

**Darby Scott, Ltd. v Michael S. Libock & Co. LLC
CPAs**

2020 NY Slip Op 34343(U)

December 31, 2020

Supreme Court, New York County

Docket Number: 653044/2013

Judge: Robert D. Kalish

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**SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY**

PRESENT: <u>HON. ROBERT DAVID KALISH</u> <p style="text-align: center;"><i>Justice</i></p> <p>-----X</p> <p>DARBY SCOTT, LTD.,</p> <p style="text-align: right;">Plaintiff,</p>	PART	IAS MOTION 29EFM INDEX NO. <u>653044/2013</u> MOTION DATE <u>12/10/2019</u> MOTION SEQ. NO. <u>006</u>
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- v -

MICHAEL S. LIBOCK & CO LLC CPAS, MICHAEL LIBOCK

Defendant.

-----X

**DECISION + ORDER ON
MOTION**

HON. ROBERT D. KALISH, J.S.C.:

The following e-filed documents, listed by NYSCEF document number (Motion 006) 185-211, 218-279, 286-287 were read on this motion for summary judgment.

Motion seq. 006 by defendants Michael S. Libock & Co. LLC CPAs (Libock CPA) and Michael S. Libock (Libock) (collectively, “defendants”), pursuant to CPLR 3212 for summary judgment dismissing the complaint is granted.

This accounting malpractice action arises out of services rendered by defendants for plaintiff Darby Scott, Ltd. (plaintiff or the Company) between October 2003 and October 2010. After discovery, plaintiff seeks damages consisting of (a) \$269,053 in unaccounted-for inventory, (b) \$156,908 in overpayments to vendors, (c) \$219,831 in fees paid to Libock CPA and (d) \$14,150 for remediation efforts necessitated by defendants’ malpractice. Defendants now move for summary judgment, pursuant to CPLR 3212, dismissing the complaint.

BACKGROUND FACTS AND PROCEDURAL HISTORY

The following facts are taken from the parties' pleadings, deposition transcripts, affidavits and documentary evidence, and are undisputed unless otherwise indicated. The Company is a designer and manufacturer of luxury women's clothing, handbags, jewelry, and other apparel and accessories. Between 2003 and 2010, it sold primarily to luxury retailers, such as Neiman Marcus, Bergdorf Goodman (Bergdorf), and Saks Fifth Avenue, and directly to individual customers. The Company's largest customers were Neiman Marcus and Bergdorf (together NM/BG). Karen Darby Scott (Scott) is the president of plaintiff (Karen Darby Scott Affidavit [Dkt. 278] ¶¶ 1, 3-4).¹

Libock CPA is an accounting firm, of which Libock is a partner. Libock is a certified public accountant licensed in New York and New Jersey and is a member of the American Institute of Certified Public Accountants (Michael S. Libock Affidavit [Dkt. 189] ¶¶ 1-2).

In or around September 2003, Scott met with Libock, who at the time was a partner at the accounting firm of Libock & Friedkin Co. LLC (Libock/Friedkin), to discuss her company's engagement of his firm (Scott Aff. ¶ 14). On or around October 1, 2003, Scott executed an engagement letter (Mark Anesh 12/10/2019 Affidavit [Dkt. 187], Ex. D [Dkt. 193]) retaining Libock/Friedkin. In it, the firm agreed to provide the following services:

We will assign a senior staff person to perform bookkeeping and administrative tasks, including but not limited to -- entering bills, paying bills, entering factor advances, reconciling bank and factor accounts, contacting customers, preparing quarterly sales tax returns, recording payroll from ADP records, etc. Our fee for this service will be \$400 per week.

¹ References to "Dkt." followed by a number refer to documents filed in this action in the New York State Courts Electronic Filing (NYSCEF) system.

We will prepare your corporate business tax returns and your individual tax returns for you and your immediate family for the year ending December 31, 2003.

We will be available to prepare any additional financial or tax compliance analysis or reports that you may require.

In 2004, Libock formed a new accounting firm, defendant Libock CPA (Libock Aff. ¶ 9).

On or about November 29, 2004, the Company retained Libock CPA pursuant to another engagement letter (Anesh Aff. 12/10/2019, Ex.E [Dkt. 194]) which provided for the same services identified in the first engagement letter, but for a fee of \$600 rather than \$400 per week. Both engagement letters stated: “Our fee assumes adequacy of records, internal controls and cooperation and assistance of your accounting personnel.” The letters also provided that their terms would “serve as an understanding [of] the nature of our engagement on a continuing basis unless sooner terminated in writing by either of us.”

Michael S. Libock’s Testimony

Libock testified that he understood that under his engagement agreement with the Company, his firm was to provide the Company with a bookkeeper one day a week to pay the bills that Scott authorized, book its staff’s sales, record receipts of accounts receivable, record payroll and prepare quarterly sales tax returns (Libock Aff. ¶ 16; Libock Deposition Transcript 23:19-24). From 2003 to 2006, his firm arranged for at least two of its employees, including Kami Pyun (Pyun), an accountant, and Fran Kummerfeldt (Kummerfeldt), a bookkeeper and QuickBooks specialist to provide the bookkeeping services. From 2006 to 2010, his firm arranged for a 1099 independent contractor, Susanne Gil (Gil), to provide the bookkeeping

services (*id.*, ¶ 15). Pyun, Kummerfeldt and Gil would travel to the Company's offices each week to help keep track of the receivables/payables, enter pertinent information into QuickBooks, present Scott with completed invoices for her to approve payment, and draw checks for her review and execution. Scott was the sole signatory for the Company (*id.*, ¶¶ 17, 26-27).

