Kentucky Law Journal

Volume 49 | Issue 4 Article 7

1961

Accounting and the Unauthorized Practice of Law: Balance Sheet or Brief?

Robert C. Shelton
University of Kentucky

ACCOUNTING AND THE UNAUTHORIZED PRACTICE OF LAW: BALANCE SHEET OR BRIEF?

The overlapping of law and accounting in the field of taxation has made it difficult, if not impossible, to differentiate between what is properly the purview of the attorney and what is the field of the accountant.[1] It is understandable, therefore, why two of the world's oldest and most respected professions have engaged in a bitter controversy over their respective areas of activity. If the general public is to be provided with competent, efficient tax advice and both professions are to operate without friction in the penumbra, some legally tenable line of demarcation must be established. By analyzing the leading reported decisions which permeate this area one can synthesize a sufficient test of what in the tax field constitutes "the practice of law"—an area restricted to licensed attorneys as a matter of public protection.[2]

In order to explore this growing conflict[3] between the two professions, it is worthwhile to take note of the generally accepted definitions of each. Accounting may be defined as:

> [T]he art of recording, classifying, and summarizing in a significant manner and in terms of money, transactions, and events which are, in part at least, of a financial character, and interpreting the results thereof.[4]

Similarly, a generally accepted definition of the practice of law is:

> [T]he doing or performing services in a court of justice, in any manner depending therein, throughout its various stages, and in conformity to the adopted rules of procedure. But in a larger sense it includes legal advice and counsel, and the preparation of legal instruments and contracts by which legal rights are secured, although such matters may or may not be depending in a court.[5]

Unfortunately, such criteria have been of little help in dissolving the confusion in the field of income taxation, for the accountant in many instances is often engaged in activities outside the confines of the accepted definition. True, there seems to be no argument that the mere preparation of a tax return constitutes the practice of law.[6]

---

[1] Austin, "Relations Between Lawyers and Certified Public Accountants in Income Tax Practice," 36 Iowa L. Rev. 227 (1950-1951).

[2] For a collection of the statutes of each state prohibiting the practice of law by laymen, see Otterbourg, "A Study of Unauthorized Practice of Law," Unauthorized Practice News 61 (Special Issue, Sept. 1951).

[3] 20 Unauthorized Practice News, No. 3, 3-5 (Oct. 1954).

[4] "Accounting Research Bulletin No. 9" as reported in 32 A.B.A.J. 5, n. 2 (1946).

[5] Eley v. Miller, 7 Ind. App. 529, 34 N.E. 836, 837-38 (1893).

[6] Agran v. Shapiro, 127 Cal. App. 2d 807, 273 P.2d 619, 623 (1954).

However, beyond this point there is a dispute among the authorities[7] as to the type of problem the accountant may handle incidental to the preparation of a return. It is in this realm that the courts have set up various tests to determine what is and what is not the practice of law.

Generally, services commonly performed by lawyers, in or out of court, may not be performed by non-lawyers.[8] To avoid a strict application of the rule, the courts have adopted exceptions, which permit accountants to perform functions seemingly covered by the definition of the practice of law, at least to a limited extent. The fact that courts do allow laymen to engage in activities commonly performed by lawyers is the basis for the various legal tests applied by the courts.[9]

Three principal tests have been developed which can be described as: (1) The "wholly within the field of law" test;[10] (2) The "incidental" test;[11] (3) The "difficult or doubtful question of law" test.[12] However, it has been pointed out that the "incidental" test and the "difficult or doubtful question of law" test are the only exceptions to the general rule; in purporting to apply the "wholly within the field of law" test, the courts have done no more than apply the general rule.[13]

The "wholly within the field of law" test was established in *Lowell Bar Ass'n v. Loeb*, a Massachusetts case.[14] In that case the defendant, neither an accountant nor lawyer, was the proprietor of an income tax service. Her clients' incomes consisted wholly or almost wholly of salaries or wages. The court, in reaching the conclusion that defendant was not guilty of the unlawful practice of law, reasoned that even though the preparation of the income tax returns involved legal matters to some extent, it did not lie wholly within the field of law as any intelligent taxpayer could prepare the single returns involved. The court said: "But any service that lies wholly within the practice

---

[7] See authorities cited in Lowell Bar Ass'n v. Loeb, 315 Mass. 176, 52 N.E.2d 27, 33 (1954).

