



1997

Proposed Arkansas Model Fraud Jury Instructions (Unofficial Working Draft)

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Charles D. Harrison, Roger D. Rowe, and William A. Waddell Jr., *Proposed Arkansas Model Fraud Jury Instructions (Unofficial Working Draft)*, 20 U. ARK. LITTLE ROCK L. REV. 51 (1997).

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PROPOSED ARKANSAS MODEL FRAUD JURY INSTRUCTIONS
[Unofficial Working Draft]

*Charles D. Harrison**
*Roger D. Rowe***
*William A. Waddell, Jr.****

PREFACE

Fraud litigation in Arkansas has expanded beyond the reach of the current Arkansas Model Jury Instructions. The one approved jury instruction for the tort of deceit, AMI 405,¹ does not describe the elements of constructive fraud² or fraudulent concealment.³ These claims are alleged as frequently as the traditional claim of deceit. In addition, key terms such as "representation" and "justifiable reliance" are not defined for the jury.

Furthermore, Arkansas case law recognizes the distinction between claims for breach of contract and fraud.⁴ Without additional model instructions, the present AMI 405 is inadequate to allow a jury to understand the distinction.

Therefore, the drafters believe these proposed model instructions will improve the trial practice of fraud cases in Arkansas. Every effort has been made to make the instructions complete, impartial, and in conformity with Arkansas law. However, the drafters make no warranty as to the instructions. The instructions are submitted solely for consideration and comment as a service to members of the bench and bar with the expectation that a final revised draft may be proposed for study and adoption by the Arkansas Supreme Court. Comments concerning the instructions may be submitted to William A. Waddell, Jr., Friday, Eldredge & Clark, 2000 First Commercial Building, 400 West Capitol Avenue, Little Rock, Arkansas 72201.

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1. In ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, No. 405 (3d ed. & Supp. 1995). The jury is instructed that the following five elements are essential for a claim of deceit: (1) damage to claimant, (2) false representation of a material fact, (3) defendant's knowledge of falsity or lack of basis, (4) defendant's intent to induce reliance on the false representation, and (5) claimant's justifiable reliance to his detriment.

2. See *South County, Inc. v. First W. Loan Co.*, 315 Ark. 722, 871 S.W.2d 325 (1994); *Morrison v. Back Yard Burgers, Inc.*, 91 F.3d 1184, 1188 (8th Cir. 1996).

3. See *Ward v. Worthen Bank & Trust Co.*, 284 Ark. 355, 681 S.W.2d 365 (1984); *Copelin v. Corter*, 291 Ark. 218, 724 S.W.2d 146 (1987).

4. See, e.g., *Evans Indus. Coatings, Inc. v. Chancery Court of Union County*, 315 Ark. 728, 870 S.W.2d 701 (1994); *Fidelity Mortgage Co. v. Cook*, 307 Ark. 496, 821 S.W.2d 39 (1991) (Newbern, J., dissenting).

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CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-1
ELEMENTS OF CLAIM

_____ claims(s) (plaintiff(s)) damages from _____ (defendant(s)) for deceit and [has] [have] the burden of proving each of five essential propositions:

First, that [he] [she] [they] [has] [have] sustained damages;

Second, that a false representation of fact was made by _____ (defendant(s));

Third, that _____ (defendant(s)) knew or believed that the representation was false, [or did not have a sufficient basis of information to make it];

Fourth, that _____ (defendant(s)) intended to induce _____ (plaintiff(s)) [to act] [or] [to refrain from action] in reliance upon the misrepresentation; and

Fifth, _____ (plaintiff(s)) justifiably relied upon the representation and, as a result, sustained damages.

[If you find from the evidence in this case that each of these propositions has been proved, then your verdict should be for _____ (plaintiff(s)) (against the party or parties who made the false representations); but if, on the other hand, you find from the evidence that any of these propositions has not been proved, then your verdict should be for _____ (defendant(s)).]

COMMENT

This instruction is identical to AMI 405.⁵ However, the drafters believe the instruction should be changed to omit the bracketed portion of the third element which states "or did not have a sufficient basis of information to make it" for two reasons. First, this phrase does not appear consistently in the elements of fraudulent misrepresentation as set forth in Arkansas case law.⁶ Second, the bracketed phrase is more appropriate in the proposed model instruction A-3 which sets forth those situations in which "knowledge of falsity" is established. Until the Arkansas Supreme Court expresses an opinion on this issue, however, practitioners should continue to use AMI 405 as promulgated.

5. See *supra*, note 1.

6. Compare *Calandro v. Parkerson*, 327 Ark. 131, 137, 936 S.W.2d 755, 759 (1997) with *Wheeler Motor Co. v. Roth*, 315 Ark. 318, 324, 867 S.W.2d 446, 449 (1993), *modified*, *Woodline Motor Freight, Inc. v. Troutman Oil Co.*, 327 Ark. 448, 938 S.W.2d 565 (1997) (modifying measurement of prejudgment interest).

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-2
"REPRESENTATION" - DEFINED

A representation sufficient to form the basis of an action for fraudulent misrepresentation must be a material, false statement of fact which is made before or at the time the plaintiff acts on the representation.

COMMENT

This instruction states the rule in *South County, Inc. v. First Western Loan Co.*; ⁷*P.A.M. Transportation v. Arkansas Blue Cross & Blue Shield*; ⁸*Baskin v. Collins*; ⁹and *Vanderboom v. Sexton*. ¹⁰ With the exception of the bracketed portions that follow, the drafters believe that this instruction is appropriate in every case when a claim of fraudulent misrepresentation is made. The following bracketed instructions should only be used when appropriate.

[Representation as to Future Event]

[The representation must relate to a past event, or a present circumstance, but not to a future event.]

