



Federal Securities Law Forum: Accountant Liability Trends

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Accountants' Liability

- **Private Securities Litigation**
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 - Section 11
- **SEC Developments**
 - *Jarkesy* impact on enforcement
 - SEC Enforcement Developments
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The Audit Report Generally

The Audit Report

- The Audit Report is the only statement made by the auditor.
 - The Audit Report accompanies the financial statements, but, the financial statements are the responsibility of management and are issued by the Company.
 - Auditors are not liable for the statements of the issuer.
 - The arguments surrounding whether auditors are liable for alleged misstatements in the Audit Report hinge on whether the audit report is a protected statement of opinion.

The Audit Report – AS 3101 Elements of “Report of Independent Registered Public Accounting Firm”

- The first section of the Report must contain, among other things:
 - “An opinion that the financial statements present fairly, in all material respects, the financial position of the company as of the balance sheet date and the results of its operations and its cash flows for the period then ended in conformity with the applicable financial reporting framework.” AS3101.08(e)

Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of Apple Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Apple Inc. (the "Company") as of September 28, 2024 and September 30, 2023, the related consolidated statements of operations, comprehensive income, shareholders' equity and cash flows for each of the three years in the period ended September 28, 2024, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company at September 28, 2024 and September 30, 2023, and the results of its operations and its cash flows for each of the three years in the period ended September 28, 2024, in conformity with U.S. generally accepted accounting principles ("GAAP").

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the Company's internal control over financial reporting as of September 28, 2024, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated November 1, 2024 expressed an unqualified opinion thereon.

The Audit Report – AS 3101 Elements of “Report of Independent Registered Public Accounting Firm” (con’t)

- The second section of the Report contains standard statements about the “Basis for Opinion” including:
 - “the financial statements are the responsibility of the company’s management”
 - “that the auditor’s responsibility is to express an opinion on the financial statements based on the audit”
 - “that the audit was conducted in accordance with the standards of the PCAOB”

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

The Audit Report – AS 3101 Elements of “Report of Independent Registered Public Accounting Firm” (con’t)

- “standards require that the auditor plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud”
- Standard statements about the audit, that it provides a reasonable basis for the auditor’s opinion
- A statement that the accounting firm is registered with the PCAOB and is required to be independent

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

The Audit Report – Limitations

- “Since the auditor’s opinion on the financial statements or internal control over financial reporting is based on the concept of obtaining reasonable assurance, the auditor is not an insurer and his or her report does not constitute a guarantee. Therefore, the subsequent discovery that either a material misstatement, whether from error or fraud, exists in the financial statements or a material weakness in internal control over financial reporting exists does not, in and of itself, evidence (a) failure to obtain reasonable assurance, (b) inadequate planning, performance, or judgment, (c) the absence of due professional care, or (d) a failure to comply with [PCAOB] standards.” AS 1015.13.

Section 10(b) of the Exchange Act

Section 10(b)

- A showing that an auditor either lacked a genuine belief that its representations were supported by adequate information or engaged in auditing practices so shoddy that they amounted at best to a “pretended audit” has traditionally supported a finding of liability. In re Suprema Specialties, Inc. Sec. Litig., 438 F. 3d 256 (3d Cir. 2006)

New England Carpenters Guaranteed Annuity & Pension Funds v. DeCarlo, 80 F. 4th 158 (2d Cir. 2023)

- The Court underscored the materiality requirement.
- Found that the failure to adequately allege a link between the alleged misstatement in the Auditor's Opinion and the errors in the Form 10-K was fatal.
- Concluded that “general” statements in the Auditor's Opinion are not enough without detailed allegations about how the auditor's “failure to supervise, review, document and perform in good faith” its audit “would have been significant to a reasonable investor in making its investment decisions.”

- Auditor Dismissed
 - Cesario v. Biocept, Inc., 2025 U.S. Dist. LEXIS 28660, *67 (S.D. Cal. Feb. 18, 2025)
 - The plaintiff failed to allege scienter against the auditor where the alleged misrepresentations related to non-financial information in audited documents and in certain unaudited documents, which exceed the scope of responsibility of an auditor.

2024 and 2025 Scorecard

- Ap-Fonden v. DePaolo, 2025 U.S. Dist. LEXIS 52788 (E.D.N.Y. Mar. 21, 2025)
 - Shareholder class action against audit firm and directors and officers of Signature Bank dismissed after FDIC intervened and challenged plaintiff's standing because of the Succession Clause of the Financial Institutions Reform, Recovery and Enforcement Act, 12 U.S.C. §1821(d)(2)(A).
 - Court recognized Circuit Split. Fourth, Seventh, and Eleventh have held it only applies to derivative claims. First Circuit has held it applies to all shareholder claims. Ninth and Tenth have left open possibility that applies to more than derivative claims.

