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DROWNING IN A SEA OF CONTRACT: APPLICATION OF THE ECONOMIC LOSS RULE TO FRAUD AND NEGLIGENT MISREPRESENTATION CLAIMS

The economic loss rule is stated with ease but applied with great difficulty. . . . Lawyers and judges alike have found it difficult to determine when the rule applies and when an exception is appropriate.¹

The economic loss rule is one of the most confusing doctrines in tort law.² The rule defines the boundary between the overlapping theories of tort law and contract law by barring the recovery of purely economic loss in tort, particularly in strict liability and negligence cases.³ The rationale behind the rule is that contract law and the Uniform Commercial Code (UCC) are expressly designed to deal with disappointed economic expectations and, therefore, the recovery of economic losses.⁴ Confusion arises, however, when courts apply the economic loss rule to torts that expressly provide for the recovery of purely economic losses,⁵ such as misrepresentation.⁶

1. *Sandarac Ass'n v. W.R. Frizzell Architects, Inc.*, 609 So. 2d 1349, 1352 (Fla. Dist. Ct. App. 1992).

2. See Paul J. Schwiep, *The Economic Loss Rule Outbreak: The Monster that Ate Commercial Torts*, FLA. B.J., Nov. 1995, at 34, 34 ("[I]t is clear that judges, lawyers, and commercial clients alike are all desperately struggling to define the parameters of the economic loss doctrine.").

3. See *infra* notes 37-45 and accompanying text.

4. See *infra* notes 46-79 and accompanying text.

5. Torts that allow the recovery of economic loss include, but are not limited to, defamation, conversion, malicious prosecution, invasion of privacy, and tortious interference with business advantage. See *W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS* § 116A, at 843-44, § 119, at 887-88, § 130, at 1006 (5th ed. 1984); see also *Tommy L. Griffin Plumbing & Heating Co. v. Jordon, Jones & Goulding, Inc.*, 463 S.E.2d 85, 88 (S.C. 1995) ("Purely 'economic loss' may be recoverable under a variety of tort theories."). Unlike misrepresentation, courts readily conclude that the economic loss rule does not apply to other torts that permit the recovery of economic loss. See, e.g., *Canal Elec. Co. v. Westinghouse Elec. Co.*, 973 F.2d 988, 998 (1st Cir. 1992) (explaining that the law permits recovery of economic loss for intentional torts, such as defamation); *Pershing Indus. v. Sanz*, 740 So. 2d 1246, 1248 (Fla. Dist. Ct. App. 1999) (finding the economic loss rule does not bar claims for conversion and civil theft); *Facchina v. Mutual Benefits Corp.*, 735 So. 2d 499, 502-03 (Fla. Dist. Ct. App. 1999) (having "little trouble in concluding" that the economic loss rule did not bar defamation and invasion of privacy).

6. Throughout this Note the generic term misrepresentation includes both inten-

In states adopting the economic loss rule, courts struggle with the questions of if, when, and how the economic loss rule should apply to claims arising out of a defendant's fraudulent conduct. Accordingly, courts have designed diverse rationales in determining when, and if, the economic loss rule should bar recovery in a misrepresentation claim.⁷

Illustrating the diverse application of the economic loss rule is the different treatment of similar claims involving the same defective product, fire-retardant treated (FRT) plywood.⁸ In the mid-1980s, the American Plywood Association notified its members that FRT plywood was subject to thermal degradation.⁹ Despite this warning and without disclosing the dangers, the manufacturers continued to promote and sell the product.¹⁰ As roofs deteriorated, they posed a risk of collapsing.¹¹ Accordingly,

tional (i.e. fraudulent) and negligent misrepresentation. When the discussion focuses on a particular claim, the discussion will be so distinguished by reference to a particular type of misrepresentation.

7. See *All-Tech Telecom, Inc. v. Amway Corp.*, 174 F.3d 862, 867 (7th Cir. 1999) (noting the various applications of the economic loss rule to misrepresentation claims).

8. FRT plywood is a chemically treated plywood designed to resist fire that was used as roof sheathing on buildings, including residential homes. See *Pulte Home Corp. v. Ply Gem Indus.*, 804 F. Supp. 1471, 1477 (M.D. Fla. 1992).

9. See *Morris v. Osmose Wood Preserving*, 639 A.2d 147, 149-50 (Md. Ct. Spec. App. 1994), *aff'd in part, rev'd in part*, 667 A.2d 624 (Md. 1995). When FRT plywood is exposed to elevated temperatures (alleged by the plaintiffs to begin at 130° fahrenheit) a chemical reaction occurs that destroys the bond between the plywood laminates and weakens the wood, resulting in deterioration, loss of strength capacity, and impairment of structural integrity. See *Morris*, 667 A.2d at 628. The plaintiffs claimed that roofs can reach temperatures of 180° fahrenheit without being exposed to fire. See *id.* They further alleged that the reaction inevitably occurs in roofs, without regard to ventilation or moisture levels in attics. See *id.*

10. Although the manufacturers did not disclose the defective condition of the FRT plywood, the public learned of its dangers on April 11, 1990, most notably through a front page article in the *New York Times*. See Iver Peterson, *A Plywood Used in Many Homes Is Found to Decay in a Few Years*, N.Y. TIMES, Apr. 11, 1990, at A1.

11. See, e.g., *Cintron v. Osmose Wood Preserving, Inc.*, 681 So. 2d 859, 860 (Fla. Dist. Ct. App. 1996) (alleging personal injuries suffered by a homeowner working on a roof who fell through the roof constructed of FRT plywood); *Citizens Ins. Co. v. Osmose Wood Preserving, Inc.*, 585 N.W.2d 314, 315 (Mich. Ct. App. 1998) (alleging FRT-plywood roof collapsed on business); *King-Bradwall Partnership v. Johnson Controls, Inc.*, 865 S.W.2d 18, 20 (Tenn. Ct. App. 1993) (seeking recovery from the manufacturer for damage to a roof after a worker fell through a roof constructed of FRT plywood); see also *Morris*, 667 A.2d at 629 n.3 (alleging instances of homeowners falling through roofs constructed of FRT plywood and further, that local fire depart-

homeowners and builders sought to recover the cost to repair or replace the roof—a classic example of purely economic loss.¹² In each case, the plaintiff(s) alleged that the defendants' misrepresentations as to the suitability of FRT plywood as roofing material induced the purchase of the product.¹³

The Maryland courts dismissed the homeowners' negligent misrepresentation claims because the "plaintiffs [could not] recover in tort for . . . purely economic losses,"¹⁴ even when privity of contract barred the plaintiffs' contract claims.¹⁵ While Maryland law would permit recovery if the FRT-plywood roof had collapsed and damaged other property¹⁶ (e.g., the contents of the home), Michigan law does not provide such an exception.¹⁷ When a Michigan restaurateur's FRT-plywood roof collapsed and destroyed his business, the Michigan courts dismissed his fraud claim because "the UCC provide[d] the exclusive remedy."¹⁸ Because the defective FRT plywood did not deteriorate and destroy his business within the UCC's four-year statute of limitations, no remedy was available.¹⁹

Although Maryland and Michigan courts afforded no recovery, Florida courts allowed a homebuilder's negligent misrepresentation and fraud claims that sought to recover the cost of replacing

ments cautioned fire fighters not to walk on roofs containing FRT plywood).

12. For further discussion of the meaning of economic loss, see *infra* notes 27-36 and accompanying text.

13. See *Cintron*, 681 So. 2d at 862; *Morris*, 667 A.2d at 629; *Citizens Ins.*, 585 N.W.2d at 317; *King-Bradwall Partnership*, 865 S.W.2d at 20.

14. *Morris*, 667 A.2d at 631.

15. The homeowners had purchased homes that contained FRT-plywood roofs. Accordingly, the plaintiffs were not in privity with the manufacturer and the court held that a product sold as part of a constructed home did not constitute a consumer product. See *id.* at 637-38.

16. See *id.* at 630 (noting that under Maryland law, the economic loss rule does not apply where a defective product has damaged other property).

17. See *Citizens Ins.*, 585 N.W.2d at 316 ("Unlike some jurisdictions, the economic loss doctrine applies in Michigan even when the plaintiff is seeking to recover for property other than the product itself").

18. *Id.*

19. See *id.* at 317. Unless the restaurateur knew of the product defect prior to the roof crashing in, the statute of limitations would not have barred the tort claim because, unlike a contract claim in which the statute of limitations begins to run from the date of delivery, a tort claim's statute of limitations runs from the date on which the plaintiff discovered or should have discovered the defect. See *infra* notes 238-44 and accompanying text.

all the FRT plywood in homes the home builder had constructed.²⁰ The Florida economic loss rule barred claims for strict liability and negligence, but did not apply to torts that were independent of the contract, such as fraud and negligent misrepresentation, even when warranty law also afforded recovery.²¹ Although the Florida plaintiff's claims were nearly identical to those of the Maryland homeowners, the economic loss rule did not apply.²² Similarly, Virginia law allowed homeowners' fraud claims,²³ even though the condominium owners also had a viable contract claim.²⁴ Unlike Florida, the Virginia economic loss rule would have barred negligent misrepresentation claims.²⁵ Finally, Alabama allowed an architect's fraud and negligent misrepresentation claims seeking purely economic losses without any mention of the economic loss rule.²⁶

As the FRT plywood cases demonstrate, states do not apply the economic loss rule uniformly to nearly identical fraud and negligent misrepresentation claims. The first section of this Note

20. See *Pulte Home Corp. v. Osmose Wood Preserving, Inc.*, 60 F.3d 734, 738 (11th Cir. 1995).

21. See *id.* at 742; see also *id.* at 738 n.13 (noting that Florida law treated the fraud and misrepresentation claims identically).

22. See *id.* at 742. The plaintiff's misrepresentation claims ultimately failed, because the court concluded that the plaintiff had failed to prove the misrepresentation claims, not because they were barred by the economic loss rule. See *id.*

23. See *Providence Village Townhouse Condominium Ass'n v. Amurcon-Loudoun Corp.*, No. 12206, 1994 WL 740045, at *5 (Va. Cir. Ct. Jan. 19, 1994). Although the plaintiff's fraud claims were dismissed for failing to plead with sufficient specificity, the dismissal was with leave to plead. See *id.*

24. See *id.* at *4. In contrast to the law in Michigan or Maryland, the Virginia UCC does not require privity between the plaintiff and the defendant for the plaintiff to recover under a breach of warranty theory, so long as the plaintiff is someone whom the manufacturer or seller might reasonably have expected to use, consume, or be affected by the goods. See *id.* (quoting VA. CODE ANN. § 8.2-318 (Michie 1991)).

25. See *Tidemark Bank for Sav., F.S.B. v. Morris*, No. 94-1598, 1995 U.S. App. LEXIS 15170, at *11 (1st Cir. June 19, 1995) ("Virginia has chosen not to recognize tort claims to recover purely economic loss for negligently supplied misinformation absent privity between the parties." (citing *Ward v. Ernst & Young*, 435 S.E.2d 628, 631-32 (Va. 1993) (finding that unlike fraud, negligent misrepresentation is not an exception to the economic loss rule))).

26. See *Chambless-Killingsworth & Assocs., P.C. v. Osmose Wood Preserving, Inc.*, 695 So. 2d 25 (Ala. Civ. App. 1996). The architect sought recovery for damages to his business reputation and loss of income as a result of the architect's use of FRT plywood in a local school. See *id.* at 27.

provides a general overview of the economic loss rule and its rationale. The second and third sections examine the application of the economic loss rule to fraud and negligent misrepresentation claims respectively. The fourth section analyzes these rules and suggests a rule that is the most consistent with both the purpose of the economic loss rule and the tort of misrepresentation.

AN OVERVIEW OF THE ECONOMIC LOSS RULE

Defining an "Economic Loss"

Generally, the phrase "economic loss" is defined as losses other than those resulting from an injury to the plaintiff's person or other property.²⁷ Economic loss is divided further into direct and consequential, or indirect, economic loss.²⁸ Direct economic loss is the difference between the value of the contract or product as promised, and the actual value as delivered.²⁹ In the context of products liability, direct economic loss occurs when a product is damaged and the buyer seeks to recover the price of the product.³⁰ Direct economic loss can be measured in several ways. First, an "out-of-pocket" loss provides recovery for the difference in value between what is given and what is received.³¹ Second, "repair costs" provide the cost of replacement or repair to a product that is not delivered as promised.³² Third, the "benefit of the bargain" approach measures the difference between the value of what is received and the value as repre-

27. See *Rich Prods. Corp. v. Kemutec, Inc.*, 66 F. Supp. 2d 937, 968 (E.D. Wis. 1999); see also *Miller v. United States Steel Corp.*, 902 F.2d 573, 574 (7th Cir. 1990) (distinguishing the "economic loss" cost of "replacing a defective product . . . from an injury to the plaintiff's person or property").

28. See Note, *Economic Loss in Products Liability Jurisprudence*, 66 COLUM. L. REV. 917, 918 (1966) [hereinafter Note, *Economic Loss*]; see also Comment, *Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages—Tort or Contract?*, 114 U. PA. L. REV. 539, 541-42 (1966) (discussing judicial application of the economic loss principle). Courts frequently cite these two articles for a definition of a purely economic loss. See, e.g., *Redarowicz v. Ohlendorf*, 441 N.E.2d 324, 327 (Ill. 1982); *Northridge Co. v. W.R. Grace & Co.*, 471 N.W.2d 179, 181 (Wis. 1991).

29. See Note, *Economic Loss*, *supra* note 28, at 918.

30. See *Moorman Mfg. Co. v. National Tank Co.*, 414 N.E.2d 1302, 1305 (Ill. App. Ct. 1980), *overruled on other grounds*, 435 N.E.2d 443 (Ill. 1982).

31. See Note, *Economic Loss*, *supra* note 28, at 918.

32. See *id.*

sented.³³ Consequential or indirect economic loss consists of an injury extrinsic to the product and attributable to the product defect, such as lost profits resulting from the inability to make use of the product.³⁴

As Judge Posner has explained, the term "economic loss" is a misnomer: "It would be better to call it a 'commercial loss,' . . . because personal injuries and especially property losses are economic losses, too—they destroy values which can be and are monetized. . . ."³⁵ Commercial losses are not confined to transactions involving business entities; rather, the term encompasses any contractual dispute involving disappointed economic expectations.³⁶

The Economic Loss Rule

The economic loss rule is a judicially created doctrine,³⁷ first articulated by the California Supreme Court in *Seely v. White Motor Co.*³⁸ In *Seely*, the plaintiff sought damages resulting from the purchase of a defective truck.³⁹ The plaintiff suffered no

33. See *id.*

34. See *Moorman Mfg.*, 414 N.E.2d at 1305; see also *Seely v. White Motor Co.*, 403 P.2d 145 (Cal. 1965) (upholding the plaintiff's recovery of lost profits); Note, *Economic Loss*, *supra* note 28, at 918 ("Consequential economic loss includes all direct loss, such as loss of profits resulting from inability to make use of the defective product.").

35. *Miller v. United States Steel Corp.*, 902 F.2d 573, 574 (7th Cir. 1990). The term "commercial loss" did not originate with Posner. The *Seely* decision described the damages sought by a plaintiff as "commercial losses" (and interchangeably "economic losses"), see *Seely*, 403 P.2d at 150, as have other courts adopting the economic loss rule, see, e.g., *Nobility Homes, Inc. v. Shivers*, 557 S.W.2d 77, 80 (Tex. 1977).

36. See *Rich Prods. Corp. v. Kemutec, Inc.*, 66 F. Supp. 2d 937, 968 (E.D. Wis. 1999) (explaining that "commercial injuries are the type on which a breach of contract or breach of warranty suit is based").

37. The "economic loss rule" is also referred to as the "economic loss doctrine." Whatever the name, the principle is the same.

38. 403 P.2d 145 (Cal. 1965); see also *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1169 n.12 (3d Cir. 1981) (identifying *Seely* as the leading case propounding the economic loss rule). Although *Seely* is the best known case, it was not the first case to find that a plaintiff could not "sue directly the manufacturer [in negligence] . . . for damage limited to the allegedly defective product itself." *Trans World Airlines, Inc. v. Curtiss-Wright Corp.*, 148 N.Y.S.2d 284, 287 (Sup. Ct. 1955).

39. See *Seely*, 403 P.2d at 147.

personal injury damages in the accident, but sought damages for the repair of the truck, the purchase price of the truck, and lost profits because of an inability to use the truck.⁴⁰ Recognizing the overlap between products liability and contract law, the *Seely* court held that in the absence of personal injuries or physical injury to property other than to the product, a buyer's sole remedy lay in warranty, not strict liability or negligence.⁴¹

Today, courts routinely apply the economic loss rule to both strict liability and negligence claims.⁴² The economic loss rule, simply stated, is as follows:

"[W]here a purchaser's expectations in a sale are frustrated because the product he bought is not working properly, his remedy is said to be in contract alone, for he has suffered only 'economic' losses." *This doctrine hinges on a distinction drawn between transactions involving the sale of goods for commercial purposes where economic expectations are protected by commercial and contract law, and those involving the sale of defective products to individual consumers who are injured in a manner which has traditionally been remedied by resort to the law of torts.*⁴³

The rule requires a purchaser to recover in contract for purely economic loss due to disappointed expectations, unless he can

40. See *id.* at 147-48.

41. See *id.* at 150-51. Although a negligence claim was not before the court, the *Seely* court nonetheless concluded that "[e]ven in actions for negligence . . . there is no recovery for economic loss alone." *Id.* at 151; see also David B. Gaebler, *Negligence, Economic Loss, and the U.C.C.*, 61 IND. L.J. 593, 620-21 (1986) ("Ironically . . . *Seely* reaches this question only in dictum. . . . In the twenty years since the *Seely* decision, this dictum has been cited so frequently to deny tort recovery of economic loss in products cases that it seems almost to be the foundation of the rule.").

42. See, e.g., *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858, 871 (1986) (finding that, in admiralty law, no recovery exists under a negligence or strict products liability theory when a defective product only injures itself); *Transport Corp. of Am., Inc. v. IBM*, 30 F.3d 953, 956 (8th Cir. 1994) ("The economic loss doctrine in Minnesota bars recovery under the tort theories of negligence or strict liability for economic losses. . . ."); *S.M. Wilson & Co. v. Smith Int'l, Inc.*, 587 F.2d 1363, 1376 (9th Cir. 1978) ("Whether the complaint is cast in terms of strict liability in tort or negligence should make no difference.").

43. *Neibarger v. Universal Coops., Inc.*, 486 N.W.2d 612, 615 (Mich. 1992) (emphases added) (quoting *Kershaw County Bd. of Educ. v. United States Gypsum Co.*, 396 S.E.2d 369, 371 (S.C. 1990)); accord *East River S.S.*, 476 U.S. at 858; *Seely*, 403 P.2d at 145.

demonstrate harm above and beyond a broken contractual promise.⁴⁴ Quite simply, the economic loss rule "prevent[s] the law of contract and the law of tort from dissolving one into the other."⁴⁵

Rationale for the Economic Loss Rule

The distinction drawn by the economic loss rule reaches to the heart of the differences between the underlying purposes of tort and contract law.⁴⁶ The distinction between tort and contract law rests upon the source of the duty,⁴⁷ the role that the parties' play in determining their rights and responsibilities,⁴⁸ and the time at which duties and obligations are determined.⁴⁹

Contract law is individualistic because contractual duties and assignment of risk arise from agreements between the parties.⁵⁰ Contract law operates on the premise that contracting parties, in the course of bargaining for terms of a sale, are able to allocate risks and costs of the potential nonperformance.⁵¹ The underlying assumption is that the contract is the result of an arms-length negotiated transaction.⁵² In a negotiated transaction, the buyer either may insist on additional warranties or may assume a greater risk in exchange for a lower price.⁵³

44. See *Redarowicz v. Ohlendorf*, 441 N.E.2d 324, 327 (Ill. 1982); see also *East River S.S.*, 476 U.S. at 873, 874 n.9 (explaining that, whereas contract damages generally protect the benefit of the bargain, tort damages are more analogous to reliance damages).

