

# Accountants cannot give legal advice: what that means for them, their clients and the lawyers

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**Abstract:** A recent AAT decision highlighted a problem that has existed for many years. Accountants have long-believed that they are entitled to give advice, including legal advice, about the operation of tax laws. This article considers the extent to which accountants' "bread and butter" work involves the provision of legal advice.

The article discusses why accountants incorrectly believe that they can give legal advice, the risks for accountants who give legal advice, and how tax practitioners can ameliorate those risks.

The article concludes with some suggested curative approaches.

## Introduction

In *Sinclair and Commissioner of Taxation*,<sup>1</sup> the Deputy President found,<sup>2</sup> inter alia, that:<sup>3</sup>

- a reasonable person with the taxpayer's (Sinclair's) attributes would be on notice to obtain legal advice about the consequence of the transaction;<sup>4</sup> and
- Sinclair's accountant, even though a Fellow of The Tax Institute, could not give legal advice regarding the taxation implications of the arrangements.

Sinclair sought a tax deduction for "prepaid interest". Experience suggests that:

- any solicitor of moderate experience would have recognised that the proposed transaction was a tax-driven transaction and would likely have assured the accountant at the meeting that he would provide documents to secure the tax deduction; and
- in preparing Sinclair's tax return, his accountant is likely to have understood the impact of the transaction documents, prepared by the lawyer, to be the creation of a deduction for prepaid interest for the year ended 30 June 2005.

Sinclair's solicitor, whom the Deputy President chose not to identify (much to the annoyance of many accountants), wrote to the Administrative Appeals Tribunal five years after the events in question "[denying] giving specific legal advice about the particular arrangement entered by Sinclair" but did not provide any corroborating evidence.

Although Sinclair was liable to pay the resulting administrative penalty, it is

accountants (including tax practitioners), rather than clients, who have the real problem:

- the "bread and butter" work for most accountants routinely involves the provision of legal advice about taxation laws and/or other legislative provisions and/or the effect of documents;
- a client may have rights against an accountant for any loss that they suffer; and
- professional indemnity insurance policies for accountants almost uniformly exclude coverage when the accountant engages in legal practice.

A more serious consequence could be prosecution for contravention of the relevant prohibition.

This problem impacts all accountants — whether they work in a first-tier firm or a one-person practice.

## Accountants' bread and butter

The bread and butter work of accountants routinely involves them in some or all of the following:

- providing advice in relation to income tax laws, GST laws, FBT laws and possibly the *Taxation Administration Act 1953* (Cth);
- providing advice about directors' obligations under the *Corporations Act 2001* (Cth);
- drafting trustee resolutions, interpreting loan agreements, administering deceased estates and interpreting contracts of sale;
- acquiring a trust deed for a client from a website;

- interpreting a sale contract to determine the GST outcomes;
- interpreting a trust deed;
- giving legal advice that is incidental to advising in relation to taxation laws;
- giving legal advice that is incidental to making a statement to the Commissioner of Taxation;
- determining whether a document is a lease for the purposes of the in-house asset rules or the separate business premises test within the personal services income rules or the active asset test in the small business concessions;
- drafting an instrument whereby a guardian approves of an amendment to a trust deed or a distribution;
- appearing on a tax prosecution at a state Magistrates' Court or District Court; and
- giving advice in relation to state tax legislation.

## Accountants and legal advice

Accountants have long believed that they are entitled to give advice, including legal advice, about the operation of the income tax laws. In *Sinclair*, the Deputy President simply highlighted a problem that has existed for many years. Accountants have no legal basis for this belief, even if the advice is provided in relation to the preparation and lodging of a tax return. The problem could have been addressed, at least for tax practitioners, in the 16 years during which the recently enacted *Tax Agent Services Act 2009* (Cth) was negotiated.

## Giving legal advice and engaging in legal practice?

There is little scope to argue that:

- giving legal advice does not involve engaging in legal practice; or
- giving advice about legislation is anything other than legal advice.

