

FRAUD AND MISREPRESENTATION CLAIMS AGAINST LAWYERS

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INTRODUCTION

Most lawyers are competent, diligent, and honest. No lawyer is immune to error, however, and some are guilty of serious misjudgments. When lawyers allegedly err in the course of clients' representations, or, worse, allegedly engage in deliberate misconduct, aggrieved clients may sue for professional negligence, commonly described as legal malpractice, or for breach of fiduciary duty.¹ A lawyer who treats a client dishonestly may face liability on either of

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¹ Liability for legal malpractice generally requires a plaintiff to prove the existence of an attorney-client relationship, giving rise to a duty of care on the lawyer's part, breach of that duty, proximate cause, and damages. *In re Estate of Powell*, 12 N.E.3d 14, 19 (Ill. 2014); *Sabin v. Ackerman*, 846 N.W.2d 835, 839 (Iowa 2014); *Harris v. O'Connor*, 842 N.W.2d 50, 54 (Neb. 2014). Breach of fiduciary duty and legal malpractice generally are separate causes of action. *Slovensky v. Friedman*, 49 Cal. Rptr. 3d 60, 72 (Ct. App. 2006) (quoting *Stanley v. Richmond*, 41 Cal. Rptr. 2d 768, 776 (Ct. App. 1995)). The elements of the causes of ac-

these theories.² Lawyers' alleged dishonesty in their practices exposes them to potential liability to third parties as well. For example, if a lawyer knowingly and substantially assists or encourages a client's wrongdoing, those who are harmed by the client's misconduct may sue the lawyer in tort for allegedly aiding and abetting the client's misdeeds.³ Yet, while the potential consequences of lawyers' alleged dishonesty should be apparent, lawyers seldom consider themselves at risk for liability based on fraud or misrepresentation arising out of clients' representations. This perspective probably traces, at least in part, to common notions of litigation practice, where parties generally cannot base fraud claims on opposing lawyers' misrepresentations.⁴ Any comfort lawyers derive from this impression, however, overlooks three key points. First, lawyers may be sued for fraud or negligent misrepresentation by adversaries in litigation, as where, for example, they are alleged to have knowingly misrepresented material facts in negotiations.⁵ Second, transactional practice is such that business lawyers are natural targets of fraud and negligent misrepresentation claims by third parties based on alleged false statements and failures to disclose infor-

tion, however, are similar. Liability for breach of fiduciary duty requires a plaintiff to prove "(1) the existence of a fiduciary duty; (2) breach of the fiduciary duty; and (3) damage proximately caused by the breach." *Id.* (quoting *Stanley*, 41 Cal. Rptr. 2d at 776); *see also* *Robert T. McLean Irrevocable Trust v. Patrick Davis, P.C.*, 283 S.W.3d 786, 792–93 (Mo. Ct. App. 2009) (quoting *Koger v. Hartford Life Ins. Co.*, 28 S.W.3d 405, 411 (Mo. Ct. App. 2000)). Some states distinguish between legal malpractice claims based on alleged professional negligence, or a breach of the standard of care, and an alleged breach of fiduciary duty, sometimes described as a breach of the standard of conduct. *See, e.g.*, *Crist v. Loyacono*, 65 So. 3d 837, 842 (Miss. 2011) (employing this terminology). Other states merge the causes of action where the lawyer's alleged misstep is both a breach of the standard of care and a breach of fiduciary duty. *See, e.g.*, *Klemme v. Best*, 941 S.W.2d 493, 496 (Mo. 1997) ("If the alleged breach can be characterized as both a breach of the standard of care (legal malpractice based on negligence) and a breach of a fiduciary obligation (constructive fraud), then the sole claim is legal malpractice.").

² *See, e.g.*, *Charnay v. Cobert*, 51 Cal. Rptr. 3d 471, 480–81, 481 n.12 (Ct. App. 2006) (stating that "billing for work not performed or performed by others with lower billing rates than those charged constitutes a breach of fiduciary duty"); *Capital Care Corp. v. Hunt*, 847 A.2d 75, 84 (Pa. Super. Ct. 2004) ("[A]n attorney who undertakes representation of a client owes that client both a duty of competent representation and the highest duty of honesty, fidelity, and confidentiality. An *intentional* misrepresentation to a client during any transaction where an attorney represents that client is clearly a violation of that attorney's duty of honesty.") (citation omitted).

³ *See* *Frederico v. Maric*, 226 P.3d 403, 405 (Ariz. Ct. App. 2010) (listing elements of the tort of aiding and abetting); *Tensfeldt v. Haberman*, 768 N.W.2d 641, 649 n.12 (Wis. 2009) (same). *See generally* Douglas R. Richmond, *Lawyer Liability for Aiding and Abetting Clients' Misconduct Under State Law*, 75 DEF. COUNS. J. 130 (2008) (exploring aiding and abetting claims against lawyers).

⁴ *Safeway Ins. Co. v. Guerrero*, 106 P.3d 1020, 1029 (Ariz. 2005).

⁵ *See, e.g.*, *Slotkin v. Citizens Cas. Co. of N.Y.*, 614 F.2d 301, 314 (2d Cir. 1979) (reasoning that jury reasonably could have found lawyer liable for fraud under New York law for misrepresenting the amount of insurance coverage available to settle the plaintiff's medical malpractice claim).

mation.⁶ Third, clients may sue their own lawyers for alleged fraud and misrepresentation in appropriate cases.⁷

In fact, fraud and misrepresentation are common theories of liability in suits against lawyers by both clients and third parties.⁸ In 2012, for example, the Cincinnati law firm of Dinsmore & Shohl LLP suffered a \$12.6 million judgment after a jury found the firm and one of its partners, Harvey Cohen, liable for fraud and negligent misrepresentation.⁹ Cohen had represented Douglas Machine & Tool Co. in its sale to TurboCombustor Technology Inc.¹⁰ He allegedly knew of a Douglas Machine shareholder dispute that substantially lowered the company's value but he did not disclose the dispute to TurboCombustor in connection with the sale.¹¹ TurboCombustor alleged that it would not have purchased Douglas Machine had it known of the shareholder dispute.¹² In addition to awarding compensatory damages, the jury found that Dinsmore & Shohl was liable for punitive damages, but that aspect of the case was bifurcat-

⁶ See, e.g., *Cromeans v. Morgan Keegan & Co.*, 69 F. Supp. 3d 934, 938–40 (W.D. Mo. 2014) (permitting the plaintiff to pursue a negligent misrepresentation claim against a law firm for allegedly false statements in a bond offering); *Farmers State Bank v. Huguenin*, 469 S.E.2d 34, 36–37 (Ga. Ct. App. 1996) (reversing summary judgment for lawyer on bank's claim that lawyer for borrower failed to disclose cloud on title to real estate to be used to secure loan); *Taylor v. Riley*, 336 P.3d 256, 272 (Idaho 2014) (permitting non-client's suit against lawyer based on allegedly false statements in an opinion letter); *Hansen v. Anderson, Wilmarth & Van Der Maaten*, 630 N.W.2d 818, 827 (Iowa 2001) (permitting lawyer to sue opposing counsel for indemnity based on falsified documents presented during the sale of a business); *Dean Foods Co. v. Pappathanasi*, No. Civ.A. 01-2595 BLS, 2004 WL 3019442, at *11–21 (Mass. Super. Ct. Dec. 3, 2004) (concluding that a law firm committed negligent misrepresentation in issuing an opinion letter); *JJJ Walker, LLC v. Yollick*, 447 S.W.3d 453, 459–73 (Tex. App. 2014) (concluding that a lawyer could be liable for fraud while acting as a bank's agent).

⁷ See, e.g., *Bryant v. Robledo*, 938 So. 2d 413, 419 (Ala. Civ. App. 2005) (permitting fraud claim against lawyer for lawyer's attempt to obtain fees to represent an incompetent client); *Ratcliff v. Boydell*, 674 So. 2d 272, 280 (La. Ct. App. 1996) (concluding that lawyer defrauded client by inflating value of structured settlement to obtain an excessive contingent fee); *Vt. Mut. Ins. Co. v. McCabe & Mack, LLP*, 964 N.Y.S.2d 160, 163 (App. Div. 2013) (holding that client stated fraud claim by alleging that lawyers said they had filed a motion for default judgment when they had not done so and billed the client for preparing the phantom motion).

⁸ See RONALD E. MALLEN & ALLISON MARTIN RHODES, 1 LEGAL MALPRACTICE § 8:31 (2015 ed.) (“Fraud is a common claim, easy to allege, and often accompanied by other theories.”).

⁹ Jon Newberry, *Law Firm Dinsmore & Shohl Hit with \$12.6 Million Judgement*, CINCINNATI BUS. COURIER (Oct. 26, 2012, 2:55 PM), <http://www.bizjournals.com/cincinnati/blog/2012/10/law-firm-dinsmore-shohl-hit-with.html>; Nate Raymond, *Dinsmore Hit with \$12.6 Mln Fraud Verdict*, REUTERS (Oct. 29, 2012), [http://newsandinsight.thomsonreuters.com/Legal/News/2012/10_October/Dinsmore_hit_with_\\$12.6 mln_fraud_verdict](http://newsandinsight.thomsonreuters.com/Legal/News/2012/10_October/Dinsmore_hit_with_$12.6 mln_fraud_verdict).

¹⁰ Newberry, *supra* note 9; Raymond, *supra* note 9.

¹¹ Newberry, *supra* note 9; Raymond, *supra* note 9.

¹² Newberry, *supra* note 9; Raymond, *supra* note 9 (reporting TurboCombustor's claim that the undisclosed shareholders' dispute lowered Douglas Machine's value from \$19 million to \$4 million).

ed, and the firm confidentially settled with TurboCombustor before the jury could reconvene to weigh punitive damages.¹³

Fraud and misrepresentation claims pose an array of challenges for targeted law firms and lawyers. Fraud claims may support punitive damage awards in cases where punitives would not otherwise be recoverable, or open the door to discovery that a court might refuse if only the lawyer's professional negligence was in dispute.¹⁴ Because the presence of fraud normally is a question of fact,¹⁵ well-pleaded fraud claims are difficult for defendants to defeat at the motion to dismiss stage. Similarly, "[a] claim for negligent misrepresentation is ordinarily one for a jury, unless the undisputed facts are so clear as to permit only one conclusion,"¹⁶ thus devaluing a motion to dismiss as a defense tactic in many cases. Again, because fraud and negligent misrepresentation claims are fact-intensive,¹⁷ a plaintiff may be able to avoid summary judgment, and by forcing the defendant to contemplate the risk of trial, achieve a favorable settlement. Fraud and negligent misrepresentation claims are particularly valuable to plaintiffs who cannot establish the existence of an attorney-client relationship with a lawyer-defendant because they avoid the general requirement of privity for liability based on professional negligence.¹⁸ *First Ark. Bank & Trust v. Gill Elrod Ragon Owen & Sherman, P.A.*,¹⁹ is an illustrative case.

First Arkansas arose out of a failed attempt by a limited liability company known as Dream Team to develop a residential subdivision called Belclaire.²⁰ Dream Team formed a municipal improvement district to issue tax-free municipal bonds to finance streets, sewers, and other public improvements in

¹³ Kimball Perry, *Dinsmore Settles Second Half of \$12.6M Suit*, CINCINNATI.COM (Nov. 26, 2012, 3:35 PM), <http://www.cincinnati.com/article/20121126/news0107/311260075>.

¹⁴ See RESTATEMENT (SECOND) OF CONTRACTS § 355 (AM. LAW INST. 1981) ("Punitive damages are not recoverable for a breach of contract unless the conduct constituting the breach is also a tort for which punitive damages are recoverable."); 1 MALLEEN & RHODES, *supra* note 8, § 23:6 (explaining that fraud is separate from legal malpractice and that the fraud is usually alleged to support a claim for punitive damages).

¹⁵ *Chism v. Protective Life Ins. Co.*, 234 P.3d 780, 787 (Kan. 2010); *Croslin v. Enerlex, Inc.*, 308 P.3d 1041, 1046 (Okla. 2013).

¹⁶ *Nota Constr. Corp. v. Keyes Assocs., Inc.*, 694 N.E.2d 401, 405 (Mass. App. Ct. 1998).

¹⁷ See *St. Louis v. Wilkinson Law Offices, P.C.*, 55 A.3d 443, 447 (Me. 2012) ("Whether a party made a misrepresentation and whether the opposing party justifiably relied on a misrepresentation are questions of fact.").

¹⁸ See, e.g., *Fortress Credit Corp. v. Dechert LLP*, 934 N.Y.S.2d 119, 121–22 (App. Div. 2011) (concluding that the plaintiffs' professional negligence claim failed for a lack of privity but finding that the plaintiffs could maintain a negligent misrepresentation claim against the law firm based on relationship of near-privity before exonerating the firm); *Ginsburg Dev. Cos., LLC v. Carbone*, 926 N.Y.S.2d 156, 157–58 (App. Div. 2011) (noting that legal malpractice allegations predicated on fraud avoid the privity requirement); *Credit Union Cent. Falls v. Groff*, 966 A.2d 1262, 1271 (R.I. 2009) ("Fraud is a well-settled exception to the privity requirement that historically bars nonclient recovery for attorney malpractice.").

¹⁹ 427 S.W.3d 47 (Ark. 2013).

²⁰ *Id.* at 49.

Belclaire.²¹ The district hired Christopher Travis of the Gill law firm as bond counsel. Travis prepared the preliminary official statement (“POS”) and official statement (“OS”) that were provided to the underwriter, American Municipal Securities, Inc. (“AMS”), for use in marketing the bonds.²² The district issued two series of bonds, Series A and Series B. The Series B bonds were backed by a mortgage on land in Belclaire that Dream Team owned and by capital use improvement fees that Dream Team was to collect.²³ The POS and OS did not identify a prior mortgage held by First Federal Bank securing the loan used to purchase the land for Belclaire.²⁴ AMS sold the Series B bonds to Arkansas Banker’s Bank, which retained some and sold the remainder to other banks.²⁵

Dream Team defaulted on payment of the capital use improvement fees and on the First Federal mortgage.²⁶ The banks that purchased the Series B bonds sued the Gill firm for legal malpractice, violations of the Arkansas Securities Act, and fraud. They alleged that Travis failed to disclose in the bond offering that the First Federal mortgage was superior to the lien created by the capital improvement use fees obligation.²⁷ The priority of the First Federal mortgage allegedly devalued the banks’ Series B bonds.²⁸ The Gill firm obtained summary judgment on all counts and the banks appealed to the Arkansas Supreme Court.²⁹

The Arkansas Supreme Court affirmed summary judgment for the Gill firm on the plaintiffs’ Arkansas Securities Act claims because the Gill firm was not a seller of the bonds, did not control their sale, and did not materially aid in their sale as required for liability under the Arkansas statute.³⁰ The court also affirmed summary judgment for the Gill firm on the plaintiffs’ legal malpractice claim based on a lack of privity because the Gill firm was retained by the district and had no attorney-client relationship with any of the plaintiffs.³¹

That left the plaintiffs’ fraud claim, because the Arkansas lawyer-immunity statute requiring privity for legal malpractice liability contained an exception for acts or omissions by lawyers constituting fraud or intentional misrepresentations.³² The court began its analysis by stating that to prove fraud, a plaintiff had to show that: (1) the defendant made a false representation of material fact; (2) the defendant knew the representation was false or that there was insuffi-

²¹ *Id.*

²² *Id.* at 50.

²³ *Id.*

²⁴ *Id.* at 51–54.

²⁵ *Id.* at 50.

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.* at 51–52.

³¹ *Id.* at 52–53.

³² *Id.* at 53 (quoting *McDonald v. Pettus*, 988 S.W.2d 9, 12 (Ark. 1999)).

cient evidence upon which to make the representation; (3) the defendant intended to induce action or inaction by the plaintiff in reliance upon the representation; (4) the plaintiff justifiably relied on the representation; and (5) the plaintiff was damaged as a result.³³

Here, the Gill firm admitted that it knew of the First Federal mortgage, but argued that given the structure of the transaction, the mortgage was not information that might have assisted prospective purchasers in evaluating the risks of buying the bonds and, therefore, was not a material fact that had to be disclosed in the POS or the OS.³⁴ Conversely, the plaintiffs asserted that: (1) the priority of the mortgage was material and, thus, the Gill firm had a duty to disclose it; (2) the Gill firm intentionally failed to disclose the First Federal mortgage and that had the mortgage been disclosed, the bond issue would not have closed; and (3) the Gill firm's failure to disclose the mortgage was done with the intent to defraud purchasers of the bonds so as to secure the fees the Gill firm expected to realize from the bond issue.³⁵ The plaintiffs' critical point was that genuine issues of material fact remained, and thus the trial court erred by awarding summary judgment to the Gill firm on the fraud claim.³⁶ The *First Arkansas* court agreed with the plaintiffs, reversed the trial court's grant of summary judgment on the fraud count, and remanded the case for further proceedings.³⁷

First Arkansas illuminates lawyers' vulnerability to misrepresentation claims and the difficulty they may encounter in defeating them short of trial. It therefore nicely launches our examination of lawyers' and law firms' potential civil liability for fraud and negligent misrepresentation. Looking ahead, Part I of this article provides an overview of the common law causes of action available to potential plaintiffs: (a) common law fraud, also described as actual fraud or intentional misrepresentation; (b) fraudulent concealment; (c) constructive fraud; and (d) negligent misrepresentation.³⁸ After discussing these causes of action, Part I examines the role that rules of professional conduct play in establishing a standard of care or conduct, or the reasonableness of a plaintiff's reli-

³³ *Id.* at 53–54.

³⁴ *Id.* at 54. According to the Gill firm, if the Arkansas municipal improvement district statute is followed, any mortgages are subordinate to liens arising from related bonds. Thus, the mortgage did not have to be disclosed because amounts due on the bonds from landowners would have created a lien superior to the mortgage. This argument failed because genuine issues of material fact remained in dispute. *Id.*

³⁵ *Id.*

³⁶ *Id.*

³⁷ *Id.* at 54–55.

³⁸ This article does not discuss lawyers' civil liability under attorney deceit statutes. *See, e.g.*, N.M. STAT. ANN. § 36-2-17 (West 2010) (“If an attorney is guilty of deceit or collusion or consents thereto with intent to deceive the court, judge or party, he shall forfeit to the injured party, treble damages to be recovered in a civil action”); N.Y. JUD. LAW § 487 (McKinney 2005) (subjecting a lawyer who “[i]s guilty of any deceit or collusion, or consents to any deceit or collusion, with intent to deceive the court or any party” to treble damages).

ance on a lawyer's alleged misrepresentations. Part II looks at four illustrative negligent misrepresentation and fraud cases against lawyers; two arising out of underlying litigation matters and two arising out of lawyers' transactional practices. Part III offers lawyers some brief practical advice on avoiding potential liability for fraud and negligent misrepresentation.

