

WHY IS MY ACCOUNTANT SO INTERESTED IN WHERE I LIVE? AN ANALYSIS OF THE RECOVERABILITY OF THE INTEREST PENALTY IN ACCOUNTANT MALPRACTICE SUITS

Courts around the country apply traditional damages principles in almost every type of tort litigation. However, the measure of damages that a successful plaintiff-taxpayer may recover from an accountant, whose negligence in preparing the plaintiff's tax return results in additional monies being owed the Internal Revenue Service ("IRS"), is one area in which traditional damages principles are not applied uniformly. Some jurisdictions award the successful plaintiff the amount of the interest penalty assessed by the IRS for the period between when the tax was owed and when it was paid. Other jurisdictions allow no recovery of the interest penalty. Because of this inconsistency among jurisdictions, forum plays a more significant role in the amount of damages the plaintiff-taxpayer may recover¹ in accountant malpractice suits than should be the case under a system with well-established damages principles.² Depending on the state in which the case is decided, as opposed to the actual injury suffered, taxpayers suing their tax preparers for negligence may or may not be able to recover the interest penalty assessed against them.³

1. Forum can also play a significant role if the plaintiff is a third party not in privity of contract with the accountant. Denzil Y. Causey, Jr., *Accountants Liability in an Indeterminate Amount for an Indeterminate Time to an Indeterminate Class: An Analysis of Touche Ross & Co. v. Commercial Union Inc. Co.*, 57 MISS. L.J. 379, 381 (1987). States holding a "liberal view [that accountants owe a duty to all who could foreseeably rely on the report are] California, Minnesota, Mississippi, New Jersey, Ohio, Wisconsin and one of two Texas jurisdictions." *Id.* at 386-87. Colorado, Florida, Indiana, New York, and a court applying Pennsylvania law all take the position that the accountant's liability ends with his client. *Id.* at 382. Several states adopt the *Restatement (Second) of Torts* approach, which states that accountants only owe a duty of care to those whom the accountant intends the report to influence. *Id.* at 387.

2. There is no statute, either state or federal, that lists the obligations of tax-preparers with respect to their clients. All applicable standards in this area are judicially created. See Phillip E. Hassman, Annotation, *Tax Preparer's Liability to Taxpayer in Connection with Preparation of Tax Return*, 81 A.L.R. 3D 1119, 1122 (1995). However, the tax preparer does have obligations under a variety of criminal statutes. For example, civil penalties may be imposed under 26 U.S.C. § 6701 on persons aiding and abetting the understatement of an individual's tax liability or on tax preparer's who willfully assist in the preparation of returns the accountant knows to be false or fraudulent. 26 U.S.C. § 7206(2) (1994). Any statutory violation that accompanies the negligent preparation of a client's return will be disregarded for purposes of this Note.

3. A taxpayer is obligated to pay interest whenever a tax owed is not paid when due. Section 6601(a) states:

This Note discusses how courts have applied traditional damages principles in this context⁴ and proposes a method that all courts should adopt to correctly apply traditional damages principles in accordance with equity and justice. Part I provides a brief background on the growth of accountant malpractice suits and the elements that must be proved to establish a claim. Part II discusses judicial applications of traditional damages principles in this context. Part III analyzes the applications of these principles and discusses problems with several of the approaches commonly used by courts. Part IV proposes a new analysis that should be applied in accountant malpractice litigation to best serve the interests of both plaintiff-taxpayers and defendant-accountants.

I. BACKGROUND

The number of suits involving taxpayers suing their accountants for malpractice⁵ has risen dramatically⁶ since the 1970s.⁷ Although many professionals have voiced opinions regarding why accountant malpractice litigation in particular⁸ has increased,⁹ a popular reason is the influence of

If any amount of tax imposed by this title (whether required to be shown on a return, or to be paid by stamp or by some other method) is not paid on or before the last date prescribed for payment, interest on such amount at the underpayment rate established under section 6621 shall be paid for the period from such last date to the date paid.

26 U.S.C. § 6601(a) (1994). Section 6621(a) establishes the underpayment rate at the federal short term rate plus three percentage points during the prescribed quarter. 26 U.S.C. § 6621(a) (1994). The interest owed is compounded each day after the deficiency has been assessed, based on tables published by the IRS. Rev. Proc. 83-7, 1983-1 C.B. 583.

4. To prove damage, the plaintiff must show that he would not have suffered a loss if the accountant had prepared the return correctly. GEORGE SPELLMIRE ET AL., ACCOUNTANTS' LEGAL LIABILITY GUIDE § 14.01 (1990). The amount of the damage must be proven with reasonable certainty; although it need not be proven exactly, the amount cannot be based on pure speculation. *Id.* (citing *Wagenheim v. Alexander Grant & Co.*, 482 N.E.2d 955, 967 (Ohio Ct. App. 1983)).

5. The term malpractice is commonly understood to refer to a professional's breach of the standard of care. SPELLMIRE ET AL., *supra* note 4, § 10.02, cited in Howard M. Garfield & Thomas Weathers, *A Survey of Accountant Malpractice: Breach of Contract or Tort?*, in ACCOUNTANTS' LIABILITY 1995, at 271, 273 (PLI Litig. & Admin. Practice Course Handbook Series No. H-526, 1995).

6. The number of malpractice suits brought in the last 15 years is greater than the number of suits brought up to that point in the entire history of the profession. Robert Mednick, *Accountant's Liability: Coping with the Stampede to the Courtroom*, 9 J. ACCT. 118 (1987). Tax practice in particular spawns a greater number of malpractice suits than any other area of accounting practice. Deniz Y. Causey, Jr., *How to Repair Errors That Occur in an Accountant's Everyday Tax Practice*, 39 TAX'N FOR ACCT. 76 (1987).

7. See Causey, *supra* note 6.

8. Accountant malpractice litigation has risen even when compared to other areas of

new standards promulgated by the American Institute of Certified Public Accountants ("AICPA")¹⁰ for professional malpractice.¹¹ The new standards, among other things, extend an accountant's potential liability to third parties where it is reasonably foreseeable that the third party will rely on the accountant's information.¹²

Inconsistency among courts with respect to recoverable damages is one of many rifts in this area.¹³ The existence of such inconsistencies may be attributable to the relative nascency of accountant malpractice litigation, which has led to an absence of common law precedent for courts to follow. Courts differ on such fundamental questions as the elements that the plaintiff must prove to establish both liability and the measure of damages awarded.¹⁴ Courts are divided on issues such as when the statute of limitations is tolled¹⁵

professional malpractice, including medical and legal malpractice. *Id.*

9. Other writers have suggested that additional factors contributing to the increase in accountant malpractice litigation relative to other suits involving professional malpractice include the greater accessibility of accountants' services and materials and the accountant's greater responsibility in the potential detection of fraud. *See, e.g.*, Frank J. Macchiarola, *The Accountant's Liability Controversy*, 1988 COLUM. BUS. L. REV. 177, 180 (1988). Another contributing factor is the frequency of tax code reformations in recent decades. SPELLMIRE ET AL., *supra* note 4, § 5.01. Small and medium sized accounting firms are becoming increasingly susceptible to malpractice claims because they lack the resources necessary to keep up with the current state of the tax code. *Id.*

10. AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS, STATEMENTS ON AUDITING STANDARDS (1988). The AICPA issues guidelines defining acts that are prohibited, recommended, mandatory, discretionary and questionable for accounting professionals. *Id.* Although these standards are not binding on professionals, they can be considered in determining whether a particular accountant has breached a professional duty owed to the client. Brian K. Kirby & Thomas L. Davies, *Accountant Liability: New Exposure for an Old Profession*, 36 S.D. L. REV. 574 n.6 (1991).

11. *See* Mednick, *supra* note 6, at 78.

12. *Id.* *See infra* note 16 for a discussion of the judicial application of the accountant's duty of care to third persons when it is reasonably foreseeable that these parties may rely on the accountant's information.

13. *See infra* notes 14-16 and accompanying text for a discussion of various judicial disputes in the context of accountant malpractice litigation.

14. *See* Denzil Y. Causey, Jr., & Sandra A. Causey, *The Accounting Profession in the Courts*, 12 MISS. C. L. REV. 7 (1991). Compensatory damages are almost always awarded to the successful plaintiff, although the exact amount of compensation varies from case to case. *See* Slaughter v. Roddie, 249 So. 2d 584, 586 (La. Ct. App. 1971) (holding that the plaintiff could not recover attorney's fees unless such compensation was stipulated by contract or statute). Punitive damages may also be awarded where the tax preparer has made false representations about expertise in preparing certain returns. *See* Midwest Supply, Inc. v. Waters, 510 P.2d 876 (Nev. 1973); *cf.* H & R Block, Inc. v. Testerman, 338 A.2d 48, 54 (Md. 1975) (holding that punitive damages were improperly awarded even though the tax preparer had grossly understated the amount of plaintiff's income where the tax preparer had not acted with malice). Courts have also denied a plaintiff's request for damages for mental anguish suffered after the IRS repeatedly badgered the taxpayer for the deficiency owed through a tax preparer's negligence. *See id.* at 55.