According to Libock, the Company employed a small team of production assistants (the Production Department) that was responsible for its day-to-day operations. From 2007 to 2010, Theresa A. Guirola (Guirola) was Scott's lead production assistant. Between 2003 and 2010 the team's other employees included Joan Jungwirth (Jungwirth), Hillary Hart (Hart), Nichole Jones (Jones) and Solange Khavkine (Khavkine) (*id.*, ¶ 7).

The Production Department and Scott provided Gil with the information she used to perform her bookkeeping services (*id.*, ¶ 19). They were also responsible for the physical handling, packaging and tracking of inventory and orders, including the shipping and product returns (*id.*, ¶ 7, 20). Because the Company used a periodic rather than perpetual inventory system, its inventory was not tracked in QuickBooks (*id.*, ¶¶ 21-22).² Libock CPA did not

² As one treatise explains:

“A *perpetual* inventory system keeps a continuous record of the cost of inventory on-hand and the cost of inventory sold. Under the perpetual inventory system, when a company purchases an item of inventory, it increases the asset inventory or raw material, of any item claimed, by the invoice cost of the merchandise plus other applicable charges. Because of computer technology, many industries, such as retail stores, use a perpetual inventory system. The computer system simultaneously increases cash (or accounts receivable) and sales revenue for the item's sales price, reduces inventory and increases cost of goods sold by the amount of that item's cost, and updates the count of the quantity of inventory on-hand.

A *periodic* inventory system does *not* keep a continuous record of the on-hand and sold (removed),

perform any services for the Company with respect to its inventory (*id.*, ¶ 12), other than prepare tax returns based upon the inventory information provided by the Production Department once a year (*id.*, ¶ 22).

Libock further testified as to his understanding that Scott did not always properly secure the Company's inventory. Libock testified that Scott left valuable jewelry and handbags in a storage room that was not always locked, and even when it was locked, could be accessed by any member of the Production Department. Libock further claimed that without maintaining a dedicated inventory log, Scott loaned out jewelry and handbags to employees, transported items for off-site sales and provided them for photo shoots and promotional events (*id.*, ¶ 25). Libock also stated that he understood that Scott had filed an "employee dishonesty claim" with Travelers Insurance, alleging that the Company's own employees were responsible for theft but never recovered on it. Libock testified that Scott also reported said theft to the NYPD and the New York District Attorney's office but no individual or entity was ever charged (*id.*, ¶ 35).

In or around the summer of 2010, Libock claimed that the relationship between Scott and Gil became contentious and that Gil no longer desired to perform services for the Company. It was during this same period that Scott began making accusations regarding stolen inventory and requested that his firm investigate her claims (*id.*, ¶¶ 31-32). Libock stated that because his firm's engagement with the Company did not cover such services, Libock presented Scott with a

but it determines the inventory at the end of each accounting period by physically counting. Because a periodic inventory system does not reduce the inventory account on an ongoing basis, the only time the company knows the cost of its inventory or the cost of goods sold is when it counts inventory."

(Billie M. Cunningham, et al., *Accounting Information for Business Decisions* [2000] at 172-75.)

further engagement letter providing for an analysis of the Company's records to uncover potentially stolen funds and/or inventory for an additional fee. Libock asserted that the parties discontinued their relationship after they were unable to reach an agreement regarding the newly-requested services (*id.*, ¶¶ 33-34).

Karen Darby Scott's Testimony

According to Scott's affidavit, when she met with Libock in September 2003 she described the Company's business and explained to him that a portion of its sales were through consignment. She also told him that the Company did not have accounting personnel and that it therefore wanted to retain an accounting firm to take care of all the accounting and financial aspects of its business. She claimed that Libock specifically told her that he and his firm would establish internal controls for inventory and recordkeeping, and that he never advised her that his engagement was limited in any way (Scott Aff. ¶¶ 14-18). At her deposition, however, Scott could not recall the "sum and substance" of any specific conversation with Libock about internal controls or the adequacy of records (Anesh Aff., Ex. G [Dkt. 196] [Scott Deposition Transcript 10/24/2017], 136:20-138:10).

Scott stated that personnel from Libock CPA thereafter served as the Company's "de facto accounting department" and performed a number of services not specifically enumerated in the engagement letters. These services included meeting with potential investors, preparing loan applications, and discussing new business efforts, providing advice on factoring and vendor agreements, hiring interns, and completing health insurance enrollments (Scott Aff. ¶¶ 24-25). Scott also contended that Libock told her that one of his firm's employees was setting up the

Company's inventory controls (*id.*, ¶ 26). She claimed that Libock never made any recommendations with respect to internal controls or advised her that there was anything wrong with them, so she assumed the controls were adequate (*id.*, ¶ 53).

Scott asserted that in 2004, Libock sent her a list of bookkeeping errors that his firm had discovered, including large overpayments to vendors (Robert A. O'Hare, Jr. Aff. [Dkt. 219], Ex 22 [Dkt. 241].) She said she assumed that his firm was addressing the errors and that they would not be repeated (Scott Aff. ¶ 28.). However, Scott stated that she made several complaints to Libock over the years about the quality of his personnel's work, particularly relating to the collection of accounts receivable, and she states that Libock promised to address the issues. Scott further stated that she was also aware of minor disputes with retailers over what items were received or returned, but she stated that she was copied on the relevant communications and understood that defendants were handling them (*id.*, ¶¶ 51-52).