I. UNDERSTANDING FRAUD AND MISREPRESENTATION

Plaintiffs suing lawyers or law firms for alleged misrepresentations or omissions may pursue several theories of recovery, including: (a) common law fraud, also referred to as actual fraud or intentional misrepresentation; (b) fraudulent concealment, also described as fraud by silence or silent fraud; (c) constructive fraud; and (d) negligent misrepresentation. Depending on the case and cause of action, plaintiffs may attempt to use rules of professional conduct to define the standard of care or conduct against which a defendant's duty is measured, or establish key elements required for liability.

A. Common Law Fraud

As a California court once observed, "[a] fraud claim against a lawyer is no different from a fraud claim against anyone else."³⁹ The Restatement (Second) of Torts explains liability for common law fraud as follows:

One who fraudulently makes a misrepresentation of fact, opinion, intention or law for the purpose of inducing another to act or to refrain from action in reliance upon it, is subject to liability to the other in deceit for pecuniary loss caused to him by his justifiable reliance upon the misrepresentation.⁴⁰

A misrepresentation may be either oral or written.⁴¹

Under the Restatement approach, a listener's reliance on a misrepresentation is justifiable only if the matter misrepresented is material.⁴² Many courts that generally follow the Restatement, however, treat materiality as an element separate from reliance.⁴³ Either way, a matter is deemed to be material if (1) a reasonable person would attach importance to its existence or absence in determining how or whether to act in the subject transaction; or (2) the maker knows or has reason to know that the recipient regards or is likely to regard the matter as important in determining a course of action even though a reasonable person would not so consider it.⁴⁴

With respect to justifiable or reasonable reliance, the person to whom a fraudulent misrepresentation is made is generally entitled to rely on the misrepresentation even if she might have learned that it was false through investiga-

³⁹ *Vega v. Jones, Day, Reavis & Pogue*, 17 Cal. Rptr. 3d 26, 31 (Ct. App. 2004).

⁴⁰ RESTATEMENT (SECOND) OF TORTS § 525 (AM. LAW INST. 1977).

⁴¹ *Freedman v. Brutzkus*, 106 Cal. Rptr. 3d 371, 374 (Ct. App. 2010).

⁴² RESTATEMENT (SECOND) OF TORTS § 538(1) (AM. LAW INST. 1977).

⁴³ *See infra* notes 50–51, 54–56.

⁴⁴ RESTATEMENT (SECOND) OF TORTS § 538(2) (AM. LAW INST. 1977).

tion.⁴⁵ As a rule, a party has no duty to investigate the truthfulness of a representation and may justifiably or reasonably rely on a representation so long as the party does not know it to be false or it is not obviously false.⁴⁶

The base question, of course, is what makes a misrepresentation fraudulent? Section 526 explains that a misrepresentation is fraudulent if the maker:

- (a) knows or believes that the matter is not as he represents it to be, (b) does not have the confidence in the accuracy of his representation that he states or implies, or (c) knows that he does not have the basis for his representation that he states or implies.⁴⁷

Courts frequently describe this element of a defendant's conduct as scienter.⁴⁸ The maker's scienter is critical to a finding of fraud.⁴⁹ The existence of scienter is a question of fact.⁵⁰

Common law fraud has no all-encompassing or uniform definition or description.⁵¹ A cause of action for fraud certainly has essential elements as outlined in section 525, although some jurisdictions that have embraced the Restatement describe or list those elements in different ways. For example, Idaho courts hold that fraud has nine elements:

- (1) a statement or representation of fact; (2) its falsity; (3) its materiality; (4) the speaker's knowledge of its falsity; (5) the speaker's intent that there be reliance; (6) the hearer's ignorance of the falsity of the statement; (7) reliance by the hearer; (8) justifiable reliance; and (9) resultant injury.⁵²

⁴⁵ *Id.* § 541.

⁴⁶ *Donner v. Nicklaus*, 778 F.3d 857, 870 (10th Cir. 2015) (applying Utah law); *Yazdianpour v. Safeblood Techs., Inc.*, 779 F.3d 530, 536–37 (8th Cir. 2015) (applying Arkansas law and distinguishing affirmative misrepresentations from failures to disclose); *Hoyt Props., Inc. v. Prod. Res. Grp., L.L.C.*, 736 N.W.2d 313, 321 (Minn. 2007). *See also* *Jane Doe 43C v. Diocese of New Ulm*, 787 N.W.2d 680, 685 (Minn. Ct. App. 2010) (explaining that “a party is under no duty to investigate a fraud it has no reason to suspect”). *Cf.* *Specialty Marine & Indus. Supplies, Inc. v. Venus*, 66 So. 3d 306, 310 (Fla. Dist. Ct. App. 2011) (explaining that fraud does not include a justifiable reliance element because a hearer may rely on the truth of a representation even if the falsity of the representation could have been discovered through reasonable investigation).

⁴⁷ RESTATEMENT (SECOND) OF TORTS § 526 (AM. LAW INST. 1977).

⁴⁸ *See, e.g., Dier v. Peters*, 815 N.W.2d 1, 8 (Iowa 2012) (“The knowledge of falsity element of a fraud claim is also commonly known as the scienter element.”).

⁴⁹ *Butler v. Harris*, 13 N.E.3d 380, 387 (Ill. App. Ct. 2014); *Weston v. Northampton Personal Care, Inc.*, 62 A.3d 947, 960 (Pa. Super. Ct. 2013).

⁵⁰ *Meecorp Capital Mkts., LLC v. PSC of Two Harbors, LLC*, 776 F.3d 557, 565 (8th Cir. 2015) (applying Minnesota law).

⁵¹ *Mancuso v. Burton Farm Dev. Co. LLC*, 748 S.E.2d 738, 749 (N.C. Ct. App. 2013) (quoting *Forbis v. Neal*, 649 S.E.2d 382, 387 (N.C. 2007)); *Hodge v. Craig*, 382 S.W.3d 325, 342 (Tenn. 2012).

⁵² *April Beguesse, Inc. v. Rammell*, 328 P.3d 480, 489 (Idaho 2014) (quoting *Bank of Commerce v. Jefferson Enters., LLC*, 303 P.3d 183, 192 (Idaho 2013)).

Mississippi, Missouri, Utah, and Washington courts also list nine elements and describe them similarly.⁵³

Other jurisdictions reduce a cause of action for common law fraud to four, five, or six elements. Connecticut, for example, lists four elements: “(1) a false representation was made as a statement of fact; (2) the statement was untrue and known to be so by its maker; (3) the statement was made with the intent of inducing reliance thereon; and (4) the other party relied on the statement to his detriment.”⁵⁴ Florida similarly lists four elements.⁵⁵ Alaska, California, Delaware, Illinois, and New York courts, among others, identify five elements, which, while varying slightly in description, generally are: (1) misrepresentation of an existing material fact; (2) made with knowledge of its falsity; (3) the speaker’s intent that the listener rely on the statement; (4) justifiable reliance by the listener; and (5) resulting damages.⁵⁶ Indiana, Kentucky, Michigan, Nebraska, Pennsylvania, and Texas consider common law fraud to have six elements.⁵⁷ With slight variation, those states require proof that: (1) the defendant made a material representation; (2) the representation was false; (3) the representation was known to be false or was recklessly made; (4) the representation was intended to induce the plaintiff to act; (5) the plaintiff relied on the misrepresentation; and (6) the plaintiff was damaged as a result.⁵⁸

⁵³ See, e.g., *Kinney v. Catholic Diocese of Biloxi, Inc.*, 142 So. 3d 407, 418 (Miss. 2014) (quoting *Schmidt v. Catholic Diocese of Biloxi*, 18 So. 3d 814, 831 (Miss. 2009)); *Stander v. Szabados*, 407 S.W.3d 73, 81 (Mo. Ct. App. 2013); *Carlton v. Brown*, 323 P.3d 571, 581–82 (Utah 2014) (quoting *Giusti v. Sterling Wentworth Corp.*, 201 P.3d 966, 977 n.38 (Utah 2009)); *Alexander v. Sanford*, 325 P.3d 341, 366 (Wash. Ct. App. 2014) (quoting *Stiley v. Block*, 925 P.2d 194, 204 (Wash. Ct. App. 1996)).

⁵⁴ *Reville v. Reville*, 93 A.3d 1076, 1087 (Conn. 2014) (quoting *Weinstein v. Weinstein*, 882 A.2d 53, 63 (Conn. 2005)) (internal quotation marks omitted).

⁵⁵ *Jackson v. Shakespeare Found., Inc.*, 108 So. 3d 587, 595 n.2 (Fla. 2013).

⁵⁶ *Taylor v. Wells Fargo Home Mortg.*, 301 P.3d 182, 191 (Alaska 2013) (quoting *Asher v. Alkan Shelter, LLC*, 212 P.3d 772, 782 (Alaska 2009)); *State ex rel. Wilson v. Super. Ct.*, 174 Cal. Rptr. 3d 317, 333 n.21 (Ct. App. 2014) (describing the tort of “deceit”); *Vichi v. Koninklijke Philips Elecs., N.V.*, 85 A.3d 725, 773 (Del. Ch. 2014); *Bonhomme v. St. James*, 970 N.E.2d 1, 10 (Ill. 2012); *Neckles Builders, Inc. v. Turner*, 986 N.Y.S.2d 494, 497 (App. Div. 2014) (quoting *Introna v. Huntington Learning Ctrs., Inc.*, 911 N.Y.S.2d 442, 445 (App. Div. 2010)).

⁵⁷ *Kesling v. Hubler Nissan, Inc.*, 997 N.E.2d 327, 335 (Ind. 2013) (quoting *Lawyers Title Ins. Corp. v. Pokraka*, 595 N.E.2d 244, 249 (Ind. 1992)); *Elendt v. Green Tree Servicing, LLC*, 443 S.W.3d 612, 615 (Ky. Ct. App. 2014); *Lucas v. Awaad*, 830 N.W.2d 141, 152 (Mich. Ct. App. 2013); *Bott v. Holman*, 850 N.W.2d 800, 807 (Neb. Ct. App. 2014); *Weston v. Northampton Pers. Care, Inc.*, 62 A.3d 947, 960 (Pa. Super. Ct. 2013) (quoting *Heritage Surveyors & Eng’rs, Inc. v. Nat’l Penn Bank*, 801 A.2d 1248, 1250–51 (Pa. Super. Ct. 2002)); *Landers v. Aurora Loan Servs., LLC*, 434 S.W.3d 291, 293–94 (Tex. App. 2014) (quoting *Aquaplex, Inc. v. Rancho La Valencia, Inc.*, 297 S.W.3d 768, 774 (Tex. App. 2009)).

⁵⁸ *Kesling*, 997 N.E.2d at 335 (quoting *Lawyers Title*, 595 N.E.2d at 249); *Giddings & Lewis, Inc. v. Indus. Risk Insurers*, 348 S.W.3d 729, 747 (Ky. 2011); *Lucas*, 830 N.W.2d at 152; *Bott*, 850 N.W.2d at 807; *Weston*, 62 A.3d at 960 (quoting *Heritage Surveyors & Eng’rs, Inc.*, 801 A.2d at 1250–51); *Landers*, 434 S.W.3d at 293–94 (quoting *Aquaplex, Inc.*, 297 S.W.3d at 774).

Some aspects of common law fraud transcend jurisdictional boundaries but reduce to the principle that the cause of action is disfavored. First, outside the context of constructive fraud,⁵⁹ fraud is never presumed,⁶⁰ nor is it lightly inferred.⁶¹ To the contrary, courts presume a defendant's honesty and innocence.⁶² Second, plaintiffs generally must plead fraud with particularity.⁶³ A plaintiff's failure to specifically plead in her complaint or petition the acts or facts allegedly evidencing fraud generally justifies dismissal of the case.⁶⁴ Third, plaintiffs typically must prove fraud by clear and convincing evidence.⁶⁵ "Clear and convincing evidence is such a high standard that even the over-

⁵⁹ See *infra* Part II.C.

⁶⁰ *Byrd v. Lamar*, 846 So. 2d 334, 343 (Ala. 2002) (quoting *Wilson v. S. Med. Ass'n*, 547 So. 2d 510, 514 (Ala. 1989)); *Slaick v. Arnold*, 728 S.E.2d 782, 784 (Ga. Ct. App. 2012); *Fisher v. Grove Farm Co., Inc.*, 230 P.3d 382, 403 (Haw. Ct. App. 2009) (quoting *Shoppe v. Gucci Am., Inc.*, 14 P.3d 1049, 1067 (Haw. 2000)); *Chism v. Protective Life Ins. Co.*, 234 P.3d 780, 787 (Kan. 2010); *Harmony Glob. Sourcing, LLC v. Stigliano*, No. L-003621-05, 2009 WL 2461262, at *3 (N.J. Super. Ct. App. Div. Aug. 13, 2009); *Anderson v. Zimbelman*, 842 N.W.2d 852, 857 (N.D. 2014) (quoting *First Union Nat'l Bank v. RPB 2, LLC*, 674 N.W.2d 1, 8 (N.D. 2004)); *Bowman v. Presley*, 212 P.3d 1210, 1218 (Okla. 2009); *Law Capital, Inc. v. Kettering*, 836 N.W.2d 642, 647 (S.D. 2013); *Homestead Grp., LLC v. Bank of Tenn.*, 307 S.W.3d 746, 751 (Tenn. Ct. App. 2009); *Priddy v. Rawson*, 282 S.W.3d 588, 598 (Tex. App. 2009); *White v. Shane Edeburn Constr., LLC*, 285 P.3d 949, 957 (Wyo. 2012) (quoting *Osborn v. Emporium Videos*, 870 P.2d 382, 383 (Wyo. 1994)).

⁶¹ *Law Capital, Inc.*, 836 N.W.2d at 647.

⁶² *Bowens v. Allied Warehousing Servs., Inc.*, 729 S.E.2d 845, 851–52 (W. Va. 2012) (quoting *Hunt v. Hunt*, 114 S.E. 283, 285 (W. Va. 1922)); *White*, 285 P.3d at 957 (quoting *Osborn*, 870 P.2d at 383).

⁶³ See, e.g., FED. R. CIV. P. 9(b) ("In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake.").

⁶⁴ See, e.g., *Decker v. Nagel Rice LLC*, No. 09 Civ. 9878(SAS), 2010 WL 2346608, at *6 (S.D.N.Y. May 28, 2010) (dismissing client's fraud claim against lawyer for failure to plead facts allegedly constituting fraud with particularity).

⁶⁵ See, e.g., *In re Estate of Nethken*, 978 A.2d 603, 607 (D.C. 2009); *Frontier Dev. Grp., LLC v. Caravella*, 338 P.3d 1193, 1198 (Idaho 2014); *Hanson-Suminski v. Rohrman Midwest Motors, Inc.*, 898 N.E.2d 194, 202 (Ill. App. Ct. 2008); *Chism*, 234 P.3d at 787; *Barr v. Dyke*, 49 A.3d 1280, 1286 (Me. 2012); *Dep't of Human Servs. v. Ray*, 997 So. 2d 983, 991 (Miss. Ct. App. 2008) (quoting *Hamilton v. McGill*, 352 So. 2d 825, 831 (Miss. 1977)); *Stander v. Szabados*, 407 S.W.3d 73, 81 (Mo. Ct. App. 2013) (quoting *Kempton v. Dugan*, 224 S.W.3d 83, 87 (Mo. Ct. App. 2007)); *Bott v. Holman*, 850 N.W.2d 800, 807 (Neb. Ct. App. 2014); *Harmony Glob. Sourcing, LLC*, 2009 WL 2461262, at *3; *Anderson*, 842 N.W.2d at 857 (quoting *First Union Nat'l Bank*, 674 N.W.2d at 8); *Bowman*, 212 P.3d at 1218; *Rohm & Haas Co. v. Cont'l Cas. Co.*, 781 A.2d 1172, 1179 (Pa. 2001); *In re Estate of Alden v. Dee*, 35 A.3d 950, 961 (Vt. 2011); *Quicken Loans, Inc. v. Brown*, 737 S.E.2d 640, 653 (W. Va. 2012); *White*, 285 P.3d at 957 (quoting *Osborn*, 870 P.2d at 383). *But see* *Benton v. Clay*, 123 So. 3d 212, 219 (La. Ct. App. 2013) (stating that fraud need only be proved by a preponderance of the evidence); *Sejnoha v. City of Yankton*, 622 N.W.2d 735, 739 (S.D. 2001) (applying a preponderance of the evidence standard to fraud).

whelming weight of the evidence does not rise to the same level.”⁶⁶ Fourth, the failure of any one element of the cause of action will defeat a fraud claim.⁶⁷

When considering lawyers’ potential liability for fraud, perhaps the most surprising thing is the Restatement’s position that fraud may be predicated on a statement of opinion.⁶⁸ Indeed, even a cursory review of case law will reveal ample recent authority holding that a statement of opinion will not support a cause of action for fraud.⁶⁹ *Merrilees v. Merrilees*⁷⁰ illustrates this principle in the context of law practice.

Merrilees arose out of the divorce of Robert and Pamela Merrilees, which began in 2005. In 1999, Robert had formed Spot Trading LLC (“Spot”).⁷¹ Although the Merrilees were married in 1993, Robert argued in the dissolution proceedings that Spot was not marital property and further asserted that his distributions from Spot adequately compensated the marital estate.⁷² In 2009, the Merrilees negotiated a marital settlement agreement that (a) allocated to Pamela \$18 million and the couple’s \$1 million home, tax free; and (b) allocated Spot to Robert.⁷³ The agreement recited that the Merrilees had disputed Spot’s value, but stated that Pamela had been advised by her own expert on Spot’s value, stated that she was satisfied with that valuation, and provided that she disclaimed any interest in Spot.⁷⁴ The trial court approved the agreement and incorporated it into the judgment for dissolution of the marriage.⁷⁵

In 2010, Pamela sued Robert and his lawyers on various theories, including fraud, alleging that they had understated Spot’s value and falsely informed her that Spot was not marital property.⁷⁶ Her fraud claim rested on three documents that Robert’s lawyers gave her in the divorce case: an asset list, a memorandum

⁶⁶ *Moran v. Fairley*, 919 So. 2d 969, 975 (Miss. Ct. App. 2005).

⁶⁷ *Nash v. Studdard*, 670 S.E.2d 508, 513 (Ga. Ct. App. 2008) (quoting *Butler v. Terminix Int’l, Inc.*, 334 S.E.2d 865, 867 (Ga. Ct. App. 1985)); *Morgan Stanley Credit Corp. v. Fillingier*, 979 N.E.2d 362, 368 (Ohio Ct. App. 2012); *Allegro, Inc. v. Scully*, 762 S.E.2d 54, 68 (S.C. Ct. App. 2014) (quoting *Austin v. Stokes-Craven Holding Corp.*, 691 S.E.2d 135, 149 (S.C. 2010)); *Parsons v. Greenberg*, No. 02-10-00131-CV, 2012 WL 310505, at *10 (Tex. App. Feb. 2, 2012); *In re Estate of Alden*, 35 A.3d 950, 961 (Vt. 2011).

⁶⁸ RESTATEMENT (SECOND) OF TORTS § 525 (AM. LAW INST. 1977).