15. *See* Ronald E. Mallen, *Limitations and the Need for "Damages" in Legal Malpractice*

and whether auditors may be held liable to third parties who rely on their report of an entity's financial condition.¹⁶

A dispute between the taxpayer and the accountant arises when the IRS issues a deficiency assessment.¹⁷ When a deficiency assessment issued to a taxpayer is due to the accountant's negligence, most taxpayers bring causes of action in tort to recover damages associated with the accountant's breach of professional care.¹⁸ Alternatively, some plaintiffs allege breach of an implied contract¹⁹ when suing the tax preparer. The difference is important because

Actions, 60 DEF. COUNS. J. 234 (1993). Most jurisdictions recognize that the statute of limitations begins to run when all the elements essential to the cause of action, including an actual injury, have been established. *Id.* at 234. The confusion among courts concerns when the injury to the plaintiff occurs. *Id.* at 237. Some courts hold that the statute of limitations is tolled when the tortious conduct occurs, i.e., when the tax preparer breaches a duty of care that causes the taxpayer to incur a liability at law. *Id.* at 241. Where the occurrence of damages is contingent on other events, other jurisdictions do not consider the statute of limitations tolled until the plaintiff should have discovered the negligence. *Id.*

16. In 1987, the Mississippi Supreme Court held that an independent auditor is "liable to reasonably foreseeable users of the audit, who request and receive a financial statement from the audited entity for a proper business purpose, and who then detrimentally rely on the financial statement, suffering a loss, proximately caused by the auditor's negligence." Causey, *supra* note 1, at 379 (citing *Touche Ross & Co. v. Commercial Union Ins. Co.*, 514 So. 2d 315 (Miss. 1987)). However, other jurisdictions limit the accountant's duty of care to clients by requiring third parties to demonstrate an intentional or reckless misrepresentation by the accountant to recover. *Id.* at 380. For a more detailed discussion of the scope of professional liability to third parties as a result of auditing services, see Kirby & Davies, *supra* note 10.

17. A deficiency is assessed when it is recorded with the IRS that a particular taxpayer has underpaid taxes. 26 U.S.C. § 6203 (1994). Section 6212(a) authorizes the IRS to send out notices to taxpayers once a deficiency has been assessed. 26 U.S.C. § 6212(a) (1994). However, an assessment of a deficiency is valid even without notice to the taxpayer. *Id.* There is, however, a more extensive process behind the final issuance of the deficiency assessment. The process begins when the IRS conducts an audit, or any other examination of the plaintiff's books. *Ackerman v. Price Waterhouse*, 591 N.Y.S.2d 936, 941 (Sup. Ct. 1992). If the audit raises questions with the IRS, the Department of Revenue issues a "30-day letter" that contains the specific findings and issues in dispute. *Id.* The party can then appeal to the IRS, which, if denied, results in a final notice of the proposed deficiency, known as the "90-day letter." *Id.* This letter is issued approximately 90 days before the actual deficiency assessment is issued. *Id.* at 942. After that date, a taxpayer can only avoid payment by instituting suit in Tax Court. *Id.*

18. See Garfield & Weathers, *supra* note 5, at 273.

19. "An implied contract, [is] a fiction of the law adopted to achieve justice where no true contract exists . . . the existence and terms of which are manifested by conduct." *Lien v. McGladrey & Pullen*, 509 N.W.2d 421, 423 (S.D. 1993) (citing *Weller v. Spring Creek Resort, Inc.*, 477 N.W.2d 839, 841 (S.D. 1991)). The plaintiff normally alleges that the defendant breached the accountant's implied agreement to operate within the parameters of the standard of care imposed upon members of the profession. SPELLMIRE ET AL., *supra* note 4, § 10.04. The elements of a breach of contract claim and a tort claim are very similar in that the plaintiff must prove duty, breach, causation, and damages. *Id.* § 10.05. The existence of a contract is established either expressly through oral representations or an engagement letter, or by implication. *Id.* A minority of courts hold that malpractice actions can only

tort and contract claims differ both in the elements that the plaintiff must prove²⁰ and in the damages²¹ that may be recovered.²² The scope of this Note is limited to suits that allege negligence on the part of the tax preparer,²³ both because the majority of claims brought against accountants sound in tort²⁴ and because traditional tort damages principles are most commonly applied when resolving the problem.

To prove negligence, the plaintiff must establish that the accountant had a

be brought in tort, and refuse to consider a breach of contract claim alone. *Id.* (citing *Robertson v. White*, 633 F. Supp. 954 (W.D. Ark. 1986)). In *Robertson*, the court stated that contract law insures that both parties get the benefit of their bargain, while the foundation of tort law is to remedy injury to the plaintiff. *Robertson*, 633 F. Supp. at 974. The court refused to entertain a breach of contract claim where the complaint alleged defendant's poor performance, rather than a failure to perform altogether. *Id.*

20. To establish common law breach of contract, the plaintiff must show (1) an agreement between the parties; (2) a failure to perform on at least one of the material terms; (3) the defendant's failure to perform as a cause in fact; and (4) the injuries suffered by the plaintiff. See *Garfield & Weathers*, *supra* note 5, at 273 (citing Kathryn A. Oberly & Melanie T. Morris, *Accountants' Liability in Connection with Failed Financial Institutions*, in *FAILING FINANCIAL INSTITUTION LITIGATION* 261, 276 (ALI-ABA Course of Study Materials, No. C767, 1992)).

21. A plaintiff who successfully brings an accountant malpractice claim in tort may recover all foreseeable damages directly flowing from the accountant's duty of care violation. *SPELLMIRE ET AL.*, *supra* note 4, §§ 14.03-.04, §§ 14.07-.08. In a contract action, the plaintiff's recovery will most likely be limited to the accountant's fees, lost profits, and prejudgment interest. *Id.* It should be noted here that "injury", "damage," and "damages" are not synonymous: Injury refers to the unjustifiable invasion of a legal right; damage is the loss or harm caused by the illegal invasions; whereas damages refers to the compensation awarded for the loss suffered. See *Hanna v. Martin*, 49 So. 2d 585, 587 (Fla. 1950); *Monsanto Co. v. Miller*, 455 N.E.2d 392, 394 (Ind. Ct. App. 1983).

22. There are a number of other differences between actions brought in tort and contract, including the applicable statute of limitations, the unavailability of a contributory or comparative negligence defense in a contract claim, and the ability of a third party to claim that it was an intended beneficiary of an implied contract to surmount the accountant's privity defense. For a more complete discussion of the differences between suits brought in tort and contract, see *Garfield & Weathers*, *supra* note 5.

23. The tax preparer may be subjected to liability for a wide range of actions, including late filing of a return, gross overstatement of the taxpayer's tax liability, gross understatement of income, or misrepresentations about the applicable tax regulations. *Brackett v. H&R Block & Co.*, 166 S.E.2d 369 (Ga. Ct. App. 1969) (accepting plaintiff's allegation that the accountant's gross overstatement of her tax liability forced her to sell her home when denying defendant's motion to dismiss); *Cameron v. Montgomery*, 225 N.W.2d 154, 155 (Iowa 1975) (holding that the accountant's filing of a return four months after the due date constituted negligence); *Bancroft v. Indemnity Ins. Co. of N. Am.*, 203 F. Supp. 49 (W.D. La.), *aff'd*, 309 F.2d 959 (5th Cir. 1962) (allowing recovery where the client relied on the defendant-accountant's erroneous investment advice); *cf. Smith v. St. Paul Fire & Marine Ins. Co.*, 366 F. Supp. 1283, 1286 (M.D. La. 1973) (holding that the taxpayer could not recover when there was no jurisprudence to suggest that the accountant's advice was erroneous at the time it was rendered); *H&R Block v. Testerman*, 338 A.2d 48, 48 (Md. 1975) (holding accountant liable for compensatory but not punitive damages where the accountant was negligent in preparing the plaintiff's taxes).

24. See *Mednick*, *supra* note 6, at 118.

duty to the plaintiff, the duty was breached through lack of care by the defendant, the plaintiff was injured, and the injury would not have occurred but for the defendant's breach of his duty.²⁵ A professional accountant is held to the standard of care of an accountant exercising reasonable professional judgment.²⁶

In the majority of cases discussed in this Note, the plaintiff has already satisfied three elements of the claim: duty, breach and causation. The question that remains to be answered is what injury the plaintiff has suffered from the defendant's failure to exercise reasonable care. Most taxpayers who bring suit seek to recover the fee paid to the accountant for tax preparation services,²⁷ as well as the amount of any penalties assessed against them by the IRS, including the interest penalty.²⁸ Courts almost never allow the plaintiff to recover the amount of the deficiency itself because the taxpayer would have had to pay that amount at the original date of filing even if the accountant had not breached a duty of care when preparing the plaintiff's return.²⁹ However,

25. *Id.*

26. Courts generally agree that accountants do not guarantee that their judgment will be correct or even that their decisions will reflect the best professional judgment possible. Causey & Causey, *supra* note 14, at 20-21 (citing *Delmar Vineyard v. Timmons*, 486 S.W.2d 914, 920 (Tenn. Ct. App. 1972)). Instead, the accountant is obligated to perform to the level of usual care and competence exercised by professionals in the field. *Id.* Courts frequently apply the standard of care enunciated in section 299A of the *Restatement (Second) of Torts*:

Unless he represents that he has greater or less skill or knowledge, one who undertakes to render services in a practice of a profession or trade is required to exercise the skill and knowledge normally possessed by members of that profession or trade in good standing in similar communities.

RESTATEMENT (SECOND) OF Torts § 299A (1979), *cited in* SPELLMIRE ET AL., *supra* note 4, §§ 12.01-.02. This definition highlights the fact that the standard of care depends on the particular community and is measured from a subjective viewpoint of what a reasonable accountant would have done under the same circumstances at the time when the advice was given or the services performed. *Id.* § 12.02.

27. *See, e.g.*, *Orsini v. Bratten*, 713 P.2d 791 (Alaska 1986) (awarding plaintiff both accountant's fees and interest penalty); *Dail v. Adamson*, 570 N.E.2d 1167 (Ill. App. Ct. 1991) (seeking damages equivalent to interest penalty and accountant's fees); *Wynn v. Estate of Holmes*, 815 P.2d 1231 (Okla. Ct. App. 1991) (seeking both interest penalty and accountant's fees at trial level).