COMMENT

This subparagraph is appropriate when there is an issue as to whether the representation relates to a present circumstance or to a future event. The instruction is derived from *Morrison v. Back Yard Burgers, Inc.* ¹¹ and *Delta School of Commerce, Inc. v. Wood*. ¹² A representation limited to a future event may be a promise which forms the basis of an action for breach of contract, or a mere prediction which does not give rise to such a claim, but the representation is not a fraudulent one.

7. 315 Ark. 722, 871 S.W.2d 325 (1994).

8. 315 Ark. 234, 868 S.W.2d 33 (1993).

9. 305 Ark. 137, 806 S.W.2d 3 (1991).

10. 460 F.2d 362 (8th Cir. 1972).

11. 91 F.3d 1184, 1186.

12. 298 Ark. 195, 200, 766 S.W.2d 424, 427 (1989).

[Representation Misleading Because Incomplete]

[A representation stating the truth so far as it goes but which the maker knows or believes to be materially misleading because of his failure to state additional or qualifying facts is a false representation of fact.]

COMMENT

This subparagraph should be used when the plaintiff alleges that the representation is fraudulent because it is incomplete. The instruction follows the Restatement rule.¹³ The drafters note also that partial disclosure with knowledge that the partial disclosure is misleading may create a duty to disclose the omitted facts.¹⁴

[Misrepresentation of Intention]

[A representation of the maker's intention to do or not to do a particular thing is a false representation of fact if he knows he does not have that intention when the representation is made.]

COMMENT

This subparagraph should be used when there is an issue as to whether the defendant misrepresented his intention. The instruction states the Restatement rule regarding promissory fraud¹⁵ and is consistent with *Undem v. First National Bank*,¹⁶ *Anthony v. First National Bank of Magnolia*,¹⁷ and the dissent in *Fidelity Mortgage Co. of Texas v. Cook*.¹⁸ Two restrictions on the application of the doctrine of promissory fraud are incorporated in this instruction. First, the intention not to perform must be contemporaneous with the making of the promise.¹⁹ Second, evidence of a misrepresentation recklessly made is not sufficient to support an inference of intent.²⁰

13. See RESTATEMENT (SECOND) OF TORTS § 529 (1977).

14. See *Ragland v. Shattuck Nat'l Bank*, 36 F.3d 983 (10th Cir. 1994); *Roddenberry v. Roddenberry*, 51 Cal. Rptr. 2d 907 (Cal. Ct. App. 1996).

15. See RESTATEMENT (SECOND) OF TORTS § 530 (1965).

16. 46 Ark. App. 158, 165, 879 S.W.2d 451, 454 (1994).

17. 244 Ark. 1015, 1028, 431 S.W.2d 267, 275 (1968).

18. 307 Ark. 496, 821 S.W.2d 39 (Newbern, J., dissenting). See also *Sudul v. Computer Outsourcing Servs.*, 868 F. Supp. 59 (S.D.N.Y. 1994); *McIntyre v. McLeod*, 678 So. 2d 1105 (Ala. Civ. App. 1995).

19. See *Exeter Bancorporation, Inc. v. Kemper Sec. Group, Inc.*, 58 F.3d 1306 (8th Cir. 1995).

20. See *National Sec. Ins. Co. v. Donaldson*, 664 So. 2d 871, 876-77, (Ala. 1995).

The instruction does not apply when the maker misrepresents a third party's intention. The drafters believe the misrepresentation of a third party's intent should be treated as any other claim for the misrepresentation of a material fact.²¹

[Statement of Opinion or Belief]

[An erroneous expression of opinion or belief, if honestly made, is not a false representation of fact.]

COMMENT

This subparagraph should be used when there is an issue as to whether an alleged representation is a statement of opinion or belief or is a fraudulent misrepresentation. The instruction states the rule in *Anthony v. First National Bank of Magnolia*²² and *Delta School of Commerce, Inc. v. Wood*.²³

[Misrepresentation of Law]

COMMENT

The drafters propose no model instruction regarding misrepresentations of law. Although the Restatement defines the elements of an actionable tort for misrepresentation of law²⁴ and other states have model instructions for the tort,²⁵ the drafters found no Arkansas authority approving an action for deceit for the misrepresentation of domestic law.²⁶

21. See *Delta Sch. of Commerce, Inc. v. Wood*, 298 Ark. 195, 766 S.W.2d 424 (1989).

22. 244 Ark. 1015, 1028, 431 S.W.2d 267, 274 (1968).

23. 298 Ark. 195, 766 S.W.2d 424.

24. See RESTATEMENT (SECOND) OF TORTS § 545 (1977).

25. See, e.g., OKLAHOMA UNIFORM JURY INSTRUCTIONS, CIVIL, No. 18.9 (2d ed.).

26. See *Glasgow v. Greenfield*, 9 Ark. App. 224, 230, 657 S.W.2d 578, 581 (1983) (citing *Adkins v. Hoskins*, 176 Ark. 565, 3 S.W.2d 322 (1928) (recognizing the general rule that fraud cannot be predicated upon a misrepresentation of law); *McDonald v. Smith*, 95 Ark. 523, 527 (1910) (holding that where the attorney-defendant only expressed an opinion of the law, there was no fraudulent misrepresentation)).

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-3
KNOWLEDGE OF FALSITY

A person knows or believes that a representation is false if the evidence demonstrates that (1) the person actually knew that the representation was false when made or (2) the person lacked a sufficient basis for making the representation and knew he did not have a sufficient basis for making the representation.

[Ambiguous Representation]

[If a person makes a representation which he knows to be capable of two interpretations, one of which he knows to be false and the other true, the representation may constitute a false representation of fact if the representation was made with the intention that it be understood in the sense in which it is false.]

