# Common Law Fraudulent Misrepresentation and Negligent Misrepresentation

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## § 1.1 INTRODUCTION

The Great Recession generated a slew of claims for misrepresentation that, 10 years later, remain in litigation. Are plaintiffs casting blame for business decisions that succumbed to an unforgiving market? Or did the financial crisis expose actual misrepresentations that otherwise might have gone unnoticed? These questions have been the fulcrum of fraud cases nationwide.

This chapter addresses common law claims of fraudulent and negligent misrepresentation, focusing primarily on intentional misstatements or omissions. In addition to exploring the elements, it discusses strategies that plaintiffs and defendants can use to build their case and tell their story.

# § 1.2 ELEMENTS OF FRAUDULENT MISREPRESENTATION

Whether it is called common law fraud, fraudulent misrepresentation, or intentional misrepresentation, the elements of the claim are the same. The first three elements largely address the defendant's conduct or state of mind, and the last two address the plaintiff's. The elements are:

- (1) The defendant made a false representation of a past or existing material fact susceptible of knowledge.
- (2) The defendant did so knowing the representation was false, or without knowing whether it was true or false.
- (3) The defendant intended to induce the plaintiff to act in reliance on that representation.
- (4) The plaintiff acted in reliance on the defendant's false representation.
- (5) The plaintiff suffered pecuniary damage as a result of that reliance.

Valspar Refinish, Inc. v. Gaylord's, Inc., 764 N.W.2d 359, 368 (Minn. 2009); Hoyt Props. v. Prod. Res. Grp., LLC, 736 N.W.2d 313, 318 (Minn. 2007); Specialized Tours, Inc. v. Hagen, 392 N.W.2d 520, 532 (Minn. 1986). See also Martens v. Minnesota Mining & Mfg. Co., 616 N.W.2d 732, 747 (Minn. 2000) (breaking down claim into seven elements); Davis v. Re-Trac Mfg. Corp., 149 N.W.2d 37, 38–39 (Minn. 1967) (11 elements).

# § 1.3 FALSITY

Truth is an absolute defense to a claim of misrepresentation. "It is axiomatic that fraud cannot be predicated on the truth. A true representation is not actionable." *Franklin Theatre Corp. v. City of Minneapolis*, 198 N.W.2d 558, 560 (Minn. 1972) (quoting *Rien v. Cooper*, 1 N.W.2d 847, 851 (Minn. 1942)).

## § 1.4 REPRESENTATION BY AFFIRMATIVE MISSTATEMENT OR BY OMISSION

An affirmative misstatement—saying or writing something that is not true—is the most common form of false representation. But if there is a duty to disclose, silence may also constitute fraud. A failure to speak is actionable if there is a "suppression of facts which one party is under a legal or equitable obligation to communicate to the other, and which the other party is entitled to have communicated to him." *Richfield Bank & Trust Co. v. Sjogren*, 244 N.W.2d 648, 650 (Minn. 1976). The Minnesota Supreme Court has identified three "special circumstances" in which silence may be fraudulent.

## A. Half-Truth

"One who speaks must say enough to prevent his or her words from misleading the other party." *Id.*; see also Heidbreder v. Carton, 645 N.W.2d 355, 367 (Minn. 2002) ("A duty to disclose may exist ... when disclosure

would be necessary to clarify information already disclosed."). For example, in *Commercial Property Investments, Inc. v. Quality Inns Int'l, Inc.*, 938 F.2d 870, 877 (8th Cir. 1991), the defendant hotel franchisor touted the prospects of building a hotel in Roseville, citing the high occupancy rates of nearby hotels and the proximity of a civic center. The Eighth Circuit held that the defendant may be liable for fraud because it did not further disclose that the nearby hotels enjoyed advantages the new project lacked, and the civic center was failing. *Commercial Prop. Inv. Inc.*, 938 F.2d at 877 (applying Minnesota law).

# B. Special Knowledge

"One who has special knowledge of material facts to which the other party does not have access may have a duty to disclose these facts to the other party." *Richfield Bank*, 244 N.W.2d at 650. The party with special knowledge must "know[] that the other party acts on the presumption that no such facts exist." *Driscoll v. Standard Hardware*, *Inc.*, 785 N.W.2d 805, 812 (Minn. Ct. App. 2010) (quoting *Richfield Bank*). This exception rarely applies, particularly "in arm's-length business transactions between commercial entities." *Id.* at 813.

Richfield Bank was one of those rare instances. The plaintiff borrower sought financing to purchase goods from a manufacturer, which also was a depositor at the defendant bank. Richfield Bank, 244 N.W.2d at 649. The plaintiff executed a promissory note for the purchase, the proceeds of which went to the manufacturing company. Id. At that time, the bank's loan officer knew that the manufacturer was irretrievably insolvent, but said nothing. Id. at 649–50. The bank was found liable for fraud because the bank knew there was no reasonable way the manufacturer would fulfill its obligation to plaintiff. Id. at 651–52.

# C. Confidential or Fiduciary Relationship

"One who stands in a confidential or fiduciary relation to the other party to a transaction must disclose material facts." *Id.* at 650. Trustees, attorneys, and business partners may be among those with a duty to disclose. *See*, *e.g.*, *Appletree Square I Ltd. P'ship v. Investmark, Inc.*, 494 N.W.2d 889, 892 (Minn. Ct. App. 1993) (in selling property to fellow partners in a limited partnership, defendants had fiduciary duty to disclose presence of asbestos); *In re Boss*, 487 N.W.2d 256, 259 (Minn. Ct. App. 1992) (attorney had fiduciary duty to disclose his beneficial interest in client's transaction).

# § 1.5 PAST OR EXISTING FACTS SUSCEPTIBLE OF KNOWLEDGE

For a representation to be actionable, the subject of the alleged misstatement must be knowable as either true or false. The pattern jury instructions explain: "This means it must be possible to discover the fact." CIVJIG 57.10. Statements about past or existing facts generally are actionable, but predictions, opinions, and statements of law typically are not.

#### A. Statements About the Future

A statement about the future—i.e., a prediction or projection—does not support a claim of fraud just because the forecasted event does not occur. *Vandeputte v. Soderholm*, 216 N.W.2d 144, 147 (Minn. 1974); *see also Valspar*, 764 N.W.2d at 369 (alleged misrepresentations were not actionable because they "were expressions of confidence that the paint application problems would be resolved, and thus were predictions of future results"); *Kennedy v. Flo-tronics, Inc.*, 143 N.W.2d 827, 830 (Minn. 1966) (no fraud where "the prophecy or prediction of future value or profits is made in good faith and without a misrepresentation of fact").