⁶⁹ *See, e.g.*, *RHA Constr., Inc. v. Scott Eng’g, Inc.*, C.A. N11C-03-013 JRJ CCLD, 2013 WL 3884937, at *4 (Del. Super. Ct. July 24, 2013); *Burds v. Hipes*, 763 S.E.2d 887, 889 (Ga. Ct. App. 2014); *Ill. Non-Profit Risk Mgmt. Ass’n v. Human Serv. Ctr. of S. Metro-East*, 884 N.E.2d 700, 710 (Ill. App. Ct. 2008); *Flegles, Inc. v. TruServ Corp.*, 289 S.W.3d 544, 549 (Ky. 2009) (quoting *McHargue v. Fayette Coal & Feed Co.*, 283 S.W.2d 170, 172 (Ky. 1955)); *Lasater v. Guttmann*, 5 A.3d 79, 103 (Md. Ct. Spec. App. 2010); *Heath v. Palmer*, 915 A.2d 1290, 1296 (Vt. 2006); *Sales v. Kecoughtan Housing Co., Ltd.*, 690 S.E.2d 91, 94 (Va. 2010).

⁷⁰ *Merrilees v. Merrilees*, 998 N.E.2d 147 (Ill. App. Ct. 2013).

⁷¹ *Id.* at 153.

⁷² *Id.*

⁷³ *Id.* at 153–54.

⁷⁴ *Id.* at 154.

⁷⁵ *Id.*

⁷⁶ *Id.*

explaining Robert's position, and a flow chart.⁷⁷ The trial court dismissed her case in its entirety and she fared just as badly on appeal.⁷⁸ The appellate court easily dispatched her fraud claim, first reasoning that the allegedly false documents "were expressions of opinion and were given to support Robert's positions during settlement negotiations in the divorce case."⁷⁹ Because she could "not identify any misstatements of material fact on which she reasonably relied," the *Merrilees* court affirmed the trial court's judgment in favor of Robert's lawyers.⁸⁰

The plaintiff's fraud claim also failed in *Cain v. Osman*.⁸¹ The lawyer in that case, Ronald Osman, declined to pursue a qui tam action against General American Life Insurance Co. on behalf of a podiatrist, John Cain, telling Cain that he "did not believe" Cain had "a viable action under the False Claims Act."⁸² Then, a few months later, Osman sued General American for similar misconduct on behalf of two other relators, Harry and Nancy Riggs, and the three of them were rewarded when the government intervened in the action and obtained a \$70 million settlement.⁸³ An outraged Cain sued Osman on various theories, including fraud, alleging that Osman had used information he provided to pursue the Riggs' case.⁸⁴ The district court dismissed the case and Cain appealed to the Seventh Circuit.⁸⁵

Cain contended that the district court had erred in dismissing his fraud claim by not recognizing that he had alleged a false statement of material fact: Osman's representation that he did not believe that Cain had a "viable action under the False Claims Act."⁸⁶ The Seventh Circuit rejected Cain's argument on the basis that in declining to represent him, Osman had offered "a legal opinion, not a representation of fact."⁸⁷ In the end, the Seventh Circuit affirmed the district court's judgment for Osman across the board.⁸⁸

Notwithstanding the results in *Merrilees* and *Cain*, the general rule that mere statements of opinion and statements of legal opinion will not support fraud allegations is subject to several qualifications or exceptions. First, the general rule may not apply because what is claimed to be a statement of opin-

⁷⁷ *Id.* at 158.

⁷⁸ *Id.* at 153.

⁷⁹ *Id.* at 158.

⁸⁰ *Id.* at 159.

⁸¹ *Cain v. Osman*, 286 F. App'x 934 (7th Cir. 2008).

⁸² *Id.* at 936 (internal quotation marks omitted).

⁸³ *Id.*

⁸⁴ *Id.*

⁸⁵ *Id.*

⁸⁶ *Id.*

⁸⁷ *Id.*

⁸⁸ *Id.* at 938.

ion may actually be a misrepresentation of fact.⁸⁹ “A fact is something ‘susceptible of knowledge.’”⁹⁰ For example, while “a representation of law is a statement of opinion as to what the law permits or prohibits” and will not support a fraud claim, “[a] statement concerning the law is a misrepresentation of fact if it involves ‘statements that imply the existence of accurate and readily ascertainable facts that either concern the law or have legal significance, but which are not part of the law themselves.’”⁹¹ Or, as a Minnesota court more succinctly stated, while “abstract statements of law or pure legal opinions are not actionable [as fraud], statements of law that imply knowledge of facts are actionable.”⁹²

Second, a lawyer who offers a knowingly false legal opinion may commit fraud.⁹³ Such cases are understandably rare because lawyers seldom have reason to furnish knowingly false legal opinions, although it is conceivable that a lawyer who is desperate to tell a client what it wants to hear to attract or retain business, or who is hoping to conceal some error or misconduct, might resort to such dishonesty.⁹⁴

Third, there is a “relationship exception” to the general rule, which applies where: (a) the parties are in a fiduciary relationship; (b) the maker of the allegedly false statement is a lawyer and the circumstances required her to divulge all the information she had to the plaintiff; or (c) the maker of the allegedly false statement is a lawyer and knows that the plaintiff was relying on her “as one learned in the law.”⁹⁵ As the Alabama Supreme Court explained in discussing the relationship exception, “a client who asks the opinion of his attorney on

⁸⁹ See RESTATEMENT (SECOND) OF TORTS § 525 cmt. d (AM. LAW INST. 1977) (explaining when statements of law constitute statements of opinion and when they constitute statements of fact).

⁹⁰ *Zimmerman v. Kent*, 575 N.E.2d 70, 75 (Mass. App. Ct. 1991) (quoting three Massachusetts cases).

⁹¹ *Brodeur v. Am. Home Assurance Co.*, 169 P.3d 139, 153 (Colo. 2007) (quoting *Equal Justice Found. v. Deutsche Bank Trust Co. Am.*, 412 F. Supp. 2d 790, 795–96 (S.D. Ohio 2005)).

⁹² *Hoyt Props., Inc. v. Prod. Res. Grp., L.L.C.*, 716 N.W.2d 366, 372–73 (Minn. Ct. App. 2006), *aff’d*, 736 N.W.2d 313 (Minn. 2007).

⁹³ See, e.g., *Green v. White*, 494 S.E.2d 681, 685 (Ga. Ct. App. 1997) (involving a lawyer who allegedly knew that he gave his client inaccurate advice and did not inform the client); *Brownell v. Garber*, 503 N.W.2d 81, 87 (Mich. Ct. App. 1993) (determining that the plaintiff stated a cause of action for fraud by alleging that his divorce lawyer knew that a property settlement would have adverse tax consequences at the time he recommended it while representing otherwise, or never analyzed the tax aspects of the property settlement notwithstanding his representations to the contrary); *Rice v. Heilbronner*, 708 N.Y.S.2d 684, 685 (App. Div. 2000) (concluding that the “[p]laintiffs’ allegations that [the lawyer] expressed an opinion that he did not believe to be true and made such statement with an intent to deceive [were] sufficient to state a cause of action for fraud”).

⁹⁴ See, e.g., *Encinias v. Whitener Law Firm, P.A.*, 310 P.3d 611, 620 (N.M. 2013) (recognizing fraud claim against lawyer who allegedly told client that statute of limitations had not run when it had).

⁹⁵ *Brodeur*, 169 P.3d at 154.

a point of law may assume that the attorney has special knowledge of the law and is entitled to a[n] honest opinion from him on which the client may justifiably rely.”⁹⁶

Finally, there is a “superior knowledge” or “special knowledge” exception to the general rule.⁹⁷ It applies where a party to a transaction with superior knowledge about the subject of the transaction or an aspect of it opines on an issue material to the transaction.⁹⁸ A lawyer’s allegedly false statements to an unrepresented non-lawyer are the paradigmatic case for application of this exception.⁹⁹

B. *Fraudulent Concealment*

In some instances, a dishonest defendant’s potential liability pivots not on a false statement of material fact, but on the alleged failure to disclose a key fact. Here, the cause of action is fraudulent concealment.¹⁰⁰ Fraudulent concealment is simply another form of common law fraud.¹⁰¹ It is sometimes referred to as “fraud by silence,”¹⁰² or “silent fraud.”¹⁰³ To establish fraudulent concealment, a plaintiff must prove that: (1) the defendant owed the plaintiff a duty to disclose a material fact; (2) the defendant failed to do so; (3) the defendant intended to defraud or deceive the plaintiff; (4) the plaintiff acted in justifiable reli-

⁹⁶ *Lawson v. Cagle*, 504 So. 2d 226, 227 (Ala. 1987); *see also Encinias*, 310 P.3d at 620 (“[I]t is reasonable for clients to assume that they can rely on their attorneys’ legal advice.”).

⁹⁷ *Brodeur*, 169 P.3d at 154; *GJP, Inc. v. Ghosh*, 251 S.W.3d 854, 889–90 (Tex. App. 2008).

⁹⁸ *Brodeur*, 169 P.3d at 154; *Merrilees v. Merrilees*, 998 N.E.2d 147, 160 (Ill. App. Ct. 2013). *See, e.g., Boyles Bros. Drilling Co. v. Orion Indus., Ltd.*, 761 P.2d 278, 282 (Colo. App. 1988) (“The alleged misrepresentation here was as to the legal effect of words used in the indorsement [sic] and assignment. It was made by an attorney to a layman and goes to the very essence of the agreement between the parties.”).

⁹⁹ *See, e.g., Boyles Bros.*, 761 P.2d at 282 (involving a lawyer’s statements to a layman; whether the layman was represented by counsel and thus could not claim reasonable reliance was a question of fact).

¹⁰⁰ *See PNC Multifamily Capital Inst. Fund XXVI Ltd. P’ship v. Bluff City Cmty. Dev. Corp.*, 387 S.W.3d 525, 550 (Tenn. Ct. App. 2012) (“A party commits fraudulent concealment for failing to disclose a known fact or condition where he or she had a duty to disclose and another party reasonably relies upon the resulting misrepresentation, thereby suffering injury.”).

¹⁰¹ *See Blickman Turkus, LP v. MF Downtown Sunnyvale, LLC*, 76 Cal. Rptr. 3d 325, 332 (Ct. App. 2008) (“Concealment is a species of fraud or deceit.”); *Graphic Comm. Loc. 1B Health & Welfare Fund “A” v. CVS Caremark Corp.*, 850 N.W.2d 682, 695 (Minn. 2014) (“Under the common law, a party may be liable for fraud either by making an affirmative statement that is false or by concealing or not disclosing facts under certain circumstances.”); *Hodges v. Rajpal*, 459 S.W.3d 237, 246 n.11 (Tex. App. 2015) (describing fraudulent concealment as a subcategory of common law fraud).

¹⁰² *See, e.g., Stechschulte v. Jennings*, 298 P.3d 1083, 1097 (Kan. 2013) (listing the elements of the tort).

¹⁰³ *See, e.g., Barclae v. Zarb*, 834 N.W.2d 100, 115–16 (Mich. Ct. App. 2013) (describing the tort this way).

ance on the concealment; and (5) the plaintiff was damaged as a result.¹⁰⁴ As with common law fraud, fraudulent concealment allegations are subject to heightened pleading requirements, and a plaintiff generally must establish fraudulent concealment through clear and convincing evidence.¹⁰⁵

The existence of a duty to disclose on the defendant's part is the threshold inquiry in a fraudulent concealment case.¹⁰⁶ A duty to disclose may be either legal or equitable,¹⁰⁷ and may arise "where the parties have a relation of trust and confidence or where there is inequality of condition and knowledge, or where there are other attendant circumstances."¹⁰⁸

Obviously, the defendant must know of the subject fact to have a duty to disclose it.¹⁰⁹ More particularly, the defendant must have *actual knowledge* of the fact; it is not enough that the defendant should have known of the fact or might have discovered it, or that knowledge of the fact might be imputed to the defendant.¹¹⁰

*Vega v. Jones, Day, Reavis, & Pogue*¹¹¹ is an interesting fraudulent concealment case against a law firm. *Vega* arose out of Transmedia Asia Pacific, Inc.'s merger with Monsterbook.com. Jones Day represented Transmedia, while Heller, Ehrman, White & McAuliffe represented Monsterbook.¹¹² Plaintiff Frank Vega owned common stock in Monsterbook.com and his shares were exchanged in the merger for shares of Transmedia restricted stock.¹¹³

In March 2000, Transmedia agreed to acquire Monsterbook in a stock deal that valued Monsterbook at \$15 million.¹¹⁴ Shortly after execution of the merger agreement, but before closing, Transmedia agreed to issue \$10 million in "toxic" convertible preferred stock to a third party.¹¹⁵ Although the toxicity of the preferred stock is not explained in the opinion, it had the effect of diluting the value of the shares of Transmedia stock held by all other Transmedia shareholders, including Vega.¹¹⁶

Following Transmedia's commitment to issue the convertible preferred stock, Jones Day prepared and sent to Heller Ehrman, for execution by the

¹⁰⁴ *Blondell v. Littlepage*, 991 A.2d 80, 94 (Md. 2010) (quoting *Lloyd v. Gen. Motors Corp.*, 916 A.2d 257, 274 (Md. 2007)).

¹⁰⁵ *Picher v. Roman Catholic Bishop of Portland*, 82 A.3d 101, 102 (Me. 2013).

¹⁰⁶ *Blondell*, 991 A.2d at 93.

¹⁰⁷ *Barr v. Dyke*, 49 A.3d 1280, 1287 (Me. 2012); *Lucas v. Awaad*, 830 N.W.2d 141, 152 (Mich. Ct. App. 2013).

¹⁰⁸ *Hobson v. Entergy Ark., Inc.*, 432 S.W.3d 117, 125 (Ark. Ct. App. 2014).

¹⁰⁹ *PNC Multifamily Capital Inst. Fund XXVI Ltd. P'ship v. Bluff City Cmty. Dev. Corp.*, 387 S.W.3d 525, 550 (Tenn. Ct. App. 2012).

¹¹⁰ *Jehly v. Brown*, 327 P.3d 351, 353–55 (Colo. Ct. App. 2014).

¹¹¹ 17 Cal. Rptr. 3d 26 (Ct. App. 2004).

¹¹² *Id.* at 29.

¹¹³ *Id.*

¹¹⁴ *Id.*

¹¹⁵ *Id.*

¹¹⁶ *Id.*

Monsterbook shareholders, a form seeking written consent to Transmedia's issuance of the preferred stock.¹¹⁷ The form reflected the initial conversion rate of the preferred stock, but it did not reflect the toxic anti-dilution provisions, instead referring to a certificate to be filed with the Delaware Secretary of State that would reflect the deal's complete terms.¹¹⁸ Meanwhile, in connection with the Delaware Secretary of State filing, Jones Day prepared a disclosure schedule that "clearly described and properly disclosed" the toxic aspect of the third-party investment, but did not share that schedule with Heller Ehrman, allegedly because doing so would have killed the merger.¹¹⁹ In sum, Jones Day prepared *two versions* of a disclosure schedule relating to the convertible preferred stock for inclusion with the merger agreement, but sent only the unrevealing one to Heller Ehrman.¹²⁰

Later that month, Transmedia filed the certificate with respect to the convertible preferred stock with the Secretary of State of Delaware and closed the preferred stock financing.¹²¹ Heller Ehrman apparently never requested a copy of the certificate from Jones Day or from the Delaware Secretary of State.¹²² In April 2000, Transmedia completed its acquisition of Monsterbook and Monsterbook's former common stockholders thus became common stockholders of Transmedia.¹²³ Vega, however, did not learn of the full terms of the convertible preferred stock transaction until December 2000.¹²⁴

Vega sued Jones Day in California state court for negligent misrepresentation and fraud.¹²⁵ With respect to the fraud claim, the key issue was Jones Day's allegedly active concealment or suppression of material facts.¹²⁶ The trial court dismissed Vega's case on Jones Day's demurrer and Vega appealed.¹²⁷

As the appellate court summarized Vega's fraudulent concealment theory, "Jones Day hid the existence of the 'toxic' stock provisions with the intent to induce Vega to give up his valuable stock in Monsterbook in exchange for Transmedia's . . . worthless stock."¹²⁸ Jones Day deliberately concealed the toxic stock provisions by failing to provide proper written disclosure, and by in-

¹¹⁷ *Id.*

¹¹⁸ *Id.* at 30, 35.

¹¹⁹ *Id.* at 29.

¹²⁰ *Id.* at 29–30.

¹²¹ *Id.* at 30.

¹²² *Id.* at 29–30, 33.

¹²³ *Id.* at 30.

¹²⁴ *Id.*

¹²⁵ *Id.* at 29.

¹²⁶ *See id.* at 32 (discussing the elements of fraud and the active concealment or suppression of material facts as the equivalent of a false statement).

¹²⁷ *Id.* at 31; *Demurrer*, BLACK'S LAW DICTIONARY (10th ed. 2014) (explaining that a demurrer is the equivalent of a motion to dismiss a case for failing to state a claim upon which relief may be granted).

¹²⁸ *Vega*, 17 Cal. Rptr. 3d at 31.

stead providing a sanitized version of the disclosure.¹²⁹ Vega purportedly lost his \$3.45 million interest in Monsterbook as a result.¹³⁰

After observing that “[a] fraud claim against a lawyer is no different from a fraud claim against anyone else,”¹³¹ and rejecting fraud liability against Jones Day based on an allegedly false statement about the unremarkable nature of the third-party transaction,¹³² the court turned to Jones Day’s fraud based on non-disclosure:

More problematic, however, is the question of active concealment or suppression of facts, which is the equivalent of a false representation. Vega alleges that Jones Day, after telling Heller Ehrman that Transmedia was about to close a \$ 10 million private stock transaction which it wanted to include in its disclosure schedules, prepared a proper disclosure schedule containing the pertinent terms, but provided a “different sanitized version” of the schedule, without the “toxic” stock provisions. Thus, Vega alleges that Jones Day “deliberately or with a reckless disregard of the truth concealed the ‘toxic’ stock provisions” from Vega, Monsterbook and Heller Ehrman. These allegations state an “active concealment or suppression of facts.”¹³³

Jones Day argued that liability for fraudulent concealment requires the defendant to have a duty to disclose the suppressed fact, and that as Transmedia’s counsel, it had no duty to disclose the terms of the third-party investment to Monsterbook, its shareholders, or Heller Ehrman.¹³⁴ Thus, its failure to share the complete disclosure schedule was “entirely irrelevant.”¹³⁵ The *Vega* court disagreed, reasoning that Jones Day specifically undertook to disclose the third-party transaction and, having done so, could not conceal a material term.¹³⁶ Even if no duty to disclose otherwise exists, “where one does speak he must speak the whole truth to the end that he does not conceal any facts which materially qualify those stated.”¹³⁷ Although Jones Day owed no professional duty of care to Vega as an adverse party in a merger, it did have a duty “not to defraud another, even if that other [was] [Heller Ehrman] negotiating at arm’s length.”¹³⁸ Ultimately, the court reversed the trial court’s dismissal of Vega’s complaint and remanded the case for further proceedings.¹³⁹

Business lawyers might well argue that the *Vega* court erred in ruling as it did. The disclosure schedules were Transmedia’s, not Jones Day’s. There could

¹²⁹ *Id.*

¹³⁰ *Id.* at 29.

