

Levin v PriceWaterhouseCoopers, LLC

2001 NY Slip Op 30045(U)

November 21, 2001

Supreme Court, New York County

Docket Number: 0110886/2000

Judge: Helen E. Freedman

Republished from New York State Unified Court
System's E-Courts Service.

Search E-Courts (<http://www.nycourts.gov/ecourts>) for
any additional information on this case.

This opinion is uncorrected and not selected for official
publication.

SUPREME COURT OF THE STATE OF NEW YORK - NEW YORK COUNTY

PRESENT: HELEN E. FREEDMAN
Justice

PART 39

Neil Levin

INDEX NO. 110 886 / 00

MOTION DATE _____

MOTION SEQ. NO. 001

MOTION CAL. NO. _____

- v -

Price Waterhouse Coopers

The following papers, numbered 1 to _____ were read on this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause - Affidavits - Exhibits ...	_____
Answering Affidavits - Exhibits	_____
Replying Affidavits	_____

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion ~~is~~ is decided in accordance with accompanying memorandum decision.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE

Dated: 11/21/01

[Signature]

J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 39

..... x

NEIL D. LEVIN, Superintendent of Insurance
of the State of New York, as Liquidator of
HOME MUTUAL INSURANCE COMPANY
OF BINGHAMTON, NY and NEW YORK
MERCHANT BAKERS INSURANCE COMPANY,

Plaintiff,

Index No.: 110886/00

- against -

DECISION

PRICEWATERHOUSECOOPERS, LLP,
f/d/b/a/ Coopers & Lybrand, et al.,

.
:

Defendants.

-----x

HELEN FREEDMAN, J.

The Superintendent of Insurance, as liquidator (the “Superintendent”), brings this action on behalf of two now-defunct insurance companies, Home Mutual Insurance Company of Binghamton (“Home Mutual”) and Merchant Bakers Insurance Company (“Merchant Bakers”), their policyholders, and other creditors against PriceWaterhouseCoopers, LLP (“Coopers”), the accounting firm that audited some of the Companies’ 1993-1997 financial statements, and former company officers and directors, alleging, *inter alia*, that Coopers failed to properly audit the companies, which ultimately become insolvent and seeking damages of at least \$100,000,000. The complaint alleges sixteen causes of action, seven of which are asserted against Coopers: Fraud and Deceit; Negligent Misrepresentation; Professional Malpractice/Negligence; Breach of Fiduciary Duty; Aiding and Abetting Officers and Directors’ Wrongdoing; Breach of Contract; and Insurance Law Violations.

Coopers now moves to dismiss the complaint against it in lieu of answering pursuant to CPLR 3211(a) and 3016, on statute of limitations grounds, for failure to state a cause of action, failure to plead fraud with the requisite particularity, and duplicity of claims.

Allegations

The complaint alleges that Home Mutual and Merchant Bakers were property casualty insurers specializing in automobile insurance. Throughout the years 1993 to July 1997, Coopers' served as "auditors, actuaries and business advisors" to Home Mutual, Merchant Bakers, and non-party Home State Holdings, Inc.², the former holding company of Merchant Bakers and former manager of Home Mutual ("Home State"; hereafter Home Mutual, Merchant Bakers and Home State are defined as the "Companies"). Coopers allegedly "audit[ed] [the Companies'] financial statements and applicable portions of the consolidated financial statements of Home State, and opin[ed] and provid[ed] insurance industry advice as to the internal controls and practices of these entities, including as to loss reserves and reinsurance accounting."

Coopers performed the following audit services for the Companies: for Home State, Coopers audited the Company's consolidated financial statements for the years ended December 31, 1993-96, issuing reports that Home State included in its Annual Reports on

²In 1998 Coopers & Lybrand, LLP merged with Price Waterhouse to form PriceWaterhouseCoopers, LLP.

³Home State is an insurance holding company which from 1993-1997 conducted its business through its insurance subsidiaries, including Home Mutual and Merchant Bakers. In 1998, Home State filed a Voluntary Petition for Reorganization pursuant to Chapter 11 of the Bankruptcy Code, and has continued in possession of its business and property.

Form 10-K. Coopers issued its'last audit report to Home State on March 31, 1997. Each audit was conducted and each report issued pursuant to a series of Letters of Arrangement between Coopers and Home State. Home State also hired Coopers to audit its statements for 1996, but Coopers resigned, for reasons discussed below, before completing the audit or issuing the report.