That said, a statement about the future may give rise to fraud in at least two circumstances. First, a promise to perform may be fraudulent if "the promisor had no intention to perform at the time the promise was made." *Martens v. Minn. Mining & Mfg. Co.*, 616 N.W.2d 732, 747 (Minn. 2000) (quoting *Vandeputte*, 216 N.W.2d at 147). "A subsequent intention to break the promise or failure to fulfill it does not constitute fraud." *Benson v. Rostad*, 384 N.W.2d 190, 195 (Minn. Ct. App. 1986). Affirmative evidence of the promisor's contemporaneous intent is required. *Vandeputte*, 216 N.W.2d at 147; *Kramer v. Bruns*, 396 N.W.2d 627, 631 (Minn. Ct. App. 1986).

Second, predictions or projections may be fraudulent if they fail to "reflect past or present facts." *Berg v. Xerxes-Southdale Office Bldg. Co.*, 290 N.W.2d 612, 615 (Minn. 1980) (positive cash flow projection was actionable where defendant concealed current year's negative cash flow). Without new facts that would presage a turnaround, optimistic forecasts that are inconsistent with prior or current performance may amount to fraud. The Minnesota Supreme Court stated: "Projections should be considered actionable or not in fraud, depending upon whether they accurately reflect past and present circumstances." *Id.* 

## B. Statements of Pure Opinion

Expressions of pure opinion do not amount to fraud. "A wide variety of statements ordinarily used in sales negotiations are not actionable as fraud. These include ordinary sales puffing, statements of opinion, and promises of future performance." *Am. Computer Trust Leasing v. Jack Farrell Implement Co.*, 763 F. Supp. 1473, 1487 (D. Minn. 1991) (citations to Minnesota law omitted), *aff'd*, 967 F.2d 1208 (8th Cir. 1992). For example, in *American Computer Trust*, the defendant's statements that it was a "proven dealer in data processing" and "capable of dramatically increasing efficiency and profitability" were not actionable. *Am. Computer Trust*, 763 F. Supp. at 1487; *see also Smith v. Brutger Cos.*, 569 N.W.2d 408, 414 (Minn. 1997) (same for statements that building was "luxury apartment complex" and a "very safe environment").

## C. Statements of Law

An abstract statement of law or pure legal opinion likewise cannot be a fraudulent misrepresentation. *Hoyt*, 736 N.W.2d at 318. "[T]he law is presumed to be equally within the knowledge of both parties." *Miller v. Osterlund*, 191 N.W. 919, 919 (Minn. 1923). There are two exceptions, however. A general statement of law may be actionable when the speaker either "is learned in the field and has taken advantage of the solicited confidence of the party defrauded," or "stands with reference to the person imposed upon in a fiduciary or other similar relation of trust and confidence." *Northernaire Prods., Inc. v. Cnty. of Crow Wing*, 244 N.W.2d 279, 281 (Minn. 1976) (quoting *Stark v. Equitable Life Assurance Soc'y*, 285 N.W. 466, 469 (Minn. 1939)).

Additionally, a legal opinion that also "carries an implication of fact" may be actionable. *Hoyt*, 736 N.W.2d at 318. A mixed statement of law and fact may give rise to a fraud claim if: (1) it implies that facts exist that support the legal opinion expressed; and (2) the other party would ordinarily have no knowledge of those facts. *Id.* (allowing fraud claim to proceed where attorney stated there was no way to pierce the corporate veil, thereby implying that no facts existed to support veil piercing).

# § 1.6 DIRECT CONTACT NOT REQUIRED

The defendant need not communicate the misrepresentation directly to the plaintiff and may retain responsibility for false statements communicated through a third party. If the defendant knows and intends that the third party will relay the misrepresentation to the plaintiff, the defendant may be liable for fraud. Personal contact between the plaintiff and the defendant is not required. *See Vikse v. Flaby*, 316 N.W.2d 276, 284 (Minn. 1982) (corporate officers and directors were liable for false statements to broker who passed on misinformation to potential investors); *see also* 

Luckey v. Alside, Inc., 245 F. Supp. 3d 1080, 1094 (D. Minn. 2017) (discussing Vikse and related rule from Restatement (Second) of Torts § 533).

# § 1.7 MATERIALITY

A lie that has no impact on the listener does not amount to fraud. The false representation must affect the plaintiff's ultimate decision and conduct. "A statement of fact is material if it would naturally affect the conduct of the party addressed." *Yost v. Millhouse*, 373 N.W.2d 826, 830 (Minn. Ct. App. 1985).

In this formulation, materiality overlaps with actual and reasonable reliance. "If a party is justified in his belief that a representation is true and this belief substantially affects his decision to act, the representation is material." *Nave v. Dovolos*, 395 N.W.2d 393, 398 (Minn. Ct. App. 1986) (citing Prosser and Keeton on the Law of Torts § 108 (5th ed. 1984)); *see also Sit v. T&M Props.*, 408 N.W.2d 182, 186 (Minn. Ct. App. 1987) (representation is material "if it influenced a party's judgment or decision"); CIVJIG 57.10 ("A fact is material if it would have influenced the other person's judgment or decision had (he) (she) known about it.").

# § 1.8 FRAUDULENT INTENT

To be liable for fraudulent misrepresentation, a defendant need not mean to hurt anyone. The defendant who misrepresents his assets to obtain a loan, or overstates her customer base to close a deal, may believe nothing will come of the lie. With the loan proceeds, the defendant generate the revenue to service the debt. Or, with the deal closed, the defendant can attract the customers she claimed to have. In many instances, the defendant expects that its counterparty will be fully paid, and even profit. But when the transaction goes south for whatever reason, the defendant's expectations at the outset are no defense to fraud.

