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## *Regulation of Tax Professionals*

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Bad ethics drive out good.

—Adapted from Gresham's Law

It would be difficult to have a well-functioning tax system without tax advisors. Because most taxpayers are not familiar with the intricacies of the tax laws, tax advisors are needed so that taxpayers can fulfill their complicated tax obligations. As informed members of the public, tax advisors also provide input to the formulation of legislation and regulations.

By counseling taxpayers on how to comply with their legal obligations, tax advisors serve an important public interest; the state has an interest in fostering and protecting this role. The role of tax advisors, however, differs from that of the tax authorities in that their primary loyalty is to their client, not to the state. An important function of the regulation of tax advisors is to help strike an appropriate balance between loyalty to the system and loyalty to the client.

Regulation also has the goal of protecting clients from unscrupulous or incompetent tax advisors. Here, the regulatory interest of the state is similar to that in other areas of consumer protection. The danger is that such regulation might serve instead to protect the economic interests of those permitted to act as tax advisors, or might strangle the free exercise of the profession by creating undue bureaucratic control.

This chapter reviews the regulation of tax advisors in different countries. Such a review is multifaceted, for several reasons. First, different countries have adopted rather different regulatory approaches. Second, tax advice is typically given by different types of professionals—lawyers, accountants, auditors

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and others—each of which may be subject to independent regulation of its profession. Third, “tax advice” covers a multitude of different activities, which can be performed by professionals with different qualifications and which may call for different regulatory approaches. Fourth, tax advisors do not operate purely domestically, and a different regulatory approach may be appropriate, for example, for foreign tax advisors who render advice within a country, perhaps to a largely foreign-based clientele. Finally, the role of tax advisors cannot properly be viewed in isolation from a country’s culture and its legal and economic system. Therefore, approaches that may work in one country may not be appropriate for another.

Because of the practical importance of tax advisors for the functioning of the tax system, it is important that the system of tax legislation provide an underpinning for their role, whatever regulatory approach is adopted in a particular country. At a minimum, the law should spell out the taxpayer’s right to use a representative and the consequences of that use. Whether it is appropriate to go beyond this and provide more detailed regulation is a matter to be decided in light of the circumstances of the country concerned and the stage of development of the tax advisory profession in that country. In most transition countries, there are very few tax advisors. This is due to the youth of the tax system as a whole and to the fact that there has not been time for professional education and experience. In part because of the paucity of tax advisors, taxes in these countries are often designed so as to minimize the number of taxpayers who must take positive action with respect to their tax affairs, for example, through the use of final withholding taxes and registration thresholds. Detailed regulation of tax advisors would not seem to be a top priority for transition countries, compared with other areas where the tax system needs development. Nevertheless, several transition countries (e.g., China, Poland, and the Slovak Republic) have undertaken such regulation.

## **I. Basic Policy Considerations in Regulating Tax Advisors**

### **A. Balance of Supply and Demand**

Regulating a profession by imposing conditions for admission inevitably reduces the supply of potential professionals. Whenever a service industry is regulated, a rough balance between supply and demand for professional services should be maintained. Therefore, in any proposal to regulate a professional service, like tax advice, it is of crucial importance to know in advance how many people can be admitted to the profession immediately or within a short period of time, given the regulations contemplated. The standards of experience and education that are set in the regulation will to a large extent determine the volume of the supply of tax advisors. Flexible transitional measures may also have a major impact on the balance between supply and demand for tax services.

On the demand side, an analysis should be made of what type of professionals will be required by what type of taxpayer. For example, there is a huge difference in qualification requirements between a tax lawyer able to take complicated cases in court and a person able to prepare simple returns for small rural businesses. The demand for tax advisors will depend, among other things, on the development of the economy and the legal system and on requirements imposed on taxpayers (e.g., how many taxpayers are required to file returns). On the supply side, the major constraint in many countries is likely to be the availability of proper training.

The necessity of providing a rough balance between supply and demand for tax advice is of decisive importance in deciding (1) whether or not to regulate the profession, and (2) how to regulate the profession and more specifically what the qualifications should be for admission to the profession and whether the profession should be granted a monopoly on some or all aspects of tax practice.

The most burning political question concerns granting a monopoly for the exercise of the profession. From the point of view of the tax profession, a monopoly may be highly desirable. However, it is the general interest and not the interest of the profession that should decide this issue. The general interest is best served by high-quality service at a low price. A monopoly is supposed to exclude incompetence and low quality but tends to result in higher prices and may in certain circumstances result in corruption (e.g., there can be corruption in terms of entry to the profession). Moreover, a monopoly cannot fully exclude incompetent advice. If incompetent advisors can make it into the monopoly, and are able to keep competent advisors out, then a monopoly offers a lower quality of advice than a regime of free competition. Quality standards can also be fostered by regulatory measures that do not create a monopoly.

A monopoly for tax advice is also difficult to enforce. A great deal of tax advice is generated by the activities of professions such as accountants (internal audit), auditors (external audit), lawyers (advising on business transactions, tax litigation), notaries (conveyancing), real estate agents, and customs agents. Each of these activities can in its own right involve some form of tax advice. Establishing a monopoly for tax advisors will not exclude all these professionals from offering tax advice. This means that establishment of a monopoly is not likely to be very effective in achieving the desired policy goals.

Moreover, an alternative means is available for providing consumers access to a regulated profession. The profession can be regulated and its title protected by law (which means that an individual who is not duly accredited is not allowed to use the title of tax advisor), but without giving members of the profession a monopoly on tax advice. Under such a scheme, consumers would have the choice of obtaining tax advice from an accredited tax advisor or of consulting another professional. This solution maintains competition between rival professions in the market for tax advice, while at the same time setting adequate quality standards for the profession of tax advisors. It is one possibil-

ity among the alternative approaches to regulation discussed in section III of this chapter.

## B. Maintenance of Quality Standards

Maintenance of quality standards does not necessarily involve a legally imposed regulatory scheme. For example, in the Netherlands there are two strong private organizations that impose strict rules on their members.<sup>1</sup> Although there is no official recognition of these private organizations, the Ministry of Finance considers them to be representative partners in dealing with problems of the tax profession. These organizations police the quality of their members and accordingly offer the public a choice about whom to consult on tax matters. Their private status gives them flexibility in setting professional standards. However, such a situation, whereby a private organization imposes quality standards on its members, requires time and tradition to develop. This model would probably be difficult to follow in most countries in transition.

Many developing and transition countries that decide to regulate tax practitioners may choose to determine professional requirements by law rather than by relying on private organizations, unless these are well developed. The question of the professional qualifications required for admission is a difficult one, because the profession is in practice exercised at very different quality levels, ranging from quite simple to highly sophisticated. In setting educational and professional standards, one should also take into account a country's educational and professional tradition.

In the United Kingdom, for instance, professional education of lawyers and accountants traditionally took the form of on-the-job training, while the role of universities and other institutions of formal education was rather limited. This may be related to the English tradition of professional education in which solicitors and barristers traditionally learned their trade at the Inns of Chancery and the Inns of Court in London rather than in universities. In more recent years, however, the norm in the United Kingdom has become a university degree. In setting standards for admission, a country having a similar tradition of on-the-job training could put more emphasis on professional experience than on university degrees. Countries with a strong tradition of academic education in law or other relevant disciplines (e.g., accounting) can rely more on degrees in setting standards for admission.

Keeping in mind the basic requirement of a balance between supply and demand for tax advice, limitations on resources for training and education are likely to constitute the major bottleneck in the supply of tax advisors in developing and transition countries. To avoid such bottlenecks, any regulation

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<sup>1</sup>These are de Nederlandse Orde van Belastingadviseurs (NOB) [The Dutch Order of Tax Advisors] and de Nederlandse Federatie van Belastingconsulenten (NFB) [The Dutch Federation of Tax Consultants].

should avoid exclusive channels of access to the profession. When the main requirement is professional experience, the law regulating the profession should not give the profession exclusive control over quality standards, but should share this control with the government, enabling the latter to keep channels of access open. When the main requirement is a diploma or degree, the law should provide that the government can organize official examinations for candidates without the degree, requiring the same level of competence as the examinations organized by universities and other institutions of higher learning.

