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Comparative Negligence in Suits Against Accountants: A Statutory and Policy Analysis

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Comparative Negligence in Suits Against Accountants: A Statutory and Policy Analysis

I. Introduction

One of the most puzzling and debated issues in accounting malpractice cases is whether and to what extent the defense of comparative negligence is available to accountants. In *Fullmer v. Wohlfeiler & Beck*,[1] the Court of Appeals for the Tenth Circuit, interpreting Utah law, affirmed the federal district court's adoption of a judicial policy limiting an accountant's defense of comparative negligence to cases in which a plaintiff's negligence interfered with the accountant's ability to perform his duty.[2] Applied in a number of jurisdictions,[3] this policy is commonly known as the *National Surety*[4] rule. In a recent trend, however, courts in other jurisdictions have rejected the *National Surety* limitation on the apportionment of fault in accounting malpractice cases.[5] This comment argues that comparative negligence should be applied in accounting malpractice actions unrestricted by the *National Surety* rule.

Whether and to what extent a state's comparative negligence statute applies to accounting malpractice cases turns on the answers to three questions. First, as a matter of statutory construction, does the statute apply to cases in which the injury is only pecuniary and involves no damage to physical property? Second, are actions against accountants primarily contractual in nature, thereby possibly precluding application of comparative negligence? And, third, assuming the statute does apply to actions against accountants, should its application be restricted to cases in which the plaintiff's negligence has interfered with the accountant's ability to perform his duty?

Sections II and III of this comment analyze the first two questions in the context of Utah's comparative negligence statute. Neither question has been conclusively decided by Utah courts. Although the focus is on Utah law, the analysis is applicable to jurisdictions with similar

1. 905 F.2d 1394 (10th Cir. 1990)

2. The court did not address the viable issue of whether the Utah comparative negligence statute then in effect was applicable to pecuniary losses. *See infra* notes 8-33 and accompanying text.

3. *See* cases cited *infra* note 52.

4. National Sur. Corp. v. Lybrand, 256 A.D. 226, 9 N.Y.S.2d 554 (1939). For discussion of the *National Surety* rule, see *infra* notes 42-101 and accompanying text.

5. *See infra* notes 53-76 and accompanying text.

statutes. These sections conclude that Utah's comparative negligence statute is applicable in tort suits brought against accountants.

Section IV analyzes the *National Surety* rule in its historical context, arguing that the rule is obsolete in modern comparative negligence jurisdictions. Section V reviews cases representing a trend away from *National Surety*. Section V also analyzes the *National Surety* rule in light of the fairness, deterrence, and compensation policies of tort law in an effort to determine whether those policies are better served by limiting the defense of comparative negligence in suits against accountants. The analysis shows that the *National Surety* rule produces, in certain situations, a profound distortion in tort law policies. This comment concludes that the unrestricted application of comparative negligence serves the ends of the law better than the restrictions imposed by the *National Surety* rule.

II. Application of Utah's Comparative Negligence Statute to Pecuniary Losses in Suits Against Accountants

The type of injury resulting from accounting malpractice is pecuniary in nature. Whether Utah's or any state's comparative negligence statute applies to cases involving only pecuniary injury is first a question of statutory construction. This section addresses the question of statutory construction by analyzing Utah's comparative negligence statute in both its current[6] and previous[7] forms. It also reviews Utah court decisions interpreting the statutes and case law from other jurisdictions interpreting similar statutes.

A. *Utah's Original Comparative Negligence Statute*

Utah initially adopted comparative negligence in 1973 by legislative enactment.[8] Prior to being repealed and replaced by a significantly different comparative negligence statute in 1986,[9] section 1 of the 1973 statute read:

> Contributory negligence shall not bar recovery in an action by any person or his legal representative to recover damages for negligence or gross negligence resulting in *death or injury to person or property*, if such negligence was not as great as the negligence or gross negligence of the person against whom recovery is sought, but any damages al-

6. Utah Code Ann. § 78-27-38 (1987).

7. Utah Code Ann. § 78-27-37 (repealed 1986). Because of its potential applicability to pending accounting malpractice cases, Utah's former comparative negligence statute is also examined. *See infra* notes 8-33 and accompanying text.

8. Utah Code Ann. § 78-27-37 (repealed 1986) [hereinafter 1973 statute].

9. Utah Code Ann. § 78-27-38 (1987).

> lowed shall be diminished in the proportion to the amount of negligence attributable to the person recovering. As used in this act, "contributory negligence" includes "assumption of the risk."[10]

The most significant question posed by the 1973 statute in suits against accountants is whether the "property" clause encompasses pecuniary losses where there is no damage to physical property. Although Utah courts have not directly addressed this issue,[11] there is support for the proposition that the 1973 statute contemplates pecuniary losses. First, the 1973 statute was modeled after the Wisconsin statute, and Wisconsin courts have applied their statute to pecuniary losses.[12] Second, courts in other jurisdictions with similar statutes also apply them to pecuniary losses.[13] Third, the policies behind the comparative negligence statute warrant application to pecuniary injury.[14]

1. *Wisconsin roots*

The first section of Utah's 1973 statute was adopted from, and comprises the whole of, the Wisconsin Comparative Negligence Act in effect in 1971.[15] In *Jensen v. Intermountain Health Care, Inc.*,[16] the court not only recognized that the Utah legislature intended to adopt the Wisconsin comparative negligence statute but also recognized when a statute from another state is adopted, the legislature is presumed to have adopted that state's judicial interpretations of the statute as well.[17]

The presumption that Utah has adopted Wisconsin's judicial interpretations does not require Utah Courts to summarily adopt every Wisconsin decision.[18] This is illustrated by the Utah Supreme Court's rejection of the Wisconsin method of comparing a plaintiff's negligence

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10. UTAH CODE ANN. § 78-27-37 (repealed 1986) (emphasis added).