¹³¹ *Id.* at 31.

¹³² *Id.* at 32.

¹³³ *Id.*

¹³⁴ *Id.* at 33.

¹³⁵ *Id.* (quoting Jones, Day, Reavis & Pogue’s brief).

¹³⁶ *Id.*

¹³⁷ *Id.* (quoting *Cicone v. URS Corp.*, 227 Cal. Rptr. 887, 891 (Ct. App. 1986)).

¹³⁸ *Id.* at 34 (quoting *Shafer v. Berger, Khan, Shafton, Moss, Figler, Simon & Gladstone*, 131 Cal. Rptr. 2d 777, 790 (Ct. App. 2003)).

¹³⁹ *Id.* at 39.

have been no active concealment of the preferred stock transaction when the transaction's terms were available from the Delaware Secretary of State and a Jones Day lawyer had apparently told a Heller Ehrman lawyer that Transmedia was "about to close a private stock financing" that was not listed in the Transmedia's disclosure schedules before the preferred stock deal closed.¹⁴⁰ If Heller Ehrman: (a) failed to follow up on the telephone alert to the third-party financing; (b) failed to obtain the certificate from the Delaware Secretary of State; or (c) did not request a copy of the certificate and any related documents from Transmedia before permitting the Transmedia-Monsterbook transaction to close, then it was Heller Ehrman that should have been in Vega's crosshairs—not Jones Day.

But even if all those arguments resonate with practicing lawyers, it is understandable that the *Vega* court would hold as it did. To start, the case came to it on an appeal from a demurrer. The court thus assumed all well-pleaded facts in Vega's complaint to be true and applied a *de novo* standard of review to determine whether the complaint stated a cause of action on any theory.¹⁴¹ In short, the standard of review strongly favored Vega. Although it is true that the disclosure schedules were Transmedia's and not Jones Day's,¹⁴² the record reflected that Jones Day prepared them and, having prepared two versions, shared only the supposedly innocent one with Heller Ehrman¹⁴³—arguably because sharing the schedule that included the preferred stock transaction would have aborted the Transmedia-Monsterbook deal. The fact that Jones Day did so as Transmedia's agent did not absolve Jones Day of its own potential liability for fraud.¹⁴⁴ As for Jones Day's argument that there could have been no fraudulent concealment given the availability of the certificate and thus knowledge of the preferred stock transaction through the Delaware Secretary of State, the court disagreed, explaining that "[t]he mere fact that information exists somewhere in the public domain is by no means conclusive" when debating fraudulent concealment.¹⁴⁵ Finally, but critically, whether Jones Day concealed the contours or terms of the preferred stock transaction to induce Vega to believe that the transaction was immaterial, and whether the consent form stating that a certificate revealing the third-party investment and its terms would be filed in Delaware, effectively furnished Vega with the information to which he was entitled were "questions of fact to be resolved on the evidence, not as a matter of law on a demurrer."¹⁴⁶

¹⁴⁰ *Id.* at 29 n.2.

¹⁴¹ *Maslo v. Ameriprise Auto & Home Ins.*, 173 Cal. Rptr. 3d 854, 859 (Ct. App. 2014) (quoting *Kyablue v. Watkins*, 149 Cal. Rptr. 3d 156, 158 (Ct. App. 2012)).

¹⁴² *Vega*, 17 Cal. Rptr. 3d at 29.

¹⁴³ *Id.* at 30.

¹⁴⁴ *Shafer v. Berger, Khan, Shafton, Moss, Figler, Simon & Gladstone*, 131 Cal. Rptr. 2d 777, 788–90 (Ct. App. 2003); RESTATEMENT (THIRD) OF AGENCY § 7.01 (AM. LAW INST. 2006).

¹⁴⁵ *Vega*, 17 Cal. Rptr. 3d at 35.

¹⁴⁶ *Id.* at 35–36.

C. Constructive Fraud

Unlike common law or actual fraud and fraud by concealment, which are similar wrongs, constructive fraud is distinguished by the parties' relationship. Constructive fraud requires a fiduciary or confidential relationship between the parties.¹⁴⁷ A "confidential relationship" for constructive fraud purposes is a relationship in which one party reposes special trust and confidence in the other, with the latter positioned to have and exercise influence over the first.¹⁴⁸ An attorney-client relationship unquestionably satisfies the fiduciary or confidential relationship requirement.¹⁴⁹ On the other side of the coin, the absence of a confidential or fiduciary relationship is fatal to a constructive fraud claim,¹⁵⁰ meaning that lawyers generally cannot be liable to third parties on this theory.¹⁵¹ Given lawyers' duty of loyalty to their clients, courts are understandably unwilling to extend lawyers' fiduciary duties to third parties.¹⁵²

Constructive fraud does not require actual dishonesty or intent to deceive by the alleged offender.¹⁵³ Even innocent misrepresentations, negligent misrepresentations, or failures to disclose material facts will support constructive fraud allegations.¹⁵⁴ With constructive fraud, intent is inferred from the existence of the fiduciary or confidential relationship and its breach.¹⁵⁵ In other words, the element of scienter that characterizes fraud and fraudulent concealment is replaced in constructive fraud theory by a confidential or fiduciary relationship.¹⁵⁶ The law describes the breach of a confidential or fiduciary relationship as fraud because of its tendency to deceive, to violate confidences, or to injure public interests.¹⁵⁷ Apart from the replacement of the element of scienter with a confidential or fiduciary relationship, the other requirements for common law fraud liability remain in place.¹⁵⁸

¹⁴⁷ *Prakashpalan v. Engstrom, Lipscomb & Lack*, 167 Cal. Rptr. 3d 832, 854 (Ct. App. 2014) (quoting *Michel v. Moore & Assocs., Inc.*, 67 Cal. Rptr. 3d 797, 802 (Ct. App. 2007)).

¹⁴⁸ *Estate of Draper v. Bank of Am., N.A.*, 205 P.3d 698, 707 (Kan. 2009).

¹⁴⁹ *Sanders v. Townsend*, 582 N.E.2d 355, 358 (Ind. 1991).

¹⁵⁰ *See, e.g., Petrello v. White*, 412 F. Supp. 2d 215, 229 (E.D.N.Y. 2006) (applying New York law).

¹⁵¹ *See, e.g., Rosenbaum v. White*, 692 F.3d 593, 601–04 (7th Cir. 2012) (holding that lawyers were not liable for constructive fraud to investors with whom they had no attorney-client relationship).

¹⁵² *Accident & Injury Med. Specialists, P.C. v. Mintz*, 279 P.3d 658, 663 (Colo. 2012).

¹⁵³ *Hobson v. Entergy Ark., Inc.*, 432 S.W.3d 117, 123 (Ark. Ct. App. 2014); *Hemphill v. Shore*, 289 P.3d 1173, 1182 (Kan. 2012); *Eggleston v. Kovacich*, 742 N.W.2d 471, 482 (Neb. 2007); *Croslin v. Enerlex, Inc.*, 308 P.3d 1041, 1045–46 (Okla. 2013).

¹⁵⁴ *Croslin*, 308 P.3d at 1046.

¹⁵⁵ *Country Cove Dev., Inc. v. May*, 150 P.3d 288, 294 (Idaho 2006).

¹⁵⁶ *Petrello v. White*, 412 F. Supp. 2d 215, 229 (E.D.N.Y. 2006) (applying New York law).

¹⁵⁷ *Canaj, Inc. v. Baker & Div. Phase III*, 893 A.2d 1067, 1095 (Md. 2006) (quoting *Md. Evtl. Trust v. Gaynor*, 803 A.2d 512, 516–17 (Md. 2002)); *Eggleston*, 742 N.W.2d at 482.

¹⁵⁸ *Petrello*, 412 F. Supp. 2d at 229 (discussing New York law).

Constructive fraud also differs from common law or actual fraud in the allocation of the burden of proof. In a constructive fraud case, once the plaintiff establishes the existence of a fiduciary relationship with the defendant, thus making the challenged transaction presumptively fraudulent, the burden shifts to the defendant to prove that he acted fairly and honestly in the affair.¹⁵⁹ Or, perhaps more precisely, the burden shifts to the defendant to defeat any one of the remaining elements of the plaintiff's constructive fraud claim and, in so doing, disprove the claim altogether.¹⁶⁰ The defendant generally must do so by clear and convincing evidence.¹⁶¹

If a plaintiff pleads both breach of fiduciary duty and constructive fraud claims, there is a reasonable likelihood that a court will determine the causes of action to be duplicative and dismiss one as superfluous, or submit only one of them to the jury.¹⁶² That is not always the case, however, and it certainly is not assured in jurisdictions where constructive fraud is distinguished from breach of fiduciary duty by an additional requirement: that a defendant charged with constructive fraud sought to gain some advantage or benefit through her position of trust.¹⁶³ Fortunately for lawyers, the receipt of fees should not be treated as a benefit that will support liability for constructive fraud.¹⁶⁴ This is because a lawyer's fee generally can be divorced from conduct allegedly constituting constructive fraud.¹⁶⁵ In other words, a lawyer gains no advantage or benefit through a fee paid to her in connection with a matter tainted by constructive fraud because the lawyer would have earned a fee if she had acted properly in the representation.¹⁶⁶ By way of qualification, this reasoning seems to depend

¹⁵⁹ *Culhane v. Culhane*, 969 F. Supp. 2d 210, 225 (D. Conn. 2013) (applying Connecticut law); *King v. Bryant*, 737 S.E.2d 802, 809 (N.C. Ct. App. 2013) (quoting *Collier v. Bryant*, 719 S.E.2d 70, 81 (N.C. Ct. App. 2011)); *Lee v. Hasson*, 286 S.W.3d. 1, 21 (Tex. Ct. App. 2007); *Grubb v. Grubb*, 630 S.E.2d 746, 751 (Va. 2006).

¹⁶⁰ *Demming v. Underwood*, 943 N.E.2d 878, 892 (Ind. Ct. App. 2011).

¹⁶¹ *Utzler v. Braca*, 972 A.2d 743, 755 (Conn. App. Ct. 2009) (quoting *Dunham v. Dunham*, 528 A.2d 1123, 1134 (Conn. 1987), *overruled in part on other grounds by Santopietro v. New Haven*, 682 A.2d 106, 109 n.8 (Conn. 1996)); *Hassan v. Yusuf*, 944 N.E.2d 895, 914 (Ill. App. Ct. 2011); *Demming*, 943 N.E.2d at 892; *In re Jane Tiffany Living Trust 2001*, 177 P.3d 1060, 1063 (Nev. 2008); *Grubb*, 630 S.E.2d at 751.

¹⁶² *See In re Wayport, Inc. Litig.*, 76 A.3d 296, 327 (Del. Ch. 2013) (“On the facts of this case, the breach of fiduciary duty count confronts directly the implications of the fiduciary relationship, rendering the constructive fraud count redundant and superfluous.”).

¹⁶³ *See, e.g., Sheaff Brock Inv. Advisors, LLC v. Morton*, 7 N.E.3d 278, 288 (Ind. Ct. App. 2014) (listing as an element of constructive fraud “the gaining of an advantage by the party to be charged at the expense of the complaining party”); *Dewey v. Stringer*, 325 P.3d 1236, 1239–40 (Mont. 2014) (quoting Montana’s constructive fraud statute); *Crumley & Assocs., P.C. v. Charles Peed & Assocs., P.A.*, 730 S.E.2d 763, 767 (N.C. Ct. App. 2012) (“To establish constructive fraud, a plaintiff must show that defendant (1) owes plaintiff a fiduciary duty; (2) breached this fiduciary duty; and (3) sought to benefit himself in the transaction.”).

¹⁶⁴ *NationsBank of N.C., N.A. v. Parker*, 535 S.E.2d 597, 602 (N.C. Ct. App. 2000) (citing *Barger v. McCoy Hillard & Parks*, 488 S.E.2d 215, 224 (N.C. 1997)).

¹⁶⁵ *See id.*

¹⁶⁶ *Id.*

on the lawyer's fee not being inflated by the conduct allegedly constituting constructive fraud.¹⁶⁷

D. Negligent Misrepresentation

In addition to potential liability for some form of fraud, lawyers may be accused of negligent misrepresentation.¹⁶⁸ Most jurisdictions have adopted the definition of negligent misrepresentation set forth in section 552(1) of the Restatement (Second) of Torts:

One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.¹⁶⁹

Liability for negligent misrepresentation is principally distinguished from liability for fraud by the defendant's mental state.¹⁷⁰ Negligent misrepresentation requires no intent to deceive by the defendant.¹⁷¹ The defendant need not know that the statement in dispute is false;¹⁷² rather, a defendant need only be careless or negligent in ascertaining the truth of the statement.¹⁷³ Thus, a defendant may be liable for negligent misrepresentation where she acted with no ill intent but failed to exercise the degree or level of care required under the circumstances.¹⁷⁴

Negligent misrepresentation, like other forms of negligence, naturally counts among its elements a duty owed by the defendant to the plaintiff.¹⁷⁵ This

¹⁶⁷ See *id.* ("Allegations . . . are that defendant 'took advantage of his position of trust and benefit[t]ed . . . in that he was paid for his services in closing the subject loan transaction.' There was no evidence that the amount paid defendant for notarizing and witnessing the loan documents *would have been any different* if the documents had not been forged.") (emphasis added).

¹⁶⁸ See, e.g., *Greycas, Inc. v. Proud*, 826 F.2d 1560, 1564–68 (7th Cir. 1987) (affirming a judgment against a lawyer); *Wafra Leasing Corp. v. Prime Capital Corp.*, 192 F. Supp. 2d 852, 873–74 (N.D. Ill. 2002) (concluding that the plaintiff had stated a negligent misrepresentation claim against a lawyer based on statements in an opinion letter).

¹⁶⁹ RESTATEMENT (SECOND) OF TORTS § 552(1) (AM. LAW INST. 1977).

¹⁷⁰ *Jane Doe-3 v. McLean Cty. Unit Dist. No. 5 Bd. of Dirs.*, 973 N.E.2d 880, 889 (Ill. 2012); *Zawaideh v. Neb. Dep't of Health & Human Servs. Regulation & Licensure*, 825 N.W.2d 204, 212 (Neb. 2013).

¹⁷¹ *Moncada v. W. Coast Quartz Corp.*, 164 Cal. Rptr. 3d 601, 611 (Ct. App. 2013) (quoting *Intrieri v. Super. Ct.*, 12 Cal. Rptr. 3d 97, 108 (Ct. App. 2004)); *Sundberg v. TTR Realty, LLC*, 109 A.3d 1123, 1131 (D.C. Cir. 2015).

¹⁷² *Sundberg*, 109 A.3d at 1131; *Simmons v. Campion*, 991 N.E.2d 924, 932 (Ill. App. Ct. 2013).

¹⁷³ *Jane Doe-3*, 973 N.E.2d at 889.

¹⁷⁴ *Nelson v. Wardyn*, 820 N.W.2d 82, 87 (Neb. Ct. App. 2012).

¹⁷⁵ *Sw. Non-Profit Hous. Corp. v. Nowak*, 322 P.3d 204, 208 (Ariz. Ct. App. 2014); *Bock v. Hansen*, 170 Cal. Rptr. 3d 293, 302 (Ct. App. 2014); *Simmons, Morris & Carroll, LLC v. Capital One, N.A.*, 144 So. 3d 1207, 1215 (La. Ct. App. 2014); *Williams v. Smith*, 820

duty is not boundless.¹⁷⁶ It is not a duty to take every possible precaution against misstatements, nor is it a duty to be right about the content or subject of the representation; rather, it is the familiar duty to exercise reasonable care in the circumstances.¹⁷⁷

Liability for negligent misrepresentation is more limited than liability for fraud.¹⁷⁸ Section 552(2) of the Restatement (Second) of Torts specifies those limits in general terms, stating that a defendant's liability for negligent misrepresentation is restricted to losses suffered:

- (a) by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it; and
- (b) through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.¹⁷⁹

With respect to negligent misrepresentation claims against lawyers, plaintiffs usually are third parties.¹⁸⁰ Clients seldom sue their lawyers for negligent misrepresentation for the simple reason that they do not need the cause of action to vindicate their rights; ordinary professional negligence claims against lawyers may be based on either conduct or alleged misrepresentations.¹⁸¹ But while it is clear that third parties may sue lawyers for negligent misrepresentation, courts carefully define the classes of third parties to whom lawyers may owe duties and, in so doing, limit the reach or scope of lawyers' duties.¹⁸² This attempt at precision is grounded in the recognition that whether a lawyer may be held to owe a duty to a third party "depends on balancing the attorney's duty to represent clients vigorously . . . with the duty not to provide misleading information on which third parties foreseeably will rely."¹⁸³ As a result, a lawyer may owe a duty to a third party for negligent misrepresentation purposes when: (1) the lawyer knows or reasonably should know that a third party will rely on

N.W.2d 807, 815 (Minn. 2012); *UBS Fin. Servs., Inc. v. Thompson*, 94 A.3d 176, 191 (Md. Ct. Spec. App. 2014) (quoting *Lloyd v. Gen. Motors Corp.*, 916 A.2d 257, 273 (Md. 2007)).

¹⁷⁶ See *Halcrow, Inc. v. Eighth Judicial Dist. Court*, 302 P.3d 1148, 1153 (Nev. 2013) (explaining limits on liability for negligent misrepresentation).

¹⁷⁷ *Carolina Chloride, Inc. v. Richland Cty.*, 714 S.E.2d 869, 873–74 (S.C. 2011) (quoting *AMA Mgmt. Corp. v. Strasburger*, 420 S.E.2d 868, 874 (S.C. Ct. App. 1992)).

¹⁷⁸ *Hodge v. Craig*, 382 S.W.3d 325, 344 (Tenn. 2012).

¹⁷⁹ RESTATEMENT (SECOND) OF TORTS § 552(2) (AM. LAW INST. 1977).

¹⁸⁰ See 1 MALLEN & RHODES, *supra* note 8, § 7:34. See, e.g., *Finova Capital Corp. v. Berger*, 794 N.Y.S.2d 379, 381 (App. Div. 2005) (exonerating the lawyer because the plaintiff did not rely on the alleged negligent misrepresentation in an opinion letter).

¹⁸¹ 1 MALLEN & RHODES, *supra* note 8, § 7:34.

¹⁸² See, e.g., *Prudential Ins. Co. of Am. v. Dewey Ballantine, Bushby, Palmer & Wood*, 605 N.E.2d 318, 320 (N.Y. 1992) (limiting lawyers' potential liability for negligent misrepresentation to cases where "there [is] either actual privity of contract . . . or a relationship so close as to approach that of privity . . . in order to provide fair and manageable bounds to what otherwise could prove to be limitless liability").