A model of the latter approach can be found in the Eighth European Directive of April 10, 1984,<sup>2</sup> regulating admission to the auditing profession. This directive requires candidates to have a university-level education and practical training.<sup>3</sup> This theoretical education can be provided either by universities or other institutions of higher learning or by the profession itself. The same holds for practical training. The important thing is that the directive provides for alternative channels of access (universities or the profession). The directive is also flexible in that it does not require the applicant to take courses and lectures. The only requirement is that the applicant present a theoretical examination on a minimum number of courses and proof of practical training.<sup>4</sup> The applicant has the choice between a university or other school of higher learning, or an examination board organized by the state. This is not to suggest that degree requirements for tax advisors should all be set at the university level: a multilayered approach may be more advisable.<sup>5</sup>

Finally, in implementing a regulatory scheme that involves professional standards, it may be necessary to provide for a transitional period during which access to the profession is permitted on the basis of an examination, in a few areas that are essential to tax practice, such as general principles of tax law, substantive law of major taxes—such as income tax (individual and corporate) and value-added tax or turnover taxes—tax procedure and company law, and accountancy, without any formal requirement of prior education (except basic secondary education). The exact program could be detailed by regulation. Examinations could be organized by universities or other institutions of higher learning, or by educational centers of the tax administration that organize the training of tax officials.

### C. Conflicting Loyalties of Tax Advisors

The development of appropriate regulation of tax advisors must recognize the dichotomy between the state's interest in raising revenue and in applying

<sup>2</sup>Council Directive 84/253, 1984 O.J. (L 126) 20.

<sup>3</sup>*Id.* art. 4.

<sup>4</sup>*Id.* arts. 4, 5, 8.

<sup>5</sup>See *infra* sec. II.

its taxation law in a consistent, efficient, and equitable manner and the client's interest in minimizing tax.

Some taxpayers are prepared to violate the law in order to pay less tax. Others wish to act legally but to obtain as much after-tax profit as possible. They will legally seek to do this by exploiting inconsistencies and ambiguities in the tax legislation. Where different tax consequences follow two different forms of a transaction, the taxpayer will, if properly advised, often adopt the form that incurs the lowest tax burden. Similarly, if two types of transaction bear different tax burdens, the taxpayer can be expected to characterize the transaction employed by the taxpayer as one qualifying for the lower tax burden. And, finally, where there is some ambiguity in the application of the statute, the taxpayer will seek to interpret the ambiguous wording in the most advantageous way possible.

In addition, a taxpayer may consult an advisor to make sure that a particular transaction or business structure does not result in unfavorable tax treatment or to learn how to comply with tax legislation.

An underlying question is the extent to which, in different circumstances, the tax consultant must act in the interests of the state or the client if the interests of the two parties diverge. This question should be borne in mind in considering the various functions that a tax advisor can perform. The basic rule in most countries is that the private tax advisor must act in complete independence from the tax administration. The tax advisor must of course respect all legal obligations that flow from the tax law, but his or her primary loyalty lies with the client, the taxpayer. For example, the advisor must generally respect client confidences and may not report the client to the tax authorities.<sup>6</sup> This independence results from the general attitude taken toward professional services, such as those of lawyers, physicians, and accountants. This independence may be very valuable, particularly in transition countries, which until recently had an experience of interference by public authorities in all areas of public and private life. The loyalty to the client is not, however, unqualified. A tax advisor is not generally permitted, for example, to participate in fraud or to lie to the government.<sup>7</sup>

Some countries have a different emphasis. According to the Japanese Law on Certified Tax Accountants of 1951, the mission of a certified tax accountant (CTA) is to implement the taxpayer's obligation to pay taxes as stipulated in the law. The CTA must be impartial between the taxpayer and the tax administration and make the CTA's position clear to both parties. The Japanese Ministry of Finance may also disbar or suspend a CTA; some argue that this makes the professional subject to the tax administration to some degree.<sup>8</sup> Similarly, in

<sup>6</sup>See *infra* sec. 1(H).

<sup>7</sup>See Bernard Wolfman et al., *Standards of Tax Practice* § 403.2 (3rd ed. 1995).

<sup>8</sup>See Masayoshi Hanaki, *Japanese Certified Tax Accountant System* (paper presented at International Seminar, Beijing, Apr. 1994).

countries with rules contemplating the certification of a tax return by a professional, the professional on his or her personal responsibility certifies that the return is in compliance with the law, thereby placing the tax advisor in a position of some independence vis-à-vis the client.<sup>9</sup>

Closely tied to the question of loyalty is the question of whether tax officials may practice as tax advisors. This question is particularly crucial in transition countries because the tax administration may constitute the only reservoir of professional expertise for private practice. Regardless of the circumstances, the basic rule should be that an official of the tax administration is prohibited from engaging in any form of private tax practice while in government employment.<sup>10</sup> The reason for this incompatibility between public and private tax practice is that it is impossible to serve two masters at the same time. There would be a clear conflict of interest between loyalty to the tax administration on the one hand and loyalty to the client on the other.

This incompatibility should not be confused with the duty of the tax official to help some kinds of taxpayers file their tax returns. In many countries the tax administration opens its offices to taxpayers who are illiterate, low-income, or elderly. The taxpayer must be aware that the tax official is acting in the exercise of the official's public office in providing this service. These services can be provided for small taxpayers with simple tax returns reporting fixed salaries or pensions. They should not be open to taxpayers with important sources of revenue, because in such instances they could easily result in corruption.

Another question is whether a tax official can enter into private tax practice after leaving the tax administration. Tax officials often resign from their official duties to accept lucrative consulting jobs in the private sector. Basically, this should be permitted in developing and transition countries. However, to avoid a massive flight from the tax administration into private practice, after the tax officials have completed their professional training in the tax administration, a minimum number of years in public service could be imposed.<sup>11</sup> Finally, and in order to avoid a conflict of interest, a former tax official should be prohibited from dealing as a private advisor with files with which the official has been in contact directly or indirectly while working for the tax administration.<sup>12</sup>

<sup>9</sup>See *infra* sec. IV(A).

<sup>10</sup>See, e.g., 31 C.F.R. § 0.735-20, -21(b), -39 (1994) (USA) (Treas. Dept. employees may not engage in outside employment involving a conflict of interest; federal employees may not act as attorney or agent of a party in a case before a court or agency where the government is an opposing party).

<sup>11</sup>This could take the form of a promise that is not legally binding, a contract with a damages clause, or a legally imposed period prohibiting private practice for a certain time if the minimum length of service is not satisfied.

<sup>12</sup>See 18 U.S.C. § 207 (USA); Treas. Dept. Circ. No. 230, § 10.26 (USA) [hereinafter Circular 230]. In Germany, there is also a three-year waiting period before a former tax official may represent a client whose tax matters the official dealt with. See DEU StBerG § 61.

### D. Relationship Between Tax Consulting and the Legal and Accounting Professions

The variety of functions performed by tax consultants overlaps the responsibilities ordinarily carried out by other professionals, chiefly lawyers and accountants. Thus, it is impossible to consider the regulation of tax consultants without considering how the legal and accounting professions are regulated, the extent to which these professions are guaranteed monopolies in practicing in their respective areas, and the extent to which tax consulting activities are considered the practice of law or the practice of accounting.

In almost all jurisdictions, controls are placed on who is entitled to practice law or accountancy. The controls usually work in conjunction with measures that provide for the establishment and recognition of independent, self-governing professional bodies that are responsible, among other things, for establishing the prerequisites for admission to practice in the profession, the continuing education and other conditions for continuing qualification, and the disciplining of members of the profession with respect to breaches of their professional responsibilities. Legislation imposing criminal sanctions is often used to enforce the professional monopolies and restrict practice to persons who meet the requirements of the state and of the relevant professional body.

The boundaries between legal advice, accounting advice, and advice that is neither legal nor accounting are inherently unclear in the tax area. All advice about tax *law* can be characterized as legal advice. Jurisdictions vary in the extent to which they give a monopoly on the provision of legal advice to lawyers and on how they define the monopoly. In countries such as the United States and France, which restrict the provision of legal advice to lawyers, there can be disputes about the extent to which the provision of tax advice by non-lawyers is the unauthorized practice of law. In Germany (and other countries with analogous regulatory schemes), the situation is more complicated, because there is a legally created monopoly on both the practice of law and on the practice of tax advice, so that the lawyers' monopoly must make exceptions to take into account the competing monopoly of the tax advisors, and vice versa. No jurisdiction, however, has provided that only lawyers may give tax advice, because so many other professionals deal with tax matters.<sup>13</sup>

Because legal, accounting, and tax services are so closely connected, it is desirable to approximate certain professional rules in the three professions. If those professional rules were very different, competition between the three professions could be distorted. The areas in which professional rules should be approximated include the following: (1) permissibility of advertising, (2) rules for professional liability, (3) the parallel activities that are compatible with the exercise of the profession, (4) whether a person can become a member of more than one profession and which profession would then control professional and

<sup>13</sup>See *infra* sec. 11.



ethical standards, (5) whether a legal person can become a member of the profession, (6) fees, (7) privileged information, and (8) ethics, for instance, conflicts of interest, limitations on holding financial interests in clients, and procedures for a client to consult another professional.