28. In addition to the imposition of an interest penalty, *see supra* note 3, the IRS can also impose a negligence penalty for returns filed late or for an inadequate amount where the delay is not justified by reasonable cause. 26 U.S.C. § 6651(a) (1994). The statutory penalty is 5% of the tax owed for the first month, and an additional 5% of the tax for each month thereafter. *Id.* Courts vary on what constitutes reasonable cause sufficient to avoid imposition of the negligence penalty. For example, a taxpayer who knew the due date for his return was not acting with ordinary business care by virtue of the fact that he relied on his accountant to apply for an extension. *Twin City Constr. Co. v. United States*, 515 F. Supp. 767 (N.D. 1981); *cf.* *Burton Swartz Land Corp. v. Commissioner of Internal Revenue*, 198 F.2d 558 (5th Cir. 1952) (holding that a taxpayer's reliance on the advice of his accountant constitutes reasonable cause for failure to file a return).

29. *See supra* note 3.

courts almost uniformly allow the plaintiff to recover the assessed negligence penalty because this is usually an injury to the plaintiff that would not have been incurred but for the defendant-accountant's negligence.³⁰

II. PROBLEM

A. *The Time Value of Money*

The first element to this problem is determining why the IRS assesses an additional amount of money³¹ to compensate for the time between the original filing and when the taxpayer pays the deficiency. The answer lies in the changing value of money over time.³² At any given point in time, an individual or firm can take a particular sum of money and lend it to someone else (i.e., invest it). The lender commonly charges the borrower some fee for the use of the money and to compensate the lender for going without the money for a certain period.³³ This fee is usually fixed at a percentage, known

30. See *supra* note 23.

31. Money is defined as a medium of exchange that has a value which enables consumers to purchase whatever they choose. GEORGE N. HALM, *MONETARY THEORY: A MODERN TREATMENT OF THE ESSENTIALS OF MONEY AND BANKING* 14 (2d ed. 1946). Halm credits money with our ability to operate in a highly structured exchange economy. *Id.* at 2. Because it would take far too long to calculate the relative value of every good sought to be exchanged for another, we use money as a standard "good" which can be estimated in units. *Id.* Actors in the market are able to compare these like units easily in determining a fair price. *Id.* Although the medium of exchange does not have to be the same good as the standard of value (for example one dog could represent the value of four cows), money is used in reference to both the medium of exchange and the standard of value in economic systems as we know them. *Id.* at 3. However, the value of money in the American market is far greater than the value of what it is actually made of. *Id.* at 27. Contrary to a metallic medium of exchange (i.e., gold), paper money is considered token money, as opposed to full-bodied. *Id.*

32. The change in value of money over time must be understood in relation to the factors that determine the value of money at any given point in time. *Id.* at 18. Because goods are bought when individuals spend money, the value of money to any person depends on the sum total of different goods that an individual can obtain with any given sum of money. *Id.* The value of money is the inverse ratio of prices, which is determined by the total amount of money that is spent in a given period of time (the flow of money) in light of a given supply of goods in the market. *Id.* at 19. Halm rejects the hypothesis that the value of money is contingent on the supply of money in the market. *Id.* at 20; cf. CHARLES RIST, *HISTORY OF MONETARY AND CREDIT THEORY FROM JOHN LAW TO THE PRESENT DAY* 337-38 (1940) (stating that it became well established among economists in the nineteenth century that the value of money was contingent on its supply).

33. The concept of lending money on credit took hold when our economy developed from one in which individuals traded finished goods made by handicraft or agricultural goods to an industrial economy—a development which required initial capital for the construction of production operations. KARL H. NIEBYL, *STUDIES IN THE CLASSICAL THEORY OF MONEY* 19 (1946). Capital was needed both to purchase machinery and equipment and to pay laborers until the enterprise saw a return on its investment. *Id.*

as the interest rate.³⁴ Therefore, any given unit of money is worth more at a later point in time than it is today by virtue of the fact that the possessor could have invested that unit of money and earned interest on it. It follows, then, that the IRS charges the taxpayer a fee (i.e., interest penalty) for the taxpayer's use of the money prior to the payment of the deficiency, because the IRS was prevented from using the funds during that time in a way that would have allowed the IRS to earn interest and make a profit.³⁵

B. Interest and the Application of Traditional Damages Principles

Depending on whether they consider the interest penalty as "damage"³⁶ to the plaintiff, courts reach opposite conclusions about a plaintiff's right to recover the interest penalty. Courts that do not allow the plaintiff to recover the interest penalty believe that paying the penalty does not put the plaintiff in worse position than he would have been in if the tax preparer had not been negligent.³⁷ These courts reason that the penalty merely compensates the IRS for the time that it lost the use of the money.³⁸ Utilizing this rationale, plaintiffs actually benefit from the accountants' negligence because they presumably have use of the additional funds until the IRS assesses the deficiency.³⁹ Use of these funds allows the taxpayer to earn interest on the money; interest the IRS would have been able to earn if the return had been prepared correctly.⁴⁰ Therefore, using this rationale, the plaintiff is not injured

34. In nineteenth century America, unreasonable or excessive imposition of an interest rate by a lender resulted in the lender being guilty of the crime of usury. *See* JAMES A. WEBB, A TREATISE ON THE LAW OF USURY §§ 107-137 (St. Louis, F.H. Thomas Law Book Co. 1899). In the early twentieth century, usury laws resulted in the application of caps on interest rates. FRANKLIN W. RYAN, USURY AND USURY LAW: A JURISTIC-ECONOMIC STUDY OF THE EFFECTS OF STATE STATUTORY MAXIMUMS FOR LOAN CHARGES UPON LENDING OPERATIONS IN THE UNITED STATES 1 (1924).

35. For purposes of this section, this Note will not consider the effects of inflation and changes in price on the increased value of money over time. For a more extensive discussion in this area, see ODD AUKRUST ET AL., WORLDWIDE INFLATION: THEORY AND RECENT EXPERIENCE (Lawrence B. Krause & Walter S. Salant eds., 1977). However, the effect of inflation with respect to the injury suffered by the plaintiff will be discussed in the proposal and analysis sections.

36. See *supra* note 21 and accompanying text for the legal definition of damage. In this sense, damage refers to the plaintiff's loss as a result of the defendant's unlawful invasion of a taxpayer's legal right. In the case of accountant malpractice suits, the legal right invaded is the one to have returns prepared correctly by one who holds himself out to be a professional.

37. See, e.g., *Orsini v. Bratten*, 713 P.2d 791 (Alaska 1986); *Alpert v. Shea Gould Climenko & Casey*, 559 N.Y.S.2d 312 (App. Div. 1990).

38. See, e.g., *Orsini*, 713 P.2d 791; *Alpert*, 559 N.Y.S.2d 312.

39. See *infra* notes 84-99 and accompanying text.

40. See *supra* notes 31-35 and accompanying text for the rationale underlying the imposition of the interest penalty.

by paying the interest penalty; he is only required to repay the IRS for a benefit wrongfully gained.⁴¹

Courts that permit the plaintiff to recover the interest penalty posit that often the taxpayer does not invest the money and is therefore not earning interest prior to the issuance of a deficiency assessment.⁴² These courts regard the interest penalty as a payment that would not have been made to the IRS if the tax preparer had not breached the duty to exercise due care.⁴³ The rationale underlying these decisions is that the plaintiff, although theoretically able to gain a benefit from the use of the money, is, from a practical standpoint, put in a worse position by having to pay the interest penalty if he used the money in a way that would not allow him to earn interest on it.⁴⁴

There are several damages principles that courts have commonly applied in developing the common law with respect to the recoverability of the interest penalty. The collateral source rule⁴⁵ stipulates that the damages recoverable from the defendant cannot be offset by any money received by the plaintiffs from a source "wholly independent of and not in behalf of the wrongdoer."⁴⁶ This prevents a defendant from escaping liability when the

41. If the plaintiff has not lost any money as a result of the defendant's negligent preparation of the plaintiff's return then there is no "damage" for which he must be compensated.

42. See *infra* notes 54-85 and accompanying text for judicial opinions that permit the plaintiff to recover the interest penalty. Although taxpayers who do not invest the amount owed to the IRS prior to the deficiency assessment are perhaps foolish, there is no reason why they should be punished for having spent what they believed was their own money in whatever way they choose. Foolishness on the part of the plaintiff cannot amount to contributory negligence, because the plaintiff has no reason to suspect that the money actually is owed to the IRS.

43. See *infra* notes 54-85 and accompanying text.

44. Both courts that award the interest penalty and courts that do not award the interest penalty generally do not consider the influence of inflation on a benefit gained by a taxpayer because the interest penalty is designed to make the value of the deficiency assessment equal today what it did on the original date it was owed.

45. Although the collateral source rule has gained widespread acceptance, a minority of authors criticize its application. See, e.g., Note, *Unreason in the Law of Damages: The Collateral Source Rule*, 77 HARV. L. REV. 741 (1964) (recommending that third parties be allowed to institute recovery actions against tortfeasors to avoid a conflict between damages principles). A minority of states, including Alabama, Louisiana, and New York, have held that the collateral source rule is inapplicable where the injury does not cause a financial loss to plaintiffs to the extent that the payment from a third party places the victims in as good a position as they would be in otherwise. *Id.* Other states distinguish payments made as gratuities and those that resulted from a legal obligation, such as workers' compensation benefits. See, e.g., *McGinley v. United States*, 329 F. Supp. 62 (E.D. Pa. 1971); *Rankin v. Blue Grass Boys Ranch, Inc.*, 469 S.W.2d 767 (Ky. Ct. App. 1971); *Moon v. St. Louis Transit Co.*, 152 S.W. 303 (Mo. 1912).