But the problems for accountants are far more wide-ranging. Comments by Simmonds J,<sup>5</sup> addressing a function commonly undertaken by accountants, deserve consideration:

“171 It seems to me that on the evidence before me I should find beyond a reasonable doubt that the provision of the trust deed involved [the Accounting Practice] “directly or indirectly” performing, carrying out or engaging in any work in connection with the practice of law ...

172 On the evidence before me, of the trust deed itself, ... I do not consider an inference that [the Accounting Practice] was simply performing[a clerical function] is reasonably open ...”

In *Cornall v Nagle*<sup>6</sup> a case involving the prosecution of a person for carrying out solicitor’s work, Phillips J said:

“In my opinion, the giving of *legal advice*, at least as part of a course of conduct and for reward, can properly be said to lie at or near the very centre of the practice of the law, and hence of the notion of acting or practising as a solicitor which is itself central to s.90.” (emphasis added)

Phillips J declined to lay down any precise rule as to when a person acts as a solicitor.<sup>7</sup>

In a later English decision, *Andre Agassi v Robinson*,<sup>8</sup> the dispute involved Agassi’s entitlement to be paid costs following his successful appeal against an assessment for tax on income received under contracts with Nike Inc and Head Sports AG, a short point of statutory interpretation requiring neither the marshalling of evidence nor the calling of witnesses. Agassi considered that it was more efficient to use Tenons, experts in the field of tax law, rather than a firm of solicitors.

Mr Mills of Tenons was a member of the Chartered Institute of Taxation and, in that capacity, was entitled to instruct counsel under the Bar’s licensed access scheme.<sup>9</sup>

The *Solicitor’s Act 1974* precluded Agassi from recovering costs from the Inspector of Revenue unless certain work, including work acting as a solicitor, was performed by a qualified person. Mills was not a qualified person.

Much of the argument in *Agassi*<sup>10</sup> was as to whether certain work carried out by Mr Mills was in the nature of administrative support rather than acting as solicitor. The court, comprising Brook, Carnwath and Dyson LJJ, said:

“45. This is a difficult area. There is no statutory (and so far as we are aware no other) definition of “acting as a solicitor”. The phrase “administrative support” may seem to be a convenient label to use to refer to those activities which do not amount to acting as a solicitor, but it is not particularly illuminating shorthand for the only activities that may be carried out by an unqualified person on a proper application of the *Piper Double Glazing test*.”

The court considered the judgment in *Cornall* and, although referring to it as comprehensive, subsequently applied the narrower Piper Double Glazing Test:<sup>11</sup>

“46. The hallmark of a solicitor is that he is professionally qualified to practise law, is subject to regulation by the Law Society and owes important duties to the court. For this reason, there is much to be said in favour of a broader view of “acting as a solicitor” so as to include the approach adopted by Phillips J in *Cornall v Nagle* [1995] 2 VR 188, a decision of the Supreme Court of Victoria.”

## Who can give legal advice?

Each state and territory, other than South Australia,<sup>12</sup> prohibits a person from engaging in legal practice rather than prohibiting a person from providing “legal advice” (the term used by the Deputy President in *Sinclair*). The mechanics of each of the state prohibitions on people engaging in legal practice are similar to the mechanics of the prohibition in the *Tax Agent Services Act 2009*.<sup>13</sup>

Table 1 conveniently summarises the present position on a state-by-state basis. The near unanimity of the prohibition in the current legislative instruments reflects the ongoing efforts of the Legal Profession — Model Laws Project to incorporate core provisions within the National Model Bill 2006 to deliver virtual national legislation for the legal profession.