COMMENT

This instruction states the general rule concerning knowledge of the falsity of a representation. Subpart (1) is based upon *Clark v. Ridgeway*.²⁷ Subpart (2) is derived from *Morrison v. Back Yard Burgers, Inc.*²⁸ The situation in subpart (2) is distinguishable from the situation where the defendant did not know he had an insufficient basis to make the statement and negligently made the statement. The latter situation is not fraud.²⁹ With the exception of the bracketed portions of the instruction, the drafters believe that the instruction is appropriate in every case in which there is a claim of fraudulent misrepresentation.

The bracketed portion of the instruction—ambiguous representation—should be used only when there is an issue as to whether the representation at issue was intentionally ambiguous. This portion of the instruction is derived from the Restatement³⁰ and amplifies the third element of fraudulent misrepresentation stated in AMI 405.³¹

27. 323 Ark. 378, 914 S.W.2d 745 (1996).

28. 91 F.3d 1184, 1186.

29. See *South County, Inc. v. First W. Loan Co.*, 315 Ark. 722, 871 S.W.2d 325 (1994).

30. See RESTATEMENT (SECOND) OF TORTS § 527(1977). The drafters elected not to include the remainder of § 527 because they believed those sections were inconsistent with the concept of intentional fraud.

31. ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, No. 405 (3d ed. & Supp. 1995). See *supra*, note 1

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-4
REPRESENTATION TO AGENT OR THIRD PARTY

You are instructed that the maker of a fraudulent representation to the agent of the plaintiff or to a third party may be liable for damages to the plaintiff who justifiably relies upon the representation if: (1) the representation is made to the agent or third party; and (2) the maker either intends or has reason to expect that the representation will be repeated to the plaintiff; and (3) that it will influence his conduct in the transaction.

COMMENT

This instruction follows the Restatement rule.³² This instruction is appropriate when the defendant made the representation to an agent of the plaintiff or to a third party.

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-5
"MATERIAL" - DEFINED

A fact or statement of fact is material if it was a substantial factor which influenced the plaintiff's decision. It is not necessary, however, that the fact or statement of fact be the paramount or decisive factor, only that it be a fact to which a person might reasonably and justifiably be expected to attach importance in making his decision.

COMMENT

This instruction is derived from *Ellis v. Litter*.³³ The drafters believe this instruction is appropriate for use in every case in which there is an allegation of fraudulent misrepresentation or fraudulent concealment.

32. See RESTATEMENT (SECOND) OF TORTS § 533 (1977).

33. 311 Ark. 35, 38, 841 S.W.2d 155, 157 (1992) (quoting W. PAGE KEETON, ET AL., PROSSER & KEETON ON THE LAW OF TORTS, § 108 (5th ed. 1984)).

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-6
"JUSTIFIABLE RELIANCE" - DEFINED

Reliance is justifiable if the plaintiff actually relied upon a misrepresentation by the defendant and that the plaintiff's reliance was reasonable. Actual reliance means that the plaintiff either acted or did not act by reason of the defendant's misrepresentation.

COMMENT

This instruction states the rule in *McAnally v. Gildersleeve*,³⁴ and *MFA Mutual Insurance Co. v. Keller*.³⁵ The drafters believe this instruction is appropriate whenever justifiable reliance is an element of fraud, including a claim of constructive fraud.³⁶

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-7
KNOWLEDGE OF THE MISREPRESENTED FACT

If a party knows the falsity of facts being represented, that party has no right to act upon that misrepresentation and, therefore, any reliance upon such a misrepresentation is not justifiable.

COMMENT

This instruction is derived from *Mid-America Truck & Equipment, Inc. v. Mack Trucks, Inc.*³⁷ This instruction may be appropriate when there are facts presented which suggest that the plaintiff had knowledge of the falsity of the misrepresented fact.

34. 16 F.3d 1493 (8th Cir. 1994).

35. 274 Ark. 281, 623 S.W.2d 841 (1981).

36. See *infra* Chapter 3, Form C-1.

37. 519 F. Supp. 461 (W.D. Ark. 1981).

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-8
COMPARATIVE FAULT

If you should find that the plaintiff's damage was proximately caused by fault on the part of the defendant and not by fault on the part of the plaintiff, then the plaintiff is entitled to recover the full amount of any damages you may find he sustained as a result of the occurrence.

If you should find that the occurrence was proximately caused by fault of both the plaintiff and the defendant, then you must compare the percentages of their fault.

If the fault of the plaintiff is of less degree than the fault of the defendant, then the plaintiff is entitled to recover any damages which you may find he has sustained as a result of the occurrence after you have reduced them in proportion to the degree of his own fault.

On the other hand, if the defendant was not at fault or if the fault of the plaintiff is equal to or greater in degree than the fault of the defendant, then the plaintiff is not entitled to recover any damages.

COMMENT

This instruction follows the model of AMI 2102-2115³⁸ on comparative fault. Although some Arkansas trial courts have indicated that the Arkansas comparative fault statute³⁹ applies to fraud claims, the drafters are not aware of any appellate decision which directly addresses this issue.⁴⁰ The typical fraudulent misrepresentation case is essentially an "all or nothing" proposition for a plaintiff. Use of comparative fault may permit a jury to reach some middle ground between the positions of the parties. For variations of this instruction which may be necessary depending upon the nature and number of other claims, see AMI 2102-2115.⁴¹

38. ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, Nos. 2102-2115 (3d ed. & Supp. 1995).