[8] Rembar, "The Practice of Taxes," 54 Colum. L. Rev. 338 (1954).

[9] Dean Griswold has pointed out that, insofar as the accountant's place in tax practice is concerned, to put the problem in terms of "practicing law" is to beg the question: "If we start with that approach, then the conclusion is going to follow as surely as the night follows the day that much of what the accountants have long and customarily done is improper for them to do." Griswold, "A Further Look: Lawyers and Accountants," 41 A.B.A.J. 1113, 1114 (1955).

[10] Lowell Bar Ass'n v. Loeb, 315 Mass. 176, 52 N.E. 2d 27, 32 (1943).

[11] *In re* Bercu, 273 App. Div. 524, 78 N.Y.S. 2d 209, 220 (1948), *aff'd*, 299 N.Y. 728, 87 N.E. 2d 451 (1949).

[12] Gardner v. Conway, 234 Minn. 468, 48 N.W. 2d 788, 796 (1951).

[13] Rembar, *supra* note 8, at 343.

[14] 315 Mass. 176, 52 N.E. 2d 27, 34 (1943).

of law cannot lawfully be perfomed by an accountant or any other person not a member of the bar."[15]

It is immediately apparent that in the "wholly within the field of law" test the line of demarcation between that which is and that which is not the practice of law is drawn at the point where the services of a lawyer become absolutely essential. The advocates of the test argue that the dictates of reality require lawyers to recognize the vast areas of the law in which laymen are competent to give advice.[16] The only significance of the test is that it recognizes legal questions which can quite properly be answered by a layman.

In *In re Bercu*[17] the New York court applied the "incidental" test. In this case Bercu, a certified public accountant, was called upon to give advice regarding the deductibility of certain taxes accrued on a corporation's books in an earlier year. In a conference between the corporation's lawyer and Bercu a difference of opinion arose as to the proper method of making certain deductions from the corporation's 1943 federal income tax return, and Bercu offered to substantiate his position by locating certain rulings with which he was familiar. He made a study of the point at issue and submitted a memorandum to the corporation citing the ruling which would permit the company to effect a substantial saving. The New York court, held that, while application of legal knowledge by accountants in the keeping of books and preparation of tax returns is permissible because merely "incidental" to those accounting functions, legal advice "unconnected with accounting work" is unauthorized practice of law. The court said:

> It is not expected or permitted of the accountant, despite his knowledge or use of law, to give legal advice which is unconnected with accounting work. That is exactly what this respondent did. He was doing no accounting work for the Croft Company within the ordinary or proper conception of an accountant's work.[18]

Conversely in the *Loeb* case, *supra,* the Massachusetts court recognized that "A sharp line cannot be drawn between the field of the lawyer and that of the accountant. Some matters lie in a penumbra."[19]

In the *Bercu* case, it is interesting to note that the accountant was held to have practiced law principally because he was not in charge of the books of the corporation involved, and did not render any other accounting service for his client apart from the advice above described.

---

[15] *Id.* at —, 52 N.E.2d at 32.
[16] Ashley, "The Unauthorized Practice of Law," 16 A.B.A.J. 558, 559 (1930).
[17] 273 App. Div. 524, 78 N.Y.S.2d 209 (1948), *aff'd,* 299 N.Y. 728, 87 N.E. 2d 451 (1949).
[18] *Supra* note 17, at — 78 N.Y.S.2d, at 216.
[19] Lowell Bar Ass'n v. Loeb, 315 Mass. 176, 52 N.E.2d 27, 33 (1943).

Certainly, one implication which follows is that if Bercu had been the regular accountant for the corporation any advice which he might have given regarding the legal effect of the transaction would have been within the "incidental" test laid down by the court, and therefore not the practice of law.

This implication creates an anomaly in that the same question answered by the accountant may, on the one hand, constitute the practice of law where he is not the regular accountant while on the other hand, it may not constitute the practice of law where the legal question is resolved as incident to the preparation of the taxpayer's tax return. The New York court seemed to recognize this when it stated:

> Respondent is most persuasive when he challenges the consistency of recognizing an accountant's right to prepare income tax returns while denying him the right to give income tax advice. As respondent says, precisely the same questions may at one time arise during the preparation of an income tax return and at another time serve as the subject of a request for advice by a client. The difference is that in the one case the accountant is dealing with a question of law which is only incidental to preparing a tax return and in the other case he is addressing himself to a question of law alone.[20]

The "difficult or doubtful question of law" test was laid down in *Gardner v. Conway*.[21] In this case defendant had advertised himself as a "Tax Consultant" and an "Income Tax Expert" although he was neither a lawyer nor a certified public accountant. An investigator from the Minnesota Bar came to defendant with a fictitious set of facts and asked him to prepare a tax return. Defendant accepted a fee for his services in preparing the return for the supposed client, in the preparation of which he answered questions as to the client's marital and partnership status and deductible business losses.