Scott confirmed that Libock assigned Gil to her company between 2006 and 2010, praising her work and saying that she would watch the Company's pennies as if they were her own (*id.*, ¶ 29). Scott stated that she understood that Gil had access to NM/BG's online system, from which she could retrieve information about sales, returned merchandise, and check remittances to the Company. Scott further understood that nothing could be entered into NM/BG's inventory without the product first being entered as a purchase order and the product being listed on a computer manifest. Also, nothing could be returned from NM/BG without it being reflected on a return-to-vendor (RTV) document (*id.*, ¶¶ 33-34, 47). Gil was responsible for reviewing, with one of the Company's production assistants, NM/BG's weekly reports

reflecting sales of the Company's products to ensure that payment was received on sold items (*id.*, ¶ 35). Gil also monitored the bank statements, merchandise shipping and return documentation relating to private customers and reviewed and reconciled spreadsheets reflecting the transactions with a production assistant and Scott (*id.*, ¶¶ 36-40, 45-46, 48)

Scott's affidavit asserts that defendants had access to all documents necessary to track the Company's inventory, including invoices and shipping records, customer's sell-through reports, RTV reports, checks remittances and other receiving documents, and that such information was recorded in QuickBooks (*id.*, ¶¶ 41-43). At her deposition, however, Scott testified that she did not know where defendants got the information that was entered into QuickBooks (Scott Dep. Tr. 10/24/2017, 98:3-9). She also testified that Libock did not work on the premises but would review the Company's year-end reporting of the inventory (A nesh Aff., Ex. H [Scott Deposition Transcript 10/26/2017], 39:25-40:3). Nevertheless, she says she understood that defendants were maintaining a perpetual inventory system to which she was providing periodic updates, and she was never informed of any shortage of inventory (Scott Aff. ¶¶ 41-44). She also stated that she and the Production Department physically handled the inventory, not Gil (Scott Dep. Tr. 10/24/2017, 175:22-176:9; *see also* Ex. F [Interrogatory Responses] ¶¶ 18-19). Up to five times a year, she and her in-house staff would count the inventory and pass the information on to defendants to reconcile with the Company's records (Scott Dep. Tr. 10/24/2017, 275:21-277:1; *see also* Interrogatory Responses, ¶ 20).

In August or September of 2010, Scott asserted that she was advised by NM/BG that they were getting invoices for goods they had never received or which had been returned. They told

Scott that they had previously told Gil about the problem and had informed her that some invoices they had paid had been reissued and doctored to show different items and new amounts. NM/BG claimed that the practice had been going on for years while they were regularly in communication with defendants' staff. When Scott asked Libock whether he reviewed Gil's work he said there was no need because it was beyond reproach (Scott Aff. ¶¶ 54-55, 57).

Libock emailed NM/BG in September 2010 about the issue. However, after Libock insisted that Scott sign a new engagement letter as a condition of reviewing the matter, she lost confidence in his firm and terminated her Company's relationship with it. When the Company again sought defendants' assistance in investigating the matter in 2013, defendants refused to cooperate because Scott would not sign a release (*id.*, ¶¶ 59-60).

Also following the discovery of the problem with NM/BG, the Company retained AlixPartners LLC (Alix) to perform a forensic analysis of its book and records. Alix concluded that the accounting records managed by Libock were in complete disarray and the invoices, payments on invoices, credit memos, and RTV records could not be reconciled. In the course of the review, Scott also found a 2006 check for \$21,441.04 payable to Larry Weber (Weber), one of the owners of one of her largest vendors, Finesse La Model (Finesse). Although the check bears her purported signature, Scott asserted that she never would have signed a check payable to an individual rather than the company and had always made previous check payable to Finesse. Furthermore, while the check was supposedly issued to pay off Finesse's 2004 invoices, she found no documentary record of that debt, and Weber never mentioned it during their near-daily conversations in 2006 (*id.*, ¶ 65).

Scott also discovered that entries were being made in QuickBooks without supporting documentation, and that Gil was constantly deleting QuickBooks and Excel spreadsheets. When she presented her findings to an NYPD financial investigator, he told her that he did not think defendants knew what they were doing, but that the records were in such disarray that a criminal investigation would be difficult. A detective at the NYPD financial crimes unit suggested that she should consider bringing a civil lawsuit (*id.*, ¶¶ 68-71).

Susanne Gil's Testimony

Gil earned a BBA in accountancy and a certified bookkeeper certificate (Anesh 12/10/2019 Aff., Ex. K [Gil Deposition Transcript], 11:2-3, 15-16). She worked at the Company only one day a week, starting in 2006 (*id.* 18:4-9; 24:15-25). She entered vendor invoices, sales invoices and payroll reports into QuickBooks and prepared tax returns (*id.* 27:24-28:9). The information she entered was based upon documentation supplied by Company employees (*id.* 65:22-67:19; 68:5-14). She would prepare and present checks to Scott for signature in connection with accounts payable (*id.*, 89:22-90:2).

Gil also issued credit memos for a returned item after confirming with Scott or a staff member that the item matched that on the relevant invoice (*id.*, 104:3-12). Gil stated that she could not make adjustments without their input because she did not deal with inventory (*id.*, 30:13-17; 104:20-105:6). She did not make adjustments to the inventory account when an item was shipped because she did not maintain a perpetual inventory. The only accounts affected were receivables and sales. Inventory would be adjusted at the end of the year when Scott gave Libock the value she thought she had in inventory (*id.*, 9:25-30:7; 100:6-21). Gil did not know where the

inventory was stored in the Company's first office, and she did not have a key to the vault in which the inventory was kept after the Company moved (*id.*, 71:23-72:10).

