
Are lawsuits against CPA's poised to spike?

By WebCPA Staff

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New Year's Resolution: review client relationship practices

After a year of record-setting investor losses, a leading securities attorney warned that accounting firms will face a rising tide of enforcement actions and litigation in 2010, and should take steps to ensure their client relationship practices reflect recent court decisions.

In a guest speech at the New York State Society of CPAs 2009 Investment Companies Conference, leading civil litigation and enforcement defense attorney **Richard A. Roth** of the New York-based Roth Law Firm PLLC, told 350 assembled CPAs that shareholders are now engaging in a high-stakes version of "Pin the Tail on the Donkey."

"Shareholders in 2009 sustained huge losses from investments in failed companies, and investors took unprecedented baths in the fraudulent ponzi schemes of Madoff and others," **Roth** said. "The money is largely gone, and historically, investors will go after whoever still has money that could satisfy a legal judgment; this creates tremendous risk for accountants."

"Or, to put it more bluntly," **Roth** told the accountants, "shattered investors will pin the tail on anyone in range, and you don't want to be the ass."

Roth, who has litigated hundreds of commercial and securities disputes in his career for financial institutions, broker-dealers, consulting firms and individuals, also noted that audit firms could be susceptible to additional SEC enforcement. "Because of situations like the Madoff debacle, regulators – and particularly the SEC – are

under pressure to widen the net of businesses and entities under regulation."

Court decisions also shifted the rules for audit firms' best practices, clarifying the laws in some cases against CPA's, and in other cases in their favor. The bottom line – "Be F.I.T. in 2010" **Roth** said:

F – Fee Agreement: audit firms' engagement letters should clearly limit the representation to specific services or a limited time frame, at most annually, said **Roth**. While it may be convenient for a firm to have ongoing engagements, clients have a statutorily limited time to sue directly, if you have not engaged in "continuous representation," which courts have recently construed against the CPA firm when engagement letters are ambiguous.

I – Independence: auditors can't have financial interest in the subject company, **Roth** reminded the CPA's. "While this has always been a basic tenet, courts, regulators and particularly plaintiffs' lawyers are digging deeper to find any accountant/client interrelationship to pin that tail."

T – Thoroughness: "Meticulously analyze each and every transaction," **Roth** said. "In this financial and political climate, you do not want to leave a jury or a regulator with any doubt as to whether you were dotting every 'I' and crossing every 'T'."

In addition, **Roth** recommended that CPAs continue putting in place programs to comply with the FTC "Red Flag" rule and generally should ensure protection of client files and data.

Although enforcement of the “Red Flag” rule was delayed by Congress to June 1, 2010, the AICPA is still recommending that CPAs be prepared for its eventual implementation. “If you lose your client’s data or it is misappropriated due to your negligence, you are going to have a problem regardless of the ‘Red Flag’ rule,” **Roth** said.

According to the Treasury Department’s Advisory Committee on the Auditing Profession, the six largest auditing firms paid out nearly \$6 billion to resolve audit cases in a 12-year period ending in 2007, with litigation and “practice protection” costs representing 6.6% of revenue in the most recent fiscal year prior to the 2008 report. “This was before the full force of financial meltdown,” **Roth** said.

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