IN THE SUPREME COURT OF FLORIDA

CASE NO. 74,031

PEAT, MARWICK, MITCHELL & CO.,)

Petitioner,)

v.)

FRANK A. LANE and CAROL P. LANE,)

Respondents.)

ON DISCRETIONARY REVIEW OF A
DECISION OF THE THIRD DISTRICT COURT OF APPEAL
CERTIFIED TO BE IN DIRECT CONFLICT WITH A
DECISION OF ANOTHER DISTRICT COURT OF APPEAL

INITIAL BRIEF OF PETITIONER PEAT, MARWICK, MITCHELL & CO.

THOMSON MURARO BOHRER & RAZOOK, P.A.
Parker D. Thomson
Karen Williams Kammer
2200 One Biscayne Tower
2 South Biscayne Boulevard
Miami, Florida 33131
(305) 350-7200

Attorneys for Peat, Marwick, Mitchell & CO.

TABLE OF CONTENTS

	PAGE
TABLE OF AUTHORITIES	iv
STATEMENT OF THE CASE	1
STATEMENT OF THE FACTS	3
SUMMARY OF ARGUMENT	9
ARGUMENT	12
I. THE THIRD DISTRICT IGNORED THE FACT THAT A STATUTE OF LIMITATIONS IS A LEGISLATIVE DETERMINATION THAT CLAIMS MUST BE COMMENCED WITHIN A SPECIFIED TIME AFTER DISCOVERY OF THE CLAIM, OR THEY ARE FOREVER BARRED	12
II. THE EXHAUSTION RULE APPLIED BY THE THIRD DISTRICT IS INAPPLICABLE TO ACTIONS FOR NEGLIGENCE WITH RESPECT TO FEDERAL TAX MATTERS	16
A. The Consequences Of Accounting Negligence In Connection With Federal Tax Matters Are Fundamentally Different From Those Connected With General Attorney Negligence	17
1. The exhaustion rule for determining when the statute of limitations begins to run utilized in many attorney malpractice actions and relied upon erroneously by the Third District overlooks the unique nature of the IRS procedures triggered by accounting malpractice	18
2. On issuance of the 90-Day Letter, a taxpayer knows or should know that his accountant may have been negligent	22

B. All Courts In Other Jurisdictions Which Have Passed On The Issue Embrace The Rule That An Action For Negligence With Respect To Federal Tax Matters Accrues, At The Latest, On Issuance Of The 90-Day Letter 23

C. Commencement Of The Running Of The Statute Of Limitations On Issuance Of The 90-Day Letter Imposes No Burden On The Judicial System 27

D. This Court Should Adopt The Accepted Rule That A Cause Of Action For Accounting Negligence Accrues -- And Thus The Statute Of Limitations Begins To Run -- On Issuance Of The 90-Day Letter And Not When The Taxpayer Has Exhausted All Avenues Of Review 29

111. EVEN IF THIS COURT FINDS THAT THE LIMITATIONS RULE GOVERNING ACTIONS FOR ATTORNEY NEGLIGENCE ALSO APPLIES TO ACTIONS FOR NEGLIGENCE WITH RESPECT TO FEDERAL TAX MATTERS, THE RUNNING OF THE LIMITATIONS PERIOD BEGINS ON ISSUANCE OF THE 90-DAY LETTER 30

A. Under <u>Edwards v. Ford</u>, The Statute Of Limitations Begins To Run On A Cause Of Action For Attorney Negligence When The Plaintiff Knows Or Should Know That A Cause Of Action Has Accrued In His Favor 30

1. This Court in <u>Edwards</u> held that a cause of action accrues for attorney negligence when any damage, however slight, is sustained as a result of such negligence 32

2. This result obtains despite the fact that a plaintiff may take subsequent measures to reduce the amount of such damages or that the precise amount of damages has not been ascertained 33

B. This Court Should Reaffirm The Edwards Rule And Reject The Contrary Rule Of The Court Below That A Cause Of Action For Attorney Negligence Does Not Accrue Until A Final Adverse Judgment Has Been Entered On The Underlying Claim.. 41

1. The rule espoused by many post-Edwards district court cases, requiring exhaustion of all avenues of review before a cause of action for legal malpractice can be said to accrue, directly contradicts the language of Section 95.11(4)(a), Florida Statutes 42

2. An exhaustion rule effectively abrogates the Legislature's express intent to encourage the speedy resolution of professional malpractice claims and constitutes an impermissible judicial attempt at policymaking 43

3. An exhaustion rule contravenes logic and public policy 44

C. Edwards Thus Requires That The Two-year Statute Of Limitations For Professional Malpractice Actions In Florida Begins To Run On Claims For Negligence With Respect to Federal Tax Matters On Issuance Of The 90-Day Letter By The IRS 45

CONCLUSION 46

CERTIFICATE OF SERVICE 47

TABLE OF AUTHORITIES

Cases | Paae

Adams v. Sommers,
475 So.2d 279 (Fla. 5th DCA 1985) 39, 40

Baxter's Asphalt & Concrete, Inc. v. Liberty County,
406 So.2d 461 (Fla. 1st DCA 1981),
quashed on other grounds,
421 So.2d 505 (Fla. 1982) 19, 22

Birnholz v. Blake,
399 So.2d 375 (Fla. 3d DCA 1981) 37

Breakers of Fort Lauderdale, Ltd. v. Cassel,
528 So.2d 985 (Fla. 3d DCA 1988) 38, 42

Brower v. Davidson, Deckert,
Schutter & Glassman, P.C.,
686 S.W.2d 1 (Mo. App. 1984) 22

Canadian Universal Insurance Co. v.
Employers Surplus Lines Insurance Co.,
325 So.2d 29 (Fla. 3d DCA),
cert. denied, 336 So.2d 1180 (Fla. 1976) 19, 22

Chapman v. Garcia,
463 So.2d 528 (Fla. 3d DCA 1985) 37, 38

Chisholm v. Scott,
86 N.M. 707, 526 P.2d 1300 (Ct. App. 1974) 26

City of Miami v. Brooks,
70 So.2d 306 (Fla. 1954) 23, 34, 39

Diaz v. Piquette,
496 So.2d 239 (Fla. 3d DCA 1986),
review denied, 506 So.2d 1042 (Fla. 1987) 38

Diaz v. Rodriguez,
384 So.2d 906 (Fla. 3d DCA 1980) 38

Downing v. Vaine,
228 So.2d 622 (Fla. 1st DCA 1969),
appeal dismissed, 237 So.2d 767 (Fla. 1970) 31

Edwards v. Ford,
279 So.2d 851 (Fla. 1973) 11, 30-46

Feldman v. Granaer,
255 Md. 288, 257 A.2d 421 (1969) 23-26

Freel v. Fleminq,
489 So.2d 1209 (Fla. 1st DCA 1986) 35

Godfrev v. Bick & Monte, P.C.,
77 Or. App. 429, 713 P.2d 655
review denied, 301 Or. 165,
719 P.2d 874 (1986) 19, 21, 23

Green v. Adams,
343 So.2d 636 (Fla. 4th DCA 1977),
cert. denied, 353 So.2d 673 (Fla. 1977) 39

Hashavesh v. Clark,
520 So.2d 58 (Fla. 3d DCA 1988) 38, 41

Heard v. Mathis,
344 So.2d 651 (Fla. 1st DCA 1977) 13

Isaacson, Stolper & Co. v. Artisan's Savinqs Bank,
330 A.2d 130 (Del. 1974) 22, 23

Kellermever v. Miller,
427 So.2d 343 (Fla. 1st DCA 1983) 34-36

Kellev v. School Board of Seminole County,
435 So.2d 804 (Fla. 1983) 16, 33, 34

Lane v. Peat, Marwick, Mitchell & Co.,
540 So.2d 922 (Fla. 3d DCA 1989) 2, 15, 16

Leonhart v. Atkinson,
265 Md. 219, 289 A.2d 1 (1972),
overruled on other srounds,
Poffenberser v. Risser, 290 Md. 631,
431 A.2d 677 (1981) 23, 25

Levin v. Berlev,
728 F.2d 551 (1st Cir. 1984) 19

McHan v. Huggins,
459 So.2d 1172 (Fla. 5th DCA 1984) 13

McKeown v. First Interstate Bank of California,
240 Cal. Rptr. 127, 194 Cal. App. 3d 1225
(Cal. Ct. App. 1987) 19

Mills v. Garlow,
768 P.2d 554 (Wyo. 1989) 22, 23, 26, 27

Petition of Kearnev,
63 So.2d 630 (Fla. 1953) 17

<u>Richards Enterprises, Inc. v. Swofford</u>,
495 So.2d 1210 (Fla. 5th DCA 1986),
<u>dismissed without opinion</u>,
515 So.2d 231 (Fla. 1987) 40, 42

<u>Sawyer v. Earle</u>,
14 F.L.W. 413 (Fla. 2d DCA
Feb. 17, 1989) 2, 34, 36

<u>Schetter v. Jordan</u>,
294 So.2d 130 (Fla. 4th DCA 1974) 39

<u>Seaboard Air Line Railroad Company v. Ford</u>,
92 So.2d 160 (Fla. 1955) 34

<u>Shearn v. Orlando Funeral Home, Inc.</u>,
88 So.2d 591 (Fla. 1956) 13

<u>Snipes v. Jackson</u>,
69 N.C. App. 64, 316 S.E.2d 657
<u>review denied</u>, 312 N.C. 85,
321 S.E.2d 899 (1984) 18

