
Legal Updates & News

Legal Updates

Second Circuit Decision “Squarely Holds” Accountants May Be Primarily Liable Under Federal Securities Laws

February 2007

Related Practices:

- [Litigation](#)
- [Securities Litigation, Enforcement and White-Collar Defense](#)

In a decision issued yesterday, the Second Circuit held that an accountant has a duty to correct its certified opinions, and may incur primary liability under § 10(b) and Rule 10b-5 if it fails to fulfill that duty in certain circumstances. The decision, written by C.J. Straub, claims to be the first in this Circuit to squarely hold that an accountant has such a duty or may be primarily liable under federal securities laws. The auditor in this case is Todman & Co., CPA, P.C., and its successor in interest, Trien, Rosenberg, Rosenberg, Weinberg, Ciullo & Fazzari, LLP.

The decision, *Overton v. Todman & Co., CPAs, P.C.*, No. 06-2496-cv, reversed a lower court decision dismissing a securities fraud claim against Todman & Co. Plaintiffs alleged that from 1999 through 2002, Todman & Co. issued opinions certifying that the financial statements of a broker-dealer accurately reflected the broker-dealer's fiscal health. But the auditor, Plaintiffs alleged, failed to correct those opinions, ignoring warning signs that the broker-dealer's financial statements understated its liability for payroll taxes. Plaintiffs alleged that, in 2003, the broker-dealer's payroll tax liability led to the broker-dealer's collapse.

After surveying its prior law on accountants' primarily liability, the Second Circuit ruled that the District Court erred in dismissing the fraud claim against Todman & Co. The Second Circuit acknowledged that only in dicta did its previous opinions attribute to accountants a duty to correct certified opinions. "Presented with the opportunity to do so," the Second Circuit's *Overton* opinion "squarely" holds that "an accountant violates the 'duty to correct' and becomes primarily liable under § 10(b) and Rule 10b-5 when it (1) makes a statement in its certified opinion that is false or misleading when made; (2) subsequently learns or was reckless in not learning that the earlier statement was false or misleading; (3) knows or should know that potential investors are relying on the opinion and financial statements; yet (4) fails to take reasonable steps to correct or withdraw its opinion and/or the financial statements; and (5) all the other requirements for liability are satisfied."