Within the National Model Bill 2006:

- “engage in legal practice” includes “practise law”; and
- unhelpfully, and more dangerously, “practise law” is undefined.<sup>16</sup>

The definition of “engage in legal practice” in the National Model Bill 2006:

- provides no clear boundaries as to what conduct will constitute to “engage in legal practice”;
- clearly encompasses establishing the legal effect of a document;
- leaves little scope to argue that providing legal advice does not constitute engaging in legal practice; and
- can be informed by case law developed in relation to earlier forms of the several state based prohibitions

## Accountants and their belief that they can give legal advice

Accountants’ assumed entitlement to give legal advice in relation to taxation laws is rooted in their collective failure to appreciate the limits of the former s 251L of the *Income Tax Assessment Act 1936* (Cth) (ITAA36).<sup>17</sup> The operation of s 251L ITAA36 was considered in a prosecution launched by the Western Australian Legal Practice Board against an accounting practice.<sup>18</sup> The Legal Practice Board alleged that the accounting practice had engaged in legal practice when it provided, to a client, a superannuation fund deed that the accounting practice had obtained from the Cleardocs website.

In relation to the accountant’s submission that s 251L ITAA36 provided a defence to the charge of engaging in legal practice by entitling the accountant to provide the superannuation fund deed to the client, Simmonds J said:

“31. [Section 251L], in my view, simply includes allowance for relief for registered tax agents from the prohibition in the provision. It does not purport to provide relief, for registered tax agents, or any one else, from any other prohibition, whether under federal or state law, including other prohibitions of the same conduct as that prohibited by s 251L.

32 Still less does that provision authorise registered tax agents or any other person to engage in any conduct, such that it might be contended *Legal Practice Act*, s 123(3)(c), applies.”

Section 251L:

- never entitled tax agents to engage in legal practice or to practise law; and
- prohibited a person, other than a registered tax agent, from demanding or accepting a fee for a number of things, including giving advice about a taxation law on behalf of a taxpayer.

Table 1

Legislature	Legislation	Section	Prohibited behaviour	Is the prohibited behaviour defined?
WA	<i>Legal Profession Act 2008</i>	12(2)	To engage in legal practice	“Engage in legal practice” includes practise law
TAS	<i>Legal Profession Act 2007</i>	13	To engage in legal practice when not entitled	Engage in legal practice includes practise law but subject to safe harbours listed in s 21(2)
QLD	<i>Legal Profession Act 2007</i>	24	To engage in legal practice	Engage in legal practice includes practise law.
ACT	<i>Legal Profession Act 2006</i>	16 <sup>14</sup>	To engage in legal practice	“Engage in legal practice” includes practise law
VIC	<i>Legal Profession Act 2004</i>	2.2.2	To engage in legal practice	
NSW	<i>Legal Profession Act 2004</i>	14	To engage in legal practice	“Engage in legal practice” includes practise law
NT	<i>Legal Profession Act</i>	18	To engage in legal practice	“Engage in legal practice” includes practise law
SA	<i>Legal Practitioners Act 1981</i>	21	To practise the profession of the law <sup>15</sup>	Defined in s 21 non-exhaustively but with carve-outs

to the Australian Taxation Office (ATO) must satisfy themselves that they have a reasonable basis to conclude that the lawyer’s view is correct — all the while avoiding “engaging in legal practice.”<sup>19</sup>

If clients prefer to use their own lawyer in circumstances where:

- the accountant is familiar with the lawyer and his skill set — the client can expect the accountant to provide a written sign off as to the tax outcomes under the document; or
- where the accountant has no familiarity with the lawyer or his skill set and no way of establishing the extent of their skill set, or if the client’s lawyer is unable or unwilling to provide the written sign off — the client can expect the accountant to require a second lawyer to interpret the document and provide a written sign off as to its effect.

Where legal advice, rather than a transactional document, is sought, the accountant must ensure that:

- the lawyer comprehensively sets out, in writing, the relevant facts in relation to which the advice is given; and
- those facts are still relevant and correct at the time of lodging the document or making the statement with the ATO.

### Finding a suitable cure

At the time of writing, the ATO has included the issue of tax practitioners giving legal advice in relation to taxation laws on the agenda for the NTLG, but the issue cannot be resolved satisfactorily at the NTLG level.

