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### The Citadel Falls?--Liability for Accountants in Negligence to Third Parties Absent Privity: Credit Alliance Corp. v. Arthur Andersen & Co.

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## COMMENTS

### THE CITADEL FALLS?—LIABILITY FOR ACCOUNTANTS IN NEGLIGENCE TO THIRD PARTIES ABSENT PRIVACY: *CREDIT ALLIANCE CORP. V. ARTHUR ANDERSEN & CO.*

Accountants generally have been insulated from liability to third parties for negligent misrepresentation absent proof of contractual privity between the injured party and the accountant.<sup>1</sup> Al-

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<sup>1</sup> See *Ultramares Corp. v. Touche*, 255 N.Y. 170, 179-89, 174 N.E. 441, 444-48 (1931). The requirement of privity was first established in *Winterbottom v. Wright*, 152 Eng. Rep. 402 (1842). In *Winterbottom*, a passenger injured in the collapse of a coach was denied recovery from the party who negligently failed to maintain the coach because no duty existed in the absence of contractual privity between the two. *Id.* at 403. The stated purpose of privity was to shield fledgling industries from potentially unlimited tort liability to the general public. See *id.* at 405; W. PROSSER & W. KEETON, HANDBOOK OF THE LAW OF TORTS § 93, at 668 (5th ed. 1984). Historically, absent a contractual relationship, the negligent party did not owe a duty of care to the injured party and, thus, the injured party could not recover in negligence for either personal or pecuniary injury. W. PROSSER & W. KEETON, *supra*, § 93, at 668. While lack of privity has long been abandoned as a bar to recovery for personal injuries, vestiges of the doctrine remain where relief for only economic harm is sought. See *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 389, 111 N.E. 1050, 1053 (1916); RESTATEMENT (SECOND) OF TORTS § 402A (1976); W. PROSSER & W. KEETON, *supra*, § 97, at 690, § 107, at 747. One such vestige is accountants' liability to non-privity third parties. W. PROSSER & W. KEETON, *supra*, § 107, at 746-47; see also *Ultramares*, 255 N.Y. at 179, 174 N.E. at 444 (permitting third parties to recover in negligence "may expose accountants to liability in an indeterminate amount for an indeterminate time to an indeterminate class"); *Candler v. Crane, Christmas & Co.*, [1951] 2 K.B. 164, 169 (accountants owe no duty of care absent contractual privity). The continued application of the privity requirement to accountant negligence cases may be attributed to the unique position of accountants in the business community as producers of financial information that is distributed to an enormous and varied group of potential users. See Comment, *Auditor's Third Party Liability: An Ill-Considered Extension of the Law*, 46 WASH. L. REV. 675, 680-81 & n.30 (1971) (accounting firms exposed to widespread liability due to number of people likely to rely on auditor's opinion and amount of revenue involved) (quoting Note, *Potential Liability of Accountants to Third Parties for Negligence*, 41 ST. JOHN'S L. REV. 588, 597 (1967)).

Until the late 1960's, parties lacking privity were reluctant to bring negligence actions against auditors presumably because there was little authority to support their claims. See Besser, *Privity—An Obsolete Approach to the Liability of Accountants to Third Parties*, 7

though plaintiffs have successfully predicated recovery from accountants on fraud,<sup>2</sup> liability for auditors' negligence remains the final bastion in "the assault upon the citadel of privity . . ."<sup>3</sup> De-

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SETON HALL L. REV. 507, 507 n.2, 517-18 & n.39 (1976) (citing Wall St. J., Nov. 15, 1966, at 1, col. 6, at 13, col. 2) (figures showing small number of suits against accountants). Thus, not only did few opportunities arise for the judiciary to question the reasoning behind the privity requirement, but also, because of the great deference given to Chief Judge Cardozo, the author of the opinion in *Ultramares*, few courts actually questioned the doctrine. See Wiener, *Common Law Liability of the Certified Public Accountant for Negligent Misrepresentation*, 20 SAN DIEGO L. REV. 233, 236 & n.9 (1983).

<sup>2</sup> See, e.g., *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 207 (1976) (federal securities law subjects accountants to liability for fraud based on "willing, knowing, or purposeful conduct"); *Herzfeld v. Laventhol, Krekstein, Horwath & Horwath*, 378 F. Supp. 112, 131 (S.D.N.Y. 1974) (accountants owe common-law duty to third parties to act without fraud in the preparation of financial statements), *aff'd in part and rev'd in part*, 540 F.2d 27 (2d Cir. 1976); *Fidelity & Deposit Co. v. Atherton*, 47 N.M. 443, 449, 144 P.2d 157, 161 (1943) (accountants who knew or should have known their employer intended to display financial statements to third persons owe those third persons duty not to act fraudulently); see also *Ultramares*, 255 N.Y. at 189-93, 174 N.E. at 448-50 (discussion of accountants' liability for fraud). See generally *Symposium on Accounting and the Federal Securities Laws*, 28 VAND. L. REV. 1 (1975) (discussing potential aspects of accountants' liability).

Fraudulent representations by accountants generally are actionable without the establishment of privity. E.g., *Ultramares*, 255 N.Y. at 189, 174 N.E. at 448. Chief Judge Cardozo wrote that to escape liability for fraud, accountants must have a "sincere or genuine belief when they certif[y] to an opinion that the balance sheet faithfully reflect[s] the condition of the business . . ." *Id.* at 193, 174 N.E. at 450. Chief Judge Cardozo stated that although even gross negligence alone was not enough to create liability, a jury may be able to infer fraud from negligent conduct. *Id.* at 190-91, 174 N.E. at 449; see also *State St. Trust Co. v. Ernst*, 278 N.Y. 104, 112, 15 N.E.2d 416, 419 (1938) ("[a] refusal to see the obvious, a failure to investigate the doubtful, if sufficiently gross, may furnish evidence leading to an inference of fraud").

Through the Securities and Exchange Act of 1934, ch. 404, § 1, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-78kk (1982)) (the Act), Congress attempted to promulgate standards of conduct for participants in the securities markets to prevent repetition of the chaos of the early 1930's. See Vernava, *Responsibility of the Accountant Under the Federal Securities Exchange Act of 1934*, 6 J. CORP. L. 317, 318 (1981). Investors relying on intentionally or knowingly misleading statements to their detriment may employ § 10(b) of the Act, 15 U.S.C. § 78j(b) (1982), in conjunction with Rule 10b-5, 17 C.F.R. § 240.10b-5 (1984), to recover for such statements from accountants. Vernava, *supra*, at 321-23. However, the Supreme Court has held that under § 10(b) and rule 10b-5, accountants must have acted with scienter; thus, mere negligence is not enough. See *Ernst & Ernst*, 425 U.S. at 199 (§ 10(b) requires "intentional or willful conduct designed to deceive or defraud investors").