The difficulty of segregating legal and accounting advice from tax advice and from business and financial planning advice does not arise with respect to other functions performed by tax consultants where the nature of the service is easy to identify, namely, the preparation of tax returns and the representation of a taxpayer in contacts with revenue authorities or before an appeals board or court. The relative clarity of these latter functions probably explains to a large degree why, as explained further below, in some jurisdictions<sup>14</sup> efforts to supervise and regulate tax consultants concentrate on these responsibilities.

### **E. Admission of Legal Persons to the Profession**

The development of rules allowing or disallowing tax advisors to operate through different business forms will depend in part on the conceptual model underlying the profession to which the advisor belongs. Two competing models have emerged—the traditional concept of a liberal profession as it has been developed in continental Europe and the more modern Anglo-American concept of a profession providing intellectual services through entities such as the big accounting or law firms. In the former concept, the person of the practitioner takes a central position and the practitioner's personal qualities determine the quality of his or her professional practice. In the latter, the organization and its techniques and procedures are crucial, and the person of the practitioner is of secondary importance because the practitioner's quality is determined by the working procedures of the organization. These two alternatives are not mutually exclusive because systems permitting practice by legal persons also allow practice by individuals.

If legal persons are admitted to practice as such, two basic issues arise, one with respect to the professional quality and responsibility of the individuals working for the organization and another with respect to the independence of the organization from its clients and the rules with respect to conflicts of interest and other matters of professional ethics.

Preservation of the virtues of personal professional responsibility and quality of the services provided are good reasons for not admitting legal persons to the exercise of the profession. The argument that admission of legal persons is necessary for the buildup of large organizations is not valid. The existence of major European and American law firms that have several hundreds of lawyers and thousands of employees, and that are not admitted to practice as an organization, is sufficient to refute this argument.

<sup>14</sup>See *infra* secs. II(D–F), III.

However, some countries (such as France and Germany) have chosen to admit legal persons to practice.<sup>15</sup> Under such a system, a major policy question is the extent to which a director, partner, shareholder, or employee is required to be an individual member of the profession with all rights, privileges, and responsibilities related to that status. In the extreme case, one could have a firm with only one individual being a member of the profession and all other partners and employees not being members. It is clear that certain minimum standards should be fixed as to the level in the organization at which individuals must be members of the profession.

Closely tied to this question is that of corporate control. If a firm is admitted to the profession, it is important to know who will control it. If bankers, industrialists, and shopkeepers can exercise control of a tax consulting firm, it will be very difficult to enforce the standards of ethics and independence of the profession because no banker, industrialist, or shopkeeper is bound by such standards. Again, if one takes the independence and ethics of the profession seriously, it would seem that the minimum rule ought to be that control over all professional decisions must be in the hands of persons who, as individuals, are members of the profession and subject to its ethical rules. This may require a majority of the outstanding capital and of the votes in the general meeting of shareholders and even exclusive representation on the board and other bodies of the legal person.<sup>16</sup>

The admittance of legal persons to the profession also raises some secondary questions, namely, how ethical rules can be enforced against a legal person and how the legal person can participate in the life of the profession (voting rights in the general meeting of the professional association, representation on its executive board, etc.).

## F. Regulation of International Tax Consulting Services

Those countries that leave the tax profession largely unregulated do not face a problem in dealing with foreign practitioners. Where a country seeks to establish a monopoly on tax practice, however, problems arise in applying the regulations to tax consulting services that cross borders.

Consideration of the tax implications of international transactions and investments will inevitably involve consideration of local tax laws and the tax laws of the jurisdiction in which the other party to the transaction or investment is resident. In the case of multinational corporations, it is likely that the

<sup>15</sup>See DEU StBerG §§ 3(1)1, 49, 72, 74; Loi No. 90-1258 of Dec. 31, 1990, relative à l'exercice sous forme de sociétés des professions libérales soumises à un statut législatif ou réglementaire ou dont le titre est protégé, J.O. Jan. 5, 1991 (FRA) [hereinafter Loi No. 90-1258]. The Slovak Republic has changed its rules to prevent limited liability companies from providing tax consultancy services. See Alzbeta Bobáková, *LLCs Can No Longer Provide Tax Services in Slovakia*, 11 Tax Notes Int'l 32 (1995). The law regulating tax advisors is SVK TAL.

<sup>16</sup>See DEU StBerG §§ 50, 50a; Loi No. 90-1258, *supra* note 15, arts. 5-13.

tax implications in many jurisdictions, where various branches of the company are resident, will have to be taken into account before the details of a transaction can be finalized.

Persons qualified to provide advice on domestic taxation are unlikely to have sufficient knowledge of relevant foreign tax systems to advise on all aspects of the foreign law. To obtain that information, a taxpayer will quite likely require the advice of a foreign tax consultant. The qualifications required of (and supervision of) foreign tax consultants will depend on how the advice is provided. The advice can be sought directly by a taxpayer in the country or through a tax consultant practicing in the country. In both cases, the advice can be sought in a number of ways, such as asking an expert abroad to provide advice; arranging for a foreign advisor to visit the country for a brief period; using a foreign expert who is resident in the country; or having the tax analysis be done in another country where a multinational is based or has operations.

Pragmatic considerations suggest that it is difficult to regulate the provision of this sort of advice. Excessive regulation might result in simply pushing businesses to seek tax advice offshore. It should also be taken into consideration that foreign tax advisors are likely to bring international technical expert knowledge to the tax profession that a country may very much need to participate in international economic transactions. A pragmatic solution strongly suggests *not* to establish a monopoly for tax advice, or at least not to establish a monopoly on international and foreign tax practice, so as to leave foreign tax experts free to practice in the international area and in the domestic tax area of their country of origin.

Moreover, jurisdictions that are part of a common market area may face legal constraints in imposing restrictions on freedom of establishment and the freedom to provide cross-border services that discriminate against foreign nationals.<sup>17</sup> A foreign professional who has been qualified abroad may wish to practice in the country without having fulfilled all the in-country educational requirements normally required of domestic individuals who wish to become licensed. If certain aspects of tax practice are restricted to persons with given qualifications, this problem can be dealt with by providing for a simplified procedure for foreign practitioners to qualify to practice in the country in recognition of the fact that they have already had to become qualified abroad.<sup>18</sup>

When foreign members of a regulated profession are allowed to practice in a country, an important question arises as to which will be the competent disciplinary authority: the authority of the territory in which the activity has been exercised or that of the territory in which the professional was admitted to practice. This question has not yet received a final answer. It is clear that international law firms and accounting firms would prefer disciplinary author-

<sup>17</sup>See *supra* ch. 2, sec. II(G).

<sup>18</sup>See, e.g., DEU StBerG § 36(3) (simplified procedure for citizens of other EU states).

ity to rest with the competent authority of the country in which the professional has been admitted to practice. They are familiar with those rules, and application of those rules would provide legal security, which may be necessary to convince an international tax advisor to practice in a country that is otherwise unknown to him or her.

On the other hand, a country may want to subject foreign members of a regulated profession allowed to practice in the country to the same professional rules as its own national professionals. Different professional rules may distort competition to the disadvantage of domestic professionals.

## G. Provision of Tax Services by Employees

Any regulatory scheme should take account of the fact that the major portion of tax services to corporations is provided not by outside advisors but by employees. The regulatory interest in controlling what employees can do is weak, since presumably the employer can exercise the control desired. Generally, employees are free to provide tax services to their employer without any state control over their qualifications, except in cases involving representation of the employer before a court,<sup>19</sup> and they may be exempted from requirements that apply to independent tax advisors.<sup>20</sup> In drafting a regulatory scheme, the supply and demand implications of service rendering by employees should be taken into account. Moreover, it should be clearly specified which activities can be undertaken without government control. A regulatory scheme that is restrictive and leads to a scarcity of available advisors will create pressure for corporations to do their tax work internally rather than to retain outside advisors.