There are two components to the defendant's intent. First, what did the defendant know about the truth or falsity of his or her representation? "Fraudulent intent is, in essence, dishonesty or bad faith." *Florenzano v. Olson*, 387 N.W.2d 168, 173 (Minn. 1986). A defendant is dishonest when he or she makes a representation known to be false. *Id.* A defendant acts in bad faith when he or she speaks without knowing whether the statement is true or false. *Id.* The Minnesota Supreme Court explained: "Fraudulent intent is also present when a misrepresenter speaks positively and without qualification, but either is conscious of ignorance of the truth, or realizes that the information on which he or she relies is not adequate or dependable enough to support such a positive, unqualified assertion." *Id.* 

Second, did the defendant intend for the listener to act in reliance on the false misrepresentation? The intent-to-induce element may be satisfied where the defendant had reason to expect that the plaintiff would alter its conduct based on the misrepresentation and was substantially certain that the plaintiff would do so—even if the defendant did not actually intend for the plaintiff to alter its conduct. *See TCI Bus. Capital, Inc., v. Five Star Am. Die Casting, LLC*, 890 N.W.2d 423, 433 (Minn. Ct. App. 2017) (citing RESTATEMENT (SECOND) OF TORTS § 531 (1977)).

The facts of *TCI Business Capital* demonstrate how a defendant may be liable for fraud without meaning to hurt anyone. TCI's former chief restructuring officer (CRO) falsified TCI's books to show that a customer's debt was less than half of what the customer actually owed. *Id.* The CRO testified that he falsified the records because he wanted his supervisors to believe he was doing a good job, and he had his own plan to collect even beyond his bosses' expectations. *Id.* But the CRO was fired for unrelated reasons. *Id.* Unaware of the inaccuracy in its books, TCI settled with the customer for a fraction of the actual outstanding amount. *Id.* TCI later discovered the CRO's scheme and sued him, in part, for fraudulent misrepresentation. *Id.* The CRO testified that he never intended for TCI to settle in reliance on the inaccurate records; instead, he intended to recover the full amount. *Id.* at 435.

Even accepting the CRO's testimony, the court of appeals held there was enough evidence to establish fraudulent intent. *Id.* The CRO falsified TCI's records of outstanding customer debts, and he knew that TCI's practice was to rely on those records in pursuing settlement. *Id.* Even though the CRO never intended for TCI to settle based on the falsified records, and even though he did not personally gain from the settlement, he nonetheless had fraudulent intent. *Id.* 

In other cases, the defendant's intent to induce reliance is more straightforward. For example, in *Sorchaga v. Ride Auto, LLC*, 893 N.W.2d 360 (Minn. Ct. App. 2017), *aff'd*, 909 N.W.2d 550 (Minn. 2018), the plaintiff truck buyer alleged that the dealer intentionally misrepresented the condition of the truck. The circumstances surrounding the misrepresentation were enough to establish intent to induce the plaintiff's reliance. "Because Ride Auto knew its representation about the truck was false and it made that representation in the context of selling the truck, sufficient evidence supports the district court's finding that Ride Auto misrepresented the condition of the truck with the intention of inducing Sorchaga to purchase the truck." *Sorchaga*, 893 N.W.2d at 371.

# A. Proving Fraudulent Intent

The courtroom confession that closed every *Perry Mason* episode is confined to fiction. The witness who admits wrongdoing under a withering cross-examination alone does not exist. Likewise, few defendants will concede they made a misrepresentation knowingly or in bad faith, or with the purpose of inducing the plaintiff's reliance. Instead, the plaintiff must present other evidence of fraudulent intent.

Among the best proof: contemporaneous, usually internal, documents that are at odds with the representation. If the defendant's employees say one thing publicly and another privately, that may be evidence of fraud. Likewise, if documents indicate that corporate leadership possessed information counter to their public statements, these "red flags" may be evidence of outright dishonesty, or, at a minimum, making representations without knowing if they are true or false.

Because evidence of intent is often within the defendant's exclusive possession, custody, and control, a plaintiff should move quickly and proactively in document discovery. A fraud plaintiff should consider, among other things, the following:

- Hold Order. Notify the defendant immediately of its duty to preserve all relevant documents, particularly electronically-stored information (including texts and other smartphone data).
- **Document Collection**. Collaborate with the defendant on search terms, as well as custodians for the defendant's document collection.
- Buzz Words. In reviewing the defendant's production, search for words or phrases that may indicate fraud. A request to speak in person or by phone ("I'll stop by," "let's discuss," "call me") may indicate an effort to conceal. A plaintiff should also scour for words like "troubled," "concerned," or "worried," questions about ethics, and jokes about misconduct. Bullying, hostility, or curse words can also suggest fraud.
- Third-Party Subpoenas. Make liberal use of subpoenas to ensure a complete record. Bank statements, audit work papers, and the defendant's communications with lenders, suppliers, and other counterparties are sources of information known to the defendant that could contradict the representations to the plaintiff.

With these contemporaneous documents, the plaintiff should work to build a compelling narrative that explains why and how the defendant committed fraud. This story of motive and opportunity need not paint the de-

fendant as greedy or immoral. As discussed earlier, a common narrative is the defendant who is desperate to keep their business afloat. Jurors can sympathize with a defendant who made a bad choice, but they should still find the defendant liable for fraud.

# B. Showing an Innocent State of Mind

On the flip side, the defendant should develop a competing narrative showcasing his or her innocent state of mind. It rarely suffices to tackle the alleged misrepresentations one by one—e.g., the first was technically true, the plaintiff did not actually rely on the second, the third was mere puffery, and so on. The plaintiff always bears the burden of proof. But jurors—and judges on summary judgment—should understand the defendant's view of the big picture.

#### 1. Lack of Motive

If possible, a defendant should demonstrate there was no motive to defraud. For example, a sales agent may be accused of making a false representation to earn a commission. Why would a broker risk his or her all-important reputation just to earn a commission that is a fraction of annual compensation?

# 2. Knowledge at the Time, Not in Hindsight

In another scenario, subsequent events may establish beyond dispute that the defendant's prior representations were false. The defendant should then focus the judge and jury on what it knew and understood at the time, no matter what happened next. For example, the defendant may be the middleman who caused the plaintiff to do business with a now-insolvent company whose insiders have been exposed as criminals. How can the defendant counter accusations that it knowingly misrepresented the insolvent company's financial condition? The defendant may try to develop a narrative that it too was misled. While the insiders' misconduct may now be public, no one knew about it at the time. Instead, the defendant relied on market indicators—such as stock price, credit ratings, independent audit reports, and blue-chip clientele—that reflected a healthy and profitable company. To the extent the plaintiff now alleges that the defendant knew of "red flags" suggesting fraud, the plaintiff has the benefit of hindsight: at the time, those same facts were insignificant against the backdrop of the company's sterling reputation and strong performance. The defendant can strengthen its story if it also lost money in its own dealings with the company.