39. ARK. CODE ANN. § 16-64-122 (Michie 1987 & Supp. 1995).

40. *Compare* WOODS & DEERE, COMPARATIVE FAULT, § 14:51 (3d ed. 1996), Quinney v. Pittman, 320 Ark. 177, 188, 895 S.W.2d 538, 544 (1995), and Merrill Lynch, Pierce, Fenner & Smith, Inc. v. First Nat'l Bank, 774 F.2d 909 (8th Cir. 1985).

41. *Supra*, note 38.

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-9
CAUSATION

To prove the element of causation, the plaintiff must prove that he sustained damage as a result of his justifiable reliance on the defendant's misrepresentation.

COMMENT

This instruction is based upon *MFA Mut. Ins. Co. v. Keller*.⁴² The drafters believe this instruction is appropriate in each case in which a claim of fraudulent misrepresentation is made.

CHAPTER 1: FRAUDULENT MISREPRESENTATION (DECEIT)
FORM A-10
MEASURE OF DAMAGES

If you find for the plaintiff on the question of liability, you must then fix the amount of money which will reasonably and fairly compensate him [for the following element of damage][for any of the following elements of damage] caused by the [fraudulent misrepresentation][fraudulent concealment] [constructive fraud] of the defendant:

[Here insert the element or elements]

Whether [this element][any of these elements] of damage [has] [have] been proved by the evidence is for you to determine.

COMMENT

This instruction follows the format of AMI 2221.⁴³

42. 274 Ark. 281, 623 S.W. 2d 841 (1981).

43. ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, Nos. 2221 (3d ed.) For a discussion of the elements of damage available in fraud cases, see HOWARD W. BRILL, ARKANSAS LAW OF DAMAGES § 33-7 (3d ed. 1996). For a discussion of the "benefit of the bargain" and "out-of-pocket" measures of damages applied in fraud cases, see *Interstate Freeway Servs., Inc. v. Houser*, 310 Ark. 302, 835 S.W.2d 872 (1992).

CHAPTER 2: FRAUDULENT CONCEALMENT
FORM B-1
ELEMENTS OF CLAIM

The plaintiff alleges and has the burden of proving that the defendant fraudulently concealed from the plaintiff [state alleged fact concealed]. In order to prove fraudulent concealment on the part of the defendant, the plaintiff must prove each of the following elements by a preponderance of the evidence:

First, [either (1) the plaintiff and defendant were in a confidential relationship; or (2) the defendant had superior knowledge and knew the plaintiff was mistaken about a material fact and had no access to the information known by the defendant; or (3) the defendant has made a representation of material fact and must disclose more information to prevent the representation from being misleading to the plaintiff.]

Second, that the defendant failed to disclose a material fact to the plaintiff;

Third, that the plaintiff could not have learned the omitted fact by reasonable inquiry or diligent attention and observation;

Fourth, that the defendant failed to disclose the material fact with the intention that the plaintiff be misled;⁴⁴ and

Fifth, that the failure of the defendant to disclose [state the alleged fact not disclosed] proximately caused the plaintiff to suffer damages.

COMMENT

This instruction is derived from *Camp v. First Fed. Savings & Loan*,⁴⁵ *Ward v. Worthen Bank & Trust Co., N.A.*;⁴⁶ *Copelin v. Corter*;⁴⁷ and *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. First National Bank*.⁴⁸ Compare this proposed instruction to California, Oklahoma, and Tennessee jury instructions.⁴⁹

While the issue of whether a confidential relationship exists (and, therefore, a duty to disclose) is sometimes characterized as a matter of law, the

44. This element supplies the scienter requirement for a fraud claim. See *Wilson v. Misko*, 508 N.W.2d 238 (Neb. 1993).

45. 12 Ark. App. 150, 671 S.W.2d 213 (1984).

46. 284 Ark. 355, 681 S.W.2d 365 (1984).

47. 291 Ark. 218, 724 S.W.2d 146 (1987).

48. 774 F.2d 909 (8th Cir. 1985).

49. See CALIFORNIA JURY INSTRUCTIONS, CIVIL, Nos. 12.35, 12.37 (2d ed. 1994); OKLAHOMA UNIFORM JURY INSTRUCTIONS, CIVIL, Nos. 18.2, 18.5 (2d ed.); TENNESSEE PATTERN JURY INSTRUCTIONS, CIVIL, Nos. 8.45, 8.47 (2d ed. 1988).

Arkansas Court of Appeals in *Camp*, noted that, in light of language from *Berkeley Pump Co. v. Reed-Joseph Land Co.*,⁵⁰ the circumstances in *Camp* were sufficient to submit to the jury the question of whether there was a "duty to speak."⁵¹ Therefore, the drafters included the determination of whether a confidential relationship existed as one of the factual elements for the jury.⁵² However, this issue needs further clarification by Arkansas courts.

The drafters found the first element of fraudulent concealment to be the most difficult to define. A duty to speak arises by virtue of either a confidential relationship or the peculiar situation of the parties. This first element sets forth those scenarios. Different courts have stated the three subparts of this element in different forms in describing when a duty of disclosure arises.⁵³ The drafters believe the court must first determine if a fact question is presented as to any of the three subparts of this element. If so, the court should submit one or more of these subparts as a part of the instruction. If the court finds that there is insufficient evidence to create a fact question on any of the subparts of the first element, then there is no duty of disclosure and the tort of fraudulent concealment should not be submitted to the jury.

The third element of this claim also presents an open question. Based upon the language of *Brookside Village Mobile Homes v. Meyers*,⁵⁴ the drafters believe the duty to investigate in cases alleging fraud by omission might be considered the counterpart to justifiable reliance in cases alleging affirmative misrepresentation.⁵⁵ However, compare the elements of this claim as stated in other states which suggest justifiable reliance is the standard.⁵⁶ The drafters note that the elements of this claim in Nebraska also include "that the plaintiff

50. 279 Ark. 384, 653 S.W.2d 128 (1983). See also 37 AM. JUR. 2D, *Fraud and Deceit* § 146 (1968 & Supp. 1997).