11. Dicta in one Utah case could be interpreted as excluding pecuniary injury from the 1973 statute. *See infra* note 33 and accompanying text.

12. *See infra* notes 15-20 and accompanying text.

13. *See infra* notes 21-27 and accompanying text.

14. *See infra* notes 28-33 and accompanying text.

15. Wisconsin's Comparative Negligence Act provides:

> Contributory negligence shall not bar recovery in an action by any person or his legal representative to recover damages for negligence resulting in death or an injury to person or property, if such negligence was not greater than the negligence of the person against whom recovery is sought, but any damages allowed shall be diminished in the proportion to the amount of negligence attributable to the person recovering.

WIS. STAT. ANN. § 895.045 (West 1983). Utah courts have recognized that the 1973 statute is patterned after the Wisconsin statute. *See* Dixon v. Stewart, 658 P.2d 591, 593 (Utah 1982); Jensen v. Intermountain Health Care, 679 P.2d 903, 904 (Utah 1984).

16. 679 P.2d 903 (Utah 1984).

17. *Id.* at 904.

18. The dissent in *Jensen* stated that case law from states with similar comparative negligence statutes is also persuasive. *Id.* at 911 (Hall, C.J., dissenting).

with each defendant individually.[19] However, it may be argued that Wisconsin case law is particularly persuasive in interpreting Utah's 1973 statute. This is important because the Wisconsin case *Imark Industries, Inc. v. Arthur Young & Co.*[20] applied comparative negligence to apportion liability for pecuniary losses in a suit against accountants. Several cases from other jurisdictions, including *Imark Industries*, are reviewed below.

2. *Case law from jurisdictions with similar statutes*

Other jurisdictions have applied statutes similar to Utah's 1973 comparative negligence statute to pecuniary losses in suits against accountants,[21] other professionals,[22] and in other cases of economic loss.[23] In *Imark Industries, Inc. v. Arthur Young & Co.*,[24] a Wisconsin court upheld the division of liability for pecuniary losses in an accounting malpractice case according to Wisconsin's comparative negligence statute. Significantly, the issue of whether comparative negligence was applicable to pecuniary losses was not addressed by the court, and no previous Wisconsin court had ruled on the issue. A legitimate inference can be made that Wisconsin's comparative negligence statute, and by implication Utah's 1973 statute, contemplates pecuniary losses.

Similarly, in *Darnell Photographs, Inc. v. Great American Insurance Co.*,[25] the Colorado appellate court specifically rejected the notion that the phrase "injury to property" in the Colorado comparative negligence statute (nearly identical to Utah's 1973 statute) is limited to tangible property. The court stated that

> [i]t is well recognized that comparative negligence statutes have been enacted to ameliorate harsh results which sometimes occur under the doctrine of contributory negligence. To adopt the narrow construction

19. *Id.* at 909-10. The court based its conclusion to reject the Wisconsin method of comparison on additional sections added to the Utah statute that were not found in the Wisconsin statute.

20. 148 Wis. 2d 605, 436 N.W.2d 311 (1989).

21. Halla Nursery v. Baumann-Furrie & Co., 454 N.W.2d 905 (Minn. 1990); H. Rosenblum, Inc. v. Adler, 93 N.J. 324, 461 A.2d 138 (1983) (New Jersey statute modeled after Wisconsin's); First Nat'l Bank v. Kehn Ranch, 394 N.W.2d 709 (S.D. 1986) (interpretation of Minnesota law); University Nat'l Bank v. Ernst & Whinney, 773 S.W.2d 707 (Tex. Ct. App. 1989); Imark Indus. v. Arthur Young & Co., 148 Wis. 2d 605, 436 N.W.2d 311 (1989).

22. Somma v. Gracey, 15 Conn. App. 371, 544 A.2d 668 (1988) (attorney); Erlich v. First Nat'l Bank, 208 N.J. Super. 264, 505 A.2d 220 (Law Div. 1984) (investment advisor).

23. Robinson v. Poudre Valley Fed. Credit Union, 680 P.2d 241 (Colo. Ct. App. 1984) (suit against bank and its employee); Darnell Photographs v. Great Am. Ins. Co., 33 Colo. App. 256, 519 P.2d 1225 (1974); Lippes v. Atlantic Bank, 69 A.D.2d 127, 419 N.Y.S.2d 505 (App. Div. 1979) (bank); *cf.* Miller v. Pine Bluff Hotel Co., 286 F.2d 34 (8th Cir. 1961) (interpreting Arkansas statute).

24. 148 Wis. 2d 605, 436 N.W.2d 311 (1989).

25. 33 Colo. App. 256, 519 P.2d 1225 (1974).

> of the statute as proposed by defendant would defeat the purpose for which it was designed; therefore, we hold that the phrase "injury to property" in the comparative negligence statute is not necessarily limited to a physical injury to tangible property, but rather includes any damage resulting from invasion of one's property rights by actionable negligence.[26]

The Colorado court's reasoning is compelling. It is unlikely that a legislature would intend to ameliorate the harsh results of contributory negligence in cases of damage to physical property and at the same time intend to retain the same harsh results in cases of pecuniary loss. Although no Utah court has conclusively ruled on the issue, statements of policy found in several Utah opinions are consistent with the rationale of *Darnell Photographs*, as reviewed below.[27]

3. *Policy behind the comparative negligence statute*

The Utah Supreme Court first examined Utah's 1973 statute in *Rigtrup v. Strawberry Water Users Association*.[28] There, the court stated that "the purpose of [that] statute was to abolish contributory negligence as a complete defense and thus avoid the harshness which sometimes resulted when a party seeking redress was himself negligent . . . ."[29] Later, in *Jensen v. Intermountain Health Care, Inc.*,[30] the court described the two objectives of the 1973 statute as "first, to alleviate the harshness of the old common law doctrine of contributory negligence; and second to provide for a system of loss allocation by apportioning liability based at least in part on fault . . . ."[31] Given these objectives, it makes little sense to alleviate the harshness of the common law in some negligence cases but not in others. Further, no Utah court has articulated a useful purpose that would be served by not applying comparative negligence in cases where pecuniary losses are not accompanied by damage to tangible property.