46. *Burk Royalty Co. v. Jacobs*, 387 P.2d 638, 640 (Okla. 1963). *Burk Royalty* involved an action by landowners against an oil and gas lessee for damage to property as a result of saltwater and oil pollution. *Id.* at 638. The defendant appealed the lower court's exclusion of evidence showing that

plaintiff's family members or friends helped the plaintiff financially prior to trial or the plaintiff is receiving benefits obtained from the legal obligation of a third party.⁴⁷ Policy concerns dictate that the liable defendant should not benefit from the generosity of others or the ingenuity of the plaintiff.⁴⁸

A second principle frequently relied on by courts in accountant malpractice cases is the *Restatement (Second) of Torts*'s benefit rule.⁴⁹ The rule provides:

When the defendant's tortious conduct has caused harm to the plaintiff or to his property and in so doing has conferred a special benefit to the interest of the plaintiff that was harmed, the value of the benefit conferred is considered in mitigation of damages, to the extent that this is equitable.⁵⁰

This principle prevents a plaintiff from being unjustly enriched as a result of any benefits simultaneously gained from the defendant's negligence.⁵¹ Although the harm to a plaintiff may be greater than any benefit conferred, courts believe that any award of damages should only reflect the actual damage suffered by the plaintiff.⁵² The benefit rule incorporates the proposition that the plaintiff should only be put in as good a position as he

the plaintiffs had made a contract with the federal government allowing the government to impose a civil penalty on anyone who knowingly and willfully grazed or harvested any crop from the land subject to the contract. *Id.* at 639-40. The court held that the

[p]laintiffs' compensation by the federal government under the contract is merely compensation from a collateral source. We have many times held that a payment to plaintiffs from a source wholly independent of and not in behalf of the wrongdoer cannot inure to the benefit of the wrongdoer to lessen the damages recoverable from him

Id. at 640.

47. See *infra* note 49 for a discussion of the various third party applications of the collateral source rule.

48. Although the purpose of tort law is limited to compensating a plaintiff for his losses, reducing the damages awarded by the amount of the benefits received by the plaintiff from a third party would result in a diversion of the benefits from the intended beneficiary (the injured victim) to the tortfeasor. Courts generally agree that if one of the parties receives a windfall, it is more just for the injured plaintiff to profit. See, e.g., *Overton v. United States*, 619 F.2d 1299 (8th Cir. 1980); *Grayson v. Williams*, 256 F.2d 61 (10th Cir. 1958); *District of Columbia v. Jackson*, 451 A.2d 867 (D.C. 1982).

49. RESTATEMENT (SECOND) OF TORTS § 920 (1979). The difference between the collateral source rule and the benefit rule is that the former applies to benefits received from third parties and the latter applies to benefits conferred on the complainant by the defendant. See, e.g., *Hume v. Lacey*, 245 P.2d 672 (Cal. Ct. App. 1952).

50. RESTATEMENT (SECOND) OF TORTS § 920 (1979).

51. See, e.g., *Wynn v. Estate of Holmes*, 815 P.2d 1231 (Okla. Ct. App. 1991); *Dail v. Adamson*, 570 N.E.2d 1167 (Ill. App. Ct. 1991).

52. See *Dail*, 570 N.E.2d at 1169.

would have been in if the defendant had not been negligent.⁵³ Courts apply the preceding principles in a variety of situations, and in so doing, reach dramatically different results.

B. Judicial Applications of the Damages Principles

In *Wynn v. Estate of Holmes*,⁵⁴ the Oklahoma District Court awarded the taxpayers the amount of the interest penalty from the estate of their deceased accountant.⁵⁵ The defendant argued that the taxpayers had use of the money from the due date, April 15, 1980, until the IRS assessed the deficiency on December 10, 1984.⁵⁶ According to the defendant, if the taxpayers were allowed to recover the interest penalty, the defendant would be forced to pay the taxpayers despite the fact that they had not suffered an injury.⁵⁷

The court ultimately rejected the defendant's unjust enrichment argument. The court relied on the factual distinction between the case cited by the defendant in support of the benefit rule, *Morris v. Sanchez*,⁵⁸ and the situation before the court in *Wynn*.⁵⁹ In *Morris*, the plaintiffs brought a medical malpractice action against a surgeon, alleging that the defendant negligently sterilized the plaintiff.⁶⁰ Because the procedure was performed incorrectly, the

53. *Morris v. Sanchez*, 746 P.2d 184, 185 (Okla. 1987).

54. *Wynn*, 815 P.2d at 1231.

55. The accountant in this case had prepared both the plaintiffs' personal and corporate returns for several years prior to this suit. *Id.* The plaintiffs were notified that they were the subject of an IRS audit in 1981. *Id.* Accountant-Holmes represented the plaintiffs during the course of the audit. *Id.* The cause of the deficiency was a loss claimed by the defendant on the plaintiffs' return on a small amount of business stock in which they held an interest. *Id.* The figure Holmes used to calculate the stock deduction exceeded the maximum allowable claim under 26 U.S.C. § 1244. *Id.* As a result, the IRS found the plaintiffs deficient in the payment of their taxes for 1979. *Id.* Negotiations with the IRS proceeded for several years, with Holmes and his office assuring the plaintiffs that the debt could be "written off" in other ways. *Id.* at 1232. However, Holmes died during the course of the negotiations. *Id.* The plaintiffs received an IRS proposal, which Holmes's office urged them to accept. *Id.* They received a final deficiency assessment notice of \$47,148.57 in additional taxes and \$36,089.42 in interest. *Id.*

56. *Id.*

57. The defendant offered into evidence an exhibit illustrating the interest that could have been earned on the \$47,148.57 if the money had been placed in certificates of deposit during the four-year period before the final deficiency assessment was issued. *Id.*

58. 746 P.2d 184 (Okla. 1987).

59. *Wynn*, 815 P.2d at 1234. The court also noted that the *Morris* court refused to apply the benefit rule to the situation before it. *Id.*

60. The Oklahoma Supreme Court consolidated the cases of *Rhonda Morris and Michael Morris v. Gabriel Sanchez, M.D.* and *Kathy Stout and Jay Stout v. United States*. Both women gave birth to healthy babies after the sterilization procedures were performed. *Morris*, 746 P.2d at 185.

plaintiff was not actually sterilized and became pregnant after the surgery.⁶¹ Under traditional tort doctrine, the plaintiff argued that she should be allowed to recover the cost of raising the healthy child,⁶² because these costs would not be incurred but for the surgeon's negligence. However, the surgeon argued that if those expenses were recoverable,⁶³ they had to be offset by the benefits the plaintiffs gained from the child's life.⁶⁴

The *Morris* court noted that the majority of jurisdictions do not allow plaintiffs to recover the expense of raising a healthy child as a measure of damages in a wrongful birth case.⁶⁵ The court rejected the benefit rule cited by the defense, noting that the Restatement section on which courts rely for the benefit rule in wrongful birth cases had been criticized as inapplicable in that context.⁶⁶ Specifically, comment b of section 920 of the Restatement does not allow damages of one type of interest to be offset by benefits of another type of interest.⁶⁷ Therefore, the monetary costs incurred in raising a healthy child should not be offset by the emotional benefit the parents' gain in the form of companionship and love during the life of the child.⁶⁸ More

61. *Id.*

62. The court noted that only a minority of jurisdictions analyze the issue of medical malpractice suits involving a breach in the performance of a sterilization procedure under traditional tort principles. *Id.* at 186; *University of Ariz. Health Sciences Ctr. v. Superior Court*, 667 P.2d 1294 (Ariz. 1983) (en banc); *Stills v. Gratton*, 55 Cal. App. 3d 698 (Cal. Ct. App. 1976) (holding that while costs of raising a child are recoverable, offsets for benefits conferred may also be demonstrated).

63. The court held that although the right to undergo the sterilization procedure is protected under the Constitution, the measure of damages flowing from a physician's negligent performance of that procedure is subject to conflicting policy concerns. *Morris*, 746 P.2d at 185-86.

64. *Id.* at 186.

65. *Id.* at 187. The court reviewed de novo whether a plaintiff could recover the costs of raising a healthy child in a negligent sterilization suit, and, if so, whether benefits should be offset against the cost incurred. *Id.*

66. *Id.* at 186.

67. The *Restatement (Second) of Torts* states:

Damages resulting from an invasion of one interest are not diminished by showing that another interest has been benefited. Thus one who has harmed another's reputation by defamatory statements cannot show in mitigation of damages that the other has been financially benefited from their publication (see Illustration 4), unless damages are claimed for harm to pecuniary interests. (See Illustration 5). Damages for pain and suffering are not diminished by showing that the earning capacity of the plaintiff has been increased by the defendant's act. (See Illustration 6). Damages to a husband for loss of consortium are not diminished by the fact that the husband is no longer under the expense of supporting the wife.

RESTATEMENT (SECOND) OF TORTS § 920 cmt. b. (1979).

68. *Morris*, 746 P.2d at 186. However, the benefit rule's roots in the principle of unjust enrichment has led courts to conclude that it would be unfair to rigidly apply the Restatement's "same interest" limitation. *Id.* Courts have supported this position on the grounds that the economic burden and emotional distress associated with raising the unexpected child are so closely related that they can

importantly, the *Morris* court declined to engage in a cost-benefit analysis, stating that policy concerns associated with human life⁶⁹ prevent a court from assigning a monetary value to the benefit gained by the parents from the child's life.⁷⁰

The court in *Wynn* rejected the benefit rule because the facts of *Morris* were too dissimilar to analogize to the accountant malpractice situation.⁷¹ Instead, the court looked to the collateral source rule in upholding the taxpayers' request for interest penalty damages.⁷² The defendant argued that the taxpayers were not injured by the imposition of the interest penalty because the amount had been paid. Although the collateral source rule would prevent the defendant from claiming a credit for money paid to the taxpayers from an independent source, the court doubted whether such an independent fund existed.⁷³ The taxpayers apparently had sufficient funds to pay the amount of money actually owed the IRS at the original due date, but failed to set this money aside.⁷⁴ By the time they became aware of the deficiency assessment, the value of their property had diminished and the taxpayers were

be considered the same interest for purposes of damages. *Id.*

69. The court refused to consider the birth of a healthy child a harm for which damages could be recovered. *Id.* at 187.