## H. Privileged Communications and Work Product

In many countries, professionals rendering tax advice enjoy professional privilege under which documents furnished to, and communications with, a tax advisor may be exempt from disclosure to the government.<sup>21</sup> Usually, the rules in this area follow the general rules of privilege. Communications to lawyers may be eligible for privilege, but communications to accountants or tax advisors who are not lawyers are generally not. Not all communications to lawyers are privileged; thus, privilege generally extends only to communications in confidence for the purpose of obtaining legal advice. Financial documents,

<sup>19</sup>See, e.g., Circular 230, *supra* note 12, § 10.7(c).

<sup>20</sup>E.g., Finance Act 1995 § 172(1) (IRL)(employee not subject to rule described *infra* note 30).

<sup>21</sup>This is known in some countries as professional secret (in France, *secret professionnel*, see Décret No. 91-117 of Nov. 27, 1991, organisant la profession d'avocat, J.O. Nov. 28, 1991, and in Germany, *Berufsgeheimnis*, see DEU AO § 102(1)3(b)). For discussion of professional privilege in the tax area in the United States, see Wolfman et al., *supra* note 7, at § 306.4.4.1; Michael Saltzman, IRS Practice and Procedure ¶ 13.11 (2d ed. 1991).

however, furnished to a lawyer for the purpose of tax return preparation might not be privileged because they have not been prepared by the client for the purpose of confidential communication to the attorney.<sup>22</sup> Communications made to an attorney for the purpose of return preparation might not be privileged because the preparation of tax returns does not constitute rendering legal advice.<sup>23</sup> On the other hand, the taxpayer's attorney's work product (e.g., notes analyzing the taxpayer's case) may be immune from disclosure to the tax authorities.<sup>24</sup> The U.S. Supreme Court has not, however, extended the attorney work product doctrine to accountants.<sup>25</sup>

Where privilege is available with respect to some professions, but not with respect to tax advisors generally, there is a distortion of competition between tax advisors who are members of different professions, since taxpayers may prefer an advisor to whom communications are protected by privilege. On this basis, some of the distinctions that are drawn between different professions in the recognition of privilege can be faulted.<sup>26</sup>

Many tax administrations are opposed to professional privilege for communications to tax consultants, because it would impede the efficiency of tax audits. Obtaining information about the client's tax affairs from an advisor can be a particularly useful tool for the tax administration, because the tax advisor may have analyzed the client's situation and identified points of weakness in positions the client has taken.<sup>27</sup>

The question of privilege comes up where the government seeks to obtain documents or testimony from the tax advisor. A related, but distinct, issue is the advisor's responsibility to keep client confidences; that is, are there any circumstances under which the advisor is permitted or required to report the client's misconduct to the tax authorities? The general obligation to maintain client confidences is imposed by the general professional standards that govern the practice of lawyers and accountants. A duty to maintain confidentiality

<sup>22</sup>See *Colton v. United States*, 306 F.2d 633 (2d Cir. 1962).

<sup>23</sup>See *In re Schroeder*, 842 F.2d 1223 (11th Cir. 1987).

<sup>24</sup>See *Hickman v. Taylor*, 329 U.S. 495 (1947); *Upjohn Co. v. United States*, 449 U.S. 383 (1981).

<sup>25</sup>See *United States v. Arthur Young & Co.*, 465 U.S. 805 (1984).

<sup>26</sup>See, e.g., Nancy Loube, *Attorney-Client Privilege in the Context of Section 6662*, 10 Tax Notes Int'l 2103 (1995).

<sup>27</sup>For example, in *United States v. Arthur Young & Co.*, 465 U.S. 807 (1984), the IRS sought the tax accrual workpapers of the taxpayer's accountant through an administrative summons. Tax accrual workpapers are the independent auditor's papers used in the process of determining the adequacy of the corporation's reserve account for contingent tax liabilities. "Tax accrual workpapers also contain an overall evaluation of the sufficiency of the corporation's reserve for contingent tax liabilities, including an item-by-item analysis of the corporation's potential exposure to additional liability. In short, tax accrual workpapers pinpoint the 'soft spots' on a corporation's tax return by highlighting those areas in which the corporate taxpayer has taken a position that may, at some later date, require the payment of additional taxes." *Id.* at 813.

may also apply to tax advisors who are not lawyers or accountants if these are regulated.<sup>28</sup>

As a general matter, the practitioner may not reveal client confidences to the government. For example, if a client commits tax fraud, a practitioner representing the client in an audit who learns of the fraud from the client may not inform the tax authorities. Instead, the practitioner may be required by professional standards of practice to advise the client to inform the tax authorities of the fraud. If the client refuses to do so, then the practitioner may be required to cease representing the client, if continuing to do so would make the practitioner a party to the fraud.<sup>29</sup> Ireland has recently amended its tax law to require an advisor to a company who becomes aware of certain tax offenses committed by the company to first ask the company to report the situation to the tax authorities.<sup>30</sup> If the company refuses to do so, then the advisor is required to cease working for the company as auditor or as tax advisor for a period of three years.<sup>31</sup> If the advisor who is required to resign is an auditor, the advisor must notify the company of his or her resignation and send a copy of the notice of resignation to the tax authorities.<sup>32</sup> An exception is provided for a person assisting or advising the company in preparation for legal proceedings.<sup>33</sup>

## II. Tailoring Regulation to Functions of Tax Advisors

The resolution of the interests of the state and of the taxpayer requires a multifaceted response in light of the fact that the category "tax consultants" encompasses persons with quite different roles and responsibilities. For example, in situations such as those of a lawyer defending a client against criminal prosecution, it is appropriate for the advisor to act with total loyalty to the client, subject only to the ethical principles that apply to lawyers (such as the duty not to lie to a tribunal). In other cases, such as where the tax advisor assists in planning transactions, it is not appropriate for the advisor to act as aggressively as possible in the client's interest.<sup>34</sup> A preliminary step in regulating tax consultants, therefore, is to identify the different types of consultants and consulting activities and to consider each separately in the context of alternative regulation models. This section reviews the different functions that are typically performed by tax advisors, and how considerations for regulation might differ for each.

<sup>28</sup>See Wolfman et al., *supra* note 7, § 403.1.1; USA IRC § 7216.

<sup>29</sup>See Wolfman et al., *supra* note 7, § 403.2.2.

<sup>30</sup>Finance Act 1995 § 172(2) (IRL).

<sup>31</sup>*Id.* § 172(2)(b).

<sup>32</sup>*Id.* § 172(3).

<sup>33</sup>See *id.* § 172(2)(b); See also Miriam H. O'Brien, *Ireland: Parliament Passes Finance Act 1995 With Controversial Reporting Obligation for Tax Advisors*, 10 Tax Notes Int'l 1955 (1995).

<sup>34</sup>See Wolfman et al., *supra* note 7, §§ 501–505.

## A. Tax Planning

Tax advice, because it can be approached from different angles, is part of a much wider package of legal and economic services, including auditing, accounting, financial, legal, and management services. Tax problems can arise not only from the company's accounts and records, but also from legal obligations flowing from company law, securities regulation, bankruptcy law, and so on. Therefore, it is important to recognize that many different kinds of professionals will deal with tax problems as a natural extension of their nontax activities. In countries with complex tax laws, virtually every business or financial transaction may call for review of its tax implications. Advice on tax planning can therefore arise in quite different contexts and be given by different professionals, not just by tax specialists.

## B. Advice Ancillary to Financial and Other Services

Tax advice is also provided by some ordinary business enterprises like banks, insurance companies, brokerages, and real estate companies as a service ancillary to their main business. For example, life insurance products may be eligible for special tax treatment, which insurance brokers will explain to clients. The same will be true for many financial products. The advice given here will typically be very narrow in scope, focusing on the tax treatment of the financial product being sold. These business enterprises cannot be compared to independent professions and should not be regulated like independent professions, provided that their tax services remain truly ancillary to other economic activities. In Western Europe, the financial services industry has recently been seeking to enter the market for tax services, thereby raising the question of whether those activities should be regulated the same way as the independent professions.

## C. Preparation and Auditing of Commercial Accounts

A primary function of commercial accounts is to provide financial information to the owners and creditors of a business. Commercial considerations have led to the imposition of standards and controls on persons preparing or auditing commercial accounts. In most cases, the qualifications for preparing accounts are less severe than those for the independent professionals who audit accounts (certified public accountants). While the commercial accounts may be of great importance in the determination of tax liability,<sup>35</sup> there is usually no regulation by the tax authorities of persons preparing commercial accounts.