51. *Camp*, 12 Ark. App. 150, 155, 671 S.W.2d 213, 216 (1984).

52. Cf. *Lambert v. Mail Handlers Benefit Plan*, 682 So. 2d 61 (Ala. 1996).

53. See, e.g., *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. First Nat'l Bank*, 774 F.2d 909 (8th Cir. 1985) (applying Arkansas law and stating the superior knowledge scenario); *Exeter Bancorporation, Inc. v. Kemper Sec. Group, Inc.*, 58 F.3d 1306, 1314 (8th Cir. 1995) (applying Minnesota law and stating all three scenarios); *Camp v. First Fed. Sav. & Loan*, 12 Ark. App. 150, 671 S.W.2d 213 (1984) (stating the confidential relation scenario); *Barsam v. Pure Tech Int'l, Inc.*, 864 F. Supp. 1440 (S.D.N.Y. 1994) (applying New York law and stating the confidential relationship and superior knowledge scenarios); *Swersky v. Dreyer & Traub*, 643 N.Y.S.2d 33 (N.Y. App. Div. 1996) (applying New York law and stating the superior knowledge scenario); and *Banco Urquijo, S.A. v. Signet Bank/Maryland*, 861 F. Supp. 1220 (M.D. Pa. 1994) (applying Pennsylvania law and stating the confidential relation scenario).

54. 301 Ark. 139, 142, 782 S.W.2d 365, 367 (1990).

55. See also *Berkeley Pump Co. v. Reed-Joseph Land Co.*, 279 Ark. 384, 653 S.W.2d 128 (1983).

56. See, e.g., *Davsko v. Golden Harvest Products, Inc.*, 965 F.Supp. 1467, 1476 (D. Kan. 1997).

was reasonably so misled" which is also akin to the concept of justifiable reliance.⁵⁷

The fourth element supplies the scienter requirement for a fraud claim.⁵⁸

**CHAPTER 2: FRAUDULENT CONCEALMENT
FORM B-2
CONFIDENTIAL RELATIONSHIP**

You are instructed that a confidential relationship existed between the plaintiff and defendant if you find the following:

First, that the plaintiff put his trust in the defendant to act on the plaintiff's behalf;

Second, that the defendant knew, or by his conduct acknowledged, that the plaintiff was placing his trust in the defendant to act on the plaintiff's behalf; and

Third, that the defendant was in a position to have and to exert influence over the plaintiff and purported to act or advise with the plaintiff's interest in mind.

A confidential relationship cannot be created unilaterally and must be known to both parties. Mere subjective trust on the part of one person and a cordial friendship do not create a fiduciary relationship.

COMMENT

This instruction is derived from *Horton v. Koner*,⁵⁹ *Camp v. First Federal Savings & Loan*,⁶⁰ *Capital Bank v. MVB, Inc.*,⁶¹ *Salem v. Central Trust Co., N.A.*,⁶² and *Hallmark v. Port/Cooper-T. Smith Stevedoring Co.*⁶³ This instruction is appropriate for use with Form B-1 and Form C-1.

57. *See Wilson v. Misko*, 508 N.W.2d 238, 250 (Neb. 1993).

58. *See id.*

59. 12 Ark. App. 38, 671 S.W.2d 235 (1984).

60. 12 Ark. App. 150, 671 S.W.2d 213 (1984).

61. 644 So. 2d 515 (Fla. Dist. Ct. App. 1994).

62. 657 N.E.2d 827 (Ohio Ct. App. 1995).

63. 907 S.W.2d 586 (Tex. App. 1995). *Compare* CALIFORNIA JURY INSTRUCTIONS, CIVIL, Nos. 12.36, 12.37 (7th ed. 1986); TENNESSEE PATTERN JURY INSTRUCTIONS, CIVIL, Nos. 8.46, 8.47 (2d ed. 1988).

**CHAPTER 2: FRAUDULENT CONCEALMENT
FORM B-3
COMPARATIVE FAULT**

COMMENT

See Form A-8.

**CHAPTER 2: FRAUDULENT CONCEALMENT
FORM B-4
MEASURE OF DAMAGES**

COMMENT

See Form A-10.

**CHAPTER 3: CONSTRUCTIVE FRAUD
PREFACE TO CHAPTER 3**

Constructive fraud is ill-defined in Arkansas and is therefore a difficult subject matter for jury instruction.⁶⁴ It could be argued that constructive fraud, as defined by Arkansas courts, is an equitable theory more suited to equitable relief such as restitution, reformation or rescission.⁶⁵

Also unanswered is whether a claim of constructive fraud will support an award of punitive damages.⁶⁶ Other state courts are divided on this question and practicing attorneys need guidance on the issue from Arkansas courts.

64. *Cf. Morrison v. Back Yard Burgers, Inc.*, 91 F.3d 1184, 1188 (8th Cir. 1996). In *Morrison*, the court stated that although a plea of constructive fraud relieves plaintiffs of the burden of proving fraudulent intent, "[p]laintiffs must still prove the other elements of common law fraud, including a false representation of a material fact and justifiable reliance upon the representation." *Id.*

65. The Arkansas Supreme Court, in *Miskimins v. City Nat'l Bank*, defined constructive fraud as the "breach of a legal or equitable duty which the law declares to be fraudulent because of its tendency to deceive others, regardless of the moral guilt, purpose or intent of the fraud feisor." *Miskimins v. City Nat'l Bank*, 248 Ark. 1194, 1204, 456 S.W.2d 673, 679 (1970) (citations omitted). The Arkansas Supreme Court commented in *South County, Inc. v. First Western Loan Co.*, that constructive fraud has been recognized by the court in cases involving rescission of deeds and other instruments and breaches of fiduciary duties. *South County, Inc. v. First W. Loan Co.*, 315 Ark. 722, 871 S.W.2d 325 (1994). However, Arkansas courts have not so limited the claim.