One Utah case which came close to applying the 1973 statute to pecuniary losses was *Acculog, Inc. v. Peterson*.[32] There, the court approved the allocation of fault where pecuniary losses (lost profits) were the result of negligent injury to physical property. It should be noted, however, that in Justice Oaks' concurrence, he stated that comparative

26. *Id.* at 258, 519 P.2d at 1226 (citations omitted).
27. *See infra* notes 28-33 and accompanying text.
28. 563 P.2d 1247 (Utah 1977) (overruled on other grounds by Moore v. Burton Lumber & Hardware, 631 P.2d 865 (Utah 1981)).
29. *Id.* at 1249.
30. 679 P.2d 903 (Utah 1984).
31. *Id.* at 907.
32. 692 P.2d 728 (Utah 1984) (damage to truck and equipment used in business).

negligence "only applies to negligence 'resulting in death or in injury to person or property.' "[33] Justice Oaks did not elaborate on what he meant by "only," but a logical inference is that the 1973 statute does not apply to pecuniary losses. Nevertheless, case law from other jurisdictions, as well as compelling public policy arguments, strongly suggests that the 1973 statute applied to pecuniary losses. The same question does not exist under the current statute.

B. *The Current Comparative Negligence Statute*

In 1986, the Utah Legislature repealed the 1973 statute and replaced it with the following:

> The fault of a person seeking recovery shall not alone bar recovery by that person. He may recover from any defendant or group of defendants whose fault exceeds his own. However, no defendant is liable to any person seeking recovery for any amount in excess of the proportion of fault attributable to that defendant.[34]

The Legislature defined the term "fault" to mean "any actionable breach of legal duty, act or omission proximately causing or contributing to injury or damages . . . ."[35] This definition, coupled with the fact that the 1986 statute omits the phrase "death or injury to person or property," broadens the 1986 statute to clearly apply to purely economic losses.

At first blush, the language of the 1986 statute appears to significantly expand the scope of cases in which the defense of comparative negligence is available. However, the 1986 statute may be nothing more than a clarification of the intent embodied in the 1973 statute; that is, comparative negligence applies to all negligence actions.

III. The Contractual Versus Tortious Nature of Accounting Malpractice

The second question of the three-part analysis is whether actions against accountants are contractual or tortious in nature. Some courts have answered this question by holding that actions against accountants arising from performance of their services may be brought in contract or tort.[36] Comparative negligence, however, is generally inapplicable in

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33. *Id.* at 732 (Oaks, J., concurring) (quoting Utah's 1973 statute).

34. Utah Code Ann. § 78-27-38 (1987) [hereinafter 1986 statute]. The 1986 statute became effective April 28, 1986, and because no intention of retroactive application was articulated by the legislature, it is inapplicable to injuries occurring before that date. Stephens v. Henderson, 741 P.2d 952, 953-54 (Utah 1987).

35. Utah Code Ann. § 78-27-37 (1987).

36. *See* Blumberg v. Touche Ross & Co., 514 So. 2d 922 (Ala. 1987); Billings Clinic v. Peat

contract actions.[37] In variations of this general rule, it has been held that comparative negligence principles may be used to apportion damages in claims for breach of implied warranty[38] and failure to mitigate damages.[39] Because actions against accountants may be brought in either contract or tort, a question arises whether the application of comparative negligence should be limited to actions solely grounded in tort.

In *Cenco, Inc. v. Seidman & Seidman*,[40] the Court of Appeals for the Seventh Circuit solved this problem by combining tort and contract claims against an accountant into a single cause of action. The court stated that "[d]espite the plurality of charges [whether management wrongdoing is a defense in a suit against accountants] is one question because breach of contract, negligence, and fraud, when committed by auditors, are a single form of wrongdoing under different names."[41] Although comparative negligence is generally inapplicable to actions in contract, combining both tort and contract claims into one cause of action effectively makes comparative negligence a defense to a contract claim. While this approach may enhance judicial administration, it raises serious concerns whether plaintiffs in accounting malpractice cases would essentially be denied their contractual causes of action.

A plaintiff in an accounting malpractice action generally controls whether the defense of comparative negligence will be available by choosing whether to litigate in tort or contract. Unless the court combines tort and contract causes of action into one, or employs comparative negligence principles to apportion damages in the contract suit, the theory ultimately prevailed upon will dictate whether comparative negligence will be used to apportion damages in suits against accountants.

IV. The *National Surety* Rule—A Judicial Doctrine of Limiting Application of Comparative Negligence in Suits Against Accountants

The final question to be answered before comparative negligence

Marwick Main & Co., 797 P.2d 899 (Mont. 1990); Video Corp. of Am. v. Frederick Flatto Assoc., 58 N.Y.2d 1026, 448 N.E.2d 1350, 462 N.Y.S.2d 439 (1983): *see also* Hawkins, *Professional Negligence Liability of Public Accountants*, 12 Vand. L. Rev. 797 (1959).

37. *See, e.g.*, Federal Sav. & Loan Ins. Corp. v. Huff, 237 Kan. 873, 704 P.2d 372 (1985); Lesmeister v. Dilly, 330 N.W.2d 95 (Minn. 1983) (citing comments to Unif. Comp. Fault Act § 1, 12 U.L.A. 35 (Supp. 1982)); Behring Int'l v. Greater Houston Bank, 662 S.W.2d 642 (Tex. Ct. App. 1983); Cline v. Sawyer, 600 P.2d 725 (Wyo. 1979).