For Home Mutual, Coopers audited the Company's statutory-basis financial statements for the years ended December 31, 1993-95, pursuant to Letters of Arrangement. The last report was issued on September 6, 1996.

For Merchant Bakers, Coopers audited the Company's statutory-basis financial statements for the year ended December 31, 1995, pursuant to a Letter of Arrangement; Coopers issued its report on March 14, 1996. Merchant Bakers also hired Coopers to audit its statements for 1996, but Coopers resigned before completing the audit or issuing the report.

In each report that it issued for the Companies, Coopers stated that, in its unqualified opinion, the Companies had fairly presented their financial statements in all material respects, that those statements could be relied upon, and that the statements complied with all reporting requirements.

The Superintendent also alleges that Coopers, as actuary, issued actuarial opinions on Home Mutual's and Merchant Baker's loss reserves, including its loss and loss adjustment and expense reserves, as of December 31, 1996.

The complaint next alleges that Coopers performed other professional services for the Companies. Coopers "review[ed]" the quarterly statements that Home State filed with

the Securities and Exchange Commission (“SEC”), but neither audited these quarterly statements nor reviewed them before their release. The last such quarterly statement was filed in 1996. Coopers also reviewed Home Mutual’s quarterly statutory filings for the years 1993 through 1997, and reviewed Merchant Baker’s filings for the years 1995 through 1997, again without auditing them.

Finally, the complaint alleges that Coopers acted as a “consultant” for the Companies:

Coopers represented, promised and agreed that it would provide insurance industry advice, expert opinion, and guidance as to specific areas of risk to [the Companies] and audit as to such areas with a heightened degree of care, including as to such areas as internal controls, claims, loss reserves, reinsurance, policy acquisition costs, underwriting, the premium cycle and the overall financial soundness of [the Companies.]

Despite Coopers’ audits, it is alleged that the Companies’ financial statements contained material misstatements and omissions with respect to their true condition. Among other deficiencies, the Companies understated their loss reserves and misstated their reinsurance accounts by overstating their reinsurance profit-sharing accruals. As a result, the Companies’ statements of earnings and shareholder equity were inflated. In addition, the Companies disguised and concealed that they lacked adequate internal management controls causing the Companies to write ever-increasing volumes of new business based upon the false financial information that Coopers had audited.

Shortly after Coopers issued its audit opinion for Home State’s 1996 financial statements, the complaint alleges, the truth about the Companies’ finances began to come out. In May 1997, Home State filed a Notification of Late Filing for its financial statements for the quarter ending March 31, 1997 because of “[f]actors including review of case reserve

development and adjustments to balance sheet items.” In June 1997, a Home State filing indicated that, until it had determined why it suffered substantial operating losses in the first quarter of 1997, its 1996 financial statements and Coopers’ related audit report “should not be relied upon.”

In July 1997, Coopers withdrew its audit opinions on the ground that the Companies had misstated their financial statements since 1994 and that the Companies lacked sufficient internal controls. Coopers resigned as auditor for the Companies on July 15, 1997. In August 1997, Home Mutual and Merchant Bakers were declared insolvent and placed in rehabilitation. In January 1998, the Home Mutual and Merchant Bakers’ rehabilitation proceedings were converted to liquidation proceedings.

The Superintendent alleges that Coopers knew about the internal control lapses and other problems that plagued the Companies as early as 1993, yet Coopers ignored or concealed these problems, ultimately causing their insolvency, and leaving the New York Property/Casualty Insurance Fund, the New York Public Motor Vehicle Liability Security Fund, and the New York insurance-buying public responsible³ for losses estimated at over \$100,000,000.

Discussion - Malpractice/Negligence

The professional malpractice/negligence claim against Coopers is dismissed as time-barred by the three year statute of limitations set forth in CPLR 214(6). Actions for

³These state security funds are financed through assessments on insurance companies doing business in New York which, in turn, pass the costs on to policyholders through their premiums..

accountant malpractice generally accrue “on the date the accountant’s work product is received by the client.” *Ackerman v. Price Waterhouse*, 84 N.Y.2d 535,541 (1994). Here, Coopers delivered its only audit report for Merchant Bakers by March 14, 1996, its final report for Home Mutual by September 9, 1996, and its final report for Home State by March 31, 1997, i.e., more than three years before plaintiff commenced this action on May 12, 2000.

