

Accountants' Liability

# Get the Professional Advice You're Entitled To

BY LAURI CROCE, ESQ.

In September 2003, the California Court of Appeal issued an unpublished decision in the case, *Rancho Santa Fe Association v. Ernst & Young, LLP*, holding that the Association could hold its accountants liable for damages caused by the accountants' failure to offer unsolicited advice. (As mentioned in previous editions of this newsletter, an unpublished decision may not be cited as legal precedent, but it can nevertheless provide excellent insight into the workings of local judicial minds.)

The Rancho Santa Fe Association hired Ernst & Young beginning in the 1970's to audit the Association's annual financial statements and prepare its federal and state (income) tax returns. In 1998, the Association became aware (from a source other than Ernst & Young) that it was overpaying the County for property taxes by more than \$90,000 per year. The Association requested its accountants obtain a refund for the overpayments. The County Assessor refunded some \$190,000 for tax years 1995, 1996 and 1997, but refused to refund any

overpayments for years prior to 1995 on a statute of limitations grounds.

The Association sued Ernst & Young, alleging malpractice for not telling the Association it had a possible claim for a tax refund in the earlier years. One argument advanced by Ernst & Young to defend its actions was that the company had not been hired to give advice about property taxes. The Court of Appeal in San Diego strongly disagreed, stating:



"Importantly, a professional's standard of care may require advice with respect to matters which are beyond the terms of any formal retention and about which the client or patient has made no specific request for advice."

Citing cases applying to lawyers and doctors, the court explained that professionals (including accountants) are held to a higher standard with respect to their particular areas of expertise. If they wish to limit the scope of their professional duties, they must do so in writing signed by the client or patient which cautions that certain matters will not be investigated and that another professional should be consulted on such topics.

An interpretation giving the benefit of the doubt to Ernst & Young suggests that the accountants made the erroneous assumption that the Rancho Santa Fe Association was more sophisticated than it really was. A less flattering interpretation is that Ernst & Young failed to give the Association all of the professional advice to which it was entitled. This is an especially worrisome mistake when it comes to homeowners associations. All homeowners associations are governed by volunteer boards made up of ordinary



homeowners, some of whom might be accountants or doctors or lawyers, but most of whom are not. Hence, associations by definition must seek advice from all sorts of professionals, ranging from association managers to accountants to structural engineers. They rely upon both the professionals' expertise and the professionals' character. It is incumbent upon the professionals to deliver the services requested of them, which includes pointing out issues of which the client might not otherwise be aware. Ernst & Young should have asked about the property tax situation when reviewing the line items in the financial statements, or preparing the income tax returns, or both, or specifically advised that the Rancho Santa Fe Association should seek advice from another accounting firm regarding its property taxes. It is a simple lesson that Ernst & Young has been forced to learn the hard way. ■

*The A&K News is written to provide information and education, not legal advice. If you have legal questions or issues, consult a lawyer.*

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