<sup>3</sup> *Ultramares*, 255 N.Y. at 180, 174 N.E. at 444; see Recent Decision, 59 NOTRE DAME L. REV. 281, 295 (1983) (accountants' liability for negligence to third parties described as an anachronism). In products liability cases, the privity requirement has been dispensed with when the plaintiff asserts a claim for personal injury, see *Henningsen v. Bloomfield Motors, Inc.*, 32 N.J. 358, 372, 161 A.2d 69, 77 (1960); *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 389, 111 N.E. 1050, 1053 (1916); *Baxter v. Ford Motor Co.*, 168 Wash. 456, 463, 12 P.2d 409, 412 (1932), and, in many jurisdictions, privity no longer is a prerequisite to recovery for pecuniary loss, see *Peterson v. North Am. Plant Breeders*, 218 Neb. 258, 267, 354 N.W.2d 625, 631 (1984); *Hiles Co. v. Johnston Pump Co.*, 93 Nev. 73, 78-79, 560 P.2d 154, 157

spite repeated criticism by commentators disturbed by judicial refusal to apply the general negligence formula to accountant liability cases,<sup>4</sup> the privity requirement remains entrenched in many

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(1977); *Randy Knitwear, Inc. v. American Cyanamid Co.*, 11 N.Y.2d 5, 13, 181 N.E.2d 399, 402-03, 226 N.Y.S.2d 363, 368 (1962).

Similarly, in actions seeking to recover from professionals other than accountants, the privity requirement has begun to vanish. See Sanbar & Pataki, *Professional Liability: Malpractice of Attorneys, Accountants, Architects, and Engineers*, 3 OKLA. CITY L. REV. 689, 689-90 (1979). Originally, attorneys were held responsible only to parties in privity. *Savings Bank v. Ward*, 100 U.S. 195, 200 (1879); see Sanbar & Pataki, *supra*, at 699-700. However, the recent trend is to permit plaintiffs lacking a contractual relationship with the attorney to recover for their injuries. See *Fickett v. Superior Court*, 27 Ariz. App. 793, 794-95, 558 P.2d 988, 989-91 (1976); *Garcia v. Borelli*, 129 Cal. App. 3d 24, 32, 180 Cal. Rptr. 768, 772 (1982); *Needham v. Hamilton*, 459 A.2d 1060, 1062-63 (D.C. 1983). But see *Calamari v. Grace*, 98 App. Div. 2d 74, 77-79, 469 N.Y.S.2d 942, 944-45 (2d Dep't 1983) (New York requires privity of contract as element of cause of action for attorney malpractice). The liability of architects and engineers to third parties not in privity is more readily justifiable, because the negligence of these professionals often results in personal injury as well as pecuniary loss. See, e.g., *Nelson v. Union Wire Rope Corp.*, 31 Ill. 2d 69, 83-84, 199 N.E.2d 769, 778-81 (1964) (privity of contract not prerequisite to recovery when negligent engineering work resulted in collapse of construction hoist that killed seven people); see also Sanbar & Pataki, *supra*, at 710-11. In fact, some cases involving only economic harm have not required any showing of privity between the plaintiff and the defendant architect or engineer. Sanbar & Pataki, *supra*, at 710-11; see *Robert & Co. v. Rhodes-Haverty Partnership*, 250 Ga. 680, 681-82, 300 S.E.2d 503, 504 (1983); see also *Rozny v. Marnul*, 43 Ill. 2d 54, 59-62, 250 N.E.2d 656, 660-63 (1969) (surveyor liable to third parties for faulty survey).

<sup>4</sup> See Kelly, *An Overview of Accountants' Liability*, 15 FORUM 579, 582 (1980). Many commentators view privity as a crude and artificial restraint that arbitrarily forecloses foreseeable plaintiffs. See *id.*; Note, *Potential Liability of Accountants to Third Parties for Negligence*, 41 ST. JOHN'S L. REV. 588, 597 (1967); Recent Decision, *supra* note 3, at 295. But see Comment, *supra* note 1, at 707 (abrogation of privity doctrine will damage users and suppliers of capital, auditors, and channels of resource distribution).

Chief Justice Cardozo's opinion in *Ultramares* was heavily criticized by his contemporaries, see, e.g., Seavey, *Mr. Justice Cardozo and the Law of Torts*, 39 COLUM. L. REV. 20, 49 (1939), and this criticism continues among those modern commentators who believe that Chief Judge Cardozo's concern that accountants would be incapable of compensating those injured by negligently prepared financial statements is no longer an appropriate consideration, see, e.g., Besser, *supra* note 1, at 535-37; see also Note, *Accountants' Liability for Negligence—A Contemporary Approach for a Modern Profession*, 48 FORDHAM L. REV. 401, 401, 414-15 (1979) (accounting profession today is most capable of adequately distributing risk of making negligent misstatement to non-privy third party through professional malpractice insurance) [hereinafter cited as *Contemporary Approach*]. There is little economic justification for allowing auditors to escape traditional negligence liability since the present-day accounting industry is fiscally sound. See 43 Facts on File 366, col. 2, May 20, 1983; see also Wiener, *supra* note 1, at 236 n.10 (noting economic maturation of accounting industry).

The changing function of accountants in modern business presents another compelling argument for the imposition of liability on accountants without privity. See *infra* note 51. Today, commercial and private investors use financial statements to evaluate business opportunities, see *Contemporary Approach, supra*, at 414, and federal securities laws require filings and distribution of such statements to stockholders, see Securities Act of 1933, § 7, schedule A & B, 15 U.S.C. §§ 77g, 77aa (1982).

jurisdictions.<sup>5</sup> Recently, however, in *Credit Alliance Corp. v. Arthur Andersen & Co.*,<sup>6</sup> the Appellate Division, First Department, while holding that a party without privity can recover from auditors provided he is within a limited class of foreseen users,<sup>7</sup> suggested, in dictum, that auditors' liability be extended to all foreseeable users of negligently prepared financial statements.<sup>8</sup>

In *Credit Alliance*, the plaintiffs, Credit Alliance Corp. (Credit Alliance) and Leasing Services Corp. (Leasing Services), had extended limited financing to L.B. Smith, Inc. (Smith) through the purchase of chattel paper.<sup>9</sup> Subsequently, in alleged reliance upon Smith's financial statements prepared by the defendant, Arthur Andersen & Company (Arthur Andersen), Credit Alliance and Leasing Services greatly increased the amount of credit extended to Smith.<sup>10</sup> The financial statements, certified by Arthur Andersen