45. *Rich Prods. Corp. v. Kemutec, Inc.*, 66 F. Supp. 2d 937, 968 (E.D. Wis. 1999).

46. See *Twin Disc, Inc. v. Big Bud Tractor, Inc.*, 772 F.2d 1329, 1332 (7th Cir. 1985).

47. See, e.g., *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1169 (3d Cir. 1981).

48. See *St. Denis v. Department of Hous. & Urban Dev.*, 900 F. Supp. 1194, 1202 n.11 (D. Alaska 1995); see also *Neibarger*, 486 N.W.2d at 615 (explaining that tort law "protects society's interest in freedom from harm" while contract law protects "society's interest in the performance of promises" (quoting *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 489 A.2d 660, 672 (N.J. 1985))).

49. See *St. Denis*, 900 F. Supp. at 1202 n.11.

50. See *id.*

51. See *Neibarger*, 486 N.W.2d at 615.

52. See *Detroit Edison Co. v. NABCO, Inc.*, 35 F.3d 236, 240 (6th Cir. 1994); see also *Clark v. Rowe*, 701 N.E.2d 624, 626 (Mass. 1998) ("When the economic loss rule has been applied, the parties usually were in a position to bargain freely concerning the allocation of risk. . . .").

53. See *Detroit Edison*, 35 F.3d at 240.

In contrast, tort law is paternalistic because tort duties arise from policy considerations with little or no regard to whether an agreement exists between the parties.⁵⁴ As a general proposition, "[t]ort law . . . governs the relationship between a [buyer] and a [seller], where it is impractical or impossible . . . to negotiate either the terms of a sale or each party's duty to the other."⁵⁵ Thus, tort duties arise to protect individuals unable to protect themselves from the unscrupulous actions of others and irrespective of the existence of a contract.

Both a contract claim and a tort claim, however, may arise from the same conduct.⁵⁶ For example, when a defective product physically harms the purchaser or his property, recovery is provided in both tort and contract.⁵⁷ To the extent that the legal theories overlap, they are said to be competing interests.⁵⁸ The purpose of the economic loss rule is not to bar the recovery of economic losses but is to prevent parties from recovering in tort to extricate themselves from prior freely negotiated agreements.⁵⁹

The economic loss rule applies where the duties owed are created solely by contract.⁶⁰ The focus of whether a plaintiff may maintain an action in tort for purely economic losses turns on the source of the duty that the plaintiff claims the defendant owed.⁶¹ If the duty arises merely out of the parties' agreement, then the proper remedy is in contract;⁶² if the duty arises inde-

54. See *St. Denis*, 900 F. Supp. at 1202 n.11; *Neibarger*, 486 N.W.2d at 616.

55. *Detroit Edison*, 35 F.3d at 239.

56. See *Roebber Films v. American Airlines*, No. 85-Civ-1072, 1989 U.S. Dist. LEXIS 10998, at *7 n.4 (S.D.N.Y. Sept. 19, 1989) (citing *Carmania Corp., N.V. v. Hambrecht Terrell Int'l*, 705 F. Supp. 936, 938 n.1 (S.D.N.Y. 1989)).

57. See *Kershaw County Bd. of Educ. v. United States Gypsum Co.*, 396 S.E.2d 369, 371 (S.C. 1990) (quoting *Kennedy v. Columbia Lumber & Mfg. Co.*, 384 S.E.2d 730, 736 (S.C. 1989)).

58. See *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 489 A.2d 660 (N.J. 1985).

59. See *In re Consolidated Vista Hills Retaining Wall Litig.*, 893 P.2d 438, 446 (N.M. 1995).

60. See *Kennedy v. Columbia Lumber & Mfg. Co.*, 384 S.E.2d 730, 737 (S.C. 1989).

61. See *Tommy L. Griffin Plumbing & Heating Co. v. Jordan, Jones & Goulding, Inc.*, 463 S.E.2d 85, 88 (S.C. 1995).

62. Framed another way, the conduct must be tortious despite the existence of a contract. See *Hargrave v. Oki Nursery, Inc.*, 636 F.2d 897, 899 (2d Cir. 1980).

pends on any contractual duties, then the proper remedy is in tort.⁶³

The economic loss doctrine relies on three rationales to preserve contract law as a generally superior remedy for breaches resulting solely in economic loss.⁶⁴ An overview of these principles and rationales serves to illuminate when the doctrine should be applied to misrepresentation claims. First, contract law permits the parties to negotiate the allocation of risk.⁶⁵ As parties to a contract are better suited to allocate risk and negotiate terms of the contract,⁶⁶ courts should not interfere when equally positioned parties fairly negotiate a contract.⁶⁷ In such situations, parties to a contract do not need the special protections of tort law.⁶⁸ Indeed, permitting parties to sue in tort over a contract dispute allows the parties to rewrite the agreement by allowing a party to recoup a benefit that was not part of the bargain.⁶⁹ By refusing to extricate parties from the bargains that

63. See *id.*

64. Some commentators and courts have criticized these underlying assumptions, or the application of the economic loss rule when the assumptions are not present, particularly in nonnegotiated or noncommercial cases. See, e.g., *Moorman Mfg. Co. v. National Tank Co.*, 414 N.E.2d 1302, 1307 (Ill. App. Ct. 1980) ("[A] personal injury is not necessarily a more overwhelming misfortune . . . than is an economic loss."), *aff'd in part, rev'd in part*, 435 N.E.2d 443 (Ill. 1982); cf. *Utah Int'l, Inc. v. Caterpillar Tractor Co.*, 775 P.2d 741, 744 (N.M. Ct. App. 1989) (applying the economic loss rule only "when there is no great disparity in bargaining power").

65. See *Terry's Floor Fashions, Inc. v. Georgia-Pacific Corp.*, 36 U.C.C. Rep. Serv. 2d (CBC) 680, 683-684 (E.D.N.C. July 23, 1998).

66. See *South Carolina Elec. & Gas Co. v. Westinghouse Elec. Corp.*, 826 F. Supp. 1549, 1557 (D.S.C. 1993). "Even where the law acts to assign risk through implied warranties," risk may be shifted through the use of disclaimers. 2000 Watermark Ass'n v. Celotex Corp., 784 F.2d 1183, 1185-86 (4th Cir. 1986).

67. See *City of Richmond v. Madison Management Group, Inc.*, 918 F.2d 438, 446 (4th Cir. 1990); *In re Consol. Vista Hills Retaining Wall Litig.*, 893 P.2d 438, 446 (N.M. 1995).

68. See *South Carolina Elec. & Gas Co.*, 826 F. Supp. at 1557.

69. Judge Crabb explained in *Stoughton Trailers, Inc. v. Henkel Corp.*, 965 F. Supp. 1227 (W.D. Wis. 1997) that:

Commercial entities are capable of bargaining to allocate the risk of loss inherent in any commercial transaction. Courts should assume that parties factor risk allocation into their agreements and that the absence of comprehensive warranties is reflected in the price paid. Permitting parties to sue in tort when the deal goes awry rewrites the agreement by allowing a party to recoup a benefit that was not part of the bargain.

Id. at 1230.

they have struck, the economic loss rule encourages parties to consider the possibility that the product will not perform properly and either assign risk or negotiate the price accordingly.⁷⁰ Consequently, contract damages are limited to those within the contemplation of the parties framing their agreement.

Second, in the event of a breach, the UCC and contract law are better suited to remedy disappointed economic expectations.⁷¹ The essence of the UCC is to provide a complete and independent statutory scheme to govern all commercial transactions resulting from a party's *failure to perform a contract*.⁷² Allowing a plaintiff a choice of recovery would undermine the need for contract law, because plaintiffs find tort remedies more attractive.⁷³ Consequently, tort law would swallow the carefully construed rules of the UCC and contract law.

Finally, preventing parties from extricating themselves from freely bargained contracts also prevents unending liability.⁷⁴ The economic consequences of any single accident are virtually limitless,⁷⁵ and thus, "[i]f defendants were held liable for every economic effect of their negligence, they would face virtually uninsurable risks far out of proportion to their culpability, and far greater than is necessary to encourage . . . care in their endeavors."⁷⁶ Such unending liability would decrease certainty and

70. See *Detroit Edison Co. v. NABCO, Inc.*, 35 F.3d 236, 239 (6th Cir. 1994).

71. See *Neibarger v. Universal Coops., Inc.*, 486 N.W.2d 612, 615 (Mich. 1992) ("Contract principles . . . are generally more appropriate for determining claims for consequential damage that the parties have, or could have, addressed in their agreement." (quoting *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 489 A.2d 660, 672 (N.J. 1985))).

72. See *Hapka v. Paquin Farms*, 458 N.W.2d 683, 688 (Minn. 1990). The UCC was *not*, however, designed to eliminate a cause of action for fraud or misrepresentation as the Code specifically contemplates additional causes of action for fraud and misrepresentation. See U.C.C. §§ 1-103, 2-721 (1999); *infra* notes 254-60 and accompanying text.

73. See *Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d 1244, 1245 (Fla. 1993). Generally, plaintiffs prefer tort because it permits greater damages and avoids the restrictions of contract. See *id.*

74. See *id.* at 1247; Christopher Scott D'Angelo, *The Economic Loss Doctrine: Saving Contract Warranty Law from Drowning in a Sea of Torts*, 26 U. Tol. L. Rev. 591, 594-95 (1995).

75. See *In re Chicago Flood Litig.*, 680 N.E.2d 265, 274 (Ill. 1997).

76. *Id.* (alteration in original) (internal quotation marks omitted). It is debatable that such liability would be "unending" as tort law also requires that damages be

predictability in allocating risk,⁷⁷ and thereby impede future business activity and contract negotiation.⁷⁸ At the bottom of all the rationales is one simple principle: "The economic loss doctrine helps ensure that contract claims are resolved by contract law."⁷⁹

Status of the Economic Loss Rule Today

The U.S. Supreme Court first considered the economic loss rule in the context of admiralty law in *East River Steamship Corp. v. TransAmerica Delaval Inc.*⁸⁰ In a unanimous decision, the Court recognized the importance of products liability in protecting people from dangerous products, but also emphasized that if products liability "were allowed to progress too far, contract law would drown in a sea of tort."⁸¹ Accordingly, the Court adopted the economic loss rule and held that a manufacturer in a commercial relationship could not be held liable "under either a negligence or strict products-liability theory" to the buyer for purely economic losses.⁸² The Court, however, explicitly refused to resolve whether the economic loss rule applied to all tort actions in admiralty.⁸³ Clearly, the Court left open the question of whether the economic loss rule applied to misrepresentation.

Following *East River*, state courts increasingly adopted the economic loss rule.⁸⁴ A few states have declined to follow the

proximately caused, or foreseeable. See *infra* text accompanying notes 250-53.

77. See *Griffith v. Centex Real Estate Corp.*, 969 P.2d 486, 491 (Wash. Ct. App. 1998), review denied, 980 P.2d 1283 (Wash. 1999).

78. See *id.*

79. *Dinsmore Instrument Co. v. Bombardier, Inc.*, 199 F.3d 318, 320 (6th Cir. 1999).

80. 476 U.S. 858 (1986). In *Saratoga Fishing Co. v. J.M. Martinac & Co.*, 520 U.S. 875 (1997), the Court recently affirmed and explained further the holding of *East River* as it applies to other property. See *id.* at 876-82.

81. *East River*, 476 U.S. at 866 (citing GRANT GILMORE, *THE DEATH OF CONTRACT* 87-94 (1974)).

82. *Id.* at 871.

83. See *id.* at 871 n.6.

84. See *Duquesne Light Co. v. Westinghouse Elec. Corp.*, 66 F.3d 604, 618 (3d Cir. 1995) ("[A]pplication of the [economic loss rule] gained momentum when the Supreme Court adopted it in the context of admiralty products liability law."). After *East River*, the leading opponent of the economic loss rule, the Supreme Court of New Jersey revisited its twenty-year-old rejection of the economic loss rule in *Santor v. A&M Karagheusian*, 207 A.2d 305 (N.J. 1965). In *Spring Motors Distributors, Inc.*

economic loss doctrine,⁸⁵ but the overwhelming majority of jurisdictions have adopted the economic loss doctrine in one variation or another.⁸⁶ These variations generally concern whether the economic loss rule applies (1) to "ordinary consumers,"⁸⁷ (2) to a

v. Ford Motor Co., 489 A.2d 660 (N.J. 1985), the New Jersey Supreme Court concluded that a commercial buyer's remedies for economic losses were restricted to those provided by contract law. *See id.* at 671-73. Then in *Alloway v. General Marine Industries, L.P.*, 695 A.2d 264 (N.J. 1997), the New Jersey Supreme Court concluded that allowing a consumer to recover purely economic losses in tort was no longer necessary. *See id.* at 275.

85. *See, e.g.*, *Blagg v. Fred Hunt Co.*, 612 S.W.2d 321, 323-24 (Ark. 1981); *Alloway*, 695 A.2d at 271 ("Only a handful of jurisdictions have followed *Santor*" in rejecting the economic loss rule); *Sterner Aero AB v. Page Airmotive, Inc.*, 499 F.2d 709 (10th Cir. 1974) (applying Oklahoma law). Some states that initially adopted *Santor* were overruled by their legislatures. *See, e.g.*, *Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1*, 881 P.2d 986, 990 (Wash. 1994) (stating that the legislature had overruled the Washington Supreme Court's adoption of *Santor*). More commonly, courts that once adopted the *Santor* rule later adopted the economic loss doctrine. *Compare Cova v. Harley Davidson Motor Co.*, 182 N.W.2d 800, 804 (Mich. Ct. App. 1970) (adopting the *Santor* rule), *with Neibarger v. Universal Coops., Inc.*, 486 N.W.2d 612, 618 (Mich. 1992) (adopting the economic loss doctrine). The continuing validity of the minority position found in *Santor* remains suspect as an increasing number of lower courts adopt the economic loss rule, despite prior decisions allowing recovery of purely economic loss in tort. *Compare Hiigel v. General Motors Corp.*, 544 P.2d 983, 989 (Colo. 1975) (adopting *Santor*), *with Terrones v. Tapia*, 967 P.2d 216, 220 (Colo. Ct. App. 1998) (applying the economic loss rule), *and Jardel Enters., Inc. v. Triconsultants, Inc.*, 770 P.2d 1301, 1303-04 (Colo. Ct. App. 1988) (adopting the economic loss rule); *compare C&S Fuel, Inc. v. Clark Equip. Co.*, 524 F. Supp. 949 (E.D. Ky. 1981) (allowing recovery of economic loss in tort), *with Bowling Green Mun. Utils. v. Thomasson Lumber Co.*, 902 F. Supp. 134, 136 (W.D. Ky. 1995) (applying the economic loss rule only in a commercial setting).

86. *See Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d 1244, 1246 n.2 (Fla. 1993).

87. *Cf. East River*, 476 U.S. at 869 n.4 (1986) ("Interestingly, the New Jersey and California Supreme Courts have each taken what appears to be a step in the direction of the other since *Santor* and *Seely*"). For an overview of states adopting a consumer exception, see, for example, *Minnesota Forest Prods., Inc., v. Ligna Mach., Inc.*, 17 F. Supp. 2d 892, 902 (D. Minn. 1998) ("Minnesota law limits recovery for economic loss that arises from the sale of goods in a commercial setting."); *Mainline Tractor & Equip. Co. v. Nutrite Corp.*, 937 F. Supp. 1095, 1104 (D. Vt. 1996) (holding that an ordinary consumer who suffers purely economic loss may recover under products liability theories of negligence or strict liability); *Lloyd Wood Coal Co. v. Clark Equip. Co.*, 543 So. 2d 671, 672 (Ala. 1989) (adopting the economic loss rule for "a claim solely for damage to the product itself . . . which was for commercial use, as opposed to consumer use"); *Lloyd F. Smith Co. v. Den-Tal-Ez, Inc.*, 491 N.W.2d 11, 17 (Minn. 1992) (recognizing a consumer exception); *Rousseau v. K.N. Constr., Inc.*, 727 A.2d 190, 193 (R.I. 1999) (limiting the economic loss rule to commercial transactions that do not involve consumers).

defective product that poses an unreasonable risk of harm, but has caused only economic loss to the product itself,⁸⁸ or (3) outside of a products liability context.⁸⁹ Although the rule originated in the context of products liability, the current trend expands the rule to apply in other contexts, most notably in real property transactions⁹⁰ and service contracts.⁹¹ As courts expand the economic loss rule outside of UCC transactions, the looming question is whether the economic loss rule applies to misrepresentation claims.

THE ECONOMIC LOSS RULE APPLIED TO FRAUD CLAIMS

Although the economic loss doctrine is now over thirty years old, its application to fraud claims is relatively recent.⁹² Prior to the adoption of the economic loss rule, courts routinely awarded purely economic damages when a defendant's misrepresentation induced a transaction.⁹³

88. See *Alloway*, 695 A.2d at 273. Although the RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 21 (1997) seemingly adopts the *Seely* analysis to exclude recovery under tort theories for damage to a product itself, the comments explain that "[a] plausible argument can be made that products that are dangerous [in these respects (i.e. discovery of the defect prevented harm from occurring or the only harm was to the product itself, but not to other persons or property)] rather than merely ineffectual, should be governed by the rules governing products liability law." *Id.* cmt. d.

89. See *Sebago, Inc. v. Beazer E., Inc.*, 18 F. Supp. 2d 70, 96 n.11 (D. Mass. 1998) ("Some jurisdictions have expressly limited the economic loss doctrine to product liability claims."). Compare *Cargill, Inc. v. Boag Cold Storage Warehouse, Inc.*, 71 F.3d 545, 550-51 (6th Cir. 1995) (holding that the economic loss doctrine applies only to products liability), and *Scap Motors, Inc. v. Pevco Sys. Int'l, Inc.*, No. CV 970348461S, 1999 WL 643378, at *2 (Conn. Super. Ct. Aug. 12, 1999) (refusing to apply the economic loss rule outside of products liability), with *Sun Co. v. Badger Design & Constructors, Inc.*, 939 F. Supp. 365, 372 (E.D. Pa. 1996) (rejecting the *Cargill* approach).

90. See, e.g., *Nastri v. Wood Bros. Homes, Inc.*, 690 P.2d 158, 164 (Ariz. Ct. App. 1984); *Casa Clara Condominium*, 620 So. 2d at 1244; *Redarowicz v. Ohlendorf*, 441 N.E.2d 324 (Ill. 1982).