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<sup>35</sup>See vol. 2, ch. 16.

## **D. Preparation of Tax Returns**

Countries with a system of licensed tax professionals will typically stipulate that only persons who are licensed as return preparers may prepare a return for remuneration. Even when a country does not want to regulate the tax profession or tax advice as such, it may wish to have certain controls on the persons who prepare and file tax returns on a taxpayer's behalf. The minimal rule may be that when the taxpayer does not personally prepare the tax return, the person who prepares the return has to identify himself or herself. This allows the taxpayer to hire anyone to prepare the return, but it also permits the tax administration to keep track of professionals engaged in the business of preparing returns and to impose penalties where called for.

In any scheme that imposes requirements or restrictions on return preparers, it will be necessary to identify who is a preparer. In most cases it is easy to identify the preparer. However, in the case of complex returns, many people may contribute to the preparation of a return. In these cases, a person furnishing substantial information or advice that is an input to the preparation of the return may appropriately be considered a return preparer. Of course, under this rule, it is possible that many persons will be considered preparers with respect to a single return. For some purposes, one can provide special rules limiting the number of preparers (e.g., one could provide that only the principal preparer must sign the return).

## **E. Representation of Taxpayer Before the Tax Administration**

A tax advisor representing a taxpayer before the tax authorities acts as an advocate. Because of the skills required, there are often restrictions as to who can act in this capacity, and the rules typically differ depending on the procedural formality that the proceedings take. When the profession is regulated, it is generally provided that the tax advisor may represent the taxpayer before the tax authorities. Generally, this right of representation is shared with other professions, such as lawyers and accountants. Representation can take place to obtain a ruling; in connection with audits or investigations, before or after assessment; and before administrative tribunals or tax boards.

## **F. Representation Before the Courts**

In some countries, all tax litigation is decided by the civil courts, rather than by administrative courts. In countries where administrative tribunals initially hear a case, depending on the rules of tax procedure, appeals in tax litigation are most often decided by the civil courts, while tax fraud and tax evasion belong to the competence of the criminal courts.

Representation of taxpayers before the civil or the criminal courts is generally reserved exclusively to lawyers. The argument in favor of restricting ap-



pearances in courts (or administrative tribunals with procedural rules similar to those of courts) to lawyers is that professionals who may be tax experts but are not litigation experts may not be qualified to serve their client in such a setting. However, in countries where there is a comprehensive regulation of the tax profession, tax advisors may also be permitted to represent taxpayers in litigation before the civil courts. In such cases, specific competence in legal or tax procedure is most often required. Representation of taxpayers in criminal cases is the exclusive competence of lawyers in most countries.

Where nonlawyers are allowed to represent taxpayers, they are often required to be licensed by the tribunal and must take an examination for this purpose.<sup>36</sup> Particularly if the number of lawyers available to take tax cases is inadequate, this kind of licensing might be a solution to providing professional representation for taxpayers.

### III. Approaches to Regulation

The extent of regulation of the tax profession differs substantially from country to country. Three general approaches can be identified. The first, exemplified by Austria, China, Germany, and Japan,<sup>37</sup> establishes a regulated professional monopoly for tax practice (similar to the professional monopoly that lawyers enjoy in many countries for legal practice) that is shared in most cases with other regulated professions such as lawyers and accountants. The second, exemplified by the United States, does not establish a monopoly for tax advice or return preparation, but does restrict certain representational activity to licensed practitioners and members of other regulated professions and involves a well-developed regulatory framework. The third, which most countries follow, involves an essentially unregulated tax profession that coexists with regulated professions such as lawyers and accountants. However, the regulations applicable to these professions do not deal specifically with the provision of tax services. Within these three general approaches, there are differences in detail in different countries' approach to the tax profession.

#### A. Full Regulation: The German Model

In Germany, the Tax Consultancy Law<sup>38</sup> comprehensively regulates the provision of tax advice. Article 2 provides that assistance in tax matters on a commercial basis may be provided only by persons who are authorized to do so by the law. Under article 3, those who are generally competent to give tax ad-

<sup>36</sup>See, e.g., U.S. Tax Court Rule 200(a), 60 T.C. 1152 (1973).

<sup>37</sup>See Law on Certified Tax Accountants of 1951 (JPN); State Administration of Taxation, Interim Measures on Tax Agents (Sep. 16, 1994) (CHN); DEU StBerG.

<sup>38</sup>DEU StBerG.

vice are licensed tax advisors, lawyers, accountants, and auditors. Thus, a person who is licensed as a lawyer or an accountant need not obtain a special license for tax practice, but no other person may generally give tax advice without a license. The seriousness of this general restriction of tax practice is underscored by article 4, which lists in detail the limited situations in which nonlicensed persons may provide tax advice.<sup>39</sup> To become a licensed tax advisor, an individual must follow a program of courses and take an examination. A separate regulation provides a schedule of allowable fees.<sup>40</sup>

## B. Partial Regulation: The U.S. Model

Like Germany, the United States regulates tax practice.<sup>41</sup> The scope of this regulation is, however, much less extensive than in Germany in that anyone, even someone with no professional training or qualifications, is allowed to give tax advice<sup>42</sup> or to prepare a return for someone else. A person preparing a return is, however, required to sign it as preparer. This requirement allows penalties to be imposed, if warranted. It also makes the return preparer take responsibility for the return, which is important in and of itself. Finally, by keeping track of persons signing as return preparers, the tax authorities can detect whether returns with particular problems are originating from particular preparers. In the United States, as part of signing the return, the preparer must list the name of the firm, his or her social security number (which is used as the tax identification number), and the employer identification number (i.e., the tax identification number) of the firm. The use of identification numbers enables the tax authorities to keep track of return preparers with greater certainty.

Other types of representation before the Internal Revenue Service are restricted to persons who are attorneys, certified public accountants, or enrolled agents.<sup>43</sup> Enrolled agents are regulated by the Treasury Department; they are generally required to take an examination and may be disbarred for miscon-

<sup>39</sup>For example, to list only 3 of the 13 cases listed in article 4, patent lawyers are allowed to give tax advice within the scope of their work as patent lawyers, employers are allowed to render assistance to their employees in matters concerning taxation of wages, and administrators of property may give advice with respect to the property they administer. *Id.* § 4(2), (10), (8).

<sup>40</sup>See *Steuerberatergebührenverordnung* reprinted in *Deutsche Steuergesetze* 1992, at 1192 (4th ed. 1992).

<sup>41</sup>See, e.g., Circular 230, *supra* note 12.

<sup>42</sup>However, if the rendering of tax advice is considered to be legal advice, then it may constitute the unauthorized practice of law (and therefore be prohibited) if done by someone who is not an active member of the bar. Because the practice of law is regulated by each state, this is a matter that is not regulated by the federal tax authorities.

<sup>43</sup>See Circular 230, *supra* note 12, § 10.3. Enrolled agents must generally either pass an examination or be a former IRS employee with sufficient experience. *Id.* § 10.4. To remain in good standing, enrolled agents must satisfy continuing professional education requirements. *Id.* § 10.6. A similar regulatory scheme applies in Israel. See ISR IT §§ 236–236H.

duct. A person who is not otherwise eligible to practice before the IRS but who has prepared a return that is being audited may represent the taxpayer in the audit proceedings (but not before the Appeals Office).<sup>44</sup> Before the Tax Court, a taxpayer may be represented by an attorney or by someone who has been admitted to practice before the court by taking an examination.<sup>45</sup> Nonattorneys cannot represent taxpayers in other courts that hear tax cases.

Another country with partial regulation of tax practitioners is Australia, where only lawyers and tax agents are allowed to prepare returns for remuneration; thus, accountants must be registered as tax agents in order to carry out such work.<sup>46</sup> Taxpayers may deduct fees for tax advice only if the advice is furnished by a registered tax agent or by a barrister or a solicitor.<sup>47</sup> A recent policy review in Australia conducted jointly by revenue authorities and professional bodies recommended that qualified accountants who are not tax agents be allowed to charge a tax-deductible fee as well.<sup>48</sup> Overall, the Australian regulatory scheme as it currently stands falls somewhere between the U.S. and the German models in that there is effectively a monopoly provided both on the provision of tax advice and on return preparation, although the regulatory scheme is not as comprehensive as the German.