While the ATO has apparently indicated that it may waive any penalty in those circumstances, neither clients nor insurance companies will be quite so forgiving.

A tax practitioner’s incorrect conclusion that a contract provides for a going concern might result in a client having an unplanned liability for GST, the payment of which in turn threatens the viability of an acquisition. Even if the NTLG can address penalty, there is little that the NTLG can do about the general interest charge on the shortfall amount.

The observations of the Law Lords in *Andre Agassi v Robinson*,<sup>20</sup> with appropriate adaptations, show a pathway for addressing the problem in Australia:

“84 ... So long as members of the Institute continue to act as Tenon acted in this case without the rights and duties that flow from

### How can tax practitioners deal with the problem?

The situation for tax practitioners is analogous to the situation that financial planners will soon confront in relation to providing tax agent services.

In the short term, accountants just have to “grin and bear it”. In the longer term, a legislative cure that protects both tax practitioners and consumers is required.

An accountant is not entitled to determine the several GST outcomes that might arise under a contract of sale that contains such cute expressions as “GST applies if applicable”.

An accountant who commissions a document from a lawyer for a client:

- should only do so as the duly authorised agent of the client;
- should choose a “tax lawyer” to prepare the document;

- should require the tax lawyer to specify the tax effect of the document;
- should obtain a written warranty from the tax lawyer as to the tax effect of the document; and
- even if the tax lawyer asks the accountant what outcome is required, the accountant must have the written warranty from the tax lawyer as to the effect of the document.

Lawyers who provide documents, whether for a client or for an accountant:

- must warrant the tax outcomes generated by the document and can expect to be required to do so in writing; and
- if they are unwilling or unable to do so, they can expect to be bypassed by accountants and their clients in favour of a tax lawyer who will do so.

In all situations, accountants who are lodging documents or making statements

the possession of a statutory right to conduct litigation (in however limited a field), then this will disadvantage their clients as compared with those who instruct an authorised litigator. But this is very much a matter in relation to which the Institute (and other similar bodies) must weigh up the advantages and disadvantages of seeking the status of authorised litigator for its members."

## Conclusion

The author submits that:

- many registered legal practitioners have either no skill and or no interest in giving legal advice in relation to taxation laws either of the state or federal variety;
- the government and the ATO have invested too much in the tax agent services regime to run from the necessary cure;
- from a tax practitioner's point of view, a prohibition without clearly defined boundaries is a disaster;
- the ability of an insurer to hide behind an unclear prohibition deserves immediate attention, particularly in the context of consumer protection of the Tax Practitioners Board and the current dispute involving insurers and the cause of water damage;<sup>21</sup>
- tax practitioners should be entitled to safe harbours that allow them to engage in legal practice to the extent that the legal practice is relevant to making a statement in relation to taxation laws (and similar laws within the states);
- it may be appropriate to require registered tax practitioners to undertake relevant continuing professional development in order to qualify for any safe harbour; and
- the complexity of the tax legislation in conjunction with the requirements of the Code of Professional Conduct in the *Tax Agent Services Act 2009* make it inappropriate for tax practitioners to rely on the advice of legal practitioners who are not supervised by the Tax Practitioners Board.

Practitioners, who have become aware of the situation, are concerned about their exposure. What is needed is strong leadership and commitment to obtaining a solution sooner rather than later. The looming debate over privilege should be viewed as an opportunity to address both problems at the same time.