<u>Sperry v. Florida Bar</u>,
373 U.S. 379 (1963), <u>reversing</u>
<u>State of Florida ex rel. the Florida Bar v.</u>
<u>Sperry</u>, 140 So.2d 587 (Fla. 1962) 17

<u>Welch v. Helvering</u>,
290 US. 111 (1933) 5

<u>Zakaks v. Broida and Napier, P.A.</u>,
14 F.L.W. 1356 (Fla. 2d DCA June 9, 1989) 36, 37

<u>FLORIDA LAWS AND STATUTES</u>

§ 57.105, Fla. Stat. (1987) 13

§ 95.031, Fla. Stat. (1987) . . . . <u>passim</u>

§ 95.11, Fla. Stat. (1987) 12

§ 95.11(3)(c), Fla. Stat. (1987) 33

§ 95.11(4)(a), Fla. Stat. (1987) . . . . <u>passim</u>

FEDERAL STATUTES

28 U.S.C.A. § 1346(a)(1) (West Supp. 1989) 6

INTERNAL REVENUE CODE

I.R.C. § 6072 (1988) 21
I.R.C. § 6151(c) (1988) 21
I.R.C. § 6155 (1988) 4, 6
I.R.C. § 6203 (1988) 4
I.R.C. § 6212 (1988) 4
I.R.C. § 6213(a) (1988) 4
I.R.C. § 6213(b)(4) (1988) 5
I.R.C. § 6214 (1988) 21
I.R.C. § 6303 (1988) 4, 6
I.R.C. §§ 6321-6327 (1988) 4
I.R.C. §§ 6331-6344 (1988) 4
I.R.C. § 6402 (1988) 6
I.R.C. § 6532 (1988) 6
I.R.C. § 6601 (1988) 6, 20, 21
I.R.C. § 7422 (1988) 6

UNITED STATES TAX COURT RULES

Tax Court Rule 142(a) 5
Tax Court Rule 200(a) 17

UNITED STATES TREASURY REGULATIONS

26 C.F.R. § 601.105(a) (1988) 4
26 C.F.R. § 601.105(b)(4) (1988) 4
26 C.F.R. § 601.105(d)(2) (1988) 5

THOMSON MURARO BOHRER & RAZOOK, P.A. 2200 ONE BISCAYNE TOWER, 2 SOUTH BISCAYNE BOULEVARD, MIAMI, FL 33131

OTHER AUTHORITIES

1 CCH Internal Revenue Manual (Audit) ch. 4463, at 7887-2 et seq. 6

1 CCH Internal Revenue Manual (Audit) Exhibit 4460-1 at 7905 6

Staff Analysis, Committee Substitute for HB 895, §§ 1-3. . 14

W. Keeton, D. Dobbs, R. Keeton and D. Owen, Prosser and Keeton on The Law of Torts, § 30 (5th ed. 1984) 13

STATEMENT OF THE CASE

This case, involving the application of the professional malpractice statute of limitations to actions for accounting malpractice, is one of first impression for this Court.

On February 22, 1985, Frank A. Lane and Carol P. Lane, both attorneys (the "Taxpayers"), filed this accounting malpractice action against Peat, Marwick, Mitchell & Co.1/ ("Peat Marwick"). Taxpayers alleged that Peat Marwick negligently advised Taxpayers to invest in a limited partnership known as Northern Voices, Ltd. (the "Partnership"), and negligently prepared Taxpayers' tax returns for 1976 and 1977 by claiming certain deductions resulting from that investment.

Peat Marwick answered and asserted as one of its affirmative defenses that Taxpayers' claim was barred by the two-year statute of limitations governing professional malpractice actions, Section 95.11(4)(a), Florida Statutes (1987). Peat Marwick then moved for summary judgment on the basis that the limitations period with respect to Taxpayers' claims had begun when the Internal Revenue Service (the "IRS") sent the Statutory Notice of Deficiency -- commonly referred to as the 90-day letter -- to Taxpayers on March 17, 1981. Because Taxpayers filed their complaint almost four years later, argued Peat Marwick, their claim was time-barred. The

1/ Peat, Marwick, Mitchell & Co. is now known as Peat Marwick Main & Co.

Circuit Court agreed and entered summary judgment in Peat Marwick's favor.

On appeal, the Third District Court of Appeal ("Third District") reversed and remanded. Lane v. Peat, Marwick, Mitchell & Co., 540 So.2d 922 (Fla. 3d DCA 1989). The Third District reasoned that the limitations period did not begin to run until the United States Tax Court entered a stipulated order on May 9, 1983 -- based on an agreement between Taxpayers and the IRS -- reaffirming that a deficiency existed.

The Third District certified its decision to be in conflict with the Second District Court of Appeal's decision in Sawyer v. Earle, 14 F.L.W. 413 (Fla. 2d DCA Feb. 17, 1989). This Court has accepted jurisdiction.

STATEMENT OF THE FACTS[2/]

Peat Marwick's Services and IRS Audit

Taxpayers had retained Peat Marwick as their accountants to provide them with tax advice and to prepare their federal income tax returns. In December 1976, Peat Marwick suggested that Taxpayers invest in the Partnership, a new limited partnership formed to purchase rights in musical recordings. Taxpayers invested in the Partnership, and, in preparing Taxpayers' 1976 and 1977 income tax returns, Peat Marwick claimed deductions relating to that investment. But the melody hit a sour note when the IRS notified Taxpayers that the Partnership was under examination and that the IRS therefore wished to examine Taxpayers' 1976 and 1977 returns.

IRS Procedures

This case turns on the effect of an IRS Statutory Notice of Deficiency -- the so-called 90-Day Letter. This factual statement therefore can only be understood in the context of the IRS procedures for determining tax deficiencies.[3/] That process begins, as it did with Taxpayers,

---

2/ Because this case concerns review of an order granting summary judgment, the Statement of Facts is a summary of the allegations of Taxpayers' complaint, which, for this purpose, are treated as true.

3/ All references to the Internal Revenue Code are to the Internal Revenue Code of 1986 as amended through the end of 1988. There have been no material changes in the Code sections cited since the facts set out here occurred.

when the IRS selects certain tax returns for audit or examination.[4] After the examination, the taxpayer receives a report containing the examiner's findings with regard to any adjustments in tax liability. If the taxpayer agrees and signs the requisite form evidencing such agreement,[5] the agreed-upon deficiency is immediately assessable.[6]

Of course, the taxpayer need not accede to the examiner's findings. If the taxpayer does not accede, he will receive a Preliminary Notice of Deficiency -- commonly referred to as the 30-day letter (the "30-Day Letter")-- advising him of a proposed adjustment to his return. The taxpayer may then: (i) remit the full amount, (ii) make a

---

4/ 26 C.F.R. § 601.105(a) (1988). (A. 76). References to record pages will be shown by "R." followed by the record page number, as in "R. 1". References to pages in the attached Appendix will be shown by "A." followed by the appendix page number, as in "A. 1".

5/ This form is known as a Consent to Assessment (IRS Form 870). Although there are several such forms, Form 870 is the most common. 26 C.F.R. § 601.105(b)(4) (1988). (A. 77, 95-6).

6/ The IRS generates federal income tax revenues by a method known in IRS parlance as "assessment" followed by a "notice and demand" for the assessed amount. Unless waived, the 90-Day Letter (asserting that there is a deficiency between the amount of tax paid and the amount the taxpayer actually owed) is a prerequisite to an assessment. I.R.C. §§ 6212 and 6213(a) (1988). (A. 12-16). The actual assessment occurs when the IRS finally enters into its records the fact that there is a deficiency and the taxpayer owes a specified amount of unpaid tax. <u>See</u> I.R.C. § 6203 (1988). (A. 11). After an assessment is made, the tax is due and payable when the taxpayer receives the notice and demand. I.R.C. §§ 6155 and 6303 (1988). (A. 10, 23). At this point the IRS may institute the various collection procedures at its disposal, including liens (I.R.C. §§ 6321-6327 (1988)) or the seizure of property (I.R.C. §§ 6331-6344 (1988)). (A. 24-59).

partial payment and protest the balance, (iii) protest the entire amount, or (iv) simply ignore the 30-Day Letter. Following either of the first two routes results in immediate assessment of the amount remitted.[7]

If the taxpayer chooses to protest, he must do so within 30 days, hence the name 30-Day Letter. If he does protest, he is afforded a conference with the appropriate IRS appeals office.[8] If the taxpayer disagrees with the appeals office decision or ignores the 30-Day Letter, the IRS will send the taxpayer the Statutory Notice of Deficiency, the 90-day letter (the "90-Day Letter").

The 90-Day Letter reflects the IRS' conclusive determination that an error or errors in preparation of a taxpayer's return resulted in underpayment of federal income tax, and that within 90 days the taxpayer must either remit the tax due, including accrued interest and penalties (if any), or prove that he does not owe the tax.[9] The 90-Day Letter expressly advises the taxpayer that the IRS has "determined that there is a deficiency (increase) in your income tax," stating the amount due and setting forth the

---

7/ I.R.C. § 6213(b)(4) (1988). (A. 17).