### C. The Model of No Regulation

In many countries, including Belgium, Italy, Portugal, Spain, and the United Kingdom, the provision of tax advice and return preparation is generally unrestricted as to profession. Some countries, however, provide special treatment for certain professionals in certain circumstances.<sup>49</sup>

With the exception of countries following the U.S. or German models, representation before the tax authorities is relatively unrestricted. Most countries allow representation by nonlawyers in administrative proceedings, since these are not based on formal procedure and rules of evidence that might apply in court. Often, the return preparer defends the case.

### D. Issues in Regulation of Tax Consultancy

The issues to be dealt with in any regulation of the tax profession depend, of course, on the type of regulation that is to be introduced: full regulation, partial regulation, or no regulation at all. However, even in the third case there

<sup>44</sup>See Circular 230, *supra* note 12, § 10.7(c)(1)(viii).

<sup>45</sup>See USA IRC § 7452; U.S. Tax Court Rule No. 200, 60 T.C. 1152 (1973).

<sup>46</sup>See AUS ITAA § 251L(1).

<sup>47</sup>See *id.* § 69(4), (11) (there is also an exception for persons who are exempt from registering as an agent, but this is of limited application).

<sup>48</sup>See National Review of Tax Standards for the Tax Profession, Tax Services for the Public 73 (1994).

<sup>49</sup>See *infra* sec. IV.

may be a need for some rules, to govern cases where the taxpayer is assisted in filing the tax return, or is represented by someone else before the tax administration.

In the model of full regulation the following items should be taken care of:

- (1) The question of whether tax consultants should have a monopoly, and the sanctions for violating the monopoly.<sup>50</sup>
- (2) When the regulation does not provide a monopoly, it should determine the nature of the advantage of title protection, which titles (e.g., tax advisor, tax consultant, tax lawyer, or tax accountant) are protected, the sanctions for violating this protection of title, and the obligation always to use the title in professional tax practice.
- (3) Apart from the advantages of monopoly or title protection, the law should also list any other advantages to be provided, such as facilities in representing taxpayers before the tax administration, in communicating documents and notifications to the tax administration, or obtaining delays for filing or payment, and waiver of penalties.
- (4) Regardless of whether there is a monopoly, or only title protection, the regulation should set out which activities are protected under the law: advice, preparation of tax returns, representation before the tax administration, litigation in courts, and services ancillary to these activities.
- (5) Regardless of the scope and the nature of the regulation of the profession (monopoly or title protection), exceptions should be made for other professions that are closely connected with tax advice, such as lawyers, accountants, auditors, notaries, real estate agents, and patent advisors for the tax aspects of their field of activities.<sup>51</sup>
- (6) The regulation should also specify the educational standards required for admission to the profession.<sup>52</sup> Two things should be regulated: the level of education (university, vocational) and its content (accounting, basic principles of public and private law, major taxes, and the rules of professional ethics). Depending on the level of educational requirements, practical experience may also be required.<sup>53</sup>
- (7) Any full regulation of the profession should also contain organizational rules on the creation of an order or an institute, with a seat, a board, a general meeting, membership dues, a list of licensed members, and bylaws.

<sup>50</sup>See *supra* sec. I(A).

<sup>51</sup>See DEU StBerG §§ 3, 4.

<sup>52</sup>See *supra* sec. I(B).

<sup>53</sup>For example, in the German model, the duration of practical experience increases as the level of education decreases. See DEU StBerG § 36.

- (8) The supervision of the profession should also be regulated. The choice is between supervision by the tax administration, by a self-governing body (as for the legal and medical professions), or by a body with representatives of the general public (consumer protection agencies) and the tax administration. The way in which the profession is supervised also determines the nature of disciplinary measures and procedures, which should also be spelled out in the professional regulation, as well as rules on the relationship between disciplinary law and ordinary civil law (professional liability) and criminal law.
- (9) The regulation should stipulate whether legal persons can be admitted as full members of the profession.<sup>54</sup> It should also indicate whether tax advisors can exercise their profession in company form. If legal persons are admitted to practice, secondary questions arise, such as the control on the board of directors and the general meeting of shareholders by physical persons licensed to practice, the way legal persons participate in the life of the professional organization (voting rights in the general meeting of the profession, representation in the executive board, membership dues), and the way ethical rules are enforced against legal persons.
- (10) Cooperation with other regulated and unregulated professions is also a problem to be dealt with. Conditions for cooperation on an individual basis or within the framework of a legal person should be spelled out, including the question of whether a person can become a member of more than one profession, as well as rules with respect to activities compatible with the exercise of the profession.
- (11) The regulation should also deal with tax advice provided by employees in the service of their employer and tax advice for third parties. This is a specific problem because employees do not have the same guarantees of independence as independent licensed tax advisors.
- (12) Full regulations may contain rules on ethical standards with regard to advertising, conflict of interest (particularly when tax advisors collaborate with other professions in the framework of a legal person), and limitations on financial interests in potential clients.
- (13) Rules on professional privilege should be set down, when such professional privilege is granted to the tax profession.
- (14) Rules on professional liability vis-à-vis customers and rules with respect to the obligation to carry professional insurance should also be spelled out.
- (15) Some regulations contain a full schedule of fees.<sup>55</sup>

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<sup>54</sup>See *supra* sec. I(E).

<sup>55</sup>See *supra* note 40.

- (16) Last but not least, the regulation should contain transitional measures. These are very important because they will determine the balance between supply and demand during the early stages, when the professional regulation is taking effect. The balance between the flexibility of transitional regulations and the strictness of the final regime should be watched very closely. Too often tax practitioners succumb to the temptation of keeping the door wide open during the transitional regime, setting almost no meaningful standards for admission and slamming it shut after the transitional period, so that the established professionals are sitting pretty, while young and capable candidates are kept away by insurmountable entry barriers.

In the model of partial regulation, the extent of regulation is of course much more restricted. In the U.S. model, there is no place for an order or an institute, so that all rules with respect to such institutions become irrelevant. Many tax advisors will be governed by disciplinary rules applicable to their professions of law or accounting. Disciplinary rules for those admitted to practice before the tax authorities should be provided for in the regulation, to be enforced by the government. Because there is no monopoly, there are no problems to regulate with respect to the relationship with other professions. Anyone will be allowed to file tax returns and provide tax advice. There is protection of title, in the sense that persons who are not admitted to practice before the tax authority cannot use the title pertaining to those who are. Educational, professional, or other quality standards, including a minimal tax examination, will have to be provided for those admitted to practice before the tax authority. However, because practice in the form of preparing returns or offering tax advice will generally be open, these requirements will not keep out those who wish to practice without formal admission to practice.

Even when there is no regulation for the tax profession at all, there may still be some rules as to preparing tax returns, providing tax advice, and representing taxpayers before the tax administration and the courts. These rules are usually found in the general tax legislation. They deal with questions such as the liability of and sanctions against persons helping or advising the taxpayer in cases of fraud and tax evasion, the legal consequences of the use of outside services to fulfill personal tax obligations, and rules with respect to the question of who has standing to represent a taxpayer before the tax administration, the tax courts, and the courts of tax appeals.

## **E. Penalties for Practitioners**

Whatever the degree of regulation a country wants to introduce for the tax profession, legislation should contain clear, comprehensive rules providing penalties for violations by tax practitioners. Tax practitioners who are lawyers,

accountants, or auditors are subject to discipline by the licensing authority of the jurisdiction in which they are licensed to practice. If the behavior of such a professional while acting in a tax matter runs counter to the standards of professional conduct of the jurisdiction, he or she is therefore subject to disciplinary punishment that can range from a reprimand to suspension or disbarment from practicing.

The above-described sanctions may not be tailored to tax practice and are applicable only to practitioners who are also lawyers, accountants, or auditors. Therefore, where persons are engaged in tax practice, regardless of whether it is regulated or not, there are typically additional sanctions that are tailored to taxation and that apply to all those engaged in tax practice. These sanctions may be contained in a specific professional regulation, but most often they are part of the general tax law. Typically, these rules will apply in cases of misbehavior, such as filing false returns or aiding a taxpayer in cases of fraud or tax evasion, and provide for criminal sanctions and a prohibition against representing taxpayers before the tax administration. For example, in the United States, the Treasury Department has issued regulations<sup>56</sup> governing practice before the Internal Revenue Service that contain rules for disciplinary proceedings and that allow the Treasury Department to disbar from practice before the IRS persons who violate the rules.