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A negligence cause of action traditionally consists of four elements: (1) the existence of a duty between the plaintiff and the defendant; (2) a failure to fulfill that duty adequately; (3) an injury to one who is owed the duty; and (4) a causal relationship between the failure of the duty and the resulting injury. *W. PROSSER & W. KEETON, supra* note 1, § 30, at 143; see *Frazier v. United States*, 481 F. Supp. 645, 646-47 (N.D. Cal. 1979); *Barr v. County of Albany*, 69 App. Div. 2d 914, 915, 415 N.Y.S.2d 471, 473 (3d Dep't 1979), *modified*, 50 N.Y.2d 247, 406 N.E.2d 481, 428 N.Y.S.2d 665 (1980). This four-pronged negligence test has seldom been fully applied in accountant's negligence cases because the lack of privity traditionally has prevented a non-privity plaintiff from establishing that a duty was owed to him by the defendant auditors. See, e.g., *Investment Corp. v. Buchman*, 208 So. 2d 291, 293-96 (Fla. Dist. Ct. App.) (negligence action against defendant properly dismissed without consideration by jury when no privity between defendant and plaintiff is pleaded), *cert. dismissed*, 216 So. 2d 748 (Fla. 1968); *MacNerland v. Barnes*, 129 Ga. App. 367, 370, 199 S.E.2d 564, 566 (1973) (summary judgment in favor of defendant auditors proper when no contractual duty exists between plaintiff and defendant). There are few cases in which all elements of a negligence cause of action have been applied to accountants, because even when privity does not bar recovery, settlements are often arranged. See *Wiener, supra* note 1, at 233 n.1.

<sup>5</sup> See, e.g., *Stephens Indus., Inc. v. Haskins & Sells*, 438 F.2d 357, 360 (10th Cir. 1971); *Investors Tax Sheltered Real Estate, Ltd. v. Laventhol, Krekstein, Horwath & Horwath*, 370 So. 2d 815, 817 (Fla. Dist. Ct. App. 1979), *cert. denied*, 381 So. 2d 767 (Fla. 1980); *Dworman v. Lee*, 83 App. Div. 2d 507, 507, 441 N.Y.S.2d 90, 90 (1st Dep't 1981), *aff'd*, 56 N.Y.2d 816, 438 N.E.2d 103, 452 N.Y.S.2d 570 (1982).

<sup>6</sup> 101 App. Div. 2d 231, 476 N.Y.S.2d 539 (1st Dep't 1984).

<sup>7</sup> *Id.* at 235-36, 476 N.Y.S.2d at 542.

<sup>8</sup> *Id.* at 238, 476 N.Y.S.2d at 543-44.

<sup>9</sup> *Id.* at 232, 476 N.Y.S.2d at 540. Credit Alliance and Leasing Services are associated organizations that provide financing for capital equipment through leasing programs and installment sales. *Id.* Smith, a seller and lessor of construction equipment, received financing through the assignment of its customers' obligations to the plaintiffs, while Smith remained contingently liable to the plaintiffs in the event of customer default. *Id.*

<sup>10</sup> *Id.* at 232-34, 476 N.Y.S.2d at 540-41. Credit Alliance and Leasing Services requested audited statements from Smith before complying with Smith's request to increase their financial commitment. *Id.* at 233, 476 N.Y.S.2d at 540-41. In the course of the financial relationship between Smith and the plaintiffs, Arthur Andersen prepared two sets of financial

as an accurate reflection of Smith's financial position,<sup>11</sup> portrayed Smith as a financially sound corporation.<sup>12</sup> Within two years of acquiring the increased financing from Credit Alliance and Leasing Services, however, Smith defaulted on its obligations to the plaintiffs and filed for bankruptcy.<sup>13</sup> Credit Alliance and Leasing Services brought suit against Arthur Andersen for losses resulting from reliance upon Arthur Andersen's alleged negligently prepared financial statements.<sup>14</sup> The Supreme Court, Special Term, New York County, dismissed the plaintiffs' negligence claim as time-barred,<sup>15</sup> but subsequently reinstated the claim on rehear-

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statements on behalf of Smith. *Id.* at 234, 476 N.Y.S.2d at 541. The first set of financial statements reflected Smith's financial position as of December 31, 1977 (1977 statements). *See id.* at 233, 476 N.Y.S.2d at 541. Allegedly relying on the 1977 statements, the plaintiffs significantly increased their financing to Smith. *Id.*

In 1979, the plaintiffs asked Smith for updated financial statements as a prerequisite to the continuation of the financing arrangement. *Id.* Smith provided the plaintiffs with financial statements prepared by Arthur Andersen that reflected Smith's position as of February 28, 1979 (1979 statements). *Id.* In alleged reliance upon the 1979 statements, Credit Alliance and Leasing Services continued their financial relationship with Smith. *Id.*

<sup>11</sup> *Id.* at 234, 476 N.Y.S.2d at 541. Arthur Andersen issued an auditor's report with both the 1977 statements and the 1979 statements. Record on Appeal at 38, 50, *Credit Alliance Corp. v. Arthur Andersen & Co.*, 101 App. Div. 2d 231, 476 N.Y.S.2d 539 (1st Dep't 1984) [hereinafter cited as Record on Appeal]. Both reports contained the unqualified opinion of Arthur Andersen that Smith's financial status was accurately reflected by the statements. Record on Appeal, *supra*, at 38, 50. The type of opinion issued by an auditor depends upon the compliance of the audit with generally accepted auditing standards (GAAS) and upon the conformity of the audited party's financial statements with generally accepted accounting principles (GAAP), as promulgated by the American Institute of Certified Public Accountants (auditing standards) and the Financial Accounting Standards Board (accounting principles). *See* D. TAYLOR & G. GLEZEN, *AUDITING: INTEGRATED CONCEPTS AND PROCEDURES* 18-20 (2d ed. 1982). An unqualified opinion indicates full compliance with both GAAS and GAAP. *Id.* at 19. The three other types of opinions—qualified, disclaimer, and adverse—are used to indicate varying levels of non-conformity with GAAS or GAAP. *Id.*

<sup>12</sup> Record on Appeal, *supra* note 11, at 38-60.

<sup>13</sup> *Credit Alliance*, 101 App. Div. 2d at 233, 476 N.Y.S.2d at 541. At the time Smith filed its bankruptcy petition, it was indebted to Credit Alliance for more than \$7.9 million, and to Leasing Services for nearly \$1 million. *Id.* at 233-34, 476 N.Y.S.2d at 541.

<sup>14</sup> *Id.* at 234, 476 N.Y.S.2d at 541.

