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Nos. A10-1439 and A10-1447

State of Minnesota

In Court of Appeals

Ames & Fischer Co., II, LLP, et al.,

Respondents,

v.

John R. McDonald, et al.,

Appellants (A10-1439),
Defendants (A10-1447),

Larsen, Larsen & Associates, P.A.,

Defendants (A10-1439),
Appellants (A10-1447).

REPLY BRIEF OF APPELLANTS LARSEN, LARSEN & ASSOCIATES, P.A., JAMES LARSEN AND MICHAEL LARSEN

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ARGUMENT

The initial appellate brief of appellants Larsen, Larsen & Associates, P.A., James Larsen and Michael Larsen (collectively, "Larsen") demonstrated that respondents' claims for improper tax advice accrued upon Larsen's preparation of tax returns for the year 2000. Larsen prepared and signed these returns in early 2001 and respondents filed the returns shortly thereafter. Respondents then waited more than seven years to commence this lawsuit. This Court should reject respondents' efforts to defend their delay. As predicted in Larsen's initial brief, these efforts amount to an attempt to focus on isolated trees within the forest. This Court should resolve the certified question by instructing the district court that a claim arising out of the failure to make 754 elections accrues when the tax returns are prepared and signed for filing by the taxpayer.[1]

I. Larsen's And McDonald's Defenses to Respondents' Allegations Are Irrelevant to the Statute of Limitations Issue.

Throughout their brief, respondents devote extensive resources to setting forth their view of Larsen's deposition testimony in response to their allegations and to McDonald's answer to their complaint.[2] But appellants' "explanations" (as respondents call this information) are irrelevant to the question before this Court.

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[1] While perhaps unimportant given this case's procedural posture, this Court should note an apparent error in respondents' brief. On page 26, respondents state that the district court "entered amended orders that dismissed the Larsens' statute of limitations defenses for both tax years and McDonald's statute of limitations defense for tax year 2001." The district court's March 31, 2010 Order specifically stated that McDonald's statute of limitations defense was dismissed. (M.Add. 17.) However, no such language appears in the court's December 31, 2009 Order denying Larsen's motion for summary judgment. (L.Add. 2.) Thus, it is not at all clear that the district court actually dismissed Larsen's statute of limitations defense.

[2] Larsen does not concede that respondents have accurately characterized their testimony.

As set forth in Larsen's initial brief, professional negligence claims, including accounting malpractice, must be brought within six years. Minn. Stat. § 541.05, subd. 1(5). The limitation period starts to run when the cause of action accrues; "that is, when the plaintiff can allege sufficient facts to survive a motion to dismiss for failure to state a claim upon which relief can be granted." *Antone v. Mirviss*, 720 N.W.2d 331, 335 (Minn. 2006) (citing *Dalton v. Dow Chemical Co.*, 280 Minn. 147, 152-53, 158 N.W.2d 580, 584 (1968). Thus, the key question is, "At what point in time would respondents have been able to assert allegations against Larsen sufficient to survive a Rule 12.02 motion to dismiss? In considering this question, this Court should note, "The showing that a plaintiff must make in order to survive a motion to dismiss under Rule 12.02(e) is minimal." *Noske v. Friedberg*, 670 N.W.2d 740, 742 (Minn. 2003).

Respondents contend, incorrectly, that Larsen's "explanation" for not having made the 754 elections at the first opportunity is relevant in determining when the claim accrued. But in determining the point at which a claim could be brought sufficient to withstand a Rule 12 motion, the defendants' "explanations" are irrelevant. Rule 12.02 allows a party to seek to dismiss the claims made against it because of "failure to state a claim upon which relief can be granted." Minn. R. Civ. P 12.02(e). The relevant standard for determining if a motion to dismiss under Rule 12.02(e) should be granted is whether the complaint sets forth a legally sufficient claim for relief. *Hauschildt v. Beckingham*, 686 N.W.2d 829, 836 (Minn. 2004). On a motion to dismiss for failure to state a claim under Rule 12.02(e), the district court may consider <u>only</u> the complaint and the documents referenced therein. *Martens v. Minn. Mining & Mfg. Co.,* 616 N.W.2d

732, 739 (Minn. 2000) (emphasis added). The Court treats the allegations in the complaint as true. *See Wiegand v. Walser Automotive Groups, Inc.*, 683 N.W.2d 807, 811 (Minn. 2004). It is immaterial whether or not the party against whom dismissal is sought can prove any of the facts alleged. *Carlson v. Estes*, 458 N.W.2d 123, 124 (Minn. App. 1990). In short, in testing whether a claim is sufficient to withstand a Rule 12 motion, the Court does not – indeed, cannot – consider the defendant's "explanations."