The Supreme Court of Minnesota unanimously held that defendant was guilty of the unauthorized practice of law. The test of what constitutes the unauthorized practice of law, said the court, cannot be defined in terms of what is incidental or primary in relation to the alleged practitioner's main occupation. Such a test completely ignores the public welfare considerations for which attorneys are licensed. In approving the "difficult or doubtful question of law" test, the court stated:

> Generally speaking, whenever . . . a layman, as part of his regular course of conduct, resolves legal questions for another, at the latter's request and for a consideration, by giving him advice or by taking action for and in his behalf, he is practicing law if difficult or doubt-

[20] *In re* Bercu, 273 App. Div. 524, 78 N.Y.S.2d 209, 220 (1948), *aff'd*, 299 N.Y. 728, 87 N.E.2d 451 (1949).

[21] 234 Minn. 468, 48 N.W.2d 788 (1951).

> ful legal questions are involved which, to safeguard the public, reasonably demand the application of a trained legal mind. What is a difficult or doubtful question of law is not to be measured by the comprehension of a trained legal mind, but by the understanding thereof which is possessed by a reasonably intelligent layman who is reasonably familiar with similar transactions.[22]

The Minnesota court thus adopted a legal test which looks to the nature of the advice given, rather than to the circumstances under which it was given. If the advice involves a doubtful and difficult question of law, the layman must defer to the lawyer. The reasonableness of this approach is seen in its emphasis on the function of the attorney. As pointed out by the court, prohibition of unauthorized practice is designed to protect the public from the incompetence of lay advice in a technical field.[23] Therefore, as to legal propositions which do not demand technical legal competence, the layman is free to counsel.

The standard laid down by the Minnesota court is not at all favorable to the accountant, for he now has to guess what a reasonably intelligent layman would consider to be a "difficult or doubtful question of law" and then decide whether to call in a lawyer or not.

The judicial spotlight was then focused on the State of California in *Agran v. Shapiro*,[24] in which a decision was rendered on the same subject. Agran, a certified public accountant, was engaged by Shapiro to prepare income tax returns for a period of four years. Pursuant to the preparation of one of these returns, Agran filed an application for a tentative carry-back adjustment claiming a net operating loss. When the claim was disputed by Treasury agents, Agran, in an effort to support his contention, personally conducted extensive research, reading "over one hundred cases." In the ensuing conferences Agran cited numerous cases unearthed by his research, and ultimately was able to convince the Internal Revenue agents of the validity of the carry-back adjustments. Thereafter, Agran submitted a bill based, not on any accounting work but, on negotiations with revenue agents and preparation of tax returns; and when Shapiro refused to pay, Agran instituted this action to recover his fee.

The California court held that the contract between Agran and Shapiro for services rendered in appearing before the Treasury Department was illegal because such service constituted the practice of law by one not a licensed member of the Bar.[25] Further, although

---

[22] *Id.* at —, 48 N.W.2d at 796.
[23] *Id.* at —, 48 N.W.2d at 795.
[24] 127 Cal. App.2d 807, 273 P.2d 619 (1954).
[25] Cal. Bus. and Prof. Code § 6125: "No person shall practice law in the State unless he is an active member of the State Bar."

Agran was an enrolled agent of the Treasury Department, under whose regulations he purported to act, the regulation involved did not permit such an agent to practice before the Treasury Department if it constituted unlawful practice of law as determined by the law of the state in which the hearing was held.[26]

Later in its opinion, the court came to grips with the "incidental" test as expressed by the *Bercu* case; and while it said that *Bercu* was not a binding precedent because of a dissimilarity in the fact situation, the court stated: "[T]he criterion formulated by the New York court for determining whether a particular activity does or does not constitute the practice of law is unsatisfactory. . . ."[27]

The reason behind this language is that the real issue involved is whether or not the test serves the interest of the public. The court took the position that performance of a legal service by a layman is contrary to the public interest even though it happens to be incidental to the layman's calling and to the principal service which he is engaged to render.[28] Thus the "incidental" test is rejected.