<sup>15</sup> *See Credit Alliance Corp. v. Arthur Andersen & Co.*, 122 Misc. 2d 1045, 1046, 471 N.Y.S.2d 938, 939 (Sup. Ct. N.Y. County 1983) (referring to prior unreported decision), *aff'd*, 101 App. Div. 2d 231, 476 N.Y.S.2d 539 (1st Dep't 1984). Arthur Andersen contended that the complaint did not state a cause of action for negligence, and asserted that any negligence action was barred by the statute of limitations. *Credit Alliance*, 122 Misc. 2d at 1046, 471 N.Y.S.2d at 939. Concluding that the negligence claim was time-barred, the trial court agreed with Arthur Andersen's contention that a claim for alleged professional negligence accrues upon completion of the disputed work. *Id.* at 1046, 471 N.Y.S.2d at 939; *see Sosnow v. Paul*, 43 App. Div. 2d 978, 979, 352 N.Y.S.2d 502, 504 (2d Dep't 1974), *aff'd*, 36 N.Y.2d 780, 330 N.E.2d 643, 369 N.Y.S.2d 693 (1975). Notwithstanding the operation of the statute of limitations, the trial court stated that the "plaintiffs were in the limited class of

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The Appellate Division affirmed the reinstatement, finding that the plaintiffs were members of a limited class of foreseen users who might have detrimentally relied on Smith's financial statements and, as such, were owed a duty of care by the defendants.<sup>17</sup> Writing for the majority, Judge Ross reiterated the long-standing rule of *Ultramares Corp. v. Touche*<sup>18</sup> that accountants are not liable for negligently prepared financial statements absent proof of contractual privity.<sup>19</sup> However, Judge Ross determined

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financiers whose reliance on [Andersen's] financial reports was foreseeable. Plaintiffs were thus owed a duty of care by Andersen." *Credit Alliance*, 122 Misc. 2d at 1046-47, 471 N.Y.S.2d at 939-40.

Additionally, Credit Alliance and Leasing Services alleged that Arthur Andersen committed fraud in the preparation of the Smith financial statements. *Id.* The trial court refused to grant the defendant's motion to dismiss the fraud count for lack of particularity in the pleading. *Id.*

<sup>16</sup> *Credit Alliance*, 122 Misc. 2d at 1045, 471 N.Y.S.2d at 938. The court determined that, since no contractual agreement existed between the plaintiffs and the defendant, the plaintiffs' action was not one for professional malpractice, and should be governed by the 3-year statute of limitations applied for garden variety negligence. *See id.* at 1049, 471 N.Y.S.2d at 941. The court looked to *White v. Guarente*, 43 N.Y.2d 356, 372 N.E.2d 315, 401 N.Y.S.2d 474 (1977), to support the proposition that the plaintiffs, members of a known class of users of financial information, could not detrimentally rely on that information until the financial statements actually were received. *See Credit Alliance*, 122 Misc. 2d at 1047, 471 N.Y.S.2d at 941. Thus, the trial court concluded that the plaintiffs' cause of action accrued upon receipt of the financial statements. *Id.*

<sup>17</sup> *Credit Alliance*, 101 App. Div. 2d at 235-36, 476 N.Y.S.2d at 542. Addressing the statute of limitations issue, the Appellate Division agreed with the determinations of the trial court that the plaintiffs' action was grounded in ordinary negligence, and thus was not time-barred. *Id.* at 236-37, 476 N.Y.S.2d at 543. The lower court's ruling on the fraud claim was unanimously affirmed without discussion. *Id.* at 232, 476 N.Y.S.2d at 540.

<sup>18</sup> 255 N.Y. 170, 174 N.E. 441 (1931).

<sup>19</sup> *Credit Alliance*, 101 App. Div. 2d at 235, 476 N.Y.S.2d at 542. In *Ultramares*, the defendant public accounting firm was engaged by Fred Stern & Co. (Stern) to prepare and certify financial statements. *Id.* at 173, 174 N.E. at 442. The defendant knew that Stern required substantial outside financing and that Stern would exhibit the financial statements to potential funding sources such as banks and stockholders. *Id.* While the statements and the auditor's report certified that Stern was in good financial condition, *id.* at 174, 174 N.E. at 442, Stern was actually insolvent, *id.* at 175, 174 N.E. at 442.

*Ultramares*, claiming reliance upon the balance sheets prepared by Touche in extending financing to Stern, sued the accountants in both negligence and fraud. *Id.* at 175-76, 174 N.E. at 443. Chief Judge Cardozo, writing for a unanimous Court of Appeals, held that public accountants are not liable for the negligent preparation of financial statements in the absence of privity of contract. *See id.* at 179-89, 174 N.E. at 444-48. The court expressed fear that the accounting profession could not survive if its smallest errors were actionable by all potential creditors and investors that received and relied upon financial statements. *See id.* at 179, 174 N.E. at 444. Chief Judge Cardozo determined that only the legislature had authority to impose such immense liability on the accounting profession. *See id.* at 187, 174 N.E. at 447.

that the facts in *Credit Alliance* fell within the narrow exception to the privity requirement recognized by the New York Court of Appeals in *White v. Guarente*,<sup>20</sup> which allowed a limited, foreseen class of plaintiffs to recover for detrimental reliance upon negligently prepared statements by independent auditors.<sup>21</sup> Based upon the presence of certain information in the financial statements, Judge Ross determined that Arthur Andersen foresaw the plaintiffs' reliance on those statements.<sup>22</sup>

In dictum, the court suggested abandoning the privity requirement and holding accountants liable to all foreseeable—as distinguished from merely foreseen—plaintiffs.<sup>23</sup> Advocating the excision of the privity rule from accountants' negligence cases, Judge Ross cited the accounting profession's development of self-regulatory guidelines that recognize a degree of responsibility to the general public.<sup>24</sup> The majority also observed that the federal securities laws impose liability on accountants to third parties even in the absence of privity.<sup>25</sup> Finally, Judge Ross noted that a recent United States

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<sup>20</sup> 43 N.Y.2d 356, 372 N.E.2d 315, 401 N.Y.S.2d 474 (1977).