66. See HOWARD W. BRILL, ARKANSAS LAW OF DAMAGES § 33-8 (3d ed. 1996).

**CHAPTER 3: CONSTRUCTIVE FRAUD
FORM C-1
ELEMENTS OF CLAIM**

In order to prove his claim for constructive fraud, the plaintiff must prove each of the following elements by a preponderance of the evidence:

First, that plaintiff and defendant were in a confidential relationship;

Second, that defendant breached the confidential relationship by making a false representation of material fact, either knowing that the representation was false or, not knowing, asserting the representation to be true;

Third, that plaintiff justifiably relied upon the representation; and

Fourth, that, as a result of plaintiff's reliance, plaintiff suffered damages.

COMMENT

This instruction has been pieced together from statements of law made by courts in the following cases: *Morrison v. Back Yard Burgers, Inc.*;⁶⁷ *Miskimins v. City National Bank*;⁶⁸ *Bridges v. United Savings Association*;⁶⁹ *South County, Inc. v. First Western Loan Co.*;⁷⁰ and *Union National Bank v. Farmers Bank*.⁷¹ The drafters believe the instruction accurately states current Arkansas law on this tort.

**CHAPTER 3: CONSTRUCTIVE FRAUD
FORM C-2
CONFIDENTIAL RELATIONSHIP**

COMMENT

See Form B-2.

67. 91 F.3d 1184 (8th Cir. 1996).

68. 248 Ark. 1194, 456 S.W.2d 673 (1970).

69. 246 Ark. 221, 438 S.W.2d 303 (1969).

70. 315 Ark. 722, 871 S.W.2d 325 (1994).

71. 786 F.2d 881 (8th Cir. 1986).

**CHAPTER 3: CONSTRUCTIVE FRAUD
FORM C-3
COMPARATIVE FAULT**

COMMENT

See Form A-8.

**CHAPTER 3: CONSTRUCTIVE FRAUD
FORM C-4
MEASURE OF DAMAGES**

COMMENT

See Form A-10.

**CHAPTER 4: FRAUDULENT CONVEYANCE
PREFACE TO CHAPTER 4**

The instructions in this chapter are designed to assist in implementing the statutory causes of action created by the General Assembly in the Arkansas Fraudulent Transfer Act (the Act).⁷²

Because of the historic division of courts of law and of equity in Arkansas, few actions for fraudulent transfer have been tried before juries. The chancery courts, as a matter of common law, have historically avoided and set aside fraudulent transfers and imposed equitable liens for the benefit of creditors who lacked an adequate remedy at law.⁷³ Prior to the adoption of the Act, the Arkansas statutes also recognized the equitable remedy of avoidance against those transactions that were fraudulent as to creditors.⁷⁴

The Act, passed by the General Assembly in 1987, is comprehensive in its scope, but the remedies provided to creditors generally remain equitable in nature: avoidance of transactions, injunctions, receivers, and equitable liens.⁷⁵ The Act also provides a remedy at law—the recovery of a money judgment—against the transferor and his transferees for the value of an asset wrongfully transferred.⁷⁶ Although the Act provides causes of action for the

72. ARK. CODE ANN. §§ 4-59-201 to -213 (Michie 1996).

73. See *Horstmann v. LaFargue*, 140 Ark. 558, 564-66, 215 S.W. 729, 730-31 (1919), *overruled on other grounds by Spitzer v. Barnhill*, 237 Ark. 525, 374 S.W.2d 811 (1964).

74. See ARK. STAT. ANN. § 68-1302 (1979 & Supp. 1985).

75. See ARK. CODE ANN. § 4-59-207 (Michie 1996).

76. See *id.* § 4-59-208.

fraudulent transfer of property and the fraudulent incurring of obligations,⁷⁷ the Act only provides a remedy in the form of a money judgment for the fraudulent transfers of property.⁷⁸ These proposed model instructions therefore address only the elements of causes and defenses for the transfer of property, as those are the causes and defenses for which a right to jury trial would be recognized in the Arkansas courts by virtue of the remedy of a money judgment.

For those cases under the Act to be tried to juries, the drafters believe that practicing attorneys need guidance in the form of model jury instructions. The drafters propose jury instructions for the factual issues most likely to arise under the Act. By not including in these model instructions a reference to, or an instruction on, all potential factual issues under the Act, the drafters do not intend to imply that there are no other factual issues that should be submitted to the jury in a particular case.

Finally, the Act does not address the standard of proof required to establish claims and defenses under the Act. In addition, the annotations to the Act suggest there may be disagreement as to the standard of proof. The drafters believe the proper standard is the preponderance of the evidence when the plaintiff seeks damages.⁷⁹ Accordingly, the drafters suggest that AMI 202⁸⁰ be submitted in conjunction with these instructions.

CHAPTER 4: FRAUDULENT CONVEYANCE
FORM D-1
FRAUDULENT TRANSFER - BEFORE OR AFTER
CLAIM AROSE - ACTUAL INTENT TO DEFRAUD

Plaintiff contends that defendant transferred [the property] with the actual intent to hinder, delay or defraud a creditor and has the burden of proving each of the following three essential propositions:

First, that plaintiff is a creditor of defendant;

Second, that defendant made the transfer with the actual intent to hinder, delay, or defraud any creditor; and

Third, that the plaintiff has sustained damages.

77. *See id.* §§ 4-59-204(a)(1), -204(a)(2), -205(a).