#### 3. Focus on the Plaintiff

A fraud defendant will typically spotlight the plaintiff's own conduct, knowledge, and motives. As detailed below, the plaintiff's experience, savvy, and intelligence is central to evaluating reasonable reliance. If possible, the defendant may want to show that the plaintiff was a sophisticated entity with industry expertise, had access to material information, and itself sought to score a huge profit despite known or knowable risks. Now, the defendant may argue, the plaintiff seeks to blame someone else for the consequences of its own decisions.

If the plaintiff had a hand in the fraud, the defendant may invoke the equitable doctrine of in pari delicto. This doctrine "operates to prevent wrongdoers at equal fault from recovering against one another," and it applies when the plaintiff knowingly and willingly participates in the misconduct. *Christians v. Grant Thornton LLP*, 733 N.W.2d 803, 810, 814 (Minn. Ct. App. 2007). It typically comes into play when the plaintiff is a trustee or receiver of a now-insolvent company that perpetrated a fraud, and the earlier corporate misconduct is imputed to the trustee or receiver who now stands in the company's shoes. *Id*.

## 4. Proactive Investigation

A defendant should not wait for discovery to develop the facts that compose its competing narrative. The defendant's counsel should consider immediately collecting core documents and interviewing key witnesses, before memories fade and employees leave. To ensure that the interview notes and memoranda are not discoverable, outside counsel should conduct the interviews, inform employees that these are privileged and confidential communications for the purpose of providing legal advice, and instruct them not to discuss the litigation among themselves or anyone else.

## § 1.9 ACTUAL RELIANCE

The plaintiff must actually rely on the false representation to his or her detriment. In other words, the plaintiff must establish that the misrepresentation in fact affected his or her conduct. The misrepresentation need not be the sole cause of the plaintiff's conduct, but it must have been a "substantial factor" in causing the plaintiff to act. *Davis v. Re-Trac Mfg. Corp.*, 149 N.W.2d 37, 39 (Minn. 1967).

Where the statement did not alter the plaintiff's course of action, however, he or she did not rely on it. For example, in *Popp Telecom, Inc. v. American Sharecom*, 361 F.3d 482, 491–92 (8th Cir. 2004), the plaintiffs were dissenting shareholders who failed to prevent a corporate merger; they then sued and alleged that the acquiring corporation made false representations in trying to induce them to sell their shares. However—even though the merger went through—the plaintiffs could not establish actual reliance because they were never convinced to sell their shares and instead voted against the merger. *Popp Telecom, Inc.*, 361 F.3d at 491–92 (applying Minnesota law).

Likewise, there can be no reliance when the plaintiff took the complained-of action before learning of the alleged misrepresentation. *Watkins v. Lorenz*, 119 N.W.2d 482 (Minn. 1963); *Rien v. Cooper*, 1 N.W.2d 847, 853 (Minn. 1942) ("Fraud cannot be predicated upon a representation made subsequent to the act claimed to have been induced thereby.").

## § 1.10 REASONABLE RELIANCE

It is not enough that the plaintiff actually rely on the fraudulent misrepresentation; the plaintiff's reliance must be reasonable. Hoyt Props. v. Prod. Res. Grp., LLC, 736 N.W.2d 313, 321 (Minn. 2007).

The reasonableness of reliance is a subjective standard that varies by the specific plaintiff. "Reliance in fraud cases is generally evaluated in the context of the aggrieved party's intelligence, experience, and opportunity to investigate the facts at issue." *Valspar Refinish, Inc. v. Gaylord's, Inc.*, 764 N.W.2d 359, 369 (Minn. 2009). One standard applies to the individual of limited education who ventures outside of his or her field to do business with a large company, and another to a sophisticated corporation that engages in a typical transaction with a comparable business entity. As the Eighth Circuit put it: "Fraud must be proved with reference to the specific intelligence and experience of the party alleging it." *Children's Broad. Corp. v. Walt Disney Co.*, 245 F.3d 1008, 1020 (8th Cir. 2001) (applying Minnesota law). Reasonableness cannot typically be resolved on summary judgment and usually is a fact-intensive question for the jury to decide—even when the plaintiff is sophisticated, educated, and experienced in the matters at hand. *Hoyt*, 736 N.W.2d at 321 (holding that reasonable reliance was a jury question despite plaintiff's extensive business and legal background).

"A party can reasonably rely on a representation unless the falsity of the representation is known or obvious to the listener." *Id.* (citing *Spiess v. Brandt*, 41 N.W.2d 561, 566 (Minn. 1950)). There is no duty to investigate, *id.*, but a party who does investigate is held to the results of his or her investigation. "When a party conducts an independent

factual investigation before it enters into a commercial transaction, that party cannot later claim that it reasonably relied on the alleged misrepresentation." *Valspar*, 764 N.W.2d at 369 (reliance was not reasonable where both parties were "sophisticated business equals operating in a commercial setting," and plaintiff conducted its own investigation and experimentation on defendant's product).

# A. Reliance on Extra-Contractual Representations

Although the reasonableness of reliance is usually ill-suited for summary judgment, there is an exception to this general rule. In a common scenario, the plaintiff alleges that the defendant's fraudulent misrepresentation induced it to enter into a written contract. But if the written contract directly contradicts the alleged oral misrepresentation, reliance on the oral statement is unreasonable as a matter of law. *Dahmes v. Indus. Credit Co.*, 110 N.W.2d 484, 490 (Minn. 1961). In other words, if "the written contract provision explicitly stated a fact completely contradictory to the claimed misrepresentation," the plaintiff cannot establish reasonable reliance. *Johnson Bldg. Co. v. River Bluff Dev. Co.*, 374 N.W.2d 187, 194 (Minn. Ct. App. 1985). The Minnesota Court of Appeals has increasingly invoked this rule to resolve fraud claims on summary judgment, but it has not designated its decisions for publication.

The key question is: Can the alleged oral misrepresentation and the written contract provision both be true? The court carefully compares the content of the alleged oral misrepresentation with the text of the written contract. If the plaintiff could accept both as true, then reliance on the oral statement may remain reasonable. But if the oral representation cannot be reconciled with the parties' agreed writing, then reliance is unreasonable as a matter of law.