¹⁸³ *Petrillo v. Bachenberg*, 655 A.2d 1354, 1357 (N.J. 1995).

her representation and the third party is not too remote from the lawyer to deserve protection;¹⁸⁴ (2) the lawyer or her client (with the lawyer's acquiescence) "invites" a third party to rely on the lawyer's opinion or delivery of other legal services and the third party is not "too remote from the lawyer to be entitled to protection;¹⁸⁵ or (3) the lawyer and the third party enjoy a relationship of "near-privacy."¹⁸⁶ In fact, all of these descriptions of lawyers' duties to third parties comport with the section 552(2) restrictions.¹⁸⁷

Although fraud and negligent misrepresentation are different causes of action, and fraud is plainly distinguished from negligent misrepresentation by the element of scienter, misrepresentation is a core concept of each claim. This raises the parallel questions of (1) whether plaintiffs suing for negligent misrepresentation should have to meet the stringent pleading requirement for fraud; and (2) whether plaintiffs should have to prove negligent misrepresentation by clear and convincing evidence, the common standard for fraud cases.

The easy answer to both questions is no. As to the first, rules of civil procedure that mandate particularized pleading for fraud do not similarly specify negligent misrepresentation;¹⁸⁸ negligence claims do not have to be pleaded with particularity;¹⁸⁹ and, from a defendant's perspective, negligent misrepresentation allegations do not pose the potential reputational harm that fraud allegations do.¹⁹⁰ Regarding the second question, proof of negligence is evaluated under a preponderance of the evidence standard and negligent misrepresentation is simply a form of that tort.¹⁹¹ Not all courts accept these answers, however.

Federal courts are split on whether plaintiffs must plead negligent misrepresentation with the particularity required for fraud under Federal Rule of Civil Procedure 9(b), or whether negligent misrepresentation allegations are gov-

¹⁸⁴ *Id.* at 1359–60.

¹⁸⁵ RESTATEMENT (THIRD) OF LAW GOVERNING LAWYERS § 51(2) (AM. LAW INST. 2000).

¹⁸⁶ *Thomas H. Lee Equity Fund V, L.P. v. Mayer Brown, Rowe & Maw LLP*, 612 F. Supp. 2d 267, 285 (S.D.N.Y. 2009) (applying New York law); *see also Hedges v. Durrance*, 834 A.2d 1, 5 (Vt. 2003) (reciting an identical standard).

¹⁸⁷ *See Petrillo*, 655 A.2d at 1359–60 (referring to a draft of the RESTATEMENT (THIRD) OF LAW GOVERNING LAWYERS and to RESTATEMENT (SECOND) OF TORTS § 552); *McCamish, Martin, Brown & Loeffler v. F.E. Appling Interests*, 991 S.W.2d 787, 793–95 (Tex. 1999) (reasoning to the same effect).

¹⁸⁸ *See, e.g., FED. R. CIV. P. 9(b)* ("In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake.").

¹⁸⁹ *Tricontinental Indus., Ltd. v. PricewaterhouseCoopers, LLP.*, 475 F.3d 824, 837 (7th Cir. 2007).

¹⁹⁰ *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1104 (9th Cir. 2003).

¹⁹¹ *Commercial Molasses Corp. v. N.Y. Tank Barge Corp.*, 314 U.S. 104, 113 (1941) (negligence must be proven by a preponderance standard); *Halcrow, Inc. v. Eighth Judicial Dist. Court*, 302 P.3d 1148, 1154 (Nev. 2013) (evidence needed to prove negligent misrepresentation is "almost identical" to that needed to prove negligence).

erned by the less rigorous notice pleading requirement of Rule 8,¹⁹² as understood in light of the Supreme Court's decisions in *Bell Atlantic Corp. v. Twombly*¹⁹³ and *Ashcroft v. Iqbal*.¹⁹⁴ The First and Second Circuits hold that negligent misrepresentation claims are subject to Rule 9(b)'s heightened pleading standard.¹⁹⁵ The First Circuit requires a plaintiff to plead negligent misrepresentation with particularity under Rule 9(b) because the cause of action at its core "effectively charge[s] fraud."¹⁹⁶ In comparison, the Second Circuit grounds its approach in the recognition that plaintiffs suing for negligent misrepresentation often plead fraud in the alternative, and vice versa, and it makes little practical sense to impose inconsistent standards of proof.¹⁹⁷ While the Second Circuit's approach has practical appeal, the First Circuit's approach makes no sense at all. A negligent misrepresentation claim *does not effectively charge fraud* for the simple reason that liability for negligent misrepresentation does not require a defendant to have acted with scienter.¹⁹⁸

In contrast to the First and Second Circuits, the Fifth and Seventh Circuits adhere to the more forgiving Rule 8 notice pleading requirement for negligent misrepresentation.¹⁹⁹ The Fifth Circuit relies on a literal reading of Rule 9(b),²⁰⁰ which refers only to fraud or mistake, and the Seventh Circuit appears to do likewise.²⁰¹ The Fifth Circuit may, however, require parties to plead negligent misrepresentation with particularity when they do not "urge[] a separate focus on the negligent misrepresentation claims," as where fraud and negligent misrepresentation causes of action "are based on the same set of alleged facts."²⁰²

¹⁹² See FED. R. CIV. P. 8(a)(2) (requiring "a short and plain statement of the claim showing that the pleader is entitled to relief").

¹⁹³ *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007) (requiring plaintiffs to plead "enough facts to state a claim to relief that is plausible on its face").

¹⁹⁴ *Ashcroft v. Iqbal*, 556 U.S. 662, 679 (2009) ("[A] court considering a motion to dismiss can choose to begin by identifying pleadings that, because they are no more than conclusions, are not entitled to the assumption of truth. While legal conclusions can provide the framework of a complaint, they must be supported by factual allegations. When there are well-pleaded factual allegations, a court should assume their veracity and then determine whether they plausibly give rise to an entitlement to relief.").

¹⁹⁵ *N. Am. Catholic Educ. Programming Found., Inc. v. Cardinale*, 567 F.3d 8, 15 (1st Cir. 2009); *Aetna Cas. & Sur. Co. v. Aniero Concrete Co.*, 404 F.3d 566, 583 n.14 (2d Cir. 2005).

¹⁹⁶ *Cardinale*, 567 F.3d at 15.

¹⁹⁷ *Aniero*, 404 F.3d at 583 n.14.

¹⁹⁸ See *Renaissance Leasing, LLC v. Vermeer Mfg. Co.*, 322 S.W.3d 112, 134 (Mo. 2010) ("A claim for negligent misrepresentation, unlike one for fraud, does not involve a question of intent. Rather, such a claim is premised on the theory that the speaker believed the information supplied was correct but was negligent in so believing.").

¹⁹⁹ *Tricontinental Indus., Ltd. v. PricewaterhouseCoopers, LLP.*, 475 F.3d 824, 839 n.10 (7th Cir. 2007); *Gen. Elec. Capital Corp. v. Posey*, 415 F.3d 391, 396–97 (5th Cir. 2005).

²⁰⁰ *Posey*, 415 F.3d at 396–97.

²⁰¹ *Tricontinental*, 475 F.3d at 839 n.10.

²⁰² *Benchmark Elecs., Inc. v. J.M. Huber Corp.*, 343 F.3d 719, 723 (5th Cir. 2003).

The Fourth, Sixth, Eighth, and Ninth Circuits hold that the correct pleading standard depends on applicable state law.²⁰³ In short, if “negligent misrepresentation is a subspecies of fraud” under applicable state law or the state law requires an essential showing of fraud as an element of negligent misrepresentation,²⁰⁴ these courts will apply the Rule 9(b) heightened pleading standard.²⁰⁵ At least one district court in the Tenth Circuit has taken the same approach.²⁰⁶ By extension, lawyers must also recognize that the pleading standard for negligent misrepresentation versus fraud varies between states.²⁰⁷

With respect to the burden of proof, courts are again split. Some courts hold that a plaintiff must prove negligent misrepresentation by a preponderance of the evidence,²⁰⁸ while other courts require clear and convincing evidence,²⁰⁹ which is the standard generally applied to fraud claims. The former approach makes more sense because, again, negligent misrepresentation is a form of negligence and generally does not carry the risk of stigma or reputational harm that accompanies liability for fraud. On the other hand, most lawyers value their professional reputations and count on their good standing to advance their prac-

²⁰³ *Farm Credit Servs. of Am., FLCA v. Haun*, 734 F.3d 800, 805 (8th Cir. 2013); *Republic Bank & Trust Co. v. Bear Stearns & Co.*, 683 F.3d 239, 247–48 (6th Cir. 2012); *Baltimore Cnty. v. Cigna Healthcare*, 238 F. App’x 914, 921 (4th Cir. 2007); *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1103 (9th Cir. 2003).

²⁰⁴ *See Farm Credit Servs. of Am.*, 734 F.3d at 805 (applying Nebraska law, which treats negligent misrepresentation as a “subspecies of fraud”); *Baltimore Cnty.*, 238 F. App’x at 921 (holding that Rule 9(b) did not apply because Maryland law did not require an essential showing of fraud to impose liability for negligent misrepresentation).

²⁰⁵ *See, e.g., Republic Bank & Trust Co.*, 683 F.3d at 247–48 (applying Kentucky law).

²⁰⁶ *City of Raton v. Ark. River Power Auth.*, 600 F. Supp. 2d 1130, 1143–44 (D.N.M. 2008) (discussing Colorado and New Mexico law).

²⁰⁷ *Compare Thomas v. Schneider*, No. 2009-CA-002132-MR, 2010 WL 3447662, at *1 n.2 (Ky. Ct. App. Sept. 3, 2010) (“Like fraud, allegations of negligent misrepresentation must be pled with particularity.”), *and Hardin Cnty. Sav. Bank v. Hous. & Redevelopment Auth. of City of Brainerd*, 821 N.W.2d 184, 191 (Minn. 2012) (explaining that because “negligent misrepresentation constitutes fraud,” a plaintiff must plead negligent misrepresentation with particularity), *with Hayes v. Iworx, Inc.*, No. CV-06-168, 2006 WL 2959702, at *4 (Me. Super. Ct. July 31, 2006) (“A claim for negligent misrepresentation . . . does not sound in fraud or mistake, but in negligence, and [Rule] 9(b)’s pleading requirements are inapplicable to claims sounding in negligence.”), *and Davis, Malm, D’Agostine, P.C. v. Vale*, No. 041495, 2005 WL 1155171, at *3 (Mass. Super. Ct. Mar. 31, 2005) (“A claim of fraudulent misrepresentation must be pleaded with particularity. . . . Negligent misrepresentation, on the other hand, need only be averred generally.”), *and Delaney v. Bates*, No. BDV-92-1120, 1993 Mont. Dist. LEXIS 698, at *9 (Mont. Dist. Ct. Jan. 27, 1993) (“Unlike pleading fraud, there is no requirement that negligent misrepresentation be plead with any degree of particularity.”), *and Hunter v. Guardian Life Ins. Co. of Am.*, 593 S.E.2d 595, 600 (N.C. Ct. App. 2004) (declining to impose a particularity requirement on plaintiff’s negligent misrepresentation claim as it did on fraud claim).

²⁰⁸ *See, e.g., Holland v. Peoples Bank & Tr. Co.*, 3 So. 3d 94, 101 (Miss. 2008); *In re Convisser*, 242 P.3d 299, 307 (N.M. 2010); *McLaughlin v. Williams*, 665 S.E.2d 667, 670 (S.C. Ct. App. 2008); *Excel Constr., Inc. v. HKM Eng’g, Inc.*, 228 P.3d 40, 49 (Wyo. 2010).

²⁰⁹ *See, e.g., Aesthetics in Jewelry, Inc. v. Brown*, 339 S.W.3d 489, 495 (Ky. Ct. App. 2011); *Dewar v. Smith*, 342 P.3d 328, 336 (Wash. Ct. App. 2015).

tices in a variety of ways, and therefore consider any finding of liability to be injurious. It is thus fair for lawyers to argue that, in their cases, plaintiffs should be required to prove negligent misrepresentation by clear and convincing evidence. The strong counter-argument, of course, is that negligent misrepresentation calls into question a lawyer's carefulness in a single matter rather than her honesty, and it is only the latter that can reasonably be considered to have reputational value supporting a higher burden of proof. Were it otherwise, professional negligence claims against lawyers would always call for proof by clear and convincing evidence.

E. The Role of Rules of Professional Conduct

In considering the issue of duty in negligent misrepresentation cases and justifiable or reasonable reliance in both fraud and negligent misrepresentation claims, it is logical to question the role that rules of professional conduct do or should play in making these determinations. Several ethics rules appear to have obvious application depending on the facts of the case. For example, Model Rule of Professional Conduct 1.2(d) provides that a lawyer "shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent."²¹⁰ Model Rule 4.1(a) states that in representing a client, a lawyer "shall not knowingly . . . make a false statement of material fact or law to a third person."²¹¹ Model Rule 4.1(b) provides that in representing a client, a lawyer cannot "knowingly . . . fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client," unless the lawyer's duty of confidentiality under Model Rule 1.6 prohibits disclosure.²¹² Finally, Model Rule 8.4(c) broadly prohibits lawyers from engaging "in conduct involving dishonesty, fraud, deceit or misrepresentation."²¹³

To be sure, a lawyer's violation of an ethics rule is not independently actionable.²¹⁴ Thus, and by way of example, a person to whom a lawyer allegedly made a false statement of material fact could not sue the lawyer for negligent misrepresentation on the basis that the lawyer violated Rule 8.4(c), which, to repeat, prohibits lawyers from engaging in conduct involving "misrepresenta-

²¹⁰ MODEL RULES OF PROF'L CONDUCT r. 1.2(d) (AM. BAR ASS'N 2015).

²¹¹ *Id.* r. 4.1(a).

²¹² *Id.* r. 4.1(b).

²¹³ *Id.* r. 8.4(c).

²¹⁴ *Accident & Injury Med. Specialists, P.C. v. Mintz*, 279 P.3d 658, 664 (Colo. 2012); *In re Disciplinary Action Against Montez*, 812 N.W.2d 58, 66–67 (Minn. 2012); *Lucas v. Stevenson*, 294 P.3d 377, 382 (Mont. 2013); *Green v. Morgan Props.*, 73 A.3d 478, 494 (N.J. 2013); *Spencer v. Barber*, 299 P.3d 388, 395–96 (N.M. 2013); *Unarco Material Handling, Inc. v. Liberato*, 317 S.W.3d 227, 239 (Tenn. Ct. App. 2010); *Joyner v. DeFriend*, 255 S.W.3d 281, 283 (Tex. App. 2008); *Behnke v. Ahrens*, 294 P.3d 729, 738 (Wash. Ct. App. 2012); Douglas R. Richmond, *Why Legal Ethics Rules Are Relevant to Lawyer Liability*, 38 ST. MARY'S L.J. 929, 937 (2007).

tion.”²¹⁵ But what of the more confined question of duty? Model Rules 4.1(a) and 8.4(c) certainly impose a duty of honesty on lawyers in a professional responsibility sense. Could a plaintiff claiming negligent misrepresentation successfully extend that duty to tort law and allege that a lawyer owed her a duty of reasonable care under the circumstances by virtue of Model Rules 4.1(a) and 8.4(c)?

While there are sound arguments in some cases for basing a lawyer’s alleged duty on related rules of professional conduct, courts have held that the answer to that question is no; any alleged duty has to be grounded in the common law.²¹⁶ In our hypothetical case, that would likely be case law in the jurisdiction adopting section 552 of the Restatement (Second) of Torts.²¹⁷ Indeed, if the jurisdiction had adopted section 552, the plaintiff would not need Model Rules 4.1(a) or 8.4(c) or state analogs to support an alleged duty.²¹⁸

This does not mean, however, that rules of professional conduct are irrelevant to our hypothetical plaintiff or to the duty owed by the defending lawyer. Although the rules may not be employed to establish the lawyer’s duty, they may be relevant to the standard of care or conduct against which the lawyer’s duty is measured.²¹⁹ For example, the plaintiff might rely on Rule 4.1(a) or Rule 8.4(c) to argue that the lawyer did not exercise reasonable care in obtaining or communicating the information at issue—that the lawyer’s ethical obligations required her to do more to ascertain that the information was accurate, or that because of the rules the lawyer was obligated to do more along those lines than someone else would have been.

Rules of professional conduct play a greater role in negligent misrepresentation and fraud cases in which the defending lawyer contends that the plaintiff did not justifiably or reasonably rely on her alleged misstatements. Here, ethics rules imposing on lawyers an obligation of honesty to third parties may be quite relevant to the reasonableness of a plaintiff’s reliance on a lawyer’s representations.²²⁰ An essential fact, however, will be the plaintiff’s knowledge of those rules. For a plaintiff to have justifiably relied on a lawyer’s statements based on ethics rules imposing a duty of honesty on the lawyer, such as Model Rules

²¹⁵ MODEL RULES OF PROF’L CONDUCT r. 8.4(c) (AM. BAR ASS’N 2015).

²¹⁶ *Rosenbaum v. White*, 692 F.3d 593, 604 (7th Cir. 2012) (applying Indiana law); *Blankinship v. Brown*, 399 S.W.3d 303, 311 (Tex. App. 2013).

²¹⁷ See RESTATEMENT (SECOND) OF TORTS § 552 (AM. LAW INST. 1977) (“Information Negligently Supplied for the Guidance of Others”).

²¹⁸ See generally *Schmitz v. Davis*, No. 10-CV-4011-SAC, 2010 WL 3861843, at *7 (D. Kan. Sept. 23, 2010) (observing that “[a]ttorney conduct which violates an ethics rule may also violate an independent legal duty and a cause of action may ensue”).

²¹⁹ *Rosenbaum*, 692 F.3d at 604; *Spencer*, 299 P.3d at 395–96.

²²⁰ *Matsuura v. E.I. du Pont de Nemours & Co.*, 73 P.3d 687, 703 (Haw. 2003); see also *Hoyt Props., Inc. v. Prod. Res. Grp., L.L.C.*, 716 N.W.2d 366, 375 (Minn. Ct. App. 2006) (“A jury could reasonably conclude that because attorneys have a professional duty not to make false assertions, even to adversaries, [the plaintiffs’ owner’s] reliance was reasonable.”).

4.1(a) or 8.4(c), the plaintiff must have known of the rules and the duties they impose on lawyers at the time of the alleged misrepresentation.²²¹ Furthermore, the application of ethics rules alone will seldom serve to establish plaintiffs' justifiable or reasonable reliance; other factors frequently come into play.²²² Still, there is no doubting the potential force of rules of professional conduct when analyzing the element of reliance in fraud and negligent misrepresentation cases against lawyers.²²³

Rules of professional conduct may play a greater role in constructive fraud cases because constructive fraud requires a fiduciary or confidential relationship between the parties.²²⁴ Ethics rules may inform the scope of lawyers' fiduciary duties.²²⁵ In some jurisdictions, a lawyer's violation of an ethics rule may be sufficient to support a plaintiff's claim that the lawyer violated a fiduciary duty.²²⁶ Thus, in a constructive fraud case, a lawyer's violation of an ethics rule might evidence a breach of fiduciary duty, ultimately leading to liability for constructive fraud if the plaintiff can satisfy the remaining elements of the cause of action.

II. ILLUSTRATIVE CASES

Lawyers may be sued for fraud or negligent misrepresentation in various contexts. This Part discusses four illustrative cases: two based on lawyers' statements in connection with litigation, and two arising out of lawyers' transactional practices.