Gil stopped working for the Company on August 26, 2010 (*id.*, 59:13).

Theresa A. Guirola's Testimony

Guirola started working at the Company in the late summer or early fall of 2007 as an assistant to Scott (Anesh Aff. 12/10/2019, Ex. I [Theresa A. Guirola Deposition Transcript], 15:13-15; 19:5-16). Over time her responsibilities increased and she became a production coordinator (*id.*, 15:25-16:3). She organized the office and the closets, merchandised collections for buyers at Bergdorf, responded to customer inquiries, repaired merchandise, sourced skins, checked on production at the factory, and helped pack and deliver merchandise (*id.*, 21:14-18; 22:18-23:4; 25:7-24). No one from Libock's office packed or delivered merchandise (*id.*, 27:9-11).

The inventory was kept in a locked room which could be accessed by means of a key by members of the Company's staff who were counting inventory or loaning out a bag for a magazine shoot (*id.*, 31:7-22). One project Guirola started in late 2007 or early 2008 was comparing factory orders for merchandise to the actual physical inventory (*id.*, 36:14-18; 53:5-10; 56:7-57:18). Additionally, she would participate in periodic, random checks of inventory, but did not believe that Gil or anyone from Libock's office played a role in checking it (*id.*, 60:23-61:15). Guirola used the Lightspeed program for tracking it (*id.*, 35:21-26:9; 38:8-14; 40:18-22), but did not remember how the Company kept an accurate record of the inventory before it was used (*id.*, 40:23-41:3). Excel was also used to track inventory, but not QuickBooks

(*id.*, 57:19-58:3). At times employees would borrow products for social occasions but Guirola did not believe these loans were recorded (*id.*, 165:20-166:25).

Gil was the one who primarily used QuickBooks at the Company. Guirola only used the program in connection with deliveries to Bergdorf or processing an RTV (*id.*, 34:19-35:6). Guirola would communicate with Gil about RTVs for the purpose of determining whether the item had to be billed or paid for but did not inform Gil whether it was being returned to inventory because that was not her area (*id.*, 124:12-125:4). Guirola's employment at the Company was terminated in September 2010 (*id.*, 51:14-17).

Sandra Louise Mayo's Testimony

Mayo is the general manager of the Company (Sandra Louise Mayo Affidavit [Dkt. 279] ¶ 1). Mayo was hired as Scott's assistant in August 2014 to help with production and customer support (Anesh 12/10/2019 Aff., Ex.N [Dkt. 203] [Sandra Louise Mayo Deposition Transcript 4/12/2018] , 9:12-15; 20:13-20). Her highest level of education is high school and before joining the Company she worked as an office manager at a machine shop for 21 years (*id.*, 10:10-12; 14:6-11).

Shortly after the termination of defendants' services to the Company, Mayo commenced an investigation to determine if any items were missing from the Company's inventory. Alix assisted her in the investigation and analysis. For the period between January 1, 2003 and October 11, 2010, she examined invoices received from the Company's vendors in connection with the production of each product and the Company's QuickBooks payment records and hardcopy records relating to payments made to vendors. For the period between October 1, 2003

and December 31, 2010, she examined the Company's QuickBooks report of sales, and customer sales invoices and return-to-vendor reports. She also examined the Company's 2010 year-end inventory spreadsheet, which identified products in physical inventory as of December 31, 2010 (Mayo Aff. ¶¶ 5-6).

Mayo first determined the total number of handbags, wallets and similar products (collectively handbags) that were in the Company's inventory at any time during the Company's engagement by compiling the vendors' invoices and the Company's corresponding payment records for the merchandise. From those records, she created a spreadsheet (the historical spreadsheet) compiling the identifying information including invoice numbers, check numbers, product model numbers, product material and colors. After that, she compared the information in the spreadsheet to the Company's sales records, including the Company's QuickBooks sales reports between October 1, 2003 and December 31, 2010, to determine which inventory had been sold. She then reviewed the Company's return-to-vendor reports and payment records to establish how many items had been returned. Comparing the data on the historical spreadsheet with the Company's 2010 year-end inventory spreadsheet, she established the number of items that were unaccounted for (*id.*, ¶¶ 7-18).

To complete the analysis, she calculated the Company's damages by determining the total cost to manufacture the products, reviewing receipts and invoices reflecting the costs of the materials and labor. She concluded that there were 256 handbags missing with a total value of \$259,865 (*id.*, ¶¶ 19-20). Using a similar methodology, she determined that there were 18 missing pieces of jewelry with a total value of \$9,187 (*id.*, ¶¶ 21-25).

Mayo also sought to determine whether the Company had made overpayments to its vendors. To this end, she reviewed statements of accounts from Finesse between 2000 and 2006, the Company's QuickBooks and hardcopy records of amounts owed and paid to Finesse between 2003 and 2010. She found that there were \$156,908.02 in overpayments made to Finesse between January 2003 and February 2006 (*id.*, ¶¶ 26-31).