8/ 26 C.F.R. § 601.105(d)(2) (1988). (A. 85).

9/ The taxpayer's burden is a heavy one, for the deficiency is presumed to be correct as a matter of law. See Welch v. Helvering, 290 US. 111, 115 (1933) (holding IRS' determination is presumptively correct with burden on taxpayer to prove otherwise); Tax Court Rule 142(a). (A. 88).

basis of the IRS' calculations.[10/] (R. 93-96). Although collection is temporarily deferred, it is nevertheless certain to occur upon notice and demand.[11/] Once he receives the 90-Day Letter, the taxpayer may avoid IRS collection procedures only by: (i) remitting the amount of tax owed or (ii) petitioning for a redetermination of the deficiency in Tax Court.[12/]

If the taxpayer chooses to remit the amount owed, he still may pursue a judicial evaluation of the IRS' deficiency determination by bringing a civil action for a refund in either federal district court or the United States Claims Court.[13/]

10/ See generally 1 CCH Internal Revenue Manual (Audit) ch. 4463, at 7887-2 et seq., and Exhibit 4460-1 at 7905. (A. 92-94).

11/ I.R.C. §§ 6155 and 6303 (1988). (A. 10, 23).

12/ Although the taxpayer has 90 days in which to pay or petition for a redetermination, interest and penalties nevertheless accumulate and thus it behooves the taxpayer to remit the unpaid tax as soon as possible. See I.R.C. § 6601 (1988). (A. 65-70).

13/ 28 U.S.C.A. § 1346(a)(1) (West Supp. 1989). (A. 75). Before a taxpayer may institute a civil refund action, however, he must first file a claim for a refund with the IRS. I.R.C. §§ 6402 and 7422 (1988). (A. 60-62, 71-74). The taxpayer may not sue until six months after he does so or after the date the IRS renders a decision on his claim, whichever date is earlier. If the IRS disallows the refund, the taxpayer must bring suit no later than two years after that date. I.R.C. § 6532 (1988). (A. 63-64).

Receipt of 90-Day Letter by Taxpayers

On March 17, 1981, the IRS disallowed the Partnership-related deductions Taxpayers had claimed for 1976 and 1977,[14/] allegedly on the advice of Peat Marwick, and on that date the IRS sent Taxpayers a 90-Day Letter. (R. 93). The letter is addressed to Taxpayers and reads, in pertinent part, as follows:

> Sir and Madam:
>
> We have determined that there is a deficiency (increase) in your income tax as shown above. This letter is a NOTICE OF DEFICIENCY sent to you as required by law. The enclosed statement shows how we figured the deficiency.
>
> If you want to contest this deficiency in court before making any payment, you have 90 days from the above mailing date of this letter . . . to file a petition with the United States Tax Court for a redetermination of the deficiency.
>
> . . .
>
> If you decide not to file a petition with the Tax Court, we would appreciate it if you would sign and return the enclosed waiver form. This will permit us to charge your account quickly and will limit the accumulation of interest.
>
> . . .
>
> If you have any questions, please contact [J. D'Addario].

(R. 93, A. 6).[15/]

[14/] The deductions claimed were Taxpayers' distributive share of Partnership losses and credits for those years.

[15/] A copy of the letter in its entirety, including attachments, appears in the Appendix.

As of March 17, 1981, the IRS had conclusively determined that because it was disallowing the Partnership-related deductions, Taxpayers had underpaid their 1976 and 1977 federal income tax by almost $22,000. Specifically, the 90-Day Letter notified Taxpayers that there was a deficiency of $9,980 on their 1976 return and a deficiency of $11,746 on their 1977 return, and the attachments explained how the IRS calculated those amounts. (R. 93-96, A. 6-6c).

Taxpayers elected not to pay the amount past due, and instead filed a petition in Tax Court for a redetermination of the deficiency. (R. 36). Taxpayers and the IRS finally agreed to a total deficiency of approximately $15,000 -- $3,230 for 1976 and $12,019 for 1977. A stipulated order of the Tax Court was entered May 9, 1983, reflecting the agreed amount. (R. 7).

Respondents then filed this lawsuit against Peat Marwick on February 22, 1985, almost four years after the IRS had determined that Respondents had underpaid their tax and informed them of the deficiency and accrued interest.

SUMMARY OF ARGUMENT

The question presented by this case is the time at which Florida's two-year statute of limitations for professional malpractice actions begins to run on a claim for accounting negligence.

A statute of limitations represents the Legislature's determination that once a cause of action has accrued, the claimant must bring his claim before the court within a specified period of time, or else he is forever barred from doing so. The statute of limitations plays no favorites. Even meritorious claims, that is, those which would have succeeded had they been fully litigated, are barred. As in most states, in Florida the limitations period begins to run on a cause of action for professional malpractice when the client discovers or should discover with the exercise of due diligence that he has such a claim (that is, the client has a good faith belief that the professional's alleged negligence may have caused the client some injury). The cause of action accrues when the last element constituting the cause of action -- usually the injury -- occurs.

The consequences flowing from accounting negligence provide a clear and easy reference point for the accrual of the negligence claim and thus the running of the limitations period. Unlike the negligence associated with the general practice of law, an improperly prepared federal income tax return activates an elaborate administrative response, culminating with the IRS issuing the 90-Day Letter to the taxpayer. The 90-Day Letter reflects the IRS' conclusive determination that the taxpayer has underpaid his federal income tax. That determination constitutes legally cognizable injury, notice that an accountant's error may have been the cause, and thus the commencement of the limitations period.

On March 17, 1981, the IRS sent Taxpayers a 90-Day Letter. That 90-Day Letter notified Taxpayers the IRS concluded that they had underpaid their federal income taxes for 1976 and 1977 by almost $22,000 due to deductions Peat Marwick had allegedly approved but which the IRS did not. At that point, according to the letter, Taxpayers either had to remit the amount past due, with interest, or incur the expense of seeking a redetermination in Tax Court.

Other than the Third District here, all courts addressing the issue have held that a cause of action for accounting negligence accrues no later than the time at which the IRS sends the 90-Day Letter to the taxpayer. The reasoning of these courts is eminently sound, reflecting the importance of the procedures concerning federal tax deficiencies. This Court should likewise conclude that Florida's limitations period for accounting malpractice actions should begin to run no later than the 90-Day Letter.

The Third District erroneously concluded that the general rules governing legal malpractice actions should apply to this case, although the effects of accounting negligence bear little, if any, resemblance to the effects of general legal malpractice. But even if this Court chooses to apply the limitations rule governing actions for attorney malpractice, this Court's decision in Edwards v. Ford, 279 So.2d 851 (Fla. 1973), nevertheless requires that the 90-Day Letter start the limitations period running.

The district court cases since Edwards addressing the limitations issue with respect to actions for general legal malpractice have been contradictory and confusing. If this Court determines that the rule for general legal malpractice should apply to negligence with respect to federal tax matters, this Court should reaffirm the rule of Edwards, and clarify that the key -- and only -- issues relevant to determining the commencement of the limitations period are discovery of the event alleged to constitute malpractice plus some injury as a result of that alleged malpractice. With respect to Taxpayers, this Court should then find the limitations period on their malpractice claim against Peat Marwick began to run no later than the 90-Day Letter, almost four years before Taxpayers filed their malpractice action.

ARGUMENT

I. THE THIRD DISTRICT IGNORED THE FACT THAT A STATUTE OF LIMITATIONS IS A LEGISLATIVE DETERMINATION THAT CLAIMS MUST BE COMMENCED WITHIN A SPECIFIED TIME AFTER DISCOVERY OF THE CLAIM, OR THEY ARE FOREVER BARRED.

Two sections of Florida's statute of limitations are crucial to the appropriate resolution of this case. Section 95.031, Florida Statutes (1987), provides in relevant part:

> 95.031 Computation of time
>
> . . . the time within which an action shall be begun under any statute of limitations runs from the time the cause of action accrues.
>
> (1) A cause of action accrues when the last element constituting the cause of action occurs.

Section 95.11, Florida Statutes (1987), provides in relevant part:

> 95.11 Limitations other than for the recovery of real property
>
> Actions . . . shall be commenced as follows:
>
> . . .
>
> (4) WITHIN TWO YEARS. --
>
> (a) An action for professional malpractice . . . whether founded on contract or tort; provided that the period of limitations shall run from the time the cause of action is discovered or should have been discovered with the exercise of due diligence.