91. See, e.g., *AFM Corp. v. Southern Bell Tel. & Tel. Co.*, 515 So. 2d 180 (Fla. 1987); *Anderson Elec., Inc. v. Ledbetter Erection Corp.*, 503 N.E.2d 246 (Ill. 1986).

92. "[O]nly a handful of jurisdictions" had addressed the issue before 1995. See *Huron Tool & Eng'g Co. v. Precision Consulting Servs., Inc.*, 532 N.W.2d 541, 544 (Mich. Ct. App. 1995); see also *Moorman Mfg. Co. v. National Tank Co.*, 414 N.E.2d 1302, 1306 (Ill. App. Ct. 1980) (considering and rejecting the application of the economic loss rule to fraud claims), *aff'd in part, rev'd in part*, 435 N.E.2d 443 (Ill. 1982).

93. See, e.g., *Haarberg v. Schneider*, 117 N.W.2d 796 (Neb. 1962) (finding that the

The rules for recovery in fraud inherently conflict with the economic loss rule. Fraud expressly allows for the recovery of purely economic losses arising out of a defendant's misrepresentations in a sale of goods or other property.⁹⁴ Conversely, the economic loss rule prohibits the recovery of purely economic losses in tort—particularly when the claim arises out of a contract.⁹⁵ The courts' struggle with this conflict can be categorized into three approaches.

Fraud: An Exception to the Economic Loss Rule

The first approach exempts fraud, or fraudulent inducement, from the economic loss rule based on three rationales.⁹⁶ The California Court of Appeals indirectly addressed this issue in *Kahn v. Shiley, Inc.*,⁹⁷ when the recipient of a defective heart valve alleged that the manufacturer's misrepresentations about the quality and durability of the heart valve induced her to purchase the product.⁹⁸ The court distinguished the other tort claims by explaining that, "[a]llegations of fraud . . . are in a

proper measure of damages in fraud is the difference between the value represented and the actual value); *Stewart v. Potter*, 104 P.2d 736 (N.M. 1940) (holding defrauded purchaser could recover the difference between the real and represented value of the automobile); *Clouse v. Chairtown Motors, Inc.*, 195 S.E.2d 327 (N.C. Ct. App. 1973) (allowing recovery of purely economic loss in fraud). In order to prove fraud, a plaintiff must show (1) a misrepresentation (false statement, concealment, or nondisclosure), (2) scienter (i.e., knowledge of falsity), (3) intent to defraud (i.e., induce reliance), (4) justifiable reliance, and (5) resulting damage. See, e.g., *Kahn v. Shiley, Inc.*, 266 Cal. Rptr. 106, 112 (1990); *KEETON ET AL.*, *supra* note 5, § 105, at 728, § 106, at 736-37.

94. See *KEETON ET AL.*, *supra* note 5, § 110, at 766.

95. See *supra* text accompanying notes 37-45.

96. See *Cunningham v. PFL Life Ins. Co.*, 42 F. Supp. 2d 872, 887 (N.D. Iowa 1999) ("In many jurisdictions, claims for fraud are an exception to the economic loss doctrine."); *Council of Unit Owners of Sea Colony E. v. Carl M. Freeman Assocs., Inc.*, Nos. 96C-AU-49, 86C-AU-50, 86C-AU-51, 86C-AU-52, 1990 Del. Super. LEXIS 412, at *15-16 (Oct. 16, 1990) ("Fraud is a recognized exception to the limitations of the economic loss doctrine.").

97. 266 Cal. Rptr. 106, 112 (Ct. App. 1990). Clearly, under California law, fraud includes the ability to recover purely economic losses. See *Alliance Mortgage Co. v. Rothwell*, 900 P.2d 601, 609 (Cal. 1995) (stating that the general rule in California is that a defrauded party is ordinarily entitled to "out-of-pocket" loss); *Continental Airlines, Inc. v. McDonnell Douglas Corp.*, 264 Cal. Rptr. 779 (Ct. App. 1989) (allowing recovery of purely economic loss for fraud arising out of a commercial contract).

98. See *Kahn*, 266 Cal. Rptr. at 108.

class by themselves. . . . Unlike the other theories, in which the safety and efficacy of the *product* is assailed, the fraud claim impugns defendants' *conduct*.⁹⁹ Rather, the *Kahn* court confirmed "that a manufacturer of a product may be liable for fraud when it" misleads potential users about material product information.¹⁰⁰ Thus, the viability of a fraud claim rests on the defendant's conduct and not on the type of damage or on the existence of an underlying contract.¹⁰¹ Clearly then, fraud allows the recovery of purely economic loss because the presence or absence of physical injury makes no difference.¹⁰²

By analyzing the source of the duty, the Texas Supreme Court utilized a similar rationale to conclude the economic loss rule did not apply to intentional misrepresentation.¹⁰³ In *Formosa Plastics Corp. v. Presidio Engineers & Contractors, Inc.*, the Texas Supreme Court distinguished an action in contract as breaching a duty arising out of the parties' agreement from a tort action that arises from a breach of a duty imposed by law.¹⁰⁴ Tort law "has long imposed a duty to abstain from inducing another to enter into a contract through the use of fraudulent misrepresentations."¹⁰⁵ As this duty is "separate and independent from the duties established by the contract itself,"¹⁰⁶ the economic loss

99. *Id.* at 112.

100. *Id.*

101. *See id.*; *see also Continental Airlines*, 264 Cal. Rptr. at 801 (allowing a fraud claim arising out of a contract between two commercial entities). The California Civil Code expressly declares unlawful "[a]ll contracts which . . . exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another" CAL. CIV. CODE § 1668 (West 1985).

102. *See Davis v. Shiley, Inc.*, 75 Cal. Rptr. 2d 826, 833 (Ct. App. 1998) (Sills, J., dissenting); *see also id.* at 828 n.3 (acknowledging the dissent's position on this issue as correct).

103. *See Formosa Plastics Corp. USA v. Presidio Eng'rs & Contractors, Inc.*, 960 S.W.2d 41 (Tex. 1998). Indeed, the *Formosa* court expressed disapproval at lower court decisions that overextended the economic loss rule. *See id.* at 47; *see also Eastman Chem. Co. v. Niro*, No. Civ. A G-99-623, 2000 WL 94931, at *5 (S.D. Tex. Jan. 24, 2000) (noting *Formosa's* disapproval of overextension by lower courts).

104. *See Formosa*, 960 S.W.2d at 45 (quoting *International Printing Pressmen & Assistants' Union v. Smith*, 198 S.W.2d 729, 735 (Tex. 1946)).

105. *Id.* at 46.

106. *Id.* Although the Texas Supreme Court has adopted an "independent injury" requirement for other torts, fraud is exempt from that requirement. *See Eastman*, 2000 WL 94931, at *5.

rule does not apply to fraud claims regardless of whether the duties were subsumed later into the contract, or the losses were purely economic.¹⁰⁷

In one of the earliest cases addressing the issue, *Moorman Manufacturing Co. v. National Tank Co.*,¹⁰⁸ the Illinois Supreme Court expended one sentence in affirming the decision of the court of appeals that intentional misrepresentations were outside the scope of the economic loss rule.¹⁰⁹ Rather than focus on the defendant's conduct, the court of appeals explained only that the "loss of the bargain" is the measure of damages for fraud:

Illinois courts have traditionally taken the position that "loss of bargain" is the measure of damages for misrepresentation. . . . [O]ur Supreme Court [has] stated: "In an action on the case for fraudulent representations in the sale of property, the measure of damages is the difference between the value of the property as it is and what it would be worth if the representations had been true."¹¹⁰

Since the time of the *Moorman* decision, the Illinois Supreme Court has clarified that "the concept of duty" is the rationale for this exception to the economic loss rule.¹¹¹ This approach treats fraud as an exception to the economic loss rule because (1) fraud impugns the defendant's conduct, (2) the source of the duty arises out of tort, not contract, and (3) the measure of damages for fraud is purely economic "benefit of the bargain" damages. Accordingly, a plaintiff may maintain both a fraud and a contract action simultaneously.¹¹²

107. See *Formosa*, 960 S.W.2d. at 46-47. Texas and Illinois are not alone in this analysis. See, e.g., *Tommy L. Griffin Plumbing & Heating Co. v. Jordan, Jones & Goulding, Inc.*, 463 S.E.2d 85, 89 (S.C. 1995) (recognizing that a breach of a duty arising independently of contractual duties may support a tort action for economic loss).

108. 435 N.E.2d 443 (Ill. 1982).

109. See *id.*

110. *Moorman Mfg. Co. v. National Tank Co.*, 414 N.E.2d 1302, 1312 (Ill. App. Ct. 1980) (quoting *Schwitters v. Springer*, 86 N.E. 102, 103 (Ill. 1908)), *overruled on other grounds*, 435 N.E.2d 443 (Ill. 1982).

111. 2314 Lincoln Park W. Condominium Ass'n v. Mann, Gin, Ebel & Frazier, Ltd., 555 N.E.2d 346, 351 (Ill. 1990).

112. See *Southwestern Bell Tel. Co. v. Delaney*, 809 S.W.2d 493, 499 (Tex. 1991) (explaining that even where a contract exists, "[i]f the defendant's conduct . . .

Fraud: A Limited Exception to the Economic Loss Rule

Despite the long-standing rule allowing recovery of purely economic loss damages in fraud cases, two states recently limited recovery in fraud cases to only those damages unrelated to an underlying contract. Indeed, the growing trend among courts is to craft a limited exception to claims for economic loss in fraud cases.¹¹³

The leading case advocating a limited exception for fraud is the Michigan Court of Appeals decision in *Huron Tool & Engineering Co. v. Precision Consulting Services, Inc.*¹¹⁴ Prior to *Huron Tool*, the Michigan Supreme Court adopted the economic loss rule in negligence cases¹¹⁵ and explained that "where a plaintiff seeks to recover for economic loss caused by a defective product purchased for commercial purposes, the exclusive remedy is provided by the UCC. . . ."¹¹⁶ In that context, the Michigan Court of Appeals addressed the application of the doctrine to actions for intentional torts, particularly fraud.¹¹⁷ Although the

give[s] rise to [independent] liability . . . the plaintiff's claim may also sound in tort"); see also *Nepomuceno v. Knights of Columbus*, No. Civ. A-96-C-4789, 1999 WL 66570, at *11 (N.D. Ill. Feb. 8, 1999) (allowing the plaintiffs to maintain fraud actions despite the existence of contract claims and losses that were purely economic); *Hoechst Celanese Corp. v. Arthur Bros., Inc.*, 882 S.W.2d 917 (Tex. Ct. App. 1994) (permitting recovery for fraud despite the existence of contract claims).

113. See *Concord Boat Corp. v. Brunswick Corp.*, No. LR-C-95-781, 1998 U.S. Dist. LEXIS 14565, at *6 (E.D. Ark. Apr. 7, 1998) ("There is a current trend allowing a limited exception to the economic loss doctrine for fraud where the claims at issue arise independent of the underlying contract."). The so-called *Huron Tool* rule has been adopted by courts in Florida, see *HTP, Ltd. v. Lineas Aereas Costarricenses*, 685 So. 2d 1238 (Fla. 1996), Minnesota, see *AKA Distrib. Co. v. Whirlpool Corp.*, 137 F.3d 1083 (8th Cir. 1998); *Marvin Lumber & Cedar Co. v. PPG Indus., Inc.*, 34 F. Supp. 2d 738 (D. Minn. 1999), South Carolina, see *South Carolina Elec. & Gas v. Westinghouse Elec.*, 826 F. Supp. 1549 (D.S.C. 1993), and Wisconsin, compare *Raytheon v. McGraw-Edison Co.*, 979 F. Supp. 858 (E.D. Wis. 1997) (adopting the rule), with *Budgetel Inns, Inc. v. Micros Sys., Inc.*, 8 F. Supp. 2d 1137 (E.D. Wis. 1998) (rejecting the rule), and *Budgetel Inns, Inc. v. Micros Sys., Inc.*, 34 F. Supp. 2d 720 (E.D. Wis. 1999) (denying reconsideration despite a split within the district).

114. 532 N.W.2d 541 (Mich. Ct. App. 1995); see *Budgetel*, 8 F. Supp. 2d at 1144 (stating that *Huron Tool* is the leading case).

115. See *Neibarger v. Universal Coops., Inc.*, 486 N.W.2d 612, 618 (Mich. 1992). Prior to *Neibarger*, lower courts in Michigan, as well as courts within the Sixth Circuit, had applied the economic loss doctrine for a number of years. See *id.* at 617.

116. *Id.* at 618.

117. See *Huron Tool*, 532 N.W.2d at 544-46.

Huron Tool court recognized that fraud in the inducement presented a special situation, because misrepresentations undermine the ability to negotiate freely,¹¹⁸ the court added an additional caveat: The fraud claim must be factually distinguishable.¹¹⁹ At first glance, this rule creates an exception for fraud claims. Yet the additional caveat requires that the misrepresentations be unrelated to the contract.¹²⁰ If the defendant's misrepresentations concerned the subject matter of the contract—the quality of the goods, for example—then they are said to be “interwoven” with the contract.¹²¹ If the fraud claim is “interwoven” with a contract claim, then no independent intentional misrepresentation exists. In such a case, the economic loss rule restricts the plaintiff to whatever contractual remedies exist.¹²²

The result in *Huron Tool* is perhaps the best example of how the Michigan rule operates. The *Huron Tool* plaintiffs convinced the court of appeals that fraud was an exception to the economic loss rule, but the misrepresentations at issue in the case concerned the quality and characteristics of the goods. Although the defendant's representations about the quality of the goods fraudulently induced the plaintiffs to contract, the court determined those claims to be indistinguishable from the terms of the contract.¹²³ Accordingly, because the fraud claims were not “independent,” the economic loss rule barred the fraud claims.¹²⁴

In formulating this rule, the *Huron Tool* court relied heavily on the parties' ability to negotiate the terms of *commercial* transactions.¹²⁵ Subsequent decisions have extended the rule to

118. *See id.* at 545.

119. *See id.* at 546.

120. *See id.* Even a fraud allegation concerning representations “made in connection with the making of a contract” has been interpreted to be “not extraneous to the contract.” *Dinsmore Instrument Co. v. Bombardier, Inc.*, 199 F.3d 318, 321 (6th Cir. 1999) (emphasis added) (quoting from Dinsmore's complaint).

121. *See Huron Tool*, 532 N.W.2d at 546.

122. *See id.*

123. *See id.*

124. *See id.*

125. *See id.* at 545. The court explained that the policy behind the doctrine “encourages parties to negotiate economic risks through warranty provisions and price.” *Id.* (quoting *Florida Power & Light Co. v. Westinghouse Elec. Corp.*, 510 So. 2d 899, 901 (Fla. 1987)). The court also concluded that the quality and characteristics of the goods were not extraneous to the contract because the parties were still free to

nonnegotiated transactions¹²⁶ and consumers.¹²⁷ Moreover, the practical effect of the additional requirement has rendered the exception a nullity.¹²⁸ No court correctly applying the *Huron Tool* rule has found that a misrepresentation was independent of the contract.¹²⁹

Florida nominally adopts the *Huron Tool* rule¹³⁰ in barring the recovery of purely economic losses. The crucial difference between how Florida and Michigan handle the application of the rule in misrepresentation cases lies in the decision of when the economic loss rule should apply. Rather than apply a per se rule, the Florida courts determine whether the economic loss rule applies to a fraudulent inducement claim on a case-by-case basis.¹³¹

The Florida Supreme Court recently acknowledged that its own "pronouncements on the economic loss rule have not always been clear."¹³² The lack of clarity of the Florida economic loss

negotiate the warranty and other terms in order to account for possible defects in the goods. *See id.*

126. *See* Citizens Ins. Co. v. Osmose Wood Preserving, Inc., 585 N.W.2d 314 (Mich. Ct. App. 1998) (finding no fraud in the inducement exception even when the buyer was not in a position to negotiate the terms of the sale); *see also id.* at 318 (Kelly, J., dissenting) (suggesting that the economic loss rule should apply only when the plaintiff is in the same business as the defendant and may anticipate properly the foreseeability of the risks involved).

127. *See, e.g.,* Parkhill v. Minnesota Mut. Life Ins. Co., 995 F. Supp. 983 (D. Minn. 1998) (applying the economic loss rule to fraud claims by consumers who purchased insurance policies).

128. *See* Budgetel Inns, Inc. v. Micros Sys., Inc., 8 F. Supp. 2d 1137, 1146-49 (E.D. Wis. 1998) (declining to adopt the *Huron* rule).

129. *See id.* at 1146 n.2.

130. *See* Pressman v. Wolf, 732 So. 2d 356, 361 (Fla. Dist. Ct. App. 1999) (explaining that "the [Florida] Supreme Court adopted the analysis and explanation in *Huron Tool*"). Though Florida has adopted the Michigan rule, *see* HTP, Ltd. v. Lineas Aereas Costarricenses, S.A., 685 So. 2d 1238, 1239 (Fla. 1996), it applied a similar rule even prior to *Huron Tool*, *see* Florida Power & Light Co. v. Westinghouse Elec. Corp., 510 So. 2d 899 (Fla. 1987) (holding that a party cannot recover in tort for economic losses incurred pursuant to the terms of a written contract).

131. *See* Force v. ITT Hartford Life & Annuity Ins. Co., 4 F. Supp. 2d 843, 852 (D. Minn. 1998) (applying Florida law and explaining that "Florida courts have not adopted a per se rule regarding whether the economic loss rule applies to claims of fraudulent inducement; rather, such a determination depends on the specifics of each case").

132. *Comptech Int'l, Inc. v. Milam Commerce Park, Ltd.*, Nos. 93,336, 93,126, 1999 WL 983857, at *5 (Fla. Oct. 28, 1999).

rule derives from conflicting statements in the supreme court decision in *HTP, Ltd. v. Lineas Aereas Costarricenses, S.A.*¹³³ The Florida Supreme Court recognized that fraudulent inducement "occurs prior to the contract and the standard of truthful representation placed upon the defendant is not derived from the contract,"¹³⁴ and explained that the "economic loss rule has not eliminated causes of action based upon torts independent of the contractual breach."¹³⁵ While the Florida Supreme Court recognized that fraudulent inducement was "an independent tort in that it requires proof of facts separate and distinct from the breach of contract,"¹³⁶ the court also adopted the analysis of *Huron Tool*¹³⁷ and stated that a tort action exists only for "intentional or negligent acts considered to be independent from acts that breached the contract."¹³⁸

A number of lower Florida courts have interpreted these conflicting statements to require a bar similar to the one that the *Huron Tool* court imposed: "[W]here the alleged fraudulent misrepresentations are inseparably embodied in the parties subsequent agreement."¹³⁹ Unlike Michigan courts, however, Florida courts recognize that a fraudulent inducement claim can coexist with a contract claim.¹⁴⁰ Nonetheless, the decision of the oft-quoted statement from the Florida Third District Court of Appeals demonstrates the conflicting concerns and interests of applying the economic loss doctrine to fraud claims:

133. 685 So. 2d 1238 (Fla. 1996).

134. *Id.* at 1239 (quoting *Woodson v. Martin*, 663 So. 2d 1327, 1331 (Fla. Dist. Ct. App. 1995) (en banc) (Altenbernd, J., dissenting)).

135. *Id.*

136. *Id.*

137. *See id.* at 1239-40.

138. *Id.* at 1239 (citations omitted) (emphasis added).