At her deposition, Mayo testified that she was not familiar with QuickBooks and did not use it as Scott's assistant, except to review the Company's QuickBooks files in connection with the investigation described above (Mayo Dep. Tr. 25:18-26:9). She believed that QuickBooks was used to track inventory but did not recall if anyone told her that. She did not know how the Company tracked its inventory between 2003 and 2010 or whether it employed a perpetual inventory system (Anesh 12/10/2019 Aff., Ex.O [Dkt. 204] [Sandra Louise Mayo Deposition Transcript 4/18/2018] 130:15-22; 140:20-141:2).

In preparing the spreadsheet to identify unaccounted for inventory, she determined that receipts were missing but did not seek to recover them from the vendors (*id.*, 123:2-125:15). Apart from vendor invoices, she did not rely on any other evidence that the items actually came into the Company's possession (*id.*, 126:24-127:3; 182:21-183:15). Each item had an identifying model number but if several identical handbags were received, they would share the same model number. During Mayo's tenure each item was made trackable with a unique bar code; but Mayo could not say whether this was the case for the items that she reviewed (*id.*, 127:8-128:18).

Testimony of Andrew P. Ross (Defendant's Expert)

Defendant's expert, Andrew P. Ross (Ross), is a certified public accountant, certified

fraud examiner, a certified valuation analyst, and a partner in the accounting firm of Gettry Marcus CPA, P.C. (Andrew P. Ross Affidavit [Dkt. 188] ¶ 1). Upon a review of the record in this action, Ross opined, with a reasonable degree of certainty, that defendants did not owe the Company a specific duty to track or safeguard inventory or to implement or maintain internal controls related to the physical custody of the inventory, did not depart from the applicable standard of care in performing accounting services to the Company, and did not cause any damages to the Company (*id.*, ¶¶ 5-10). He stated that pursuant to generally accepted business and accounting practices, the obligation to track and safeguard the inventory would fall upon the Company, and that this obligation was confirmed by the engagement letters (*id.*, ¶¶ 12-14), the Company's actual procedures with respect to the safeguarding and tracking of inventory (*id.*, ¶¶ 15, 24-29), its use of a periodic rather than perpetual inventory system (*id.*, ¶¶ 17-22, 40-41) and defendants' lack of any actual involvement with the inventory (*id.*, ¶¶ 14-16), including its use of QuickBooks, which was not used to track inventory (*id.*, ¶¶ 10, 17, 30).

Ross additionally disputed Mayo's calculation of the Company's damages. He discounted her reliance on the QuickBooks records in view of his conclusion that that program was not employed to track inventory. With respect to her analysis of the loss of handbags and jewelry, he faulted her spreadsheets for failing to include basic information such as the date that the item was first entered into inventory or sold to a customer, any associated sales invoice or purchase order numbers, and the date that the item was first discovered to be missing (*id.*, ¶¶ 43-45).

As to the alleged overpayments to Finesse, Ross again criticized Mayo's reliance on QuickBooks. He also criticized her use of records pre-dating defendants' engagement, and her

reliance on handwritten invoices from Finesse. He asserted that her analysis was not a proper forensic accounting, but merely a comparison of flawed records which failed to account for the fact that Scott herself affirmatively approved the payment of the invoices (*id.*, ¶ 46). Finally, he opined that in addition to the fact that defendants lacked any obligation to track inventory, the records contain no evidence that they contributed to the losses. Rather, he contended that the Company's own lax inventory control systems caused the losses (*id.*, ¶¶ 47-42).

Testimony of Brian Jenkins (Plaintiff's Expert)

Plaintiff's expert, Brian Jenkins (Jenkins), is a certified public accountant, certified fraud examiner and a director at Alix (Brian Jenkins Affidavit [Dkt. 276] ¶ 1). Jenkins averred that in 2014 his firm analyzed 139 invoices for product shipments to Bergdorf totaling \$211,506 which were recorded in the Company's QuickBooks records between October 2005 and October 2009. Alix determined that Bergdorf did not acknowledge the documentation as representing either products received, or amounts owed to the Company. Furthermore, Alix's own analysis revealed incomplete or inaccurate supporting documentation for the invoices, including missing documentation for credit memos or payments recorded in QuickBooks, or misapplied credit memos or payments. In performing the analysis, Alix assumed the completeness and accuracy of the Company's QuickBooks records, supporting accounting records, and of Bergdorf's records (*id.*, ¶¶ 8-9, 10 fn.4).

Jenkins stated that 118 of the 139 invoices (reflecting \$170,658 in merchandise) had no supporting documentation for a credit memo recorded in QuickBooks; 13 invoices (reflecting \$23,091 in merchandise) had payments and credit memos that were misapplied in the records;

and 8 invoices (representing \$17,757 in merchandise) had no supporting documentation for the payment reflected in the records (*id.*, ¶ 10). Jenkins concluded that these discrepancies “impugn[] the validity of the accounting records and raises the possibility of fraud and/or missing inventory” (*id.*, ¶ 11).

Jenkins additionally contended that through Gil, defendants were aware of ongoing accounting issues. For this conclusion, he relied upon Gil’s deposition testimony regarding the issuance of two invoices with the same number to Neiman Marcus, the invoicing of Bergdorf with the wrong order numbers, and the voiding of certain Bergdorf invoices for merchandise that was apparently never received. He also noted that Gil described "ongoing" and "constant" issues with invoices provided to and credits taken by the Company’s customers, including Bergdorf. Jenkins concluded that defendants’ failure to supervise Gil constituted a violation of the American Institute of Certified Public Accountants (AICPA) Rules of Conduct and professional standards (*id.*, ¶¶ 12-33). He further concluded that defendants failed in their professional obligation to inform the Company of the ongoing accounting issues (*id.*, ¶¶ 34-37).