In general, a cause of action consists of some injury and an event which the claimant discovers -- or should discover

THOMSON MURARO BOHRER & RAZOOK, P.A. 2200 ONE BISCAYNE TOWER, 2 SOUTH BISCAYNE BOULEVARD, MIAMI, FL 33131

-- may have caused that injury.[16] That a claimant has a cause of action does not suggest that he will necessarily prove the required elements of his case. The existence of a cause of action merely endows the claimant with the right to bring his claim before a court of law. Shearn v. Orlando Funeral Home, Inc., 88 So.2d 591, 593 (Fla. 1956). He need not prove his opponent's liability before instituting a lawsuit; he need only have a good faith belief that liability exists.[17]

Because Section 95.11(4)(a), like all statutes of limitation, must be raised defensively (as an affirmative defense as in this case, or, if its application is clear on the face of the complaint, by a motion to dismiss), whether the claimant ultimately succeeds in carrying his burden of proof is immaterial. The limitations defense assumes that the claimant can prove his cause of action, yet for policy reasons nevertheless prevents him even from attempting to do so. "Discovery rule" statutes of limitations such as Florida's

---

16/ See generally W. Keeton, D. Dobbs, R. Keeton and D. Owen, Prosser and Keeton on The Law of Torts, § 30 (5th ed. 1984); Heard v. Mathis, 344 So.2d 651, 655 (Fla. 1st DCA 1977) (describing elements of cause of action to include legal right in plaintiff, corresponding duty in defendant, and violation of duty leading to injury in plaintiff).

17/ See McHan v. Huggins, 459 So.2d 1172, 1174 (Fla. 5th DCA 1984) (on motion for recovery of attorney's fees under Section 57.105, Florida Statutes, requiring only that "reasonable efforts to ascertain parties and issues" be made, not "absolute verification").

reflect the Legislature's attempt[18] to strike a balance: (i) ameliorate the harshness of a rule requiring a claimant to bring a malpractice action the instant alleged negligent conduct occurs, notwithstanding the fact that the nature of such conduct might not manifest itself until years later, while (ii) imposing upon the claimant the obligation to use diligence in order to discover such alleged negligence.

The Legislature's plan encourages speedy resolution of malpractice claims. By barring even a meritorious claim if it is not filed within two years of a discoverable event plus some injury resulting from that event, the statute of limitations encourages a claimant with a cause of action to file suit as soon as he discovers or should discover he has such a cause of action. This rule protects defendants from having to defend against stale claims while preserving the integrity of the judicial process itself.

The Third District opinion evidences a fundamental misunderstanding of the purpose of a statute of limitations in general, and of Sections 95.031 and 95.11(4)(a) in particular. In holding that the limitations period did not begin to run until the adverse Tax Court order had been entered against Taxpayers, the Third District declared that Taxpayers:

> did not suffer redressable harm until the tax court entered judgment against them. Until that time, [Taxpayers] knew only

---

[18] Florida's statute codifies the common law. <u>See</u> Staff Analysis, Committee Substitute for HB 895, §§ 1-3. (A. 97-98).

> that Peat Marwick might have been negligent; however, if the tax court did not uphold the deficiency, [Taxpayers] would not have a cause of action against Peat Marwick for accounting malpractice.

Lane v. Peat, Marwick, Mitchell & Co., 540 So.2d 922, 924 (Fla. 3d DCA 1989) (emphasis added). The court did not explain why it believed entry of a Tax Court order to be the key, opting instead to substitute bare assertion for explanation.

The court erred in suggesting that Taxpayers had to prove with certainty that Peat Marwick was negligent before they could bring suit, something Taxpayers might never have been able to do. By the time Taxpayers received the 90-Day Letter, a cause of action for accounting malpractice -- in the sense contemplated by the statute -- had indeed accrued in their favor. Taxpayers sustained legally cognizable injury as of that time, the 90-Day Letter reflecting the IRS' conclusive determination that they had underpaid their federal income tax, allegedly because of erroneous tax advice resulting in an improperly prepared tax return. Quite simply, to avoid IRS collection procedures Taxpayers at that time either had to remit the amount of tax owed, or prove they did not owe the tax by petitioning for a redetermination of the deficiency in Tax Court. Moreover, Taxpayers discovered or should have discovered that a cause of action thus had accrued. The language of the 90-Day Letter is unmistakable, notifying Taxpayers they had underpaid their federal income taxes for 1976 and 1977 by almost $22,000.

Thus, by the time of the 90-Day Letter, Taxpayers had a discoverable -- and in fact, a discovered -- cause of action, as provided by Sections 95.031 and 95.11(4)(a), entitling them to file a malpractice action against Peat Marwick.[19] The key is that Taxpayers could have filed a lawsuit at that time, having sustained some injury and having discovered what might have been the cause of that injury. Instead, despite the clear mandate of the statute of limitations, Taxpayers delayed bringing such suit until almost four years later.

II. THE EXHAUSTION RULE APPLIED BY THE THIRD DISTRICT IS INAPPLICABLE TO ACTIONS FOR NEGLIGENCE WITH RESPECT TO FEDERAL TAX MATTERS.

The Third District erred in finding that accounting malpractice actions are "sufficiently analogous to actions based on legal malpractice" so that decisions concerning the latter are helpful to a consideration of the former. Lane, 540 So.2d at 923-24. The court's statement reflects a fundamental misunderstanding of the qualitative difference between the consequences flowing from a professional's negligence with respect to the handling of federal tax matters[20] and

---

[19] See Kelley v. School Board of Seminole County, 435 So.2d 804, 806 (Fla. 1983) (in professional negligence action based on construction defect, finding it sufficient for limitations purposes that client have notice that "it had, or might have had, a cause of action") (emphasis added).

[20] While an attorney skilled in tax matters may render tax advice or prepare an income tax return just as an (continued...)

the consequences arising out of negligence associated with the general practice of law.[21/]

A. <u>The Consequences Of Accounting Negligence In Connection With Federal Tax Matters Are Fundamentally Different From Those Connected With General Attorney Negligence.</u>

Whether an attorney is engaged for the purpose of pursuing or defending litigation, or is engaged for the purpose of structuring a transaction, the result of any negligence in his work most likely is litigation intended to remedy the error. The client already in litigation will probably appeal or in some other way seek to have the initial adverse judgment set aside. Similarly, the client involved in a transaction

---

20/ (...continued) accountant, for purposes of clarity and ease of discussion, however, Peat Marwick hereafter adopts the following shorthand: (i) "accountant" will refer to a professional who prepares a tax return or otherwise provides tax advice to a taxpayer, whether such professional is an accountant, an attorney or both, but will exclude the representation of a taxpayer in Tax Court; and (ii) "attorney" will refer to a professional who performs legal services other than those services described above related to tax matters, but will <u>include</u> representation of a taxpayer in Tax Court. Likewise, the terms "accounting negligence" or "accounting malpractice" will refer to negligence associated with the services of an accountant as so defined, while "attorney negligence" or "attorney malpractice" will refer to negligence in performance of services by an attorney as so defined. Peat Marwick recognizes, however, that one need not be an attorney or an accountant to be admitted to practice before the Tax Court. Tax Court Rule 200(a). (A. 90).

21/ This Court at one time believed that advice on tax matters constituted the practice of law which, if done in this state, required the state's approval. The United States Supreme Court disagreed. <u>See</u> <u>Sperry v. Florida Bar</u>, 373 U.S. 379 (1963), <u>reversing</u> <u>State of Florida ex rel. the Florida Bar v. Sperry</u>, 140 So.2d 587 (Fla. 1962) (following <u>Petition of Kearney</u>, 63 So.2d 630 (Fla. 1953), relating to tax matters).

likely will turn to litigation in an attempt to protect the deal his attorney has struck.

In contrast, when a professional -- whether he is an accountant or attorney, or has the credentials of both-- renders advice as to tax matters or prepares his client's tax return, the consequences are strikingly different. The result of any negligence is the institution of the exhaustive administrative process set out in the Statement of Facts.22/ This process is begun not at the urging of the client or professional but instead at the insistence of the IRS, and involves procedures and rules uniquely its own.23/

1. The exhaustion rule for determining when the statute of limitations begins to run utilized in many attorney malpractice actions and relied upon erroneously by the Third District overlooks the unique nature of the IRS procedures triggered by accounting malpractice.

As discussed above, whether there exists any cognizable legal injury with respect to accounting malpractice depends not upon a determination by a court of law, but depends instead upon a determination by the IRS. Such determination

---

22/ See pages 3-6, supra. Obviously, the IRS cannot detect every erroneous tax return, either because of time or manpower constraints, or the IRS' own inadvertence.

23/ See generally Snipes v. Jackson, 69 N.C. App. 64, 316 S.E.2d 657, 661, review denied, 312 N.C. 85, 321 S.E.2d 899 (1984) (distinguishing accounting malpractice from attorney malpractice based on fact that no injury occurs until the IRS says there is).

occurs, by design, before a taxpayer has exhausted all avenues of review.