2024 and 2025 Scorecard

- Auditor Not Dismissed
 - IBEW Loc. 98 Pension Fund v. Deloitte & Touche LLP, 348 F.R.D. 35 (D.S.C. Nov. 12, 2024)
 - Class was certified against auditor where it allegedly made false statements in its audit reports regarding the company's ability to complete a project on time to obtain tax credits and recover costs.
 - The audit report did not explicitly make statements regarding the project. The auditor stated only that the 2015 "financial statements were present[ed] fairly, in all material respects and in accordance with GAAP." Those financial statements allegedly stated that the project was on schedule for a 2021 completion.

Section 11 of the Securities Act

Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension Fund, 575 U.S. 175, (2015)

- To state a Section 11 claim against an auditor for its statement of opinion, Plaintiffs must plead either that the auditor did not “actually hold[]” its opinions at the time it consented to their incorporation by reference into the offering materials, or that the auditor omitted material facts about its inquiry into or knowledge concerning the opinion that made the opinion misleading to a reasonable investor.

Defenses to Section 11 Claims

- An auditor can avoid section 11 liability by showing it complied with applicable principles.
- An auditor can avoid liability if the challenged statements are opinions versus embedded facts or disclaimers, and plaintiff fails to show the auditor did not honestly believe its opinion.
- Slack Technologies, LLC v. Pirani (2023), Supreme Court held that plaintiffs must plead and prove that they bought shares registered under that registration statement.
 - On February 10, 2025, the Ninth Circuit ruled in favor of Slack.
 - Unclear whether SEC proposals to revive Section 11 claims will move forward.

- Auditor Not Dismissed

- Glenmede Trust Co., N.A. v. Infinity Q Capital Mgt. LLC, 2024 N.Y. Misc. LEXIS 535 (U.S. Dist. LEXIS 28660, *67 (N.Y. Cty. Supr. Jan. 31, 2024)
 - Motion to dismiss denied where Plaintiff alleged a number of red flags, the omission of which would render the audit opinion materially misleading.
 - Plaintiff alleged that the auditor "had access to [] counterparties' valuations" of positions in funds, "ignored that Infinity Q's valuations were significantly higher than the counterparties' valuations", "actually was aware of these disparate valuations", but disregarded them.

SEC Enforcement Developments

Before Summer of 2024, There Was Increased Scrutiny on Auditors

- In 2023 Chair Gary Gensler and Chief Accountant Paul Munter issued a series of statements focused on auditors:
 - 3/17/23 – Paul Munter, Chief Accountant – Responsibilities of Lead Auditors to Conduct High-Quality Audits When Involving Other Auditors
 - 8/25/23 – Paul Munter, Chief Accountant – The Importance of a Comprehensive Risk Assessment by Auditors and Management
 - 10/25/23 – Chair Gary Gensler – “Partners of Honest Business and Prosecutors of Dishonesty”; 2023 Securities Enforcement Forum

Expanded Enforcement

- Engagement Quality Review (EQR) Partner
- Firms for internal control issues
- National office partners
- Changes to confirmation process

The Increased Scrutiny on Auditors Appears to Have Waned

- In the Summer of 2024, the U.S. Supreme Court in *SEC v. Jarkesy*, held that SEC ALJ proceedings violate a respondent's Seventh Amendment right to a jury trial when the SEC uses the ALJ forum to adjudicate claims that are "legal in nature," *i.e.*, fraud and other claims imposing civil penalties.
- *Jarkesy* did not address the constitutionality of non-monetary sanctions limiting practice before the commission under Rule 102(e). Other challenges are pending.
- Between August through November of 2024, the SEC dismissed seven Rule 102(e) proceedings against accountants.

Rule 102(e)

- May be denied privilege to appear or practice if found to have engaged in “improper professional conduct”, which means:
 - Intentional or knowing conduct, or
 - Either of two types of negligent conduct:
 - Single instance of highly unreasonable conduct.
 - Repeated instances of unreasonable conduct.

- The term “repeated” may encompass as few as two separate instances of unreasonable conduct occurring within one audit, or separate instances of unreasonable conduct within different audits.

Section 17

- **Negligence-Based Fraud in the Offer or Sale of Securities in violation of Sections 17(a)(2) and (3)**
 - 17(a)(2): It shall be unlawful for any person in the offer or sale of any securities . . . directly or indirectly – to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading
 - 17(a)(3): It shall be unlawful for any person in the offer or sale of any securities . . . directly or indirectly – to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 17

- The SEC has successfully used Section 17 recently against a former mutual fund portfolio manager, and an audit firm.
 - *SEC v. Walczak* (W.D. Wisc. 11/22/24) (Jury verdict; ordered to pay \$11.2 million and enjoined from managing or advising on investments for others)
 - *SEC v. Prager Metis* (S.D.N.Y 9/17/24) (Consent judgment as part of settlement; combined disgorgement against two entities of \$3.9 million and civil penalties of \$1 million)

Section 17 - Defenses

- Split of authority, depending on jurisdiction, about whether an auditor's statement that it complied with GAAS is an actionable misstatement.
- SEC must prove that the statement was material to investors.
- Split of authority on how SEC must prove that an auditor "directly or indirectly obtained money or property." – Is regular salary enough?

Thank you.

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