A Historical Approach to Negligent Misrepresentation and Federal Rule of Civil Procedure 9(b)

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INTRODUCTION

Imagine two investors in Houston invest separately in a publicly traded art gallery in New York City. Each reaches an agreement to buy preferred stock and the gallery offers each a painting to sweeten the deal. Shortly after both deals close, a prominent art critic discovers that approximately 50 percent of the gallery's art collection is inauthentic. This includes the paintings that the company gave to the investors. When the gallery acquired the art it had negligently assumed that the pieces were genuine. As a result, the value of the preferred stock tumbles and the paintings become worthless.

In order to recoup their money, the investors sue the gallery for negligent misrepresentation. Both investors file their claims in federal court—the first in the Southern District of New York and the second in the Southern District of Texas. For the paintings, both investors plead under state law. For the preferred stock, each uses state law and the Securities Act of 1933[1] ("Securities Act"), the latter of which creates a cause of action if a person provides false information in a securities transaction.[2] For each claim the investors provide the minimal amount of specificity required under the federal pleading standard—Federal Rule of Civil Procedure (FRCP) 8(a)—which requires "a short and plain statement . . . showing that the pleader is entitled to relief."[3] The gallery moves to dismiss all claims.

Although the complaints contain the same allegations, the district courts reach different results. The Southern District of New York throws out the state-law claims regarding the painting and the stock, but allows the Securities Act claim to proceed.

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1 Pub L No 73-22, ch 38, 48 Stat 74, codified as amended at 15 USC § 77a et seq.

2 See 15 USC § 77l(a)(2).

3 FRCP 8(a)(2).

While this may seem like an absurd result, the court is following Second Circuit precedent. The Second Circuit classifies state-law negligent misrepresentation as a type of fraud claim.[4] As such, the two state-law claims fall under a heightened pleading standard—FRCP 9(b)—which requires that parties plead "fraud or mistake" with particularity.[5] The pleadings contain enough detail to satisfy the minimal requirements of Rule 8(a), but not enough detail to satisfy the more stringent Rule 9(b) requirements applicable to state-law claims. Meanwhile, the Securities Act claim, which contains the same elements as state-law negligent misrepresentation,[6] is not considered fraud under Second Circuit precedent.[7] Consequently, Rule 9(b) does not apply, and the claim survives under the more lenient Rule 8(a).

By contrast, the Southern District of Texas allows all three claims to proceed. Under Fifth Circuit precedent, negligent misrepresentation claims are not fraud, whether pleaded under state law[8] or the Securities Act.[9] Therefore, Rule 8(a)—not Rule 9(b)—applies.

Same claims. Same facts. Different results.

The law surrounding Federal Rule of Civil Procedure 9(b) and negligent misrepresentation is convoluted. Under Rule 9(b), a party who sues for fraud or mistake—or who uses fraud or mistake as a defense—must give a detailed account of the claim.[10] Currently, courts disagree about whether Rule 9(b)

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[4] See *Aetna Casualty and Surety Co v Aniero Concrete Co*, 404 F3d 566, 583 (2d Cir 2005).

[5] FRCP 9(b).

[6] Compare *J.A.O. Acquisition Corp v Stavitsky*, 8 NY3d 144, 148 (NY 2007) (A claim for negligent misrepresentation requires the plaintiff to demonstrate (1) the existence of a special or privity-like relationship imposing a duty on the defendant to impart correct information to the plaintiff, (2) that the information was incorrect, and (3) reasonable reliance on the information), with *Melder v Morris*, 27 F3d 1097, 1100 (5th Cir 1994) (listing the elements of a violation of the Securities Act as "(1) a misstatement or omission (2) of a material fact (3) made with scienter"—negligence in the case of negligent misrepresentation—"(4) on which the plaintiff relied (5) that proximately caused the plaintiff's injury").

[7] See *Rombach v Chang*, 355 F3d 164, 171 (2d Cir 2004) ("[W]hile a plaintiff need allege no more than negligence to proceed under Section 11 [of the Securities Act] . . . , claims that do rely upon averments of fraud are subject to the test of Rule 9(b).").

[8] See *General Electric Capital Corp v Posey*, 415 F3d 391, 394 (5th Cir 2005) (holding that state-law negligent misrepresentation is not a fraud claim and therefore not subject to Rule 9(b)).

[9] See *Melder*, 27 F3d at 1100 n 6 (holding that 9(b) applies when "Securities Act claims are grounded in fraud rather than negligence").

[10] FRCP 9(b) ("In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake.").

applies when a party sues for negligent misrepresentation—a fraud-like tort that holds parties liable for careless misstatements.[11] Some federal circuit courts hold that negligent misrepresentation constitutes fraud for the purposes of the Rule.[12] Other circuits determine that Rule 9(b) does not apply.[13] A third group of circuits looks to state law to determine whether negligent misrepresentation is fraud.[14] Compounding the confusion, some courts find that negligent misrepresentation is fraud if the party uses state law to file the claim,[15] but not fraud if the party uses the Securities Act of 1933[16]—a federal statute concerning the registration and sale of securities. This inconsistency can lead to absurd results.

The inconsistent approaches described above create two principal issues. First, the circuit split creates incentives for forum shopping. Plaintiffs will file negligent misrepresentation claims in federal courts with the most lenient pleading standards. Forum shopping between federal courts to gain better treatment under the Federal Rules undermines "the goal of uniformity of federal procedure."[17] If a favorable federal court is not available, a plaintiff will file in a lenient state court. The Supreme Court has discouraged state-federal forum shopping because of concerns of equal treatment and legal reciprocity.[18] Defendants will also forum shop by attempting to remove the claim to a court in which the standard may be higher, which raises the same concerns.

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[11] See, for example, *Dallas Aerospace, Inc v CIS Air Corp*, 352 F3d 775, 788 (2d Cir 2003) (listing "carelessness in imparting words" as an element of negligent misrepresentation).

[12] See, for example, *North American Catholic Educational Programming Foundation, Inc v Cardinale*, 567 F3d 8, 15 (1st Cir 2009) (holding that a core allegation of fraud in a complaint will incorporate negligent misrepresentation under Rule 9(b)).

[13] See, for example, *Tricontinental Industries, Ltd v PricewaterhouseCoopers, LLP*, 475 F3d 824, 833 (7th Cir 2007) (holding that negligent misrepresentation "is *not* governed by . . . Rule 9(b)").

[14] See, for example, *Trooien v Mansour*, 608 F3d 1020, 1028 (8th Cir 2010).

[15] See, for example, *Aetna Casualty and Surety*, 404 F3d at 583 (stating that negligent misrepresentation "must be pled in accordance with the specificity criteria of Rule 9(b)").

[16] See, for example, *Rombach*, 355 F3d at 171.

[17] *Hanna v Plumer*, 380 US 460, 463 (1965) (stating that the Court granted certiorari "[b]ecause of the threat to the goal of uniformity of federal procedure").

[18] See id at 468 (stating that one of *Erie*'s "twin aims" was to prevent state-federal forum shopping); Note, *Forum Shopping Reconsidered*, 103 Harv L Rev 1677, 1682 (1990) ("[T]he Supreme Court denounces state-federal forum shopping on grounds of comity and parity.").

Second, the difference between how courts treat state-law and Securities Act claims creates an unnecessary trap for plaintiffs. Parties who understand the issue will simply file under both state law and the Securities Act. It is unclear, however, who is aware of the discrepancy. No court or law review article has addressed the differential treatment.

Despite the different approaches adopted by the circuits and the potential for inconsistent and absurd results, the Supreme Court has not resolved the issue. This Comment examines the circuit split and the tension between state-law negligent misrepresentation and the Securities Act in order to demonstrate that Rule 9(b) should not apply to negligent misrepresentation. Part I provides relevant background on Rule 9(b), state-law negligent misrepresentation, and the Securities Act. The development of these three areas of law provides important insights into the relationship between negligent misrepresentation and Rule 9(b). Part II traces how courts have applied Rule 9(b) with respect to negligent misrepresentation under state law and the Securities Act. This Part also outlines the circuit split in more detail and highlights the differences between courts' treatment of state-law negligent misrepresentation and Securities Act negligence.

Part III advocates for a unified approach to adjudicating negligent misrepresentation claims under both state law and the Securities Act. In short, Part III concludes, based on a historical analysis of Rule 9(b), that federal courts should not apply the Rule to negligent misrepresentation. Fraud, mistake, and negligent misrepresentation were separate causes of action when Rule 9(b) was adopted in 1938. Since the text of Rule 9(b) limits its scope to claims of fraud and mistake—and since negligent misrepresentation was not included in the definition of either fraud or mistake in 1938—Rule 9(b) should be interpreted according to its terms and should not be applied to negligent misrepresentation claims.

I. BACKGROUND

Whether Rule 9(b) applies to negligent misrepresentation depends on the interpretation of three different bodies of law: Rule 9(b), state-law negligent misrepresentation, and the Securities Act of 1933. This Part examines the history and current state of each of these areas of law with an emphasis on how they relate to one another.

A. Federal Rule of Civil Procedure 9(b)

All complaints filed in federal court must comply with FRCP 8(a), which requires "a short and plain statement . . . showing that the pleader is entitled to relief."[19] For allegations of "fraud or mistake" a party must also meet the heightened requirements of Rule 9(b), which requires that the party describe "the circumstances" of the claim "with particularity."[20]

The particularity requirement in Rule 9(b) has its roots in the English common law. In England, pleading was an oral tradition until sometime between the fifteenth and sixteenth centuries.[21] As pleadings moved to written form, specialized pleading standards emerged.[22] These pleading standards migrated to the United States by way of reception statutes—laws passed by states adopting the English common law.[23]

"Prior to the merger of law and equity, fraud and mistake were [traditionally] grounds for equity jurisdiction."[24] A party who wanted to raise a fraud or mistake defense in a legal dispute had to file a separate action in equity to enjoin the enforcement of the legal judgment.[25] When raised as a defense in equity, a party had to plead fraud and mistake with particularity.[26]

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19 FRCP 8(a)(2).

20 FRCP 9(b). See also *Ashcroft v Iqbal*, 556 US 662, 686–87 (2009) (stating that FRCP 9(b) does not allow the plaintiff to evade the "less rigid—though still operative—strictures of Rule 8").

21 See Christopher M. Fairman, *An Invitation to the Rulemakers—Strike Rule 9(b)*, 38 UC Davis L Rev 281, 283 (2004) ("Pleadings began as an oral tradition in the English common law courts and were reduced to writing sometime between the fifteenth and sixteenth centuries.").

22 See id ("This transformation from oral to written pleadings brought with it an increased emphasis on form.").

23 See, for example, NY Const of 1777 Art XXXV (superseded 1821), reprinted in Francis Newton Thorpe, 5 *The Federal and State Constitutions, Colonial Charters, and Other Organic Laws of the States, Territories, and Colonies Now or Heretofore Forming the United States of America* 2623, 2635 (GPO 1909):

> And this convention doth further, in the name and by the authority of the good people of this State, ordain, determine, and declare that such parts of the common law of England, and of the statute law of England and Great Britain, and of the acts of the legislature of the colony of New York, as together did form the law of the said colony.