In addition to the specific penalties of suspension and disbarment provided under such regulations, tax laws may provide penalties for tax return preparers and others who engage in tax practice and who commit designated offenses, usually relating to specific tax returns.<sup>57</sup> This type of penalty is similar in structure to penalties applicable to the taxpayer (such as for late filing, late payment, negligence, or fraud) but is imposed directly on the preparer for the preparer's improper conduct. The penalty should not apply if the preparer is not at fault, for example, if the taxpayer fails to provide information to the preparer and the latter does not have reason to believe that the information reflected on the return is false.

For example, in the United States, a penalty applies to a return preparer who fails to sign the return. Code section 6694 imposes a penalty on a person who prepares an income tax return that reflects a position for which there was not a realistic possibility of being sustained and imposes a higher penalty for willful or reckless conduct in preparing a return. Of course, if the tax advisor's conduct is particularly outrageous, so that the advisor is an accomplice in tax evasion, then criminal sanctions may apply.

Regulation may also be accomplished by courts. For example, the rules of the U.S. Tax Court provide ethical standards for those practicing before it.<sup>58</sup>

<sup>56</sup>31 C.F.R. §§ 10.0–10.101 (USA).

<sup>57</sup>See, e.g., Wolfman et al., *supra* note 7, §§ 301.1–305.3.

<sup>58</sup>See U.S. Tax Court Rule 201, 202, 60 T.C. 1153–54 (1973); U.S. Tax Court Rule 33(b), 85 T.C. 1125–26 (1985); Wolfman et al., *supra* note 7, at § 106.

Those engaged in tax practice who behave negligently may also be liable to their clients or to third parties in a civil action for negligence or breach of contract.<sup>59</sup>

In some countries, the tax advisor is held personally liable to the state for any taxes or penalties due in case of avoidance or evasion.<sup>60</sup> This model is not followed, however, in most countries. Except when the tax advisor himself breaks the law as an accomplice to the tax evasion of a client, the advisor should not be held personally liable for the taxes or penalties imposed on the client. The advisor should be subject only to specific penalties for his or her unlawful behavior.

## IV. Legal Consequences of Using Advisors

### A. Returns

In some countries, the law encourages or requires the use of qualified professionals in preparing returns on the theory that a return prepared by a professional will be on a sounder footing and less likely to be fraudulent. For example, if an alternative income tax is directed at businesses maintaining questionable (or no) accounts, the law may apply the tax generally and then provide an exception for companies maintaining audited accounts.<sup>61</sup> Most countries do not, however, provide special treatment for returns based on audited books.

In Israel, companies are required to submit income tax returns that are certified by an auditor, as defined in the Auditors Law, and that are adjusted by the auditor for the purposes of the tax.<sup>62</sup> In Turkey, taxpayers above a certain size are required to have their returns certified by a sworn fiscal advisor.<sup>63</sup>

### B. Liability for a Tax Advisor's Mistakes

A tax return prepared by a registered tax preparer may give rise to penalties for reasons that are the fault of the tax preparer rather than of the client for whom the return was prepared. For example, the preparer may make errors

<sup>59</sup>See Wolfman et al., *supra* note 7, at §§ 601–605; Geoffrey Lehmann & Cynthia Coleman, *Taxation Law in Australia* ¶ 11.74 (3rd ed. 1994).

<sup>60</sup>See Mustafa Çamlica, *Compulsory Return Certification and Sworn Fiscal Advisory in Turkey*, 10 *Tax Notes Int'l* 1584, 1586 (1995) (responsibility of sworn fiscal advisor for tax and penalties in respect of return certified by him or her); Luis F. Ramírez A., *Privatization of Tax Administration*, in *Improving Tax Administration in Developing Countries* 377, 388 (Richard M. Bird & Milka Casanegra de Jantscher eds., 1992) (in Mexico, accountant who certifies return is liable for penalties).

<sup>61</sup>See SLE IT § 23 (minimum chargeable income provisions do not apply where taxpayer's books of account have been audited by "a reputable firm of Accountants" and the Commissioner has conducted a satisfactory field audit).

<sup>62</sup>See ISR IT § 131(c).

<sup>63</sup>See Çamlica, *supra* note 60, at 1585.



or omissions that give rise to penalties, file the return late, and so forth. The question arises as to whether the taxpayer should be immune from penalty where the conduct giving rise to the penalty is that of a registered tax preparer.

This problem can be approached in one of three ways:

1. The taxpayer can be liable for penalties but retain the right available under the general law to sue the tax preparer under tort or contract law for recovery of the amounts.
2. The taxpayer can be liable for penalties but be protected by specific legislation that requires tax preparers to indemnify taxpayers.
3. The taxpayer can be excused from penalties arising out of errors or failures by a tax preparer; penalties may also be imposed directly on the tax preparer instead of on the taxpayer.

The rationale for the third approach is that a taxpayer who deliberately seeks professional advice and assistance, among other reasons, to avoid errors or omissions, should not then be penalized because of another person's inadequate performance. This position is strongly supported, perhaps surprisingly, by professional tax preparers in some jurisdictions. Where there is a "reasonable cause" exception to imposition of a penalty, the argument is that in relying on a professional, the taxpayer acted reasonably and therefore should not be penalized.<sup>64</sup>

The practical problem that would be encountered if the third approach were adopted is that of evidentiary dispute. It will often not be clear to revenue authorities who was to blame for the problem giving rise to a penalty, and these authorities cannot be expected to investigate and ascertain blame before levying a penalty.

While ordinary contract or tort law may be sufficient to protect a taxpayer if the third option is not considered feasible, a specific statutory remedy may be desirable to avoid any doubt about the matter.<sup>65</sup> Moreover, inclusion of such a measure in the tax legislation could be used as a means of bringing the action within the ambit of the tax litigation system and provide the parties with access to the tax appeal system, where they will encounter tribunals and courts with greater tax expertise and more knowledge about the technical problems that gave rise to the penalties in the first place.

<sup>64</sup>See Saltzman, *supra* note 21, ¶ 7B.06[3][c]. Under U.S. law, the question can be framed as to whether reliance on professional advice constitutes reasonable cause that allows the taxpayer to escape from the penalty. In the case of a failure to file a return, the Supreme Court has decided that reliance on an advisor who failed to file cannot be considered reasonable cause. See also *United States v. Boyle*, 469 U.S. 241 (1985).

<sup>65</sup>E.g., AUS ITAA § 251M. For a discussion of problems under this provision, see National Review of Standards for the Tax Profession, *supra* note 48, at 91–93. For a discussion of the tax advisor's liability for negligence and criminal liability under Danish law, see Anders Vinding Kruse and Jesper Lett, *Civil and Criminal Liability for Advice Pertaining to Issues of Taxation*, 33 *Scandinavian Studies in Law* 167 (1989).

As indicated above, in some cases penalties may be waived when the technical violation of the tax law was due to the fault or negligence of the tax agent. However, in most cases the taxpayer will remain liable to tax and interest. So, for example, if the tax advisor fails to file a tax protest in time, and on account of this negligence the taxpayer is not able to defend the taxpayer's case, the amount of tax assessed will be due from the taxpayer. The fact that the taxpayer used the services of a tax advisor is not an excuse for not filing the protest in time. The taxpayer will have to pay the full amount of tax and recover damages from the tax advisor in a court suit on professional liability. Any other rule would allow the taxpayer to use the tax advisor as an alibi for not playing by the rules of the tax law.

The use of a tax advisor may be seen as an attenuating circumstance, however, when the taxpayer is accused of tax evasion. The fact that the taxpayer used the services of a tax advisor is often seen as an indication that the taxpayer intended to fulfill all the taxpayer's tax obligations in accordance with the law, so that it becomes more difficult for the tax administration to accuse the taxpayer of tax evasion. This presumption is of course valid only when the taxpayer provided all necessary information to the advisor.

### C. Facilities for Taxpayers' Use of Tax Advisors

Even when the profession of tax advisors does not have a monopoly on the provision of tax services, the legislator may recognize the advantage of having professionals prepare tax returns, thereby reducing the administrative burden for the tax administration. The regulations may provide for some facilities that are available only to licensed professionals. These may include the following: automatic acceptance of credentials as an attorney for the taxpayer, flexible rules with respect to the filing of tax returns and payment of the taxes due, and informal ways of communication between the tax advisor and the tax administration.