38. Signal Oil & Gas Co. v. Universal Oil Prods., 572 S.W.2d 320 (Tex. 1978).

39. Mike's Fixtures v. Bombard's Access Floor Sys., 354 N.W.2d 837 (Minn. Ct. App. 1984).

40. 686 F.2d 449 (7th Cir.), *cert. denied*, 459 U.S. 880 (1982) (interpreting Illinois law).

41. *Id.* at 453; *see also* Wedtech Corp. v. Hurdman (*In re* Wedtech Corp.), 81 Bankr. 240, 241 (S.D.N.Y. 1987) (citing *Cenco*, 686 F.2d at 453).

can be asserted in an accounting malpractice action is whether the defense should be judicially restricted to cases in which a plaintiff's negligence interfered with the accountant's ability to fulfill his duty. The origin of this theory can be traced to *National Surety Corp. v. Lybrand*,[42] a 1939 New York case. *Craig v. Anyon*,[43] a 1925 New York decision, is generally cited as the antithesis of *National Surety*. Although decided over two generations ago under common law contributory negligence, the debate sparked by these two cases still thrives in jurisdictions that have not conclusively decided the issue.[44] This section reviews the development of the *Craig v. Anyon* and *National Surety* rules and examines their underlying policies. What we find is that the two cases are not as diametrically opposed as is often stated. The conclusion reached is that the *National Surety* rule is obsolete and comparative negligence better serves the policies of tort law.

A. The Craig v. Anyon *and* National Surety *Split*

Craig v. Anyon and *National Surety* appear to set forth very different rules for allowing contributory negligence defenses in suits against accountants. Most later courts considering the issue have adopted one or the other based on its own interpretation of the merits of the case.[45] However, upon closer examination, *Craig v. Anyon* and *National Surety* may not be as far apart as is generally assumed. Rather than conflicting policies of law, the differences can be better explained by the facts of each case, as discussed below.

1. Craig v. Anyon

In *Craig v. Anyon*, the client of an accounting firm sought damages from the accountant auditors for negligently failing to detect a large embezzlement scheme perpetrated by an employee. Recovery was denied, however, because the plaintiff was found to be contributorily negligent in giving the employee absolute control over the department

42. 256 A.D. 226, 9 N.Y.S.2d 554 (1939).

43. 212 A.D. 55, 208 N.Y.S. 259 (1925), *aff'd*, 242 N.Y. 569, 152 N.E. 431 (1926).

44. Articles by several commentators have addressed these two cases: Hawkins, *supra* note 35; Mendel, *The Defense of Contributory Negligence in Accountant's Malpractice Actions*, 12 SETON HALL 292 (1983); Note, *The Peculiar Treatment of Contributory Negligence in Accountants' Liability Cases*, 65 N.Y.U. L. REV. 329 (1990); Comment, *Damage Apportionment in Accounting Malpractice Actions: The Role of Comparative Fault*, 1990 B.Y.U. L. REV. 951. Professor Hawkins makes a persuasive argument that the *National Surety* rule is the preferred approach.

45. *See, e.g.*, Devco Premium Fin. Co. v. North River Ins. Co., 450 So. 2d 1216 (Fla. Dist. Ct. App. 1984) (following *Craig v. Anyon*); Lincoln Grain v. Coopers & Lybrand, 216 Neb. 433, 345 N.W.2d 300 (1984) (following *National Surety*).

from which he embezzled, and for failing to supervise him. Both the auditors and the employer had been deceived by the employee. The court found that the embezzlement would have been discovered had the audit been performed properly, but it would also have been discovered had the employer properly supervised the employee.[46] Faced with deciding which of the negligent parties would bear the entire loss under New York's contributory negligence law, the court chose the plaintiff, stating: "We think the damages cannot be said to flow naturally and directly from defendants' negligence or breach of contract. Plaintiff's should not be allowed to recover losses which they could have avoided by the exercise of reasonable care."[47] The dilemma faced in *National Surety* was similar, but the outcome quite different.

2. National Surety

National Surety Corp. v. Lybrand[48] is often cited for the proposition that the "[n]egligence of the employer is a defense only when it has contributed to the accountant's failure to perform his contract and to report the truth."[49] In *National Surety*, the defendant auditors failed to detect a "kiting"[50] scheme perpetrated by an employee. The auditors would have detected the scheme had they performed the relatively simple procedure of verifying cash balances. Upon being sued, the accountants asserted the defense of contributory negligence, arguing that the client's negligence in conducting its business made possible the undetected embezzlement. In rejecting the defense of contributory negligence, the court stated:

> We are, therefore, not prepared to admit that accountants are immune from the consequences of their negligence because those who employ them have conducted their own business negligently . . . . Accountants, as we know, are commonly employed for the very purpose of detecting defalcations which the employer's negligence has made possible. Accordingly, we see no reason to hold that the accountant is not liable to his employer in such cases. *Negligence of the employer is a defense only when it has contributed to the accountant's failure to perform his contract and to report the truth* . . . . That was the principle applied in *Craig v. Anyon* where the embezzler had been negligently represented to the accountants as a person

46. 212 A.D. at 64, 208 N.Y.S. at 267.
47. *Id.* at 66, 208 N.Y.S. at 268.
48. 256 A.D. 226, 9 N.Y.S.2d 554 (1939).
49. *Id.* at 236, 9 N.Y.S.2d at 563.
50. "Kiting" is the process of transferring funds from one account to another in a circular fashion, thereby disguising a shortfall of funds in the accounts.

to be trusted.[51]

This rule has been adopted in a number of jurisdictions.[52]

It is interesting to note that the court saw its opinion as being in harmony with *Craig v. Anyon*. If *National Surety* and *Craig v. Anyon* are indeed in harmony, a good deal of discussion over the years was made on the wrong premise. Regardless of whether the differences are perceived or actual, the cases continue to be useful for discussing the merits of whether comparative negligence should apply in accounting malpractice actions where the plaintiff has not impeded the accountant's ability to fulfill his duty.