<sup>21</sup> *Credit Alliance*, 101 App. Div. 2d at 235, 401 N.Y.S.2d at 542. In *White*, auditors were retained by a limited partnership to perform auditing and tax services pursuant to a specific provision in the partnership agreement. 43 N.Y.2d at 359, 372 N.E.2d at 317, 401 N.Y.S.2d at 476. The auditors were sued for negligently failing to disclose that several partners had withdrawn partnership funds in violation of the partnership agreement. *Id.* at 360, 372 N.E.2d at 317-18, 401 N.Y.S.2d at 477. The majority concluded that the auditors owed a duty to audit carefully to the plaintiffs, the limited partners, because the auditors knew or should have known that the limited partners would use the partnership statements in preparing their personal tax returns. *See id.* at 361-62, 372 N.E.2d at 318-19, 401 N.Y.S.2d at 477-78. The court charged the auditors with this knowledge because the uses and users of the statements were specified in the partnership agreement that the auditors had examined prior to performing the audit. *See id.* at 361, 372 N.E.2d at 318-19, 401 N.Y.S.2d at 477. The *White* court distinguished *Ultramares* by noting that "the services of the accountant were not extended to a faceless or unresolved class of persons, but rather to a known group possessed of vested rights, marked by a definable limit and made up of certain components." *See id.*

<sup>22</sup> *See Credit Alliance*, 101 App. Div. 2d at 234-35, 476 N.Y.S.2d at 542 (quoting from Record on Appeal, *supra* note 11, at 59). The *Credit Alliance* court noted that a footnote to the financial statements explained Smith's contingent liability to outside financial institutions. *See* 101 App. Div. 2d at 234-35, 476 N.Y.S.2d at 542. Additionally, the court noted that Arthur Andersen did not contest the plaintiffs' assertion that few companies could provide the type of financing used by Smith. *See id.*; *see also id.* at 233, 476 N.Y.S.2d at 540-41 (company president's affidavit stated less than eight companies capable of satisfying Smith's financial need).

<sup>23</sup> 101 App. Div. 2d at 237-38, 476 N.Y.S.2d at 543-44 (dictum).

<sup>24</sup> *Id.* at 237, 476 N.Y.S.2d at 543.

<sup>25</sup> *Id.*; *see also supra* note 2 (discussion of accountants' liability under federal securities laws).



Supreme Court opinion suggested that accountants be responsive to their role as "public watchdog[s]" in the preparation of financial reports.<sup>26</sup>

Acknowledging the existence of the *White* exception,<sup>27</sup> Judge Milonas nevertheless dissented, stressing the continued validity of the privity rule.<sup>28</sup> The dissent noted that *White* extended accountant liability to include only the individual, existing partners of a limited partnership that had contracted with the defendant accountants, and thus constituted only a minor retreat from the privity doctrine.<sup>29</sup> Judge Milonas declared that the plaintiffs in *Credit Alliance* could not be among the intended beneficiaries of the auditor's report, because it was specifically directed to Smith's board members and stockholders.<sup>30</sup> Thus, the dissent factually distinguished *White* and found no basis for the majority's refusal to apply the privity doctrine and dismiss the negligence action against Arthur Andersen.<sup>31</sup>

The *Credit Alliance* court has attempted to persuade the Court of Appeals through dictum that accountants should owe a general duty of care to third parties despite the absence of any

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<sup>26</sup> *Credit Alliance*, 101 App. Div. 2d at 238, 476 N.Y.S.2d at 544 (quoting *United States v. Arthur Young & Co.*, 104 S. Ct. 1495, 1503 (1984)). In *Arthur Young*, the Internal Revenue Service (IRS), while performing an audit, sought the tax accrual workpapers prepared by the defendant public accountants for a client. 104 S. Ct. at 1498. Attempting to resolve a conflict between the accountant-client privilege and certain visitorial provisions of the Internal Revenue Code, the Court concluded that the tax code provisions relating to IRS investigations provided substantial justification for overcoming the privilege. *See id.* at 1502-03. In reaching this conclusion, the Court acknowledged the public responsibility of accountants. *See id.* at 1503. The Supreme Court's recognition that financial statements are prepared for distribution to a wide variety of investors and creditors, *see id.*, was interpreted by the *Credit Alliance* majority as supportive of increased liability of accountants to those relying on their work, *see Credit Alliance*, 101 App. Div. 2d at 237, 476 N.Y.S.2d at 543 (dictum).

<sup>27</sup> *Credit Alliance*, 101 App. Div. 2d at 240-41, 476 N.Y.S.2d at 545 (Milonas, J., dissenting).

<sup>28</sup> *Id.* at 240-41, 476 N.Y.S.2d at 545-46 (Milonas, J., dissenting). The dissent cited *Dworman v. Lee*, 83 App. Div. 2d 507, 507, 441 N.Y.S.2d 90, 91 (1st Dep't 1981), *aff'd*, 56 N.Y.2d 816, 438 N.E.2d 103, 452 N.Y.S.2d 570 (1982), which stated that "there can be no doubt that the rule in *Ultramares* remains authoritative . . ." *Credit Alliance* 101 App. Div. 2d at 241, 476 N.Y.S.2d at 546 (Milonas, J., dissenting).

<sup>29</sup> *Credit Alliance*, 101 App. Div. 2d at 240-41, 476 N.Y.S.2d at 545 (Milonas, J., dissenting); *see White v. Guarente*, 43 N.Y.2d at 362-63, 372 N.E.2d at 319, 401 N.Y.S.2d at 478.

<sup>30</sup> *Credit Alliance*, 101 App. Div. 2d at 241, 476 N.Y.S.2d at 545 (Milonas, J., dissenting); *see Record on Appeal*, *supra* note 11, at 38, 50 (auditor's reports for 1977 and 1979 statements).

<sup>31</sup> *Credit Alliance*, 101 App. Div. 2d at 241-42, 476 N.Y.S.2d at 546 (Milonas, J., dissenting).

contractual relationship. It is submitted, however, that the court failed to support adequately and logically the extension of auditors' liability. This Comment will suggest a more complete consideration of the grounds supporting the disposal of the privity doctrine by using reasoning similar to that used in excising the privity barrier from the law of products liability. Unlike products liability, however, which has become synonymous with strict liability,<sup>32</sup> it will be suggested that accountants' liability should be based upon the traditional negligence formula.

#### LIABILITY TO A FORESEEN CLASS—AN APPROPRIATE FIRST STEP

The majority in *Credit Alliance*, while attempting to influence the Court of Appeals to extend the scope of accountants' liability,<sup>33</sup> recognized the necessity of remaining within the precedent set by *Ultramares* and *White*.<sup>34</sup> Judge Ross equated the known, limited class of creditors in *Credit Alliance* with the known class of limited partners in *White*,<sup>35</sup> since neither the limited partners in *White* nor the limited class of financiers in *Credit Alliance* enjoyed any direct contractual relationship with the auditors.<sup>36</sup> It is submitted that the *Credit Alliance* court's determination of the applicability of the *White* exception is consistent with precedent and comports with underlying policy.<sup>37</sup>

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<sup>32</sup> See W. PROSSER & W. KEETON, *supra* note 1, § 98; see also Henderson, *Extending the Boundaries of Strict Products Liability: Implications of the Theory of the Second Best*, 128 U. PA. L. REV. 1036, 1042 & n.26 (1980) (strict liability universally applied in cases involving physical harm, but less absolute in areas of pecuniary loss); cf. Schwartz, *The Vitality of Negligence and the Ethics of Strict Liability*, 15 GA. L. REV. 963, 965-77 (1981) (although strict liability has not definitely established itself as successor to negligence, the possibility does exist).