For example, in *Crowell v. Campbell Soup Co.*, 264 F.3d 756, 762–64 (8th Cir. 2001), the plaintiff farmers alleged that the defendant induced them to enter into a poultry production contract through a variety of oral misrepresentations, including that the contract could be terminated only for cause, that there would be a long-term commitment to continue placing flocks with the plaintiffs beyond 35 to 40 flocks, and that the plaintiffs would realize a certain amount of profits per year after the first seven or eight years. The Eighth Circuit scrutinized each alleged misrepresentation, and found that none could be reconciled with the contract's written terms. *Crowell*, 264 F.3d at 762–64. First, the contract permitted termination "essentially any time," which "plainly contradicts" the alleged oral promise to terminate only "for cause." *Id.* at 763. Second, the alleged long-term commitment beyond 35 to 40 flocks was likewise "in plain contradiction of the written contract provisions granting to [the defendant] the express right to terminate the contracts *prior to* the placement of 35 or 40 flocks." *Id.* (emphasis in original). Third, the alleged revenue misrepresentation also "plainly contradicts" the contract's termination-at-will provision and payment schedule. *Id.* at 763–64.

Where, however, the plaintiff could conceivably accept as true both the oral and the written statements without inconsistency, reasonable reliance remains for the jury. For example, in *Northstar Industries, Inc. v. Merrill Lynch & Co., Inc.*, 558 F. Supp. 2d 944 (D. Minn. 2008), the plaintiff broker alleged it slashed its finder's fee from \$7.1 million to \$1.5 million in reliance on the defendant's representation that all parties were taking pro rata cuts to close a deal, which otherwise "would be dead." The defendant contended that any claim of fraudulent inducement was directly contradicted by the parties' written agreement, which stated that defendant would "in no case" pay plaintiff more than \$1.5 million. The court disagreed and explained that "such contract language does not contradict alleged promises about pro rata reductions and the potential death of the deal. Indeed, the ... agreement contains no reference to pro rata reductions or deal saving actions, and without explicit mention of these matters, there can be no complete contradiction." *Northstar Indus. Inc.*, 558 F. Supp. 2d at 949.

#### B. Disclaimers of Reliance

In Minnesota, integration clauses and general contractual disclaimers of reliance do not preclude reasonable reliance as a matter of law. A commercial contract typically provides that the written document composes the parties' entire agreement and supersedes all prior agreements, understandings, promises, and the like with respect to the subject matter. In the same vein, the parties expressly disclaim reliance on any representations and warranties that are not included in the written contract.

General disclaimers of reliance do not bar claims of misrepresentation under Minnesota law. This reflects a policy choice made many years ago: a party may not escape liability for fraudulent statements by providing in the contract that the other party should not rely on them. "The law should not and does not permit a covenant of immunity to be drawn that will protect a person against his own fraud." *Ganley Bros., Inc. v. Butler Bros. Bldg. Co.*, 212 N.W. 602, 603 (Minn. 1927); *see also Nat'l Equip. Corp. v. Volden*, 252 N.W. 444, 445 (Minn. 1934) ("A party who makes fraudulent misrepresentations to induce another to make a contract cannot escape liability for his fraud by incorporating a disclaimer of fraud in the contract.").

The Minnesota Supreme Court most recently affirmed this policy in *Sorchaga v. Ride Auto, LLC*, 909 N.W.2d 550 (Minn. 2018). The court held that a seller's fraudulent misrepresentation about the condition of goods to a consumer prevents the merchant from disclaiming the implied warranty of merchantability. *Sorchaga*, 909 N.W.2d at 554–57. Enforcing "as is" disclaimers under these facts would allow a seller "to profit from its fraud and to be effectively granted a license to mislead or conceal facts." *Id.* at 556 (internal citation, quotation marks, and brackets omitted).

Where the disclaimer is specific to the subject matter of the intentional misrepresentation, it still may not preclude reliance as a matter of law. *See Dakota Bank v. Eiesland*, 645 N.W.2d 177, 184–85 (Minn. Ct. App. 2002). Instead, where the plaintiff alleges that the defendant acted with fraudulent intent, the significance of the disclaimer typically is for the jury to decide. *Id.*; *see also St. Croix Printing Equip. v. Rockwell Int'l Corp.*, 428 N.W.2d 877, 881–82 (Minn. Ct. App. 1988).

Even assuming the court declines to rule as a matter of law, is there any reason to include disclaimers of reliance in contracts under Minnesota law? There are at least two. First, disclaimers should factor into the jury's fact-intensive evaluation of reasonable reliance, particularly where the plaintiff is sophisticated and experienced. The defendant can emphasize that the plaintiff's assertions of reliance in court are at odds with his or her own representations when executing the contract. The defendant can ask: Was the plaintiff lying then, or lying now? Second, even if the disclaimers do not defeat the fraud claim, they should preclude a claim for breach of contract based on the same misrepresentation, which can yield a greater recovery.

# § 1.11 DAMAGES AND REMEDIES

## A. Compensatory Damages

Money damages are an essential element of fraud. *Nodland v. Chirpich*, 240 N.W.2d 513, 517 (Minn. 1976). Minnesota measures a fraud plaintiff's damages by his or her out-of-pocket loss—that is, the difference between the value of the property received and the price paid, plus "any special damages naturally and proximately caused by the fraud prior to its discovery, including expenses incurred in mitigating damages." *B.F. Goodrich Co. v. Mesabi Tire Co.*, 430 N.W.2d 180, 182 (Minn. 1988). Minnesota is in the minority. Most states permit a fraud plaintiff to recover the benefit of the bargain—that is, the difference between the value of the property actually received and the value the plaintiff would have received if the representations had been true. *Id.* 

The "out-of-pocket loss" measurement assumes that the plaintiff received something from the defendant, and paid more than its true value because of the defendant's false representation. Because not all misrepresentations fit these facts, "Minnesota courts have ... taken a broad view of what constitutes out-of-pocket losses." *Commercial Prop. Invs., Inc. v. Quality Inn Int'l, Inc.*, 61 F.3d 639, 647 (8th Cir. 1995). The Eighth Circuit characterized Minnesota's approach in practice as a hybrid of "a strict application of the out-of-pocket loss rule and the more liberal benefit-of-the-bargain rule." *Id.*; *see also Jensen v. Peterson*, 264 N.W.2d 139, 143 (Minn. 1978) (noting that the court "has been flexible in the past where the strict application of an out of pocket damage rule would fail to do substantial justice").