70. *Id.* Courts that do not allow the plaintiff to recover the expenses associated with raising a healthy child offer various reasons to support their position, but a common theme that unites them is the sanctity of human life. The court in *Morris* reasoned that if it allowed the benefits gained by the parents from the life of the child to be offset against the cost of raising the child in wrongful birth cases, it would likewise be required to offset the benefit to the parent of not having to raise the child to be offset against the emotional injury suffered to compute damages in wrongful death cases. *Id.* This calculation of the child's death as a benefit to the parent was an impermissible application of the law to the court. *Id.* at 188.

71. *Wynn v. Estate of Holmes*, 815 P.2d 1231, 1234 (Okla. App. Ct. 1991). "[The] primary holding [in *Morris*] is that 'plaintiffs in a medical malpractice action for negligent sterilization may not recover the costs of raising a healthy, normal, but unplanned child as an element of damage.'" *Id.* (quoting *Morris*, 746 P.2d at 189.)

72. *Wynn*, 815 P.2d at 1235. Although the opinion is unclear, the defendant disputed that the plaintiffs suffered an injury from the interest penalty assessment either because the bank had paid the deficiency or because the plaintiffs could have paid the penalty if they had invested their tax savings in interest-bearing funds. *Id.*

73. Although the court did not state its reasons for believing that the bank was not a fund independent of the plaintiff, the court may have relied on the fact that a bank loan does not fall into one of the common sources to which the collateral source rule is applied, namely: gifts, insurance proceeds, pension and retirement benefits, government benefits, and wage continuation benefits. See James P. Mocerri & John L. Messina, *The Collateral Source Rule in Personal Injury Litigation*, 7 GONZ. L. REV. 310 (1972).

74. *Wynn*, 815 P.2d at 1235. The court was persuaded by the plaintiffs' argument that they did not set aside because "there was no reason to do so." *Id.* The defendants assured the plaintiffs throughout the negotiation process that there would be no economic loss to them. *Id.* at 1232.

obligated to borrow money to cover the amount owed to the IRS.⁷⁵ The court reasoned that the defendant should not be able to reduce his liability just because the taxpayers may have been able to pay the amount of the interest penalty from a bank loan or proceeds from investments of the principle amount of the deficiency.⁷⁶

Illinois courts have applied a similar rationale in allowing plaintiffs to recover the interest penalty as a measure of damages from negligent accountants. In *Dail v. Adamson*,⁷⁷ the taxpayer brought suit to recover damages sustained after an Illinois Department of Revenue audit.⁷⁸ The trial court found for the plaintiff and awarded penalties in the amount of \$426 as well as ten percent of the fees the plaintiff paid for the defendant's services.⁷⁹ However, the trial court refused to award the interest assessed by the Illinois Department of Revenue, reasoning that the plaintiffs had use of the money prior to the deficiency assessment.⁸⁰ The lower court felt that attempting to calculate the value of the money to the plaintiffs and offsetting that amount by the amount of the interest penalty would be speculative.⁸¹

75. *Id.* at 1235.

76. *Id.* The damages suffered by the plaintiffs in the form of interest led the court to uphold the lower court decision awarding the plaintiffs prejudgment interest because the penalty constituted compensable injury through the defendant's action under applicable Oklahoma law. *Id.* at 1235-56. The statute requires:

When a verdict for damages by reason of personal injuries or injury to personal rights including, but not limited to, injury resulting from bodily restraint, personal insult, defamation, invasion of privacy, injury to personal relations, or detriment due to an act or omission of another is accepted by the trial court, the court in rendering judgment shall add interest on said verdict . . . from the date the suit was commenced to the date of verdict

OKLA. STAT. tit. 12, § 727(A)(2) (1990). The court held that the interest penalty was an injury that fell within the confines of § 727(A)(2) because it was caused by defendant's action of negligently preparing the plaintiffs' return. *Wynn*, 815 P.2d at 1235. The cited Oklahoma statute only answers the question of causation; in this case, the question of the interest penalty as an injury to the plaintiff remains unanswered.

77. 570 N.E.2d 1167 (Ill. App. Ct. 1991).

78. *Id.* at 1167. Taxpayer-Dail retained defendant-E.K. Williams & Co. to prepare sales returns for his gas station. *Id.* at 1168. Dail was audited for the years 1984 to 1987 by the Illinois Department of Revenue when he closed his business. *Id.* The State of Illinois assessed \$8,268.00 in additional taxes, \$426.00 in penalties, and \$3,691.74 in interest. *Id.* Dail brought suit alleging both negligence and breach of contract on the part of the defendant. *Id.* The defendant counterclaimed for tortious interference and slander. *Id.* The trial court found for the plaintiff on the negligence claim. *Id.* The court denied the defendant's counterclaim of tortious interference with business, but did award the defendant \$500 in general damages for the slander claim. *Id.*

79. *Id.*

80. *Id.*

81. *Id.* The trial court seemed to suggest that it would apply the benefit rule to the interest penalty calculation as a measure of damages. *Id.* However, the court felt that attempting to ascertain the value

In reversing the lower court, the Illinois Appellate Court began with the premise that “the appropriate measure of damages is the difference between what the (taxpayers) would have owed in any event if the tax returns were properly prepared, and what they now owe because of their accountants’ negligence, plus incidental damages.”⁸² Following this logic, the court agreed with the plaintiff that the interest penalty would not have been incurred but for the accountant’s negligence in preparing the return.⁸³ Consequently, the court awarded the interest penalty because this “properly returns the plaintiff to the position he would have been in but for the negligence and/or the breach by the defendants.”⁸⁴ Unlike *Wynn*, there was no evidence regarding how the plaintiff used the money before the deficiency was assessed, or whether the plaintiffs were able to pay the interest penalty without the assistance of a third party.⁸⁵

Courts that do not recognize the interest penalty as an appropriate measure of damages believe that the plaintiff suffers no injury from the interest penalty. Alaska is one state that characterizes the penalty as the prevention of an unjust enrichment to the plaintiff. In *Orsini v. Bratten*,⁸⁶ the plaintiffs sued their accountant, alleging negligent misrepresentation and breach of contract.⁸⁷ Based on his investment advice, the Brattens allowed Mr. Orsini to

of the money to the plaintiff and offsetting it against the interest charged by the Department of Revenue would be speculative. *Id.* at 1168.

82. *Id.* at 1169 (citing *Thomas v. Cleary*, 768 P.2d 1090, 1091-92 (Alaska 1989)). The *Dail* court noted that Illinois had not yet addressed the recoverability of the interest penalty in accountant malpractice suits for negligent preparation of returns. *Id.* at 1168. However, in *Thomas*, the Supreme Court of Alaska did decide that the interest penalty was recoverable. 768 P.2d at 1092. The court found for the defendants, reasoning that the award of damages was speculative since the IRS had neither issued a deficiency assessment nor imposed any additional liability on Thomas. *Id.* The *Thomas* court noted that a “mere breach of a professional duty, causing only nominal damages, speculative harm, or the threat of future harm—not yet realized—does not suffice to create a cause of action for negligence.” *Id.* at 1092 (citing *Budd v. Nixen*, 491 P.2d 433, 436 (Cal. 1971)) (citations and footnote omitted).

83. *Dail*, 570 N.E.2d at 1168. Again, the court addressed the issue of causation without first determining whether actual injury occurred.

84. *Id.* The court noted that the interest paid by the plaintiff to the state was easily ascertainable and was a direct consequence of the defendants’ negligence. *Id.* The court did not consider the trial court’s determination that it would be speculative to determine the value of the money to the plaintiff during the subject period and then off-set it against the interest. *Id.*

85. *Id.*

86. 713 P.2d 791 (Alaska 1986).

87. *Id.* at 792. The accountant suggested that the plaintiffs invest in a purchase-leaseback arrangement, involving mostly furniture, with the “Roaring 20’s Hotel” in Fairbanks. *Id.* The return on their \$54,000 investment that accountant-Orsini projected was a direct cash flow of \$57,200 and tax savings of \$69,985 over the seven year period of the leaseback agreement. *Id.* The total projected return according to the accountant was \$158,085 or 41.8%. *Id.* Evidence indicated that the plaintiffs

prepare their 1977 tax return and amend their 1974 and 1975 returns to reflect investment tax credits for those years.⁸⁸ The IRS audited the Brattens in 1980 and determined that they were not entitled to claim the investments as deductions.⁸⁹ The trial court found for the plaintiffs⁹⁰ and awarded them the amount of the interest penalty associated with the deficiency assessment as damages.⁹¹

The Supreme Court of Alaska reversed the damages award on appeal.⁹² The court reasoned that the plaintiffs had the use of the money and

had discussed several other investment options with Orsini, including real estate and tax-exempt municipal bonds. *Id.* After the plaintiffs agreed to the investment, Orsini prepared their 1977 returns and amended their 1974 and 1975 returns to claim investment tax credits. *Id.* In 1980, the IRS audited the plaintiffs for 1974, 1975 and 1977. *Id.* As a result of the audit, the IRS determined that the purchase-leaseback did not allow the plaintiffs to claim an investment tax credit. *Id.* At trial, Orsini did not deny that the rental income was left out by "mistake" from the estimate he provided for the plaintiffs. *Id.* The plaintiffs alleged negligent misrepresentation against the accountant, claiming that because of Orsini's errors their actual return was \$143,400 less than projected. *Id.*

