

SUING ACCOUNTANTS

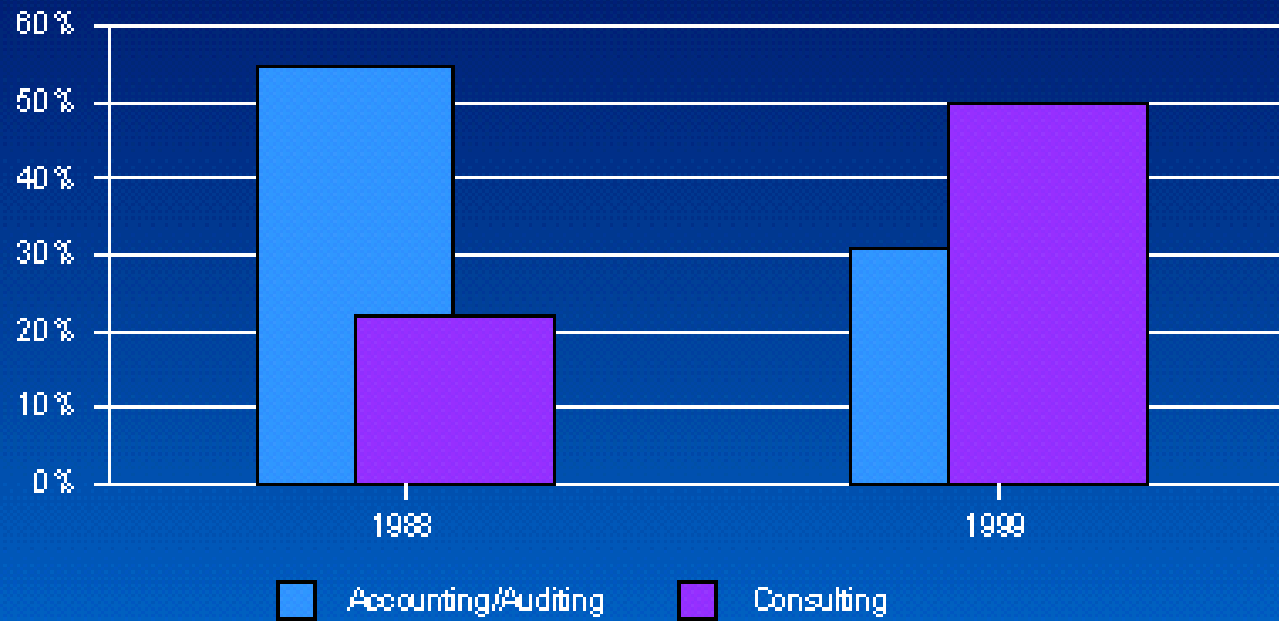
BY VINCE LOUWAGIE

The World According to Vince

- Auditing was one of accountants' *raison d'être*.
- Auditing became a commodity
 - Margin pressure
- Consulting is king.
 - Higher margins
 - Bigger projects
 - More subjective quality determinations

Shift to Consulting

Revenue of the Big Five Accounting Firms



Pendulum Swings for Accountants

- Standing issues
- 1995 Private Securities Litigation Reform Act.
 - Proportionate Liability v. joint and several

Restatements/Scandals

- 4 of 5: questionable accounting is widespread
- Restatements rampant:
 - ▶ 1988-1997: Average restatements = 46
 - ▶ 1998-2000: Average restatements = 155

PRE-SUIT CONSIDERATIONS

- **SOLVENCY OF DEFENDANT**
 - INSURED?
 - SELF-INSURED?
- **CHECK OUT REGISTRATION**
 - SECTION 102 OF THE ACT - - FINANCIAL INFO?
- **STATUTE OF LIMITATIONS**
- **EXPERT WITNESS**
 - AFFIDAVIT OF ATTORNEY
 - EXCUSE

AUDITOR

Arthur Andersen

PricewaterhouseCoopers

KPMG

Deloitte & Touche

Ernst & Young

COMPANIES

Enron*, WorldCom*,
Qwest*, Global Crossing*,
Dynegy*, CMS Energy*,
Halliburton*, Peregrine*,
Merck*

Tyco

Xerox*

El Paso Corp*, Adelphia

AOL, Williams Cos.

As reported by CNN. This table reflects the auditors at the time these companies allegedly used questionable accounting practices. Companies marked with an asterisk have changed their auditors since then.

CAUSES OF ACTION

- NEGLIGENCE/MALPRACTICE
- NEGLIGENT MISREPRESENTATION
- INTENTIONAL MISREPRESENTATION
- BREACH OF CONTRACT
- BREACH OF FIDUCIARY DUTY
- COMMON LAW AIDING AND ABETTING
- MN CONSUMER FRAUD ACT

SECURITIES CLAIMS

- **SECTION 11**
 - NO RELIANCE REQUIREMENT
 - ACCOUNTANT LIABILITY FOR EXPERTIZED PORTIONS OF REGISTRATION STATEMENT
 - LEE V. ERNST & YOUNG
- **SECTION 12**
 - Only if accountant is a seller.
- **Rule 10b-5**
- **Section 80A.23**

STANDING/RELIANCE

- RELATES TO NEGLIGENT MISREP. CLAIM
- PRIVITY
- REASONABLY FORSEEABLE
- SECTION 522. Liability is limited:
 - (a) by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it; and
 - (b) through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.

Minnesota cases under 552

Bonhiver v. Graf

TCF v. Arthur Young

Noram v. Stirtz Bernards

BESPEAKS CAUTION

- Court created: No securities fraud if the allegedly fraudulent statements are accompanied by (cloaked in) sufficient cautionary language.
- PSLRA - - projections given a safe harbor if the projections are clearly identified as forward looking statements.

KEY ELEMENTS OF NEW LAW

- Must change audit partner every 5 years
- Severe limits on consulting for audit clients.
- Extend statute of limitations.
- CEO and CFO must certify. 10 years for false cert.
- Creates accounting oversight board under SEC.
- Tougher penalties for corporate fraud.
- Increases SEC budget.
- 2 Biz day disclosure of insider stock sales.
- Prediction: Will make auditors richer.

Look for the Shredder

- New law puts 20 yr penalty for shredding documents.
- Find former employees
- What is missing?
- Document retention policies
 - Changes in enforcement or in policies themselves
 - New law imposes 7 yr retention policy for audit work papers.