Where a strict "out-of-pocket" calculation would not return the plaintiff to the status quo, the court may award all economic loss that is the direct and natural consequence of the misrepresentation. *Lewis v. Citizens Agency of Madelia, Inc.*, 235 N.W.2d 831 (Minn. 1975). In *Lewis*, the defendant insurance agent said that the plaintiff's premium payments would purchase an insurance policy on her husband's life, when in fact they secured only an annuity. A strict out-of-pocket measurement would recover her annuity payments, but not the life insurance proceeds that plaintiff thought she purchased—and now needed. Because refunding the premiums alone would not make the plaintiff whole, she could recover the lost insurance proceeds as her full economic injury. *Id.* Similarly, in *Hughes v. Sinclair Marketing, Inc.*, 389 N.W.2d 194, 199 (Minn. 1986), the Minnesota Supreme Court affirmed an award of lost future profits because out-of-pocket damages would not have returned the plaintiff to the status quo.

No matter the measurement, the plaintiff must establish that the false representation proximately caused the damages. *Driscoll v. Standard Hardware, Inc.*, 785 N.W.2d 805, 811–12 (Minn. Ct. App. 2012) (affirming dismissal of fraud claim on summary judgment for lack of proximate cause); *Bryan v. Kissoon*, 767 N.W.2d 491, 495–96 (Minn. Ct. App. 2009) (affirming judgment as matter of law on same grounds).

#### **B.** Rescission

Where the plaintiff was fraudulently induced to enter into a contract, the plaintiff may seek to rescind the contract as a remedy for the intentional misrepresentation. *U.S. Installment Realty Co. v. De Lancy Co.*, 188 N.W. 212 (Minn. 1922). Rescission voids the contract and returns the parties to the position they occupied before the contract was formed. *Hatch v. Kulick*, 1 N.W.2d 359, 360 (Minn. 1941).

While fraud otherwise need be established only by a preponderance of the evidence, the remedy of rescission requires "clear and convincing evidence." *Weise v. Red Owl Stores, Inc.*, 175 N.W.2d 184, 187 (Minn. 1970); *Bolander v. Bolander*, 703 N.W.2d 529, 541 (Minn. Ct. App. 2005). "Clear and convincing evidence" is more than a preponderance, "but less than proof beyond reasonable doubt." *Weber v. Anderson*, 269 N.W.2d 892, 895 (Minn. 1978).

An alleged victim of fraud must act diligently and promptly in seeking to rescind. *Clark v. Reddick*, 791 N.W.2d 292, 294 (Minn. 2010); *Hemming v. Ald, Inc.*, 155 N.W.2d 384, 387 (Minn. 1967) (citing principles of waiver, laches, and estoppel); *Johns v. McGenty*, 23 N.W.2d 289, 292 (Minn. 1946) ("The power of avoidance from fraud or misrepresentation is lost if, after acquiring knowledge thereof, the injured party unreasonably delays manifesting to the other party his intention to avoid the transaction."); *Everson v. J.L. Owens Mfg. Co.*, 176 N.W. 505, 506–07 (Minn. 1920) (the defrauded party "cannot sleep on his rights, but must be reasonably diligent in seeking his remedy, and if he delays beyond a reasonable time, his right to rescind is lost").

A plaintiff waives the right to rescind if, after discovering the alleged fraud, the plaintiff chooses to perform the contract and accept its benefits. *Proulx v. Hirsch*, 155 N.W.2d 907, 912 (Minn. 1968); *Carpenter v. Vreeman*, 409 N.W.2d 258, 261–62 (Minn. Ct. App. 1987); *see also Shell Petroleum Corp. v. Anderson*, 253 N.W. 885, 887

(Minn. 1934) ("defrauded parties cannot disaffirm a contract after having affirmed it with knowledge of the fraud"). "To establish a waiver or ratification of fraud, there must be evidence that the waiving party had full knowledge of the facts and his or her legal rights, and intended to relinquish these rights." *Carpenter*, 409 N.W.2d at 262.

# C. Punitive Damages

A plaintiff alleging fraudulent misrepresentation may ask to recover punitive damages. The purpose of punitive damages is to punish the defendant and deter others from similar misconduct; it is not to compensate the plaintiff. *See* CIVJIG 94.10; *Hodder v. Goodyear Tire & Rubber Co.*, 426 N.W.2d 826, 837 (Minn. 1988). The plaintiff must prove by "clear and convincing evidence that the acts of defendant show deliberate disregard for the rights or safety of others." MINN. STAT. § 549.20, SUBD. 1(a). "Deliberate disregard" means that the defendant: (1) knew or intentionally ignored facts that created a high probability of injury to the rights or safety of others; and (2) deliberately acted with conscious or intentional disregard or with indifference to that risk. MINN. STAT. § 549.20, SUBD. 1(b); CIVJIG 94.10. The statute specifies various factors for the jury to consider in deciding the amount of punitive damages. MINN. STAT. § 549.20, SUBD. 3.

The initial complaint may not seek punitive damages. MINN. STAT. § 549.191. Instead, the plaintiff must move to amend the pleadings and show the factual basis for claiming punitive damages. *Id.* The court shall permit amendment if it finds prima facie evidence in support. *Id.* "Prima facie' does not refer to a quantum of evidence, but to a procedure for screening out unmeritorious claims for punitive damages." *Swanland v. Shimano Indus. Corp.*, *Ltd.*, 459 N.W.2d 151, 154 (Minn. Ct. App. 1990). The court continued: "The trial court may not allow an amendment where the motion and supporting affidavits 'do not reasonably allow a conclusion that clear and convincing evidence will establish the defendant acted with [deliberate disregard]...." *Id.* (quoting *McKenzie v. N. States Power Co.*, 440 N.W.2d 183, 184 (Minn. Ct. App. 1989)).

## § 1.12 NEGLIGENT MISREPRESENTATION

Negligent and fraudulent misrepresentation share many common elements. "We have said in the past that negligent misrepresentation constitutes fraud." *Hardin Cnty. Sav. Bank v. Housing & Redevelopment Auth. of the City of Brainerd*, 821 N.W.2d 184, 191 (Minn. 2012) (citing *Gen. Ins. Co. of Am. v. Lebowsky*, 252 N.W.2d 252, 255 (Minn. 1977)).