B. Choosing Between Craig v. Anyon *and* National Surety*—A Choice Past Its Prime*

Courts adopting either *National Surety* or *Craig v. Anyon* have often overlooked three key points suggesting that the rationale for adopting either rule outside of the context of contributory negligence is inappropriate. First, both *Craig v. Anyon* and *National Surety* were decided under a common law contributory negligence scheme of all-or-nothing. The harshness of that rule required a court to justify its balancing of the equities of the case in favor of one litigant over the other. Second, the facts in *National Surety* were weighted in the plaintiff's favor; that is, the accountant's conduct was clearly more egregious than the plaintiff's. However, under the contributory negligence standard, the plaintiff would have been denied recovery for being somewhat negligent. Third, the facts in *Craig v. Anyon* were more heavily weighted in favor of the defendant accountant, whose negligence appeared less a cause of the losses than the plaintiff's. Accordingly, the court fashioned a remedy under the contributory negligence standard that barred the plaintiff from recovery.

The facts, therefore, offer a better explanation of the different rulings than does the interpretation that the cases set forth broad polar pronouncements of policy. Laboring under the harsh realities of the all-or-nothing rule of contributory negligence, the court in each case justified its holding by articulating a policy behind it. It is inappropriate, therefore, to take these two decisions out of context and apply them

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51. 256 A.D. at 235-36, 9 N.Y.S.2d at 563 (citations omitted) (emphasis added).

52. Cases adopting the *National Surety* rule include: Fullmer v. Wohlfeiler & Beck, 905 F.2d 1394 (10th Cir. 1990) (interpreting Utah law); Shapiro v. Glekel, 380 F. Supp. 1053 (S.D.N.Y. 1974); Lincoln Grain v. Coopers & Lybrand, 216 Neb. 433, 345 N.W.2d 300 (1984); Jewelcor Jewelers & Distribs. v. Corr, 373 Pa. Super. 536, 542 A.2d 72 (1988); Greenstein, Logan & Co. v. Burgess Mktg., 744 S.W.2d 170 (Tex. Ct. App. 1987). ***But see*** University Nat'l Bank v. Ernst & Whinney, 773 S.W.2d 707 (Tex. Ct. App. 1989).

across the board in all accounting malpractice cases. This is especially so in a comparative negligence jurisdiction where some middle ground is available to alleviate the harshness of the all-or-nothing result of contributory negligence.

When viewed in their factual and historical contexts, *Craig v. Anyon* and *National Surety* may well be decisions of a by-gone era. While they and the service they rendered should be remembered with respect, they should not continue to rule in their infirmity if a better rule is available. The case for unrestricted application of comparative negligence in accounting malpractice cases is compelling, as discussed in the balance of this comment.

V. THE CASE FOR UNRESTRICTED APPLICATION OF COMPARATIVE NEGLIGENCE—TRENDS AND POLICIES

Recent cases show a trend toward less restrictive application of comparative negligence in suits against accountants. A jurisdictional review of cases reflective of this trend and the policies they articulated is presented below. The *National Surety* rule is analyzed in the context of the fairness, deterrence, and compensation policies of tort law. The conclusion drawn from this exercise is that policy concerns are better satisfied within the comparative negligence framework.

A. *Recent Cases Applying Comparative Negligence in Suits Against Accountants*

1. *Wisconsin*

In *Imark Industries, Inc. v. Arthur Young & Co.*,[53] Imark Industries brought an action for negligent misrepresentation against Arthur Young after a debtor of Imark Industries defaulted on a loan. Arthur Young had audited the financial statements of the defaulting company, and Imark Industries had allegedly relied on the statements in extending credit. The jury found that the officers of the defaulting company had made intentional misrepresentations to Arthur Young in the course of the audit and that Arthur Young had justifiably relied on those misrepresentations.[54] However, the jury also found that the majority of the audit errors resulted from Arthur Young's own negligence.[55] The trial court applied comparative negligence principles and divided the fault between the officers who made the initial misrepresentations and Arthur Young.

53. 148 Wis. 2d 605, 436 N.W.2d 311 (1989).
54. *Id.* at 614-16, 436 N.W.2d at 315-16.
55. *Id.*

The issues raised on appeal were related to certain aspects of the application of comparative negligence to the peculiar facts of the case. However, the applicability of the comparative negligence statute to accounting malpractice actions was not questioned nor the *National Surety* rule discussed. Rather, the comparative negligence issue appears to have been sent to the jury as a matter of course, and its application was not challenged on appeal.[56] Under *National Surety*, the defense of contributory negligence would not have been available.

2. *Minnesota*

In *Halla Nursery, Inc. v. Baumann-Furrie & Co.*,[57] the Minnesota Supreme Court specifically rejected the *National Surety* rule.[58] In that case, plaintiff sought to hold accountants liable for negligent failure to detect embezzlements by the plaintiff's employees. The trial court, however, denied plaintiff's motion in limine to bar evidence of the plaintiff's negligence that did not directly affect the ability of the accountants to perform their duty. Consequently, the jury apportioned 80% of the liability to the plaintiff.[59] On appeal, the court of appeals held that the trial court erred in not following the *National Surety* rule.[60]

The Minnesota Supreme Court reversed, stating that the "application of the broad definition of fault as set forth in the comparative fault statute can be particularly appropriate . . . in an action by a client against an accountant for negligent failure to discover embezzlements . . . ."[61] The supreme court's rationale for rejecting the *National Surety* rule was that "the persons who hire accountants, usually businesspersons, should also be required to conduct their business activities in a reasonable and prudent manner."[62] The conclusion reached by the Minnesota Supreme Court is more akin to the *Craig v. Anyon* approach permiting the jury to consider the plaintiff's negligence.