139. *Hotels of Key Largo, Inc. v. RHI Hotels, Inc.*, 694 So. 2d 74, 77 (Fla. Dist. Ct. App. 1997) (contending that certain fraudulent inducement claims are barred by the economic loss rule); cf. *supra* notes 114-24 and accompanying text (discussing the *Huron Tool* rule).

140. *See Force v. ITT Hartford Life & Annuity Ins. Co.*, 4 F. Supp. 2d 843, 852 (D. Minn. 1998) (interpreting Florida law and noting that "[t]he court in *HTP* . . . expressly rejected . . . [the idea that] fraudulent inducement claims cannot co-exist with breach of contract claims"); *Parkhill v. Minnesota Mut. Life Ins. Co.*, 995 F. Supp. 983, 993-94 (D. Minn. 1998) (interpreting Florida law and citing *HTP* to reach the same conclusion) *HTP*, 685 So. 2d at 1238-40 (rejecting *Woodson v. Martin*, 663 So. 2d 1327 (Fla. Dist. Ct. App. 1995) (en banc)).

It makes sense that a truly independent cause of action for fraudulent misrepresentation, where the ability of one party to negotiate fair terms is undermined by the other's fraudulent behavior, is not barred by the economic loss rule. However, where the only alleged misrepresentation concerns the heart of the parties' agreement, simply applying the label of "fraudulent inducement" to a cause of action will not suffice to subvert the sound policy rationales underlying the economic loss doctrine.¹⁴¹

These conflicting and unclear statements regarding application of the economic loss rule have led to a two-fold result. First, the Florida rule has sustained fraud as a viable cause of action, albeit through widely inconsistent results.¹⁴² Second, the Florida appellate courts have been deluged with a large number of cases on the applicability of the economic loss rule to fraud claims.¹⁴³

141. *Hotels of Key Largo*, 694 So. 2d at 77. Other Florida appellate panels accept the third district court of appeal's *Key Largo* pronouncement. See, e.g., *Wadlington v. Continental Med. Servs., Inc.*, 728 So. 2d 352, 353 (Fla. Dist. Ct. App. 1999) (Fourth District); *Ocean Ritz of Daytona Condominium v. GGV Assocs., Ltd.*, 710 So. 2d 702, 704 (Fla. Dist. Ct. App. 1998) (Fifth District). But see *Bradley Factor, Inc. v. United States*, No. 95-1147-CIV-T-176, 2000 WL 224618, at *5-6 (M.D. Fla. Feb. 8, 2000) (rejecting *Key Largo* in light of the *Budgetel* decision).

142. *Compare* *Pressman v. Wolf*, 732 So. 2d 356, 360 (Fla. Dist. Ct. App. 1999) (barring a fraud claim because a party may not recover in fraud for oral misrepresentations set forth in a written contract), *with* *Noack v. Blue Cross & Blue Shield of Fla., Inc.*, 742 So. 2d 433, 434 (Fla. Dist. Ct. App. 1999) (allowing a fraud claim because "the presence of a merger clause [is not] an impediment") (citing *Wilson v. Equitable Life Assurance Soc'y*, 662 So. 2d 25, 27 (Fla. Dist. Ct. App. 1993)); *compare* *Techni-Search v. Pathtech Software Solutions, Inc.*, 737 So. 2d 1133, 1136 (Fla. Dist. Ct. App. 1999) (finding "[a]s to the fraud claim . . . no amendment can get by the economic loss rule"), *with* *Davich v. Norman Bros. Nissan, Inc.*, 739 So. 2d 138, 141 (Fla. Dist. Ct. App. 1999) (finding "no merit in [defendant's] position that the economic loss rule bars [plaintiff's] counts for fraud"); *compare* *Watkins v. First Equity Corp.*, 743 So. 2d 525, 525 (Fla. Dist. Ct. App. 1999) (rejecting a contention that the relationship created by contract mandated the application of the economic loss rule), *with* *Williams v. Peak Resorts, Int'l, Inc.*, 676 So. 2d 513, 516-17 (Fla. Dist. Ct. App. 1996) (stating that a plaintiff may not recover under both contract and fraud theories unless the plaintiff proves separate damages for fraud), *and* *Clayton v. State Farm Mut. Auto. Ins. Co.*, 729 So. 2d 1012, 1013 (Fla. Dist. Ct. App. 1999) (explaining that when allegations of pre-contract misrepresentation are directly related to the breach, they do not support an independent tort action).

143. Florida easily has the largest number of judicial opinions discussing the application of the economic loss rule to fraud claims and quite often has conflicting opinions from the appellate courts on the issue.

To date, the Florida Supreme Court has not articulated a clear application of the economic loss rule to fraud claims.

Fraud: No Exception

A handful of courts have construed the economic loss rule to prohibit the recovery of purely economic losses in fraud. These courts conclude that because the economic loss rule bars recovery in tort, and because fraud is a tort, recovery of purely economic loss is therefore barred.¹⁴⁴ For example, in *Flagg Energy Development Corp. v. General Motors Corp. Allison Gas Turbine Division*,¹⁴⁵ a commercial plaintiff alleged that the defendant's misrepresentations about the quality of some engines fraudulently induced it to purchase them.¹⁴⁶ Connecticut law afforded recovery for purely economic loss in fraudulent inducement claims¹⁴⁷ and allowed a fraud claim in addition to a warranty claim.¹⁴⁸ The *Flagg Energy* court nonetheless distinguished prior fraud cases because they did not involve the sale of goods.¹⁴⁹ The Connecticut Supreme Court affirmed the trial court's reasoning that fraud claims cannot arise out of a transaction governed by the UCC.¹⁵⁰

144. See, e.g., *Nigrelli Sys., Inc. v. E.I. Dupont de Nemours & Co.*, 31 F. Supp. 2d 1134, 1138-39 (E.D. Wis. 1999) (analyzing a plaintiff's strict liability and fraud claims together and concluding that the economic loss rule applied "equally" to all the claims); *In re Ford Motor Co. Bronco II Prods. Liab. Litig.*, MDL-991, 1995 U.S. Dist. LEXIS 18207, at *21-*22 (E.D. La. Dec. 4, 1995) (construing the New York economic loss rule to bar fraud claims). The court in *Bronco II* relied solely on New York's adoption of the economic loss rule to conclude that New York law barred the recovery of economic losses in fraud. See *id.* The *Bronco II* and *Nigrelli* decisions are perhaps limited to products liability, because the cases involved defective products. See *id.* More importantly, the *Bronco II* court probably misconstrued New York law in determining that the economic loss rule would bar a fraud claim. See *Triangle Underwriters, Inc. v. Honeywell, Inc.*, 604 F.2d 737, 743-48 (2d Cir. 1979) (reversing district court's dismissal of a fraud claim that sought purely economic losses); see also *Triangle Underwriters, Inc. v. Honeywell, Inc.*, 651 F.2d 132 (2d Cir. 1981) (allowing damages after a jury verdict).

145. No. CV-92-02421985, 1993 Conn. Super. LEXIS 2624 (Oct. 1, 1993).

146. See *id.*

147. See CONN. GEN. STAT. ANN. § 42a-2-721 (West 1999).

148. See *id.* cmt.

149. See *Flagg Energy*, 1993 Conn. Super. LEXIS 2624, at *5-*10; see also *Unique Dimensions, Inc. v. Ralph Wilson Plastics Co.*, No. CV94-04-73-025, 1995 WL 404875 (Conn. Super. Ct. June 29, 1995) (reaching the same conclusion).

150. In *Flagg Energy Development Corp. v. General Motors Corp.*, 709 A.2d 1075

Although *Flagg Energy* involved a commercial purchaser in a fully negotiated transaction that was subject to the UCC, wholesale application of the economic loss rule to fraud is not limited to such cases. Courts have utilized similar rationales to apply the economic loss rule and bar fraud claims brought by consumer purchasers of defective products,¹⁵¹ and fraud claims unrelated to a sale of goods.¹⁵² The tacit directive of such decisions is to disallow fraud claims that do not seek damages for physical injury.

THE ECONOMIC LOSS RULE APPLIED TO NEGLIGENT MISREPRESENTATION

Unlike fraud, which has ancient roots in the common law,¹⁵³ negligent misrepresentation is a more recent development.¹⁵⁴

(Conn. 1998), the Connecticut Supreme Court reviewed the trial court's decision regarding a dispute over the settlement agreement. In concluding the settlement agreement in *Flagg Energy* did not extinguish the terms of the original contract, the Connecticut Supreme Court determined that the economic loss rule applied to fraud and negligent misrepresentation claims—at least those that the UCC governed. *See id.* at 1088-89; *Page v. Englander Millwork Co.*, No. CV9803329085, 1999 WL 311225, at *2 (Conn. Super. Ct. May 5, 1999) (explaining that the *Flagg Energy* decision held that claims of both negligent and fraudulent misrepresentation are inconsistent with "breach of contract and breach of warranty allegations under the [UCC]"); *see also Marvin Lumber & Cedar Co. v. PPG Indus., Inc.*, 34 F. Supp. 2d 738, 750 (D. Minn. 1999) (concluding that the Minnesota economic loss doctrine does not treat fraud differently when alleged in connection with an Article 2 contract). *But see Scap Motors, Inc. v. PEVCO Sys. Int'l, Inc.*, 1999 WL 643378, at *2 (Conn. Super. Ct. Aug. 12, 1999) (declining to apply the economic loss rule because the UCC did not govern the claims).

151. *See Page*, 1999 WL 311225, at *2-3 (dismissing the homeowner plaintiffs' fraudulent and negligent misrepresentation claims based on *Flagg Energy*); *see also Pryor v. Shiley, Inc.*, No. 89-3559, 1990 WL 159582, at *3 (9th Cir. Oct. 8, 1990) (affirming the dismissal of a consumer plaintiffs fraud claims because "Oregon treats all product liability actions the same, regardless of the theory asserted").

152. *See, e.g., PPG Indus., Inc. v. Sundstrand Corp.*, 681 F. Supp. 287, 290-91 (W.D. Pa. 1988). The dispute in *Sundstrand* centered around a professional services contract. The plaintiff alleged that the defendant made misrepresentations during their precontractual negotiations, thus suggesting a fraud in the inducement claim. *See id.* (discussing the preliminary proposals and "the arm's length nature of the negotiations"); *cf. Tommy L. Griffin Plumbing & Heating Co. v. Jordan, Jones & Goulding, Inc.*, 463 S.E.2d 85, 87 (S.C. 1995) ("[S]ome states use the 'economic loss' rule to prohibit all recovery of purely economic damages in tort.").

153. *See* 9 STUART M. SPEISER ET AL., *THE AMERICAN LAW OF TORTS* § 32:3 (1992).

154. *See id.* § 32:76.

The three approaches to negligent misrepresentation¹⁵⁵ all rest on the same basic principle, first explained by Justice Cardozo in *Glanzer v. Shepard*.¹⁵⁶ In *Glanzer*, the New York Court of Appeals held a public weigher liable to a third-party buyer of beans, because the weigher knew that the buyer would rely on the weigher's representations when purchasing the beans from the seller.¹⁵⁷ Justice Cardozo explained the court's reasoning:

[T]he law imposes a duty toward buyer as well as seller. . . . [A]ssumption of the task of weighing was the assumption of a duty to weigh carefully for the benefit of all whose conduct was to be governed. We do not need to state the duty in terms of contract or of privity. Growing out of a contract, it has none the less [sic] an origin not exclusively contractual. Given the contract and the relation, the duty is imposed by law.¹⁵⁸

Although a contractual relationship existed only between the buyer and the weigher, the law imposed a legal duty on the weigher to those who, like the bean buyer,¹⁵⁹ would foreseeably rely on his misrepresentations. Thus, negligent misrepresentation imposes a legal duty on those who supply information in the

155. The RESTATEMENT (SECOND) OF TORTS § 552 (1977) adopts the holding of *Glanzer v. Sheppard*, 135 N.E. 275 (N.Y. 1922), and provides in relevant part:

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

RESTATEMENT (SECOND) OF TORTS § 552. The akin-to-privity approach defines and limits the scope of the defendant's duty according to the defendant's state of mind and agreed upon expectation of the parties. See *Onita Pac. Corp. v. Trustees of Bronson*, 843 P.2d 890, 908 (Or. 1992). The foreseeability approach is an expansive approach that allows recovery to third parties "to the extent that damages incurred by non-clients are reasonably foreseeable." *First Nat'l Bank of Commerce v. Monco Agency Inc.*, 911 F.2d 1053, 1059 (5th Cir. 1990); see also *Scottish Heritage Trust v. Peat Marwick Main & Co.*, 81 F.3d 606, 612 (5th Cir. 1996) (comparing the three approaches).

156. 135 N.E. 275 (N.Y. 1922).

157. See *id.*

158. *Id.* at 275-76. In a later decision, Justice Cardozo made it clear that negligent misrepresentation was not a substitute for fraud. See *Ultramares Corp. v. Touche*, 174 N.E. 441 (N.Y. 1931).

159. See *Glanzer*, 135 N.E. at 275-76.

course of a business transaction in which they have a pecuniary interest.¹⁶⁰

A tension emerges between negligent misrepresentation, which allows for the recovery of pecuniary loss,¹⁶¹ and the economic loss rule, which forbids recovery of economic loss in tort.¹⁶² This tension has produced "substantial disagreement among the courts as to whether a claim for negligent misrepresentation should be recognized as an exception to the economic loss doctrine."¹⁶³ As with fraud, this tension has produced a variety of approaches to determine when the economic loss rule should apply to negligent misrepresentation.

Negligent Misrepresentation: An Exception Mirroring the Fraudulent Inducement Exception

The first approach to negligent misrepresentation treats the cause of action like fraud. Florida, the leading proponent of this view,¹⁶⁴ has fashioned its negligent misrepresentation exception

160. See *Sebago, Inc. v. Beazer E., Inc.*, 18 F. Supp. 2d 70, 95 n.10 (D. Mass. 1998) (citing section 552 of the *Restatement (Second) of Torts*).

161. See *South Carolina Elec. & Gas Co. v. Westinghouse Elec. Corp.*, 826 F. Supp. 1549, 1555 (D.S.C. 1993).

162. See *McCarthy, Lebit, Crystal & Haiman Co. v. First Union Management, Inc.*, 622 N.E.2d 1096, 1103 (Ohio Ct. App. 1993) ("'[P]ecuniary loss' is by its very definition 'economic loss.'").

163. Reeder R. Fox & Patrick J. Loftus, *Riding the Choppy Waters of East River: Economic Loss Doctrine Ten Years Later*, 64 DEF. COUNS. J. 260, 268 (1997); see also *Apollo Group, Inc. v. Avnet, Inc.*, 58 F.3d 477, 480 n.3 (9th Cir. 1995) ("There is no consensus among courts that have been squarely faced with this issue."); *John Martin Co. v. Morse/Diesel, Inc.*, 819 S.W.2d 428, 434 (Tenn. 1991) ("[T]here is no clear majority; instead, we find a split of authority among the states.").

164. Other jurisdictions follow this approach as well. See, e.g., *Arthur D. Little Int'l, Inc. v. Dooyang Corp.*, 928 F. Supp. 1189, 1204-06 (D. Mass. 1996); *Niagra Mohawk Power Corp. v. Stone & Webster Eng'g Corp.*, No. 88-CV-819, 1992 U.S. Dist. LEXIS 7721, at *90 (N.D.N.Y. 1992) (finding that when parties seek "recovery for breach of a duty extraneous to the contract, the intentional tort and negligent misrepresentation claims . . . could stand regardless of the vitality of the contract claims"). Although the *Dooyang* court rejected a claim that mirrored the breach of contract claim, it specifically did so because it was "not a claim for misrepresentation in the inducement of the contract." *Dooyang*, 928 F. Supp. at 1205. It should be noted that the District Court of Massachusetts recently distinguished *Dooyang*, finding that Massachusetts would not allow any negligent misrepresentation claims involving a defective product. See *Sebago*, 18 F. Supp. 2d at 96. At least one Illinois case has applied a Florida-style rule, treating negligent misrepresentation cases similar to cases involving fraud in the inducement. See *Budget Rent-a-Car Corp. v.*

to the economic loss rule to match its fraudulent inducement exception.¹⁶⁵ The most recent Florida Supreme Court decision on the issue, *HTP, Ltd. v. Lineas Aereas Costarricenses, S.A.*¹⁶⁶ clearly established that the Florida economic loss rule did not apply to *any* torts independent of the contract: "Where a contract exists, a tort action will lie for either intentional or negligent acts considered to be independent from acts that breached the contract."¹⁶⁷

Just as the economic loss doctrine does not preclude all claims of fraudulent inducement, the economic loss doctrine does not bar a negligent misrepresentation claim if it centers upon an alleged inducement to enter into a contractual relationship, rather than performance of the contract.¹⁶⁸ Because the economic loss rule applies identically to both fraudulent and negligent misrepresentation, widely inconsistent opinions have resulted—

Genesys Software Sys., Inc., No. 96-C-0944, 1996 U.S. Dist. LEXIS 12123 (N.D. Ill. Aug. 22, 1996). The court in *In re Ford Bronco II Prods. Liab. Litig.*, MDL-991, 1995 U.S. Dist. LEXIS 18207 (E.D. La. Dec. 4, 1995), applied a similar method to evaluate claims under West Virginia, Indiana, Texas, and New York law. *See id.* at *15-*23.

165. *See HTP, Ltd. v. Lineas Aereas Costarricenses, S.A.*, 685 So. 2d 1238, 1239 (Fla. 1996). It should also be noted that in Florida a claim of negligent misrepresentation "that resembles fraud in the inducement may support a claim for punitive damages." *Burger King Corp. v. Austin*, 805 F. Supp. 1007, 1025 n.31 (S.D. Fla. 1992).

166. 685 So. 2d 1238 (Fla. 1996). A brief per curiam opinion by the Florida Supreme Court in *PK Ventures v. Raymond James & Associates, Inc.*, 690 So. 2d 1296 (Fla. 1997), confirmed the applicability of *HTP* to negligent misrepresentation. *See id.* at 1297.

167. *HTP*, 685 So. 2d at 1239 (emphasis added); *see also McCarthy v. Southern States Utils.*, 698 So. 2d 590, 592 (Fla. Dist. Ct. App. 1997) ("[A]lthough *HTP* involved the tort of fraud, the high court was clear that *any* independent tort would satisfy the economic loss rule . . .").

168. *See Mobil Oil Corp. v. Dade County E Soil Management Co.*, 982 F. Supp. 873, 880-81 (S.D. Fla. 1997). Although a few Florida courts have differentiated negligent misrepresentation from fraudulent inducement, such decisions appear to be a misinterpretation of Florida law. *Compare Florida College of Osteopathic Med., Inc. v. Dean Witter Reynolds, Inc.*, 982 F. Supp. 862, 866-67 (M.D. Fla. 1997) (finding that the economic loss rule barred the negligent misrepresentation claim but not the fraudulent inducement claim), *with Wadlington v. Continental Med. Servs.*, 728 So. 2d 352 (Fla. Dist. Ct. App. 1999) (analyzing both intentional and negligent misrepresentation claims together under the economic loss rule), *and Parkhill v. Minnesota Mut. Life Ins. Co.*, 995 F. Supp. 983, 995 (D. Minn. 1998) (interpreting Florida law) ("For the same reasons [plaintiffs] fraud claim is barred by the economic loss rule, so too is plaintiffs negligent misrepresentation claim.").

with some courts focused on whether the tort claims "mirror" breach of contract claims and others creating a nearly absolute exception for negligent misrepresentation claims.¹⁶⁹ The recent Florida Supreme Court decision of *Moransais v. Heathman*¹⁷⁰ suggests that the latter view is correct,¹⁷¹ however, some courts may still hold onto the former view.¹⁷² Until a more definitive pronouncement comes from the Florida Supreme Court on both fraudulent and negligent misrepresentation, the only clear directive is that the economic loss rule applies equally to both claims.