Of course, defendants usually have "explanations" for the claim against them, and the "explanations" often involve taking the position that defendant committed no negligence. Thus, if the defendants' explanations were relevant in considering when the claim would survive a Rule 12 motion, then most claims would never accrue and the statute of limitations would become meaningless. Consistent with Rule 12, defendants' answer to the complaint, or their deposition testimony, is irrelevant in determining when the claim accrued.

The answer to this key question of when the claim accrued is simple: respondents would have been able to allege, sufficient to withstand a Rule 12 motion to dismiss, each of the elements of an accounting-malpractice claim (and their related causes of action) beginning the moment Larsen prepared and signed the tax returns for 2000. That occurred in early 2001 – more than seven years before respondents commenced this lawsuit. At that point, as set forth in respondents' complaint and in the report of their expert, Boesen, Larsen's alleged breach of the duty had occurred and respondents' claimed damages had begun to accrue.

This Court should answer the certified question without considering what respondents call appellants' "explanations" for the alleged error.

II. Respondents Have Not Accurately Described Their Allegations.

Respondents also devote significant resources to arguing that Larsen did not accurately describe their allegations and cause of action.[3] On pages 27-28, respondents state that paragraph 57 of their Complaint accurately sets forth their allegations and accuse Larsen of "asking the Court to ignore" their actual allegations. This Court should note, however, that Larsen quoted this same paragraph 57 of respondents' Complaint (and other paragraphs), in full. (L.Brf., p. 5.) Larsen also quoted verbatim from, and cited to, respondents' expert's report. (Id., pp. 5-9.) Far from asking this Court to "ignore" respondents' allegations, Larsen has sought to focus this Court's attention squarely upon those claims. In fact, respondents' arguments simply ignore key allegations in their complaint and in their expert's report. Respondents' actual allegations show that their claims against Larsen first accrued in early 2001.

A. Respondents have not accurately described their allegations concerning the breach of duty.

Respondents have not accurately described the record concerning their allegations about when the breach of duty occurred. When all of respondents' allegations are considered, it is apparent that their claims could have survived a Rule 12 motion to dismiss immediately after Larsen "prepared and signed" the first set of returns at issue.

The reality is simple: the first opportunity to have made the elections occurred at the time Larsen prepared and signed the 2000 returns. Whereas it may be true that there

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were later opportunities to file amended returns to make the 754 elections, respondents' case has always been that Larsen should have made the elections at the first opportunity. Thus, respondents specifically alleged in their Complaint that Larsen's breach first occurred in connection with the preparation of the 2000 returns. (L.A., 24, ¶¶ 39-41.) Respondents allege that Larsen should have, but did not, "prepare or attach" the form for the 754 election for the 2000 returns for the three entities. (Id.) Respondents' expert, Boesen, similarly claims that Larsen violated professional standards when its personnel "prepared and signed" the 2000 tax returns for all three key entities. (L.A., 41-42). Boesen states in the Conclusion to his initial report:

> Unless a fully informed taxpayer declined to make the 754 Election, the election should have been included with FMP and AFC's 2000 or 2001 tax returns. Since Larsen and Larsen didn't make the 754 Election in 2000, they breached their duty in both years.

(Id., 44-45 (emphasis added).) Thus, Boesen opined that Larsen breached its duty when it prepared and signed the income tax returns for FMP, FSA and A&F in 2000 and 2001. Similarly, respondents' other expert, Woessner, opined that it was error not to make the election with the 2000 returns because there was "little, if any, downside" in making such an election and "no good reason not to make" the election at that time. (L.A., 98-99.)

