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CPAs in Massachusetts typically hear of the Massachusetts Consumer Protection Act (Chapter 93A) when their clients become embroiled in litigation and seek their assistance. A more in-depth understanding of the statute and its potentially draconian remedies usually comes only after the CPA becomes the direct target of a 93A claim.

Accountants and their firms are viewed as “deep pocket” defendants to clients, and even third parties, who are looking to recover losses for which they may have no other recourse. Chapter 93A is often a weapon of choice. It provides a plaintiff with an opportunity to recover not only his actual damages, but also attorney’s fees and costs. In some cases, this can amount to two or three times the actual damages suffered.

Part I of this article provides an overview of Chapter 93A and its use by litigants asserting professional liability claims against accountants. Part II of this article, to be published in the next issue of SumNews (Winter I), will discuss the process by which a Chapter 93A claim is asserted, and provide guidance on the steps an accountant should take when faced with such a claim.

93A in a Nutshell

With Chapter 93A, unfair methods of competition (and unfair or deceptive acts or practices) are deemed unlawful in the conduct of trade or commerce. Accountants are susceptible to claims under Chapter 93A because they — like lawyers, brokers and other professionals involved in financial services and commercial transactions — engaged in trade or commerce when performing services for clients. Whether the accountant is a sole practitioner or a large international accounting firm makes no difference.

Similarly, a Chapter 93A claim may be asserted by an individual seeking personal accounting services, a small or mid-size business, or a large multinational corporation. The statute is available to all.

Chapter 93A claims are almost always asserted in tandem with other claims, such as breach of contract, negligence and misrepresentation. Unlike those claims, however, the statute presents potentially greater exposure as it allows a successful plaintiff to recover reasonable attorney’s fees and costs. Legal expenses can add up quickly, especially when the allegations against the CPA are hotly contested. In addition, a court can award double or treble damages if the accountant’s 93A violation is deemed to have been willful or knowing.

To guard against liability under Chapter 93A, it is important for accounting professionals to understand what constitutes unfair or deceptive business practices and who can assert such a claim.

What is “Unfair or Deceptive?”

Chapter 93A does not define “unfair or deceptive” conduct, nor does the statute’s abundant case law provide a single, binding definition. What is considered unfair or deceptive depends on the circumstances of each case, and Massachusetts courts have provided some guidance. The answer depends, in part, on the identity of the plaintiff.
Massachusetts Legislation

Section 9 of the Act gives individual consumers the right to sue businesses for unfair or deceptive acts. Section 11 affords businesses the same right to sue each other for a violation. Thus, if an individual taxpayer decided to sue his CPA, he would almost always invoke Section 9. If the CPA’s client is a business, then the client would sue under Section 11.

Courts have employed different standards for the two sections when assessing unfair conduct. As the Supreme Judicial Court recognized, “one can easily imagine cases where an act might be unfair if practiced upon a commercial innocent yet would be common practice between two people engaged in business,” Spence v. Boston Edison Co., 390 Mass. 604, 616 (1983). In other words, courts interpret Chapter 93A as tolerating a somewhat higher level of “rough and tumble” conduct between businesses than between a business and a consumer.

In a business-to-business context, Massachusetts courts have said that a defendant’s conduct must be at least tangentially related to a common law, statutory or other established concept of unfairness. The alleged conduct must be immoral, unethical, oppressive or unscrupulous, and must cause substantial injury. The case-by-case basis inquiry focuses on the nature of challenged conduct, and the purpose and effect of that conduct.

To establish malpractice on the part of a CPA, a plaintiff must show that the accountant breached a duty owed to the plaintiff by failing to exercise the degree of care, skill and competence of the average qualified member of the profession under the circumstances. However, breaching a professional duty is not necessarily tantamount to violating Chapter 93A.

Reported 93A decisions involving accountants and other professionals seem to shed more light on conduct that does not violate 93A than on conduct that does. For example, a mere breach of contract or act of professional negligence by an accountant does not, by itself, rise to the level of a Chapter 93A violation. To be sure, breaching contracts and committing negligence may result in liability, but a heightened level of misconduct is required to expose an accountant to liability under 93A.

As the following cases illustrate, where that line is drawn is not always clear.

- Gross Negligence and the “Pooling of Interests”: One Superior Court decision suggests that gross negligence—essentially an indifference to a legal duty and utter forgetfulness of legal obligations so far as other persons may be affected—may violate Chapter 93A. In Farragut Mortgage Co., Inc., v. Arthur Andersen LLP, the plaintiff engaged an auditor to advise whether a proposed merger with another company would qualify for “pooling-of-interests” accounting treatment under the Generally Accepted Accounting Principles (GAAP). After looking at only one side of the merger deal, the auditor concluded that the merger would qualify for pooling treatment. When the SEC disagreed, Farragut sued the auditor, arguing that the auditor’s “gross indifference and conscious disregard of the potential pooling problems, which [the auditor] knew or should have known” constituted the kind of misconduct Chapter 93A is designed to redress. The judge held that a jury must determine whether the auditor’s conduct was unfair or deceptive under Chapter 93A.