Finally, Jenkins asserted that he reviewed Mayo’s affidavit and understood that she used a methodology similar to the one he would have employed, and further understood from her analysis that the Company suffered the specified total damages of \$425,961. He disagreed with Ross that her reliance on the Company’s QuickBooks records was problematic, because the programs contained information regarding the acquisition of inventory, sales and returns, and because Mayo relied on other supporting documentation as well as a physical inventory count. Respecting the alleged overpayments to Finesse, Jenkins noted that Scott had no financial or

accounting background and was entitled to assume that defendants would resolve the bookkeeping errors, including vendor overpayments that defendants identified in the list they sent her in 2004. Again relying on his review of the Mayo affidavit, he expressed his understanding that the overpayments to Finesse totaled \$156,908. He concluded with a reasonable degree of certainty, under the assumption that Mayo's calculations were accurate and correct, that defendants' failure to inform the Company of the ongoing accounting issues contributed to the Company's damages (*id.*, ¶¶ 38-48).

Plaintiff commenced this action on August 30, 2013. As relevant here, defendants moved to dismiss on statute of limitations grounds in April 2014. The motion was denied by the court (Hagler, J.) by order dated October 6, 2014 [Dkt. 35] for the reasons stated on the record, although neither party has submitted the transcript of oral argument setting forth the reasons.

In addition to the claims discussed above, the complaint alleges that defendants issued fictitious invoices to cover-up theft of inventory, diverted company funds, diverted inventory to facilitate sales unlawfully made outside of the Company, diverted sales revenue, including in connection with internet sale, inflated purchase orders, falsified the recording of accounts payable, paid falsely inflated vendor invoices, destroyed electronically-stored financial information, and prepared financial statements and tax returns containing materially false and misleading entries (Complaint ¶ 14). However, Plaintiff does not address, and has thus abandoned, those claims on this motion.

Defendants now seek dismissal asserting that (1) the statute of limitations has expired, (2) plaintiff has failed to establish that defendants owed it or departed from any duty of care, (3)

plaintiff has failed to demonstrate that defendants caused any damages, and (4) defendants cannot be held liable for any actions by Gil's as she was an independent 1099 contractor.

DISCUSSION

“The proponent of a summary judgment motion must make a *prima facie* showing of entitlement to judgment as a matter of law, tendering sufficient evidence to eliminate any material issues of fact from the case. Failure to make such showing requires denial of the motion, regardless of the sufficiency of the opposing papers.” (*Santiago v Filstein*, 35 AD3d 184, 185-86 [1st Dept 2006], quoting *Winegrad v. New York Univ. Med. Ctr.*, 64 NY2d 851, 853 [1985].) “Once this showing has been made, the burden shifts to the nonmoving party to produce evidentiary proof in admissible form sufficient to establish the existence of material issues of fact that require a trial for resolution.” (*Giuffrida v Citibank Corp.*, 100 NY2d 72, 81 [2003].) “On a motion for summary judgment, facts must be viewed in the light most favorable to the non-moving party.” (*Vega v Restani Constr. Corp.*, 18 NY3d 499, 503 [2012] [internal quotation marks and citation omitted].) In the presence of a genuine issue of material fact, a motion for summary judgment must be denied. (*See Rotuba Extruders v Ceppos*, 46 NY2d 223, 231 [1978]; *Grossman v Amalgamated Hous. Corp.*, 298 AD2d 224, 226 [1st Dept 2002].)

Statute of Limitations

As a threshold matter, it is clear that all of plaintiff's claims for damages are time-barred. The statute of limitations for nonmedical malpractice, including accounting malpractice, is three years, which applies “regardless of whether the underlying theory is based in contract or tort” (CPLR 214(6); *see RGH Liquidating Trust v Deloitte & Touche LLP*, 47 AD3d 516, 517 [1st Dept

2008]; *Maya NY, LLC v Hagler*, 106 AD3d 583, 586 [2013]). The “claim accrues when the malpractice is committed, not when the client discovers it” (*Williamson ex rel. Lipper Convertibles, L.P. v PricewaterhouseCoopers LLP*, 9 NY3d 1, 7–8 [2007]). More specifically, the cause of action “accrues upon the client's receipt of the accountant's work product since this is the point that a client reasonably relies on the accountant's skill and advice” (*id.* at 8, quoting *Ackerman v Price Waterhouse*, 84 NY2d 535, 541 [1994]).

This action was commenced on August 30, 2013, a date which would render time-barred claims for any act of malpractice committed prior to August 30, 2010. Plaintiff has not identified, and the record does not reflect, any work product produced by defendants after that cut-off date. To the contrary, with respect to the missing handbags and jewelry, Mayo expressly relies on the QuickBooks records maintained by defendants which, at the latest, would have been updated by Gil on the date of her departure on August 26, 2010. The last invoices analyzed by Alix are even older, dating back to October 2009. Older still is the work product evidencing the alleged overpayments to Finesse, produced between 2004 and 2006. To the extent plaintiff's claims are based on the accountants' breach of their professional duty to supervise Gil, the malpractice statute of limitations would extinguish them, and in any event, the limitations for negligent hiring and supervision is also three years (*Kerzhner v G4S Gov't Sols., Inc.*, 138 AD3d 564, 565 [1st Dept 2016]). Defendants' alleged failure to institute internal inventory controls would likewise be encompassed by the malpractice limitations period.