<sup>33</sup> See *Credit Alliance*, 101 App. Div. 2d at 237-38, 476 N.Y.S.2d at 543-44.

<sup>34</sup> *Id.* at 235-37, 476 N.Y.S.2d at 542-43; see *White*, 43 N.Y.2d at 361-62, 372 N.E.2d at 318-19, 401 N.Y.S.2d at 477-78; *Ultramares*, 255 N.Y. at 189, 174 N.E. at 448.

<sup>35</sup> *Credit Alliance*, 101 App. Div. 2d at 235-36, 476 N.Y.S.2d at 542.

<sup>36</sup> See *White*, 43 N.Y.2d at 359, 372 N.E.2d at 317, 401 N.Y.S.2d at 476; *Credit Alliance*, 101 App. Div. 2d at 234, 476 N.Y.S.2d at 541.

<sup>37</sup> See RESTATEMENT (SECOND) OF TORTS § 552 (1976). The Restatement (Second) of Torts provides that:

[o]ne who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information . . . [provided the loss is] suffered . . . 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 . . .

Significant policy reasons support the extension of accountants' liability to all foreseen users of financial statements.<sup>38</sup> Financial statements are often used to persuade existing investors, creditors, and customers of a given company to maintain and further business relationships.<sup>39</sup> It is submitted that the knowledge of a company of the need for financial information by foreseen third parties compels the company to seek the expertise of public accountants to ensure that accurate information is provided. Thus, auditors receive the benefit of increased billing from their clients' known business relationships. In privity, the fees an accountant charges are the basis of the duty of care owed by the auditor to his clients.<sup>40</sup> It is suggested, therefore, that when a known class of users is involved, the fact that the client alone remunerates its auditor should not determine the duty of care that the auditor must heed regarding that foreseen, limited class of third parties. Instead, the fact that a benefit was generated, although not paid, from a known source should be determinative.

Additional policy reasons exist for holding accountants liable for harm caused to foreseen third parties. The improved reporting techniques that have developed since the *Ultramares* decision can be used in responding to the needs of a known class of users of financial statements to limit the incidence of negligence for which

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*Id.* § 552 (emphasis added). The *Credit Alliance* court's analysis of the duty owed by Arthur Andersen comports directly with the Restatement approach. Compare *Credit Alliance*, 101 App. Div. 2d at 236, 476 N.Y.S.2d at 542 with RESTATEMENT (SECOND) OF TORTS § 552 (1976).

Some jurisdictions have expressly adopted § 552 of the Restatement in cases of accountants' negligence. *E.g.*, *Rhode Island Hosp. Trust Nat'l Bank v. Swartz, Bresenoff, Yavner & Jacobs*, 455 F.2d 847, 851 (4th Cir. 1972) (accountants liable to bank they know to be relying on statements for guidance in evaluating loan applicant); *Ingram Indus., Inc. v. Nowicki*, 527 F. Supp. 683, 684 (E.D. Ky. 1981) (auditors' liability to third parties based on Restatement, rather than Chief Judge Cardozo's restrictive standards); *Seedkem, Inc. v. Saffranek*, 466 F. Supp. 340, 342-44 (D. Neb. 1979) (accountants potentially liable to known option holder who makes loan on basis of negligently audited financial statements).

<sup>38</sup> See *infra* notes 39-44; cf. *Credit Alliance*, 101 App. Div. 2d at 237, 476 N.Y.S.2d at 543 (development of self-regulatory guidelines in the accounting profession supports extension of liability).

<sup>39</sup> See L. BERNSTEIN, UNDERSTANDING CORPORATE REPORTS: A GUIDE TO FINANCIAL STATEMENT ANALYSIS 572 (1974) (bank loan officer, insurance company, and investors—all potential financial statement users—require analysis of financial statements before entering into any arrangement with audited company); J. MYER, FINANCIAL STATEMENT ANALYSIS 5 (4th ed. 1969) (original use of financial statements was for bank's determination of credit worthiness of potential borrower).

<sup>40</sup> See W. RICH, LEGAL RESPONSIBILITIES AND RIGHTS OF PUBLIC ACCOUNTANTS 13 (1980) (auditor's responsibility to client based in contract).

those users can recover.<sup>41</sup> Further, the common-law notion of placing the risk of loss on the party best able to withstand the burden should be considered.<sup>42</sup> Today, the accounting profession certainly occupies a sufficiently strong financial position to bear the risk of loss better than non-privy foreseen parties.<sup>43</sup> These policy reasons all strongly support the removal of the privity doctrine to permit at least a foreseen, limited class of reliant third parties to recover for injuries caused by an auditor's negligent preparation of financial statements.<sup>44</sup> Nevertheless, it is suggested that these same policy reasons support an imposition of liability on accountants for injuries to all who might foreseeably rely on negligently prepared financial statements.

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<sup>41</sup> See D. CAUSEY, DUTIES AND LIABILITIES OF PUBLIC ACCOUNTANTS 19-22 (1979) (general dissatisfaction with practices in profession before and during Depression led to widespread reform and more stringent auditing and reporting practices); Flynn, *Corporate Reporting and Accounting Principles: The Viewpoint of an Independent Accountant*, in CORPORATE FINANCIAL REPORTING: CONFLICTS AND CHALLENGES 140-41 (J. Burton ed. 1969) (reporting techniques and standards of accounting profession "hav[e] come a long way"). Indeed, the profession has acknowledged an awareness of the needs of various non-privy users of financial statements. See FINANCIAL ACCOUNTING STANDARDS BOARD, STATEMENT OF FINANCIAL ACCOUNTING CONCEPTS No. 1—OBJECTIVES OF FINANCIAL REPORTING BY BUSINESS ENTERPRISES ¶ 24 (1978); see also *Credit Alliance*, 101 App. Div. 2d at 237, 476 N.Y.S.2d at 543; *infra* note 51. Since the profession has acknowledged a duty to act carefully in response to the expectations of known third-party users of financial statements, see *infra* note 51, it must be presumed that accountants know what such persons expect from financial statements.

<sup>42</sup> See W. PROSSER & W. KEETON, *supra* note 1, § 4, at 24-25. The risks involved in preparing an opinion on financial statements can be absorbed by accountants and distributed among clients in the form of increased fees. See *id.*; Wiener, *supra* note 1, at 252-53.

<sup>43</sup> See *supra* note 4. It is estimated that the top eight accounting firms alone grossed in excess of 6 billion dollars in 1982. See 43 Facts on File 366, col. 2, May 20, 1983.