24 Fairman, 38 UC Davis L Rev at 284 (cited in note 21).

25 See id. See also William M. Richman, Donald E. Lively, and Patricia Mell, *The Pleading of Fraud: Rhymes without Reason*, 60 S Cal L Rev 959, 966 (1987).

26 See Joseph Story, *Commentaries on Equity Pleadings* § 251 at 297 (Little, Brown 5th ed 1852) (Edmund H. Bennett, ed).

In the United States, the Field Code replaced these common law pleading requirements.[27] The status of the particularity requirement under the Field Code is uncertain. The inaugural Field Code of 1848[28] did not require parties to plead fraud and mistake with particularity.[29] Some cases interpreting those rules, however, contain some of the first references to a particularity requirement in legal—as opposed to equitable—proceedings. In the 1850 case *McMurray & Thomas v Gifford*,[30] a New York court cited to § 149 of the Field Code and stated that pleading fraud as an affirmative defense in a legal action "requires a general or specific denial."[31]

The treatises at that time also demonstrate the uncertainty regarding the pleading requirement in that they treat the particularity requirement inconsistently. Judge Joseph Story's 1852 treatise *Commentaries on Equity Pleadings* states that fraud must be pleaded with particularity to enjoin a legal judgment in equity court.[32] However, two other treatises—James Gould's *Principles of Pleading*[33] and Joseph Chitty's *A Treatise on Pleading*[34]—do not mention a particularity requirement for fraud.[35]

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27 See Fairman, 38 UC Davis L Rev at 284 (cited in note 21) (noting that the Field Code replaced common law pleading in the mid-nineteenth century). The Field Code was adopted at the request of the New York legislature. See Stephen N. Subrin, *David Dudley Field and the Field Code: A Historical Analysis of an Earlier Procedural Vision*, 6 L & Hist Rev 311, 316 (1988). David Dudley Field was the most influential member of the commission that compiled the Code. Id at 317. By the turn of the century, twenty-four states had adopted all or part of the Code. See Lawrence M. Friedman, *A History of American Law* 394 (Simon & Schuster 2d ed 1985) (listing the states that had adopted the Field Code by 1900).

28 An Act to Simplify and Abridge the Practice, Pleadings and Proceedings of the Courts of This State, 1848 NY Laws 497.

29 See Fairman, 38 UC Davis L Rev at 284 (cited in note 21).

30 5 How Pr 14 (NY Sup Ct 1850). See also *Anson v Dwight*, 18 Iowa 241, 242 (1865).

31 *McMurray*, 5 How Pr at 15.

32 Story, *Commentaries on Equity Pleadings* § 251 at 297 (cited in note 26) (stating that when fraud is raised to enjoin a legal proceeding it must be pleaded with particularity).

33 James Gould, *A Treatise on the Principles of Pleading, in Civil Actions* (B. and S. Collins 2d ed 1836).

34 Joseph Chitty, 1 *A Treatise on Pleading, and Parties to Actions* (Merriam 14th American ed 1867) (J.C. Perkins, ed).

35 See Gould, *Principles of Pleading, in Civil Actions* at 51 (cited in note 33) ("All facts alleged in good pleading, consist either, 1, of the *gist* or *substance* of the complaint, or defence—or, 2, of matter of *inducement* . . . or, 3, of matter of *aggravation*. Whatever else is stated, in any part of the pleadings, is but *surplusage*."); Chitty, 1 *Treatise on Pleading* at 136–37, 581–82 (cited in note 34) (describing causes of action for fraudulent representations made to induce a contract, and noting a defendant pleading fraud as a defense can claim that it would be unnecessary to state the particulars of the fraud).

Chitty even explicitly states that fraud *should* be pleaded generally.[36] This is especially significant because Chitty also points out that other actions, such as slander, should be pleaded with particularity.[37] Even up until 1890 the particularity requirement was still "not clearly established."[38]

By 1920 the tide changed, and the particularity requirement for fraud took hold.[39] The Model Rules of Civil Procedure, published in 1919, referenced a particularity requirement.[40] Additionally, treatises from the 1920s indicate that fraud must be pleaded with particularity.[41]

Scholars have speculated as to why the particularity requirement gained strength in the 1920s. Several commentators believe that as law and equity merged, "courts simply applied the particularity requirement of the equitable defense of fraud to common law tort actions for fraud because the word 'fraud' was present in both pleadings."[42] But this explanation does not completely explain particularity's reemergence. The Field Code was largely responsible for the merger of law and equity.[43] By 1900, the Field Code was widely adopted,[44] while a particularity requirement had not yet been "clearly established."[45] So if merger were the catalyst, one would have expected to see the change closer to 1900.

Regardless of why the particularity requirement gained traction, it was eventually codified in Rule 9(b). The Rule appeared in the original draft of the Federal Rules of Civil Procedure in 1936 and has since remained unchanged.[46]

The history of Rule 9(b), however, is sparse.[47] The congressional and American Bar Association (ABA) hearings do not mention the Rule, and the Advisory Committee Note only refers

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36 Chitty, 1 *Treatise on Pleading* at 388, 536, 582 (cited in note 34) (addressing the pleading of fraud in several different circumstances).

37 Id at 536.

38 Richman, Lively, and Mell, 60 S Cal L Rev at 967 (cited in note 25).

39 See id; Fairman, 38 UC Davis L Rev at 285 (cited in note 21).

40 *Rules of Civil Procedure: Supplementary to the State-Wide Judicature Act (Bulletin VII-A) of the American Judicature Society*, 14 Am Judicature Socy 1, 62–63 (1919).

41 See Benjamin J. Shipman, *Handbook of Common-Law Pleading* 497–99 (West 3d ed 1923) (Henry Winthrop Ballantine, ed).

42 Fairman, 38 UC Davis L Rev at 285 (cited in note 21).

43 See *J. Aron and Company, Inc v Service Transportation Co*, 515 F Supp 428, 443 (D Md 1981).

44 See note 27 and accompanying text.

45 Richman, Lively, and Mell, 60 S Cal L Rev at 967 (cited in note 25).

46 See id at 965.

47 Fairman, 38 UC Davis L Rev at 286 (cited in note 21).

to the "English Rules Under the Judicature Act (The Annual Practice, 1937) O. 19, r 22."[48] The English Rule does not concern the particularity requirement in Rule 9(b), but rather Rule 9(b)'s second clause, which states that malice and intent can be pleaded generally.[49] However, the Annual Practice—an English treatise on procedure—states that "[f]raud must be distinctly alleged and proved."[50] In short, the ABA hearings and the Advisory Committee Note provide little information on how fraud and mistake should be interpreted in Rule 9(b), leaving courts with little guidance on how to apply the Rule to fraud-like torts.

Practically speaking, courts have held that Rule 9(b) requires that plaintiffs: "(1) point to a particular allegedly fraudulent statement; (2) identify who made the statement; (3) plead when and where the statement was made; and (4) explain what made the statement fraudulent."[51] A plaintiff pleading fraud must meet both this standard and the pleading standard under Rule 8.[52]

The difference between Rule 9(b) and Rule 8(a) has recently narrowed. In *Bell Atlantic Corp v Twombly*,[53] the Supreme Court raised Rule 8(a)'s pleading standard.[54] Prior to *Twombly*, federal courts only dismissed a complaint for failing to meet the pleading standard under Rule 8(a) if "it appear[ed] beyond doubt that the plaintiff [could] prove no set of facts in support of his claim."[55] *Twombly* replaced this low bar with a plausibility test.[56]

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48 FRCP 9(b), Advisory Committee Notes to the 1937 Adoption (referencing the "English Rules Under the Judicature Act" without elaboration). See also W. Valentine Ball, R.F. Burnand, and F.C. Watmough, eds, *The Annual Practice, 1937* O 19, r 22 at 369 (Sweet and Maxwell, Stevens and Sons 1937) (providing that "[f]raud must be distinctly alleged and proved" and that malice and fraudulent intent can be alleged "as a fact without setting out the circumstances from which the same is to be inferred").

49 See Fairman, 38 UC Davis L Rev at 287 (cited in note 21).

50 Ball, Burnand, and Watmough, eds, *The Annual Practice, 1937* O 19, r 22 at 369 (cited in note 48) ("Fraud must be distinctly alleged and proved. The acts alleged to be fraudulent must be stated, otherwise no evidence in support of them will be received.").

51 *Republic Bank & Trust Co v Bear Stearns & Company, Inc*, 683 F3d 239, 253 (6th Cir 2012). See also *In re GlenFed, Inc Securities Litigation*, 42 F3d 1541, 1548 (9th Cir 1994) ("[P]laintiff must include statements regarding the time, place, and nature of the alleged fraudulent activities.") (emphasis omitted).

52 See *Iqbal*, 556 US at 686–87.

53 550 US 544 (2007).

54 Id at 556. But see Bradley Scott Shannon, *I Have Federal Pleading All Figured Out*, 61 Case W Res L Rev 453, 481–82 (2010) (arguing that *Twombly* and *Iqbal* did not significantly alter federal pleading standards, but rather clarified plaintiffs' obligations and increased use of motions to dismiss).

55 *Conley v Gibson*, 355 US 41, 45–46 (1957).

56 *Twombly*, 550 US at 556.

In order to plead a viable claim under Rule 8(a) a plaintiff now must provide "enough factual matter" to raise the right to relief above the speculative level.[57]

This change, however, has not made Rule 9(b) irrelevant. Courts still distinguish between the two standards.[58] In fact, whether Rule 9(b) applies is outcome determinative in many cases.[59] Consequently, clarifying the scope of Rule 9(b) would have a significant effect on parties filing fraud-like suits such as negligent misrepresentation.

B. State-Law Negligent Misrepresentation

Like Rule 9(b), negligent misrepresentation also has its roots in the common law. Negligent misrepresentation derives from the English tort of intentional misrepresentation—otherwise known as deceit.[60] Intentional misrepresentation required that (1) the defendant intentionally misrepresented a fact, (2) the defendant intended that the plaintiff rely on the fact, and (3) the plaintiff relied on the fact and was injured as a result.[61] English law denied liability for negligent misstatements absent a "fiduciary relation between the parties."[62] Deceit

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57 Id.

58 See *Iqbal*, 556 US at 686–87 (calling Rule 8(a) a "less rigid" standard than Rule 9(b)).

59 See, for example, *In re NationsMart Corp Securities Litigation*, 130 F3d 309, 315 (8th Cir 1997) (stating that because the plaintiffs made clear in their complaint that they did not allege fraud, Rule 9(b) should not have applied and their claim "should not have been dismissed"); *Republic Bank & Trust Co*, 683 F3d at 253 ("The claim may not proceed because Republic's complaint does not pass muster under Rule 9(b).").