78. *See id.* § 4-59-208(b), (c).

79. *Compare* the annotations to ARK. CODE ANN. § 4-59-204 (Michie 1996) *and* Grendell v. Kiehl, 291 Ark. 228, 723 S.W.2d 830 (1987).

80. ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, No. 202 (3d ed.).

COMMENT

The Act provides a cause of action to creditors of the defendant(s) for transfers of property or the creation of obligations by the defendant(s) with the actual intent to hinder, delay or defraud *any* creditor.⁸¹ The transfer of property or the creation of the obligation may occur before the plaintiff's claim arose if the act occurred with the actual intent to hinder, delay or defraud the plaintiff or another creditor.

The Act further recognizes that actual intent to hinder, delay or defraud is usually proven with circumstantial rather than direct evidence. Instead of defining actual intent, the Act provides a nonexclusive list of factors that may be considered by the fact-finder in determining whether actual intent has been proved.⁸² The drafters believe an instruction restating those factors would be appropriate with this instruction.⁸³

The Act defines creditor as a person who has a right to payment from the defendant, whether the right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.⁸⁴ The Act defines transfer equally broadly as every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, lease, and creation of lien or other encumbrance.⁸⁵ In the event the status of the plaintiff as a creditor or the existence of a transfer is challenged, the drafters believe that the terms may be defined for the jury by incorporation in an instruction of the definition in the Act.⁸⁶

**CHAPTER 4: FRAUDULENT CONVEYANCE
FORM D-2**

**FRAUDULENT TRANSFER - ACTUAL INTENT TO DEFRAUD -
AFFIRMATIVE DEFENSE OF TRANSFEREE**

A transfer is not fraudulent against a person who took in good faith and for a reasonably equivalent value [or against a subsequent transferee].

81. See ARK. CODE ANN. § 4-59-204(a)(1) (Michie 1996).

82. See *id.* § 4-59-204(b).

83. For an example of the form of an instruction that includes factors for the jury to consider, see ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, No. 2215A (3d ed. & Supp. 1995).

84. See ARK. CODE ANN. § 4-59-201(3),(4).

85. See *id.* § 4-59-201(12).

86. For an example of the form of a definitional instruction, see AMI 306.

A person takes in good faith when the circumstances would not place a reasonable person on inquiry of a debtor's fraudulent purpose and a diligent inquiry would not have discovered the fraudulent purpose.

[The transferee defendant] has the burden of proving this defense.

COMMENT

The defense of good faith and the giving of reasonably equivalent value may only be submitted in response to claims of conduct with the actual intent to hinder, delay, or defraud a creditor.⁸⁷ This form is therefore limited to the submission of defenses to the cause of action in Form D-1.

Good faith is not defined in the Act. However, the drafters have included a definition of good faith which they believe is consistent with the Act.⁸⁸

Value and reasonably equivalent value are defined by example in section 203 of the Act.⁸⁹ The drafters believe that an instruction on the meaning of value or reasonably equivalent value may not be necessary in every case.

CHAPTER 4: FRAUDULENT CONVEYANCE FORM D-3 FRAUDULENT TRANSFER - BEFORE OR AFTER CLAIM AROSE - NO REASONABLY EQUIVALENT VALUE

Plaintiff contends that defendant transferred [the property] without receipt of reasonably equivalent value and has the burden of proving each of the following three essential propositions:

First, that plaintiff is a creditor of defendant;

Second, defendant made the transfer without receiving a reasonably equivalent value in exchange, and defendant either

(1) was engaged in or was about to engage in a business or a transaction for which [his, her, its] assets were unreasonably small in relation to the business or transaction, or

(2) intended to incur, or believed or reasonably should have believed that [he, she, it] would incur, debts beyond [his, her, its] ability to pay as they became due; and

Third, that the plaintiff has sustained damages.

87. See ARK. CODE ANN. § 4-59-208(a) (Michie 1996).

88. See *In re M & L Bus. Mach. Co.*, 84 F.3d 1330, 1336-1338 (10th Cir. 1996); *In re Sherman*, 67 F.3d 1348, 1355 (8th Cir. 1995); *In re Agricultural Research & Tech. Group, Inc.*, 916 F.2d 528, 536 (9th Cir. 1990).

89. See ARK. CODE ANN. § 4-59-203 (Michie 1996).

COMMENT

The cause of action provided in section 204(a)(2) of the Act does not require actual intent to hinder, delay, or defraud a creditor.⁹⁰ The essence of the cause of action is the exchange without reasonably equivalent value. The plaintiff's claim also need not arise before the making of the transfer or the incurring of the obligation.

Value and reasonably equivalent value are defined by example in section 203 of the Act.⁹¹ The drafters believe that an instruction on the meaning of value or reasonably equivalent value may not be necessary in every case.

CHAPTER 4: FRAUDULENT CONVEYANCE
FORM D-4
FRAUDULENT TRANSFER - AFTER CLAIM AROSE -
INSOLVENCY AND NO REASONABLY EQUIVALENT VALUE

Plaintiff contends that defendant transferred [the property] without receiving equivalent value and has the burden of proving each of the following four essential propositions:

First, that plaintiff is a creditor of defendant;

Second, defendant made the transfer without receiving a reasonably equivalent value in exchange for the transfer;

Third, defendant was insolvent at the time of the making of the transfer or became insolvent as a result of the transfer; and

Fourth, that the plaintiff has sustained damages.

COMMENT

The cause of action provided in section 205(a) of the Act does not require actual intent to hinder, delay, or defraud a creditor.⁹² The essence of the cause of action is the making of a transfer without the receipt of reasonably equivalent value in exchange.