## Appendix A. Organization of Tax Profession in Different Countries<sup>66</sup>

In countries such as Belgium, Italy, the Netherlands, Spain, and the United Kingdom, there are one or more private associations representing tax consultants without formal legal status. In Denmark, Greece, Ireland, Luxembourg, and Portugal, tax advisors either are not organized professionals or are members of other professional organizations, such as accountants, auditors, or lawyers, who also engage in tax activities. Germany and Austria have a profes-

<sup>66</sup>The discussion is based on Ottmar Thoemmes et al., *EG-Recht in der Steuerpraxis* (1993); and Wilfried Dann, *Das Leistungsspektrum des Steuerberaters in Europa und seine berufsrechtlichen Grundlagen*, *Internationales Steuerrecht* 44 (1993).

sion that is specifically regulated, with associations of tax professionals that are recognized by law. In France, tax advice that constitutes the provision of legal advice is regulated as part of the legal profession.

The following table lists tax professionals for each country discussed:

**Tax Professionals in Selected Countries**

Australia	lawyer, accountant, tax agent
Belgium	conseil fiscal, avocat, reviseur d'entreprise, expert comptable <sup>1</sup>
Canada	lawyer, accountant
France	comptable, expert-comptable, avocat
Germany	Steuerberater, Rechtsanwalt, Wirtschaftsprüfer, vereidigter Buchprüfer, Steuerbevollmächtigter
Italy	tributaristo, avvocato
Netherlands	belastingadviseur, belastingconsulent, advocaat, register accountant
Spain	asesor fiscal, abogado, economista
United Kingdom	accountant, tax consultant, taxation practitioner, lawyer
United States	accountant, attorney, enrolled agent

<sup>1</sup>Belastingconsulent, belastingadviseur, advocaat, bedrijfsrevisor, accountant.

In Australia, tax returns may generally be prepared for remuneration only by a tax agent or a lawyer. Tax agents are defined in legislation and are regulated by a board controlled by the tax authorities. Tax agents and lawyers may also represent taxpayers in administrative disputes, but only lawyers may represent taxpayers in court litigation.

In Belgium, a tax advisor is called *belastingconsulent-conseil fiscal*. This professional designation is not regulated by law, nor does the law regulate who may give tax advice, but there is a private professional organization to which tax advisors typically belong. Tax advice can also be given by lawyers (*advocaten/avocats*), notaries (*notarissen/notaires*), accountants (*accountants/experts-comptables*), or auditors (*bedrijfsrevisoren/reviseurs d'entreprises*), the latter being analogous to a certified public accountant. All these professions (lawyer, accountant, and auditor) are recognized and regulated by law, but typically the provision of tax services is outside the scope of this regulation. However, anyone may prepare a tax return and represent the taxpayer before the tax administration or in administrative disputes. Tax litigation before the civil courts is limited to lawyers. Except for accountants and auditors, there is incompatibility between some professions; that is, a lawyer cannot be a tax advisor, and a lawyer cannot be an auditor, but both are entitled to provide tax services.

In France, tax advice was traditionally indirectly regulated as part of legal advice in general.<sup>67</sup> The legal profession was divided into *avocats* and *conseils*

<sup>67</sup>See Loi No. 71-1130 of Dec. 31, 1971, portant réforme de certaines professions judiciaires et juridiques, J.O. Jan. 5, 1972 [hereinafter Loi No. 71-1130].

*juridiques* (legal advisors). However, legal advisors did not have a monopoly on the provision of legal advice, so that tax services were also provided by notaries (*notaires*), accountants (*comptables*, *experts-comptables*), and auditors (*commissaires aux comptes*). France also had a specialized certification for tax lawyers: *avocat spécialiste du droit fiscal*. Recently, all legal activities, including litigation, legal advice, and tax advice, were merged into a new profession whose members carry the title of *avocat*.<sup>68</sup> The provision of tax advice that constitutes legal advice is regulated as part of this legal profession. The French regulatory scheme provides for a monopoly on legal advice for people holding a professional degree in law.<sup>69</sup> Legal persons are also admitted to the profession, provided they meet certain conditions, which guarantee that physical persons who are admitted to the profession will control the legal person.<sup>70</sup> The law also sets criteria for obtaining the title of lawyer (*avocat*) that are more stringent than the conditions formerly imposed to practice as a legal advisor.<sup>71</sup> The legal profession is fully organized as a bar, with disciplinary proceedings, professional privilege, and rules of ethical conduct. All the rules that apply to lawyers also apply to tax consultancy insofar as it is a subdivision of legal advice. However, other professions, such as *experts comptables* (chartered accountants), may also provide tax advice, provided that it is in direct relationship to the services (e.g., accountancy) that they provide their clients.<sup>72</sup>

Germany (as well as Austria) is one of the few countries that has a long-established legal organization of the tax consultancy profession. The law provides a monopoly for tax advice and prohibits unauthorized persons from providing tax services.<sup>73</sup> The German law extensively regulates services relating to the administration of withholding taxes and social contributions on salaries.<sup>74</sup> It contains provisions for a full professional organization, with conditions for admission, quality and educational requirements, admission of legal entities, control of legal entities by physical persons admitted to the profession, disciplinary proceedings, ethical rules, and obligations and rights and privileges of tax consultants.

The Italian term *tributaristi* includes members of several professions: including lawyers, *dottori commercialisti*, *ragioneri*, and *notarii*. All of these profes-

<sup>68</sup>See Loi No. 90-1259 of Dec. 31, 1990, portant réforme de certaines professions judiciaires et juridiques, J.O. Jan. 5, 1991 [hereinafter Loi No. 90-1259].

<sup>69</sup>"Nul ne peut, directement ou par personne interposée, à titre habituel et rémunéré, donner des consultations juridiques ou rédiger des actes sous seing privé, pour autrui: 1° S'il n'est titulaire d'une licence en droit ou d'un titre ou diplôme reconnu comme équivalent par arrêté. . . ." *Id.* art. 26.

<sup>70</sup>This question is regulated in a separate law. See Loi No. 90-1258, *supra* note 15.

<sup>71</sup>See Loi No. 90-1259, *supra* note 69, art. 9.

<sup>72</sup>See *id.* art. 59; Décret No. 91-1197 of Nov. 27, 1991, organisant la profession d'avocat, J.O. Nov. 28, 1991.

<sup>73</sup>See DEU StBerG §§ 3, 4, 5, 160.

<sup>74</sup>See DEU StBerG §§ 13-31.

sions are regulated by law, but *tributaristi* can also be tax advisors who are not licensed professionals, because there is no monopoly on tax advice. Representation of taxpayers before the civil courts is limited to lawyers.

In the Netherlands, the profession of tax advisor is not regulated by law. Tax services are provided by a wide range of professions, all of which (except for tax advisors) are regulated by law: lawyers (*advocaten*), notaries (*notarissen*), accountants and auditors (*register accountants*), and tax advisors (*belastingconsulenten* or *belastingadviseurs*). However, the part of their activities that consists in providing tax services is not regulated. There is no incompatibility between the other professions and the tax advisors; that is, a lawyer or an accountant can at the same time be a tax advisor. The situation of tax advisors is unique in that, although the professions are not recognized by law, the two private organizations of tax advisors (NOB and NFB)<sup>75</sup> are so strong and prestigious that it is almost impossible to engage in tax services in the Netherlands without belonging to one of them. Both organizations use high professional standards for admission and strict ethical rules. The NOB requires an academic degree for membership and the NFB requires a rigorous training program with strict examinations.

In Spain, a tax advisor, called *asesor fiscal*, might be a lawyer (*abogado*), accountant (*economista*), or holder of a degree in business (*professor mercantil, intendente mercantil*). Again, the provision of tax advice is not restricted to particular professionals. Anyone can file a tax return for remuneration. However, tax litigation in civil courts is restricted to lawyers.

In the United Kingdom, tax advisors are typically known as accountants, tax consultants, or taxation practitioners, but there is no legal limitation on the general provision of tax advice. More and more solicitors are entering the field of tax advice. In the United Kingdom, external auditors, solicitors, and barristers are subject to regulations, but these do not specifically regulate tax advice. Anyone is free to prepare tax returns and to represent taxpayers before the tax administration or the tax commissioner on appeal from assessment. Only barristers can represent a taxpayer before the High Court.

Similarly, in the United States, tax advice may be given by lawyers, accountants, enrolled agents (i.e., those admitted to practice before the IRS), or those without professional certification. There is a kind of factual division of labor whereby ordinary tax returns are prepared by enrolled agents or by unregistered preparers, while more complicated cases are handled by lawyers or accountants.

<sup>75</sup>See *supra* note 1.