60 See Philip Steven Horne, Note, Onita Pacific Corp. v. Trustees of Bronson*: The Oregon Supreme Court Recognizes the Negligent Misrepresentation Tort*, 72 Or L Rev 753, 756 (1993). The English tort of deceit contains the same basic elements as modern-day fraud. In many jurisdictions, deceit and fraud are synonymous. See, for example, *Shinkle, Wilson & Kreis Co v Birney & Seymour*, 67 NE 715, 716 (Ohio 1903) ("[T]he terms 'fraud,' 'fraudulent concealment,' 'constructive fraud,' and 'deceit' are synonymous."). Some states, however, distinguish deceit and fraud based on whether parties contracted with one another. See *Delzer v United Bank of Bismarck*, 527 NW2d 650, 656 n 4 (ND 1995) ("A promise made without any intention of performing it, can constitute either deceit if there is no contract between the parties, or fraud if there is a contract and one party's apparent consent to the contract is obtained as a result of that promise.").

61 See *Derry v Peek*, 14 App Cas 337, 360–61 (HL 1889) (Herschell) (holding that an action could not be maintained against a defendant who maintained an honest belief that his statements were true, even though that belief was unreasonable); Horne, Note, 72 Or L Rev at 756 (cited in note 60).

62 William L. Prosser, *Misrepresentation and Third Persons*, 19 Vand L Rev 231, 234 (1966) ("After *Derry v. Peek* the English courts drew the unfortunate conclusion that, at least in the absence of some fiduciary relation between the parties, there was no

actions changed in 1922. In an opinion written by Judge Benjamin N. Cardozo, the New York Court of Appeals recognized a cause of action where the defendant negligently misrepresented a fact, despite a lack of fiduciary duty.[63] In the opinion, Judge Cardozo separated negligent misrepresentation from deceit by basing the new tort in negligence law.[64] Although other courts had recognized negligent misrepresentation at an earlier date,[65] Judge Cardozo's opinion is considered the point at which the tort gained traction.[66]

Courts gradually adopted the new tort, and in 1938 negligent misrepresentation was included in the Restatement (First) of Torts.[67] This date is significant because it is the same year as the adoption of Rule 9(b) in the first draft of the Federal Rules of Civil Procedure. The interplay between these two events is highly relevant to whether the words "fraud" and "mistake" in Rule 9(b) include negligent misrepresentation. Part III of this Comment argues that because negligent misrepresentation was not included in the definition of fraud in 1938—as the Restatement suggests—it should also not be included in the definition of fraud in Rule 9(b), which was enacted the same year.

Today fraud and negligent misrepresentation are similar claims. Both require that: (1) the defendant made a false statement, (2) the defendant intended to induce the plaintiff to act, (3) the plaintiff reasonably relied on the defendant's statement, and (4) the plaintiff suffered damages due to the reliance.[68] The only difference between fraud and negligent misrepresentation

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remedy for merely negligent misrepresentation, honestly believed, where the harm that resulted to the plaintiff was only pecuniary loss.").

63 *Glanzer v Shepard*, 135 NE 275, 276 (NY 1922) (holding the defendants liable for their "careless words"). See also Horne, Note, 72 Or L Rev at 756 (cited in note 60) (noting that *Glanzer* modified deceit under English law by recognizing a cause of action for negligently-made representations).

64 *Glanzer*, 135 NE at 276.

65 See, for example, *Cunningham v C. R. Pease House Furnishing Co*, 69 A 120, 121 (NH 1908) (holding that a person can be held liable for a "false statement honestly believed to be true, though negligently made").

66 See Horne, Note, 72 Or L Rev at 756 (cited in note 60) (stating that Cardozo's opinion "proved influential" and that it "propelled the new tort to widespread acceptance").

67 Restatement (First) of Torts § 552 (1938) (creating liability for negligently supplied information when the defendant "fails to exercise that care and competence in obtaining and communicating the information which its recipient is justified in expecting"). See also Horne, Note, 72 Or L Rev at 756 (cited in note 60).

68 See W. Page Keeton, *Prosser and Keeton on the Law of Torts* § 105 at 728 (West 5th ed 1984); Restatement (Second) of Torts § 552 (1977).

is scienter. Fraud requires either knowledge or severe recklessness,[69] while negligent misrepresentation requires only that the defendant acted negligently "in obtaining or communicating the information."[70] With the exception of a few states,[71] negligent misrepresentation is widely recognized across the United States.[72] Resolving the tort's relationship with Rule 9(b) will affect numerous suits going forward.

C. The Securities Act of 1933

Five years before the passage of Rule 9(b) and the publication of the Restatement (First) of Torts, Congress passed the Securities Act of 1933. The history of the Securities Act is intertwined with the rise of securities markets in the United States. In the late nineteenth century there was a surge in private investment due to the growth of several large industries and a rise in middle-class wealth.[73] The sale of speculative securities accompanied this investment boom.[74] Promoters aggressively sold high-risk investments "with tales of earth-shaking inventions, new projects, and vast wealth."[75]

As a result of public anxiety regarding fraudulent securities, states began passing "blue sky laws" to regulate the issuance and sale of securities.[76] Several states required that an administrative agency review securities for their "'merit' or intrinsic worth."[77] Other states imposed disclosure and licensing requirements on those wishing to sell securities in the state.[78] These

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69 See Keeton, *Prosser and Keeton on the Law of Torts* § 105 at 728 (cited in note 68).

70 Restatement (Second) of Torts § 552 (1977).

71 See, for example, *South County, Inc v First Western Loan Co*, 871 SW2d 325, 326 (Ark 1994).

72 See Restatement (Second) of Torts § 552 (2012 Appendix) (demonstrating that almost every state court has cited to § 552 since 1998).

73 See Jonathan R. Macey and Geoffrey P. Miller, *Origin of the Blue Sky Laws*, 70 Tex L Rev 347, 353–55 (1991) (stating that large industries such as the railroads and heavy manufacturing grew rapidly while private wealth skyrocketed); R.C. Michie, *The London and New York Stock Exchanges, 1850–1914* 224 (Allen & Unwin 1987) (stating that between 1897 and 1913 national savings quadrupled, growing from $790 million to $3.69 billion per annum).

74 See Macey and Miller, 70 Tex L Rev at 353 (cited in note 73).

75 Id at 355. See also Euphemia Holden, *The Delusion of Sudden Riches: Its Phenomena and Its Cure*, 83 Bankers Mag 186, 188–89 (1911) (describing the colorful nature by which speculative securities were sold to prospective investors).

76 See Macey and Miller, 70 Tex L Rev at 359–61 (cited in note 73).

77 Id at 349.

78 Id at 349, 378–80.

laws were the principal check on securities transactions in the United States until the 1930s.

The stock market crash of 1929 was the catalyst for federalizing securities regulation, as many perceived the crash to be at least partly the result of inadequacies in the state-law regimes.[79] This led Congress to pass a series of securities laws[80] to fill the gap, starting with the Securities Act of 1933.[81] The Securities Act established a registration and disclosure process.[82]

The Act enforces these requirements through criminal and civil liability. Sections 11 and 12 cover the civil liability. Section 11 creates a cause of action for misleading registration statements.[83] If a registration statement contains "an untrue statement of a material fact or [omits] . . . a material fact," a party who buys the security can sue those involved in filing the statement.[84] Section 11 contains a list of who specifically can be held liable.[85] Section 12 creates a cause of action for any "untrue statement of material fact" or material omission made during the sale of a security.[86] "Any person" who uses a misleading statement or omission to sell a security can be held liable to the purchasing party under § 12.[87] "In general terms, all securities fraud claims require the plaintiff to establish: (1) a misstatement or omission (2) of a material fact (3) made with scienter (4)

79 See Steven M. Axler, Comment, *The Blue Sky Laws of Louisiana*, 41 Loyola L Rev 1, 2 (1995) (stating that "[d]espite widespread enactment" of the blue sky laws, "the stock market crash of 1929 revealed the inadequacies of these statutes in combating schemes involving interstate commerce").

80 Following the Securities Act of 1933, Congress passed the Securities Exchange Act of 1934, Pub L No 73-291, ch 404, 48 Stat 881, codified as amended at 15 USC § 78a et seq, which sought "to reduce speculation through the control of credit and margins, and to provide a fair market, free from artificial manipulation and reflecting the informed judgment of actual investors." Note, *Federal Regulation of Securities: Some Problems of Civil Liability*, 48 Harv L Rev 107, 108 (1934).

81 See Macey and Miller, 70 Tex L Rev at 348 (cited in note 73) (stating that "[o]nly with the Securities Act of 1933 . . . did federal regulation begin" to address securities transactions "to any significant extent").

82 Securities Act of 1933 § 5(a), 15 USC § 77e(a) (stating that it is unlawful to sell an unregistered security); Securities Act of 1933 § 5(b), 15 USC § 77e(c) (requiring the filing of a registration statement); Securities Act of 1933 § 7, 15 USC § 77g (outlining what information the registration statement requires).

83 Securities Act of 1933 § 11(a), 15 USC § 77k(a).

84 Securities Act of 1933 § 11(a), 15 USC § 77k(a).

85 Securities Act of 1933 § 11(a), 15 USC § 77k(a).

86 Securities Act of 1933 § 12, 15 USC § 77l(a)(2).

87 Securities Act of 1933 § 12, 15 USC § 77l(a).

on which the plaintiff relied (5) that proximately caused the plaintiff's injury."[88]

The scienter requirement under §§ 11 and 12 is unclear. Both sections mention a reasonableness standard,[89] although some courts have found that strict liability applies.[90] Despite the disagreement, all courts agree that a party can be held liable for negligence under §§ 11 and 12.[91] By 1937 courts had started holding parties liable under § 11 if the parties did not use "reasonable care to assure the accuracy" of its statements.[92] This created a cause of action that has the same elements as state-law negligent misrepresentation.[93]

Rule 9(b), state-law negligent misrepresentation, and negligent misrepresentation under the Securities Act all emerged during the late 1930s. Rule 9(b) and state-law negligent misrepresentation arrived via the common law, while the Securities Act was a product of the stock market crash before the Great Depression. Part III uses the convergence of these events as a reference point to argue that Rule 9(b) should not apply to negligent misrepresentation.

II. RULE 9(B) AND NEGLIGENT MISREPRESENTATION

Even before Rule 9(b) was enacted in 1938, courts struggled to determine whether negligent misrepresentation should be pleaded with particularity.[94] This difficulty has continued through today. Negligent misrepresentation claims come before federal courts through both state law and federal statutes such as the Securities Act. A state-law claim contains the same

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88 *Melder v Morris*, 27 F3d 1097, 1100 (5th Cir 1994).

89 See Securities Act of 1933 § 11(b)(3), 15 USC § 77k(b)(3) (exempting from liability individuals who, after "reasonable investigation," had "reasonable ground to believe and did believe" that the statements "were true"); Securities Act of 1933 § 12, 15 USC § 77l(a)(2) (providing a defense to liability if a person selling a security proves that "he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission").

90 See *In re Lehman Brothers Securities and ERISA Litigation*, 799 F Supp 2d 258, 308 (SDNY 2011) ("Sections 11 and 12 . . . impose strict liability on certain enumerated categories of parties for material misstatements or omissions.").

91 See *NationsMart*, 130 F3d at 315 (stating that negligent misrepresentation is "at the heart of a § 11 claim").

92 *Martin v Hull*, 92 F2d 208, 210 (DC Cir 1937).