3. *New Jersey*

In *H. Rosenblum, Inc. v. Adler*,[63] the court expressly stated that an injured party's recovery in an accounting malpractice case may be

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56. *Id.* at 625, 436 N.W.2d at 319-20.
57. 454 N.W.2d 905 (Minn. 1990).
58. *Id.* at 909.
59. *Id.* at 906.
60. *Id.* at 907.
61. *Id.* at 909.
62. *Id.*
63. 93 N.J. 324, 461 A.2d 138 (1983).

limited or denied under New Jersey's comparative negligence statute,[64] which is also modeled after the Wisconsin statute.[65]

In discussing the increasingly open-ended exposure of accountants for their work, the court stated:

> The extent of financial exposure has certain built-in limits . . . . The injured party would be limited to recovery of actual losses due to reliance on the misstatement. *Negligence of the injured party could bar or limit the amount of recovery under the Comparative Negligence Act.* The accounting firm could seek indemnification or contribution from the company and those blameworthy officers or employees.[66]

The court in *Adler*, therefore, expresses the view that comparative negligence is a counter-balance to the expansive scope of duty that an accountant owes to those who rely on his work. The *National Surety* rule, however, would tip this counter-balance by leaving an auditor completely exposed to the more expansive liability, while at the same time greatly restricting his defense of comparative negligence.

4. *Texas*

In Texas, the use of comparative negligence in an accounting malpractice case was upheld in *University National Bank v. Ernst & Whinney*.[67] There, a bank sued its independent auditors for failure to disclose the uncollectibility of certain loans. The auditors alleged that the bank negligently caused its own damages by making the bad loans. Negligence was apportioned 59% to the bank and 41% to the auditors.[68] Nothing in the opinion indicates that the bank had in any way prevented the auditors from performing their duty, even though the previous Texas decision *Greenstein, Logan & Co. v. Burgess Marketing, Inc.*[69] adopted the *National Surety* rule.

Texas subsequently amended its comparative negligence statute in 1987 to specifically include public accountants.[70] Significantly, the new

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64. *Id.* at 350-51, 461 A.2d at 152.

65. Rawson v. Lohsen, 145 N.J. Super. 71, 366 A.2d 1022 (1976), *cited in* Jensen v. Intermountain Health Care, 679 P.2d 903, 913 (Utah 1984).

66. 93 N.J. at 350-51, 461 A.2d at 152 (citations omitted) (emphasis added).

67. 773 S.W.2d 707 (Tex. Ct. App. 1989).

68. *Id.* at 708.

69. 744 S.W.2d 170 (Tex. Ct. App. 1987).

70. TEX. CIV. PRAC. & REM. § 33.001(c) (Vernon 1987) provides:

> In an action in which a claimant seeks damages for harm other than personal injury, property damage, or death, arising out of any action grounded in negligence, including but not limited to negligence relating to any professional services rendered by an architect, attorney, [or] certified public accountant, . . . a claimant may recover damages only if his percentage of responsibility is less than or equal to 50 percent.

Texas statute groups accountants with other professionals and does not suggest that they be treated differently. Because *University National Bank* was decided after *Greenstein* and because of the statutory amendment to specifically include accountants, it appears that application of comparative negligence in comparative malpractice cases is favored by both the Texas judiciary and legislature.

5. *Michigan*

In *Capital Mortgage Corp. v. Coopers & Lybrand*,[71] defendant accountants failed during a routine audit to detect a $1.5 million dollar embezzlement. In a case of first impression, the Michigan court found that the application of comparative negligence in accounting malpractice cases is proper, stating:

> With comparative negligence the result is not so harsh and the policy considerations that accountants should not be allowed to avoid all liability due to some negligence on the part of the client are not present. We find the application of comparative negligence to be proper as neither party is absolved of fault due to the other's negligence. Comparative negligence creates an incentive for both parties to use due care.[72]

The court saw no reason to restrict the application of comparative negligence in accounting cases. The rationale of providing an incentive to both auditors and those who hire them echoes the reasoning of *Halla Nursery, Inc. v. Baumann-Furie & Co.*[73]

6. *Florida*

The court in *Devco Premium Finance Co. v. North River Insurance Co.*[74] also rejected *National Surety*, citing instead *Craig v. Anyon* as the better rule.[75] In *Devco Premium Finance*, auditors negligently failed to determine that a significant number of accounts receivable were uncollectible. The same information, however, was available to the client who also negligently failed to discover the problem. The trial court apportioned negligence 80% to the client and 20% to the accountants. On appeal of the comparative negligence issue, the court stated that "plaintiffs should not be allowed to recover for losses which they

71. 142 Mich. App. 531, 369 N.W.2d 922 (1985).
72. *Id.* at 535, 369 N.W.2d at 925.
73. 454 N.W.2d 905 (Minn. 1990). *See supra* notes 57-62 and accompanying text.
74. 450 So. 2d 1216 (Fla. Ct. App. 1984).
75. *Id.* at 1220.

could have avoided by the exercise of reasonable care."[76]

B. Cases Applying Comparative Negligence in Suits Against Other Professionals

A review of cases in which comparative negligence has been applied in suits against other professionals is also helpful in determining how it should be applied in cases dealing with accounting malpractice.

1. Illinois—attorney malpractice

Comparative negligence was applied in an attorney malpractice case brought in a federal court under Illinois law in *Greycas, Inc. v. Proud.*[77] There, an attorney told his client specifically that he had conducted a UCC search when, in fact, he had not. The court stated that comparative negligence is as much a defense to negligent misrepresentation as to any other tort of negligence.[78] Accountants often fall victim to negligent misrepresentation claims and, therefore, should likewise be permitted to invoke the defense of comparative negligence.