There are important differences, however. Chiefly, to be liable for negligent misrepresentation, the defendant need act only negligently, and not dishonestly or in bad faith. *See Florenzano v. Olson*, 387 N.W.2d 168, 173 (Minn. 1986) ("Fraud is distinguished from negligence by the element of scienter required."). To avoid widespread liability, the Minnesota Supreme Court has also narrowed the scope of a negligent misrepresentation claim—in particular, by limiting the duty of care. The elements are:

- (1) the defendant was acting in the ordinary course of their business, profession, or employment, or in any other transaction in which the defendant has a pecuniary interest;
- (2) the defendant owed a duty of care to the plaintiff;
- (3) the defendant supplied false information to guide the plaintiff in the plaintiff's own business transactions;
- (4) the defendant failed to exercise reasonable care in communicating the information;
- (5) the plaintiff justifiably relied on the false information; and

(6) the plaintiff was financially harmed by relying on the information (i.e., suffered pecuniary loss).

Hardin Cnty. Sav. Bank, 821 N.W.2d at 192; Williams v. Smith, 820 N.W.2d 807, 815 (Minn. 2012); Bonhiver v. Graff, 248 N.W.2d 291, 298 (Minn. 1976).

# A. Duty of Care

The nature of the parties' relationship determines whether a duty of care exists in communicating information. Particular professional or fiduciary relationships can give rise to a duty of care because one party is entitled to legal protection. The Minnesota Supreme Court has "recognized a duty exists in professional relationships such as an accountant/client and an attorney/client, and in certain fiduciary relationships involving, for example, guardians, executors, and directors of corporations." *Williams*, 820 N.W.2d at 816 (citing cases). *See also Hardin Cnty. Sav. Bank*, 821 N.W.2d at 193–94 (holding that banks stated claim of negligent misrepresentation against appraiser for allegedly faulty appraisal and feasibility study).

But the Minnesota Supreme Court has generally hesitated to recognize a duty outside of a professional or fiduciary relationship. The most notable exception is *M.H. v. Caritas Family Services*, 488 N.W.2d 282 (Minn. 1992), where the court held a special legal relationship existed because one party had superior knowledge. There, an adoption agency undertook to disclose some information about the birth parents and their genetic history, but withheld other facts that rendered the information misleading. *M.H.*, 488 N.W.2d 282. The supreme court held that public policy favored a duty of care to protect the adoptive parents against the agency's conduct. *Id.* 

More recently, the supreme court stressed the "limited scope of negligent misrepresentation." *Williams v. Smith*, 820 N.W.2d 807, 817 (Minn. 2012). The court wrote, "our recent cases have carefully limited recognition of the tort of negligent misrepresentation, against both private actors and government officials.... These recent decisions are consistent with earlier decisions in which we have rejected an expansive view of both negligent misrepresentation and government liability." *Id.* at 821 (citations omitted).

In *Williams*, a would-be assistant coach sued Tubby Smith, the head basketball coach at the University of Minnesota. The plaintiff quit his job on receiving an employment offer from Smith, only to be told the next day that the athletic director nixed the offer. *Id.* at 809–10. The plaintiff alleged that Smith negligently misrepresented his authority to hire. The supreme court found that Smith, as a government employee, owed no duty of care to the plaintiff, as a prospective government employee. *Id.* at 815–22. The court gave three reasons. First, the plaintiff and Smith did not stand in a professional or fiduciary relationship, Smith was not advising the plaintiff, and Smith did not have superior knowledge or expertise. *Id.* at 818–19. Second, the nature of the relationship "was that of two sophisticated business people, both watching out for their individual interests while negotiating at arm's length." *Id.* at 819. Third, there was no public policy rationale to impose a duty between sophisticated parties negotiating prospective employment. *Id.* 

The Minnesota Court of Appeals similarly has held that no duty of care exists in a commercial transaction "where adversarial parties negotiate at arm's length." *Smith v. Woodwind Homes, Inc.*, 605 N.W.2d 418, 424 (Minn. Ct. App. 2000) (affirming dismissal of negative misrepresentation claim); *see also Safeco Ins. Co. of Am. v. Dain Bosworth, Inc.*, 531 N.W.2d 867, 871 (Minn. Ct. App. 1995) (same). While the Minnesota Supreme Court has side-stepped this issue, it has observed that "other state courts that have considered the issue have not extended the duty of care to an arm's length commercial transaction." *Williams*, 820 N.W.2d at 817 (citing cases). The court continued: "The underlying reasoning is that sophisticated parties negotiating a commercial transaction are entitled to legal protection only for intentional, fraudulent conduct." *Id.* (citing RESTATEMENT (SECOND) OF TORTS § 552 (1979)).

## B. Reasonableness of Reliance

In considering whether the plaintiff's reliance on a negligent misrepresentation was reasonable, courts use much the same analysis that applies to reliance on an intentional misrepresentation. But the case law flags at least one significant distinction. A specific written disclaimer that addresses the subject of an intentional misrepresentation typically does not preclude justifiable reliance as a matter of law. With respect to a negligent misrepresentation, however, a specific disclaimer does preclude reliance. For example, in *Dakota Bank v. Eiesland*, 645 N.W.2d 177, 183–85 (Minn. Ct. App. 2002), the plaintiff bank alleged that it relied on audited compiled financial statements that it received from the defendant accountants, even though the statements "contained disclaimers clearly stating that the statements were based on the unaudited representations of the company's management and that the accountants did not express an opinion on them." The court of appeals held that these disclaimers barred the bank's negligent misrepresentation claim, but they did not bar the claim for intentional misrepresentation. *Eiesland*, 645 N.W.2d at 183–85.

Another example is *McIntosh County Bank*, in which the Minnesota Court of Appeals held that a specific disclaimer of reliance barred a claim of negligent misrepresentation as a matter of law. *McIntosh Cnty. Bank v. Dorsey & Whitney LLP*, 726 N.W.2d 108, 119–20 (Minn. Ct. App. 2007), *rev'd in part on other grounds, McIntosh Cnty. Bank v. Dorsey & Whitney LLP*, 745 N.W.2d 538 (Minn. 2008). The case involved a loan participation agreement through which various banks purchased interests in a casino loan. The participating banks alleged that the lead lender's counsel misrepresented the enforceability of the loan. The court of appeals held that any reliance was not justifiable in light of the specific disclaimers in the participation agreement. *Id.* at 120. The contract required the banks to affirm that they had made "an independent and informed judgment" with respect to the loan, and to acknowledge that the lead lender made no warranty or representation regarding enforceability. *Id.*; *see also Leonard v. Dorsey & Whitney LLP*, 553 F.3d 609, 630 (8th Cir. 2009) (under the Minnesota Court of Appeals' decision in *McIntosh*, the contractual disclaimer "effectively negates" the justifiability of the participating banks' reliance).