The cause of action provided in section 205(a) requires that the creditor's claim arise before the making of the transfer.⁹³ However, the proposed instruction includes no such element for the jury's consideration. The time of the making of a transfer or the incurring of an obligation is governed by section

90. *See id.* § 4-59-204(a)(2).

91. *See id.* § 4-59-203. Creditor is defined in section 201(3) and (4) of the Act. Transfer is defined in section 201(12) of the Act.

92. *See id.* § 4-59-205(a).

93. *See id.*

206 of the Act.⁹⁴ Because the rules in section 206 require the application of principles of property and commercial law to the facts, the drafters believe that the timing of the accrual of the claim presents a question of law for the courts.⁹⁵ The court must therefore first conclude that the creditor's claim arose before the transfer or obligation in order to properly submit this claim to the jury.

Value and reasonably equivalent value are defined by example in section 203 of the Act.⁹⁶ The drafters believe that an instruction on the meaning of value or reasonably equivalent value may not be necessary in every case.

Insolvency is defined in section 202 of the Act.⁹⁷ Section 202 creates a presumption of insolvency if the defendant/debtor is not paying debts as they become due. The definition of insolvency from section 202 will vary with the facts of the particular case.

Creditor is defined in section 201 of the Act.⁹⁸

CHAPTER 4: FRAUDULENT CONVEYANCE
FORM D-5
FRAUDULENT TRANSFER - AFTER CLAIM AROSE -
TRANSFER TO INSIDER

Plaintiff contends that defendant transferred [the property] to an insider while defendant was insolvent, and has the burden of proving each of the following five essential propositions:

First, that plaintiff is a creditor of defendant;

Second, that defendant made the transfer to an insider for an antecedent debt;

Third, defendant was insolvent at the time of the transfer;

Fourth, the insider had reasonable cause to believe that defendant was insolvent; and

Fifth, that the plaintiff has sustained damages.

94. *See id.* § 4-59-206.

95. *See* ARK. CODE ANN. § 4-59-206 (Michie 1996).

96. *See id.* § 4-59-203.

97. *See id.* § 4-59-202.

98. *See id.* § 4-59-201(3), (4).

COMMENT

The cause of action provided in section 205(b) of the Act does not require actual intent to hinder, delay, or defraud a creditor.⁹⁹ The cause of action pertains to transfers of property by a defendant to an insider only, not to obligations incurred by a defendant. The essence of the cause of action is the transfer by the defendant, while insolvent, to an insider for an antecedent debt.

Section 205(b) of the Act also requires that the creditor's claim arise before the making of the transfer or the incurring of the obligation.¹⁰⁰ However, the proposed instruction includes no such element for the jury's consideration. The time of the making of a transfer or the waiving of an obligation is governed by section 206.¹⁰¹ Because section 206 requires the application of principles of property and commercial law to the facts, the timing of the accrual of the claim presents a question of law. The court must decide whether the creditor's claim arose before the transfer or obligation in order to properly submit this claim to the jury.

Insider is defined in section 201(7) of the Act.¹⁰² Creditor is defined in sections 201(3) and (4) of the Act.¹⁰³ Transfer is defined in section 201(12) of the Act.¹⁰⁴

Insolvency is defined in section 202 of the Act. That section creates a presumption of insolvency if the defendant/debtor is not paying debts as they become due.¹⁰⁵ The definition of insolvency from section 202 will vary with the facts of the particular case.

99. *See id.* § 4-59-205(b).

100. *See id.*

101. *See Ark. Code Ann.* § 4-59-206 (Michie 1996).

102. *See id.* § 4-59-201(7).

103. *See id.* § 4-59-201(3), (4).

104. *See id.* § 4-59-201(12).

105. *See id.* § 4-59-202.

CHAPTER 4: FRAUDULENT CONVEYANCE
FORM D-6
FRAUDULENT TRANSFER -TRANSFER TO INSIDER -
AFFIRMATIVE DEFENSE

A transfer to an insider is not fraudulent:

[To the extent the insider gave new value to or for the benefit of the debtor after the transfer unless the new value was secured by a valid lien]
 or

[If the transfer was made in the ordinary course of business or financial affairs of the debtor and the insider] or

[If the transfer was made in a good faith effort to rehabilitate the debtor and the transfer secured present value given for that purpose as well as the antecedent debt of the debtor].

The defendant has the burden of proving [this] [these] defense(s).

COMMENT

This form may be used to submit defenses to the cause of action submitted in Form D-5.¹⁰⁶ If the first bracketed defense is submitted, then the fact finder should also be allowed to determine the extent of new value given and the extent to which the transfer secured an antecedent debt.¹⁰⁷

CHAPTER 4: FRAUDULENT CONVEYANCE
FORM D-7
MEASURE OF DAMAGES

If you find for the plaintiff on the question of liability you must then fix the amount of money that will reasonably and fairly compensate him for the value of the asset transferred at the time of the transfer or the amount necessary to satisfy the plaintiff's claim, whichever is less.

Whether either of these elements has been proved is for you to determine.

106. See *id.* § 4-59-208(f).

107. See ARK. CODE ANN. § 4-59-208(f)(1) (Michie 1996).

COMMENT

This instruction follows the format of AMI 2221.¹⁰⁸ As noted in the preface to this chapter, although the Act provides causes of action for the fraudulent transfer of property and the incurring of obligations, it is only the fraudulent transfers of property for which the Act provides a remedy in the form of a money judgment.¹⁰⁹

If the jury finds damages based on the value of the asset at the time of the transfer, the award may still be subject to equitable adjustment by the court.¹¹⁰

108. ARKANSAS MODEL JURY INSTRUCTIONS, CIVIL, No. 2221 (3d. ed).

109. *See* ARK. CODE ANN. § 4-59-208(b), (c).

110. *See id.* § 4-59-208(c).