2. Connecticut—attorney malpractice

In *Somma v. Gracey,*[79] a malpractice claim was brought by clients against an attorney. The court stated that "[i]n situations where the claim of malpractice sounds in negligence, the defense of comparative negligence should be permitted."[80] Connecticut's comparative negligence statute specifically applies to economic losses.[81] The Connecticut approach also supports the proposition that comparative negligence should not be limited to cases involving physical injury.

3. New Jersey—investment advisor negligence

Erlich v. First National Bank of Princeton[82] is another New Jersey case in which comparative negligence was applied to pecuniary losses occasioned by professional negligence. In that case, an investor sued a professional investment advisor who had recommended concentration in a single stock that failed. The court held the application of comparative negligence was proper because the plaintiff, though not a

76. *Id.* (quoting Craig v. Anyon, 212 A.D. at 66, 208 N.Y.S.2d at 268).
77. 826 F.2d 1560 (7th Cir. 1987), *cert denied*, 484 U.S. 1043 (1988).
78. 826 F.2d at 1566.
79. 15 Conn. App. 371, 544 A.2d 668 (1988).
80. *Id.* at 378, 544 A.2d at 672 (citations omitted).
81. *Id.*
82. 208 N.J. Super. 264, 505 A.2d 220 (N.J. Super. Ct. Law Div. 1984).

sophisticated investor, was sufficiently knowledgeable of investments to be found negligent in the handling of his own investments.[83] Likewise, it seems that sophisticated investors should not be allowed to escape liability for their own negligent decisions through application of the *National Surety* rule just because they did not interfere with an auditor's ability to perform his duty. Otherwise, accountants become guarantors of investors' losses.

These cases involving professional negligence, as well as those cases involving accountants, illustrate the increasing acceptance of applying comparative negligence principles in all professional negligence cases. The policies underlying this trend are next examined.

C. *Policy Reasons for Applying Comparative Negligence in Accounting Malpractice Actions*

The public policy underpinnings of tort law are deterrence and compensation.[84] Fairness, of course, should be a goal of any legal scheme. Comparative negligence has been adopted by a majority of states because it is thought to serve these policies better than the harsher system of contributory negligence. Each of these policies is reviewed below in light of the *National Surety* rule in an attempt to ascertain whether the purpose of the policy is better served by that rule or by the unrestricted application of comparative negligence.

1. *Fairness*

The court in *Rigtrup* stated that "the purpose of the [comparative negligence] statute was to abolish contributory negligence as a complete defense and thus avoid the harshness which sometimes resulted when a party seeking redress was himself negligent . . . ."[85] This same rationale of avoiding the harsh results of contributory negligence was stated by the court in *Capital Mortgage Corp. v. Coopers & Lybrand*[86] as the reason for applying comparative negligence in an action against an accounting firm, even though there was no showing of interference with the firm's performance of its duty.[87]

The harshness to be avoided under the common law was the all-or-nothing effect of the complete bar against plaintiffs' claims that ac-

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83. *Id.* at 302, 505 A.2d at 240.

84. *See* W. KEETON, D. DOBBS, R. KEETON & D. OWEN, PROSSER AND KEETON ON TORTS, § 1, at 5-7 (5th ed. 1984).

85. 563 P.2d 1247, 1249 (Utah 1977).

86. 142 Mich. App. 531, 369 N.W.2d 922 (1985). *See supra* notes 71-73 and accompanying text.

87. 142 Mich. App. at 535, 369 N.W.2d at 925.

companied contributory negligence. The critical question is whether the *National Surety* rule furthers the goal of minimizing the harshness of contributory negligence. A simple hypothetical shows that, in certain situations, it does not further these goals, and illustrates that the *National Surety* rule actually is an impediment to their achievement.

This hypothetical closely resembles the facts of *Halla Nursery, Inc. v. Baumann-Furrie & Co.*[88] In the hypothetical, an auditor fails to detect embezzlements by his client's employee, and the client suffers a loss. The facts are such that a jury could reasonably conclude that the accountant was 20% at fault for not discovering the defalcation and that the client was 80% at fault for negligent supervision of the employee. The client did not impede the auditor's ability to perform his duties.

Under the common law of contributory negligence, the client in this hypothetical would recover nothing; the accountant would be absolved. Pure comparative negligence avoids this result by allowing the plaintiff to recover the 20% occasioned by the accountant's negligence. The modified comparative negligence, or "50% rule," of Utah's comparative negligence statute[89] would be a complete bar to recovery. Under either pure or modified comparative negligence law, application of the *National Surety* rule produces the amazing distortion of allowing the client to recover 100% of the loss from his accountant. This distortion is caused by completely denying the accountant the defense of comparative negligence. Assuming the loss was $100,000, the apportionment of damages under the various rules would be as follows:

Rule	Amount of Loss Born by Defendant 20% Negligent	Amount of Loss Born by Plaintiff 80% Negligent
Common law	0	$100,000
Pure comp. neg.	$ 20,000	$ 80,000
50% rule	0	$100,000
National Surety	$100,000	0

This simple illustration shows that the *National Surety* rule not only maintains the harshness of the old common law of contributory negligence, but also refocuses it in the opposite direction—toward the defendant. Surely this was not the result envisioned by Justice Untermyer when he drafted the *National Surety* opinion. Justice Untermyer, it must be remembered, was laboring under the old contributory negli-

88. 454 N.W.2d 905 (Minn. 1990). *See supra* notes 57-62 and accompanying text.