93 See note 6.

94 See, for example, *Ohio-West Virginia Co v Chesapeake & O Ry Co*, 124 SE 587, 588 (W Va 1924) (holding that parties do not need to plead negligent misrepresentation with specificity).

elements as a Securities Act claim.[95] The only difference is that state-law negligent misrepresentation covers all types of misrepresentation, while §§ 11 and 12 only regulate misinformation regarding a security.[96] Despite the similarities, federal courts have treated state-law claims and Securities Act claims differently. The following Sections survey how circuit courts and district courts have ruled on whether Rule 9(b) applies to negligent misrepresentation under state law and the Securities Act.

A. Rule 9(b) and State-Law Negligent Misrepresentation

The controversy concerning Rule 9(b) and negligent misrepresentation principally concerns federal courts. Although some states model their procedural rules on the Federal Rules,[97] there is not an explicit "goal" of interstate procedural "uniformity."[98] The Federal Rules of Civil Procedure, on the other hand, are supposed to apply uniformly in all federal courts.[99] Therefore, although clarifying the relationship between Rule 9(b) and negligent misrepresentation will affect some state versions of Rule 9(b),[100] the principal effect will come to federal courts nationwide.

Federal courts take three approaches with respect to Rule 9(b) and state-law negligent misrepresentation. The First and Second Circuits apply Rule 9(b).[101] The Fifth and Seventh Circuits do not.[102] The Eighth Circuit does not take a categorical approach, but rather looks to state law to determine whether

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95 See note 6.

96 See Securities Act of 1933 § 11(a), 15 USC § 77k(a); Securities Act of 1933 § 12, 15 USC § 77l(a)(2).

97 See, for example, Utah R Civ P 6, Advisory Committee Note (stating that the 2000 amendment was made to conform with FRCP 6 and recent case law interpreting that rule).

98 *Hanna v Plumer*, 380 US 460, 463 (1965) (stating that there is a "goal of uniformity of federal procedure").

99 See id.

100 See, for example, *Arbogast Family Trust v River Crossings, LLC*, 238 P3d 1035, 1037–38 (Utah 2010) (stating that when the Utah Rules of Civil Procedure are similar to the Federal Rules, the courts can "turn to the federal rules of civil procedure and cases interpreting them for further guidance").

101 See *North American Catholic Educational Programming Foundation, Inc v Cardinale*, 567 F3d 8, 15 (1st Cir 2009); *Aetna Casualty and Surety Co v Aniero Concrete Co*, 404 F3d 566, 583 (2d Cir 2005) (stating that negligent misrepresentation "must be pled in accordance with the specificity criteria of Rule 9(b)").

102 See *General Electric Capital Corp v Posey*, 415 F3d 391, 394 (5th Cir 2005) (holding that state-law negligent misrepresentation is not a fraud claim and therefore not subject to Rule 9(b)); *Tricontinental Industries, Ltd v PricewaterhouseCoopers, LLP*, 475 F3d 824, 833 (7th Cir 2007) (stating that negligent misrepresentation "is not governed by . . . Rule 9(b)").

negligent misrepresentation constitutes fraud under Rule 9(b).[103] In unpublished opinions, Fourth and Ninth Circuit panels took a similar approach.[104] The following will examine each of the three approaches and outline the implications of the circuit split.

1. Courts applying Rule 9(b).

The First and Second Circuits categorically apply Rule 9(b). In *North American Catholic Educational Programming Foundation, Inc v Cardinale*,[105] a nonprofit organization brought suit for negligent misrepresentation, along with other claims, against an investment firm and its employees over a failed deal to lease a wireless spectrum used for transmitting data.[106] The defendants moved to dismiss the suit, in part, because the plaintiffs did not plead the claim with sufficient particularity under Rule 9(b).[107] The lower court dismissed the claim and the nonprofit appealed, claiming that Rule 9(b) did not apply.[108] The First Circuit affirmed. The court held that Rule 9(b) covers fraud-like claims such as negligent misrepresentation.[109] The court explained that although "one might think that negligent misrepresentation" is not subject to Rule 9(b), "case law here and in other circuits reads Rule 9(b) expansively to cover associated claims where the core allegations effectively charge fraud."[110]

The Second Circuit came to the same conclusion. In *Aetna Casualty and Surety Co v Aniero Concrete Co*,[111] a construction company claimed that Aetna—which was soliciting bids for a construction job—misinformed the company about the amount of

[103] See *Trooien v Mansour*, 608 F3d 1020, 1028 (8th Cir 2010) (applying Rule 9(b) because "[u]nder Minnesota law, any allegation of misrepresentation . . . is considered an allegation of fraud").

[104] See *Baltimore County v Cigna Healthcare*, 238 Fed Appx 914, 921 (4th Cir 2007) (holding that "Rule 9(b) [does] not apply" because negligent misrepresentation "does not contain an essential showing of fraud" under Maryland law); *Andresen v Hunt*, 1991 WL 268716, *3 (9th Cir) (following Oregon case law in holding that Rule 9(b) applies to negligent misrepresentation claims).

[105] 567 F3d 8 (1st Cir 2009).

[106] Id at 10–12.

[107] Id at 12–15.

[108] Id at 12–13.

[109] *North American Catholic Educational Programming Foundation*, 567 F3d at 15. See also *Hayduk v Lanna*, 775 F2d 441, 443 (1st Cir 1985) (stating that "in actions alleging conspiracy to defraud or conceal, the particularity requirements of Rule 9(b) must be met").

[110] *North American Catholic Educational Programming Foundation*, 567 F3d at 15.

[111] 404 F3d 566 (2d Cir 2005).

work the construction job required.[112] The construction company sued for negligent misrepresentation and Aetna moved to dismiss, arguing that Rule 9(b) applied.[113] The Second Circuit ruled that negligent misrepresentation "must be pled in accordance with the specificity criteria of Rule 9(b)."[114] The Second Circuit subsequently dismissed the claim for lack of particularity.[115]

The District of Delaware case *Toner v Allstate Insurance Co*[116] provided a detailed explanation for why Rule 9(b) applies.[117] The court laid out four rationales for Rule 9(b) and implied that applying the Rule to negligent misrepresentation is consistent with each of the four.[118] The four rationales are: (1) to protect defendants from "frivolous suits," (2) to put defendants "on notice as to the conduct complained of so [defendants] will have information adequate to form a defense," (3) to prevent "fraud actions in which all the facts are learned after the complaint is filed by way of the discovery process," and (4) to protect defendants "from damage to [their] reputation and goodwill."[119]

With the exception of the policy rationales in *Toner*,[120] courts have failed to provide a detailed justification for why Rule 9(b) applies. While the First and Second Circuits implied that negligent misrepresentation claims implicate Rule 9(b) in a manner similar to fraud, neither court explained why.

2. Courts not applying Rule 9(b).

In contrast to the First and Second Circuits, the Fifth and Seventh Circuits do not require heightened pleading for negligent misrepresentation. In *General Electric Capital Corp v Posey*,[121] the plaintiff invested $20 million in the defendants' company due to the defendants' assurances that the company was financially sound.[122] When those assurances turned out to be false, the plaintiff claimed negligent misrepresentation.[123] The

[112] Id at 569–72.
[113] Id at 570, 573.
[114] Id at 583.
[115] *Aetna Casualty and Surety*, 404 F3d at 583.
[116] 821 F Supp 276 (D Del 1993).
[117] Id at 285.
[118] Id at 283–85.
[119] Id at 284.
[120] See notes 118–19 and accompanying text.
[121] 415 F3d 391 (5th Cir 2005).
[122] Id at 393–94.
[123] Id.

defendants moved to dismiss the claim for failure to comply with Rule 9(b).[124] The Fifth Circuit denied the motion and held that negligent misrepresentation is "not subject to the heightened pleading requirements of rule 9(b)" because negligent misrepresentation is not a "fraud claim."[125] The court provided no further analysis of the issue.

The Seventh Circuit came to the same conclusion. In *Tricontinental Industries, Ltd v PricewaterhouseCoopers, LLP*,[126] an accounting firm audited a company that had engaged in corrupt accounting practices.[127] The accounting firm, however, failed to report the accounting problems and assured investors that the company had complied with Generally Accepted Accounting Principles.[128] The plaintiff sued for negligent misrepresentation and claimed that it had invested in the company due to the accounting firm's report.[129] The defendants moved to dismiss the claim and argued that Rule 9(b) should apply.[130] The Seventh Circuit denied the motion and held that the plaintiff's negligent misrepresentation claim "is not governed by the heightened pleading standard of Rule 9(b)."[131] The court provided no further explanation for why Rule 9(b) does not apply.[132]

Two district courts described in detail why Rule 8(a) should apply and why Rule 9(b) should not. The District of New Mexico case, *City of Raton v Arkansas River Power Authority*,[133] responded to the rationales in *Toner*. The court stated that there is less need to extend Rule 9(b) to cover negligent misrepresentation now that Rule 8(a) has become more stringent after *Twombly*.[134] The court held that Rule 8(a) now fulfills many of Rule 9(b)'s objectives as outlined in *Toner*.[135] It protects a defendant's reputation by weeding out frivolous claims and puts

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[124] Id.
[125] *General Electric Capital*, 415 F3d at 394.
[126] 475 F3d 824 (7th Cir 2007).
[127] Id at 827–29.
[128] Id.
[129] Id at 829–30.
[130] *Tricontinental Industries*, 475 F3d at 830–31.
[131] Id at 833 (emphasis omitted).
[132] Id.
[133] 600 F Supp 2d 1130 (D NM 2008).
[134] Id at 1144.
[135] Id at 1143–44; *Toner*, 821 F Supp at 283–85.

the defendant on notice.[136] The court concluded that this makes it unnecessary to extend Rule 9(b) to negligent misrepresentation.[137]

The Northern District of Texas did not apply Rule 9(b) either, although for a different reason. In *American Realty Trust, Inc v Travelers Casualty and Surety Co of America*,[138] the court applied the maxim *expressio unius est exclusio alterius*, which stands for the proposition that items not listed are assumed to be excluded.[139] The court reasoned that because Rule 9(b) mentions only "fraud or mistake," it should not apply to negligent misrepresentation.[140]

As before, the district courts provide the most detailed rationales while the circuit courts provide little to no analysis of the issue.

3. Courts applying state law.

The Fourth, Eighth, and Ninth Circuits have created a third path by looking to the state's definition of fraud to determine whether Rule 9(b) applies. In *Baltimore County v Cigna Healthcare*,[141] the Fourth Circuit reviewed a negligent misrepresentation suit out of Maryland that stemmed from a group life insurance policy.[142] The defendant had moved to dismiss the case and the same issue arose—whether Rule 9(b) applies to the negligent misrepresentation claim.[143] In an unpublished opinion, a Fourth Circuit panel held that "Rule 9(b) [does] not apply" because, under Maryland law, negligent misrepresentation "does not contain an essential showing of fraud."[144]

The Eighth Circuit used a similar methodology in *Trooien v Mansour*.[145] The plaintiff in that case brought several claims against the defendants—executives of a company in which the plaintiff had invested—including negligent misrepresentation

[136] *Arkansas River Power Authority*, 600 F Supp 2d at 1144. See also *Leatherman v Tarrant County Narcotics Intelligence and Coordination Unit*, 507 US 163, 168 (1993) (applying *expressio unius est exclusio alterius* in the 9(b) context, concluding that "the Federal Rules do address in Rule 9(b) the question of the need for greater particularity in pleading certain actions").