88. *Id.*

89. *Id.* The court held that I.R.C. § 46(e)(3) permits non-corporate lessors like the plaintiffs to claim an investment tax credit only if the length of the lease is less than 50% of the estimated useful life of the property. *Id.* In addition, the deduction claimed must exceed 15% of the rental income produced from the property for the first 12 months after the property is transferred to the lessee. *Id.* The purchase-leaseback agreement failed to meet either of these conditions. *Id.*

90. *Id.* The superior court found that the plaintiffs would not have entered into such an agreement but for the defendant's advice and that the defendant was negligent in giving the advice. *Id.* The total award was \$59,276.86, which included the fees billed to the plaintiffs by Orsini, the amount of the tax credit repaid to the state and federal government plus interest penalties, and "prospective tax liability" in the amount of \$35,320.00. *Id.*

91. *Id.* Plaintiffs claimed as their true measure of damages the difference between Orsini's projected return on their investment and their actual return, approximately \$143,340, or in the alternative, what they would have received if they had invested in real estate, approximately \$137,804, and what they actually received, which was \$14,745. *Id.* The estimation of the return they would have received from another possible real estate investment was calculated by an expert, who based his calculations on similar properties in the area. *Id.*

92. *Id.* Orsini appealed the award on the ground that the superior court erred in awarding prejudgment interest and damages against the clear weight of the evidence. *Id.* Specifically, he contested the award for "prospective tax liability" and the award for state and federal interest penalties. *Id.* However, he did not contest the award with respect to the fees billed to the plaintiffs or the disallowed tax credits. *Id.* The plaintiffs also appealed on the grounds that the award was inadequate because it only covered the investment tax credit claimed in 1977. *Id.* The Alaska Supreme Court held that the plaintiffs only received the tax credit for 1977 because Orsini agreed to it. *Id.* The court held that they may not be entitled to any recovery of this amount because the scheme was invalid and they were never entitled to the amount promised by Orsini. *Id.* at 794. The court also agreed with Orsini that the prospective tax liability award was invalid. *Id.* The court struck down the plaintiffs' cross-appeal that the lower court failed to consider Orsini's error with respect to the tax ramifications of the leaseback agreement. *Id.* The court held that deciding what the plaintiffs would have earned by investing in real estate was too speculative. *Id.* (citing *City of Whittier v. Whittier Fuel & Marine Corp.*, 577 P.2d 216, 222 (Alaska 1978)).

“presumably, were able to earn interest [on it] while they held it.”⁹³ Accordingly, paying the penalties “effectively cost... [the plaintiffs] nothing.”⁹⁴

New York courts have used similar logic, as illustrated in *Alpert v. Shea Gould Climenko & Casey*.⁹⁵ The consolidated suit arose out of a tax shelter entered into by the plaintiffs upon tax opinions issued by the defendants.⁹⁶ The IRS held the plaintiffs’ deductions for their investment in the shelter invalid.⁹⁷ Consequently, the plaintiffs paid the tax deficiencies caused by the deductions, as well as interest on the base tax amount.⁹⁸

In reversing the lower court’s denial of the tax preparer’s motion for partial summary judgment for the plaintiffs’ recovery of the interest penalty, the court characterized the interest assessed by the IRS as “a payment to the IRS for . . . use of the money during the period of time when (the taxpayer) was not entitled to it.”⁹⁹ The court held barring the plaintiffs’ recovery created an equitable result.¹⁰⁰ This bar was justified on the ground that recovery would allow the investors a windfall of both having used tax monies for several years and recovering interest on those monies.¹⁰¹ Similar to *Orsini*,

93. *Orsini*, 713 P.2d at 794.

94. *Id.* This was the extent of the court’s analysis on the issue of the plaintiffs’ actual use of the money prior to the deficiency assessment.

95. 559 N.Y.S.2d 312 (App. Div. 1990).

96. *Id.* at 313. These cases were consolidated from suits brought by George Alpert and Lee Wolfman in the same tax shelter against the defendant-law firms who had issued tax opinions with respect to the shelter and the Esanu firm that structured the shelter. *Id.* Both plaintiffs invested in the shelter because they were facing large income tax liability for the year 1977. *Id.* Each plaintiff invested \$52,500 in Logan to immediately deduct the advance minimum royalty paid by the shelter for the right to mine coal. *Id.* The claimed deduction in 1977 arising from the Logan advance minimum royalty amounted to \$219,728. *Id.*

97. *Id.* The IRS disallowed the deduction in July 1984 to Wolfman and in March 1985 to Alpert, on the grounds that the advance minimum royalty was not deductible under § 612 of the Internal Revenue Code and that the Logan Program did not have economic substance. *Id.* The U.S. Treasury amended its regulations to disallow deductions from gross income of advanced royalties paid in connection with mineral property, which had previously been allowed. *Id.* The revised rules issued by the IRS allowed deduction of the advance minimum royalties over the period for which they were paid rather than in the year of payment. *Id.* The defendant-law firms opined to the plaintiffs that the new regulations would not affect the plaintiffs’ ability to deduct the entire amount in the year it was paid. *Id.* at 314.

98. *Id.* The amount of the interest penalty was greater than the amount of the back taxes assessed by the IRS. Alpert paid \$117,451 in back taxes and \$165,818 in interest. *Id.*

99. *Id.* at 315 (citing *Freschi v. Grand Coal Venture*, 767 F.2d 1041 (2d Cir. 1985), *vacated on other grounds*, 478 U.S. 1015 (1986)).

100. *Alpert*, 559 N.Y.S.2d at 315.

101. *Id.*

there was no factual inquiry into the plaintiffs' actual use of the money prior to the deficiency assessment.

III. ANALYSIS

There are fundamental problems with the current application of tort principles as demonstrated in the cases discussed above. Contrary to the court's decision in *Wynn*, an analysis under the Restatement benefit rule is appropriate in the context of accountant malpractice suits. The court in *Wynn* refused to offset the plaintiffs' use of the money as a benefit because the case cited by the defense in support of the rule was factually distinct.¹⁰² However, the court never explained why this factual distinction prevented it from applying the basic rule.

The benefit rule is applicable to the accountant malpractice situation for the very reason that the *Morris* court rejected it. The *Morris* court refused to apply the benefit rule to the expenses associated with raising a healthy child claimed by plaintiffs bringing a wrongful birth suit because the Restatement limits the offset to benefits conferred on the same interest to which the plaintiff claims harm.¹⁰³ In *Morris*, the emotional benefits the plaintiff gained from having a child, including love and companionship, were different from the economic damages alleged—the costs associated with raising a healthy child.¹⁰⁴ The court refused to apply the rule because comment b to the Restatement precludes application of the benefit rule where the plaintiff's interest that benefited from the tortious conduct is different from the interest that was harmed by the defendant's actions.¹⁰⁵

102. See *supra* notes 59-70 and accompanying text.

103. See *supra* note 67 and accompanying text. Although the *Morris* court did acknowledge that other jurisdictions, including California and Ohio, do allow parents to recover the costs associated with raising a healthy child in a medical malpractice suit for a failed sterilization procedure, the court noted that no authority had been cited for the proposition that these costs should not be offset by the benefits gained. *Morris v. Sanchez*, 746 P.2d 184, 185 (Okla. 1987). However, the court's ultimate conclusion was that the costs associated with raising the healthy child were not recoverable at all, and so the issue of whether to apply the benefit rule did not really have to be decided. *Id.* at 188.

104. *Morris*, 746 P.2d at 186-88.

105. *Id.* at 186. Although the *Morris* court adhered strictly to comment b of section 920 of the Restatement, other courts have allowed the defendant to offset the emotional benefits gained by the parents as a result of the birth. *Id.* (citing *University of Ariz. Health Sciences Ctr. v. Superior Court*, 667 P.2d 1294 (Ariz. 1983); *Stills v. Gratton*, 127 Cal. Rptr. 652 (Cal. Ct. App. 1976); and *Tropi v. Scarf*, 187 N.W.2d 511 (Mich. Ct. App. 1971)). The opinion noted that those courts which apply the benefit rule in such cases despite the same interest limitation in comment six rely on the principle of unjust enrichment. *Morris*, 746 P.2d at 186-87. Those courts rule that the plaintiff would be unjustly

Unlike a wrongful birth case, accountant malpractice is the perfect example of a situation where any potential benefit conferred affects the same interest that was injured by the accountant's breach. The plaintiff claims economic harm by being forced to pay the interest penalty.¹⁰⁶ However, the plaintiff may have gained a monetary benefit by having the use of the money during the period in which it rightfully belonged to the IRS.¹⁰⁷ Unlike *Morris*, this benefit to the plaintiff's financial interest could be offset from the injury of having to pay the penalty incurred as a result of the accountant's negligence (a detriment to the plaintiff's financial interest) without violating the integrity of the Restatement.¹⁰⁸

Moreover, the *Morris* court's ultimate decision did not rely on perceived inconsistencies in the Restatement with respect to a strict application of the benefit rule in failed sterilization proceedings.¹⁰⁹ Instead, the true holding of the *Morris* court was that the benefit rule was inappropriate given special policy concerns associated with human life.¹¹⁰ Clearly, these same concerns with respect to judgments about the value of human life are not implicated in the context of accountant malpractice suits.

In addition, the collateral source rule,¹¹¹ which the *Wynn* court suggested could apply in upholding the plaintiffs' request for recovery of the interest

enriched by a strict application of the same interest limitation. *Id.* at 187. Other courts rely on the connection between the emotional benefits gained and the economic strain associated with raising an unexpected child. *Id.*

106. See, e.g., *supra* notes 54-85 and accompanying text.

107. This is oftentimes the defendant's argument for why the court should not award the interest penalty as a measure of damages. Defendants argue that payment of the penalty does not constitute a loss to the plaintiff because the plaintiff gained at least an equal benefit by having the use of the money during that period. Courts such as the *Alpert v. Shea Gould Climenko & Casey* court, see *supra* notes 95-101, support this view.