At this point the court concluded that the determination of whether or not the loss was a net operating loss was a "doubtful or difficult" question of law and that arguing the question before the Treasury Department constituted the practice of law.

Of the approaches taken in the leading cases considered, the "incidental" test has the characteristics of simplicity and certainty. It provides a workable distinction which is easy to apply and would be acceptable from a standpoint of public policy if one can assume that in every instance a layman is necessarily competent to do all things incidental to his occupation. However, such assumption is ill-founded because "the incidental test ignores the interest of the public as the controlling determinant."[29] Considering that the primary concern is protection of the public from incompetent and unreliable legal service it is going to extremes to say that the resolution of a legal question by a layman is more reliable when made in connection with the preparation of a tax return than when made independently of a return; and yet, such is the underlying factor in the "incidental" test. Because of this inadequacy the "incidental" test is unsafe and untenable as a line of demarcation in tax practice, except perhaps in its negative application defined and employed by the *Conway* case. That is, if the accountant preparing the return feels that he cannot handle

---

[26] Bachrach, "The Public Interest and the Preparation of Tax Returns," 41 A.B.A.J. 204 (1955).

[27] Agran v. Shapiro, 127 Cal. App.2d 807, 273 P.2d 619, 625 (1954).

[28] *Ibid.*

[29] Gardner v. Conway, 234 Minn. 468, 48 N.W.2d 788, 796 (1951).

the matter, then, in all probability, the question is of such a nature that a lawyer should be consulted. If a particular question is one that ought to be handled by a lawyer, then the mere fact that it arises incidental to the preparation of a return does not make the accountant competent to handle it.

Of course, it can be argued that such an approach will cripple the taxpayer financially for it is often too expensive to retain separate legal and accounting counsel; and indeed, from the standpoint of technical difficulty involved, it may be questioned whether the added expense of retaining two experts is justified.[30] True, it may be convenient and less expensive for the taxpayer to have an accountant prepare his return, but is this not a situation against which the rules of unauthorized practice of law are designed to protect? Certainly, a person who is unfamiliar with the law is not capable of evaluating, and therefore is not in a position to make an intelligent decision as to, whether an accountant or an attorney would best serve his needs.[31]

Logically, the "difficult or doubtful question of law" test and the "wholly within the field of law" test are, in effect, the same. Both recognize that there are some legal questions which can quite properly be answered by a layman, and presumably any determination of what is wholly within the field of law would be made in terms of how difficult or doubtful the question is. The "difficult or doubtful question of law" test would seem to be the most satisfactory criterion, because any test that a court establishes to determine what constitutes the practice of law should give weight to the effect that it will have on the public. The *Conway* case which was followed by the *Agran* case establishes a far more realistic approach to the problem. The court looks to the nature of the services performed, rather than the circumstances surrounding those services to ascertain whether they constitute the unauthorized practice of law. The test does not let the line between the field of the lawyer and that of the accountant lie in a penumbra; it recognizes that the lawyer is the only one especially trained to handle such problems, and that it is, therefore, in the public interest that others be enjoined from engaging in such practices. However, like so many legal tests the "difficult or doubtful" test suffers from indefiniteness, for no attempt is made to define precisely what constitutes such a legal problem. Rather the accountant engaged in filling out an income tax return is left to speculate as to what a reasonably intelligent layman would consider to be a "difficult or

[30] Address by Eugene H. Freedheim, before Public Accountants Society of Ohio, October 1, 1955 in 21 Unauthorized Practice News, No. 4, 26, 32 (Dec. 1955).

[31] Rembar, *supra* note 8, at 339.

doubtful question of law" and then decide whether or not to come knocking at the lawyer's door.

Left as a broad rule and used as a general solution to the overall problem, the "difficult or doubtful question of law" criterion will not promote sound public policy. Only if this standard be applied to the particular facts of each case will the primary function of judicial control over the practice of law, that is, the protection of the public from those not qualified to practice law, be accomplished. At the present time no more precise distinction can be drawn.