Issuance by the IRS of the 90-Day Letter represents legally cognizable injury. On receiving the letter, the taxpayer has no choice but to pay or do battle with the IRS in Tax Court. The text of the letter to Taxpayers made that crystal clear. If the taxpayer pays, there is injury, whether or not he subsequently sues for a refund. If, instead, he chooses not to pay and petitions for a redetermination in Tax Court, the damage is equally present: in so doing, the taxpayer necessarily incurs professional fees and other expenses connected with the Tax Court representation, all of which constitute legally cognizable injury. Godfrey v. Bick & Monte, P.C., 77 Or. App. 429, 713 P.2d 655, 657, review denied, 301 Or. 165, 719 P.2d 874 (1986) (in accounting malpractice action, finding attorney and accounting fees expended in attempt to resolve dispute with IRS to constitute legal damage).[24/] In

---

[24/] See also Levin v. Berley, 728 F.2d 551, 554 (1st Cir. 1984) (finding injury in expenses incurred in fighting IRS); McKeown v. First Interstate Bank of California, 240 Cal. Rptr. 127, 130, 194 Cal. App. 3d 1225 (Cal. Ct. App. 1987) (finding injury in choice between paying or petitioning for redetermination). To the same effect, see generally Baxter's Asphalt & Concrete, Inc. v. Liberty County, 406 So.2d 461, 467 (Fla. 1st DCA 1981), quashed on other grounds, 421 So.2d 505 (Fla. 1982) (holding attorney's fees, costs and expenses necessarily incurred by claimant in attempts to protect its interests as against third party due to wrongful act of defendant to constitute element of damages); Canadian Universal Insurance Co. v. Employers Surplus Lines Insurance Co., 325 So.2d 29, 31 (Fla. 3d DCA), cert. denied, 336 So.2d 1180 (Fla. 1976) (holding that where defendant's wrongful act forces claimant to incur expenses to protect its interests with respect (continued...)

addition, interest on the unpaid tax accrues even while the Tax Court proceeding is pending, and stops accruing only if the taxpayer posts a cash bond equivalent to the amount of the deficiency.[25/] Issuance of the 90-Day Letter, then, provides both the requisite injury and the discoverable event which together constitute the cause of action.

In fact, the 90-Day Letter itself is the culmination of an extensive administrative review process. The process begins with an examination or audit, and any resultant proposed deficiency is the subject of further negotiation and discussion. At several points during the process the taxpayer may remit the disputed amount and thereby end the IRS inquiry.

"Exhaustion" by the taxpayer beyond the 90-Day Letter thus makes no sense in this context (whatever sense it may make in other contexts). To be sure, the taxpayer does have some recourse under IRS procedures even after issuance of the 90-Day Letter -- that is, after a cause of action for accounting malpractice already has accrued in the taxpayer's favor. He may remit the past due tax, accrued interest and penalties, seek a refund by the IRS, and, if rejected, seek judicial review of the correctness of the IRS' position in federal district

---

24/ (...continued) to a third party, such costs and expenses, including attorney's fees, "should be treated as the legal consequences of the original wrongful act and may be recovered as damages").

25/ I.R.C. § 6601 (1988). (A. 65-70). Interest continues to accrue only on that portion, if any, not secured by the cash bond.

court or the United States Claims Court. Alternatively, he may decline to pay and petition the Tax Court for a redetermination of the deficiency.[26/] However, the availability of these alternatives for remedying the wrong does not postpone its existence, because a taxpayer need not pursue these remedies in order to bring his malpractice claim to court.

It is no wonder, then, that all courts that have considered the issue, until the Third District in the instant case, have held that the limitations period begins to run, at the latest, as of the 90-Day Letter. The position of the Third District that no legal injury has occurred (or, perhaps, that no event of alleged negligence has been discovered) until all avenues of review have been exhausted ignores the fact that damage has already been done.[27/]

[26/] By definition, the Tax Court proceeding is for a "redetermination of the deficiency," such proceeding occurring only after the deficiency determination has already been made. I.R.C. § 6214 (1988) (emphasis added) (A. 20-22). In fact, the IRS' conclusion that a deficiency exists -- as evidenced by the 90-Day Letter -- is entitled to a presumption of correctness in Tax Court, the burden lying with the taxpayer to prove the contrary. See footnote 9, supra.

[27/] Indeed, some damage exists even before issuance of the 90-Day Letter. The 90-Day Letter does not represent a new finding of taxes which were never owed; rather, it is notice of taxes which were due on or before the "last date prescribed for payment", that is, the last date for filing the federal income tax return. I.R.C. §§ 6151(c) and 6072 (1988). (A. 9, 7-8). Since then, interest has been accumulating on the unpaid amount. I.R.C. § 6601 (1988). (A. 65-70). Attorney's fees and related expenses incurred during the preliminary stages of negotiation and internal IRS review before issuance of the 90-Day Letter represent legally cognizable injury as well, and are recoverable in subsequent litigation. See Godfrey, 713 P.2d at 657. See generally
(continued...)

2. On issuance of the 90-Day Letter, a taxpayer knows or should know that <u>his accountant may have been negligent.</u>

Not only does the taxpayer sustain legally cognizable injury by the time of the 90-Day Letter, but also the existence of such injury should indicate to the taxpayer that his accountant may have provided erroneous tax advice, and, consequently, that he has a cause of action for negligence. The letter expressly states that a deficiency exists, including its amount. Also, the review process leading up to issuance of the 90-Day Letter provides the taxpayer with substantial opportunity to question what is, up to that point, only a proposed deficiency.

Through all this, any prudent individual (and not just taxpayers who happen to be lawyers, as here) should have

---

27/ (...continued) <u>Baxter's Asphalt</u>, 406 So.2d at 467; <u>Canadian Universal</u>, 325 So.2d at 31. At least one court has held expressly that a cause of action accrues as of the 30-Day Letter. <u>Isaacson, Stolper & Co. v. Artisan's Savings Bank</u>, 330 A.2d 130 (Del. 1974). <u>See also Brower v. Davidson, Deckert, Schutter & Glassman, P.C.</u>, 686 S.W.2d 1 (Mo. App. 1984) (limitations period begins upon issuance of IRS examiner's report [which often accompanies 30-Day Letter] advising taxpayer of proposed deficiency); <u>Mills v. Garlow</u>, 768 P.2d 554, 557 (Wyo. 1989) (holding settlement with the IRS even before issuance of the 90-Day Letter provides claimant with notice of cause of action and thus starts running of statute of limitations). Peat Marwick here, while acknowledging the force of the above argument, has not made that argument, but has contended instead that issuance of the 90-Day Letter is injury and the "last element constituting the cause of action . . . ." § 95.031, Fla. Stat. (1987).

discovered that the IRS at least questioned, and by the time of the 90-Day Letter flatly disagreed with, the tax return under investigation. If the taxpayer sought the advice of an accountant in preparing such returns, then the IRS' continued scrutiny should suggest that the accountant may have erred. The letter itself as well as the administrative review and negotiation procedures occurring prior to the 90-Day Letter being sent must suggest to any taxpayer that something is amiss. See, e.g., Feldman v. Granger, 255 Md. 288, 257 A.2d 421 (1969) (applying discovery rule to accounting malpractice action and holding that claimant knows or should know a cause of action exists as of 90-Day Letter, at the latest).[28/]

B. All Courts In Other Jurisdictions Which Have Passed On The Issue Embrace The Rule That An Action For Negligence With Respect To Federal Tax Matters Accrues, At The Latest, On Issuance Of The 90-Day Letter.

The universally accepted rule in accounting malpractice actions is that a cause of action accrues and the

---

28/ Accord Leonhart v. Atkinson, 265 Md. 219, 289 A.2d 1 (1972), overruled on other grounds, Poffenberger v. Risser, 290 Md. 631, 431 A.2d 677 (1981); Godfrey, 713 P.2d at 657 (finding taxpayer "knew of the harm without having to wait for resolution of the controversy" once IRS began to question tax return); Mills, 768 P.2d at 557 (holding that, absent prior settlement with IRS, reasonable taxpayer should know he has cause of action against accountant by time of 90-Day Letter). Cf. Isaacson, 330 A.2d 130 (finding discovery of cause of action takes place upon issuance of 30-Day Letter). See generally City of Miami v. Brooks, 70 So.2d 306, 309 (Fla. 1954) (stating general rule that limitations period begins to run when claimant has been put on notice of "an invasion of a legal right" or "his right to a cause of action").

limitations period begins to run, at the latest, upon issuance of the 90-Day Letter. The states employing the rule also adopt the "discovery rule", as does Florida, in that their statutes of limitations run from the time at which the claimant knows or should know that he has a cause of action for professional malpractice. Consequently, whether the claimant has exhausted all possible avenues of review is deemed irrelevant.

Because this case is one of first impression for this Court, examination of decisions from these other jurisdictions which have considered the limitations issue is helpful. The seminal case is Feldman v. Granger, 255 Md. 288, 257 A.2d 421 (Md. 1969). There, the question facing the Maryland Court of Appeals was identical to the issue facing this Court: whether the limitations period for accounting malpractice begins to run only after the plaintiff has exhausted all avenues of review or whether it begins on issuance of the 90-Day Letter. In Feldman, Granger, an accountant, had missed an IRS filing deadline thereby depriving Feldman of favorable tax treatment for his corporation. Feldman nevertheless filed his tax return[29/] claiming the favorable tax treatment. The IRS questioned the return and ultimately notified Feldman of a $25,000-plus deficiency, which the Tax Court later upheld. Feldman sued Granger for accounting malpractice almost one

---

29/ Feldman alleged he did so on the advice of Granger's agent, although this allegation was disputed.

and one half years after the Tax Court decision but almost four years after the 90-Day Letter, well beyond the state's three-year statute of limitations for such actions.