Negligent Misrepresentation: An Exception Limited to Defendants in the Business of Supplying Information for the Guidance of Others

Rather than extend identical exceptions for intentional and negligent misrepresentation, the Illinois Supreme Court in *Moorman Manufacturing Co. v. National Tank Co.*¹⁷³ recognized a limited exception applicable solely to cases involving negligent misrepresentation.¹⁷⁴ As one of the first states to discuss negli-

169. Compare *Parkhill*, 995 F. Supp. at 994-95 (relying on *Hotels of Key Largo, Inc. v. RHI Hotels, Inc.*, 694 So. 2d 74, 77 (Fla. Dist. Ct. App. 1997), to dismiss a negligent misrepresentation claim in the formation of a contract), with *Wassall v. Payne*, 682 So. 2d 678, 681 (Fla. Dist. Ct. App. 1996) (explaining that "where, as here, . . . negligent misrepresentation in the formation of a contract [is] alleged, the economic loss rule does not bar the tort action"); compare *Ocean Ritz of Daytona Condominium v. GGV Assocs., Ltd.*, 710 So. 2d 702, 705 (Fla. Dist. Ct. App. 1998) (explaining that the economic loss rule applied to a third party's negligent misrepresentation claim), with *Williams v. Bear Stearns & Co.*, 725 So. 2d 397, 399 (Fla. Dist. Ct. App. 1998) (concluding that the economic loss rule did not apply because there was no contractual relationship), and *Wassall*, 682 So. 2d at 679 (concluding "the lack of privity of contract" did not bar the negligent misrepresentation claim).

170. 744 So. 2d 973 (Fla. 1999).

171. See *Stone's Throw Condominium Ass'n v. Sand Cove Apartments, Inc.*, No. 98-02012, 1999 WL 1203829, at *2 (Fla. Dist. Ct. App. Dec. 17, 1999) (replacing its earlier decision, No. 98-02012, 1999 WL 445685, at *4 (Fla. Dist. Ct. App. July 2, 1999) (affirming dismissal of a negligent misrepresentation claim that mirrored the breach of contract action), in light of *Moransais*).

172. See *Monroe v. Sarasota County Sch. Bd.*, 746 So. 2d 530, 538 (Fla. Dist. Ct. App. 1999) (concluding that *Moransais's* exception was generally constrained to its facts).

173. 435 N.E.2d 443 (Ill. 1982).

174. See *id.* at 452. In making this determination, the *Moorman* court relied on prior Illinois cases allowing the recovery of purely economic loss for negligent misrepresentation. See *id.* (citing *Rozny v. Marnu*, 250 N.E.2d 656 (Ill. 1969)). The Illinois "in

gent misrepresentation in the context of the economic loss rule, Illinois became a leading authority in the area.¹⁷⁵

A claim for negligent misrepresentation in Illinois exists only against a defendant "who is in the business of supplying information for the guidance of others in their business transactions [and] makes negligent misrepresentations."¹⁷⁶ Because "the concept of duty is at the heart" of the "*Moorman* doctrine," the Illinois Supreme Court analyzed whether the duty is extracontractual in resolving this question.¹⁷⁷ An exception does not apply when the information is conveyed merely as part of a sale or contract.¹⁷⁸ Thus, a misrepresentation is not actionable against a defendant who negligently supplied false information in the course of a transaction.

The exception does not turn on the question of privity,¹⁷⁹ but rather, depends on the profession of the defendant and the na-

the business of supplying information" requirement actually predates the adoption of the economic loss rule. *See id.* Thus, the *Moorman* court merely extended a preexisting exception to the economic loss rule to cases involving negligent misrepresentation.

175. *See South Carolina Elec. & Gas Co. v. Westinghouse Elec. Corp.*, 826 F. Supp. 1549, 1557 n.4 (D.S.C. 1993) ("Illinois is one of the few jurisdictions with a plethora of cases on the subject."). Other jurisdictions have adopted the *Moorman* court's rationale. *See, e.g., Jackson v. Drake Univ.*, 778 F. Supp. 1490, 1496 (S.D. Iowa 1991); *Laetsch v. Rockwell, Int'l*, No. 93-792, 1995 Iowa Sup. LEXIS 37 (Jan. 18, 1995); *Tasco Constr., Inc. v. Town of Winchendon*, No. 910308C, 1994 Mass. Super. LEXIS 373 (Feb. 11, 1994); *see also* Richard P. Salgado, *Negligent Misrepresentation and the Economic Loss Rule*, 22 COLO. LAW. 1689 (1993) (advocating that Colorado adopt the *Moorman* doctrine for negligent misrepresentation).

176. *Moorman Mfg. Co.*, 435 N.E.2d at 452 (citing *Rozny v. Marnul*, 250 N.E.2d 656 (Ill. 1969)).

177. *Lake County Grading Co. v. Lakes Agency, Inc.*, 589 N.E.2d 1128, 1132 (Ill. App. Ct. 1992) (citation omitted); *see also Cordiant MN, Inc. v. David Cravit & Assocs. Ltd.*, No. 96-C-4276, 1997 U.S. Dist. LEXIS 12803, at *44-45 (N.D. Ill. Aug. 19, 1997) (dismissing a negligent misrepresentation claim because the information supplied "was ancillary to the sale").

178. *See Fireman's Fund Ins. Co. v. SEC Donohue, Inc.*, 679 N.E.2d 1197, 1201 (Ill. 1997).

179. *See id.* at 1200 (overruling the third-party requirement). Prior to *Fireman's Fund*, courts interpreting Illinois law required that the plaintiff be a third party. *See, e.g., Mellon Bank v. Miglin*, No. 92-C-4059, 1994 U.S. Dist. LEXIS 15439, at *24 (N.D. Ill. Oct. 26, 1994); *Grass v. Homann*, 474 N.E.2d 711, 714 (Ill. App. Ct. 1984); *see also* Norman Rifkind, *Negligent Misrepresentation in Illinois: The Third Party (Non)Requirement*, 82 ILL. B.J. 668 (1994) (arguing against a third-party requirement).

ture of the relationship between plaintiff and defendant.¹⁸⁰ If the ultimate result of the relationship is something "intangible"—the value of the services rendered lies in the ideas behind the product and not the product itself—then the exception applies.¹⁸¹ Illinois courts have allowed claims against health care professionals, insurance brokers, accountants, and attorneys,¹⁸² but not against advertising firms, architects, or engineers.¹⁸³ According to the Illinois Supreme Court, the distinguishing characteristic is that the former group have "long been held to be members of a skilled profession . . . liable for their negligent failure to observe reasonable professional competence."¹⁸⁴

Although once a certain profession is exempted it is clear that the *Moorman* doctrine no longer applies, this piecemeal determination of whether a particular profession owes some extra contractual duty has left lower courts in the "position of guessing which additional professionals [fall outside] . . . *Moorman's* economic loss doctrine."¹⁸⁵ Determining that the importance of an accountant's duty is less tangible than an architect's provides lower courts with little guidance regarding when the exception is appropriate.¹⁸⁶ In short, the *Moorman* doctrine's "in the busi-

180. See *Congregation of the Passion v. Touche, Ross & Co.*, 636 N.E.2d 503, 515 (Ill. 1994).

181. See *id.* ("Application of the *Moorman* doctrine limiting recovery of purely economic losses to contract, therefore, is inappropriate where a relationship results in something intangible . . .").

182. See *id.* (allowing accountant malpractice claim); *Collins v. Reynard*, 607 N.E.2d 1185 (Ill. 1992) (finding that an attorney malpractice claim was not barred by the economic loss rule); *2314 Lincoln Park West Condominium Ass'n v. Mann, Gin, Ebel & Frazier, Ltd.*, 555 N.E.2d 346, 353 (Ill. 1990) (stating that the *Moorman* doctrine would not bar actions against attorneys or health care professionals); *Lake County Grading*, 589 N.E.2d at 1132 (allowing negligent misrepresentation claim against broker because the relationship between the parties was a fiduciary one).

183. See *Cordiant MN, Inc. v. David Cravit & Assocs. Ltd.*, No. 96-C-4276, 1997 U.S. Dist. LEXIS 12803, at *44 (dismissing a negligent misrepresentation claim against an advertising firm); *Fireman's Fund*, 679 N.E.2d at 1201 (dismissing a negligent misrepresentation claim against an engineer); *Lincoln Park*, 555 N.E.2d at 353 (dismissing a negligent misrepresentation claim against an architect).

184. *Congregation of the Passion*, 636 N.E.2d at 515 (citation omitted).

185. *Fireman's Fund*, 679 N.E.2d at 1202 (Heiple, C.J., dissenting). The plethora of cases that the Illinois Supreme Court has resolved on this issue is a testament that the "distinguishing characteristic" has failed to provide any real guidance to the lower courts. See *supra* notes 175-78 and accompanying text (providing examples of the cases that the Illinois Supreme Court heard on this issue).

186. Cf. *Fireman's Fund*, 679 N.E.2d at 1202 (Heiple, C.J., dissenting) (contending

ness"¹⁸⁷ requirement has failed to articulate a precise formula that will allow courts to apply the economic loss rule to negligent misrepresentation claims.

Negligent Misrepresentation: An Exception Dependent on Whether the Parties Are in Privity

A third approach recognizes the difference between negligent and intentional misrepresentation and avoids the piecemeal determination of the Illinois rule by focusing on the question of privity.¹⁸⁸ Two of the leading cases advocating this approach, *South Carolina Electric & Gas Co. v. Westinghouse Electric Corp.*¹⁸⁹ and *Duquesne Light Co. v. Westinghouse Electric Corp.*,¹⁹⁰ involved factually similar claims. In each case, the plaintiffs negotiated contracts with the defendant to supply generators, with certain specifications, for use at their nuclear power plants.¹⁹¹ After the generators deteriorated, the plaintiffs filed breach of contract and negligent misrepresentation claims against the defendant.¹⁹²

In *Duquesne*, the Third Circuit utilized two rationales to apply the economic loss rule to the negligent misrepresentation

that the court has not coherently differentiated among professional groups).

187. *Moorman Mfg. Co. v. National Tank Co.*, 435 N.E.2d 443, 452 (Ill. 1982).

188. See, e.g., *Duquesne Light Co. v. Westinghouse Elec. Corp.*, 66 F.3d 604, 620 (3d Cir. 1995); *Apollo Group, Inc. v. Avnet, Inc.*, 58 F.3d 477, 480 (9th Cir. 1995) (applying Arizona law); *Bailey Farms, Inc. v. Nor-Am Chem. Co.*, 27 F.3d 188, 191 (6th Cir. 1994) (applying Michigan law); *South Carolina Elec. & Gas Co. v. Westinghouse Elec. Corp.*, 826 F. Supp. 1549, 1557 (D.S.C. 1993) (applying North Carolina law); *Flagg Energy Dev. Corp. v. General Motors Corp.*, 709 A.2d 1075, 1088 (Conn. 1998) ("[C]ommercial losses arising out of the defective performance of contracts for the sale of goods cannot be combined with negligent misrepresentation"); *Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1*, 881 P.2d 986, 993 (Wash. 1994) ("[W]hen parties have contracted to protect against potential economic liability . . . contract principles override the tort principles in [the *Restatement*] and . . . purely economic damages are not recoverable"); *Rissler & McMurtry Co. v. Sheridan Area Water Supply Joint Powers Bd.*, 929 P.2d 1228, 1235 (Wyo. 1996) (adopting *South Carolina Elec. & Gas Co.*).

189. 826 F. Supp. 1549 (D.S.C. 1993).

190. 66 F.3d 604 (3d Cir. 1995).

191. See *id.* at 607-08; *South Carolina Elec. & Gas Co.*, 826 F. Supp. at 1552-53.

192. See *South Carolina Elec. & Gas Co.*, 826 F. Supp. at 1552-53; *Duquesne Light*, 66 F.3d at 608.

claim.¹⁹³ First, the court found that ordinary contract principles governed disputes between sophisticated business entities engaging in arms-length transactions.¹⁹⁴ Second, the court explained that negligent misrepresentation governs liability only when contract remedies are unavailable.¹⁹⁵ Accordingly, the Third Circuit concluded that privity of contract between two commercial parties eliminated the "need for an additional tort of negligent misrepresentation."¹⁹⁶ The *South Carolina Electric & Gas Co.* court further distinguished negligent misrepresentation from intentional misrepresentation because fraud requires a "concomitant element of an *actual intent* to deceive."¹⁹⁷ Both courts, however, suggested that the same rationale might not apply to "an unsophisticated consumer who is party to a sales contract."¹⁹⁸ Under this approach, the economic loss rule bars the negligent misrepresentation claims of "business sophisticates . . . capable of protecting themselves by contractual agreement."¹⁹⁹

This rule suggests that it does not apply to foreseeable third parties. Accordingly, most courts adopting this rule recognize that the lack of privity by a third party renders "commercial law an inadequate framework" in which to resolve a third-party

193. See *Duquesne Light*, 66 F.3d at 620.

194. See *id.*

195. See *id.* (explaining that all of the examples in the *Restatement* involved liability to third parties).

196. *Id.*; see also *Sun Co., Inc. v. Badger Design & Constructors, Inc.*, 939 F. Supp. 365, 373 (E.D. Pa. 1996) (relying on *Duquesne Light* and concluding that as "[a]ll aspects of this controversy occurred within the setting of a private commercial transaction between two sophisticated parties. The allegations implicate no other duties than those contained in the Contract negotiated . . .").

197. *South Carolina Elec. & Gas Co.*, 826 F. Supp. at 1557 (emphasis added).

198. *Id.*; see also *Duquesne Light*, 66 F.3d at 619-20 (distinguishing prior negligent misrepresentation claims brought by "the ordinary consumer"). At least one court, however, has applied this rationale to consumers. See *Griffith v. Centex Real Estate Corp.*, 969 P.2d 486, 491 (Wash. Ct. App. 1998) ("We hold parties to their contracts. . . . [W]hen a contract allocates liability, the economic loss rule bars claims of negligent misrepresentation by homebuyers against builder-vendors." (citation omitted)).

199. *South Carolina Elec. & Gas Co.*, 826 F. Supp. at 1557. The South Carolina Court of Appeals later adopted this rationale. See *Bishop Logging Co. v. John Deere Indus. Equip. Co.*, 455 S.E.2d 183, 189 (S.C. Ct. App. 1995) (relying on *South Carolina Elec. & Gas Co.* and concluding that "negligent misrepresentation is not applicable as a matter of law . . . under the economic loss rule").

plaintiffs' claims.²⁰⁰ Thus, an exception to the economic loss rule allows tort liability when negligent misrepresentations induce third parties who justifiably rely on the information.²⁰¹

Despite the logic of this analysis—that third parties cannot transform a contract claim into a tort claim “to escape some roadblock to recovery”²⁰²—some courts have applied the economic loss rule to negligent misrepresentation claims even when privity is absent.²⁰³ Although the parties may not be in privity, these courts require that the parties must resort to contract law to protect their economic expectations.²⁰⁴ Courts justify this approach by explaining that the “economic loss doctrine was designed to prevent such a strategy”²⁰⁵ whereby the plaintiff could recover benefits it was unable to obtain in contract negotia-

200. *Apollo Group, Inc. v. Avnet, Inc.*, 58 F.3d 477, 480 n.4 (9th Cir. 1995) (applying Arizona law); *see, e.g., Squish La Fish, Inc. v. Thomco Specialty Prods., Inc.*, 149 F.3d 1288, 1291 (11th Cir. 1998) (allowing recovery by a third party who indirectly relied on a negligent misrepresentation); *Danforth v. Acorn Structures, Inc.*, No. 90C-JN-30, 1991 Del. Super. LEXIS 454, at *6-*7 (Nov. 22, 1991) (“[I]t is clear that in order . . . to invoke a cause of action under negligent misrepresentation involving § 552, the plaintiff must show that the defendant supplied the information to the plaintiff for use in business transactions with third parties.”); *Bates & Assocs., Inc. v. Romei*, 426 S.E.2d 919, 922 (Ga. Ct. App. 1993) (“Privity is not required to support an action for negligent misrepresentation.”).

201. *See Malta Constr. Co. v. Henningson, Durham & Richardson, Inc.*, 694 F. Supp. 902, 906 (N.D. Ga. 1988); *Robert & Co. Assocs. v. Rhodes-Haverty Partnership*, 300 S.E.2d 503, 504 (Ga. 1983); *accord Apollo Group*, 58 F.3d at 480 n.4 (applying Arizona law).

202. *Commercial Union Ins. Co. v. Roxborough Village Joint Venture*, 944 F. Supp. 827, 830 (D. Colo. 1996).

203. *See, e.g., National Steel Erection, Inc. v. J.A. Jones Constr. Co.*, 899 F. Supp. 268, 274 (N.D. W. Va. 1995) (finding that the economic loss rule barred negligent misrepresentation claims despite a lack of privity); *Spancrete, Inc. v. Ronald E. Frazier & Assocs.*, 630 So. 2d 1197, 1198 (Fla. Dist. Ct. App. 1994) (precluding subcontractors from bringing negligent misrepresentation claims in construction cases); *Blake Constr. Co. v. Alley*, 353 S.E.2d 724 (Va. 1987) (rejecting negligent misrepresentation claim by a contractor against engineers and architects that the owner hired).

204. *See supra* note 203; *infra* note 205.

205. *Palco Linings, Inc. v. Pavex, Inc.*, 755 F. Supp. 1278, 1280 (M.D. Pa. 1990); *see also Ocean Ritz of Daytona Condominium v. GGV Assocs., Ltd.*, 710 So. 2d 702, 705 (Fla. Dist. Ct. App. 1998) (“[T]he premise of the rule is simply that a contract action is more appropriate for recovering economic losses [even when the parties are not in privity]”). Given that the plaintiff in *Seely* was in privity with the defendant, the truth of this assertion is highly debatable. *See supra* text accompanying notes 38-41.

tions.²⁰⁶ What these courts fail to explain is how a third party is supposed to protect itself through contract negotiation when it is not in privity to the contract.

Application of the economic loss rule to third parties bars negligent misrepresentation claims even in the absence of any contractual remedy or any other basis of recovery.²⁰⁷ In addition, some courts apply the economic loss rule to bar negligent misrepresentation claims by third parties and between commercial entities in privity.²⁰⁸ Dual application of this rule—to both commercial plaintiffs in privity and plaintiffs not in privity—would relegate negligent misrepresentation claims solely to noncommercial plaintiffs. Extension of this dual application to consumer plaintiffs would eliminate negligent misrepresentation altogether.

Negligent Misrepresentation: No Exception

The final approach to resolving the tension between the economic loss rule and negligent misrepresentation concludes that “negligent misrepresentation is a species of negligence.”²⁰⁹ Accordingly, no exception applies to negligent misrepresentation.