A. *Settlement Negotiations in Litigation*

*Slotkin v. Citizens Casualty Co. of New York*²²⁷ arose out of a medical malpractice case. Charlotte Slotkin gave birth to a brain-damaged son, Steven, in Beth-El Hospital in New York City in 1963.²²⁸ She was a diabetic and Steven's

²²¹ See, e.g., *Hoyt Props.*, 716 N.W.2d at 375 (involving a business owner who was a lawyer and who thus was aware of the opposing lawyers' duties not to make false statements of fact or law under Minnesota Rule of Professional Conduct 4.1).

²²² See Richmond, *supra* note 214, at 960 (discussing a plaintiff's reliance on a lawyer's alleged misrepresentation in a Missouri case).

²²³ See, e.g., *Hoyt Props.*, 716 N.W.2d at 375 (holding that the reasonableness of the plaintiff's owner's reliance on the accuracy of the statements made by opposing counsel based on their duties under Rule 4.1 presented a genuine issue of material fact that precluded summary judgment for the defense).

²²⁴ *Prakashpalan v. Engstrom, Lipscomb & Lack*, 167 Cal. Rptr. 3d 832, 854 (Ct. App. 2014).

²²⁵ *Id.* at 851; *Kidney Ass'n of Or., Inc. v. Ferguson*, 843 P.2d 442, 446 n.12 (Or. 1992) (explaining that rules of professional conduct may describe lawyers' fiduciary duties to clients at least in part).

²²⁶ See, e.g., *Hendry v. Pelland*, 73 F.3d 397, 401 (D.C. Cir. 1996) (applying District of Columbia law).

²²⁷ 614 F.2d 301 (2d Cir. 1979).

²²⁸ *Id.* at 305.

brain damage was attributable to the hospital's failure to properly administer insulin to her before delivery.²²⁹ Steven and his father sued Beth-El for medical malpractice. Beth-El had a \$200,000 primary liability insurance policy with Citizens Casualty Co. and a \$1 million excess insurance policy issued by Lloyd's of London underwriters.²³⁰ Citizens was in somewhat precarious financial shape, inasmuch as it was undergoing liquidation and rehabilitation.²³¹

The case went to trial in February 1971. Christopher McGrath, a Beth-El defense lawyer hired by Citizens, told the plaintiffs' lawyer, Max Toberoff, that Beth-El had only \$200,000 in insurance coverage.²³² McGrath also revealed that he had not told Beth-El's in-house lawyer about the trial and he refused Toberoff's request that he notify the hospital.²³³ Toberoff was concerned about the collectability of any judgment the plaintiffs might receive and he urgently communicated with the hospital's administrator, telling him that Beth-El risked a verdict exceeding \$1 million.²³⁴ The administrator dispatched George Berkowitz, a lawyer and Beth-El trustee, to the courthouse.²³⁵ Berkowitz also told Toberoff that Beth-El had only \$200,000 in insurance coverage based on information he obtained from McGrath, another defense lawyer, and Citizens' claims manager, Paul Ratner.²³⁶ Both Toberoff and the trial judge thought it odd that Beth-El had so little insurance.²³⁷

Despite Beth-El's ostensibly low policy limits and the plaintiffs' willingness to settle within them, the case proceeded to trial. The trial unfolded nicely for the plaintiffs.²³⁸ Just before the plaintiffs rested, a key medical expert for Beth-El changed his opinion and sided with them.²³⁹ The parties hastily convened a settlement conference before the trial judge.²⁴⁰ McGrath again stated that the total insurance coverage available was \$200,000, and that "he knew that the [h]ospital did not have additional insurance with other companies."²⁴¹ Based on this representation, the case settled for \$185,000.²⁴² The lawyers drafted a stipulation to read into the record which provided that "the attorney for the defendant represents that the total insurance coverage of the defendant is the sum of \$200,000, under a policy with Citizens Casualty, and to the best of

²²⁹ *Id.*

²³⁰ *Id.*

²³¹ *Id.*

²³² *Id.*

²³³ *Id.*

²³⁴ *Id.*

²³⁵ *Id.*

²³⁶ *Id.*

²³⁷ *Id.* at 306.

²³⁸ *Id.*

²³⁹ *Id.* at 307.

²⁴⁰ *Id.*

²⁴¹ *Id.*

²⁴² *Id.*

his knowledge there are no other policies covering this event.”²⁴³ McGrath and Berkowitz verbally approved the stipulation on the record.²⁴⁴

The obvious problem was that McGrath’s and Berkowitz’s representations were false.²⁴⁵ While Berkowitz’s misstatements could be excused due to his second-hand knowledge and the lack of a reason to doubt its sources, the same could not be said of McGrath’s misrepresentations. McGrath had “complete access” to documents clearly demonstrating the existence of the excess policy, such as letters from a lawyer for the Lloyd’s of London underwriters inquiring about the Slotkin case.²⁴⁶ The file containing these letters was in the possession of McGrath’s firm during the trial.²⁴⁷

The existence of the Lloyd’s of London excess policy was revealed shortly after the settlement.²⁴⁸ The trial judge had not yet entered an order allocating the settlement funds and thus there was no final judgment.²⁴⁹ Unfortunately, the parties could not re-open settlement discussions because the Lloyd’s underwriters refused to participate based on late notice of the Slotkin claim.²⁵⁰ For a variety of reasons, the plaintiffs could not re-try the case.²⁵¹ The trial court thus approved the \$185,000 settlement, with Toberoff’s intention to sue for fraud being well known.²⁵²

The plaintiffs sued Citizens, its reinsurers, McGrath, Ratner, Berkowitz, and another lawyer for Citizens in federal court.²⁵³ The jury returned a \$680,000 verdict for the plaintiffs for fraud, allocating the damages as \$500,000 to Citizens, \$100,000 to Berkowitz, \$60,000 to Ratner, and \$20,000 to McGrath.²⁵⁴ The district court granted the defendants’ motion for JNOV.²⁵⁵ It reasoned that because the plaintiffs learned of the excess policy before the trial court had entered a final judgment, they were bound by the settlement.²⁵⁶ The court further reasoned that the “plaintiffs had not significantly changed position to their prejudice before learning the truth” about the hospital’s insurance coverage.²⁵⁷ The plaintiffs appealed to the Second Circuit.

²⁴³ *Id.*

²⁴⁴ *Id.*

²⁴⁵ *Id.* at 314–15.

²⁴⁶ *Id.* at 307.

²⁴⁷ *Id.* at 307–08.

²⁴⁸ *Id.* at 308.

²⁴⁹ *Id.* at 308–09.

²⁵⁰ *Id.* at 309.

²⁵¹ *Id.* at 309–10.

²⁵² *Id.* at 310.

²⁵³ *Id.*

²⁵⁴ *Id.* at 310–11.

²⁵⁵ *Id.* at 311.

²⁵⁶ *Id.*

²⁵⁷ *Id.*

On appeal, the *Slotkin* court concluded that the district court erred in granting the defendants' motion for JNOV.²⁵⁸ Believing that the jury could have reasonably found that the various misrepresentations made to the plaintiffs constituted legal fraud, the court addressed the defendants' liability.²⁵⁹

The Second Circuit reasoned that the jury could have properly found McGrath liable for fraud.²⁶⁰ McGrath stipulated that to the best of his knowledge, there was only \$200,000 in insurance coverage available to Beth-El, despite his possession of documents indicating that the hospital had \$1 million in excess coverage.²⁶¹ McGrath's insistence that the hospital had only \$200,000 in coverage in the face of contrary facts met the New York definition of scienter: "'a reckless indifference to error,' 'a pretense of exact knowledge,' or '[an] assertion of a false material fact "susceptible of accurate knowledge" but stated to be true on the personal knowledge of the representer.'"²⁶² Berkowitz, on the other hand, avoided liability.²⁶³ While he was easily negligent or even grossly negligent in making the statements that he did about Beth-El's insurance, his conduct did not reflect the scienter necessary for fraud liability under New York law.²⁶⁴ The court ultimately gave the plaintiffs the option of either reinstating the \$680,000 judgment, or retrying the case against all defendants except Berkowitz.²⁶⁵ McGrath petitioned for rehearing to no avail.²⁶⁶

It is difficult to understand how McGrath could have made the representations he did about insurance coverage. The notion that Beth-El had only \$200,000 in coverage struck both Toberoff and the trial court as unusual; it should have similarly impressed McGrath. At the very least, Toberoff's and the court's reservations should have inspired McGrath to attempt to ascertain the hospital's true coverage before finally committing to \$200,000.

It seems more likely that McGrath knew of the hospital's excess policy and opted to conceal its existence. After all, he had correspondence from a lawyer for the excess carrier inquiring about the status of the case in his files.²⁶⁷ A defense lawyer in McGrath's shoes would normally be expected to know about the existence of excess insurance.²⁶⁸ It is no answer to say that McGrath had

²⁵⁸ *Id.* at 314.

²⁵⁹ *Id.*

²⁶⁰ *Id.*

²⁶¹ *Id.*

²⁶² *Id.*

²⁶³ *Id.* at 315.

²⁶⁴ *Id.*

²⁶⁵ *Id.* at 318.

²⁶⁶ *Id.* at 324–25.

²⁶⁷ *Id.* at 307–08.

²⁶⁸ Today, McGrath would certainly know about the existence of excess coverage by virtue of routine pretrial discovery and disclosures. *See* FED. R. CIV. P. 26(a)(1)(A)(iv) (requiring the initial disclosure of "any insurance agreement under which an insurance business may be liable to satisfy all or part of a possible judgment in the action or to indemnify or reimburse

nothing to gain and much to lose from concealing the excess policy,²⁶⁹ because he arguably *did* have something to gain by concealing it. That is, by settling a difficult case on favorable terms, he might have impressed Citizens or the Lloyd's underwriters with his craftiness and thus have earned additional business from them. Or, he might have thought that Beth-El administrators would be impressed by his tactical prowess and engage him to defend the hospital in future medical malpractice cases. Regardless, *Slotkin* demonstrates that fraud and negligent misrepresentation claims against lawyers can even arise out of adversarial encounters.

B. Litigators' Allegedly Fraudulent Statements Outside of Settlement Negotiations

Shafer v. Berger, Kahn, Shafton, Moss, Figler, Simon, & Gladstone,²⁷⁰ like *Slotkin*, arose out of a lawyer's misstatement about insurance coverage, albeit in a different context. The plaintiffs in *Shafer* were homeowners who pursued arbitration against their builder, Tri County Builders, and Tri County's two partners, Jay DeMay and Perry Hanstad, to recover for construction defects in their home.²⁷¹ The Shafers' arbitration demand included claims for breach of contract, fraud, negligence, and intentional infliction of emotional distress, and sought both compensatory and punitive damages.²⁷² DeMay tendered the defense of the Shafers' action to Tri County's liability insurer, Truck Insurance Exchange ("Truck").²⁷³ Truck agreed to defend Tri County, DeMay, and Hanstad under a reservation of rights.²⁷⁴ DeMay responded to Truck's reservation of rights letter by asking Truck to provide him with independent counsel at its expense.²⁷⁵ DeMay was concerned that because the Shafers alleged both negligent and intentional wrongdoing, any defense lawyer Truck appointed would

for payments made to satisfy the judgment"). Toberoff would know about the presence of excess insurance for the same reason.

²⁶⁹ *Slotkin*, 614 F.2d at 318–19 (Van Graafeiland, J., dissenting).

²⁷⁰ 131 Cal. Rptr. 2d 777 (Ct. App. 2003).

²⁷¹ *Id.* at 782.

²⁷² *Id.*

²⁷³ *Id.*

²⁷⁴ *Id.* A "reservation of rights" refers to an insurance company's unilateral decision to reserve its right to later contest coverage notwithstanding its initial decision to defend the insured. *See Mastellone v. Lightning Rod Mut. Ins. Co.*, 884 N.E.2d 1130, 1139–40 (Ohio Ct. App. 2008) ("By definition, a reservation of rights means that the insurer does not believe that coverage is available under the policy, but that it is proceeding to defend a claim in order to control the defense."). An insurer reserves its rights by sending the insured a reservation of rights letter. A reservation of rights letter puts the insured on notice that there may be a conflict between its interests and those of the insurer, and that the insured may potentially be exposed to personal liability. *Atlanta Cas. Co. v. Stephens*, 825 S.W.2d 330, 333 (Mo. Ct. App. 1992).

²⁷⁵ *Shafer*, 131 Cal. Rptr. 2d at 783. For more information about insureds' right to independent counsel, see Douglas R. Richmond, *Independent Counsel in Insurance*, 48 SAN DIEGO L. REV. 857, 858–59 (2011).

have a conflict of interest given that a finding of liability based on intentional acts would allow Truck to deny coverage, while a determination of negligence would obligate it to indemnify the defendants.²⁷⁶

Truck sought advice regarding DeMay's request from Lance LaBelle of the Berger, Kahn law firm.²⁷⁷ LaBelle communicated with Chris Lundblad of Truck about modifying Truck's original reservation of rights letter so as to allow Truck to control the defense of the arbitration, rather than having to accept independent counsel.²⁷⁸ Thereafter, LaBelle issued a superseding reservation of rights letter on Truck's behalf that no longer reserved Truck's right to deny coverage for liability premised on the defendants' willful or intentional acts, but which still reserved Truck's right to deny coverage for punitive damages.²⁷⁹ This letter, when read together with the original reservation of rights letter and a separate letter from LaBelle to Lundblad regarding the plan to retain control of the defense, implicitly acknowledged Truck's obligation to indemnify the defendants if they were held liable for willful misconduct.²⁸⁰

The Shafers' case went to arbitration and the arbitrators awarded them over \$311,000 against all three defendants, and \$25,000 against DeMay alone for fraud.²⁸¹ A trial court affirmed the award and entered judgment for the Shafers.²⁸²

Truck grudgingly paid \$120,000 of the judgment.²⁸³ In a letter to the Shafers' lawyer transmitting the check for that payment, LaBelle referred to the superseding reservation of rights letter—although he did not include a copy of the letter—and asserted that California public policy precluded indemnity for fraud-related damages.²⁸⁴ In another letter to the Shafers' lawyer, LaBelle emphasized that the arbitrators had found that the defendants had never intended to perform their contract with the Shafers and explained that the Truck policy did not cover property damage expected or intended by the insureds.²⁸⁵ Truck never fully satisfied the compensatory damage portion of the judgment.²⁸⁶

Hanstad tried to discharge the judgment against him in bankruptcy but failed.²⁸⁷ He then successfully sued Truck for bad faith, represented by the Shafers' lawyer.²⁸⁸ During discovery in the bad faith case, the Shafers' lawyer

²⁷⁶ *Shaffer*, 131 Cal. Rptr. 2d at 783.

²⁷⁷ *Id.*

²⁷⁸ *Id.*

²⁷⁹ *Id.*

²⁸⁰ *Id.* at 783–84.

²⁸¹ *Id.* at 784.

²⁸² *Id.* at 784–85.

²⁸³ *Id.* at 785.

²⁸⁴ *Id.* at 785 n.4.

²⁸⁵ *Id.* at 785–86.

²⁸⁶ *Id.* at 785.

²⁸⁷ *Id.* at 786.

²⁸⁸ *Id.*

learned for the first time that Truck had agreed to indemnify Tri County, DeMay, and Hanstad against liability for willful acts.²⁸⁹ LaBelle, who was deposed in the bad faith case, acknowledged the agreement between Truck and the defendants in the underlying litigation.²⁹⁰

Armed with this information, the Shafers sued Truck and LaBelle, as well as Berger, Kahn for fraud.²⁹¹ LaBelle filed a demurrer, arguing that he had no duty to truthfully disclose the defendants' insurance coverage to the Shafers and that the Shafers had not justifiably relied on any statements he made.²⁹² The trial court granted the demurrer with leave to amend. The Shafers filed an amended complaint alleging fraud and conspiracy that read, in part, as follows:

After the Shafers obtained a judgment against Truck's insureds, LaBelle represented to the Shafers that Truck had not agreed to provide indemnity for willful acts. In fact, Truck had agreed to indemnification. While LaBelle and Truck knew that the statement about indemnity was false, the Shafers did not know of its falsity. LaBelle made the false statement with the intention of inducing the Shafers to forgo full payment on the judgment. The Shafers relied on LaBelle's false statement, resulting in economic and noneconomic damages.²⁹³

LaBelle again demurred, and this time the trial court sustained the demurrer without leave to amend and dismissed the case against LaBelle and his law firm.²⁹⁴ The Shafers appealed to the California Court of Appeal.

On appeal, the Shafers contended that the trial court erred in dismissing their fraud claim. The appellate court agreed.²⁹⁵ In doing so, the court rejected LaBelle's arguments that his statements about insurance coverage were not actionable because they were legal opinions, that he owed the Shafers' no duty of truthfulness in any event, and that any claimed reliance on the Shafers' part was unjustified.²⁹⁶

It was clear to the court from the two reservation of rights letters and LaBelle's separate letter to Lundblad that Truck had agreed to indemnify Tri County, DeMay, and Hanstad against liability arising out of their willful acts to avoid paying for independent counsel for its insureds.²⁹⁷ Yet, to justify Truck's payment of only \$120,000 toward a judgment of approximately \$336,000, LaBelle directed the Shafers' lawyer to the policy language precluding coverage for intentional acts and a California statute foreclosing insurance coverage for willful acts.²⁹⁸ "Thus, LaBelle allegedly misrepresented the scope of insurance

²⁸⁹ *Id.*

²⁹⁰ *Id.*

²⁹¹ *Id.* (noting that the Shafers also sued Truck for breach of contract and bad faith).

²⁹² *Id.*

²⁹³ *Id.* at 786–87.

²⁹⁴ *Id.* at 787.

²⁹⁵ *Id.*

²⁹⁶ *Id.* at 792.

²⁹⁷ *Id.* at 792–93.

²⁹⁸ *Id.* at 793.

coverage” even though “[h]e had a duty not to make fraudulent statements.”²⁹⁹ Under the circumstances, it was reasonably apparent that the Shafers would regard LaBelle’s statements about insurance coverage as statements of fact rather than as legal opinions.³⁰⁰ Accordingly, the Shafers’ amended complaint adequately pleaded that LaBelle had made fraudulent statements about Truck’s insurance coverage and that they reasonably viewed his statements as expressions of fact.³⁰¹

As for the reasonableness of the Shafers’ reliance on LaBelle’s statements regarding coverage, they had no reason to doubt him, and they had no reason to suspect Truck’s true coverage position, because they never received copies of either of Truck’s reservation of rights letters.³⁰² In short, “the Shafers reasonably relied on the coverage representations made by counsel for an insurance company.”³⁰³ Furthermore, LaBelle’s relationship with the Shafers was not that of an adversary or opponent, as the court explained:

Under section 11580 [of the California Insurance Code], Truck had to pay the Shafers the amount of the judgment, subject to the terms . . . of the insurance policy, including any reservation of rights In that sense, the Shafers were to be treated as the insureds. Section 11580 “inure[s] to the benefit of any and every person who might be negligently injured by the assured as completely as if *such injured person had been specifically named in the policy.*” And, as stated [earlier in the opinion], the Shafers were third party beneficiaries of the insurance policy [because they were judgment creditors of the defendants].³⁰⁴

Finally, LaBelle argued that the litigation privilege attached to his statements about insurance coverage and accordingly rendered them non-actionable.³⁰⁵ The court rejected LaBelle’s argument, reasoning that recognizing the litigation privilege would be inconsistent with section 11580 of the California Insurance Code, which empowers a party who obtains a judgment against an insured to sue the insurer as a judgment creditor to collect the judgment.³⁰⁶ As interpreted by the California Supreme Court, that statute also makes a judgment creditor a third party beneficiary of the insurance policy on which it is suing, further indicating that the litigation privilege should not operate to defeat a judgment creditor’s exercise of its statutory right.³⁰⁷ Continuing, the court explained:

²⁹⁹ *Id.*

³⁰⁰ *Id.* (quoting RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 98 cmt. c (AM. LAW INST. 2000)).