- Misrepresentation and the Reasonable Assurance Opinion: Not surprisingly, intentional misrepresentation can serve as the basis for a 93A claim, but can a misrepresentation made as a result of negligence support a 93A claim? In extreme cases, yes. As the Massachusetts Appeals Court held, “while a negligent misrepresentation may be so extreme or egregious as to constitute a violation of G.L. c. 93A, a negligent act standing by itself does not give rise to a claim under c. 93A,” O’Connor v. Merrimack Mut. Fire Ins. Co., 73 Mass. App. Ct. 100, 101 (2003).

Negligent misrepresentation—a theory often employed by third-parties who lack a contractual relationship with a putative defendant—has a mixed record when used to support a 93A claim against an accountant.

For instance, in Young v. Deloitte & Touche, LLP, a bankruptcy trustee for a corporation, its shareholders and creditors sued the company’s former auditor for fraud, negligent misrepresentation and violations of Chapter 93A.

The auditor allegedly advised management of “significant deficiencies” in its internal controls and recommended corrective action year after year, but no such action was taken. Even though it was aware of the company’s ongoing deficient internal controls, the auditor continued to provide reasonable assurance that the company’s consolidated financial statements were free of material misstatements.

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Ruling on the auditor’s motion to dismiss, the Superior Court judge held that the auditor’s conduct could support the corporation’s 93A claim, but dismissed the creditors’ and shareholders’ 93A and negligent misrepresentation claims on other grounds.

While far from clear, those cases that have permitted a negligent misrepresentation theory to support a 93A claim have generally involved conduct more akin to the traditional intentional, deceptive and reckless variety, notwithstanding the use of the “negligence” label.

- **The Mistake and Cover-up:** In a 2010 case, an automobile dealership claimed that its accountant caused it to incur additional tax liabilities, interest and penalties by negligently failing to provide proper advice, and then attempting to cover-up the adverse consequences of that advice, *Haddad Motor Group v. Karp, Ackerman, Skalowski & Hogan, P.C., et al.* The dealership became liable for a built-in gains tax of approximately $135,000 when it closed out a “margin-against-the-box” transaction in February 1999, and converted from a Subchapter C corporation to a Subchapter S corporation a month later.

The dealership did not estimate its built-in gains tax liability and make its required quarterly tax payments to the IRS in 1999. The CPA asserted that the dealership understood its liability for the built-in gains tax and deliberately underpaid in order to conserve cash. The dealership, however, claimed that the accountant never advised it of the tax liability, or of the need to make quarterly installment payments.

The CPA advised the dealership to delay filing its 1999 tax return, reportedly because of an ongoing audit of its 1997 tax year. The extension form filed by the CPA, without explanation, omitted reference to the large built-in gains tax and reported a much smaller amount. The dealership eventually paid the built-in gains tax with interest and penalties.

The jury determined that the CPA was not negligent in advising its client to close the “margin-against-the-box” transaction and convert to a Subchapter S corporation a month later. The jury, however, found the CPA negligent for failing to advise the client to pay the resulting built-in-gains tax in quarterly installments.

*Continued on page 20*
Massachusetts Legislation

The judge who heard the Chapter 93A claim determined that the CPA's attempt to conceal the consequences of its earlier advice met the “rascality” standard for a Chapter 93A violation. According to the judge, the CPA knowingly concealed the adverse tax consequences of its earlier advice, and provided false information to the IRS. In addition to the penalties and interest awarded by the jury, the judge found the CPA liable for additional penalties assessed against the dealership and awarded the dealership treble damages under Chapter 93A.

Who can sue an accountant under Chapter 93A? Can a non-client sue an accountant under Chapter 93A? As with many legal questions, the answer is: it depends.

A commercial relationship must exist between the third-party and the accountant before triggering potential Chapter 93A liability. Audit engagements often lend themselves to such claims. Typically, a third-party, such as an investor or bank, alleges that it relied on its detriment on financial statements that misstated the financial condition of a company. If the company's financial statements were audited, the third party might seek to recover directly from the accountant that conducted the audit.

To recover from the accountant, the third-party must prove, among other things, actual knowledge on the part of accountants of the limited—(though unnamed) group of potential third-parties that would rely on the accountant's report — as well as actual knowledge of the particular financial transaction that such information was designed to influence. The accountant's actual knowledge is measured at the time the report is published.

Thus, accountants risk being sued by a third party if they publish audit reports knowing that a third-party may rely on the report to decide whether to invest in, extend credit to, or do business with the company. The more egregious the conduct, the more likely the lawsuit will include a 93A claim.

Conclusion

Accountants should have a basic understanding of Chapter 93A and the potentially high exposure that such claims can present. Receiving a demand letter or complaint alleging violations of Chapter 93A should not be cause for panic. It should, however, prompt you to immediately seek the advice of counsel. Part II of this article, to be published in the next issue of SumNews, will discuss the process by which 93A claims are asserted, and the pitfalls that can arise when an accountant doesn't deal with a Chapter 93A claim in an appropriate and timely manner.