated damages that the Claimant had agreed with the owner of the damaged asset (the hire company) prior to the accident. At [63] the Judge discussed relevant case law and consideration of the limits of proprietary fiction in *Palmer on Bailment*, before deciding at [73] that the disputed claim amounted to an unacceptable expansion of the proprietary fiction in bailment.

Duty of Care

The Judge accepted [47] that it was foreseeable that damage to a hired asset might give rise to loss of use either by the hirer who was using the asset at the time it was damaged (Person B) and/or by the hire company, who owned the asset. It was not in dispute there was sufficient proximity between Person A and Person B [49].

In *Conarken Group Ltd v Network Rail Infrastructure Ltd* 2011 EWCA Civ. 644 the Court of Appeal had considered the liability of a tortfeasor who had damaged the railway infrastructure to Network Rail. Part of the loss suffered by Network Rail was loss of revenue due to sums that Network Rail had to pay as compensation to train operating companies under track access agreements.

The Court of Appeal held in Conarken that, subject to the issue of remoteness, loss of revenue was recoverable from the tortfeasor.

Influential on the Judge's reasoning appears to be the following statement of the law from Conarken (Pill LJ at [69]):

> It is not open to a party to dictate to the whole world the extent of tortious liability and what is reasonably foreseeable and not too remote in order to achieve what it regards as a satisfactory contract with a third party. It could lead to ever more ingenious attempts to attribute possible losses to a tort and would be inimical to the simple solution desired.

The Judge in Armstead noted that [55]:

> It is I believe too simplistic for the claimant to say that, because some loss of use was a reasonably foreseeable consequence of the damage, all financial loss reflected in Clause 16 is recoverable.

Therefore, whereas in *Conarken* the Court of Appeal held that loss of profits were recoverable, the Judge in *Armstead* considered [57] that the sums owed by the Claimant to the hire company were not recoverable. Finding that there was no duty of care and that it would not be just and reasonable to impose a duty of care of a nature and extent which will

4 Pump Court, Temple, London, EC4Y 7AN
T: +44 (0)20 7842 5555 F: +44 (0)20 7583 2036
www.4pumpcourt.com

avoid the claimant from the contractual liability to a third-party.

Is the loss a Relational Economic Loss?

It is well established that where Person A damages property by a negligent act or omission, the owner of that property is entitled to recover for resulting economic loss.

But what of a situation where the Claimant is not the owner of the property, seeks to claim from the tortfeasor for the economic loss suffered because of their relationship (such as a contractual relationship) with the owner of the property?

The editors of both Charlesworth & Percy on Negligence and Clerk & Lindsell on Torts describe (in different terms) a rule that such losses are not recoverable. *Clerk & Lindsell* puts it in the following terms (8-144):

> 'The general rule has been that no duty is owed by a defendant who negligently damages property belonging to a third party to a claimant who suffers because of a dependence upon that property or its owner. The general rule is that no duty is owed to the plaintiff in such a situation.'

Charlesworth & Percy's formulation of the rule (2-233) reads:

> '*Financial loss that occurs only because of the relationship between the immediate, physical, victim of a wrong and the claimant is conveniently, and quite commonly, called relational financial loss. At common law this is usually irrecoverable.*
>
> *In the case of damage to property the (equivalent) rule denies recovery for financial loss stemming from damage to the property of another person.'*

The Judge [37] – [39], expressed the application of this rule to be a point of some difficulty, but considered that this case fell within this exclusionary rule and was a relational economic loss, finding assistance in a 19th century authority (*Cattle v Stockton Waterworks*).

In *Cattle* the defendant had laid a defective water main under a road. Leaks caused by this defective work delayed the contractor's work of tunnelling beneath the road. That delay caused the Contractor to suffer a loss of profit on their contract with the road owner. The financial loss (loss of profit) only occurred because of the relationship between the immediate, physical victim of the wrong (the road owner) with whom the contractor (claimant) had a contract. The loss was held irrecoverable.

Applying the principles in a similar way, the Judge found that the hired property was owned by the hire company, and the loss said to have been suffered by the hirer (Person B) was an economic loss suffered because of the hire contract with the owner, and therefore irrecoverable because of the rule. The Judge also found that the claim did not fall within one of the few well-recognised exceptions to the rule.

Conclusion

These interesting questions, and the answers given in *Armstead*, on the extent of a duty of care and the scope of the proprietary fiction in bailment as well as the rule against relational economic loss will be of interest to practicioners in a

4 Pump Court, Temple, London, EC4Y 7AN
T: +44 (0)20 7842 5555 F: +44 (0)20 7583 2036
www.4pumpcourt.com

large number of areas. The decision in *Armstead* on these points provides very helpful guidance for cases on these and similar facts.

Written by Jonathan Schaffer-Goddard

4 Pump Court, Temple, London, EC4Y 7AN
T: +44 (0)20 7842 5555 F: +44 (0)20 7583 2036
www.4pumpcourt.com