[137] *Arkansas River Power Authority*, 600 F Supp 2d at 1144.

[138] 362 F Supp 2d 744 (ND Tex 2005).

[139] Id at 749.

[140] Id.

[141] 238 Fed Appx 914 (4th Cir 2007).

[142] Id at 915–18.

[143] Id at 921.

[144] Id.

[145] 608 F3d 1020 (8th Cir 2010).

under Minnesota common law.[146] As before, the defendants moved to dismiss the claim and argued that Rule 9(b) should apply.[147] The Eighth Circuit held that Rule 9(b) covers negligent misrepresentation in this case because "under Minnesota law, any allegation of misrepresentation . . . is considered an allegation of fraud."[148]

Finally, the Ninth Circuit echoed the Fourth and Eighth Circuits' trend in an unpublished opinion. In *Andresen v Hunt*,[149] the plaintiffs had invested in an "offshore bank," expecting 25 to 40 percent returns.[150] But the investments eventually became worthless. The plaintiffs sued for negligent misstatements under Oregon law, and the defendants moved to dismiss the claim for failure to comply with Rule 9(b).[151] The Ninth Circuit held that Rule 9(b) applied because Oregon case law treated negligent misstatements as fraud claims under the state securities statute.[152]

Several district courts have also followed the state-law approach used by the Fourth, Eighth, and Ninth Circuits.[153] These opinions do not vary in any meaningful way from the previously mentioned circuit court cases.[154]

4. Implications of the circuit split.

The resulting circuit split causes two principal problems. First, it creates incentives for forum shopping. Parties will file negligent misrepresentation claims in federal courts with the most lenient pleading standards in order to give their claims the best chance to move forward. As the hypothetical at the beginning of this Comment suggests, if a plaintiff has a choice between filing a negligent misrepresentation claim in the Second Circuit or the Fifth Circuit, the plaintiff will likely choose the Fifth Circuit, which does not require a plaintiff to plead

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[146] Id at 1028 ("Trooien also asserted a number of fraudulent and negligent misrepresentation claims against Mansour.").

[147] Id at 1026.

[148] Id at 1028–29.

[149] 1991 WL 268716 (9th Cir).

[150] Id at *1.

[151] Id at *3.

[152] Id at *2–3 ("[The Oregon securities statute] is violated in the event of a negligent misstatement or omission of a material fact.").

[153] See, for example, *Linville v Ginn Real Estate Co*, 697 F Supp 2d 1302, 1306 (MD Fla 2010).

[154] See id.

negligent misrepresentation under Rule 9(b).[155] The Second Circuit does.[156]

If a lenient federal forum is not available, the plaintiff can also file in a state with lenient pleading standards. For instance, Maine state law stipulates that "[a] claim for negligent misrepresentation [ ] does not sound in fraud or mistake, but in negligence, and 9(b)'s pleading requirements are inapplicable to claims sounding in negligence."[157] Consequently, a plaintiff in Maine would likely not file a negligent misrepresentation claim in federal court because the First Circuit requires heightened pleading.[158]

The second problem is that the circuit split causes uncertainty for parties and judges, especially in circuits that have not ruled on the issue. The Third, Tenth, Eleventh, DC, and Federal Circuits have not decided whether Rule 9(b) applies to state-law negligent misrepresentation.[159] It is unclear how a party should plead negligent misrepresentation in these circuits. Additionally, the Sixth Circuit has addressed the issue, but its relevant rulings epitomize the confusion surrounding the intersection between Rule 9(b) and state-law negligent misrepresentation. The Sixth Circuit has failed to settle on a method for interpreting Rule 9(b). It is uncertain whether the court looks to state law or has a categorical rule against using Rule 9(b).[160] Consequently, it is difficult for a plaintiff to know how to file a negligent misrepresentation claim in the Sixth Circuit. This uncertainty will cause parties in these circuits to plead negligent misrepresentation with particularity when possible. This may discourage parties with legitimate claims from filing suit. It may also cost some parties the unnecessary expense of complying with a particularity requirement that may not apply.

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[155] See *General Electric Capital*, 415 F3d at 394.

[156] See *Aetna Casualty and Surety*, 404 F3d at 583.

[157] *Hayes v Iworx, Inc*, 2006 WL 2959702, *4 (Me Super Ct).

[158] See *North American Catholic Educational Programming Foundation*, 567 F3d at 15.

[159] See, for example, *Denver Health and Hospital Authority v Beverage Distributors Co*, 843 F Supp 2d 1171, 1177 (D Colo 2012) (stating that the Tenth Circuit has not decided whether negligent misrepresentation qualifies as fraud under FRCP 9(b)).

[160] Contrast *Republic Bank & Trust Co v Bear Stearns & Co*, 683 F3d 239, 247–48 (6th Cir 2012) (holding that Rule 9(b) applies because under Kentucky law negligent misrepresentation must be pleaded with particularity), with *CNH America LLC v International Union, United Automobile, Aerospace and Agricultural Implement Workers of America (UAW)*, 645 F3d 785, 795 (6th Cir 2011) (holding that Rule 9(b) does not apply to "run-of-the-mill negligence" such as negligent misrepresentation).

B. Rule 9(b) and Negligent Misrepresentation under the Securities Act of 1933

Although federal courts are split in how they approach Rule 9(b) and state-law negligent misrepresentation, circuit courts vary little on whether Rule 9(b) applies to negligent misrepresentation under the Securities Act. The Second, Third, Fifth, Eighth, and Tenth Circuits have definitively ruled that Rule 9(b) does not apply to Securities Act negligent misrepresentation claims.[161] Each court draws a clear distinction between fraud and negligence under Rule 9(b). Additionally, the First, Fourth, and Ninth Circuits strongly imply that Rule 9(b) does not apply, without stating so directly.[162] Not one circuit has found otherwise.

This means that two circuits explicitly change how they rule based on whether the negligent misrepresentation claim arises from state law or the Securities Act. The Second Circuit makes the most drastic change. As mentioned in Part II.A.1, the Second Circuit classifies state-law negligent misrepresentation as fraud and applies Rule 9(b).[163] But under the Securities Act the court holds that negligent misrepresentation is not an "[averment] of

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[161] See *Rombach v Chang*, 355 F3d 164, 171 (2d Cir 2004) ("[W]hile a plaintiff need allege no more than negligence to proceed under Section 11 . . . claims that do rely upon averments of fraud are subject to the test of Rule 9(b)."); *In re Suprema Specialties, Inc Securities Litigation*, 438 F3d 256, 274 (3d Cir 2006) ("Rule 9(b) does not apply to Section 11 . . . claims that are expressly pled in negligence."); *Melder*, 27 F3d at 1100 n 6 (stating that 9(b) applies when "Securities Act claims are grounded in fraud rather than negligence"); *In re NationsMart Corp Securities Litigation*, 130 F3d 309, 315 (8th Cir 1997); *Schwartz v Celestial Seasonings, Inc*, 124 F3d 1246, 1251–52 (10th Cir 1997) (holding that the plaintiff's negligent misrepresentation claim "is not premised on fraud and does not trigger Rule 9(b) scrutiny").

[162] See *Shaw v Digital Equipment Corp*, 82 F3d 1194, 1223 (1st Cir 1996) ("The threshold question is whether the [ ] complaint, which sets forth claims under Sections 11 and 12(2) of the Securities Act, contains any 'averments of fraud.'"); *Cozzarelli v Inspire Pharmaceuticals Inc*, 549 F3d 618, 629 (4th Cir 2008):

> Rule 9(b) applies to allegations under the Securities Act where those allegations sound in fraud. Although claims under Sections 11 and 12(a)(2) may not have fraud as an element, Rule 9(b) refers to 'alleging fraud,' not to causes of action or elements of fraud. When a plaintiff makes an allegation that has the substance of fraud, therefore, he cannot escape the requirements of Rule 9(b) by adding a superficial label of negligence or strict liability.

(citations omitted). See also *Vess v Ciba-Geigy Corp USA*, 317 F3d 1097, 1104 (9th Cir 2003), quoting *Melder*, 27 F3d at 1100 n 6 ("When 1933 Securities Act claims are grounded in fraud rather than negligence as they clearly are here, Rule 9(b) applies.").

[163] See *Aetna Casualty and Surety*, 404 F3d at 583. See text accompanying notes 111–15.

fraud" and that Rule 9(b) does not apply.[164] Surprisingly, the court has made no reference of its contradictory holdings.

The Eighth Circuit also treats the Securities Act in a way that could result in a different pleading standard than state-law claims. The court looks to state law to determine whether Rule 9(b) applies to state-law negligent misrepresentation.[165] But under the Securities Act, the Eighth Circuit concludes that Rule 9(b) does not apply because "§ 11 does not require proof of fraud for recovery."[166] Although these rulings are not necessarily contradictory, the court makes no mention that a state-law negligent misrepresentation claim could face different pleading requirements than a Securities Act claim.

Finally, the Third and Tenth Circuits—which did not rule on whether Rule 9(b) applies to state-law negligent misrepresentation claims[167]—now hold the Rule 9(b) does not apply to negligence under the Securities Act.[168] Consequently, it is unclear whether a state-law claim will face a different pleading standard than a Securities Act claim.

The difference in how circuit courts treat negligent misrepresentation under state law and the Securities Act is significant because it creates an unnecessary trap for unsuspecting and unsophisticated plaintiffs—especially in the Second Circuit. At first blush, it appears as if the Second Circuit's inconsistent rulings would make little difference for plaintiffs. Parties who know that the Second Circuit treats negligent misrepresentation claims differently will plead under both state law and the Securities Act so that one claim will receive a lower pleading standard—thus increasing the likelihood that one of the two claims survives. But it is unclear who is aware of this issue. There is no precedent in any other area of the law for the same claim having different pleading standards depending whether the party pleads under state or federal law. Therefore, it is unlikely that a

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[164] See *Rombach*, 355 F3d at 171.

[165] See *Trooien*, 608 F3d at 1028 (applying Rule 9(b) because "[u]nder Minnesota law, any allegation of misrepresentation . . . is considered an allegation of fraud").

[166] *NationsMart*, 130 F3d at 315.

[167] See *Denver Health and Hospital Authority*, 843 F Supp 2d at 1177 (stating that the Tenth Circuit has not decided whether negligent misrepresentation qualifies as fraud under FRCP 9(b)); *Shapiro v UJB Financial Corp*, 964 F2d 272, 288 (3d Cir 1992). In that case, the court also upheld plaintiffs' state-law negligent misrepresentation claims on other grounds, without addressing the sufficiency of the pleadings (perhaps because the plaintiffs had sufficiently alleged fraud in their complaint, so the misrepresentation claims would have satisfied either pleading standard). Id at 289–90.