Although the Texas Supreme Court crafted an exception for fraudulent inducement without a requirement of independent injury in *D.S.A., Inc. v. Hillsboro Independent School District*,²¹⁰

206. See *National Steel Erection*, 899 F. Supp. at 274.

207. See, e.g., *Palco*, 755 F. Supp. at 1280 (“[Plaintiffs] inability to recover in contract or warranty due to the lack of privity, although unfortunate, does not change the fact that . . . remedies in this matter are limited by law.”); *Floor Craft Floor Covering, Inc. v. Parma Community Gen. Hosp. Ass’n*, 560 N.E.2d 206, 212 (Ohio 1990) (“There is no nexus here that can serve as a substitute for contractual privity.”).

208. Compare *Eagle Traffic Control v. ADDCO*, 882 F. Supp. 417, 420 (E.D. Pa. 1995) (holding that the economic loss rule bars claims when the parties are in privity), with *Palco*, 755 F. Supp. at 1280 (holding that the economic loss rule bars claims when the parties are not in privity).

209. *In re Ford Motor Co. Vehicle Paint Litig.*, MDL-1063, 1996 U.S. Dist. LEXIS 11063, at *33 (E.D. La. July 30, 1996); see *Nepomuceno v. Knights of Columbus*, No. 96-C-4789, 1999 WL 66570, at *11-12 (N.D. Ill. Feb. 8, 1999) (analyzing plaintiffs negligence and negligent misrepresentation claims together under the economic loss rule); accord *Arkwright-Boston Mfrs. Mut. Ins. Co. v. Westinghouse Elec. Co.*, 844 F.2d 1174, 1177 (5th Cir. 1988) (interpreting Texas law); *Essex Ins. Co. v. Blount, Inc.*, 72 F. Supp. 2d 722, 725 (E.D. Tex. 1999) (explaining that under Texas law “the same reasoning applies to [bar] claims for negligent misrepresentation” and negligence) (citations omitted).

210. 973 S.W.2d 662 (Tex. 1998).

the Texas Supreme Court articulated three reasons why negligent misrepresentation did not require a similar exception. First, unlike fraudulent inducement, the measure of damages for negligent misrepresentation did not include the "benefit of the bargain."²¹¹ Second, the rationale for fixing a narrower scope of liability for negligent misrepresentation lay in the difference in the duty imposed—the duty of honesty versus the duty of care.²¹² Third, and finally, requiring only negligent inducement would "potentially convert every contract interpretation dispute into a negligent misrepresentation claim."²¹³ Accordingly, merely negligent misrepresentations require an independent injury (e.g., actual physical harm) to overcome the economic loss rule.²¹⁴ Thus, the rule articulated by the Texas Supreme Court mirrors the economic loss rule's application to negligence and strict liability.

DO FRAUD AND NEGLIGENT MISREPRESENTATION HAVE A FUTURE?

The adoption of the economic loss rule by a majority of the states and the Supreme Court indicates that the underlying rationale to maintain a dividing line between tort and contract is a sound policy with regard to unintentional torts.²¹⁵ As the

211. See *Hillsboro*, 973 S.W.2d at 663.

212. See *id.* at 664.

213. *Id.*

214. See *id.* Although the *Hillsboro* court addressed the issue in the context of parties in privity, the Texas Court of Appeals has utilized the economic loss rule to bar negligent misrepresentation claims of a third party. See M.D. Thomson & Austin Banister Joint Venture v. Espey Huston & Assocs., 899 S.W.2d 415, 422 (Tex. Ct. App. 1995).

215. See *Cathco, Inc. v. Valentiner Crane Brunjes Onyon Architects*, 944 P.2d 365, 368 (Utah 1997); D'Angelo, *supra* note 74, at 595 ("After *East River*, courts continued to follow [the economic loss rule] . . . recognizing the sound policy reasons . . ."). Despite the nearly universal acceptance of the economic loss rule by courts, debate still surrounds the merits of the rule, particularly outside the products liability context. Critics have suggested that because tort law reduces physical injury to monetary damages, the distinction between physical injuries and economic losses is a fiction and that the rule penalizes prudent conduct by requiring plaintiffs to await physical injury prior to recovery. See F. Malcolm Cunningham, Jr. & Amy L. Fischer, *The Economic Loss Rule: Deconstructing the Mixed Metaphor in Construction Cases*, 33 TORT & INS. L.J. 147, 148 (1997). It has also been suggested that the purpose of the

Supreme Court observed in *East River*, parties would be free to extricate themselves from freely bargained-for contracts, and the well-developed body of "contract law would drown in a sea of tort without such a rule."²¹⁶

A blind application of the doctrine, however, would eviscerate fraud and negligent misrepresentation claims.²¹⁷ Failing to create a workable exception for misrepresentation claims ignores the reality that fraud and contract can coexist peacefully in the areas where the interests served by the two bodies of law merge.²¹⁸ Although tort and contract represent separate bodies of law designed to deal with different functions, their purposes and roles are not mutually exclusive.²¹⁹ The fundamental intersection of contract and misrepresentation is inevitable as misrepresentation arises in a contractual setting.²²⁰

The potential for eliminating misrepresentation claims by overapplication of the economic loss rule is evidenced by the test commonly employed by courts to determine when the economic loss rule should apply. This test focuses on the "nature of the injury": If the damages are purely economic, the rule applies.²²¹ The problem with applying this test to misrepresentation is that

rule is merely judicial economy. See Geri Lynn Mankoff, Note, *Florida's Economic Loss Rule: Will It Devour Fraud in the Inducement Claims When Only Economic Losses Are at Stake?*, 21 NOVA L. REV. 467, 471 (1996).

216. *East River S.S. Corp. v. TransAmerica Delaval, Inc.*, 476 U.S. 858, 866 (1986).

217. See *infra* note 261 and accompanying text; see also Schwiep, *supra* note 2, at 42 ("[T]he economic loss rule, rotely applied, . . . [could] defeat what has been the common law for decades . . .").

218. See *supra* text accompanying notes 56-59 (discussing the overlap of tort and contract law).

219. See William C. Way, *The Problem of Economic Damages: Reconceptualizing the Moorman Doctrine*, 1991 U. ILL. L. REV. 1169, 1173.

220. Indeed, the concept of warranty law, now a part of contract law, originated as a form of misrepresentation in the nature of deceit. See William L. Prosser, *The Implied Warranty of Merchantable Quality*, 27 MINN. L. REV. 117, 118-19 (1943); see also *Williams v. Khalaf*, 802 S.W.2d 651, 654 (Tex. 1990) (discussing the quasi-contractual origins of fraud claims).

221. See, e.g., *Carmania Corp., N.V. v. Hambrecht Terrell Int'l*, 705 F. Supp. 936, 938-39 (S.D.N.Y. 1989) (using the rationale that "[i]f the damages suffered are of the type remediable in contract, a plaintiff may not recover in tort" to bar plaintiff's fraud claims) (citations omitted); *Grace Petroleum Corp. v. Williamson*, 906 S.W.2d 66, 68 (Tex. Ct. App. 1995) ("[T]he nature of the injury most often determines which duty has been breached.").

misrepresentation affords contract-style economic loss damages.²²² Unlike other tort claims that seek to compensate the injured party, fraud seeks to remedy the wrong by restoring to the plaintiff what the defendant has taken wrongfully.²²³ Consequently, the majority of American courts have adopted a "benefit of the bargain" rule for fraud claims.²²⁴ As in contract, this measure of damages gives the plaintiff the benefit of what he was promised and allows recovery of the difference between what was received and the value to which the plaintiff was entitled, based on the defendant's representations.²²⁵ This measure of damages exists precisely because recovery in fraud seeks to restore to the plaintiff what the defendant has received.

The Advantages of Misrepresentation in the Recovery of Purely Economic Losses

Despite the apparent similarity between fraud and contract damages, the discussion of whether to allow recovery in misrepresentation versus contract is not purely academic. Allowing a plaintiff to recover under a tort claim of misrepresentation has several distinct advantages.²²⁶ First, contract law severely restricts who may recover by its privity requirement.²²⁷ Although a

222. See *supra* notes 94-95, 161 and accompanying text.

223. See KEETON ET AL., *supra* note 5, § 110, at 765-66 ("Since the purpose [of fraud] is not to compensate the plaintiff's loss, but to restore what the defendant has received, the courts look to the inequity of allowing him to retain it, rather than to the damage which the plaintiff has sustained."). Indeed, the recovery allowed by fraud sets it apart from other tort claims that allow damages similar to reliance rather than benefit of the bargain. See *supra* note 44.

224. See PETER A. ALCES, *THE LAW OF FRAUDULENT TRANSACTIONS* § 2.02[6][b][i], at 2-33 (1989).

225. See ROBERT L. DUNN, *RECOVERY OF DAMAGES FOR FRAUD* § 2.2, at 21 (1988); KEETON ET AL., *supra* note 5, § 110, at 768. It is noteworthy that for negligent misrepresentation, the majority of states allow the recovery of "out-of-pocket" damages. See DUNN, *supra*, § 2.7, at 35.

226. This list merely illustrates the principal advantages of a fraud versus a contract claim and is by no means exhaustive. Tort law may permit recovery where a contract action will not normally lie due to lack of proof of a contract, want of consideration, illegality, limitations imposed by the statute of frauds, or the parol evidence rule. Tort law may also avoid defenses such as infancy or a discharge in bankruptcy and some counterclaims. See KEETON ET AL., *supra* note 5, §§ 92-93, at 655-71.

227. See William K. Jones, *Product Defects Causing Commercial Loss: The Ascen-*

number of states, through legislation or judicial decisions, have limited or dispensed with a privity requirement in warranty cases, the absence of privity still precludes warranty actions in many states.²²⁸

Second, both express and implied warranties can be disclaimed.²²⁹ The presence of a well-drafted merger clause can limit the contract to the written agreement and thereby disclaim any warranties made prior to the contract.²³⁰ Whereas a warranty disclaimer will be inoperative if it is inconsistent with the express warranties, the UCC explicitly encourages disclaimers of warranties.²³¹ Section 2-316 of the UCC provides that, wherever reasonable, express warranties and disclaimers thereof will be "construed . . . as consistent with each other."²³² While a seller may unscrupulously try to disavow a false statement by disclaiming a warranty in the contract agreement, it will not be able to disclaim liability for fraud.²³³ Moreover, a court is more likely to dispense with a warranty limitation under a tort theory than under a contract claim.²³⁴

dancy of Contract over Tort, 44 U. MIAMI L. REV. 731, 783 (1990).

228. See *id.*; see also *Hubbard v. General Motors Corp.*, 95 Civ. 4362 (AGS), 1996 U.S. Dist. LEXIS 6974, at *15 (S.D.N.Y. May 22, 1996) (finding that, absent privity of contract, an indirect purchaser cannot recover mere economic loss under a breach of warranty claim unless the product is a thing of danger).

229. See *PETER ALCES & NATHANIEL HANSFORD, SALES, LEASES & BULK TRANSFERS* § 5.01, at 355 (1989); see also *Twin Disc Inc. v. Big Bud Tractor, Inc.*, 772 F.2d 1329, 1334-35 (7th Cir. 1985) (allowing a disclaimer of express and implied warranties); *Jaskey Fin. & Leasing v. Display Data Corp.*, 564 F. Supp. 160, 163 (E.D. Pa. 1983) (allowing a disclaimer of express and implied warranties). But see *Mainline Tractor & Equip. Co. v. Nutrite Corp.*, 937 F. Supp. 1095, 1104 (D. Vt. 1996) ("Vermont has amended its § 2-316 to provide that sellers cannot exclude or limit their liability in transactions involving ordinary consumers.").

230. See *ALCES & HANSFORD*, *supra* note 229, § 5.02, at 361-62.

231. See U.C.C. § 2-316 (1999).

232. *Id.*

233. See *Arthur D. Little Int'l, Inc. v. Dooyang Corp.*, 928 F. Supp. 1189, 1205 (D. Mass. 1996) ("[A] damage limitation clause in a contract does not bar recovery for intentional misrepresentation in the inducement of a contract."); *Noack v. Blue Cross & Blue Shield of Fla., Inc.*, 742 So. 2d 433, 434 (Fla. Dist. Ct. App. 1999) (explaining that the presence of a merger clause is not an impediment for fraud); see also *Clements Auto Co. v. Service Bureau Corp.*, 444 F.2d 169, 177 (8th Cir. 1971) ("Assuming, arguendo, that the trial court correctly found the warranty disclaimer valid, we . . . find liability for fraud." (footnote omitted)); *RESTATEMENT OF CONTRACTS (SECOND)* §§ 163, 164(1) (1981).

234. See *Jones*, *supra* note 227, at 790.

Misrepresentation claims are particularly superior to implied warranty claims. The implied warranty of merchantability does not guarantee that a plaintiff received the product as represented by defendant; rather, it requires only that the product serve the "traditionally recognized purpose" for which it is used.²³⁵ So long as the product has operated in a "safe condition" and substantially free of a manifest defect, the implied warranty of merchantability provides no remedy.²³⁶ In contrast, fraud allows recovery when a defendant has misrepresented the quality of the good or has substituted an inferior product, regardless of whether the product has actually failed.²³⁷

Third, misrepresentation claims may have a longer statute of limitations. Typically, the statute of limitations for a contract claim is four years.²³⁸ A contract may reduce, but not lengthen, this statutory period to as little as a year.²³⁹ While tort claims typically have a significantly shorter statute of limitations than contract actions, the "discovery rule" allows plaintiffs a tort action long after the contract claim has expired.²⁴⁰ In contract, the statute of limitations begins at the time of the breach.²⁴¹ In tort,

235. See U.C.C. § 2-314; see also *Carlson v. General Motors Corp.*, 883 F.2d 287, 297-98 (4th Cir. 1989) (finding a car able to meet its "purpose" of providing "safe reliable transportation"); *Hubbard v. General Motors Corp.*, 95 Civ. 4362, 1996 U.S. Dist. LEXIS 6974, at *9-10 (S.D.N.Y. May 22, 1996) (explaining that a car that does not exhibit a design defect does not give rise to a breach of warranty claim).

236. See, e.g., *Carlson*, 883 F.2d at 297-98; *In re Air Bag Prods. Liab. Litig.*, 7 F. Supp. 2d 792, 803 (E.D. La. 1998) (dismissing a warranty claim due to the plaintiffs' failure to allege that the air bags functioned improperly during their normal use); *Yost v. General Motors Corp.*, 651 F. Supp. 656, 657-58 (D.N.J. 1986) (dismissing an implied warranty of merchantability claim where plaintiff experienced no actual mechanical difficulties); *Feinstein v. Firestone Tire & Rubber Co.*, 535 F. Supp. 595, 602 (S.D.N.Y. 1982) (dismissing an implied warranty claim on tires with a latent defect where the plaintiffs had not yet experienced product failure); *Skelton v. General Motors Corp.*, 500 F. Supp. 1181, 1191-92 (N.D. Ill. 1980) (dismissing a claim where there was no product failure despite an allegation that the manufacturer substituted less desirable transmissions than those represented).

237. See *Kahn v. Shiley, Inc.*, 266 Cal. Rptr. 106, 112 (Ct. App. 1990); *Prince Mfg. Co. v. Prince's Metallic Paint Co.*, 31 N.E. 990, 994 (N.Y. 1892) (explaining that the intentional substitution of inferior goods can constitute fraud).

238. See U.C.C. § 2-725(1).

239. See *ALCES & HANSFORD*, *supra* note 229, § 4.06, at 333.

240. See *Borello v. United States Oil Co.*, 388 N.W.2d 140, 146 (Wis. 1986).

241. See U.C.C. § 2-725(2); *ALCES & HANSFORD*, *supra* note 229, § 4.06, at 333; see also, e.g., *Zhi v. Bell Helicopter Textron, Inc.*, No. 4:97-CV-404-Y, 1997 U.S. Dist.

the statute of limitations begins to run *only after the plaintiff knew or should have known* of the injury.²⁴² Even though the warranty provisions also contain a deferral clause, "its applicability is a rare exception."²⁴³ In addition, fraud itself may have a longer statute of limitations than a contract action or other tort actions.²⁴⁴ Thus, in the case of a misrepresentation that does not become known until after the contract statute of limitations expires, a plaintiff may still have a viable fraud claim.

Finally, fraud damages are more expansive than contract damages. Because fraud is a tort, nearly every state allows punitive damages for intentional fraud.²⁴⁵ Though punitive damages should not attach for mere negligent misrepresentation, one who intentionally perpetrates a fraud is "arguably a proper candidate for punishment."²⁴⁶

In addition, although both contract and tort law limit damages to those that are "foreseeable," the rules differ. The famous case of *Hadley v. Baxendale*²⁴⁷ established two rules limiting liability in contract cases. First, contract damages are limited to those that arise naturally as a result of the breach.²⁴⁸ Second, contract

LEXIS 20374, at *13 (N.D. Tex. Dec. 16, 1997) ("A cause of action for breach of warranty generally accrues at the time of the delivery, not at the time of discovery.").

242. See *Arthur D. Little Int'l, Inc., v. Dooyang Corp.*, 928 F. Supp. 1189, 1203 (D. Mass. 1996) (applying discovery rule to a fraud claim); *Moorman Mfg. Co. v. National Tank Co.*, 414 N.E.2d 1302, 1314 (Ill. App. Ct. 1980) ("[A] cause of action for misrepresentation does not accrue until the injury is discovered."), *aff'd in part, rev'd in part*, 435 N.E.2d 443 (Ill. 1982); *Thurin v. A.O. Smith Harvestore Prods., Inc.*, Nos. 95-2415, 95-3127, 1998 Wisc. App. LEXIS 819, at *23 n.8 (July 9, 1998) (stating that the discovery rule applies to misrepresentation but not to contract claims).

243. *ALCES & HANSFORD*, *supra* note 229, § 4.06, at 335; see also *id.* at 334-35 (discussing cases and rules governing the applicability of the deferral provision).

244. See generally *Triangle Underwriters, Inc. v. Honeywell, Inc.*, 604 F.2d 737 (2d Cir. 1979) (discussing the statutes of limitations for fraud (six years), contract (four years) and negligence (three years)).

245. See *ALCES*, *supra* note 224, § 2.02[G][b][iii], at 2-38; *KEETON ET AL.*, *supra* note 5, § 110, at 769; see also *Dinsmore Instrument Co. v. Bombardier, Inc.*, 999 F. Supp. 968, 972 (E.D. Mich. 1998) (dismissing a punitive damage claim because the Michigan UCC does not allow them).

246. *ALCES*, *supra* note 224, § 2.02[G][b][iii], at 2-38.

247. 156 Eng. Rep. 145 (1854).