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## References

- 1 *Sinclair and C of T* [2010] AATA 902.
- 2 The Deputy President also found that:
  - Sinclair did not approach his solicitors regarding the taxation consequences of the contractual arrangements;
  - Sinclair did approach his accountant, who worked with Sinclair and the solicitor on the contractual arrangements;
  - the solicitor did not commit to writing a view that an amount described as pre-paid interest would be deductible;
  - a reasonable person would have sought legal advice from a tax lawyer before claiming the deduction; and
  - because Sinclair had not done what a reasonable person would do, Sinclair was liable to a penalty for failing to exercise reasonable care.
- 3 *Sinclair* at [91] and [92].
- 4 In May 2005, Sinclair (a stockbroker of mature years) sought the assistance of his solicitor and accountant in relation to a proposed property purchase from a financially distressed vendor, but Sinclair "could not see how the legals would work". On 30 June 2005, acting in accordance with the special conditions inserted in the contract of sale prepared by the solicitor, Sinclair paid \$100,000 which was comprised of:
  - a payment to the vendor of the deposit of \$1,000 on a \$2m property; and
  - a payment of \$99,000 to the vendor's financier, described in the special conditions as pre-paid interest, which was an amount reflecting the vendor's liability for interest that the vendor would incur between 1 July and the proposed settlement date of December 2005.
- 5 *Legal Practice Board v Computer Accounting and Tax Pty Ltd* [2007] WASC 184.
- 6 [1995] 2 VR 188 at 208.
- 7 *Cornall* at 197.
- 8 *Andre Agassi v Robinson & Bar Council & Law Society* [2005] EWCA 1507.
- 9 The court observed (at [2]) that: "Although this appeal concerns the costs treatment of fees paid to a member of the Chartered Institute of Taxation, the issues raised have implications for fees paid to other persons who do not have the right to conduct litigation within the meaning of section 28 of the Courts and Legal Services Act 1990, and we have reconstituted the court because it was recognised that the issues were of considerable importance to the conduct of civil litigation and to the legal profession."
- 10 Both the Law Society and the Bar Council were represented at the specially convened costs hearing.
- 11 *Piper Double Glazing Ltd v DC Contracts* [1994] 1 WLR 777.
- 12 The SA legislation is a relic from an earlier age but is substantially similar to the prohibitions in other states. The national model legal profession legislation project is likely to eventually result in the SA legislation aligning with the law in the other states.
- 13 The prohibition in the *Tax Agent Services Act 2009* makes it an offence for a person to provide tax agent services unless the person is registered under that Act.
- 14 S 16 of the ACT legislation contains a non-exhaustive list of five examples of what constitutes engaging in legal practice. Four of those examples should be of concern to tax practitioners:
  - preparing an instrument which create or regulate rights between people;
  - preparing an instrument which relates to property or a legal proceeding;
  - acting as advocate for someone in a proceeding before a court or tribunal; and
  - preparing papers to be used in support of, or opposition to, an application for the grant of probate or letters of administration.
- 15 S 21(2) of the SA legislation relevantly and non-exhaustively defines "practising the profession of law" as:
  - "(b) prepares an instrument creating, transferring, assigning, modifying or extinguishing any estate or interest in real or personal property; or
  - (c) prepares any instrument relating to the formation of a body corporate, any amendment to the memorandum or articles of association, rules or regulations of a body corporate, any prospectus or take-over scheme relating to a body corporate, or any instrument affecting the rights of shareholders or debenture holders in a body corporate or any scheme of arrangement in respect of a body corporate; or
  - (d) prepares any other instrument creating, transferring, assigning, modifying or extinguishing any right, power or liability at law or in equity; or
  - (e) represents any party to proceedings in a court or tribunal."
- 16 In contemplating the view that insurance companies might take of the definition, it is instructive to consider the current debate over water damage and related definitions.
- 17 S 251L was repealed and replaced by the *Tax Agent Services Act 2009* and, in particular, the Code of Professional Conduct in that Act.
- 18 *Legal Practice Board v Computer Accounting and Tax Pty Ltd* [2007] WASC 184.
- 19 See ch 3 of the explanatory memorandum to the *Tax Agent Services Act 2009*.
- 20 *Agassi* at [84].
- 21 There is little in the way of consumer protection if the tax practitioner is a man (or woman) of straw and their professional indemnity policy excludes coverage where the negligence occurs in the course of engaging in legal practice.