Respondents did not address, or even cite to, any of this unambiguous language alleging the breach first occurred in the preparation and signing of the 2000 returns in early 2001. Instead, respondents repeatedly – and inaccurately – claim that their position is that the breach did not occur until April 2002 "at the earliest." (*See, e.g.*, R. Brf., p. 28.) Respondents justify this inaccurate claim by focusing on Boesen's supplemental

reports – which were produced only after appellants filed their motions for summary judgment. But these later reports should not be considered under Minn. Stat. § 544.42.[4] Even if they could be considered, the supplemental reports do not retract the initial opinions that the error first occurred with the preparation and signing of the 2000 tax returns. Boesen has not reversed course so as to claim that he now believes the 2000 returns were *correctly* prepared. Nor could he, given the undisputed fact that the first opportunity to have made the elections occurred at the time of the preparation and signing of the 2000 returns. His supplemental reports add nothing new to the case; they merely identify later opportunities to have amended the returns to include the forms necessary to make the 754 elections. (These later correction opportunities were also identified in respondents' Complaint.) As set forth in Larsen's initial brief, the later opportunities to have corrected the error do not toll or extend the statute.

In short, the record regarding the alleged breach is unambiguous: Respondents' claims against Larsen first accrued in connection with the 2000 tax returns. This Court should resolve the certified question by instructing the district court that a claim arising out of the failure to make 754 elections accrues when the CPA prepares and signs the tax returns for filing by the taxpayer.

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[4] This statute contains unique jurisdictional requirements for expert disclosure in professional liability cases. The claimant must provide a full disclosure of the expert's opinions within 180 days of commencing the case. Minn. Stat. § 544.42, subd. 2; *Brown-Wilbert, Inc. v. Copeland, Buhl & Co*, 732 N.W.2d 209, 215-220 (Minn. 2007). Nothing in the statute allows a plaintiff to make a new disclosure beyond the 180-day period.

B. Respondents have not accurately described their allegations concerning damages.

Respondents also have not accurately described their record concerning their allegations about when the damages began to occur. In their brief, respondents state, "Fischers' damages are generally overpaid taxes by the partners of the three entities." (R.Brf., p. 23.) This statement is correct, as far as it goes, but it fails to describe all of respondents' damages claims. When all of respondents' alleged damages are considered, it is apparent that their claims could have survived a Rule 12 motion to dismiss immediately after Larsen "prepared and signed" the first set of tax returns at issue.

As set forth on pages 6-7 and 9-10 of Larsen's brief, including the table copied from Boesen's initial report, respondents have alleged that their damages include overpayment of taxes for 2000, interest on the overpaid taxes (i.e., "loss of use" of the money), and costs to correct Larsen's alleged accounting errors. Boesen calculated FMP's overpaid taxes for 2000 as $1,487.00; A&F's overpaid taxes for 2000 as $1,469; and FSA's overpaid taxes for 2000 as $1,633. (Boesen Report, Table FMP-3 (L.A. 54-55); Table AFC-1 (id., 62-63); Table FSA-3 (id., 68-69.) Respondents became liable to pay this alleged excess tax upon the filing of the 2000 returns Larsen prepared and signed in early 2001. In addition, Boesen calculated the "loss of use of money" damages as $1,020.00 for FMP; $9,722.00 for A&F, and $1,141 for FSA. (Id.) These "loss of use" damages began to accrue upon respondents' payment of the alleged excess tax. In addition, the costs to correct the error, whether or not actually incurred at the time, also represent "some damage." *Herrmann v. McMenomy & Severson*, 590 N.W.2d 641, 643

(Minn. 1999).[5] All of these damages represent items of damage that would have been compensable in a legal action commenced immediately after Larsen prepared and signed those returns for respondents to file.

In their brief, respondents make no effort to address the significance of their allegations regarding damages for "loss of use of money" and cost to repair. Respondents do not acknowledge that their own expert, Boesen, calculated "loss of use of money" damages that began to accrue in 2001. Instead, respondents focus only on their allegation that the overpaid taxes could have been refunded. But this refund would have served only to mitigate their damages, and would have required respondents to incur costs to correct. *See May v. First Nat'l Bank of Grand Forks, ND*, 427 N.W.2d 285, 289 (Minn. App. 1988) (cost to repair cloud on title to real estate represented "some damage" that started the running of the limitations period).