Plaintiff's reliance on the continuous representation doctrine is misplaced. For that doctrine to apply, “the continuous representation must be in connection with the particular

transaction which is the subject of the action . . . and not merely during the continuation of a general professional relationship” (*Zaref v Berk & Michaels, P.C.*, 192 AD2d 346, 347–48 [1st Dept 1993]; *Transp. Workers Union of Am. Local 100 AFL-CIO v Schwartz*, 32 AD3d 710, 713 [1st Dept 2006]). Thus, “[t]he mere recurrence of professional services does not constitute continuous representation where the later services performed were not related to the original services” (*Mitschele v Schultz*, 36 AD3d 249, 253 [1st Dept 2006]). This is true even where the plaintiff alleges that the defendant exercised “general and unfettered control of [its] financial, tax and investment affairs” (*Zaref*, 192 AD2d 346, 348).

As discussed above, defendants here have established that the three-year statute of limitations bars the alleged malpractice claims. Thus, the burden shifts to plaintiff to establish a triable issue of fact as to the applicability of the continuous representation doctrine. (*Overseas Shipholding Group, Inc. v Proskauer Rose, LLP*, 130 AD3d 415, 421 [1st Dept 2015] [concurring opinion]). Plaintiff has not met this burden here. Notwithstanding that the engagement letters promised to provide bookkeeping and administrative services on “a continuing basis,” this, at most, merely points to the existence of a general professional relationship. (*Zaref*, 192 AD2d at 347–48.) It cannot be interpreted as a general and prospective waiver of the statute of limitations defense. Plaintiff has failed to identify any services rendered after August 30, 2010 that relate to the allegedly negligent transactions causing inventory loss between 2003 and August 30, 2010. To repeat, any allegedly negligent transaction causing losses could not have possibly occurred after August 26, 2010—the last day that Gil worked—and the evidence that Plaintiff points to in support of the malpractice claims were individual and separate

transactions that date to October 2009 at the latest. At most, plaintiff attempted, but failed, to secure defendants to perform the forensic analysis it ultimately delegated to Alix and Mayo. Plaintiff therefore fails to point to any specific work done by Defendants after August 30, 2010, that connects to the alleged negligent acts.

Finally, the October 2014 order denying defendants' motion to dismiss on statute of limitations grounds is not law of the case. Although the precise grounds for the dismissal are unclear, the motion was decided before joinder of issue and without the benefit of discovery (*Overseas Shipholding Group, Inc.*, 130 AD3d at 421 [concurring opinion] [stressing the need to revisit the applicability of the continuing representation doctrine on a motion for summary judgment after discovery notwithstanding the trial court's denying a motion to dismiss on said grounds]). Moreover, defendants thereafter preserved the affirmative defense by asserting in their answer, which was never the subject of a motion to strike.

Duty of Care

Plaintiff's claims would fail even if they were asserted in a timely manner. "A party alleging a claim of accountant malpractice must show that there was a departure from the accepted standards of practice and that the departure was a proximate cause of the injury," (*KBL, LLP v Cmty. Counseling & Mediation Servs.*, 123 AD3d 488, 488 [1st Dept 2014]; see *D.D. Hamilton Textiles, Inc. v Estate of Mate*, 269 AD2d 214, 215 [1st Dept 2000]). Furthermore, "[i]t is well settled that a plaintiff must establish, beyond the point of speculation and conjecture, a causal connection between its losses and the defendant's actions" (*Herbert H. Post & Co. v Sidney Bitterman, Inc.*, 219 AD2d 214, 224 [1st Dept 1996]). Although the scope of professional

accounting standards generally go beyond simple bookkeeping and auditing, the obligations may be expressly defined, and limited, by the terms of the parties' engagement agreement (*Friedman v Anderson*, 23 AD3d 163, 165 [1st Dept 2005]; *Italia Imports, Inc. v Weisberg & Lesk*, 220 AD2d 226, 226–27 [1st Dept 1995]; *Cumis Ins. Soc., Inc. v Tooke*, 293 AD2d 794, 797 [3d Dept 2002] [“express terms of the contractual agreements” governed accountant obligation to “discover irregularities, errors and defalcations”]).

The record in this action refutes plaintiff's claim that defendants agreed or undertook any duty to track or safeguard plaintiff's inventory. The engagement letter did not offer a full range of professional accounting services, but was limited to “bookkeeping and administrative tasks.” Although the agreement stated that those tasks “includ[ed] but [were] not limited to” entering and paying bills and the like, that language did not expand the duties beyond the stated parameters of bookkeeping and similar responsibilities.

Scott's claim that Libock promised to establish internal controls for inventory and recordkeeping and that defendants acted as the Company's “de facto accounting department” are also devoid of evidentiary support. Scott agreed to the limited terms of the engagement letter days after the alleged promise was made, and she could not recall any specifics of the relevant conversation. Once the relationship commenced, it is undisputed that a Libock employee or contractor appeared at plaintiff's offices just once a week, and then only to record invoices and pay bills. Although on a handful of occasions defendants performed tasks not expressly listed in the engagement letter, most of them were routine and did not require advanced accounting skills.

Most significantly, the record demonstrates that plaintiff assumed all responsibility

associated with the inventory. Defendants did not have any physical access to the inventory, as it was handled exclusively by plaintiff's employees. Although defendants processed records which referenced plaintiff's inventory, the engagement letter provided that the fee that defendants agreed to "assume[d] adequacy of records, internal controls and cooperation and assistance of your accounting personnel." Defendants were therefore under no duty to look beyond the documentation and information provided to them by plaintiff, or to then take any other action related to plaintiff's inventory.