248. See *id.* at 151 ("[T]he damages which the other party ought to receive . . . should be such as may fairly and reasonably be considered . . . arising naturally, i.e., according to the usual course of things, from such breach of contract itself . . .").

damages must "reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it."²⁴⁹ Proximate cause in tort law does not focus on either the contemplation of the parties or on the extent of the injury.²⁵⁰ Rather, a tortfeasor is liable for all consequences that follow from his impact on the plaintiff, except those that public policy limits.²⁵¹ Whereas fraud damages must also be foreseeable at the time of the misrepresentation, no case exists in which a defrauded party's proximately caused consequential damages were unforeseeable.²⁵² The foreseeability question highlights the necessity of a viable fraud claim for misrepresentation, as a defrauded purchaser cannot "reasonably be supposed" to contemplate that the other person is defrauding them at the time of the sale.²⁵³

The advantages of misrepresentation claims do not merely illustrate the advantages of a tort versus a contract claim; rather, these advantages illustrate the fundamental differences between contract actions and misrepresentation claims. The scope of these differences concern the circumstances in which recovery is permitted and the extent of that recovery. As the purpose of the economic loss rule is to prevent tort law and contract law from dissolving into one another *when they overlap*, these differences suggest that while both contract and misrepresentation arise out of commercial transactions, each serves a complementary but distinct purpose. Accordingly, this recognition must inform the correct application of the economic loss rule to misrepresentation claims.

The rule of *Hadley v. Baxendale* is now codified in section 2-715(2) of the UCC.

249. *Hadley*, 156 Eng. Rep. at 151 (emphasis added).

250. See KEETON ET AL., *supra* note 5, § 42, at 273.

251. See Way, *supra* note 219, at 1173; see also *Hap's Aerial Enters., Inc. v. General Aviation Corp.*, 496 N.W.2d 680, 683-84 (Wis. Ct. App. 1992) (remanding to the trial court with an allowance for the defendant to argue public policy grounds).

252. See DUNN, *supra* note 225, § 1.3, at 12-17.

253. "A party to a contract cannot rationally calculate the possibility that the other party will deliberately misrepresent terms critical to that contract. Public policy is better served by leaving the possibility of an intentional tort suit hanging over the head of a party considering outright fraud." *Stoughton Trailers, Inc. v. Henkel Corp.*, 965 F. Supp. 1227, 1236 (W.D. Wis. 1997).

What Should Be the Rule for Fraud?

Formulating the rule for fraud requires an understanding of the interrelation between contract and fraud. In recognizing the complementary, yet distinct nature of fraud, the UCC expressly provides that principles of law and equity, including fraud and misrepresentation, apply unless specifically displaced by the Act.²⁵⁴ This provision is not an innovation of the UCC; commercial law has long recognized that "fraud unravels everything."²⁵⁵ Despite the similarity between fraud and express warranty claims, warranty law does not supplant fraud because fraud requires additional elements.²⁵⁶ Unlike warranty, proof of fraud requires an intentional act to deceive²⁵⁷ and proof of actual reliance.²⁵⁸ Moreover, warranty and fraud claims serve distinct purposes. Warranty claims arise *from the existence of a contract* and therefore may be disclaimed according to the negotiations of the parties in allocating risk of *nonperformance*.²⁵⁹ In contrast, the duty not to engage in fraud to induce a contract is imposed by law, regardless of the contract and may not be disclaimed because parties cannot, and for public policy reasons should not, "reasonably contemplate" the risk of fraud, as compared to non-performance.²⁶⁰

254. See U.C.C. § 1-103 (1999); JAMES J. WHITE & ROBERT S. SUMMERS, HANDBOOK OF THE LAW UNDER THE UCC § 5, at 19 (2d ed. 1980); Steven C. Tourek et al., *Bucking the "Trend": The Uniform Commercial Code, the Economic Loss Doctrine, and Common Law Causes of Action for Fraud and Misrepresentation*, 84 IOWA L. REV. 875, 880-84 (1999).

255. ALCES, *supra* note 224, § 3.03[1], at 3-5; *supra* notes 92-93, 105 and accompanying text (explaining the long history of fraud in preventing misrepresentations that induce contracts).

256. See WHITE & SUMMERS, *supra* note 254, § 9-1, at 327.

257. See *Formosa Plastics Corp. v. Presidio Eng'rs & Contractors, Inc.*, 960 S.W.2d 41, 46-47 (Tex. 1998); *supra* note 197 and accompanying text.

258. Compare *Mirkin v. Wasserman*, 858 P.2d 568, 570 (Cal. 1993) (reaffirming the need to show actual reliance to establish fraud), and RESTATEMENT (SECOND) OF TORTS § 533 (1977) (requiring justifiable reliance for fraud), and *supra* note 93 (discussing the elements of fraud), with *Lennar Homes, Inc. v. Masonite Corp.*, 32 F. Supp. 2d 396, 399-400 (E.D. La. 1998) (finding that reliance is not required for a breach of express warranty claim).

259. See *supra* notes 50-53 and accompanying text (discussing the source of contractual duties); *supra* notes 64-73 and accompanying text (discussing the rationales of negotiation and risk allocation as underlying the economic loss rule); *infra* notes 274-79 and accompanying text (distinguishing fraud from contract actions).

260. See *supra* notes 54-55 and accompanying text (explaining the source of tort

Most courts recognize that fraud can be an exception to the economic loss rule. Indeed, without Michigan's and Florida's requirement that the allegations of fraud cannot be interwoven into the parties' agreement, the rules in Michigan, Florida, California, Texas, and Illinois would be identical. All three rules would allow recovery of purely economic losses when the defendant's misrepresentations fraudulently induced the plaintiff to enter into a contract. The only real differences between the rules are how and when to determine that the fraud is not merely a recasting of the breach of contract allegations.

Adopting the *Flagg Energy* court's rule would eviscerate fraud claims.²⁶¹ Under that rule, the UCC is the sole source of remedies in defective product cases, regardless of whether the contract to sell was procured by fraud.²⁶² Not only does this rule ignore the explicit provisions of the UCC,²⁶³ the rule is unsound for policy reasons as well. For example, a seller held liable only for expectation damages—namely, the benefit of contractual performance or a functional product—would, at worst, expect rescission of the contract.²⁶⁴ Because specific performance is rarely granted and punitive damages largely forbidden under contract law and the UCC,²⁶⁵ this approach fails to punish intentionally

duties arising from an inability to negotiate risk); *supra* notes 102, 104-07 and accompanying text (discussing the concept that the source of duty for fraud is one imposed by law); *supra* note 253 (explaining why parties cannot anticipate fraud when negotiating); *infra* notes 266-68 (discussing the implications if the law were to require that parties could not rely on representations in commercial transactions).

261. See *All-Tech Telecom, Inc. v. Amway Corp.*, 174 F.3d 862, 867 (7th Cir. 1999) (noting that a literal reading of the economic loss rule, as some courts have suggested, would result in commercial fraud going "completely by the boards"); cf. *Brass v. NCR Corp.*, 826 F. Supp. 1427, 1428 (S.D. Fla. 1993) ("[D]efendant's argument would result (practically speaking) in the Economic Loss Rule abolishing the tort of fraud in the inducement altogether.").

262. See *supra* text accompanying notes 144-52.

263. See *supra* notes 71-73 and accompanying text.

264. See *Davich v. Norman Bros. Nissan, Inc.*, 739 So. 2d 138, 141 (Fla. Dist. Ct. App. 1999) (explaining that if the plaintiff proves fraud, rescission would be an improper remedy because the parties would not be placed in their pre-sale positions).

265. See U.C.C. § 2-716 (1999) (allowing specific performance only when the goods are "unique or in other proper circumstances"); *Dinsmore Instrument Co. v. Bombardier, Inc.*, 999 F. Supp. 968, 972 (E.D. Mich. 1998) (dismissing punitive damages claim because the UCC does not allow them); *supra* notes 245-46 and accompanying text.

fraudulent behavior. The possibility of such a limited remedy for fraud would create an uncertain marketplace—where sellers would not be held to their representations and buyers could not rely on explicit representations by the seller.²⁶⁶ Judge Posner recently explained that such a rule invariably would increase costs for *all* commercial transactions:

If commercial fraud [is eliminated by the economic loss rule], then prospective parties to contracts will be able to obtain legal protection against fraud only by insisting that the other party to the contract reduce *all representations* to writing, and so there will be additional contractual negotiations, contracts will be longer, and in short, transactional costs will be higher. And the additional costs will be incurred *in the making of every commercial contract, not just the tiny fraction that end up in litigation.*²⁶⁷

Even if the buyer reduces all representations to writing and recovers under an express warranty, the seller would not be liable for inducing a contract that, but for the misrepresentations, would not have been made.²⁶⁸ Failing to hold the seller liable for fraud does not provide the buyer with a full and adequate remedy without any policy justifying the result.

The underlying problem with the Florida and Michigan limitations on the fraudulent inducement exception is that they rest on a misunderstanding of the tort of fraud in the inducement.²⁶⁹

266. See *Stoughton Trailers, Inc. v. Henkel Corp.*, 965 F. Supp. 1227, 1236 (W.D. Wis. 1997) (stating that a requirement that the economic loss rule bars intentional misrepresentation claims "would not be conducive to amicable commercial relations").

267. *All-Tech Telecom, Inc. v. Amway Corp.*, 174 F.3d 862, 867 (7th Cir. 1999) (emphases added); see also *Armstrong World Indus., Inc. v. Robert Levin Carpet Co.*, No. Civ. 98-CV-5884, 1999 WL 387329, at *6 (E.D. Pa. May 20, 1999) (requiring that any representations, even those that fraudulently induced the transaction, if material, must be "set forth in the parties' integrated distribution agreements"); *Pressman v. Wolf*, 732 So. 2d 356, 360 (Fla. Dist. Ct. App. 1999) (dismissing fraudulent inducement claims because of the existence of an "as is" contract).

268. See *Dexter Corp. v. Shittaker Corp.*, 926 F.2d 617, 621 (7th Cir. 1991) ("If [plaintiff] proves fraud, it can obtain all its compensatory damages and more and can forget about the contract."); see also *Tourek et al.*, *supra* note 254, at 882 (explaining that it is "well-recognized that fraudulently obtained contracts are voidable as a matter of law").

269. See *Budgetel Inns, Inc. v. Micros Sys., Inc.*, 8 F. Supp. 2d 1137, 1147-48 (E.D. Wis. 1998).

Fraud in the inducement is defined as "[m]isrepresentation as to the terms, quality or other contractual relation, venture or other transaction that leads a person to agree to enter into the transaction with a false impression or understanding of the risks, duties or obligations she has undertaken."²⁷⁰ Whereas the fraudulent inducement is always interwoven with the contract, the tort itself is always independent of the contract.²⁷¹ The *Huron Tool* court, then, was correct to distinguish the fact that fraudulent inducement claims, not fraudulent performance claims, are exceptions to the economic loss rule.²⁷² By imposing the additional requirement, however, the court vitiated the exception and for all practical purposes created no exception at all.²⁷³

Fraud in the inducement must always be interwoven with the contract because the tort of fraud is the inducement of someone to enter into a contract.²⁷⁴ The distinguishing determination is whether the fraud arises from inducement or performance; the former is a tort, the latter arises only under contract law.²⁷⁵ If the fraud took place prior to entering the contract, then it is fraud in the inducement; if not, it is breach of contract.²⁷⁶ Consequently, all fraud in the inducement claims should be exceptions

270. BLACK'S LAW DICTIONARY 661 (6th ed. 1990); see also RESTATEMENT (SECOND) OF TORTS § 530(1) (1977) ("A representation of the maker's own intention to do or not to do a particular thing is fraudulent if he does not have that intention.").

271. See *Budgetel*, 8 F. Supp. 2d at 1147; see also *supra* notes 99-107 and accompanying text (discussing the rationales for creating a true fraud exception to the economic loss rule).

272. See *supra* notes 117-22 and accompanying text (discussing *Huron Tool*).

273. See *supra* text accompanying notes 128-29; see also *supra* note 142 (discussing the varied application of the Florida economic loss rule). Compare *supra* notes 123-24 and accompanying text (discussing the application of the *Huron Tool* limitation), with *supra* notes 145-50 (discussing the results in *Flagg Energy*).

274. See *supra* notes 270-71 and accompanying text; see also *supra* notes 104-06 and accompanying text (discussing the origin of the duty for fraud).

275. See *Sun Co. (R&M) v. Badger Design & Constr., Inc.*, 939 F. Supp. 365, 370 (E.D. Pa. 1996) ("[M]ere non-performance . . . is not evidence of fraud."); *Oxford Indus. v. Luminco, Inc.*, No. 86-6417, 1991 U.S. Dist. LEXIS 7099, at *13 (E.D. Pa. May 22, 1991) ("An unperformed promise does not give rise to a presumption that the promisor intended not to perform when the promise was made, and a fraudulent intention will not be inferred merely from its nonperformance." (quoting *Fidurski v. Hammill*, 328 Pa. 1, 2 (1937))).

276. See *Budgetel*, 8 F. Supp. 2d at 1147-48; see also *supra* notes 46-49, 62-63 and accompanying text (discussing the distinction between tort and contract).

to the economic loss rule.²⁷⁷ Both the California Court of Appeals and the Texas Supreme Court correctly recognized that fraud is separate and distinct from a contract because the duty imposed is the abstention from inducing another to enter into a contract through the use of misrepresentations.²⁷⁸ The duty not to lie in contract negotiations differs substantially from a broken contractual promise.²⁷⁹ In short, fraud consists of a promise never intended to be performed (i.e., a lie) while breach consists of a promise intended to be performed but is not performed (i.e., a broken promise).

The test to determine whether a plaintiff has properly asserted a tort claim does not rest on the determination of whether the damages are physical or economic. Purely economic loss is recoverable under a variety of tort theories, including fraud.²⁸⁰ Instead, the question of whether a plaintiff correctly asserted a fraudulent inducement claim depends on the source of the duty.²⁸¹ If the duty arises solely from a provision contained within the contract, then the plaintiff has asserted a contract action.²⁸² Conversely, if the plaintiff's allegations concern misrepresentations made during contract negotiations, then the claim is a tort.²⁸³ Mere failure to perform a contract does not constitute fraud, but a party can be held liable for fraud when that party makes a misrepresentation without the intent to perform and another party is induced into a transaction.²⁸⁴ So long as the

277. See *Budgetel*, 8 F. Supp. 2d at 1147-48; *supra* text accompanying notes 42-46 (defining the economic loss rule and explaining that the heart of the economic loss rule is to distinguish tort and contract claims).

278. See *supra* text accompanying notes 96-107.

279. See *Budgetel Inns, Inc. v. Micros Sys., Inc.*, 34 F. Supp. 2d 720, 724 (E.D. Wis. 1999) (explaining that "the duty of honesty when negotiating a contract is not an obligation imposed by the contract, which does not yet exist, but instead by the common law"); *Budgetel*, 8 F. Supp. 2d at 1147-48.

280. See *supra* notes 5-6.

281. See *supra* notes 96-112 and accompanying text.

282. See *supra* note 50 and accompanying text (explaining that contract law arises from agreements of the parties); see also *Budgetel*, 8 F. Supp. 2d at 1149 (explaining that a representation made after the existence of the contract did not constitute fraudulent inducement); *Tommy L. Griffin Plumbing & Heating Co. v. Jordan, Jones & Goulding, Inc.*, 463 S.E.2d 85, 88 (S.C. 1995) (same).

283. See *Griffin Plumbing & Heating*, 463 S.E.2d at 88; *supra* notes 103-07 and accompanying text.

284. See *Royal Palm Sav. Ass'n v. Pine Trace Corp.*, 716 F. Supp. 1416, 1420 (M.D.

allegation concerns a misrepresentation made prior to the contract that induced the contract, it is a fraudulent inducement claim.

The economic loss rule clearly seeks to prevent the mere recasting of a contract claim sounding as a tort of fraud in the inducement,²⁸⁵ because tort law does not protect parties from breach of duties assumed only by agreement.²⁸⁶ Courts correctly recognize that "almost any contract claim can be framed as a fraud in the inducement."²⁸⁷ The test to determine whether a plaintiff has a fraudulent inducement action is not to examine "the gist of the action"²⁸⁸ by determining if the terms are "inseparably embodied in the parties' subsequent agreement"²⁸⁹ nor the nature of the damages claimed.²⁹⁰ These indicators suggest only that there *might* be a recasting of the contract claim; they are the beginning, not the end, of the determination.

The true test of a claim rests on the duty involved²⁹¹ and the significance of the representation: (1) Did the duty arise *before the contract*, and (2) if the misrepresentation had been known to the defrauded party, would there have been no deal?²⁹² When a plaintiff does not allege merely that the defendant failed to keep

Fla. 1989).

285. See *Commercial Union Ins. Co. v. Roxborough Village Joint Venture*, 944 F. Supp. 827, 831 (D. Colo. 1996).

286. See *Palco Linings v. Pavex, Inc.*, 755 F. Supp. 1269, 1271 (M.D. Pa. 1990).

287. *Hotels of Key Largo, Inc. v. RHI Hotels, Inc.*, 694 So. 2d 74, 77 (Fla. Dist. Ct. App. 1997) (quoting *Puff 'N Stuff of Winter Park, Inc. v. Bell*, 683 So. 2d 1176, 1179 (Fla. Dist. Ct. App. 1996)).

288. The "gist of the action" doctrine determines whether the gravamen of the complaint sounds in tort or contract. See *Sundquest Info. Sys., Inc. v. Dean Witter Reynolds, Inc.*, 40 F. Supp. 2d 644, 651 (W.D. Pa. 1999).

289. See, e.g., *Hotels of Key Largo*, 694 So. 2d at 77.

290. See *DeWitt County Elec. Co-op., Inc. v. Parks*, 1 S.W.3d 96, 105 (Tex. 1999) (explaining that the "measure of damages, standing alone, is not always determinative of whether a tort claim can co-exist with a breach of contract claim").

291. See *2314 Lincoln Park West Condominium Ass'n v. Mann, Gin, Ebel & Frazier, Ltd.*, 555 N.E.2d 346, 351 (Ill. 1990) ("[T]he concept of duty is at the heart of . . . the economic loss rule.").

292. Cf. *Douglas-Hanson Co. v. BF Goodrich Co.*, 598 N.W.2d 262, 270-71 (Wis. Ct. App. 1999) (determining that fraudulent misrepresentations that actually induce a contract create an exception to the economic loss rule, but declining to address whether the economic loss rule would bar misrepresentation claims that do not actually induce the contract).

its promise, but that either the defendant made a false statement that induced the contract or that the defendant never intended to keep the agreement, the plaintiff has properly claimed fraudulent inducement.²⁹³

The validity of this test is evidenced by the fact that "[f]raud destroys all consent."²⁹⁴ If the defrauded party's reliance on the misrepresentation induced the contract, and the representation, if not true, was a deal-breaker, then the plaintiff has truly pled a fraudulent inducement claim. Unfortunately, such a determination must be made on a case-by-case basis; it cannot be applied in a simplistic fashion by merely looking to see if the misrepresentations are "interwoven" into the contract. The misrepresentations will necessarily concern the heart of the parties' agreement.²⁹⁵ A misrepresentation that is collateral to, or a minor part of, the contract is not a deal-breaker. If the misrepresentation is such that there would have been no contract if the truth were known, the party has been tricked into contracting.²⁹⁶ Because of the misrepresentation, the plaintiff entered into a contract to which he would not have otherwise agreed.²⁹⁷ In

293. See *City of Richmond v. Madison Management Group, Inc.*, 918 F.2d 438, 446-47 (4th Cir. 1990).

294. *Ganley Bros., Inc. v. Butler Bros. Bldg. Co.*, 212 N.W. 602, 603 (Minn. 1927); see *ALCES*, *supra* note 224, §3.01, at 3-3.