In short, the record regarding the alleged damages is unambiguous: Respondents' claims against Larsen first accrued with Larsen's preparation and signing of the 2000 tax returns. This Court should resolve the certified question by instructing the district court that a claim arising out of the failure to make 754 elections accrues when the tax returns are prepared and signed for filing by the taxpayer.

III. The "Continuing Representation" Doctrine Is Not Recognized In Minnesota.

Respondents' argument that "continuing representation" is recognized in Minnesota in accounting malpractice case is simply wrong. No Minnesota Supreme

[5] Because it does not matter whether costs to correct were actually incurred at the time, respondents' argument on pages 23-24 that $100,000 in accounting fees they paid are not costs to correct is irrelevant.

Court case has ever recognized or applied "continuing representation" in an accounting malpractice case. And respondents did not rebut Larsen's argument that continuing representation should not apply in accounting malpractice cases due to the fact CPAs do not typically owe fiduciary duties to their clients.

If any accounting malpractice case had been appropriate to apply "continuing representation," *Reid* would have been that case. *Reid Enters., Inc. v. Deloitte & Touche*, No. C8-99-1801, 2000 WL 665684 (Minn. App. 2000). In *Reid*, the alleged negligence consisted of the CPA's failure to properly apply the "LIFO Conformity Rule." This error was made in tax returns which the CPA firm, Deloitte, prepared "in each and every year" from 1982 at least through 1991. *Reid*, *2. The district court held that the claim accrued at the time Deloitte prepared the first tax return in 1982 and dismissed the case. This Court affirmed. *Id.*, *2. As this Court noted,

> But Minnesota law is clear that when a professional provides a series of separate and distinct services over a period of years, the existence of an ongoing relationship does not toll the statute of limitations with regard to negligence for which service has been completed.

Id., *3 (citing *Herrmann*, 590 N.W. 2d at 643-44). Thus, the alleged continuing negligence after "some damage" occurred did not affect the determination of when the claim accrued. Instead, the claim accrued at the first moment when the negligence caused damage, even though the negligence continued (and damages apparently continued to increase) for many years thereafter.

Further, in *Reid* this Court noted that "continuing representation" is inconsistent with the "some damage" rule. The reason the two theories are inconsistent is simple: If

the claim accrues and the limitation period begins to run upon the occurrence of "some damage" as the result of the defendant's breach, then there is no reason or justification for arguing that the period should be tolled. Thus, *Reid* supports Larsen's position.

Respondents cite to *Schuster v. Magee*, No. C1-92-501, 1992 WL 213566 (Minn. App. 1992) (unpublished). Larsen rebutted respondents' reliance upon *Schuster* in its principal brief. This Court should disregard respondents' citation to *Schuster*. Respondents also rely upon a federal court case, *Anoka Ortho., P.A. v. Mutschler*, 773 F.Supp. 158 (D. Minn. 1991).[6] The *Mutschler* court stated, "the statute of limitations begins to run as of the date when the last professional service was performed." *Mutschler*, 773 F.Supp. at 169 (cited in appellant's brief at p. 31.) This statement is clearly a misinterpretation of Minnesota law in view of the later decisions in *Herrmann* and *Antone*. After the *Mutschler* decision, the Minnesota Supreme Court in *Herrmann* held that the claim accrued at the time of the first prohibited transaction in 1987, even though the defendant attorneys had continued to provide services for several years thereafter. *Herrmann*, 590 N.W.2d at 642-44. Thus, *Mutschler* is inconsistent with Minnesota Supreme Court case law, and must be disregarded.

In short, Minnesota law does not recognize the "continuous representation" doctrine as a means to toll the statute of limitations in professional liability cases. This Court should, therefore, dismiss respondents' separate notice of appeal.

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[6] Respondents also cited *Fletcher v. Zellmer*, 909 F.Supp. 678 (D. Minn. 1995), but in *Fletcher* the court did not apply the doctrine of continuing representation. *Fletcher*, 909 F.Supp. at 684.