89. Utah's statute only allows recovery by a plaintiff from a defendant "whose fault exceeds his own." UTAH CODE ANN. § 78-27-38 (1987). Therefore, if the plaintiff's negligence is 50% or greater, the statute bars any recovery.

gence standard in his attempt to fashion a fair result.[90]

2. *Deterrence*

It is well recognized that a primary goal of tort law is deterrence of future wrongs.[91] Deterrence may be looked at in the context of who is bringing the action and the type of conduct that is the object of the deterrence. In accounting malpractice cases, there are three possible parties who might be deterred from acting negligently: the accountant, the client, and the third-party user of the accountant's work. It is helpful to separately analyze the deterrent effect of comparative negligence and the *National Surety* rule on each party.

As for the auditor, the threat of liability for negligent performance of his duties is a powerful incentive to avoid negligence. The *National Surety* rule maximizes the deterrence directed toward the accountant by eliminating the possibility that anyone else will share the burden of liability by increasing the accountant's liability to 100%. This maximization is achieved, however, at the expense of fairness to the accountant and a reduction in deterrence directed at other parties.

Deterring negligent acts of clients is also a legitimate goal of tort law. The court in *Halla Nursery Inc. v. Baumann-Furrie & Co.*[92] recognized that not only auditors, but also those that hire them, must be deterred from wrongdoing.[93] Comparative negligence furthers the goal of deterrence by holding each wrongdoer liable, thereby avoiding the inequitable all-or-nothing liability (and hence, deterrence) result of contributory negligence. *National Surety* reverses the direction of the all-or-nothing result but does not change the fundamental flaw of directing the deterrence effect toward only one party.

Tort law should also deter third-party users of accountants' work, such as investors, from acting negligently. Investor negligence consists of poor investment decisions which have no effect on an auditor's ability to fulfill his duty. This poses the question of whether it is proper to compare an investor's negligent investment decision with an auditor's negligent performance of an audit. The idea is not without precedent. In *E.F. Hutton Mortgage Corp. v. Pappas*,[94] decided under Maryland law which has not adopted comparative negligence, plaintiff Hutton purchased mortgages on the secondary market from a company audited by the defendants. The plaintiffs suffered significant losses and sued the

90. *See supra* notes 48-52 and accompanying text.

91. *See, e.g.*, Condemarin v. University Hosp., 775 P.2d 348, 365 (Utah 1989).

92. 454 N.W.2d 905 (Minn. 1990).

93. *Id.* at 909.

94. 690 F. Supp. 1465 (D. Md. 1988).

auditors. The court stated that even if the financial statements plaintiffs claimed to have relied on were negligently prepared in some respects, they clearly showed the seller was in shaky financial condition and thus "did not paint a misleadingly rosy picture."[95] The court further stated that a sophisticated investor cannot claim reliance on audit reports when it could have discovered the true nature of the situation by exercising ordinary diligence.[96] The court also found that even if the audit was performed negligently in some respects, Hutton had failed to act prudently in making a proper investigation of its investment and, therefore, as a matter of law, was barred from recovery under the doctrine of contributory negligence.[97]

Similarly, in *Hasbro Bradley, Inc. v. Coopers & Lybrand*,[98] the court allowed Coopers & Lybrand to set forth as a defense five factors in the financial statements it audited that would put a prudent lender on notice of the extremely shaky character of the debtor. Assuming that negligent conduct of investors is a proper subject of the deterrent goal of tort law, the question is whether the *National Surety* rule furthers that goal better than comparative negligence. The previous discussion of client negligence leads immediately to the realization that the *National Surety* rule creates the same reverse all-or-nothing distortion, this time between the accountant and the investor. The investor may act negligently and still recoup his entire loss. This is not deterrence. Comparative negligence, however, holds each party liable for his own negligence, thereby deterring both parties from acting negligently.

3. *Compensation—accountants are not guarantors*

The primary goal of tort law is to compensate victims. However, denying the defense of comparative negligence to accountants has the effect of turning them into guarantors. To illustrate, had the court adopted the *National Surety* rule in *E.F. Hutton*,[99] the accountants would have been prevented from raising the plaintiff's negligence as a defense. The auditor, therefore, as the only party left to whom liability might attach, would have been liable for the entire loss. This policy arguably allows an investor to be more speculative in his investments by transferring the risk of loss stemming from his own negligence to the accountant. At least theoretically, an investor whose loss was caused

95. *Id.* at 1474.
96. *Id.* at 1475.
97. *Id.* at 1477.
98. 128 A.D.2d 218, 515 N.Y.S.2d 461 (1987).
99. 690 F. Supp. 1465 (D. Md. 1988). Here, the plaintiffs were sophisticated investors who negligently invested, and were denied recovery under Maryland's contributory negligence law.

99% by his own negligence and 1% by an accountant's may recoup the entire 100% of the loss from the accountant. Thus, the goal of compensating victims would undoubtedly be achieved, but only by abandoning any notion of fairness. Commenting on this notion, the court in *Delmar Vineyard v. Timmons*[100] stated that "an accountant does not guarantee correct judgment, or even the best professional judgment, but merely reasonable care and competence."[101]

V. Conclusion

Utah's comparative negligence statute should be applied in accounting malpractice cases, even though the damages are pecuniary in nature. Such application should not be limited by the *National Surety* rule to situations in which a plaintiff has interfered with the accountant's ability to perform his duty. The current trend in the law is away from the *National Surety* rule, which trend is supported by the public policy objectives of tort law. Moreover, application of comparative negligence furthers the goals of fairness, deterrence, and compensation.

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100. 486 S.W.2d 914 (Tenn. Ct. App. 1972).

101. *Id.* at 920; *see also* Lincoln Grain v. Coopers & Lybrand, 216 Neb. 433, 442, 345 N.W.2d 300, 307 (1984) (adopting *National Surety* but noting that accountants are not guarantors).