108. Because comment b to section 920 of the Restatement dictates that harm to one type of interest can only be offset by a benefit to the same interest, the *Morris* court refused to consider its application in the case of a failed sterilization procedure. *Morris*, 746 P.2d at 187. In the hypothetical in the text, however, the plaintiff's harmed interest is identical to the one benefited: namely, the plaintiff's pocketbook.

109. In fact, the *Morris* court noted that other courts have looked beyond the strict application of comment b to prevent the plaintiff from being unjustly enriched. *Id.* at 187-88; see *supra* note 68 and accompanying text.

110. *Morris*, 746 P.2d at 188. Although the court cited various decisions that denied the defendant's claim for an application of the benefit rule as well as the plaintiffs' request for the costs associated with raising an unplanned child after a failed sterilization procedure, the court stated that "[o]ne thread connects the reasoning common to all these cases. That thread is the sanctity which must be placed on human life." *Id.* at 187.

111. See *supra* notes 45-48 and accompanying text.

penalty,¹¹² cannot be applied uniformly in all accountant malpractice suits. First, the collateral source rule is applied when the plaintiff's harmed interest is remedied by a source other than the defendant or one not on the defendant's behalf.¹¹³ If the source that may have compensated the plaintiffs in *Wynn* is revenue from the investment of the deficiency, it is arguable that this source could be attributed to the defendant, because the plaintiffs would not have had the funds to invest but for the defendant's negligence. Therefore, the collateral source rule would not be applicable because the payment did not come from a source other than the defendant.

Second, the collateral source rule is a principle applied to prevent a reduction in a negligent defendant's liability where the plaintiff was compensated for loss after the injury occurred.¹¹⁴ However, this principle assumes that the plaintiff suffered an actual injury for which he can be compensated. If a taxpayer is not really harmed by compensating the IRS for his use of the money during the time that it rightfully belonged to the IRS, there is no need to apply the collateral source rule.¹¹⁵ Applying the collateral source rule in this instance merely avoids the first question that should be answered in any analysis of appropriate damages: did the plaintiff suffer actual injury by being required to pay the interest penalty?¹¹⁶

112. *Wynn v. Estate of Holmes*, 815 P.2d 1231, 1234 (Okla. Ct. App. 1991) (citing *Burk Royalty Co. v. Jacobs*, 387 P.2d 638 (Okla. 1963)). However, the extent of the court's analysis on the applicability of the collateral source rule was very limited. The court merely states that the collateral source rule is the only possible legal doctrine that might be applicable. *Id.* at 1235.

113. *See supra* notes 45-48 and accompanying text. It is unclear whether the plaintiffs argued that the payment of the interest penalty through a bank loan or from revenue generated from a possible investment of the deficiency in certificates of deposit constituted the collateral source that could not be used to offset the defendant's liability. However, the payment of the interest penalty to the IRS through a bank loan does not satisfy the definition of a collateral source. If the plaintiffs did suffer an injury by being forced to pay the interest penalty, then they have not been made whole by the payment of the penalty through a bank loan; they have even increased their injury because of the accrued interest on the note during the repayment period. This is an injury that would not have occurred but for the defendant's negligence.

114. *See supra* note 45 and accompanying text. Assuming that the defendant argued that funds from investment in certificates of deposit constituted repayment of the plaintiffs' injury, the *Wynn* court noted that no actual fund permitting an offset from the interest penalty payment existed. *Wynn*, 815 P.2d at 1235. Although the plaintiffs could have paid the amount of the deficiency at the original time of filing, no fund had been set aside for this purpose. *Id.*

115. The collateral source rule, like the benefit rule, is a damages principle applied only when actual damages have been found.

116. The *Wynn* court indirectly answered this question. Presumably, the court felt that the decline in value of the plaintiffs' investment, coupled with the fact that no funds had been set aside for the repayment of the penalty, led the court to conclude that payment of the penalty through a bank loan did constitute injury to the plaintiffs that would not have occurred but for the defendant's negligence.

There are many circumstances in which the taxpayer does benefit from the use of the money during the period prior to the deficiency assessment. The taxpayer can invest the money in stocks, a savings account, or certificates of deposit.¹¹⁷ Even absent such obvious revenue-generating uses, the plaintiff still has the use of the money for everyday needs such as groceries and household repairs. The use of the money is cheaper when the plaintiff spends it at the time of the original filing than it would be on the date of the deficiency assessment because of inflation during that period.¹¹⁸ It is in this respect that a plaintiff is able to derive a benefit from the use of the money that he would have had to pay at the date of original filing if the accountant had prepared the return correctly.¹¹⁹

However, the plaintiff in some circumstances can rightfully claim that the payment of the interest penalty places him in a worse position than he would be in if the taxpayer had not had use of the money prior to the deficiency assessment.¹²⁰ It is possible that some taxpayers may choose to donate their unexpected windfall to a charity. In this case the plaintiff would not have earned any interest or derived any benefit from the use of the money. Payment of the interest penalty would place the taxpayer in a worse position than if the accountant had not been negligent because the taxpayer would not

Wynn, 815 P.2d at 1235.

117. For example, the plaintiffs in *Wynn* may have benefited from the accountant's negligence if they had invested the deficient amount in certificates of deposit. *Id.*

118. Inflation is the rate at which prices increase each year due to factors such as an increase in the money supply or unemployment levels. When this happens, the value of the dollar falls because more dollars are needed to purchase the same good. Relative to the goods which it used to be able to buy, each dollar is worth less. The IRS assesses the interest penalty to account for the fact that the amount of money that the taxpayer owed two years ago cannot buy as much today as it could then. The principle amount of the underpayment is basically increased to reflect the same value now as it had when originally owed. In most stable economies, the interest rate and the rate of inflation are identical, which enables creditors to ensure that they will at least get back the present value of their money at the end of a loan repayment period.

119. In this situation, plaintiffs suffer no harm by being forced to pay an interest penalty because they are merely repaying the IRS the exact value of money that was originally owed. As has been discussed, *supra* note 3, the amount of the deficiency is not recoverable because the plaintiff-taxpayer would have had to pay this amount at the original date of filing if the accountant had not breached a duty of care in preparing the return.

120. This was the case in *Wynn*. Although the plaintiffs had use of the money at the original date of filing, the value of their investments had so decreased that the plaintiffs had to obtain a loan for the amount of the deficiency. *Wynn*, 815 P.2d at 1235. Because the plaintiffs in *Wynn* lost their money not through their own flagrant spending habits, but rather through market decrease in price, they did not obtain the benefit of the money prior to the deficiency assessment. *Id.* Therefore, this is one case in which the plaintiffs were harmed by the defendant's negligence by the assessment of the deficiency and the corresponding interest penalty through no fault on the plaintiffs' part.

have donated the funds if he had known that he would be forced to repay that amount at a later date. The amount of the harm suffered by a taxpayer varies depending on any possible income tax deductions that taxpayer is allowed to declare¹²¹ or the portion of the deficiency that he chose to donate to charity.¹²²

As the preceding analysis demonstrates, the strict application of a blanket rule either for or against awarding interest as a measure of damages ignores the reality that in some circumstances the plaintiff does benefit from the use of the money and in some circumstances the plaintiff is harmed by having to pay the interest penalty.¹²³ The rationale used by courts in either case fails to consider the true impact of the penalty on the plaintiff.

IV. PROPOSAL

The solution that best resolves this dilemma would take into account the unique circumstances of each case to award damages that accord with the traditional notion that plaintiffs should be placed in the same position that they would have been in but for their accountant's negligence.¹²⁴ To do this, judges presiding over any accountant malpractice suit should carefully examine the circumstances surrounding the taxpayer's actual use of the

121. *Cf. Burgess v. Premier Corp.*, 727 F.2d 826, 837-38 (9th Cir. 1984) (holding that tax benefits received by investors suing their accountants for negligent misrepresentation should not be deducted from any award of damages). The *Burgess* court felt that the only way to put the plaintiffs in the same position as they would have been in but for the defendants' fraudulent conduct was to set the damages exclusive of the tax benefits gained. *Id.* at 838. Under such an approach, the plaintiffs would not be unjustly enriched because the IRS can disallow the tax benefits wrongfully gained. *Id.* The court noted that prior cases did consider tax benefits in determining an award of damages. *Id.* (citing *In re Air Crash Disaster near Chicago, Ill.*, 701 F.2d 1189 (7th Cir. 1982), *cert. denied*, 464 U.S. 866 (1983)). However, the court noted that the actual benefits received, as opposed to the speculative benefits received in the cited precedent, warranted this approach. *Id.* However, the enjoyment of these tax benefits led the court to deny the plaintiffs' request for prejudgment interest. *Id.* at 838.

122. As the Restatement points out, only benefits to the plaintiff's economic interests may be offset from the harm caused by the assessment of the interest penalty. RESTATEMENT (SECOND) OF TORTS § 920, cmt. b (1979). Consequently, any benefit the taxpayer receives in the form of goodwill in the community or personal satisfaction should not be considered when calculating the value of the use of the money compared to the injury to the plaintiff resulting from the interest penalty assessment.

123. Judicial opinions discussed in this Note have all applied either the benefit rule, the collateral source rule, or some other damages principle without considering the true impact of the penalty on the plaintiff's actual spending history prior to the deficiency assessment. It is this approach that has led courts to ignore the true impact of the penalty on plaintiffs and has allowed these improper results to obtain.