295. Fraud in the inducement occurs when a party is induced to enter a contract "as when a seller misrepresents the quality of goods." E. ALLAN FARNSWORTH, *CONTRACTS* § 4.10, at 249 (2d ed. 1990); see also *Armstrong World Indus., Inc. v. Robert Levin Carpet Co.*, No. Civ. A. 98-CV-5884, 1999 WL 387329, at *6 (E.D. Pa. May 20, 1999) (explaining that material factors to agreements are included in the subject matter of contracts); *Eclipse Med., Inc. v. American Hydro-Surgical Instruments, Inc.*, No. 96-8532-CIV-RYSKAMP, 1999 WL 181412, at *5 (S.D. Fla. Jan. 20, 1999) (explaining that "if the representation was not important enough to make it into the comprehensive written agreement it must not have been material").

296. See *Huron Tool & Eng'g v. Precision Consulting Servs.*, 532 N.W.2d 541, 545 (Mich. Ct. App. 1995) (explaining that fraud in the inducement undermines a party's ability to negotiate freely); *Douglas-Hanson*, 598 N.W.2d at 268 (explaining that fraud undermines "one party's ability to negotiate fair terms and make an informed decision").

297.

[A] material misrepresentation of fact may render a contract void or voidable The economic loss doctrine does not apply to fraudulently induced contracts because the person fraudulently induced . . . can affirm or avoid the contract, and . . . has the option of selecting tort or contract damages. That option is inconsistent with the economic loss doctrine, . . .

essence, no agreement exists when the contract is based on fraud.

A case-by-case analysis requires that the court examine the evidence supporting the plaintiff's claims. The fact-intensive nature of a fraud claim²⁹⁸ suggests that the bottom line of this analysis rests not on the economic loss rule, but on whether the plaintiff has enough facts to support a fraudulent inducement claim.²⁹⁹ To survive judgment as a matter of law, a plaintiff must have sufficient facts to show (1) that the defendant intentionally misrepresented a material fact to induce the contract or the defendant's intent at the time prior to the contract was not to fulfill its promise, and (2) that had the plaintiff known that the representation was false, the plaintiff would not have entered into the contract.

This approach properly balances the interests of the economic loss rule and fraud claims. First, it preserves the essence of the fraudulent inducement claim, which responds to the concern of critics who allege that courts are using the economic loss rule as an "analysis-lacking short-cut" or merely as a tool of "judicial economy."³⁰⁰ Second, it suggests that fraudulent inducement requires not just reliance on the precontractual misrepresentation, but that without the misrepresentation, no contract would have been formed. By focusing both on the timing and significance of the representation, this approach responds to the concern that

which requires the contract to be affirmed.

Douglas-Hanson, 598 N.W.2d at 268-69 (citations omitted).

298. At least one court has explained that the nature and subtleties of a fraud claim are such that fraud requires a full explanation of facts and circumstances to permit a proper determination that seldom can be made without a full trial. See *Nessim v. DeLoache*, 384 So. 2d 1341, 1344 (Fla. Dist. Ct. App. 1980).

299. See *Burton v. Linotype Co.*, 556 So. 2d 1126, 1128 (Fla. Dist. Ct. App. 1989) (explaining that "[f]raud is ordinarily inappropriate for summary disposition; only after a full explanation of the facts and circumstances can the occurrence of fraud be determined"); *Nepomoceno v. Knights of Columbus*, No. Civ. A. 96-C-4789, 1999 WL 66570, at *11, *12-14 (N.D. Ill. Feb. 8, 1999) (recognizing the fact-intensive nature of misrepresentation claims). Compare *All-Tech Telecom, Inc. v. Amway Corp.*, 174 F.3d 862, 868 (7th Cir. 1999) (evaluating fraud claims on the merits), with *J Square Enters. v. Regner*, 734 So. 2d 565, 567 (Fla. Dist. Ct. App. 1999) (affirming the trial court's dismissal of fraud claims based on the economic loss rule), and *Clayton v. State Farm Mut. Ins. Co.*, 729 So. 2d 1012, 1014 (Fla. Dist. Ct. App. 1999) (affirming the dismissal of fraud claims based on the economic loss rule).

300. See *supra* note 215.

any contract claim can be converted into a fraudulent inducement claim.³⁰¹ The similarity of claims for breach of an express warranty and fraud evidences that allowing simultaneous claims to proceed will not unnecessarily burden the defendant or the court.³⁰² Finally, focusing on the timing and importance of the misrepresentation preserves fraud as a viable claim that co-exists with contract claims, as it developed in the common law³⁰³ and as contemplated by the drafters of the UCC.³⁰⁴

What Should Be the Rule for Negligent Misrepresentation—Is It More Akin to Fraud or Negligence?

The disparate treatment of negligent misrepresentation by the courts demonstrates the true debate over application of the economic loss rule to negligent misrepresentation claims. The Florida rule treats negligent misrepresentation as if it were similar to a fraudulent inducement claim; Texas and Illinois treat negligent misrepresentation as more akin to negligence. Although negligent misrepresentation does not require fraud's concomitant intent to deceive, it "is founded on the breach of a duty separate and distinct from the duty abolished by the economic loss rule."³⁰⁵

The duty imposed by negligent misrepresentation is "to exercise reasonable care or competence in obtaining or communicating information for the guidance of others in their business transactions."³⁰⁶ The goal of the economic loss rule is to prevent parties from extricating themselves from the bargains struck from freely negotiated transactions.³⁰⁷ Negligent misrepresenta-

301. See *supra* notes 274-79 and accompanying text.

302. Indeed, pleading fraud also comes with safeguards against false claims, such as the requirement of pleading fraud with particularity and, in most jurisdictions the burden of proving fraud by clear and convincing evidence, not merely a preponderance of the evidence. See *All-Tech Telecom*, 174 F.3d at 866; see also Tourek et al., *supra* note 254, at 919-21 (arguing that a host of provisions in the rules of procedure protect against improper allegations of fraud).

303. See *supra* notes 93, 215, 255 and accompanying text.

304. See *supra* notes 254-60 and accompanying text.

305. *State v. United States Steel Corp.*, 919 P.2d 294, 302 (Haw. 1996).

306. *Id.* at 303; see also *supra* note 155 (setting forth section 552 of the *Restatement (Second) of Torts*).

307. See *supra* notes 46-79 and accompanying text.

tion imposes a duty of care when the defendant supplies information intended for the guidance of others.³⁰⁸ In a negligent misrepresentation case, the plaintiff relies on that information and experiences business losses as a result.³⁰⁹

Like fraud, negligent misrepresentation also expressly provides for the recovery of purely economic losses.³¹⁰ Although the economic loss rule bars claims for disappointed economic expectations where commercial law provides an adequate remedy,³¹¹ the UCC clearly allows supplemental common law claims not only for fraud, but also for negligent misrepresentation.³¹² At least in the case of third parties, negligent misrepresentation does not protect the same interest that contract law and the UCC protect.³¹³

Adopting a view that negligent misrepresentation is so akin to negligence that the economic loss rule bars its application ignores the express intention of the UCC to allow fraud *and* negligent misrepresentation defenses to supplement the Code.³¹⁴ The "in the business" requirement crafted by the Illinois courts raises several problems. First, the Illinois courts have failed to articulate a clear and concise test to determine who is "in the business of supplying information for the guidance of others,"³¹⁵ or to explain why certain professions are included and others excluded.³¹⁶ The "in the business" requirement also ignores the plain language of the *Restatement (Second) of Torts*. The *Restatement* requires only that the supplier of information provide the information "in the course of his business . . . or employment" or supply information in connection with "any other

308. See *John Martin Co. v. Morse/Diesel, Inc.*, 819 S.W.2d 428, 430-31 (Tenn. 1991); *supra* notes 159-60 and accompanying text.

309. See *John Martin*, 819 S.W.2d at 430-31.

310. See *RESTATEMENT (SECOND) OF TORTS* § 552(1) (1977). Although the majority of states do not allow for recovery of benefit of the bargain damages for negligent misrepresentation, a few states do. See, e.g., *Vermont Plastics, Inc. v. Brine, Inc.*, 824 F. Supp. 444, 451 (D. Vt. 1993).

311. See *State v. United States Steel Corp.*, 919 P.2d 294, 306 (Haw. 1996).

312. See U.C.C. § 1-103 (1999); *supra* notes 254-55.

313. See *supra* notes 157-60 and accompanying text.

314. See U.C.C. § 1-103.

315. *Moorman Mfg. Co. v. National Tank Co.*, 435 N.E.2d 443, 452 (Ill. 1982); see also *supra* notes 174-87 and accompanying text (discussing the *Moorman* doctrine).

316. See *supra* notes 174-87 and accompanying text.

transaction in which he has a pecuniary interest."³¹⁷ A proper defendant is one who either is paid to provide information, for example, an accountant or an attorney, or one who does not receive compensation for the information, but nonetheless has a pecuniary interest in the transaction.³¹⁸

All that a negligent misrepresentation claim requires is that the information be given in the course of the defendant's business, even if no consideration exists for the information itself, and that the defendant have a pecuniary interest in the underlying transaction.³¹⁹ The *Restatement* also does not explicitly require that the plaintiff and the defendant not be in privity—only that the information be intended for the guidance of others:³²⁰

Although . . . the bulk of the decisions stem from factual situations involving damage . . . [to] third parties . . . this alone does not compel a narrow reading of section 552 that limits its applicability solely to such situations or precludes its applicability . . . to parties . . . in which the providers of information are involved.³²¹

The Illinois "in the business" requirement is correctly applied when there is a direct relationship between the parties *and* an inequality of knowledge or bargaining power. Where the information supplier has a direct relationship with the relying party and the nature of the contractual relationship is based on the information supplier's superior knowledge, the aggrieved party should have a negligent misrepresentation claim. This reasoning is consistent with other jurisdictions that have specifically exempted the economic loss rule's application to professional negligence claims.³²²

Allowing an exception for any party in privity, due merely to a negotiated contract, to seek redress through a claim of negligent misrepresentation has the potential to vitiate the economic loss

317. RESTATEMENT (SECOND) OF TORTS § 552(1) (1977).

318. See, e.g., *infra* notes 331-36 and accompanying text (discussing *Wassall v. Payne*).

319. See RESTATEMENT (SECOND) OF TORTS § 552 cmts. c-d.

320. See *id.* § 552.

321. State v. United States Steel Corp., 919 P.2d 294, 311 (Haw. 1996).

322. See, e.g., *Moransais v. Heathman*, 744 So. 2d 973 (Fla. 1999); *Clark v. Rowe*, 701 N.E.2d 624 (Mass. 1998).

rule. It is precisely for this reason that "[w]ith increasing frequency, plaintiffs are presenting their negligence claims"—or more accurately their contract claims—"in the form of negligent misrepresentation in an attempt to circumvent the economic loss rule."³²³ An action for negligent misrepresentation when the parties are in privity is indistinguishable from an action for breach of contract.³²⁴ "If one is unable to meet his [contractual] obligation . . . has he not 'negligently misrepresented' his ability to do so?"³²⁵ If this is truly the intent of allowing an exception for "independent torts" it would be better "to drive that final coffin-nail" into the economic loss rule.³²⁶ Because the economic loss rule permits and encourages parties to allocate risk through contract negotiations,³²⁷ a tort action for negligent misrepresentation where the parties are in privity of contract affords no alternative relief other than to allow the parties to extricate themselves from a fairly negotiated bargain.³²⁸ Thus, for sophisticated commercial entities who deal with each other at arms length in contract negotiations, the economic loss rule should prevent recovery in negligent misrepresentation.

The question of recovery for third parties presents an entirely different analysis. To apply the economic loss rule to bar negligent misrepresentation claims by third parties would restore the "citadel of privity" that insulated defendants from liability caused by misperformance of a contractual duty.³²⁹ Reviewing

323. Fox & Loftus, *supra* note 163, at 268.

324. See *ALCES*, *supra* note 224, § 2.02[3][b], at 2-20; see also *Sunquest Info. Sys., Inc. v. Dean Witter Reynolds, Inc.*, 40 F. Supp. 2d 644, 651 (W.D. Pa. 1999) (explaining that a negligent misrepresentation claim between two parties in privity is "merely another way of stating [a] breach of contract claim." (quoting *Factory Mkt., Inc. v. Schuller Int'l, Inc.*, 987 F. Supp. 387, 395 (E.D. Pa. 1997))).

325. *Ocean Ritz of Daytona Condominium v. G6V Assocs., Ltd.*, 710 So. 2d 702, 705 (Fla. Dist. Ct. App. 1998).

326. *Id.*

327. See *Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1*, 881 P.2d 986, 990 (Wash. 1994); *supra* notes 51-55, 65-70 and accompanying text.

328. See *City Express, Inc. v. Express Partners*, 959 P.2d 836, 840 (Haw. 1998).

329. See *Floor Craft Floor Covering, Inc. v. Parma Community Gen. Hosp. Ass'n*, 560 N.E.2d 206, 213 (Ohio 1990) (Brown, J., dissenting) (making a similar point); *Rosseau v. K.N. Constr., Inc.*, 727 A.2d 190, 193 (R.I. 1999) (explaining that when the citadel of privity fell, it eliminated the consideration of whether privity exists in a tort action); *supra* notes 203-07 and accompanying text.

the facts of *Glanzer*, it is easy to see how courts rejecting a third-party privity exception to the economic loss rule would prevent liability to the bean-weigher today.³³⁰

*Wassall v. W.H. Payne*³³¹ illustrates perhaps the best example of how the economic loss rule should apply to negligent misrepresentation. In *Wassall*, the defendant made representations to the plaintiff and a third party about the flooding propensity of a piece of property.³³² The defendant knew at the time of negotiations that the third party intended to buy the land and then lease it to the plaintiff.³³³ Both the plaintiff and the third party relied on the misrepresentation in entering into their respective transactions.³³⁴ Similarly, the plaintiff in *Glanzer* was not in privity with the defendant and sought purely economic losses—damages incurred as a result of the weigher's negligent supply of information about the weight of the beans.³³⁵ Accordingly, both plaintiffs should be and were entitled to recover.

The outcome in *Wassall* demonstrates the sound reasoning of *Glanzer*, but an overbroad application of the economic loss rule, as some courts suggest, threatens to eliminate the reasoning of *Glanzer* altogether. Such an example establishes the correct application of the economic loss rule to negligent misrepresentation claims: When a foreseeable plaintiff, although not in privity, relied on the defendant's misrepresentations in entering into his transaction, the plaintiff should be entitled to recover from the defendant as a result of justifiable reliance on the defendant's misrepresentations.³³⁶ As Justice Cardozo recognized, potential pitfalls exist if the scope of negligent misrepresentation is unlimited.³³⁷ The extent of foreseeability of the plaintiff in relying

330. Compare *supra* notes 156-60 and accompanying text (discussing *Glanzer v. Shepard*, 135 N.E. 275 (N.Y. 1922)), with *supra* notes 207-08 and accompanying text (discussing the application of the economic loss rule to bar negligent misrepresentation claims by third parties).

331. 682 So. 2d 678 (Fla. Dist. Ct. App. 1997).

332. See *id.*

333. See *id.*

334. See *id.*

335. See *supra* notes 156-60 and accompanying text (discussing *Glanzer*).

336. See *Wassall*, 682 So. 2d at 681.

337. See *Ultramares Corp. v. Touche*, 174 N.E. 441, 445-46 (N.Y. 1931); *supra* note 158.

on the information is a question to be resolved by determination of the individual claim, it is not one to be resolved by a universal application of the economic loss rule to bar negligent misrepresentation claims by third parties.

CONCLUSION

The economic loss rule has become the rule of law in almost every jurisdiction. As application of the rule expands beyond the contours of products liability, applicability of the doctrine to torts other than strict liability and negligence has come to the forefront. The recent trend by courts in crafting an exception for intentional torts, including fraud, is correct. At least in part, states adopt the economic loss rule to promote predictable and uniform results in commercial transactions. Yet variation in methods of applying the economic loss rule to misrepresentation claims threatens to undermine that uniformity.

In applying the doctrine to misrepresentation claims, courts should be mindful of the basic purpose of the economic loss rule—to prevent the law of contract and the law of tort from dissolving into each other and the simple proposition that fraud unravels a contract. Just as overextension of products liability would drown contract in a sea of tort, so too would overapplication of the economic loss rule drown misrepresentation claims in a sea of contract. An analysis of the nature of damages and whether the misrepresentation is interwoven into the contract only suggests further analysis is required.

When fraudulent misrepresentations procure a contract, there is no agreement. In determining whether a contract truly was procured by fraud, courts should examine when the alleged misrepresentation was made and the significance of the misrepresentation. This analysis will ensure that the economic loss rule does not eviscerate a valid fraudulent inducement claim.

In contrast, creating an exception for a negligent misrepresentation claim between sophisticated commercial entities in privity does not protect an independent duty. Allowing those parties to escape their agreement merely by pleading negligent misrepresentation would vitiate the economic loss rule. The tort of negligent misrepresentation has its historic origins in protecting third parties. Accordingly an economic loss rule limitation on a third party's negligent misrepresentation claim serves no pur-

pose, other than to contradict the express reasons for the tort.

Unfettered application of the economic loss rule could potentially eviscerate fraud and negligent misrepresentation claims. Without workable exceptions for fraud and negligent misrepresentation, a judicial rule will eliminate a remedy where the policy justification is absent.³³⁸ As the Florida Supreme Court recently cautioned:

[T]he economic loss rule [has] . . . genuine, but limited, value [but it was] never intended to bar well-established common law causes of action. . . . Rather, the rule was primarily intended to limit actions in the products liability context, and its application should generally be limited to those contexts or situations where the policy considerations are substantially identical to those underlying the product liability type analysis The rule should not be invoked to bar well-established causes of action in tort.³³⁹

Prohibiting otherwise viable misrepresentation claims because of an improper expansion of the economic loss rule creates a system of recovery resting on the very ground that Justice Traynor sought to avoid in *Seely*: the "luck" of one plaintiff versus another.³⁴⁰ To permit such a result would contravene a fundamental duty of government to afford its citizens redress in the courts for injury, as "[t]he very essence of civil liberty certainly consists in the right of every individual to claim the protection of the laws, whenever he receives an injury."³⁴¹

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338. See, e.g., *supra* notes 8-19 and accompanying text (discussing the unavailability of remedies for the FRT-plywood plaintiffs).

339. *Moransais v. Heathman*, 744 So. 2d 973 (Fla. 1999); see also *Comptech Int'l, Inc. v. Milam Commerce Park, Ltd.*, No. 93,336, 1999 WL 983857, at *6-*7 (Fla. Oct. 28, 1999) (reiterating this caution and quoting portions of it).

340. See *Seely v. White Motor Co.*, 403 P.2d 145, 151 (Cal. 1965). More precisely, it rests on the luck of the defendant that the plaintiff will not discover its fraudulent misrepresentations within the UCC's statute of limitations.

341. *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 163 (1803); see also *Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d 1244, 1248 (Fla. 1993) (Barkett, J., dissenting) (suggesting that the lack of a remedy due to the application of the economic loss rule violated the Florida constitution); Ned Miltenberg, *The Revolutionary "Right to a Remedy,"* TRIAL, Mar. 1998, at 48 n.1 (listing the 38 state constitutions providing a right to a remedy).