³⁰¹ *Id.* at 793.

³⁰² *Id.*

³⁰³ *Id.* at 793–94.

³⁰⁴ *Id.* at 794 (emphasis in original) (citations omitted).

³⁰⁵ *Id.* at 795. Generally speaking, the litigation privilege shields lawyers against liability based on communications made in connection with judicial or quasi-judicial proceedings. *Id.*

³⁰⁶ *Id.* at 795–96.

³⁰⁷ *Id.* at 796–97 (quoting *Murphy v. Allstate Ins. Co.*, 553 P.2d 584, 587–88 (Cal. 1976)).

Just as an insurer may be liable for defrauding its insured . . . so an insurer should not be allowed to deceive a third party beneficiary of an insurance policy. And if an insurer may be found liable to a third party beneficiary for fraud, so may its coverage counsel.

Counsel retained by an insurer has an obligation to be truthful in describing insurance coverage to a third party beneficiary. The litigation privilege is not a license to deceive an injured party who steps into the shoes of an insured. Section 11580 grants an injured party the right to file suit in order to recover under the insurance policy. Coverage counsel may not commit fraud in an attempt to defeat that right.³⁰⁸

LaBelle's litigation privilege argument was doomed from the outset for two additional reasons. One, it did not track any of the purposes underlying the litigation privilege.³⁰⁹ These include safeguarding witnesses and litigants from subsequent tort suits, ensuring open communications, promoting zealous representation, obligating litigants to expose witnesses' biases and false evidence, and enhancing the finality of judgments.³¹⁰ Two, the litigation privilege generally does not protect a lawyer against liability for fraud.³¹¹

After concluding that the Shafers could sue LaBelle for fraud and that the trial court erred in sustaining LaBelle's demurrer without leave to amend,³¹² the *Shafer* court went on to hold that the Shafers could sue LaBelle for conspiring with Truck to defraud them.³¹³ It therefore reversed the trial court's judgment for LaBelle.³¹⁴

Although surely disappointing to LaBelle and his firm, the decision in *Shafer* was unsurprising. First, recall that the case reached the *Shafer* court on appeal from a demurrer, meaning that the court assumed all well-pleaded facts in the Shafers' amended complaint to be true and applied a de novo standard of review to determine whether the amended complaint stated a cause of action.³¹⁵ Second, rather than being non-actionable legal opinions, LaBelle's coverage statements were (1) under the circumstances, reasonably capable of construction as statements of fact;³¹⁶ and (2) probably constituted "statements of law

³⁰⁸ *Id.* at 797 (citations omitted).

³⁰⁹ *Id.* at 798.

³¹⁰ *Id.*

³¹¹ *Id.* (quoting RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 98 (AM. LAW INST. 2000)); *N.Y. Cooling Towers, Inc. v. Goidel*, 805 N.Y.S.2d 779, 783 (2005); *Moss v. Parr Waddoups Brown Gee & Loveless*, 285 P.3d 1157, 1166 (Utah 2012); *Clark v. Druckman*, 624 S.E.2d 864, 870 (W. Va. 2005). *But see* *Dawley v. NF Energy Corp. of Am.*, 492 F. App'x 77, 80 (11th Cir. 2012) (applying the absolute litigation privilege to fraud claims under Florida law); *Simms v. Seaman*, 69 A.3d 880, 892 (Conn. 2013) (stating that "attorneys are shielded by the litigation privilege from claims of fraud").

³¹² *Shafer*, 131 Cal. Rptr. 2d at 799.

³¹³ *Id.* at 801.

³¹⁴ *Id.*

³¹⁵ *Maslo v. Ameriprise Auto & Home Ins.*, 173 Cal. Rptr. 3d 854, 859 (Ct. App. 2014) (quoting *Kyablue v. Watkins*, 149 Cal. Rptr. 3d 156, 158 (Ct. App. 2012)).

³¹⁶ *Shafer*, 131 Cal. Rptr. at 793.

that impl[ied] knowledge of facts,” which are actionable.³¹⁷ Third, the court’s view was surely colored by LaBelle’s offensive attempt “to have his cake and eat it too.”³¹⁸ After all, he formulated a strategy that created coverage for the Shafers’ claims to spare Truck independent counsel fees and then, to avoid the very obligation he created, turned full circle—knowingly exposing Truck’s insureds to personal liability and deliberately impairing the Shafers’ statutory rights in the process.

C. Third Party Reliance on a Lawyer’s Statements in a Real Estate Transaction

Unlike *Slotkin* and *Shafer*, where the claims against the lawyers arose out of their conduct in connection with litigation, *Petrillo v. Bachenberg*³¹⁹ arose out of a lawyer’s transactional practice. The *Petrillo* saga began in 1987, when Rohrer Construction wanted to sell a tract of undeveloped land in Union Township, New Jersey. Rohrer was represented by lawyer Bruce Herrigel.³²⁰ Rohrer hired Heritage Consulting Engineers to conduct percolation tests on the land in connection with a planned sale of the property to Land Resources Corp.³²¹ Union Township required two successful percolation tests to approve a septic system.³²² Unfortunately for Rohrer, Heritage’s first report in September 1987 revealed that only one of the twenty-two tests was successful.³²³ A second report issued in November 1987 showed that of eight tests conducted in the prior month, only one succeeded.³²⁴ In other words, of the thirty tests that Heritage conducted over the course of two months, twenty-eight were unsuccessful and only two were successful.³²⁵ This suggested that the two successful tests were anomalies and did not reflect the property’s true soil profile, and therefore that the property was not suitable for a septic system.³²⁶ Rohrer’s contract to sell the property to Land Resources thus fell through.³²⁷

Rohrer then listed the property for sale with a real estate broker, Bachenberg & Bachenberg, Inc.³²⁸ In October 1988, William Bachenberg

³¹⁷ *Hoyt Props., Inc. v. Prod. Res. Grp., L.L.C.*, 716 N.W.2d 366, 372–73 (Minn. Ct. App. 2006), *aff’d*, 736 N.W.2d 313 (Minn. 2007).

³¹⁸ *Shafer*, 131 Cal. Rptr. 2d 794.

³¹⁹ *Petrillo v. Bachenberg*, 655 A.2d 1354 (N.J. 1995).

³²⁰ *Id.* at 1355.

³²¹ *Id.* Percolation tests are used to determine whether soil is suitable for the installation of a septic system. *Id.*

³²² *Id.*

³²³ *Id.*

³²⁴ *Id.*

³²⁵ *Id.*

³²⁶ *Petrillo v. Bachenberg*, 623 A.2d 272, 274 (N.J. Super. Ct. App. Div. 1993), *aff’d*, 655 A.2d 1354 (N.J. 1995).

³²⁷ *Petrillo*, 655 A.2d at 1355.

³²⁸ *Id.*

(“Bachenberg”) asked Herrigel for information about the property.³²⁹ In response, Herrigel told Bachenberg that “he had some perc results,” and sent him a two-page document that consisted of one page from each of the two reports Heritage prepared for Rohrer.³³⁰ The first page was the first page of Heritage’s initial report, which reflected one successful test and five failed tests.³³¹ The second page was taken from Heritage’s second report; it reflected one successful and one failed test.³³² Herrigel’s “composite report” thus appeared to reflect a single series of seven percolation tests with two successful tests, rather than the true result: thirty tests with only two successful tests, an indication the property was a poor candidate for a septic system.³³³ Bachenberg & Bachenberg included Herrigel’s composite report in its sales literature.³³⁴ Herrigel would later admit that he had complete copies of both Heritage reports but that he instead gave Bachenberg the composite report.³³⁵

In December 1988, Bachenberg and a partner, John Matthews, bought the property at a sheriff’s sale for \$70,000.³³⁶ Bachenberg asked Rohrer for a copy of Heritage’s percolation test reports soon thereafter, but Rohrer refused to share them because Bachenberg would not reimburse him for the cost of Heritage’s engineering fees.³³⁷

Bachenberg later listed the property for sale at a price of \$160,000.³³⁸ In February 1989, Lisa Petrillo inquired about purchasing the property to build and operate a childcare facility.³³⁹ Bachenberg gave her a copy of the composite report during their first meeting.³⁴⁰

In June 1989, Petrillo agreed to buy the property for \$160,000.³⁴¹ Herrigel represented Bachenberg in the sale.³⁴² Herrigel did not tell Petrillo’s lawyer that the composite report omitted numerous test results.³⁴³ At the insistence of Petrillo’s lawyer, the sales contract gave Petrillo forty-five days to perform independent soil and water tests on the property, including percolation tests. The

³²⁹ *Id.*

³³⁰ *Id.*

³³¹ *Id.*

³³² *Id.*

³³³ *Id.*

³³⁴ *Id.*

³³⁵ *Id.* (noting that in Herrigel’s appellate papers he stated that “he delivered the composite report to Bachenberg,” and “[did] not deny that he prepared the composite report,” but argued that “‘there was no evidence given during plaintiff’s proofs [at trial] that [he] had in fact prepared the erroneous two-page report’”) (quoting Herrigel’s appellate papers).

³³⁶ *Id.*

³³⁷ *Id.*

³³⁸ *Id.* at 1356.

³³⁹ *Id.*

³⁴⁰ *Id.*

³⁴¹ *Id.*

³⁴² *Id.*

³⁴³ *Id.*

contract further provided that she could rescind the deal if the percolation tests were unsatisfactory to her.³⁴⁴

In August 1989, an engineering firm working for Petrillo performed six unsuccessful percolation tests on the property and concluded that it was unsuitable for a septic system.³⁴⁵ Petrillo promptly informed Bachenberg that their sales contract was null and void.³⁴⁶

In response, Bachenberg hired Heritage to design a septic system that would satisfy the Township, but Petrillo refused to accept the design.³⁴⁷ Petrillo asked for time to conduct additional percolation tests, but Bachenberg declined her request.³⁴⁸ During these ongoing negotiations, Herrigel sent Petrillo the complete copies of the Heritage reports prepared for Rohrer.³⁴⁹ Bachenberg and Petrillo never could resolve their differences.

When Bachenberg refused to return Petrillo's \$16,000 down payment on the theory that she had breached their contract, she sued him, Matthews, and Herrigel for the return of her down payment and the cost of her engineering fees.³⁵⁰ She alleged that the defendants were guilty of breach of contract, fraud, concealment, negligent misrepresentation, and conspiracy.³⁵¹ With respect to Herrigel, she alleged that his failure to timely provide her with the complete Heritage reports breached a duty he owed her.³⁵² Petrillo claimed that had she known that the property had passed only two of the thirty percolation tests, she never would have contracted to buy the land or hired engineering firms to undertake site work.³⁵³

The case went to trial, and at the close of the plaintiff's case the trial court directed a verdict for Herrigel, reasoning that he owed Petrillo no duties.³⁵⁴ Losing her remaining claims either on motion or by way of defense verdict, Petrillo appealed.³⁵⁵

The appellate court reversed the dismissal of Petrillo's negligent misrepresentation claim against Herrigel. The court reasoned that a jury could have found that when Herrigel gave Bachenberg the composite report, "Herrigel should have known that Bachenberg would provide the report to a prospective purchaser, such as Petrillo, who would rely on the report in deciding whether to

³⁴⁴ *Id.*

³⁴⁵ *Id.*

³⁴⁶ *Id.*

³⁴⁷ *Id.*

³⁴⁸ *Id.*

³⁴⁹ *Id.*

³⁵⁰ *Id.*

³⁵¹ *Id.*

³⁵² *Id.*

³⁵³ *Id.*

³⁵⁴ *Id.*

³⁵⁵ *Id.* at 1356–57.

purchase the property.”³⁵⁶ Herrigel then sought review by the New Jersey Supreme Court.³⁵⁷

The New Jersey Supreme Court observed that whether a lawyer may be held to owe a duty to a non-client requires a balancing of the lawyer’s duty to vigorously represent his client with “the duty not to provide misleading information on which third parties foreseeably will rely.”³⁵⁸ When courts extend lawyers’ duties to third parties, they typically do so where the lawyer intended that a third party would rely on the lawyer’s work or should have foreseen that possibility.³⁵⁹ The court explained that preparation of legal opinion letters is an archetypal example of lawyer conduct giving rise to third-party liability because a legal opinion letter is intended to induce reliance by others, but the preparation of other types of documents and other sales-related activities can also expose lawyers to third-party liability.³⁶⁰ The court also recognized that lawyers may owe a duty of care to non-clients when they know or reasonably should know that non-clients will rely on their representations and the non-clients are not too remote from the lawyers to deserve protection.³⁶¹ Indeed, that is the negligent misrepresentation regime expressed in section 552 of the Restatement (Second) of Torts.³⁶²

Although Herrigel did not prepare an opinion letter, he extracted information from the Heritage test reports, created the composite report, and gave the composite report to Bachenberg.³⁶³ The court’s initial task, therefore, was to determine the purpose of the composite report.³⁶⁴

It was possible that Herrigel may have intended the composite report to reflect only that the property had passed two percolation tests.³⁶⁵ But Herrigel’s subjective intent did not control the court’s analysis; rather, the objective meaning of the composite report was the relevant factor.³⁶⁶ In assessing the report’s objective meaning, the court was influenced by the parties’ roles.³⁶⁷ Herrigel was a lawyer who, in connection with his client’s efforts to sell the property,

³⁵⁶ *Id.* at 1357. The appellate court also reversed other aspects of the trial court judgment in ways favorable to Petrillo, *see id.*, but those issues are not relevant to our discussion.

³⁵⁷ *Id.* at 1355.

³⁵⁸ *Id.* at 1357.

³⁵⁹ *Id.*

³⁶⁰ *Id.* at 1360. (discussing *Molecular Tech. Corp. v. Valentine*, 925 F.2d 910, 915–17 (6th Cir. 1991) (involving a lawyer’s preparation of a private offering statement for a client); *Century 21 Deep S. Props., Ltd. v. Corson*, 612 So. 2d 359, 374 (Miss. 1992) (holding a lawyer liable to third-parties for negligence in a title search)).

³⁶¹ *Petrillo*, 655 A.2d at 1359–60.

³⁶² *Id.* at 1360 (referring to and quoting the RESTATEMENT (SECOND) OF TORTS § 552 (AM. LAW. INST. 1977)).

³⁶³ *Id.* at 1361.

³⁶⁴ *Id.*

³⁶⁵ *Id.*

³⁶⁶ *Id.*

³⁶⁷ *Id.*

delivered the composite report to a real estate broker.³⁶⁸ The court inferred that when Herrigel gave the composite report to Bachenberg, he knew, or should have known, that Bachenberg might share it with prospective purchasers of the property.³⁶⁹ Even so, Herrigel did nothing to limit prospective purchasers' foreseeable use of the report.³⁷⁰ He never indicated in the composite report or a cover letter that the report was incomplete or might be considered inaccurate because it did not reflect all percolation test results.³⁷¹

After Bachenberg purchased the property from Rohrer, Herrigel represented him in connection with the aborted sale of the property to Petrillo.³⁷² "Although compiling an engineering report to help a client sell real estate may not be part of a lawyer's stock-in-trade," the court observed, "representing the seller of real estate is a traditional legal service."³⁷³ Herrigel's continuing involvement as a lawyer in the transfer of the property permitted the court to infer "that the objective purpose of the [composite] report was to induce a prospective purchaser to buy the property."³⁷⁴ His continuing involvement supported the further inference that he knew Bachenberg intended to use the composite report to assure prospective buyers of the property's suitability for a septic system.³⁷⁵

A prospective buyer reading the composite report reasonably could believe that the property had passed two of seven percolation tests rather than two of thirty.³⁷⁶ And, based on that conclusion, a person might agree to buy the property when she would never do so if she had seen the complete set of percolation test reports.³⁷⁷ In the court's view, Herrigel should have foreseen that scenario.³⁷⁸ In summary, it would be reasonable for a jury to infer that the composite report misrepresented material facts.³⁷⁹

By giving Bachenberg the composite report and thereafter representing him in the contested sale of the property to Petrillo, "Herrigel assumed a duty to Petrillo to provide reliable information regarding the percolation tests."³⁸⁰ He "controlled the risk that the composite report would mislead a purchaser" of the property.³⁸¹ It was therefore fair for Herrigel to shoulder the risk of loss resulting from the delivery of a misleading report.³⁸² As the court summarized:

³⁶⁸ *Id.*

³⁶⁹ *Id.*

³⁷⁰ *Id.*

³⁷¹ *Id.*

³⁷² *Id.*

³⁷³ *Id.*

³⁷⁴ *Id.*

³⁷⁵ *Id.*

³⁷⁶ *Id.*

³⁷⁷ *Id.*

³⁷⁸ *Id.*

³⁷⁹ *Id.*

³⁸⁰ *Id.*

³⁸¹ *Id.*

³⁸² *Id.*

Herrigel easily could have limited his liability. Most simply, he could have sent complete copies of both [Heritage] reports to Bachenberg. Alternatively, Herrigel could have sent a letter to Bachenberg stating that the property had passed two successful percolation tests as required by Union Township. Or he could have stated either in a letter to Bachenberg or in the composite report that the report evidenced only that the property had yielded two successful percolation tests and that no one should rely on the report for any other purpose. Because Herrigel did nothing to limit the objective purpose of the composite report, he should have foreseen that Petrillo, as a prospective purchaser, would rely on the facts set forth in the report. Accordingly, Herrigel's duty extend[ed] to Petrillo. Given Petrillo's concern about percolation . . . Herrigel's duty include[d] the obligation to provide information about unsuccessful, as well as successful, percolation tests.³⁸³

The court was careful to note that its decision did not preclude a jury from finding in Herrigel's favor.³⁸⁴ It was possible that a jury might find that Petrillo only cared that the property had passed two percolation tests, or that the omission of the many unsuccessful tests from the composite report was neither material nor misleading; those were all factual issues to be resolved on remand.³⁸⁵ The *Petrillo* court decided only that a jury should be allowed to "determine . . . the effect of Herrigel's alleged negligent misrepresentation."³⁸⁶ The New Jersey Supreme Court accordingly affirmed the judgment of the lower appellate court.³⁸⁷

A dissenting justice argued that Herrigel's preparation of the composite report was nothing like the preparation of a legal opinion where, in the latter case, the authoring lawyer intends to induce reliance by third parties.³⁸⁸ The dissenting justice's essential concern was that the majority effectively was imposing on lawyers "an overbroad, virtually unlimited duty of care for remote non-clients."³⁸⁹

Had he sent the composite report to Bachenberg while representing Rohrer and then had no further dealings with Bachenberg, Herrigel might have been able to argue that any potential liability to third parties would have been too attenuated to recognize.³⁹⁰ But those weren't the facts. Herrigel represented Bachenberg in selling the property to Petrillo.³⁹¹ In furthering that sale,

³⁸³ *Id.* at 1361–62.