IV. The Preparation of the 2001 Tax Returns Did Not Re-start The Limitations Period.

Respondents argue that the 2001 tax returns gave rise to an independent cause of action. But this argument is not supported by the case law. In particular, *Devereaux v. Stroup,* No. A07-0103, 2009 WL 72712 (Minn. App. 2008) (unpublished decision) does not support respondents' position. As set forth in Larsen's principal brief, the facts and holding in *Devereaux* are materially distinguishable from this case. The holding of *Devereaux* is that the attorney's new breaches in 2002 caused new and separate damages. Here, by contrast, the alleged breach in the 2001 returns was not a new act. Instead, it arose out of the same course of events as the alleged breach in the 2000 returns. Moreover, unlike in *Devereaux*, here the alleged breach in the 2001 returns did not cause new and distinguishable damage. Instead, that alleged breach merely failed to stem the increase in respondents' claimed damages. Because the second alleged breach did not cause new damage, *Devereaux* does not apply.

In addition, in *Devereaux* the court held that the second set of breaches of the duty of care, which caused new and separately calculable damage, did not re-start the limitations period for the earlier damages. 2009 WL 72712, *3. Stated differently, in *Devereaux* the second alleged breach did not toll the limitations period applicable to the first alleged breach and damages. Thus, to the extent *Devereaux* applies to this case, it does not allow respondents to sue regarding the 2000 returns.

Moreover, in this case the preparation of the 2001 returns for FMP and A&F occurred in February and March 2002, more than six years before respondents commenced this lawsuit. If *Devereaux* applies, the only claims that could properly be

asserted would be those arising out of the preparation and signing of the tax returns for FSA, which occurred in May 2002. Respondents' claims arising out of the 2001 returns for A&F and FMP would be time-barred. Contrary to respondents' arguments, this argument was properly presented to the district court. Larsen properly raised this issue to the district court, in reply to respondents' argument that the 2001 returns constituted a separate breach. Respondents did not move to strike that argument at the time, and they offer no authority for the position that raising an issue in a reply brief filed with the district court is insufficient to permit presenting the issue to the appellate court. Further, the district court's apparent emphasis on the filing deadline is misplaced. Focusing on the filing deadline elevates form over substance. The proper inquiry, as recognized by Boesen in his initial report, is the date on which the returns were "prepared and signed" by the professional for the client to file.

V. All of Respondents' Claims Accrued in Early 2001.

As noted above, the key question is when respondents' claim could have survived a Rule 12 motion to dismiss. "A cause of action survives a motion to dismiss as long as 'some damage' has occurred as a result of the alleged malpractice." *Herrmann*, 590 N.W.2d 343, *Antone*, 720 N.W.2d at 336. Here, as demonstrated above, the alleged breach first occurred upon the preparation and signing (in plaintiff's expert's words) of the 2000 tax returns in early 2001. And the alleged damages began to occur at that point, as well. This Court should answer the certified question by instructing the district court that a claim arising out of the failure to make 754 elections accrues when the tax returns are prepared and signed by the professional for filing by the taxpayer.

VI. The District Court Properly Certified the Issue as "Important and Doubtful."

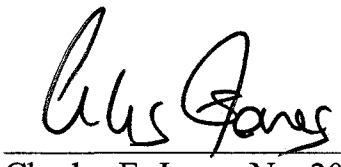
Finally, this Court should reject respondents' argument that the issue was not properly certified as "important and doubtful." Since respondents merely incorporated their prior motion to dismiss, Larsen's response to this argument is to incorporate its September 23, 2010 memorandum in response to respondents' motion to dismiss.

CONCLUSION

A claim arising out of the failure to make 754 elections accrues when the tax returns are prepared and signed by the professional for filing by the taxpayer. In this case, that occurred in early 2001. Because respondents waited more than seven years after that date to commence their lawsuit, their claims are time-barred.

Respectfully submitted,

Dated: December 15, 2010

By: 

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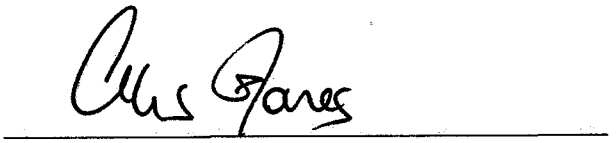

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