Defendants' and plaintiff's own procedures also confirm that defendants were not responsible for tracking inventory. As defendants' expert witness explains QuickBooks was not used for tracking inventory, and QuickBooks employed periodic rather than perpetual inventory systems. Neither of those points are disputed by plaintiff's expert. It was only after defendants' engagement ended that plaintiff attempted to track inventory using a perpetual inventory system, and then with Lightspeed or Excel rather than QuickBooks. Plaintiff's expert's observation that QuickBooks "is a repository of information pertaining to Plaintiff's acquisition of product, sales, and returns" is irrelevant to the question of whether the program tracked the actual inventory in plaintiff's possession, and ignores the fact that all the information in the repository was provided by plaintiff with a guarantee of its accuracy and completeness.

Causation/Damages

The court finds that defendants have prima facie established that plaintiff has not suffered any damages and that any possible damages were caused by defendants. In response, plaintiff has failed to establish a triable issue of fact on this point. The only actual analysis of plaintiff's

inventory was performed by its employee Mayo, who is not an accountant. In her deposition she admitted she was not familiar with QuickBooks, whether it was or could be used to track inventory, or whether it employed a perpetual inventory system. She did not know whether the items in plaintiff's inventory had unique identifiers such as barcodes prior to her employment. She also admitted that she did not attempt to secure missing vendor receipts. In the end, her affidavit does not establish that any item of inventory *was actually missing*, but only that some items were "unaccounted for" based on the available records.

As discussed above, QuickBooks was not used to track inventory, and that Mayo's analysis was flawed for assuming otherwise and for omitting basic identifying information. Plaintiff's expert does not meaningfully defend Mayo's work, but merely asserts that he "understands" that she used a methodology of which he might approve and that he "understands" that she made certain findings as to plaintiff's damages. However, plaintiff's expert did not perform his own independent investigation to confirm Mayo's analysis or calculations, so his apparent ratification of her conclusions must be disregarded (*Hambusch v New York City Transit Auth.*, 63 NY2d 723, 725 [1984]; *Gardner v Ethier*, 173 AD2d 1002, 1003 [3d Dept 1991]; *O'Shea v Sarro*, 106 AD2d 435, 437 [2d Dept 1984]).

In view of the lack of any competent, non-speculative proof that plaintiff lost any inventory, there can be no proof that defendants' acts caused any damages. And even assuming plaintiff lost inventory, plaintiff has not suggested how defendants' alleged negligence was responsible. Again, Defendants did not track inventory. Thus, even if—contrary to plaintiff's assumption—the QuickBooks record were properly maintained, defendants would not have been

alerted to inventory losses.

Liability for Actions of Gil as an Independent 1099 Contractor

The court agrees with plaintiff that there may be a question of fact as to whether Gil was actually functioning as an employee rather than an independent contractor, a point which defendants do not address (*see generally Cosmopolitan Med. Acupuncture Servs., P.C. v Allstate Ins. Co.*, 824 NYS2d 761 [App Term, 1st Dept 2006] [“While the reporting of annual pay on an IRS 1099 form may be significant in assessing whether the acupuncturists were independent contractors or employees, it is only one of the relevant factors in assessing the relationship which existed between plaintiffs and the acupuncturists”]). However, the issue is moot in view of the determinations reached above regarding the statute of limitations and liability on the merits.

In Closing

The court has considered the parties’ other arguments and finds them unavailing. As such, for all of the foregoing reasons, the action is dismissed

However, that this court has ruled in defendants favor should not be viewed as an endorsement of defendants’ professionalism and skill. Further, said ruling should not be viewed as a rejection of plaintiff’s dissatisfaction and frustration with defendants’ services. Said decision is only to say that, based on the evidence before it, this Court finds that plaintiff has failed to establish an issue of fact requiring a trial of the claims.

CONCLUSION

Accordingly, it is

ORDERED that the motion for summary judgment by MICHAEL S. LIBOCK & CO. LLC CPAS and, MICHAEL S. LIBOCK (collectively "defendants"), is granted, and the complaint is dismissed in its entirety, with costs and disbursements to defendants as taxed by the Clerk upon the submission of an appropriate bill of costs, and it is further

ORDERED that, within twenty (20) days, counsel shall serve a copy of the instant decision and order with notice of entry; and it is further

ORDERED that, upon being served with a copy of the instant decision and order with notice of entry, the Clerk is directed to enter judgment accordingly.

The foregoing constitutes the decision and order of the Court.

12/31/2020
DATE


ROBERT DAVID KALISH, J.S.C.

CHECK ONE:	<input checked="" type="checkbox"/>	CASE DISPOSED	<input type="checkbox"/>	NON-FINAL DISPOSITION
	<input checked="" type="checkbox"/>	GRANTED	<input type="checkbox"/> DENIED	<input type="checkbox"/> GRANTED IN PART
APPLICATION:	<input type="checkbox"/>	SETTLE ORDER		<input type="checkbox"/> OTHER
CHECK IF APPROPRIATE:	<input type="checkbox"/>	INCLUDES TRANSFER/REASSIGN	<input type="checkbox"/>	<input type="checkbox"/> SUBMIT ORDER
			<input type="checkbox"/>	<input type="checkbox"/> FIDUCIARY APPOINTMENT
				<input type="checkbox"/> REFERENCE