<sup>44</sup> See *Rusch Factors, Inc. v. Levin*, 284 F. Supp. 85, 91 (D.R.I. 1968). In *Rusch Factors*, a corporation applied for financing from the plaintiff commercial bank. *Id.* at 86. The certified statements requested by the plaintiff portrayed a healthy financial picture of the corporation, while in reality the corporation was insolvent. *Id.* The plaintiff, relying on these statements prepared by the defendant auditor, decided to extend the loan to the corporation. *Id.* at 86-87. Holding that the plaintiffs are owed a duty by the defendant, the court determined that questions regarding the burden of financial loss should be resolved in favor of the "innocent reliant party," *id.* at 91, and suggested that the imposition of liability would compel the profession to take greater care in conducting itself toward the public, *id.* In addition, the *Rusch Factors* court found that the accountant is better equipped to shoulder the risk of loss by increasing its cost to the public, *id.*; see *supra* notes 42-43 and accompanying text; see also Gormley, *The Foreseen, the Foreseeable, and Beyond—Accountants' Liability to Nonclients*, 14 SETON HALL L. REV. 528, 540 (1984) (*Rusch Factors* was first federal case seriously to question *Ultramares*).

RECOVERY AGAINST ACCOUNTANTS FOR FORESEEABLE  
RELIANCE—THE PROPER STANDARD

Although commentators have called for the total excision of privity from the area of accountant negligence,<sup>45</sup> many jurisdictions still retain some aspects of the doctrine.<sup>46</sup> In *H. Rosenblum, Inc. v. Adler*,<sup>47</sup> however, the Supreme Court of New Jersey became one of the first courts to eliminate privity completely as a barrier to third-party recovery for the negligent misstatements of accountants.<sup>48</sup> The *Rosenblum* court analogized accountants' liability to products liability, in which the injury resulting from negligent misrepresentations accompanying the sale of goods generally is actionable without regard to privity.<sup>49</sup> In both areas of law, the defen-

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<sup>45</sup> See Kelly, *supra* note 4, at 582; Wiener, *supra* note 1, at 260; Note, *supra* note 4, at 597. Even the foreseen plaintiff standard has been criticized as protecting "powerful and sophisticated lenders, businesses and institutions whose personnel and counsel would make certain that the auditor foresaw their reliance and knew of their transaction . . ." R. GORMLEY, *THE LAW OF ACCOUNTANTS AND AUDITORS—RIGHTS, DUTIES AND LIABILITIES* ¶ 6.01[4], at 6-17 (1981). As noted, the primary reason that privity has been adhered to is the great deference paid to precedent. See, e.g., *Credit Alliance*, 101 App. Div. 2d at 242, 476 N.Y.S.2d at 546 (Milonas, J., dissenting).

<sup>46</sup> See, e.g., *McLean v. Alexander*, 599 F.2d 1190, 1202 (3d Cir. 1979) *Investors Tax Sheltered Real Estate, Ltd. v. Laventhol, Krekstein, Horwath & Horwath*, 370 So. 2d 815, 817 (Fla. Dist. Ct. App. 1979), *cert. denied*, 381 So. 2d 767 (Fla. 1980); *MacNerland v. Barnes*, 129 Ga. App. 367, 370, 199 S.E.2d 564, 566 (1973); see also *Bunge Corp. v. Eide*, 372 F. Supp. 1058, 1063 (D.N.D. 1974) (unlimited class problem expressed in *Ultramares* and recognized by Restatement still exists).

<sup>47</sup> 93 N.J. 324, 461 A.2d 138 (1983).

<sup>48</sup> *Id.* at 353, 461 A.2d at 153; see Gormley, *supra* note 44, at 548-51. In *Rosenblum*, the defendant Touche Ross & Co. (Touche Ross), independent auditors, issued statements and unqualified opinions over the course of several years certifying the financial stability of Giant Stores (Giant). 93 N.J. at 329-30, 461 A.2d at 140-41. The plaintiff, H. Rosenblum, Inc. (Rosenblum), was approached by Giant and eventually agreed to a merger between the two, based largely upon the income stated on Giant's books at the end of the 1971 fiscal year. *Id.* at 330-31, 461 A.2d at 140-41. Touche Ross failed to discover and therefore failed to disclose on the applicable financial statements that Giant had improperly increased its asset base while decreasing its accounts payable liability. *Id.* at 331, 461 A.2d at 141. Eventually, Giant filed for bankruptcy, and Rosenblum was left with worthless shares of Giant stock. *Id.*

<sup>49</sup> 93 N.J. at 339-41, 461 A.2d at 145-47. Although the *Rosenblum* court based its analogy on New Jersey products liability cases, it is suggested that the jurisprudence of these decisions closely parallels that of products liability cases in New York. Tracing the development of the law of products liability, the court first considered the abrogation of the privity requirement when a negligent representation results in personal injury. *Id.* at 339-40, 461 A.2d at 146; see *Martin v. Bengue, Inc.*, 25 N.J. 359, 365-71, 136 A.2d 626, 629-32 (1959); *O'Donnell v. Asplundh Tree Expert Co.*, 13 N.J. 319, 331-36, 99 A.2d 577, 583-86 (1953). The *Rosenblum* court went on to discuss the removal of the distinction between personal injury and pecuniary harm in products liability cases. 93 N.J. at 340-41, 461 A.2d at 146; see *Santor v. A & M Karagheusian, Inc.*, 44 N.J. 52, 60, 207 A.2d 305, 310 (1965).

dant knows or has reason to know that the statements regarding his product or workproduct will be relied upon by parties other than those with whom he is in contractual privity.<sup>50</sup> Indeed, the accounting profession itself has acknowledged its responsibility to the general public.<sup>51</sup> In addition, accountants can better provide for the consequences of their errors through increased diligence and appropriate insurance than can those foreseeably relying on their errors.<sup>52</sup>

It is submitted that the best argument for extending auditors' liability to all foreseeable parties is that negligence actions against accountants are no different from any other type of negligence action, and, accordingly, should require proof of the same elements. Compensation for the purely economic harm generally alleged in suits against accountants is clearly within the reach of negligence law.<sup>53</sup> It is suggested that a "foreseeable plaintiff" approach frees

<sup>50</sup> 93 N.J. at 341-42, 461 A.2d at 146. The *Rosenblum* court concluded that in the area of products liability, since a claim of negligent misrepresentation is not barred for lack of privity, there is no basis on which to bar a claim of ordinary negligence for a similar lack of privity. *Id.* at 341, 461 A.2d at 147; see *Santor*, 44 N.J. at 60, 207 A.2d at 310; see also *Goldberg v. Kollsman Instrument Corp.*, 12 N.Y.2d 432, 436, 191 N.E.2d 81, 82, 240 N.Y.S.2d 592, 594 (1963).

