

discriminatory state taxation of interstate transactions,¹³ raise as many problems as they solve.¹⁴ In view of the half-hearted success of state attempted solutions, it would seem that a better approach to the solution of state income difficulties must lie along national lines. It is submitted that a general federal tax on all sales—interstate and intrastate—with an apportionment back to the states on a population-wage rate basis is a possible solution.

Torts—Liability for Accountants' Misrepresentations—[New York].—The defendant accountant, employed by a corporation which subsequently became insolvent, prepared ten copies of a financial statement with knowledge that they were to be used to obtain credit. The corporation did use one of these statements to secure a \$300,000 loan from the plaintiff. Material facts as to the stagnancy of accounts receivable and the possible inadequacy of reserves set up, of which the defendant had knowledge, were not indicated on the balance sheet in accordance with usual accounting practice, but were disclosed in a single copy of a letter sent to the corporation thirty days later. This action was brought for damages which the plaintiff suffered by reliance on the defendant's negligently made financial statement. On appeal from a judgment of Appellate Division affirming a judgment for the defendant, *held*, reversed. The evidence was sufficient to support a finding of gross negligence raising an inference of fraud. *State Street Trust Co. v. Ernst and Ernst*.¹

The New York court in *Ultramares Corporation v. Touche*² repudiated the view adopted a short time previously that one who made a negligent misrepresentation to another with knowledge of such other's intention to induce thereby the reliance of a third party, should be held liable.³ The court there decided that a negligent misrepresentation of this type which would be passed on to an indefinite class of possible reliers should not be actionable as negligence and could support liability only if the circumstances under which it was made indicated evidence of such gross negligence that the inference of fraud could be drawn. The principal case purports to follow the *Ultramares* case in that it places in the fraud category liability to third parties for gross negligence. The constant reliance for authority, however, by both the majority and dissenting opinions in the case indicates the difficulty of applying the doctrine.⁴ In imposing liability the court recognized the need of stricter requirements of accuracy in financial statements because of the increasing dependence by business on such reports.⁵

¹³ Such a bill was passed by the United States Senate in 1934—78 Cong. Rec. 4598 (1934)—but died in the House Committee on Interstate and Foreign Commerce.

¹⁴ Johnson, State Sales Taxes and the Commerce Clause, 24 Calif. L. Rev. 155, 170 (1936); Lowndes, State Taxation of Interstate Sales, 7 Miss. L. J. 223 (1935); Perkins, The Sales Tax and Transactions in Interstate Commerce, 12 N. C. L. Rev. 99, 108 (1933).

¹ 278 N.Y. 104, 15 N.E. (2d) 416 (1938).

² 255 N.Y. 170, 174 N.E. 441 (1931).

³ *Glanzer v. Shepard*, 233 N.Y. 236, 135 N.E. 275 (1922); *International Products Co. v. Erie Ry. Co.*, 244 N.Y. 331, 155 N.E. 662 (1927).

⁴ Baldwin, Liability of Public Accountants, 52 Journal of Accountancy 342 (1931).

⁵ 3 Corp. Proc. Rev. 57 (1931). George S. Olive, Conduct of an Accounting Practice, American Institute of Accountants (October, 1929). Consider Securities and Exchange Commission of the federal government.

It failed, however, to take advantage of an opportune situation to improve the nebulous basis of liability to an indefinite class of third parties enunciated in the *Ultramares* case.

Due to an early misconception of the holding in *Derry v. Peek*,⁶ courts have, with several exceptions,⁷ traditionally refused to make a defendant liable to third parties for a negligent misstatement when there was no contractual privity, confining such liability to fraudulent misrepresentation.⁸ As extended liability became increasingly desirable, courts purported to keep within the old rule but extended liability by expanding the ambit of fraud.⁹ The result is varying interpretations of fraud including misrepresentations made intentionally,¹⁰ misrepresentations made honestly but negligently,¹¹ and misrepresentations made neither intentionally nor negligently.¹² Such judicial shadow-boxing emphasises the need of a more stable category of liability.

The policy established by Justice Cardozo in the *Ultramares* case, of not subjecting a defendant to an indefinite number of suits for negligence, has no potency if courts permit juries to construe evidence of mere negligence to be fraud. Rather than permit negligence to parade as fraud and confuse the profession, courts should frankly admit that negligence should be the basis of liability in these cases. This would fit in with the recommendations urged by authorities,¹³ and adopted in several cases.¹⁴ While such a doctrine seems to open an exceedingly broad field of liability, restrictive safeguards are available. As a matter of law, liability need not be imposed where infor-

⁶ 14 App. Cas. 337 (1889); Smith, Liability for Negligent Language, 14 Harv. L. Rev. 184, 185 (1900).

⁷ One engaged in a public calling: *Tardos v. Bozant*, 1 La. Ann. 199 (1846); *Glanzer v. Shepard*, 233 N.Y. 236, 135 N.E. 275 (1922); *Mulroy v. Wright*, 185 Minn. 84, 240 N.W. 116 (1931). Negligent advertisements by manufacturers: *Henry v. Crook*, 202 App. Div. 19, 195 N.Y. Supp. 642 (1922); *Crist v. Art Metal Works*, 230 App. Div. 114, 243 N.Y. Supp. 496 (1930). Cf. *Miller v. Sears, Roebuck & Co.*, 250 Ill. App. 340 (1928).

⁸ *Savings Bank v. Ward*, 100 U.S. 195 (1879); *O'Connor v. Ludlam*, 92 F. (2d) 50 (C.C.A. 2d 1937).