Perhaps the answer to the problem can best be reached other than through the courts. In 1951 an excellent "Joint Statement of Principles Relating to Practice in the Field of Federal Income Taxation,"[32] was approved by the American Institute of Accounting and the House of Delegates of the American Bar Association. Of course, on such a difficult and nebulous matter, this *Statement of Principles* does not give all the answers. But it does outline the approach which should dispose of many of the problems.

The general spirit in which the *Statement of Principles* was adopted is indicated by the following passage from the conclusion:

> This Statement of Principles should be regarded as tentative and subject to revision and amplification in the light of future experience. The principal purpose is to indicate the importance of voluntary cooperation between our professions, whose members should use their knowledge and skills to the best advantage of the public.[33]

These sentiments are in harmony with the writings of tax practitioners in both professions who have viewed the problem objectively and conclude that voluntary co-operation between the two professions in the interest of the public is preferable to conflict between them.[34]

In summary, the *Statement* declares that only a lawyer may prepare legal documents and decries the use of the title "Tax Consultant" or "Tax Expert" by an accountant. It recommends that certified public accountants should advise clients to seek the advice of lawyers whenever legal questions are present and that lawyers should encourage clients to seek the advice of certified public accountants when accounting problems arise. It recommends that both lawyers and certified public accountants may represent taxpayers in proceedings before the Treasury Department. If, in the course of proceedings, questions of law arise, a lawyer should be retained, and vice versa

---

[32] 37 A.B.A.J. 517 (1951).

[33] *Id.* at 537.

[34] Maxwell and Charles, "Joint Statement As To Tax Accountancy And Law Practice," 32 A.B.A.J. 5 (1946).

when accounting questions are involved. It is further stated that the services of a lawyer should be obtained when claims for refund are to be prepared which are intended to be the basis of litigation, and when a taxpayer is being specially investigated for possible criminal violations of the income tax law. Further, if a formal notice of deficiency is issued by the Commissioner, the advice of a lawyer should be sought before further proceedings are contemplated.[35]

Since the *Statement of Principles* carries no legal effect there are no judicial applications or interpretations. However, it is interesting to note that in the *Agran* decision the court did set out some of the pertinent sections and relied in part on the *Statement of Principles* in reaching its decision:

> Yet another consideration confirms us in the conclusion we have reached. We refer to the Statement of Principles. . . . We can hardly believe that, if the conferees . . . were of the view that the effect of the Treasury Regulations authorized an enrolled agent who was not a lawyer to perform any and all services on behalf of others before the Treasury Department that might be performed by a lawyer, they would have given their adherence thereto.[36]

The success, therefore, of the *Statement of Principles* depends on the voluntary co-operation by the lawyer and certified public accountant in working for the public good and in determining the controversies by conference-table discussion within the boundaries of the *Statement.* Only a conference-table approach will really make it possible for the representatives of the two great professions to wrestle with and resolve specific questions which may hereafter arise. Certainly, it can be said that cooperation is preferred over conflict.

Conceivably, the most appealing solution to this growing controversy between the two professions may lie in adherence to the *Statement of Principles.* But the problem is not that simple, for the *Statement of Principles* leaves many problems unsolved. For example, there is no specific recommendation regarding the interpretation of tax laws by accountants such as occurred in the *Bercu* case. Undoubtedly, there are a larger number of laymen engaged in income tax work who are neither certified public accountants nor lawyers and in many cases are not even trained in accounting. The *Statement of Principles* as well as the "incidental" and "doubtful or difficult question of law" tests used in the *Bercu* and *Conway* cases do not deal with the problem of these unqualified tax practitioners in that they fail to distinguish between them and qualified accountants.

---

[35] For the full text of the Joint Statement, see 37 A.B.A.J. 517 (1951).
[36] Agran v. Shapiro, 127 Cal. App.2d 807, 273 P.2d 619, 630-31 (1954).

The unqualified tax practitioner who is neither lawyer nor certified public accountant is the most likely to engage in unauthorized practice of law and has been the cause of the most troublesome litigation in this field.[37] These individuals have no place whatever in the field of taxation. By elimination of the unqualified tax practitioner and closer co-operation between the lawyer and certified public accountant, the public can be provided with competent, efficient tax advice. However, such partial solution is unworkable unless both professions recognize the need for co-operation and Mr. and Mrs. General Public are educated to the dangers of poor advice.

*Robert C. Shelton**

[37] Austin, *supra* note 1, at 243.
* Third year law student.