[168] See *Schwartz*, 124 F3d at 1251–52; *In re Suprema Specialties*, 438 F3d at 274.

plaintiff would check whether a state law or Securities Act claim would have a lower pleading standard. Additionally, no scholarly articles have been written on the subject, and the Second Circuit has not realized that its own decisions are contradictory. This creates a trap for everyone except the few—if any—who recognize the problem, which may amount to the few that can afford the most sophisticated counsel. This problem runs contrary to the spirit of the Securities Act, which was meant to protect unsophisticated investors.[169]

III. A HISTORICAL APPROACH TO RULE 9(B) AND NEGLIGENT MISREPRESENTATION

Courts' handling of Rule 9(b) and negligent misrepresentation is confusing and inconsistent. The resulting uncertainty regarding this issue gives rise to the multiple problems discussed above. A principled and consistent approach to Rule 9(b) and negligent misrepresentation will lessen the effects of these problems. First, if federal courts use the same pleading standard, plaintiffs will have no pleadings-driven incentives to choose among federal courts. Some forum shopping between state and federal courts will still exist, but that is largely unavoidable. Second, harmonizing the pleading standard across state-law and Securities Act claims will eliminate an unnecessary stumbling block for plaintiffs filing negligent misrepresentation claims involving securities.

This Part advocates for such an approach by arguing that courts should not apply Rule 9(b) to negligent misrepresentation, regardless of whether the claim originates from state law or a federal statute like the Securities Act. This is the most faithful interpretation and application of Rule 9(b). There are four parts to this argument. First, fraud and mistake should have consistent definitions under Rule 9(b). Courts should not apply the definitions of fraud and mistake on a state-by-state basis. Since Rule 9(b) has not changed since its enactment in 1938,[170] courts should look to the definitions of fraud and mistake at that time. Second, negligent misrepresentation was not

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[169] See *Gilligan, Will & Co v Securities and Exchange Commission*, 267 F2d 461, 463 (2d Cir 1959) ("The principal and essential purpose of the 1933 Act is to protect investors by requiring registration with the Commission of certain information concerning securities offered for sale.").

[170] See Richman, Lively, and Mell, 60 S Cal L Rev at 965 (cited in note 25); Fairman, 38 UC Davis L Rev at 286–87 (cited in note 21).

included in the definition of either fraud or mistake in 1938; at that time, fraud, negligent misrepresentation, and mistake were distinct causes of action.[171] Third, since Rule 9(b) only mentions fraud and mistake—and not negligent misrepresentation—it can be inferred that the Rule does not apply to negligent misrepresentation. Finally, the differences between fraud and negligent misrepresentation are significant enough that the two torts should not have the same pleading standard absent express congressional provision. This Part analyzes each of these arguments in greater detail.

A. Fraud and Mistake Should Have Consistent Definitions under Rule 9(b)

When a state-law claim reaches federal court through diversity jurisdiction, courts must decide whether state law or federal law applies. In making that determination, courts ask whether the federal law is substantive or procedural.[172] A law is substantive if it "significantly affect[s] the result" of the case.[173] A law is procedural if it does not.[174]

Federal courts have consistently held that the Federal Rules of Civil Procedure are procedural law, even when they contain substantive common law elements.[175] For example, the standard for summary judgment under Rule 56(a) asks whether there is a "genuine dispute as to any material fact."[176] Materiality is a principle that has existed in American common law since the nineteenth century.[177] But federal courts do not apply the definition of materiality on a state-by-state basis in diversity actions, even though it could be outcome determinative. Instead, courts adhere to one understanding of materiality that governs the Rule in all federal courts.[178]

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171 See Restatement (First) of Torts § 552 (1938) (providing a cause of action for negligent misrepresentation); id at § 525 (providing a cause of action for fraudulent misstatement); id at § 55–57 (providing a causes of action for mistake).

172 See *Hanna v Plumer*, 380 US 460, 465 (1965) ("[F]ederal courts are to apply state substantive law and federal procedural law.").

173 *Guaranty Trust Co v York*, 326 US 99, 109 (1945).

174 Id.

175 See *Shady Grove Orthopedic Associates, PA v Allstate Insurance Co*, 130 S Ct 1431, 1442–43 (2010) (plurality).

176 FRCP 56(a).

177 See *Wright v Wright*, 6 Tex 3, 20 (1851).

178 See *Anderson v Liberty Lobby, Inc*, 477 US 242, 248 (1986) (stating that a fact is material if it "might affect the outcome of the suit").

Additionally, the standard for what is discoverable under Rule 26(b) is relevance. The Rule states that a party "may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense."[179] Relevance is a principle that has existed in American common law since the late 1700s.[180] But federal courts do not apply the definition of relevance on a state-by-state basis either, even though it could be outcome determinative.[181]

Similarly, Rule 9(b) mentions fraud and mistake, which are common law elements. This has created confusion among federal courts. Some courts have looked to state law to determine the definitions of fraud and mistake in Rule 9(b).[182] Other courts have used a single definition for all state and federal cases, without referring to state law.[183]

Although fraud and mistake are common law principles, courts should not apply those concepts on a state-by-state basis. Instead, courts should adhere to a single, nationwide definition for each word. This not only follows the precedent described above, but it also conforms with the goals of the Federal Rules. In *Hanna v Plumer*,[184] the Supreme Court stated: "One of the shaping purposes of the Federal Rules is to bring about uniformity in the federal courts by getting away from local rules. This is especially true of matters which relate to the administration of legal proceedings."[185] Common law elements are found throughout the Federal Rules. Rules 26 and 56 are just two examples. If courts were to apply every common law element on a state-by-state basis, there would be little uniformity left. The

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179 FRCP 26(b)(1).

180 See *Bebee v Tinker*, 2 Root 160 (Conn Super Ct 1794) ("[B]ut as the point to which the plaintiff called him to testify was ruled by the court, not to be relevant to the issue.").

181 See FRCP 26(b)(1) (defining relevant information as that which is "reasonably calculated to lead to the discovery of admissible evidence").

182 See *Trooien*, 608 F3d at 1028 (applying Rule 9(b) because "[u]nder Minnesota law, any allegation of misrepresentation . . . is considered an allegation of fraud"); *Cigna Healthcare*, 238 Fed Appx at 921 (holding that "Rule 9(b) [does] not apply" because negligent misrepresentation "does not contain an essential showing of fraud" under Maryland law).

183 See *General Electric Capital*, 415 F3d at 394 (holding that negligent misrepresentation is not a fraud claim and therefore not subject to Rule 9(b)); *Melder*, 27 F3d at 1100 n 6 (concluding that Rule 9(b) applies when "Securities Act claims are grounded in fraud rather than negligence").

184 380 US 460 (1965).

185 Id at 472, quoting *Lumbermen's Mutual Casualty Co v Wright*, 322 F2d 759, 764 (5th Cir 1963).

Federal Rules were meant to "get[ ] away from local rules" and create uniformity, especially with regard to legal proceedings—like pleadings standards.[186] The best way to achieve uniformity within federal courts is to apply consistent definitions of fraud and mistake nationwide. Therefore, fraud and mistake should each have a single definition for the purposes of Rule 9(b).

B. The Definitions of Fraud and Mistake Did Not Include Negligent Misrepresentation When Rule 9(b) Emerged in 1938

Since fraud and mistake should have fixed definitions within Rule 9(b), the next step is to determine what those definitions are. As mentioned in Part I.A, Rule 9(b) emerged in 1938 with the first version of the Federal Rules of Civil Procedure.[187] Although a particularity requirement for fraud and mistake existed on and off in the English common law and the Field Code, 1938 is the first date that the Rule appears in the form that we know it today.[188]

The rule makers in 1938 did not provide guidance on how to interpret fraud and mistake. The congressional and ABA hearings do not mention the Rule, and the Advisory Committee Note only refers to an English rule that addresses another part of the Rule.[189] The subsequent committees that have amended the rules have also failed to provide any clarification.

The history of the Rule, however, provides indications for how fraud and mistake should be interpreted. Rule 9(b) has not changed since it was enacted in 1938.[190] This lack of change is telling. There are three ways the Federal Rules of Civil Procedure can change. First, the Advisory Committee may suggest an amendment, which then passes through several different bodies for approval.[191] Second, the Supreme Court can alter its interpretation of the rules. Third, Congress can also issue procedural

[186] See *Lumbermen's Mutual Casualty*, 322 F2d at 764.

[187] See Richman, Lively, and Mell, 60 S Cal L Rev at 965 (cited in note 25); Fairman, 38 UC Davis L Rev at 286–87 (cited in note 21). For a discussion of the history of Rule 9(b), see Part I.A.

[188] See Richman, Lively, and Mell, 60 S Cal L Rev at 965 n 28 (cited in note 25).

[189] See id at 965–66. See also Ball, Burnand, and Watmough, eds, *The Annual Practice, 1937* O 19, r 22 at 369 (cited in note 48).

[190] See Richman, Lively, and Mell, 60 S Cal L Rev at 965 (cited in note 25).

[191] See 28 USC § 2073 (outlining the procedure for proposing new rules and for amending the existing rules).

rules.[192] These modes of change can be seen in the history of Rule 8. The Advisory Committee has amended Rule 8 four times.[193] The Supreme Court has also clarified parts of the Rule. In 2007 the Court ruled on how federal courts should interpret the phrase "a short and plain statement of the claim showing that the pleader is entitled to relief" in *Twombly*.[194] The committee amendments and *Twombly* are the principal ways in which the Rule has changed since its enactment in 1938. Congress is the only body that has not changed the rule.

Rule 9(b) has not experienced any of these modes of change. If the Advisory Committee, the Supreme Court, or Congress wanted to update the rule away from the 1938 definitions of fraud and mistake and to the current understanding of the torts, it could have on numerous occasions. But they have not. Since 1938, the Advisory Committee has amended the FRCP over thirty times. Rule 9 has been amended seven times.[195] But Rule 9(b) has remained unchanged. The Supreme Court has not ruled on the meaning of fraud and mistake, and Congress has been silent. Because the Advisory Committee and the Supreme Court have not changed the Rule since its enactment,[196] it is reasonable to assume that the 1938 definitions still apply today.

The operative question, then, is whether the definitions of fraud and mistake in 1938 included negligent misrepresentation. There is convincing historical evidence that they did not. This is apparent from the development of negligent misrepresentation in both the common law and the Securities Act.

1. Common law fraud, mistake, and negligent misrepresentation in 1938.

As mentioned in Part I.B, negligent misrepresentation appeared in 1922 by way of an opinion written by Judge Cardozo.[197] This opinion split negligent misrepresentation from intentional misrepresentation—or fraud.[198] Whereas fraud

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[192] See US Const Art I, § 8, cl 9 (granting Congress the right to form federal courts "inferior to the supreme Court"). See also 28 USC § 2071(a) (stating the procedural rules must "be consistent with Acts of Congress").

[193] FRCP 8(a), Advisory Committee Notes.

[194] 550 US at 556.