<sup>51</sup> See FINANCIAL ACCOUNTING STANDARDS BOARD, *supra* note 4, ¶ 24. The Financial Accounting Standards Board has stated that:

[m]any people base economic decisions on their relationships to and knowledge about business enterprises and thus are potentially interested in the information provided by financial reporting. Among the potential users are owners, lenders, suppliers, potential investors and creditors, employees, management, directors, customers, financial analysts and advisors . . . and the public.

*Id.*; see *Rosenblum*, 93 N.J. at 343-47, 461 A.2d at 147-50; 2 AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS, AICPA PROFESSIONAL STANDARDS ET §§ 51.04, 101.01 (1981); Wiener, *supra* note 1, at 251. Accounting professional standards indicate that the objectives behind financial reporting "stem primarily from the informational needs of external users who lack the authority to prescribe the financial information they want from an enterprise and therefore must use the information that management communicates to them." FINANCIAL ACCOUNTING STANDARDS BOARD, *supra* note 41, ¶ 28.

<sup>52</sup> *Rosenblum*, 93 N.J. at 349-50 & n.11, 461 A.2d at 151 & n.11; see *Contemporary Approach*, *supra* note 4, at 415 & nn.81, 83; cf. Horan & Guerrini, *Accountants' Professional Liability: Insurance Issues*, 15 FORUM 516, 519-20 (1980) (accountants' liability insurance does not limit claims based on "dishonest, fraudulent, criminal, or malicious acts"). *But see* Gormley, *supra* note 44, at 572 (insurance policies, when available, are either too expensive or too limited in coverage to be valid argument for extension of auditor's negligence liability to third parties).

<sup>53</sup> *Rosenblum*, 93 N.J. at 344, 461 A.2d at 148; see *Mead Corp. v. Allendale Mutual Ins. Co.*, 465 F. Supp. 355, 357 (N.D. Ohio 1979) (Ohio law permits recovery of purely economic harm); *Randy Knitwear Co. v. American Cyanamid Co.*, 11 N.Y.2d 5, 12, 181 N.E.2d 399, 401, 226 N.Y.S.2d 366, 368 (1962) (recovery in products liability for economic harm permitted). *But see* *Alfred N. Koplin & Co. v. Chrysler Corp.*, 49 Ill. App. 3d 194, 199, 364 N.E.2d

the courts from having to apply the artifice of privity in an attempt to distinguish between arguably indistinguishable classes of plaintiffs that auditors may or may not have known were relying upon negligently prepared statements. In addition, the general negligence formula would protect accountants from unlimited liability and frivolous suits by allowing recovery only by those plaintiffs who prove actual reliance on the financial statements.<sup>54</sup> Therefore, it is suggested that the appropriate test for determining accountants' liability for their negligent misstatements should be the traditional negligence standard.<sup>55</sup>

### CONCLUSION

Although the much maligned privity doctrine seems to be fading to obscurity, the doctrine maintains a position of great importance in the area of accountants' liability. As indicated by the *Credit Alliance* court, however, there is a general judicial dissatis-

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100, 104 (1977) (economic harm not actionable in Illinois without accompanying physical harm).

<sup>54</sup> *Rosenblum*, 93 N.J. at 338-39, 350-51, 461 A.2d at 145, 152; see *Citizens State Bank v. Timm, Schmidt & Co.*, 113 Wis. 2d 376, 382, 335 N.W.2d 361, 366 (1983); *Wiener*, *supra* note 1, at 255; see also *Strong v. Strong*, 102 N.Y. 69, 74-75, 5 N.E. 799, 801 (1886) (if plaintiff would not have acted but for the representations, action will lie); *Agricultural Bond & Credit Corp. v. August Brandt Co.*, 204 Wis. 48, 54, 234 N.W. 369, 372 (1931) (well settled rule that one who acts in reliance upon negligent or fraudulent representation may recover against its maker); see also 2 J. DOOLEY, *MODERN TORT LAW* § 32.21, at 252 (1982).

<sup>55</sup> Particular caution must be exercised, it is submitted, when applying the general negligence standard, especially in light of the *Rosenblum* court's analogy to products liability. Strict liability has emerged as a replacement for the general negligence standard in products liability. See *Schwartz*, *supra* note 32, at 965-77; see also *Codling v. Paglia*, 32 N.Y.2d 330, 335, 298 N.E.2d 622, 625, 345 N.Y.S.2d 461, 463 (1973) (early application of strict liability to manufacturer's torts). It is submitted that an extension of that doctrine to accountants would promote the same overbroad and excessive liability that Chief Judge Cardozo tried to negate in *Ultramares*, and would afford no more protection to the public than would the foreseeable reliance standard. An imposition of strict liability would remove any need for a plaintiff to show that the defendant accountant actually violated the applicable standard of care. W. PROSSER & W. KEETON, *supra* note 1, § 107, at 711-12. Prosser notes that the number of cases generally has increased since the advent of strict liability. *Id.*; see also Note, *Drawing the Line on Strict Liability: A Proposal for Governing the Recovery of Economic Damages in Iowa*, 67 IOWA L. REV. 995, 1012-34 (1982); Comment, *Strict Liability Versus Negligence: An Economic Analysis of the Law of Libel*, 1981 B.Y.U. L. REV. 398-406.

In addition to facilitating meritless suits in which plaintiffs attack every possible "deep pocket," it is submitted that a strict liability approach would impede the vital flow of financial information from a company to investors, creditors, and customers. Were a strict liability standard to be imposed, it is suggested that accountants, to the extent permitted by federal and state law, would either charge exorbitant fees or avoid performing audit work and procedures in instances in which a high degree of uncertainty is involved.

faction with the strained justifications given for the continued use of the privity doctrine. Although forced by precedent to limit the duty of accountants to members of a foreseen class of reliant financial statement users, the *Credit Alliance* court advocated adoption of the foreseeable reliance doctrine. While both doctrines are supported by significant policy concerns, the foreseeable plaintiff approach is superior because it encompasses all the well developed aspects of negligence law and provides reference points upon which to base the development of credible standards of duty.<sup>56</sup> Therefore, it is submitted that the Court of Appeals should recognize the overwhelming policy and legal support for applying the foreseeable plaintiff standard and thus deliver the fatal blow upon the illogical and antediluvian privity doctrine.

*James B. Blaney*

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<sup>56</sup> Cf. *Biakanja v. Irving*, 49 Cal. 2d 647, 650-51, 320 P.2d 16, 19 (1958) (advocating a balancing test in professional liability); Fiflis, *Current Problems of Accountants' Responsibilities to Third Parties*, 28 VAND. L. REV. 31, 111-12 (1975) (flexible test similar to *Biakanja*). These somewhat different tests are not generally used, but provide another viewpoint on the accountant liability issue. See Fiflis, *supra*, at 111-12.