⁹ A few courts have maintained the old rule but extended the privity of contract theory. *Brown v. Sims*, 22 Ind. App. 317, 53 N.E. 779 (1899); *Economy Bldg. and Loan Ass'n v. West Jersey Title Co.*, 64 N.J. 27, 44 Atl. 854 (1899); *Glanzer v. Shepard*, 233 N.Y. 236, 135 N.E. 275 (1922).

¹⁰ *Derry v. Peek*, 14 App. Cas. 337 (1889); *Angus v. Clifford*, [1891] 2 Ch. 449; *Reno v. Bull*, 226 N.Y. 546, 124 N.E. 144 (1919).

¹¹ *Prestwood v. Carlton*, 162 Ala. 327, 50 So. 254 (1909); *Trimble v. Reid*, 97 Ky. 713, 31 S.W. 861 (1895); *Whitehurst v. Life Ins. Co.*, 149 N. Car. 273, 62 S.E. 1067 (1908); *Williston, Liability for Honest Misrepresentation*, 24 Harv. L. Rev. 415, 429, n. 47 (1911).

¹² *Hitchcock v. Gothenburg Water Power & Irrigation Co.*, 95 N.W. 638 (Neb. 1903); *Huntress v. Blodgett*, 206 Mass. 318, 92 N.E. 427 (1910). Cf. *Chatham Furnace Co. v. Moffatt*, 147 Mass. 403, 18 N.E. 168 (1888). *Bohlen, Misrepresentation as Deceit, Negligence or Warranty*, 42 Harv. L. Rev. 733, 735 (1929); *Green, Judge and Jury*, c. 10 (1930).

¹³ *Bohlen, Should Negligent Misrepresentations be Treated as Negligence or Fraud?* 18 Va. L. Rev. 703 (1932); *Bohlen, op. cit. supra* note 12; *Carpenter, Responsibility for Intentional, Negligent, and Innocent Misrepresentation*, 24 Ill. L. Rev. 749 (1930).

¹⁴ See cases cited in note 3 *supra*. *Cunningham v. Pease House Furnishing Co.*, 74 N.H. 435, 69 Atl. 120 (1908); *Weston v. Brown*, 82 N.H. 157, 131 Atl. 141 (1925).

mation is gratuitously given.¹⁵ The right of jury trial supplies an additional safeguard. The defense of contributory negligence is also available, though limitation by statute seems desirable¹⁶ in view of increasing specialization and necessity for relying on experts' statements. A possible additional restriction, adopted in some cases,¹⁷ and urged by Jeremiah Smith,¹⁸ is the limitation of liability to cases where it appears that there was knowledge that the statement was to be used to induce reliance of third parties, and that it was "likely to produce substantial pecuniary loss if the statement proved false."¹⁹ Such a restriction in cases of negligent statements by accountants would result in an extension of liability consistent with the responsibilities of accountants to business.²⁰

Trusts—Apportionment of Proceeds of Sale of Unproductive Land—Taxes—[Illinois].—One of the provisions of a will setting up a trust which included a large amount of unproductive land was, "I hereby authorize and direct" trustees "in their judgment and discretion" to sell "any or all of my vacant real estate. I prefer that the tract of land known as 'the pasture' be sold last." Trustees held the vacant land for many years, deducting taxes and carrying charges from the income due the life tenants from other trust property. Upon the sale of the land at a greatly enhanced value, the life tenants sought apportionment of the sale price between principal and income and restitution of the amount deducted from their income for taxes and carrying charges. *Held*, that under the circumstances of the case the power was discretionary and that, therefore, the rule of apportionment which depends on an imperative power of sale is inapplicable. Furthermore, the taxes and carrying charges were properly paid out of income, inasmuch as the will directed payment of net income. *Love v. Engelke*.¹

This decision forces Illinois trustees in each case to interpret correctly at their peril whether a will establishes a discretionary or mandatory power of sale, and to look for an "intention" as to the extent of the powers of the trustee where in most instances settlors will have entertained no thoughts in regard thereto, a result which cannot help but increase litigation.

Because of the general duty of a trustee to obtain the highest income commensurate with the preservation of the principal of the trust,² the law imposes a duty on trustees to convert unproductive property.³ In order to avoid a sacrifice sale or to

¹⁵ *Carpenter, op. cit. supra* note 13, at 757; *Bohlen, Misrepresentations as Deceit, Negligence or Warranty*, 42 *Harv. L. Rev.* 733, 741 (1929); *Rosenberg v. Cyrowski*, 227 *Mich.* 508, 198 *N.W.* 905 (1924).

¹⁶ *Cf. New Brunswick Rev. Stat. (1927) c. 143, § 2; Nova Scotia Stat. (1926) c. 3, § 2; 35 Stat. 66 (1908), 45 U.S.C.A. § 53 (1926).*

¹⁷ *International Products Co. v. Erie Railroad*, 244 *N.Y.* 331, 155 *N.E.* 662 (1927); abstract cases: *Brown v. Sims*, 22 *Ind. App.* 317, 53 *N.E.* 779 (1899); *Anderson v. Spriesterbach*, 69 *Wash.* 393, 125 *Pac.* 166 (1912); *Shine v. Nash Abstract & Invest. Co.*, 217 *Ala.* 498, 117 *So.* 47 (1928).

¹⁸ *Smith, Liability for Negligent Language*, 14 *Harv. L. Rev.* 184, 195 (1900).

¹⁹ *Ibid.* ²⁰ Note 5 *supra*.

¹ 368 *Ill.* 342, 14 *N.E. (2d)* 228 (1938).

² *Rest. Trusts* §§ 176, 181 (1935).

³ 4 *Bogert, Trusts and Trustees* § 825 (1935); *Loring, A Trustee's Handbook* 127-128 (4th ed. 1928).