The court flatly rejected Feldman's contention that the limitations period should not start to run until the plaintiff has exhausted all available remedies. Were Feldman's position to hold sway, reasoned the court, then the limitations period theoretically would not begin to run until a taxpayer had pursued his IRS challenge all the way to the United States Supreme Court, thereby imposing an intolerable burden upon the accountant against whom a malpractice action was to be brought. Feldman, 257 A.2d at 424-25, 426. More importantly, on issuance of the 90-Day Letter, "any reasonable and prudent" person would have known "or certainly should have known at that time, that he had sustained legal harm as of that date, if not before." Feldman, 257 A.2d at 425. What the court found particularly persuasive was the inescapable conclusion that by the time of the 90-Day Letter it necessarily becomes apparent that the IRS disagrees with the taxpayer's position. The court rejected as immaterial the argument that the exact amount of damage may not be known at such time, reasoning that the policy prohibiting stale claims, among others, precludes such an argument. Id. at 426.[30/]

30/ See also Leonhart, 289 A.2d 1 (following Feldman in holding a reasonable person should know he has a cause of action for negligence and thus three-year statute of limitations begins to run in action for accounting malpractice on date of (continued...)

A recent Wyoming case, Mills v. Garlow, 768 P.2d 554 (Wyo. 1989), reaches the same conclusion twenty years after Feldman.[31] At issue in Mills was the time at which a taxpayer whose tax return the IRS has challenged knows or should know that he has a cause of action against the accountant who prepared that return. There, the defendant Garlow had assisted the Mills family in structuring what was intended to be a tax-free real estate transaction; Garlow subsequently prepared the Mills' tax return for 1982 based on the tax advantages connected with that transaction. In March 1985, the IRS notified the Mills that it would be auditing their 1982 return. The examiner proposed that the real estate transaction in question was not entitled to tax-free treatment and therefore that the Mills owed approximately $6,600 more than they had paid to the IRS.

The Mills filed a protest with the IRS appeals office which was later denied. In December 1986, the Mills entered into an agreement with the IRS and were subsequently billed for the unpaid tax, including interest. Less than one year

---

30/ (...continued) statutory notice of deficiency and not date on which Tax Court upholds IRS deficiency determination). Cf. Chisholm v. Scott, 86 N.M. 707, 526 P.2d 1300 (Ct. App. 1974) (holding four-year limitations period begins to run upon issuance of statutory notice of deficiency and not at time when tax return at issue was prepared).

31/ Peat Marwick recognizes that in Mills the taxpayers brought their malpractice suit within the limitations period which began to run on issuance of the 90-Day Letter. However, the principle stated in Mills -- identical to that stated in Feldman -- is on all fours with the instant case.

later, the Mills filed a negligence action against the accountant who had structured the transaction and prepared their return.

The statute of limitations at issue in Mills is similar to Florida's, prescribing a two-year limitations period which begins to run, at the latest, when the claimant discovers or should discover a cause of action for professional malpractice has accrued in his favor. The opinion contains an extensive discussion of IRS procedures as well as a discussion of accounting malpractice decisions from other jurisdictions. Relying on the nature of the IRS procedures for handling tax deficiency issues and the persuasive authority from these other jurisdictions, the Wyoming Supreme Court concluded that discovery of such a cause of action would not occur in the tax context until the parties agreed to the deficiency proposed by the IRS (as the Mills had) or, at the latest, upon issuance of the 90-Day Letter. Mills, 768 P.2d at 557. The court found that any reasonable taxpayer would know at such a time that he had a cause of action. In addition, such a rule provides certainty and comports with the policy against stale claims. Id.

C. Commencement Of The Running Of The Statute Of Limitations On Issuance Of The 90-Day Letter Imposes No Burden On The Judicial System.

It has been argued that commencement of the running of the statute of limitations on issuance of the 90-Day Letter will cause the filing of needless lawsuits when the taxpayer might later be vindicated in Tax Court. This argument as phrased has no legal validity since the statute of limitations is a legislative determination which must be followed whether or not it inconveniences the administration of the judicial system.

Yet, the argument itself is specious in several respects. First, rather than challenging the 90-Day Letter in Tax Court, the taxpayer instead may elect to pay the asserted deficiency and sue for a refund in federal district court or the United States Claims Court. By paying the deficiency plus accrued interest and penalties, the taxpayer suffers injury. He also sustains injury when he undertakes the expense of a refund action. That the court may later hold the IRS determination erroneous and refund the payment is of no consequence.

Second, the taxpayer can always seek his accountant's consent to toll the statute until the Tax Court proceeding or any appeals therefrom are concluded. The accountant might well agree rather than suffer the expense and any adverse publicity from a lawsuit.

Finally, a decision of the Tax Court, whether upholding or striking down the deficiency set forth in the 90-Day Letter, does not necessarily decide the ultimate question of the accountant's negligence. The Tax Court proceeding focuses not on the conduct of the accountant, but rather on the correctness of the IRS' determination.

D. This Court Should Adopt The Accepted Rule That A Cause Of Action For Accounting Negligence Accrues -- And Thus The Statute Of Limitations Begins To Run -- On Issuance Of The 90-Day Letter And Not When The Taxpayer Has Exhausted All Avenues Of Review.

All jurisdictions applying the discovery rule to the running of the statute of limitations that have considered the very issue facing this Court have determined that the latest point at which a taxpayer could reasonably be said to discover his accountant's negligence is on issuance of the 90-Day Letter. Such a rule comports with the clear language of Sections 95.031 and 95.11(4)(a), Florida Statutes (1987). The first section provides that the limitations period begins to run "from the time the cause of action is <u>discovered or should have been discovered</u> with the exercise of due diligence" (emphasis added). The second states that the "cause of action accrues when the last element constituting the cause of action occurs." Clearly, when circumstances make it apparent that an accountant's error has prompted the IRS to challenge the taxpayer's return as understating the tax actually due and owing, then logic compels the conclusion that there must be "discovery" of a malpractice action within the meaning of the statute. Because that "discovery" is coupled with injury (the unpaid taxes, accrued interest and penalties), the cause of action has accrued. The 90-Day Letter provides both the "discovery" and the "injury." A rule which would require that a taxpayer pursue all available avenues of review -- in Tax Court and even to the Federal Circuit and possibly the United States Supreme Court (or, in the alternative, in a federal district court or United States Claims Court refund action and then through appellate channels) -- before it properly can be said that the taxpayer has discovered or should have discovered that a cause of action has accrued in his favor abrogates the effect of the language chosen by the legislature.

III. EVEN IF THIS COURT FINDS THAT THE LIMITATIONS RULE GOVERNING ACTIONS FOR ATTORNEY NEGLIGENCE ALSO APPLIES TO ACTIONS FOR NEGLIGENCE WITH RESPECT TO FEDERAL TAX MATTERS, THE RUNNING OF THE LIMITATIONS PERIOD BEGINS ON ISSUANCE OF THE 90-DAY LETTER.

A. Under Edwards v. Ford, The Statute Of Limitations Begins To Run On A Cause Of Action For Attorney Negligence When The Plaintiff Knows Or Should Know That A Cause Of Action Has Accrued In His Favor.

This Court has spoken most recently on the running of the limitations period for attorney malpractice actions in Edwards v. Ford, 279 So.2d 851 (Fla. 1973). In that case, the Edwards had hired attorney Ford in connection with the preparation of a purchase and leaseback agreement for use in a transaction with a manufacturing company. In March 1963, several months after the parties executed the agreement, attorneys for the manufacturing company advised the Edwards that the contract was probably voidable as usurious. A member of Ford's firm then offered to correct whatever problem might exist free of charge. The company subsequently sued the Edwards seeking to have the contract set aside as usurious. The trial court held for Ford and the Edwards appealed. That appeal and two other lawsuits arising out of disputes concerning similar contracts Ford had prepared, eventually settled.[32/]

In 1968, Ford's law firm sued the Edwards for unpaid legal fees with respect to the defense of the three contract actions. The Edwards counterclaimed for legal malpractice. The trial court dismissed the counterclaim on the basis that it was barred by the statute of limitations, finding that the limitations period began to run at the time the attorney performed the services.

This Court rejected the trial court's rule as too harsh. It reasoned that a client normally would not possess the legal skill and knowledge sufficient to evaluate when his attorney might have committed an act of negligence. The Court instead found that the triggering event for limitations purposes is notice to the claimant that he has a cause of action for negligence. Edwards, 279 So.2d at 853, citing Downing v. Vaine, 228 So.2d 622 (Fla. 1st DCA 1969), appeal dismissed, 237 So.2d 767 (Fla. 1970). That notice occurred when opposing counsel in the purchase-leaseback transaction cautioned the

---

32/ In one of the two other suits, the Second District found the contract to be usurious.

Edwards that the contract Ford had prepared was possibly unenforceable, and a member of Ford's law firm offered to correct the problem. Because the Edwards then knew or at least should have known that a cause of action against Ford had accrued in their favor, their claim brought roughly five years later was time-barred.