[195] FRCP 9, Advisory Committee Notes.

[196] Id.

[197] See Horne, Note, 72 Or L Rev at 756 (cited in note 60); *Glanzer v Shepard*, 135 NE 275, 276 (NY 1922).

[198] See *Glanzer*, 135 NE at 276.

required that the defendant intentionally misled the plaintiff,[199] negligent misrepresentation only required that the defendant negligently supplied false information.[200]

This separation between fraud and negligent misrepresentation took root in the common law from 1922 to 1938. There are several key examples. In 1924, the West Virginia Supreme Court of Appeals faced the same issue that this Comment addresses—whether parties should be required to plead negligent misrepresentation with particularity. In *Ohio-West Virginia Co v Chesapeake & O Ry Co*[201] the court held that, although fraud "should be specifically and fully charged," negligent misrepresentation should not.[202] The court drew a firm distinction between the two torts. The court explained that negligent misrepresentation is "not based on fraud or deceit," but rather on "carelessness and negligence."[203]

In 1925, the Supreme Court of New Hampshire also recognized negligent misrepresentation as a cause of action separate from fraud. In *Weston v Brown*,[204] the court stated, "[t]he sole question presented is whether or not an action can be maintained for negligent misrepresentation."[205] The court concluded that "[i]n this jurisdiction the principle is well established that negligent words . . . may constitute actionable fault."[206] To bolster its point, the court cited *Cunningham v C. R. Pease House Furnishing Co*[207]—a case decided seventeen years earlier—which recognized negligent misrepresentation as a separate cause of

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[199] See *Derry v Peek*, 14 App Cas 337, 360–62 (HL 1889) (Herschell) (stating that intentional misrepresentation requires that (1) the defendant intentionally misrepresented a fact, (2) the defendant intended that the plaintiff rely on the fact, and (3) the plaintiff relied on the fact and was injured as a result).

[200] See *Capiccioni v Brennan Naperville, Inc*, 791 NE2d 553, 562 (Ill App 2003):

> Negligent misrepresentation consists of: (1) a false statement of a material fact; (2) carelessness or negligence in ascertaining the truth of the statement by the party making it; (3) an intention to induce the other party to act; (4) action by the other party in reliance on the truth of the statement; and (5) damage to the other party resulting from such reliance when the party making the statement is under a duty to communicate accurate information.

[201] 124 SE 587 (W Va 1924).

[202] Id at 588.

[203] Id.

[204] 131 A 141 (NH 1925).

[205] Id at 141.

[206] Id.

[207] 69 A 120 (NH 1908).

action.[208] The court in *Cunningham* differentiated between fraud and negligent misrepresentation by stating that "[t]here is a difference [ ] between intentional and negligent wrongs."[209] The court then enumerated how the intentional and negligent wrongs are different.[210]

In 1937, Pennsylvania followed suit. In *Ebbert v Philadelphia Electric Co*,[211] the Pennsylvania Superior Court explained that, although some have described negligent misrepresentation as a "species of fraud," the "concept of negligence [ ] predominates."[212] The Pennsylvania Supreme Court affirmed a year later.[213]

Treatises from the 1930s also confirm that negligent misrepresentation had emerged as a separate tort. In 1932, the fourth edition of Thomas Cooley's treatise *Cooley on Torts* stated the following:

> In England, the rule has been established that "generally speaking, there is no such thing as liability for negligence in word as distinguished from act." In a few recent cases in this country, however, the courts have tended towards, and finally adopted, the more logical position that circumstances which impose an obligation on the part of one to another to use care in his acts, would impose the same obligation of care in the making of statements of fact upon which such other might rely.[214]

This growing support for negligent misrepresentation culminated in 1938 with the publication of the Restatement (First) of Torts.[215] The Restatement included negligent misrepresentation

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208 Id at 121 (holding that a person can be held liable for a "false statement honestly believed to be true, though negligently made").

209 Id.

210 Id.

211 191 A 384 (Pa Super Ct 1937), affd 198 A 323 (Pa 1938).

212 *Ebbert*, 191 A at 388.

213 See *Ebbert v Philadelphia Electric Co*, 198 A 323, 329 (Pa 1938).

214 Thomas M. Cooley, 3 *A Treatise on the Law of Torts, or the Wrongs Which Arise Independently of Contract* § 497 at 461 (Callaghan 4th ed 1932) (citation omitted).

215 Restatement (First) of Torts § 552 (1938). See also Horne, Note, 72 Or L Rev at 756 (cited in note 60). See also Kristen David Adams, *The Folly of Uniformity? Lessons from the Restatement Movement*, 33 Hofstra L Rev 423, 433 (2004) (noting that the American Law Institute's Restatements constituted attempts to "restate certain areas of the common law of the United States," and were intended to "tell judges and lawyers what the law was") (quotation marks omitted).

as a tort separate from fraud.[216] This further solidified negligent misrepresentation as a distinct common law cause of action.

Because the Restatement of Torts emerged the same year as Rule 9(b), it provides a convenient way to determine what fraud meant at the time of Rule 9(b)'s enactment. Based on the Restatement and the widespread acceptance of negligent misrepresentation in the common law, it is evident that negligent misrepresentation and fraud were two distinct torts, and that negligent misrepresentation was not included in the definition of fraud at that time.

Much of the same evidence that proves that negligent misrepresentation was not fraud in 1938 also proves that negligent misrepresentation was not mistake. The Restatement (First) of Torts indicates that negligent misrepresentation was a separate cause of action in 1938.[217] The state-law cases and treatises mentioned above also prove the same point.

Additionally, since Rule 9(b) emerged in 1938, no court has characterized negligent misrepresentation as a "mistake" for the purposes of Rule 9(b).[218] This indicates that courts understood—and continue to understand—that mistake and negligent misrepresentation are distinct, and unrelated, causes of action.

2. Securities Act negligent misrepresentation in 1938.

Similar to state-law negligent misrepresentation, negligent misrepresentation under the Securities Act of 1933 also emerged as a distinct cause of action by the late 1930s. Sections 11 and 12 create civil causes of action if a person provides false information or omits a material fact with regard to a registration statement[219] or securities transaction.[220] As mentioned in Part I.C, §§ 11 and 12 mention a reasonableness standard.[221]

As soon as the Act was passed, commentators recognized that parties could be liable for negligent misrepresentation

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216 See Restatement (First) of Torts § 552 (1938) (providing a cause of action for negligent misrepresentation); id at § 525 (providing a cause of action for fraudulent misstatement).

217 See id at § 552; id at § 55–57 (providing causes of action for mistake).

218 Judge Richard Posner of the Seventh Circuit only found two mistake cases in the past fifty years that were dismissed under Rule 9(b). See *Bankers Trust Co v Old Republic Insurance Co*, 959 F2d 677, 683 (7th Cir 1992). He also noted that there was a dearth of scholarly and judicial discussion about why Rule 9(b) includes mistake. Id.

219 Securities Act of 1933 § 11, 15 USC § 77k.

220 Securities Act of 1933 § 12, 15 USC § 77l(a)(2).

221 See text accompanying notes 88–90.

under §§ 11 and 12. An article published in the *Yale Law Journal* in 1933 observed that directors and officers could be held liable under § 11 if they did not conduct a "reasonable investigation" and have "reasonable ground to believe . . . that the [registration] statement was true and involved no material omissions."[222] Reasonable investigation and reasonable belief are negligence standards. This implies that directors and officers could be held liable for negligent misrepresentation under § 11.

In 1940, another *Yale Law Journal* comment came to the same conclusion.[223] But this comment was more explicit. It stated that in the case of a misleading registration statement, "a director may also be held liable for mere negligence" under § 11.[224] A *Texas Law Review* case note in 1940 agreed.[225] The article stated that in suits under §§ 11 and 12, "the defendant sustain[s] the burden of proof that he did not know of the falsity and was not negligent in not knowing."[226]

The case law surrounding §§ 11 and 12 follows the same pattern. By 1937 courts found that a party could be liable under § 11 for negligent misrepresentation. In *Martin v Hull*[227] in 1937, the DC Circuit found that § 11 requires "reasonable care to assure the accuracy" of the registration statement.[228] As noted earlier, reasonable care is a negligence standard. In 1939, the District Court for the District of Maine came to a similar conclusion. In *Murphy v Cady*,[229] the court stated that the seller in a § 12 claim has "the burden of proving that in the exercise of reasonable care he could not have known of the falsity."[230] Again, the reasonable care language sounds like a negligence standard.

As with the commentators at Yale and Texas, courts recognized soon after the Securities Act was passed that parties could be liable for negligent misrepresentation. It is telling that none of the courts or commentators refer to negligence under §§ 11 and 12 as fraud. Presumably, if they considered negligent

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[222] William O. Douglas and George E. Bates, *The Federal Securities Act of 1933*, 43 Yale L J 171, 193 (1933).

[223] Comment, *Distribution of Risk Imposed upon Corporate Officials by Federal Securities Legislation*, 49 Yale L J 1423, 1432 (1940).

[224] Id.

[225] J.F.S. Jr, Case Note, *Fraud—Civil Liability Therefor under Federal Securities Act*, 18 Tex L Rev 507, 508 (1940).

[226] Id.

[227] 92 F2d 208 (DC Cir 1937).

[228] Id at 210.

[229] 30 F Supp 466 (D Me 1939), affd 113 F2d 988 (1st Cir 1940).

[230] *Murphy*, 30 F Supp at 468.

misrepresentation a species of fraud, at least one court or commentator would have mentioned it. From the above evidence, it is apparent that negligent misrepresentation under Securities Act—like state-law negligent misrepresentation—was a distinct cause of action by the time Rule 9(b) emerged in 1938.

C. *Expressio Unius Est Exclusio Alterius*

It is evident from the previous Sections that negligent misrepresentation was not included in the definition of fraud in 1938. It is also evident that negligent misrepresentation was not mistake. With fraud and mistake defined, traditional canons of construction illuminate the scope of Rule 9(b).

The interpretive canon *expressio unius est exclusio alterius* (*expressio unius*) stands for the proposition that items not listed are assumed to be excluded.[231] In *Barnhart v Peabody Coal Co*,[232] the Supreme Court counseled that *expressio unius* applies when a statute lists items that are "members of an associated group or series."[233] The Supreme Court has applied the interpretive canon numerous times to Rule 9(b), in each case limiting the interpretation of the Rule.[234]

When Rule 9(b) emerged in 1938, fraud, negligent misrepresentation, and mistake were distinct causes of action. And each was part of the larger "associated series" of misrepresentation claims. Fraud denotes intention to deceive; mistake denotes a no-fault misrepresentation. Negligent misrepresentation falls in the middle. Since Rule 9(b) only mentions two types of misrepresentation—fraud and mistake—courts should assume that other types of misrepresentation, such as negligent misrepresentation, should not be included.

Several courts have used *expressio unius*—either explicitly or implicitly—to determine that Rule 9(b) does not apply to

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[231] See Norman J. Singer and J.D. Shambie Singer, 2A *Statutes and Statutory Construction* § 47:23 at 398–404 (West 7th ed 2007) (describing the maxim *expressio unius* as "an inference that all omissions [from the statutory text] should be understood as exclusions").