The Superintendent claims that the statute of limitations was tolled by Coopers’ continuous representation, but that doctrine applies only when the ongoing representation is “continuous” and “related to the particular duty breached.” *Natl. Life Ins. Co. v. Frank B. Hall & Co.*, 67 N.Y.2d 1021, 1023 (1986). The continuous representation must be connected with the matter in dispute, and not merely a continuing, general professional relationship. *Id.* Here, the Superintendent contends that Coopers audited the companies’ statements negligently, inasmuch as it overlooked the misstatements in the companies’ financial statements. The Superintendent further alleges that, after Coopers resigned in 1996, it continued to perform “corrective” auditing work for the Companies as late as May 1997, but the Superintendent cannot relate any such work to the allegedly defective audits.

Since the audits form the only basis for the Superintendent’s malpractice claim, there was no continuous representation. Each audit was a discrete service, ending with Coopers’ delivery of an annual audit letter to the Companies. Moreover, the Companies signed separate engagement letters for each fiscal year, pursuant to which Coopers agreed to audit the Companies for that year. Inasmuch as there was no continuous representation, the statute of limitations was not tolled.

The Superintendent claims that Coopers' continuously represented the companies "on an ongoing basis" by "focus[ing] on the claims, reinsurance accounting, underwriting and internal controls which were identified as key *audit* areas of particular concern at the companies." (emphasis supplied) But here the Superintendent concedes that Coopers focused on these matters during its audits, which themselves were discrete services. Thus the malpractice claim must be dismissed as untimely.

Fraud, Breach of Contract, Breach of Fiduciary

The Superintendent's fraud claim is dismissed for failure to state a claim; the fraud, breach of contract, breach of fiduciary duty, and negligent misrepresentation claims are dismissed because they duplicate the malpractice claim. *See, Sane Realty Corporation v. Proskauer Rose, L.L.P.*, 251 A.D.2d 35 (1st Dept. 1998). "Where, as here, a fraud claim is asserted in connection with charges of professional malpractice, it is sustainable only to the extent that it is premised upon one or more affirmative, intentional misrepresentations – that is, something more egregious than mere 'concealment or failure to disclose [one's] own malpractice' . . . – which have caused additional damages, separate and distinct from those generated by the alleged malpractice." *White of Lake George, Inc. v Bell*, 251 AD2d 777, 778 (3rd Dept. 1998); *see also, Meccav. Shang*, 258 AD2d 569 (2nd Dept. 1999); *Sage Realty v. Proskauer Rose L.L.P.*, *supra*. The Superintendent's fraud cause of action, with respect to which no distinct damages are claimed, alleges that Coopers made material misrepresentations and omissions to induce Merchant Bakers and Home Mutual to keep

Coopers as their auditor and “to cover up and avoid the repercussions of the falsity of its prior representations and the deficiencies of its prior work.” The Superintendent further alleges that Coopers failed to independently verify the Companies’ financial statements, allowed misstatements of loss reserves and reinsurance accounting, and failed to take steps to correct internal management problems; but that is the same misconduct alleged in the malpractice cause of action. In short, notwithstanding the Superintendent’s numerous and detailed allegations, the **fraud** cause of action alleges conduct amounting to negligence, rather than an intent by Coopers to mislead Home Mutual or Merchant Bakers to their detriment. “Negligence in an accountant’s purported departure from professional standards, no matter how well particularized, does not make out fraud[.]” LaSalle National Bank v Ernst and Young, 285 A.D.2d 101 (1st Dept. 2001).

Under CPLR 214(6), a plaintiff must begin an accounting malpractice action within three years of accrual “regardless of whether the underlying theory is based in contract or tort.” See **David v. Isaacson, Robustelli, Fox, Fine, Greco & Fogelgaren, P.C.**, 258 A.D.2d 321, 321-22 (1st Dept. 1999) (finding claims for legal malpractice, fraud and breach of fiduciary duty were time-barred by the three-year statute of limitations for malpractice claims). Here, the Superintendent does not allege a contractual obligation on the part of Coopers, nor the breach thereof, beyond Cooper’s duty to perform its services pursuant to generally accepted auditing and accounting practices pursuant to the Letters of Arrangement. A breach of contract claim premised solely on an accountant’s failure to exercise due care, or to abide by general professional standards, is merely a redundant pleading of a malpractice claim. Sage Realty v Proskauer Rose L.L.P., *supra*, at 38-39.