1. <u>This Court in Edwards held that a cause of action accrues for attorney negligence when any damage, however slight, is sustained as a result of such negligence.</u>

In <u>Edwards</u>, this Court concluded that any damage, however minimal at the time the negligence is discovered, will suffice. <u>Edwards</u>, 279 So.2d at 853. The warning to the Edwards by opposing counsel and the offer of free corrective legal service by Ford's partner represented the relevant point in time. No lawsuits against the Edwards had been filed yet, but it was at that very point that the Edwards could have had their contract set aside as illegal, and, as a consequence, could have sued their attorneys for malpractice. Although this Court did not expressly describe what the damages were, the opinion suggests that the mere exposure to liability the negligently prepared contracts represented was sufficient.

2. <u>This result obtains despite the fact that a plaintiff may take subsequent measures to reduce the amount of such damages or that the precise amount of damages has not been ascertained.</u>

This Court has held repeatedly in various contexts -- just as it implied in <u>Edwards</u> -- that subsequent efforts to reduce the amount of damage sustained as a result of such negligence are immaterial to the running of the limitations period. So, too, is the inability to ascertain the precise amount of damages at the point of discovery. Because the moment of discovery is the operative point in time, by exhausting available avenues of review in an effort to remedy the effects of the negligence, the client is in no way affecting whether he has a cause of action for malpractice.

For example, in <u>Kelley v. School Board of Seminole County</u>, 435 So.2d 804 (Fla. 1983),[33/] the school board had contracted with Kelley to design and construct a number of elementary schools. Shortly after the project was completed, the roofs on each of the schools began to leak and continued to leak despite extensive repairs undertaken over the next several years.

33/ <u>Kelley</u> involved the four-year statute of limitations applicable to actions for construction defects, Section 95.11(3)(c), Florida Statutes, rather than the two-year limitations period for professional malpractice in Section 95.11(4)(a). However, the two provisions are identical with respect to the relevant standard; in both, the period commences from the time the cause of action "is discovered or should have been discovered with the exercise of due diligence."

This Court rejected a "continuous treatment" doctrine. Instead, this Court held the school board "knew something was wrong" almost seven years before it brought suit, subsequent attempts to repair the problem notwithstanding, and "[t]his knowledge meets the discovery aspect" of the statute. Kelley, 435 So.2d at 807. The full amount of damages had not been sustained when the leaks first appeared, yet the limitations period nevertheless had begun to run.[34/]

The district courts of appeal generally have declined to apply the rule this Court established in Edwards. Only the First District in Kellermeyer v. Miller, 427 So.2d 343 (Fla. 1st DCA 1983), and arguably the Second District in Sawyer v. Earle, 14 F.L.W. 413 (Fla. 2d DCA Feb. 17, 1989), have followed Edwards.[35/] More frequently, the district courts have failed, without explanation, to apply Edwards, despite the fact that Edwards should be the controlling authority. Instead, they generally have held a cause of action for attorney negligence accrues only after the claimant has exhausted all

---

34/ See also Seaboard Air Line Railroad Company v. Ford, 92 So.2d 160, 164-65 (Fla. 1955) (in action under Federal Employer's Liability Act for injuries from occupational disease, holding that first manifestation of disease starts running of limitations period); City of Miami v. Brooks, 70 So.2d 306, 308 and 309 (Fla. 1954) (in action against city hospital for excessive x-ray treatment, finding key to be notice of the act, rather than the full extent of injury flowing from it, to put plaintiff on notice of "his right to a cause of action" and thus trigger running of limitations period).

35/ The Third District Court of Appeal below certified its decision to be in conflict with Sawyer. However, this Court has declined to hear the appeal in Sawyer because the jurisdictional papers were not timely filed.

avenues of review and a final adverse judgment has been entered on the underlying claim. The opinions are contradictory and confusing and usually fail to cite to or distinguish Edwards. A survey of some of the district court decisions is therefore useful.

First District

In Kellermeyer, the First District held a legal malpractice action barred by the statute of limitations when the client filed his malpractice claim long after he incurred damage and suspected his attorney's negligence may have been the cause. There, the court found Kellermeyer had suffered legally cognizable injury the moment his mortgagor diverted other loan funds and impaired Kellermeyer's security interest as second mortgagee. The court rejected as immaterial the fact that Kellermeyer's damage could not be quantified at that point. Kellermeyer, 427 So.2d at 346. The court also rejected the argument that Kellermeyer's suit to have the first mortgage set aside changed the analysis, characterizing such conduct as merely "an attempt to mitigate damages already sustained." Id. at 347. See also Freel v. Fleming, 489 So.2d 1209 (Fla. 1st DCA 1986) (on motion to dismiss, citing Edwards for discovery rule and finding on facts before it that discovery of cause of action had not been conclusively established).

Second District

The Second District in Sawyer v. Earle relied on Kellermeyer to find another attorney malpractice claim time-barred. Sawyer allegedly lost income due to his attorney Earle's alleged malpractice and was forced to hire a second attorney to represent him in disciplinary proceedings before the Florida bar. The court found Sawyer sustained damage at that moment -- and should have discovered his claim -- well before this Court finally suspended Sawyer from the practice of law. Sawyer's inability to determine the full extent of his damages was immaterial. Sawyer, 14 F.L.W. at 414, citing Kellermeyer, 427 So.2d at 346. To hold otherwise, reasoned the court, would contravene the very language of Section 95.11(4)(a). Sawyer, 14 F.L.W. at 414.

Since Sawyer, however, the Second District has muddied the issue somewhat. In Zakaks v. Broida and Napier, P.A., 14 F.L.W. 1356 (Fla. 2d DCA June 9, 1989), Napier allegedly had failed to obtain settlement authority from his clients, the Zakaks, before making a settlement offer to the plaintiff in the personal injury action brought against them. In the Zakaks' subsequent malpractice action against Napier, the Second District -- without citing or distinguishing Edwards -- held the cause of action for malpractice accrued only when the trial court entered a final judgment against the Zakaks. Before then, reasoned the court, although the Zakaks' "liability was probably fixed" at the time of the trial court's order enforcing the settlement offer, their liability "did not become a confirmed fact until the entry of final judgment." Zakaks, 14 F.L.W. 1356. Only at that time did the Zakaks have a "matured cause of action." Id. The Second District referred to the exhaustion rule, yet, the language of the opinion suggests that, in the Second District's view, a cause of action can be discovered at some earlier date.

Third District

The Third District in Birnholz v. Blake, 399 So.2d 375 (Fla. 3d DCA 1981), held no cause of action for attorney malpractice had accrued until the underlying collection suit against a third party was completely disposed of. There, although the original lawsuit to collect unpaid fees was dismissed for want of prosecution, a second suit seeking similar relief was still pending. At that point, reasoned the court, the client had suffered no damages. The court cited Edwards for the discovery rule, yet stated that no cause of action existed until exhaustion. Birnholz, 399 So.2d at 377-78.

The Third District had an opportunity to reject the exhaustion rule four years later, but again adhered to it, this time without citing Edwards. In Chapman v. Garcia, 463 So.2d 528 (Fla. 3d DCA 1985), Chapman's attorney had permitted the statute of limitations to expire in a medical malpractice action he brought on her behalf. The legal malpractice action against the attorney was filed before the trial court in the underlying case had ruled on motions asserting the limitations defense. As long as the tort claim against Chapman's doctor remained viable, reasoned the Third District, no cause of action for attorney malpractice would accrue. Chapman, 463 So.2d at 529.

Similarly, again without citing to or distinguishing Edwards, in Diaz v. Piquette, 496 So.2d 239, 240 (Fla. 3d DCA 1986), rev. denied, 506 So.2d 1042 (Fla. 1987), the Third District required exhaustion before a cause of action for legal malpractice would accrue. Until then, said the court, the results of the attorney's conduct -- voluntarily withdrawing witnesses without an offer of proof[36/] -- are merely "temporary" and there is no "redressable harm." Diaz, 496 So.2d at 240.[37/]

Two years later in Haghayegh v. Clark, 520 So.2d 58 (Fla. 3d DCA 1988), the Third District again found exhaustion to be the key, also without citing to or distinguishing Edwards. There, Clark had failed to file a timely notice of his client's

---

36/ Diaz v. Rodriguez, 384 So.2d 906 (Fla. 3d DCA 1980) (decision in underlying lawsuit).

37/ Diaz v. Piquette was cited with approval in dicta in Breakers of Fort Lauderdale, Ltd. v. Cassel, 528 So.2d 985 (Fla. 3d DCA 1988). There, Breakers' attorney had failed to settle a lawsuit, forcing Breakers eventually to pay more than the amount contained in the unconsummated settlement. Although stating a cause of action had accrued the instant the attorney's error forced Breakers to incur the expense of having to continue to defend a lawsuit, the court distinguished the situation before it from the type of situation found in Diaz. In Diaz, which the court said was correctly decided, no injury occurred -- and thus no cause of action accrued-- until the loss at trial was "made final on appeal." Breakers, 528 So.2d at 986.

intent to exercise a real estate option. In Haghayegh's malpractice action against Clark, the Third District concluded that the limitations period on Haghayegh's claim did not begin to run until the appeals court held that his real estate option had expired.[38]

The Third District's latest decision is in the instant case.