[232] 537 US 149 (2003).

[233] Id at 168 (quotation marks omitted).

[234] See, for example, *Leatherman v Tarrant County Narcotics Intelligence and Coordination Unit*, 507 US 163, 168 (1993) (stating that Rule 9(b) "[does] not include among the enumerated actions any reference to complaints alleging municipal liability under § 1983"); *Swierkiewicz v Sorema NA*, 534 US 506, 513 (2002) (holding that because Rule 9(b) does not mention employment discrimination claims, those claims are not included under the Rule).

negligent misrepresentation.[235] But these courts define fraud and mistake as the terms are understood at the time of the decision and do not rely on the 1938 definition.[236] The argument could be made that this is the most correct approach because in 1938, fraud and mistake were common law concepts. Therefore, the understanding at that time was that the definition of fraud and mistake would change over time.

This approach is misguided for two reasons. First, the common law evolves unevenly. This is evident by the different ways that states currently treat the state versions of Rule 9(b) and negligent misrepresentation. A state court in Maine held that "[Maine Rule of Civil Procedure] 9(b)'s pleading requirements are inapplicable to claims sounding in negligence."[237] A Delaware court, on the other hand, held that 9(b) does apply.[238] Overall, it is unclear whether negligent misrepresentation would constitute fraud for the purposes of Rule 9(b) if the Rule were enacted today. Consequently, in order to apply a current definition of fraud and mistake, courts would need to define the terms on a state-by-state basis. This inconsistent treatment runs afoul of the goal of uniformity in the Federal Rules. As stated earlier, this is why other common law concepts in the Federal Rules—such as materiality and relevance—are not defined on a state-by-state basis. If there were a uniform, current definition of fraud in the common law, then using the current definition of fraud would be less problematic. The circuit split would also likely not exist.

Second, the Federal Rules of Civil Procedure do not change in a common-law-like fashion, with the exception of Supreme Court decisions. As stated earlier, there are three specific ways through which the rules change: the Advisory Committee amends them, the Supreme Court clarifies them, or Congress legislates. Each body has left Rule 9(b) untouched since its enactment.[239] Had they wanted to change or clarify the Rule so that the modern definitions apply instead of the 1938 definitions, they readily could have. They have clarified other rules on

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[235] See, for example, *American Realty Trust*, 362 F Supp 2d at 749 (applying *expressio unius* to hold that Rule 9(b) does not apply to negligent misrepresentation); *General Electric Capital*, 415 F3d at 394 (holding that negligent misrepresentation is not a fraud claim and therefore not subject to Rule 9(b)).

[236] See *American Realty Trust*, 362 F Supp 2d at 749; *General Electric Capital*, 415 F3d at 394.

[237] *Hayes v Iworx, Inc*, 2006 WL 2959702, *4 (Me Super Ct).

[238] See *Carello v PricewaterhouseCoopers LLP*, 2002 WL 1454111, *8 (Del Super Ct).

[239] See Richman, Lively, and Mell, 60 S Cal L Rev at 965 (cited in note 25).

countless occasions. But because they did not change Rule 9(b), the 1938 definitions should still apply.

D. Differences between Fraud and Negligent Misrepresentation

Besides the historical and interpretive rationales for not applying Rule 9(b) to negligent misrepresentation, the differences between fraud and negligent misrepresentation also speak to why the torts should be treated differently. Most of the controversy concerning negligent misrepresentation and Rule 9(b) centers around fraud. Some courts reason that because fraud and negligent misrepresentation are similar, they should be treated similarly under Rule 9(b).[240] As stated in Part I.B, the only difference between fraud and negligent misrepresentation is scienter.[241] Fraud requires knowledge that the representation is false.[242] Negligent misrepresentation only requires negligence of the falsity.[243]

This difference in scienter is significant for three reasons. First, in some instances civil fraud is also a crime.[244] Fraud can warrant significant criminal penalties; for example, mail fraud can carry a penalty up to thirty years in prison.[245] In contrast, negligent misrepresentation is never a crime. There is no risk of imprisonment or other criminal penalties.

Second, many areas of the law consider fraud an offense of "moral turpitude," and several professions consider this grounds for losing one's professional license.[246] For instance, in *Startzel v Pennsylvania, Department of Education*,[247] a teacher lost his teaching license for committing mail fraud because it was an offense of moral turpitude.[248] Additionally, in *Oltman v Maryland*

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[240] See, for example, *North American Catholic Educational Programming Foundation*, 567 F3d at 15.

[241] See notes 69–70 and accompanying text.

[242] See Keeton, *Prosser and Keeton on the Law of Torts* § 105 at 728 (cited in note 68) (stating that fraud requires knowledge).

[243] See Restatement (Second) of Torts § 552 (1977).

[244] See, for example, 18 USC § 1341 (criminalizing mail fraud).

[245] See 18 USC § 1341.

[246] See, for example, *In re Hallinan*, 272 P2d 768, 771–72 (Cal 1954) (denying a motion to dismiss on the grounds that a federal conviction for failure to pay taxes does not necessarily involve moral turpitude, and therefore does not justify summary disbarment).

[247] 562 A2d 1005 (Pa Commw Ct 1989).

[248] Id at 1007 (stating that mail fraud is an offense of moral turpitude).

State Board of Physicians,[249] a physician assistant lost his medical license for committing fraud with respect to prescription drugs.[250] In contrast, negligent misrepresentation denotes carelessness, not intentional harm. It is not an offense of moral turpitude[251] and will likely not result in the inability to practice one's profession.

Third, courts in many jurisdictions have held that fraud "provides an appropriate basis for an award of punitive damages."[252] This can significantly increase an individual's civil liability. By contrast, negligent misrepresentation is only subject to normal tort liability.

These differences speak to why fraud should be pleaded with particularity and why negligent misrepresentation should not. *Toner*'s rationales—outlined in Part II.A.1—serve as useful guideposts.[253] Accusing an individual of an offense of moral turpitude could severely damage that person's "reputation and goodwill," and possibly cost that person his job.[254] The accused should also be "put[] [ ] on notice" of such serious accusations.[255] Since a fraud claim could bring significant civil and criminal liability, the rules of procedure should root out as many "frivolous" claims as possible.[256] Finally, because the stakes are so high, parties should not be able to accuse people of fraud and then fish through their lives to find it during discovery.[257] The severity of the accusation warrants special treatment. Therefore, Rule 9(b) should apply.

Negligent misrepresentation, on the other hand, is far less severe. There is less need to put the defendant on notice, and there is less harm to the defendant's reputation. In fact, there is no reason why negligent misrepresentation harms a defendant's

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[249] 875 A2d 200 (Md Ct Spec App 2005).

[250] Id at 217.

[251] See *Mehboob v Attorney General*, 549 F3d 272, 276 (3d Cir 2008) (stating that the court "has drawn a line at recklessness," and that moral turpitude does not attach to the "mental state of negligence").

[252] *Markegard v Von Ruden*, 2006 WL 163508, *5 (Minn Ct App) ("Minnesota courts have long recognized that a finding of fraud provides an appropriate basis for an award of punitive damages."). See also, for example, *Rinella v Stabile*, 2011 WL 1473928, *16 (Cal Ct App) ("[F]raud is an appropriate basis for an award of punitive damages.").

[253] See text accompanying notes 116–19.

[254] *Toner*, 821 F Supp at 284.

[255] Id.

[256] Id.

[257] See id.

reputation more than any other tort pleaded under Rule 8(a).[258] Likewise, it is unclear why parties would need special protection from frivolous suits or discovery abuses in negligent misrepresentation cases. Overall, the differences between fraud and negligent misrepresentation are significant enough to warrant different pleading standards.

Similarity to mistake does not provide a ground to include negligent misrepresentation within Rule 9(b) either. Some scholars have concluded that the rationales for Rule 9(b) only apply to fraud, and not to mistake.[259] In the Seventh Circuit case *Bankers Trust Co v Old Republic Insurance Co*,[260] Judge Richard Posner stated that he "can find neither judicial nor scholarly discussion of the rationale" for pleading mistake with particularity under Rule 9(b).[261] Without a rationale for why Rule 9(b) applies to mistake, it is difficult to conclude that Rule 9(b) should cover negligent misrepresentation because of its similarity to mistake, as doing so would extend the anomaly noted by Judge Posner to another cause of action.

In summary, there is not a compelling reason to include negligent misrepresentation under Rule 9(b). Negligent misrepresentation does not carry the severity of fraud, and the inclusion of mistake in the Rule is mainly a mystery. Consequently, Rule 9(b) should not apply to negligent misrepresentation, absent a clear mandate from the Advisory Committee, the Supreme Court, or Congress.

CONCLUSION

Courts have treated negligent misrepresentation inconsistently with regard to Rule 9(b). Presently, similar claims are treated differently depending on where the party files the claim. Claims are also treated differently depending on whether the party uses state law or the Securities Act. The circuit split creates the opportunity for forum shopping, while the differential

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[258] See *Arkansas River Power Authority*, 600 F Supp 2d at 1144 ("There is no sound reason to give corporate defendants accused of negligent misrepresentation more protection that [sic] doctors accused of malpractice or automobile operators of negligence.").

[259] See, for example, Fairman, 38 UC Davis L Rev at 287, 290–97 (cited in note 21) (stating that "Rule 9(b) has become essentially a special rule for fraud," and that the rationales justifying the Rule pertain to fraud specifically).

[260] 959 F2d 677 (7th Cir 1992).

[261] Id at 683.

treatment of the Securities Act creates a trap for unsuspecting and unsophisticated plaintiffs.

As this Comment argues, fraud and mistake should have consistent definitions under Rule 9(b) in order to avoid both these disparities and to decrease the incentives for strategic behavior. The Restatement (First) of Torts and the widespread acceptance of negligent misrepresentation in the common law demonstrate that negligent misrepresentation was not included in the definition of either fraud or mistake when Rule 9(b) was enacted in 1938. Since the Rule only mentions fraud and mistake—and not negligent misrepresentation—courts should construe Rule 9(b) according to its terms and refrain from applying it to negligent misrepresentation.

Although this Comment only addressed Rule 9(b)'s relation to negligent misrepresentation, the historical approach can help courts answer questions regarding both of the Rule's clauses—whether a given tort qualifies as fraud and mistake, or whether a claim constitutes "[m]alice, intent, knowledge, and other conditions of a person's mind."[262] As the Comment demonstrates, understanding the history of Rule 9(b) is pivotal to grasping the Rule's scope even outside the limited context discussed here. Many common ways of understanding the Federal Rules of Civil Procedure—such as the Advisory Committee Notes, Supreme Court decisions, or procedural history—provide little information on the scope of Rule 9(b). Consequently, courts have few helpful options outside the Rule's history. Since the Advisory Committee, the Supreme Court, and Congress have not changed the Rule since its enactment, courts should look at what the Rule meant when it emerged in 1938. In short, the historical approach provides courts with a consistent methodology to interpret Rule 9(b) going forward.

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[262] FRCP 9(b).