³⁸⁴ *Id.* at 1362.

³⁸⁵ *Id.*

³⁸⁶ *Id.*

³⁸⁷ *Id.*

³⁸⁸ *Id.* at 1365 (Garibaldi, J., dissenting).

³⁸⁹ *Id.*

³⁹⁰ See RESTATEMENT (SECOND) OF TORTS § 552 cmt. h (AM. LAW INST. 1977) ("It is not enough [for liability] that the maker knows of the ever-present possibility of repetition [of an alleged misrepresentation] to anyone, and the possibility of action in reliance upon it, on the part of anyone to whom it may be repeated.").

³⁹¹ *Petrillo*, 655 A.2d at 1363 (Stein, J., concurring).

Bachenberg gave the composite report to Petrillo.³⁹² On those facts, a jury could conclude that Herrigel should have foreseen that Petrillo would receive a copy of the composite report and that she would detrimentally rely on it.³⁹³ Because of the discrete facts on which the court's holding rested, a concurring justice reasoned that the likelihood that the court's decision would materially affect lawyers' potential liability to third parties was "minimal indeed."³⁹⁴ As the majority also noted in blunting the dissent, the holding went "no further than to state that Herrigel had a duty not to misrepresent negligently the contents of a material document on which he knew others would rely to their financial detriment."³⁹⁵ As the court further explained, "[i]n many situations, lawyers, like people generally, may not have a duty to act, but when they act, like other people, they should act carefully."³⁹⁶

In hindsight, it is interesting that Herrigel gave Petrillo complete copies of the two Heritage reports.³⁹⁷ But he did so *after* Bachenberg had given her the composite report as part of a sales packet.³⁹⁸ Reading between the lines, those facts suggest that Herrigel had not anticipated that Bachenberg would give Petrillo the composite report. The problem for Herrigel was that he arguably *should have known* that Bachenberg would give the composite report to Petrillo, and that was enough to get the case to a jury.³⁹⁹ It was irrelevant that Herrigel did not know Petrillo's identity when he delivered the document to Bachenberg; it is sufficient for purposes of identifying a plaintiff to whom a duty may be owed "that the maker [of an alleged misrepresentation] supplies the information for repetition to a certain group or class of persons and that the plaintiff proves to be one of them, even though the maker had never heard of [her] by name when the information was given."⁴⁰⁰

D. *The Dean Foods Opinion Controversy*

The *Petrillo* court referred to opinion practice as an area in which lawyers' potential liability to third parties was well established.⁴⁰¹ By way of foundation, at the closing of a business transaction, the lawyer for the company often delivers to the opposing party—be it an acquiring company, an investor, or a lender—a closing opinion.⁴⁰² The closing opinion is in fact a letter that sets forth, in

³⁹² *Id.*

³⁹³ *Id.*

³⁹⁴ *Id.*

³⁹⁵ *Id.* at 1362 (majority opinion).

³⁹⁶ *Id.*

³⁹⁷ *Id.* at 1356.

³⁹⁸ *Id.*

³⁹⁹ *Id.* at 1361.

⁴⁰⁰ RESTATEMENT (SECOND) OF TORTS § 552 cmt. h (AM. LAW INST. 1977).

⁴⁰¹ *Petrillo*, 655 A.2d at 1359, 1361.

⁴⁰² Donald W. Glazer & Arthur Norman Field, *No-litigation Opinions Can Be Risky Business*, 14 BUS. L. TODAY 37, 37 (2005).

a series of numbered paragraphs, the lawyer's legal opinions on issues that the recipient asked to be addressed.⁴⁰³ It is common for one of the paragraphs to address legal proceedings involving the company.⁴⁰⁴ That paragraph does not actually state a legal opinion; rather, it states the fact that the lawyer knows of no legal proceedings other than those that have been disclosed to the recipient.⁴⁰⁵ This confirmation or statement of fact in a closing opinion is often described as a "no-litigation opinion."⁴⁰⁶ It is with that background that we arrive at *Dean Foods Co. v. Pappathanasi*.⁴⁰⁷

Dean Foods arose out of the acquisition by Garelick Farms, Inc., a wholly-owned subsidiary of Dean Foods, of all of the outstanding stock of Scangas Bros. Holding, Inc. ("SBHI").⁴⁰⁸ For simplicity's sake, we'll refer to the acquiring company as Dean Foods. At the time of the acquisition, West Lynn Creamery, Inc. ("WLC") was a wholly-owned subsidiary of SBHI.⁴⁰⁹ The law firm of Rubin & Rudman had represented SBHI and WLC for several years and served as their counsel in connection with the Dean Foods deal, as well as the events that would give rise to this litigation.⁴¹⁰ Michael Altman, Gene Barton, and Charles Speleotis were the principal partners at Rubin & Rudman involved in SBHI's and WLC's representation at the time of the events at issue.⁴¹¹

In early October 1997, WLC received a federal grand jury subpoena concerning payments it made to Michael and Cathy Gavriel, who owned Dunkin' Donut franchises that were WLC customers.⁴¹² WLC hired Rubin & Rudman to represent it in regard to the subpoena.⁴¹³ Altman assumed responsibility for the representation and, two weeks later, delivered responsive documents to the Assistant United States Attorney leading the investigation, John Hodgens.⁴¹⁴ Hodgens informed Altman that the government considered WLC's response to the subpoena to be incomplete and thus expected a records custodian to appear before the grand jury. Accordingly, Altman interviewed various WLC employees, spoke with counsel representing other parties named in the subpoena, and advised Speleotis of the status of the matter.⁴¹⁵

In the course of his investigation, Altman learned that the government inquiry might involve tax evasion by parties other than WLC, facilitated by

⁴⁰³ *Id.*

⁴⁰⁴ *Id.*

⁴⁰⁵ *Id.*

⁴⁰⁶ *See id.* at 37, 41, 43 (discussing practical aspects of no-litigation opinions).

⁴⁰⁷ *Dean Foods Co. v. Pappathanasi*, No. Civ.A. 01-2595 BLS, 2004 WL 3019442 (Mass. Super. Ct. Dec. 3, 2004).

⁴⁰⁸ *Id.* at *1 n.1, *6.

⁴⁰⁹ *Id.* at *6.

⁴¹⁰ *Id.* at *1, *6.

⁴¹¹ *Id.* at *1.

⁴¹² *Id.*

⁴¹³ *Id.* at *2.

⁴¹⁴ *Id.*

⁴¹⁵ *Id.* at *2-5.

WLC's payment of "rebates" intended to ensure that other vendors did not place their dairy products in WLC's coolers in Dunkin' Donuts stores.⁴¹⁶ A WLC employee testified before the grand jury in late November 1997.⁴¹⁷ From Altman's perspective, however, the matter went dormant after early December 1997.⁴¹⁸ The government made no further document requests, no WLC employees were called to appear before the grand jury, and Altman had no further contact with Hodgens or lawyers for other parties.⁴¹⁹

Beginning in late 1997 and continuing into 1998, Dean Foods talked with the SBHI shareholders about a stock acquisition of SBHI and, indirectly, WLC.⁴²⁰ These discussions faltered at least once, in part as a result of internal dissension within the ranks of the putative sellers, all of whom were family members with a history of acrimony.⁴²¹ Ultimately, in June 1998, Dean Foods agreed to acquire all of the stock of SBHI (and thus WLC) pursuant to a stock purchase agreement with the SBHI shareholders.⁴²² The selling shareholders represented to Dean Foods in the agreement that:

Except as set forth in *Schedule 2.10* of the Company Disclosure Schedule, there is no claim, action, suit, litigation, proceeding, arbitration or investigation of any kind, at law or in equity (including actions or proceedings seeking injunctive relief), pending or, to the Company's knowledge, threatened against the Company or any of its subsidiaries, and neither the Company or any of its subsidiaries is subject to any continuing order of, consent decree, settlement agreement or other similar written agreement with, or continuing investigation by, any Governmental Entity, or any judgment, order, writ, injunction, decree or award of any Governmental Entity or arbitrator, including, without limitation, cease-and-desist or other orders.⁴²³

Prior to the execution of the stock purchase agreement, Barton and Speleotis met with Arthur Pappathanasi, an SBHI shareholder who represented the other selling shareholders in the transaction.⁴²⁴ They advised him that the prudent course would be to list the grand jury investigation as on-going litigation on Schedule 2.10 to the stock purchase agreement.⁴²⁵ Barton and Speleotis provided this advice even though Altman advised them in the meeting that he had heard nothing from Hodgens for six months and that based on other tax evasion cases he had handled, it was his "guesstimate" that the matter "had probably gone away."⁴²⁶ Pappathanasi declined to follow Barton's and Speleotis' advice,

⁴¹⁶ *Id.* at *2-4.

⁴¹⁷ *Id.* at *5.

⁴¹⁸ *Id.* at *6.

⁴¹⁹ *Id.* at *5-6.

⁴²⁰ *Id.* at *6.

⁴²¹ *Id.*

⁴²² *Id.*

⁴²³ *Id.* at *7.

⁴²⁴ *Id.* at *8.

⁴²⁵ *Id.*

⁴²⁶ *Id.*

because he feared that it would reignite dissension among the disagreeable family members who were the selling shareholders and interfere with the sale.⁴²⁷ Accordingly, Schedule 2.10, as delivered to Dean Foods, did not mention the grand jury investigation.⁴²⁸

The stock purchase agreement also required the SBHI shareholders to deliver an opinion letter to Dean Foods.⁴²⁹ Thus, as part of the closing of the sale on June 30, 1998, Rubin & Rudman delivered an opinion letter that included the following paragraph:

To our knowledge, except as set forth in *Schedule 2.10* of the Company Disclosure Schedule, there is no claim, action, suit, litigation, proceeding, arbitration or, [sic] investigation of any kind, at law or in equity (including actions or proceedings seeking injunctive relief), pending or threatened against the Company or any of its subsidiaries and neither the Company nor any of its subsidiaries is subject to any continuing . . . investigation by, any Governmental Entity . . .⁴³⁰

The closing opinion also stated that, while Rubin & Rudman had relied on the factual representations in the stock purchase agreement and had not conducted an independent investigation into any factual matters, “nothing ha[d] come to [its] attention which cause[d] [it] to doubt the accuracy” of the schedules to the stock purchase agreement.⁴³¹

In September 1998, following Dean Foods’ acquisition of SBHI’s stock and, indirectly, WLC, the federal investigation of WLC resurfaced with a vengeance.⁴³² In March 2001, WLC agreed to plead guilty to conspiracy to defraud the United States by impeding the IRS’s collection of taxes and paid a \$7.2 million fine.⁴³³ WLC also incurred \$2.1 million in defense costs.⁴³⁴ Dean Foods thereafter sued the selling shareholders and Rubin & Rudman in Massachusetts state court, alleging that it would not have agreed to buy WLC had it known of the grand jury investigation.⁴³⁵

Dean Foods settled with the SBHI shareholders on undisclosed terms, but its case against Rubin & Rudman went to a bench trial.⁴³⁶ Following that trial, the court issued a somewhat disjointed opinion in which it stated:

The Rubin and Rudman defendants did not conduct the inquiry that they were required to make by customary practice. The confirmation they gave, grounded as it was on errors of fact, created for the recipients the comfort that an ongoing

⁴²⁷ *Id.*

⁴²⁸ *Id.*

⁴²⁹ *Id.* at *7.

⁴³⁰ *Id.*

⁴³¹ *Id.*

⁴³² *Id.* at *10.

⁴³³ *Id.*

⁴³⁴ *Id.* at *11.

⁴³⁵ *Id.* at *10.

⁴³⁶ *Id.* at *11 n.6.

investigation did not exist *and* that nothing had come to the attention of Rubin and Rudman that cast doubt about the accuracy of that report.⁴³⁷

The court noted that even a modest inquiry by Altman in June 1998 would have revealed that the government investigation was ongoing.⁴³⁸ The court found that Rubin & Rudman committed negligent misrepresentation in giving the opinion on the basis of such inadequate investigation.⁴³⁹ The court further held that Dean Foods had a right to rely upon the flawed no-litigation opinion.⁴⁴⁰ Dean Foods unquestionably was among a limited group of people or entities for “whose benefit and guidance Rubin & Rudman” supplied the information in the closing opinion.⁴⁴¹ Rubin & Rudman intended for Dean Foods to rely on the opinion letter as the language of the letter made clear.⁴⁴² Furthermore, the opinion letter was a condition of the sale closing, it was delivered at the closing, and the deal closed.⁴⁴³ In the end, the court awarded Dean Foods damages of approximately \$9.3 million, which represented the sum of the fine assessed against WLC plus the costs that WLC incurred in defending the criminal case, all of which were ultimately borne by Dean Foods as a result of its acquisition of WLC.⁴⁴⁴

CONCLUSION

Few lawyers think themselves to be at risk for liability based on fraud or negligent misrepresentation arising out of clients’ representations. This perspective probably rests at least in part on common notions of litigation practice, where parties generally cannot base fraud or misrepresentation claims on opposing lawyers’ statements. But lawyers may be sued for fraud or negligent misrepresentation by adversaries in litigation in some cases, as where, for example, they knowingly misrepresent material facts in negotiations. Given the nature of transactional practice, business lawyers are natural targets of fraud and negligent misrepresentation claims by counter-parties based on alleged false statements and failures to disclose information. For that matter, clients may sue their own lawyers for alleged fraud in appropriate cases. In fact, fraud and misrepresentation are common theories of liability in suits against lawyers by both clients and third parties. The question then becomes what lawyers should do to mitigate the risk of related liability. Advice to be honest is a bromide.

Transactional lawyers should generally advocate to clients full disclosure whenever known facts are arguably responsive to other parties’ requests for in-

⁴³⁷ *Id.* at *19.

⁴³⁸ *Id.* at *17.

⁴³⁹ *Id.* at *12–20.

⁴⁴⁰ *Id.* at *12, 20.

⁴⁴¹ *Id.* at *19 (quoting RESTATEMENT (SECOND) OF TORTS § 552 (AM. LAW INST. 1977)).

⁴⁴² *Id.* (quoting the opinion letter).

⁴⁴³ *Id.*

⁴⁴⁴ *See id.* at *11, 20, 23 (identifying damage elements and entering judgment).

formation. This almost certainly is lawyers' duty under applicable rules of professional conduct,⁴⁴⁵ and regardless, it is invariably in clients' interests to do so. If a client resists disclosing a matter potentially material to a transaction when there is no principled basis to do so, a lawyer should try to persuade the client to change her mind. If that effort fails, the lawyer may need to consider withdrawing from the representation. Depending on the facts, a lawyer may wish to consider withdrawing from the representation even where the client has an understandable basis for its reticence, as Pappathanasi seemingly did in the *Dean Foods* case.

Transactional lawyers offering any sort of opinions should be careful to confine their opinions to the subjects specified by the client or third party.⁴⁴⁶ They should also consider qualifying opinions and statements to third parties in appropriate matters. Consider, for example, the prudence of the law firm in *Fortress Credit Corp. v. Dechert LLP*,⁴⁴⁷ which was alleged by lenders to have misrepresented in an opinion letter that "loan documents were duly executed and delivered and the loan was a valid and binding obligation" on a realty company and New York lawyer turned notorious fraudster Marc Dreier.⁴⁴⁸ Dreier supplied the documents and information to the law firm necessary for preparation of the opinion—all of which were forged or falsified.⁴⁴⁹ Beyond the fact that the firm had no reason to suspect that the documents Dreier provided as the basis for the opinion were illegitimate, the opinion the firm provided to the lenders "was clearly and unequivocally circumscribed by the qualifications that [the law firm] assumed the genuineness of all signatures and the authenticity of the documents, made no independent inquiry into the accuracy of the factual representations . . . and undertook no independent investigation in ascertaining those facts."⁴⁵⁰ Thus, and because the opinion letter by its terms only stated legal conclusions, the law firm's statements in the opinion letter were not actionable as misrepresentations.⁴⁵¹

Business lawyers may wish to consider limiting their potential liability to those who might rely on their opinions or representations in appropriate matters. Such limitations are generally permissible under rules of professional con-

⁴⁴⁵ See MODEL RULES OF PROF'L CONDUCT r. 1.4(a)(2) (AM. BAR ASS'N 2015) (obligating a lawyer to "reasonably consult with the client about the means by which the client's objectives are to be accomplished"); *Id.* r. 1.4(b) ("A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.").

⁴⁴⁶ See, e.g., *Mega Grp., Inc. v. Pechenik & Curro, P.C.*, 819 N.Y.S.2d 796, 800 (App. Div. 2006) (finding no misrepresentation where "the parties to the sale carefully circumscribed the details to be contained within the opinion letter" and there was no evidence "that the attorneys were called upon to venture opinions beyond those agreed upon").

⁴⁴⁷ *Fortress Credit Corp. v. Dechert LLP*, 934 N.Y.S.2d 119 (App. Div. 2011).

⁴⁴⁸ *Id.* at 121.

⁴⁴⁹ *Id.*

⁴⁵⁰ *Id.* at 122.

⁴⁵¹ *Id.* (citing *Prudential Ins. Co. of Am. v. Dewey, Ballantine, Bushby, Palmer & Wood*, 605 N.E.2d 318, 322–23 (N.Y. 1992)).

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duct,⁴⁵² although commercial realities frequently prevent lawyers from seeking such protections.

For trial lawyers, the threat of liability to third parties for negligent misrepresentation or fraud is greatest when requested to disclose the existence or amount of liability insurance potentially available to satisfy a judgment or to fund a potential settlement. Lawyers cannot knowingly misrepresent either the existence or amount of insurance coverage.⁴⁵³ If they do not want to reveal either the existence or amount of insurance coverage for some strategic reason, they should simply decline to do so. If they are uncertain about the existence or amount of insurance coverage when asked about the subject and they are either required to reveal the information or wish to do so, they should obtain the necessary confirmations before making related commitments or statements.

In summary, all lawyers, regardless of practice area, must appreciate that they are potential targets of fraud and misrepresentation claims by clients and third parties. The need for care in lawyers' communications is constant.

⁴⁵² See MODEL RULES OF PROF'L CONDUCT r. 1.8(h)(1) (AM. BAR ASS'N 2015) (governing lawyers' ability to prospectively limit their malpractice liability to clients and, by implication, permitting them to limit their liability to non-clients).

⁴⁵³ See, e.g., *Fire Ins. Exch. v. Bell*, 643 N.E.2d 310, 311–13 (Ind. 1994) (concluding that a defense lawyer was potentially liable for fraud for misrepresenting to a plaintiff's lawyer the amount of insurance coverage applicable to a loss).