124. As the *Morris* court noted, a basic principle of tort law is that the liable party must be held responsible "for all the detriment flowing from his tortious act." *Morris v. Sanchez*, 746 P.2d 184, 187 (Okla. 1987).

money.¹²⁵ By conducting such an examination into the facts, a court will be able to determine whether the plaintiff has truly suffered an injury.¹²⁶ This determination will resolve whether the plaintiff has a right to recover the amount of the interest penalty from the negligent accountant.¹²⁷ Whether the plaintiff has suffered a loss that would not have occurred if the accountant had not breached a duty of care is contingent on the plaintiff's actual use of the funds during the period between the original due date and the deficiency assessment date. Only then can the court satisfy its obligation to remedy the plaintiff's actual injury. Where the plaintiff has not been harmed by the imposition of the interest penalty, no recovery should be allowed. In all other cases, where both harm and benefit have inured to the plaintiff as a result of the breach, the benefit rule should be applied to mitigate damages.

In cases where the taxpayer merely absorbs the amount of the deficiency into an ordinary course of spending, there is no injury. Because the IRS assesses interest at the federal short term rate, which usually parallels the

125. It should be noted that a negligent defendant is generally not held liable after the plaintiffs are made aware of the negligence and continue to act or fail to take some action such that their damages are increased. *Vogt v. Abish*, 663 F. Supp. 321, 324 (S.D.N.Y. 1983). In *Vogt*, for example, the defendant was not held liable after the plaintiff failed to file an amended return when he received notice that the original return filed by the defendant was deficient. *Id.* at 324. The court held that the plaintiff's failure was an intervening cause that broke the chain of causation. *Id.* Therefore, any examination of the plaintiff's use of the money in determining damages should end when the plaintiff has knowledge that the deficiency will be owed to the IRS, regardless of whether an actual deficiency has been assessed. The plaintiff in this situation has a duty to mitigate damages by not spending the money frivolously or donating it to charity.

126. See *supra* note 21 and accompanying text.

127. This type of factual determination may not be necessary where the defendant-accountant has made representations that the return is insured for any further action taken by the Department of Revenue respecting any work done by the accountant. For example, in *Slaughter v. Roddie*, the contract between the plaintiff-taxpayer and the defendant-accountant contained the following statement:

UNCONDITIONALLY GUARANTEED

In the event of an audit we cheerfully appear with you for audit of your return, subject of course to verification of each item on your return by receipts or reasonable explanation. We do not accept responsibility for estimates we are required to make in regard to interest or other items when amounts are unknown at the time of preparation. *In the event of interest or penalty assessed against this return after accounting by receipts we pay all penalties or interest assessed.* This guaranty is for the life of the return and no further charges will be made for the above service.

249 So.2d 584, 586 (3d Cir. 1971) (emphasis added). Under these facts, the *Slaughter* court held that the interest penalty was recoverable. *Id.* at 586. No factual inquiry need be made into the plaintiff's actual use of the money where the defendant has made representations that he will indemnify the plaintiff for any interest assessed resulting from underpayment of tax owed. This dispute is one of a contractual rather than tortious nature.

going rate of inflation,¹²⁸ the difference between what the taxpayer would have owed at the original date of filing and what is owed when the deficiency is assessed should equal zero.¹²⁹ Payment of the interest penalty by the plaintiff merely adjusts the amount of the deficiency to account for its present-day value.¹³⁰ This adjustment imposes no greater burden on the plaintiff than if he had paid his true tax liability at the original date of filing. Therefore, no recovery of the interest penalty should be allowed.¹³¹

In cases where the taxpayer benefits from the use of the money prior to the deficiency assessment, the taxpayer's recovery should be limited to the difference between the amount of the interest penalty and the increased value of the money to the plaintiff prior to the deficiency assessment as a result of inflation during that period. However, the plaintiff may still be able to show some harm where the money is spent in ways in which it otherwise might not if the taxpayer had known that he would have to repay the IRS. Despite the fact that the plaintiff may have benefited while he had the money, he has still suffered an injury because he would not have spent the money if the accountant had prepared the return correctly.¹³²

128. See *supra* note 118 and accompanying text.

129. Inflation occurs when the market rate of interest is kept below the rate of profit that people believe they will recoup on their investments. See HALM, *supra* note 31, at 380. When this occurs, the demand for loanable funds by people seeking to increase the means of production outweighs the supply of funds by investors. *Id.* The government usually compensates for this discrepancy by supplying new money in the market. *Id.* The new influx of money into the market may raise prices if the market feels that the dollar has been devalued. *Id.*

130. See *supra* notes 31-34, 118 and accompanying text.

131. This will likely be the common result in accountant malpractice suits. A hypothetical taxpayer who receives notice of a deficiency for \$15,000 plus \$2500 in interest three years after the original date of filing due to the negligence of the accountant may be able to avoid the imposition of a negligence penalty. However, if taxpayers take no further action with the money (i.e., do not donate it to charity or make an unexpected expenditure), but merely absorb it into the everyday cost of living, they will have gained a benefit from using money during the period of the delay. The value of the money to the plaintiff at the original date of filing was \$15,000. The equivalent value of the money in today's terms when taking into account inflation is also \$15,000. According to a correct application of the benefit rule, paying the money in today's value is equivalent to what the plaintiff was able to keep during the period of delay. Therefore, the injury to the plaintiff in the amount of \$15,000 is offset by the benefit of the money to the plaintiff of \$15,000. The plaintiff is not entitled to recover the interest penalty.

132. For example, imagine a case where the accountant, through his negligence, claims a tax deduction to which the taxpayer, Jones, is not entitled. The IRS issues a deficiency assessment of \$15,000 and an interest penalty of \$2500 three years later. Jones can establish in court that in the year in which the return was deficient, she and her family took a vacation to Hawaii that cost approximately \$20,000. Jones states that she decided to take this "little getaway" because "this was my best year ever" financially. The value of the deficiency amount when the assessment is issued is \$17,500 (adjusted for inflation). One year later, Jones filed a Chapter 7 bankruptcy proceeding. Under this

In those circumstances where the plaintiff, either through charitable donation, economic ruin, or other circumstance beyond his control, gains no benefit from the use of the money, the penalty clearly places him in a worse position than if the accountant had not been negligent. Although the taxpayer may have had to pay the amount of the deficiency at the original date of filing, he would not have had to pay the additional interest assessed by the IRS. When the plaintiff did not use the funds in a way that would generate interest, the plaintiff is forced to pay the IRS back for the time that the IRS did not have the money, despite the fact that the plaintiff did not have use of the money either. The lack of offsetting benefits entitles the plaintiff to recover from the accountant all additional costs incurred as a result of the interest penalty assessment.¹³³

VI. CONCLUSION

This proposal is a straightforward application of traditional tort principles and the benefit rule developed in the Restatement. Although this approach will require more fact-finding by the court, such an inquiry should not be unduly complicated. The court already has the opportunity to examine the plaintiff's financial situation in determining whether the accountant was negligent in the preparation of the return. Courts already engage in this type of damages assessment in many tort cases. There is no reason to bypass it in

proposal, the court should look at whether the plaintiff was truly injured by the accountant's negligence. Here, the plaintiff clearly gained a benefit from the error by being able to take a vacation with the unexpected windfall. Under the benefit rule analysis, the defendant should not be required to repay \$2500 where the plaintiff was not truly injured by the breach. However, Jones should be able to argue that she would not have taken a vacation but for the belief that she had an especially profitable year. Therefore, the difference between the cost of the vacation (\$20,000) and the benefit incurred (\$17,500) is \$2500. Jones should be able to establish that she was truly injured by the accountant's negligence because she would not have spent the extra \$2500 on a vacation if she knew the money was not hers to spend.

133. Consider the hypothetical case of Smith, whose accountant erroneously claimed a deduction to which Smith was not entitled. The IRS assesses the deficiency of \$15,000, plus an interest penalty of \$2500 three years later. However, Smith had a policy each year of donating whatever money he saved on investments to charity. Accordingly, Smith donated \$15,000 to the Make A Wish Foundation the year that he was deficient. When Smith is forced to repay the IRS three years later, he is repaying them for their loss of money that was rightfully theirs during that period. However, unlike Jones, discussed *supra* note 132, he has not gained any benefit from the delay. If the accountant had determined Smith's tax liability correctly, Smith would not have donated anything to the charity. The difference between the value of the money at the original date of filing and the date the deficiency is assessed is \$2500. Because Smith would not have had to pay this amount if the accountant had acted reasonably, Smith should be able to recover this amount.

the context of accountant malpractice in favor of a general rule that does not accord with equitable principles of relief.

It will be obvious if the plaintiff made an investment soon after the original filing and before notice of the defendant's possible negligence. It will also be obvious if the plaintiff obtained no benefit from the use of the money, due to a charitable donation or other economic loss that renders the interest penalty a harm without a corresponding benefit. In situations where the taxpayer merely absorbs the extra money into his daily finances without any exorbitant gain or loss in his records, the plaintiff should not be allowed to recover the interest penalty because he obtained the benefit of using the money at exactly the same rate as the IRS's assessment of interest. This leaves only limited circumstances in which a plaintiff will be allowed to recover the interest penalty. This is entirely fair, as the rule accounts for circumstances in which the taxpayer is put in a worse position by its assessment.

Likewise, this proposal does not preclude any application of the collateral source rule in cases where the plaintiff has truly suffered an injury but has been compensated either through gift or taking on an extra job to earn the money to pay the interest penalty. The collateral source rule should be applied to bar a defendant's claim that the plaintiff has been compensated for his injury just as in all other cases.

The benefit rule is applicable in accountant malpractice suits. However, the rule can only be applied after the court has conducted an inquiry into the plaintiff's actual use of the money prior to the deficiency assessment. This is where opinions of courts, such as in *Orsini v. Bratten*¹³⁴ and *Alpert v. Shea Gould Climenko & Casey*,¹³⁵ have failed in their analyses. By assuming that the plaintiffs in both cases had received some benefit from the use of the money, the courts undermined the basic damages principle of placing both parties in relatively equitable positions in light of their true misconduct and injury.

Shawna Jahn

134. 713 P.2d 791 (Alaska 1986).

135. 559 N.Y.S.2d 313 (App. Div. 1990).