Fourth District

The Fourth District has not addressed the limitations issue in the legal malpractice context in any substantive way. However, in Schetter v. Jordan, 294 So.2d 130 (Fla. 4th DCA 1974), the Fourth District cited Edwards for the discovery rule, but held on the facts before it that a factual issue existed as to when the client had discovered his attorney's alleged malpractice, thereby precluding summary judgment.[39]

Fifth District

The Fifth District has attempted to distinguish Edwards to justify its departure from Edwards' rule. In Adams v. Sommers, 475 So.2d 279 (Fla. 5th DCA 1985), the Fifth

---

38/ The court's proposition that the amount of damages must be determined before a cause of action will lie is clearly erroneous in light of this Court's repeated holdings. See Kelly, 435 So.2d 804; Edwards, 279 So.2d at 853; City of Miami, 70 So.2d at 308.

39/ See also Green v. Adams, 343 So.2d 636 (Fla. 4th DCA 1977), cert. denied, 353 So.2d 673 (Fla. 1977).

District considered dispositive the attorney's assurances to the client that an appellate court would uphold the satisfaction of mortgage he had prepared for her. Such assurances created an issue of fact as to when a cause of action for attorney malpractice can be said to have accrued. Because the clients in Edwards received no such assurances -- with their counsel actually admitting the possibility of error -- Edwards could not control, said the court. Adams, 475 So.2d at 281.

In Richards Enterprises, Inc. v. Swofford, 495 So.2d 1210 (Fla. 5th DCA 1986), dismissed without opinion, 515 So.2d 231 (Fla. 1987), the Fifth District again concluded that no malpractice claim had accrued until the appellate court shut the door. There, Richards lost a foreclosure suit on the ground that the original transaction Swofford had prepared was fraudulent. In Richards' subsequent malpractice action against Swofford, the Fifth District held -- without acknowledging Edwards -- that Richards' malpractice claim did not accrue until Richards had lost on appeal. Richards Enterprises, Inc., 495 So.2d at 1211.

* * * *

This Court need not reach the continuing validity of Edwards for attorney malpractice if it accepts the rule of all other jurisdictions with respect to the running of the limitations period on accounting malpractice actions. However, if this Court does decide the standard for attorney malpractice should apply to accounting malpractice, then this Court should reaffirm the rule of Edwards and, if necessary, clarify the rule for the edification of the district courts.

B. This Court Should Reaffirm The Edwards Rule And Reject The Contrary Rule Of The Court Below That A Cause Of Action For Attorney Negligence Does Not Accrue Until A Final Adverse Judgment Has Been Entered On The Underlying Claim.

Application of the Edwards rule to the instant case is an easy task. Under Edwards, a cause of action accrues when any damage occurs. The limitations period then begins to run when the claimant discovers or should have discovered his cause of action. Here, the 90-Day Letter to Taxpayers provided both the damage -- thereby completing the cause of action for asserted accounting negligence -- and the opportunity for discovery of their claim. The existence of injury to Taxpayers is clear, although, ironically, it was less so with the clients in Edwards.

What is significant about the post-Edwards cases in the district courts is those courts' repeated refusal to accept the fact that some damage has been sustained even before the client has exhausted his avenues of appellate review on the underlying claim. The cases assume, incorrectly, that no malpractice claim could have been brought before such exhaustion occurred. But, for example, in Haghayegh, the client sustained injury when the trial court determined that his real estate option had expired because his attorney had failed to file the required documents in a timely manner. So, too, did the client in Richards Enterprises, Inc. when the lower court refused to allow Richards to foreclose on the mortgage. In these and every other instance cited above, the client faced the following dilemma: (i) either accept the initial adverse outcome, entailing monetary, reputational or other injury, or (ii) expend money and other resources in an attempt to secure a favorable outcome on appeal or other means of review. The client thus not only sustains some injury before any exhaustion occurs,[40/] but also must have notice at that time that he may have a malpractice claim.

1. The rule espoused by many post-Edwards district court cases, requiring exhaustion of all avenues of review before a cause of action for legal malpractice can be said to accrue, directly contradicts the language of Section 95.11(4)(a), Florida Statutes.

The district court cases which decline to follow Edwards directly contravene the edict of Section 95.11(4)(a), Florida Statutes. That section provides that the limitations period begins to run when the cause of action is "discovered or should have been discovered with the exercise of due diligence." A cause of action exists when the client discovers or should have discovered his attorney may have been negligent,

---

40/ See, e.g., Breakers of Fort Lauderdale, Ltd., 528 So.2d at 986 (finding damage occurred and cause of action accrued "the moment [the client] was called upon to incur the expense of having to continue to defend against a lawsuit that should have been settled but for its attorney's alleged malpractice") (dictum).

and incurs some damage as a result of that perceived negligence. The district court decisions which have failed to follow Edwards ignore the fact there is damage at the moment the client is forced to decide whether to accept an adverse judgment of a trial court or an adverse transaction outcome, on the one hand, or to expend money and other resources seeking to have that adverse judgment or outcome set aside. With either option, an interest of the client has been impaired. Quite simply, the client is in a different position than the one in which he would have been but for the assertedly negligent conduct of his counsel.

2. An exhaustion rule effectively abrogates the Legislature's express intent to encourage the speedy resolution of professional malpractice claims and constitutes an impermissible judicial attempt at policymaking.

The discovery rule represents a legislative effort to ameliorate the harshness of a rule requiring that the limitations period begin to run at the instant the negligent act occurs. With professional malpractice, there often is a time lag between the act of professional negligence and any resulting detectable injury. However, in balancing the equities, the Legislature has also imposed on the client the obligation to use diligence in order to discover such negligence. The statute does not condone delay in bringing suit when the client should have known earlier that a cause of action had accrued in his favor.

The post-Edwards decisions requiring exhaustion of remedies before a cause of action will have accrued and the limitations period will begin to run permit litigants to delay bringing any malpractice action for an indeterminate period of time, although a client may know or should have known earlier that a cause of action for malpractice had accrued in his favor. Such an approach contravenes not only the language of Section 95.11(4)(a) but also its spirit. The Legislature has made its intent clear and it is not for the judiciary to alter that plan.

3. An exhaustion rule contravenes logic and public policy.

Logic compels the conclusion that the exhaustion rule adopted by many of the post-Edwards decisions cannot stand. Many of these decisions are grounded on the faulty assumption that had the initial adverse ruling on the underlying claim been reversed, there would have been no cause of action for legal malpractice. This assumption, which the Third District applied below, is erroneous. First, it ignores the fact that the client clearly has already sustained some damage, albeit likely an indeterminate amount, which, under Edwards and other decisions of this Court, is sufficient to render a cause of action complete. Second, reversal on appeal of an initial adverse judgment or outcome does not necessarily clarify the ultimate question of whether the attorney was negligent. Reversal may reflect only that the lower court judge may have erred, or that there was a failure of proof or some similar unrelated error. Furthermore, the post-Edwards decisions adopting the exhaustion rule do so in defiance of the doctrine of stare decisis and its underlying policies of certainty, clarity and predictability.

If the client so desires, nothing should preclude him from simultaneously pursuing both a malpractice action and an appeal of the initial adverse judgment or outcome. To pursue both would promote judicial economy by segregating the issues to be decided into the appropriate forum, while conforming to the legislative intent. If need be, the malpractice action could be held in abeyance pending the outcome of the appeal.[41/]

C. Edwards Thus Requires That The Two-year Statute Of Limitations For Professional Malpractice Actions In Florida Begins To Run On Claims For Negligence With Respect to Federal Tax Matters On Issuance Of The 90-Day Letter By The IRS.

Under the rule of Edwards, the limitations period begins to run when the taxpayer knows or should know that a cause of action for accounting negligence has accrued in his favor. A cause of action for malpractice accrues when any damage, however slight, is sustained as a result of such negligence. Issuance of the 90-Day Letter, containing the

41/ As noted above, a tolling agreement could be reached between attorney and client if they mutually decided, as well they might, that such an agreement would be useful.

IRS' conclusive determination that the taxpayer has underpaid his federal income tax, constitutes such damage. Accordingly, it is at that time that the taxpayer should know, if he does not already, that his accountant may have erred.

A taxpayer's subsequent attempt to challenge the deficiency in Tax Court and beyond is merely an effort to mitigate damage already sustained. Edwards and other decisions of this Court in numerous contexts make clear that the amount of damage initially suffered is immaterial. Instead, it is the very fact that some damage has occurred which determines the accrual of the cause of action, notice of such cause of action, and thus the running of the statute of limitations.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the Third District Court of Appeal and reinstate the judgment of the Circuit Court granting summary judgment in favor of Peat Marwick.

THOMSON MURARO BOHRER & RAZOOK, P.A.

Karen Kammer

Parker D. Thomson
Karen Williams Kammer
2200 One Biscayne Tower
2 South Biscayne Boulevard
Miami, Florida 33131
(305) 350-7200

Attorneys for Peat, Marwick, Mitchell & Co.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true copy of the foregoing Initial Brief of Petitioner Peat, Marwick, Mitchell & Co. was served by mail this 14th day of June, 1989, upon the following:

Shelley H. Leinicke
Wicker, Smith, Blomqvist, Tutan,
O'Hara, McCoy, Graham & Lane
Barnett Bank Plaza, Fifth Floor
One East Broward Boulevard
Post Office Box 14460
Fort Lauderdale, Florida 33302

Karen Kammer

6655.205-16.06
061489