## C. Standard of Care, Comparative Fault, and Damages

A defendant accused of negligent misrepresentation is held to the standard of care of a reasonably prudent person in the profession. *See Florenzano v. Olson*, 387 N.W.2d 168, 174 (Minn. 1986) ("A misrepresentation is made negligently when the misrepresenter has not discovered or communicated certain information that the ordinary person in his or her position would have discovered or communicated."); *Grueling v. Wells Fargo Home Mortg., Inc.*, 690 N.W.2d 757, 760 (Minn. Ct. App. 2005) ("An objective standard of reasonable care is applied to those who make misrepresentations in the course of their employment.").

Consistent with this standard of care, "the principles of comparative responsibility apply to negligent misrepresentation." *Florenzano*, 387 N.W.2d at 176 (holding that trial court properly applied comparative fault statute).

In the same vein, a plaintiff may not recover punitive damages for a negligent misrepresentation. *See Utecht v. Shopko Dep't Store*, 324 N.W.2d 652, 654 (Minn. 1982) (no punitive damages for negligent conduct). The plaintiff may recover only his or her pecuniary loss. *Smith v. Brutger Cos.*, 569 N.W.2d 408 (Minn. 1997); *Flynn v. Am. Home Prods. Corp.*, 627 N.W.2d 342, 351 (Minn. Ct. App. 2001).

#### D. Economic Loss Doctrine and Minnesota Statutes Section 604.101

Under Minnesota Statutes section 604.101, a "buyer may not bring a common law misrepresentation claim against a seller relating to the goods sold or leased unless the misrepresentation was made intentionally or recklessly." This statute bars a buyer's negligent misrepresentation claim that relates to the goods sold or leased. *Valspar Refinish Inc.* v. *Gaylord's*, *Inc.*, 764 N.W.2d 359, 369–70 (Minn. 2009) (holding section 604.101 barred claim that seller

negligently misrepresented its ability to supply paint product that would apply evenly and consistently to surface of buyer's vehicle accessories).

Section 604.101 "exhaustively states the economic loss doctrine" in Minnesota, and "there is no residual common law economic loss doctrine." *Ptacek v. Earthsolis, Inc.*, 844 N.W.2d 535, 538–39 (Minn. Ct. App. 2014) (citation and internal quotation marks omitted). Where it applies, the economic loss doctrine bars a party from suing in tort for purely monetary loss, as opposed to suing for physical injury or property damage. *Id.* at 538. Accordingly, a buyer may not sue for negligent misrepresentation relating to the goods, but the buyer may sue for intentional misrepresentation (assuming the facts support such a claim).

# § 1.13 PLEADING REQUIREMENTS AND STANDARD OF PROOF

Intentional and negligent misrepresentation share the same pleading requirements and standard of proof. Both are subject to the heightened pleading standards of Minnesota Rule of Civil Procedure 9.02. *Hardin Cnty. Sav. Bank*, 821 N.W.2d at 191.

"General allegations of fraud are insufficient to meet the requirements of Rule 9.02." *Stubblefield v. Greenberg*, 426 N.W.2d 912, 914–15 (Minn. 1988). Rule 9.02 provides that "in all averments of fraud ... the circumstances constituting fraud ... shall be stated with particularity. Malice, intent, knowledge, and other conditions of mind of a person may be averred generally." To satisfy Rule 9.02, the factual allegations must support each element. "To plead with particularity is to plead the 'ultimate facts' or the 'facts constituting fraud.' A party pleads the 'ultimate facts' of a fraud claim when it pleads facts underlying each element of the fraud claim." *Hardin Cnty. Sav. Bank*, 821 N.W.2d at 191 (internal citations omitted). *See also Juster Steel v. Carlson Cos.*, 366 N.W.2d 616, 619 (Minn. Ct. App. 1985) (affirming dismissal of fraud claim under Rule 9.02 because the complaint "facially assert[s] false representations" and only "vaguely refers to the content of the misrepresentations").

The Minnesota Court of Appeals has endorsed the federal formulation that the circumstances to be pleaded with particularity "are the time, place, and contents of the false representations, as well as the identity of the person making the misrepresentation and what he obtained thereby." *Baker v. Best Buy Stores, LP*, 812 N.W.2d 177, 184 (Minn. Ct. App. 2012) (citation omitted). Meanwhile, "particularity" is "construed to mean the who, what, when, where, and how: the first paragraph of any newspaper story." *Id.* (citation omitted).

The standard of proof for both intentional and negligent misrepresentation is the preponderance of the evidence. *See State by Humphrey v. Alpine Air Prods., Inc.*, 500 N.W.2d 788, 791 (Minn. 1993); *Dowden v. Kanuch*, 196 N.W. 819, 819 (Minn. 1924).

# § 1.14 STATUTE OF LIMITATIONS

Intentional and negligent misrepresentation also share the same six-year limitations period, which begins to run when the plaintiff discovers "the facts constituting the fraud." MINN. STAT. § 541.05, SUBD. 1(6). "The facts constituting the fraud are deemed to have been discovered when they were actually discovered or, 'by reasonable diligence, should have been discovered." *Doe v. Archdiocese of St. Paul and Minneapolis*, 817 N.W.2d 150, 172 (Minn. 2012) (quoting *Toombs v. Daniels*, 361 N.W.2d 801, 809 (Minn. 1985)). The plaintiff bears the burden of proving, under a reasonable person standard, that he or she should not have discovered the underlying facts earlier. *Id.*; *Jane Doe 43C v. Diocese of New Ulm*, 787 N.W.2d 680, 684 (Minn. Ct. App. 2010). Whether a plaintiff exercised due diligence is "ordinarily a question of fact" for the jury to decide, but the court may resolve the issue as a matter of law "where the evidence leaves no room for reasonable minds to differ." *Jane Doe 43C*, 787 N.W.2d at 684–85.