The Superintendent's breach of fiduciary duty and negligent misrepresentation causes of action also duplicate the malpractice claim, since they "arise from the same facts as [the] legal malpractice claim and do not allege distinct damages." Mecca v Shanq, *supra*, at 570. See also, White of Lake George v Bell, *supra*; Sage Realty Corp. v Proskauer Rose, *supra*.

Aiding and Abetting Officers' and Directors' Wrongdoing

In the fifth cause of action, the Superintendent alleges that the individual defendants, as officers and directors of the Companies, "owed Merchant Bakers and Home Mutual and their policyholders and other creditors the fiduciary and other duties of an officer and director," that the individual defendants breached such duties by manipulating and falsifying the companies' financials, and that "Coopers was aware of such breaches and rendered substantial assistance to the [i]ndividual [d]efendants in committing them." Coopers allegedly "was aware of the control deficiencies making the foregoing manipulations possible and of [defendant] Abidor's domination of Merchant Bakers and Home Mutual, but ignored such matters and numerous red flags as to improper practices and procedures, passively accepting the individual defendant's version of events." Finally, the Superintendent alleges that "Coopers was aware of substantial problems with the financial reporting of the [sic] Home State, but ignored the warning signs . . . and failed to take necessary audit steps to adequately investigate and evaluate such matters."

These allegations are insufficient to state a cause of action for aiding and abetting a breach of fiduciary duty, the elements of which include (1) a breach by a fiduciary of

obligations to another; (2) the defendant's knowing inducement of, or participation in, such breach, and (3) damages as a result of the breach. S & K Sales Company v Nike, Inc., 816 F.2d 843,847 (2nd Cir 1987); see also, Shearson Lehman Brothers Inc. v Bagley, 205 AD2d 467 (1st Dept 1994) (citing S & K Sales Company v Nike, *supra*). Moreover, "an essential element of aiding and abetting is that the defendant give 'substantial assistance or encouragement' to the primary wrongdoer." Portnoy v The American Tobacco Company, 1997 WL 638800 (Sup Ct NY County 1997); see also, Rostuca Holdings, Ltd v Polo, 231 AD2d 402 (1st Dept 1996) (aiding and abetting requires substantial assistance in accomplishing the underlying violations). The Superintendent's allegations that Coopers ignored or permitted the alleged breaches by the individual defendants falls short of the required "substantial assistance" necessary to sustain a cause of action for aiding and abetting.

Insurance Law Violations

Finally, the Superintendent's causes of action based on alleged violations of the Insurance Law are dismissed as barred by the three-year statute of limitations applicable to actions to recover upon a liability created by statute. CPLR 214(2); Goldberg v Manufacturers Life Insurance Company, 242 AD2d 175 (1st Dept 1998); see also, Dolce v Northwestern Mutual Life Insurance Company, 272 AD2d 432 (2nd Dept 2000); Russo v Massachusetts Mutual Life Insurance Company, 274 AD2d 878 (3rd Dept 2000). The statute of limitations on these causes of action began to run at the time the false or misleading statements were made, see generally, Goldberg v Manufacturers Life Insurance Company, *supra*, at 180, in the present case, at the time Coopers issued its opinions.

Accordingly, it is

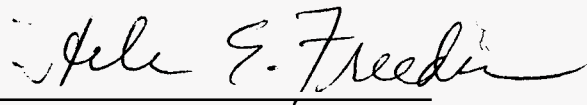
ORDERED that Coopers' motion to dismiss the complaint is granted, and the first, second, third, fourth, ~~fifth~~, and sixth causes of action are severed and dismissed, and the fifteenth cause of action is severed and dismissed as against Coopers, and it is further

ORDERED that the remainder of the action shall continue, and it is further

ORDERED that the remaining parties are directed to appear for a preliminary conference before the Court on January 8, 2002, in ~~Part 39~~, at 9:30 a.m.

Dated: November 21, 2001

ENTER:



J.S.C.

?