

GARY K. NELSON, THE ATTORNEY GENERAL
STATE CAPITOL
PHOENIX, ARIZONA

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DEPARTMENT OF LAW OPINION NO. 71-5 (R-26)

REQUESTED BY: CLYDENE F. HAUSNER
Executive Secretary
Arizona State Board of Accountancy

QUESTION: Does A.R.S. § 32-747.D, which reads: "No corporation shall be permitted to practice public accounting in this state, provided that this provision shall not apply to a professional corporation . . ." include the preparation of income tax returns and prohibit such a function to a corporate entity?

ANSWER: No. (This opinion hereby reverses Attorney General Opinion No. 61-44.)

Founded on the authority of Accounting Corporation of America v. State Board of Accountancy, 34 Cal.2d 106, 208 P.2d 984 (1949), it is a basic principle that the state, pursuant to its police power, may prohibit a corporation from practicing public accounting. The rationale on which this is based is the protection of the public welfare in an area requiring highly skilled, competent and ethical personnel. Upon this premise, the State of Arizona, as do all of our sister states, licenses certified public accountants and public accountants who hold themselves out as maintaining the highest standards of professional expertise and ethical conduct. The question then becomes whether or not the preparation of income tax returns comes within the definition of the practice of "public accounting".

Public accounting is not defined in the State of Arizona. It, therefore, becomes incumbent upon the Board of Accountancy and its legal adviser to determine whether or not the preparation of income tax returns comes within the purview of public accounting. Research by this office indicates that it does not. The general question of whether or not persons other than members of the Bar or licensed certified public accountants may prepare income tax returns is treated in 10 A.L.R.2d

1425, at pages 1444, et seq. That article stated:

"Freedom to follow any lawful occupation not injurious to others is a fundamental American liberty, secured by the Federal and State Constitutions alike. And a statute seeking to limit a citizen's right to pursue a beneficial trade, occupation, business, or profession, cannot be upheld as a police regulation unless it can be seen that the public, or a legally substantial portion of the public, will benefit therefrom."

Following this theme, the article discusses the case of Moore v. Grillis, 205 Miss. 865, 39 So.2d 505 (1949):

"Moore v. Grillis, . . . appears to be the first instance of an appellate court's considering the constitutionality of a statute setting up minimum standards to be met by persons offering their services to others in making out tax returns. There a Mississippi statute, forbidding under criminal sanctions any person other than a certified public accountant or a practicing lawyer, or their employees, with a 'grandfather clause' in favor of persons so engaged on a stated date, to receive compensation 'for making or preparing any tax return' was declared unconstitutional."

The article continues with a statement concerning the motivation for the court's decision:

"Danger from incompetency in this field was minimized. The court, after stating that tax returns, no matter by whom prepared, are examined for correctness by officials, went on to indicate that the natural shunning of those addicted to error will end in their being weeded out independently of aid from the legislature."

While the Moore case involved a non-corporate practitioner, it prepares the stage for the discussion of the question of whether or not there is valid reason to discriminate between an individual and a corporate entity. The court in the Moore case observed that there were not enough certified public accountants in the State of Mississippi to service the thousands of income tax returns filed annually. The court was cognizant of the United States Supreme Court's pronouncement that a state could not, under the guise of protecting the public, arbitrarily interfere with private business, prohibit lawful occupations or impose unnecessary restrictions upon them. Cf. Liggett Company v. Baldrige, 278 U.S. 105, 49 S.Ct. 57, 59, 73 L.Ed. 204 (1928). The court took notice of the fact that the state and federal governments have in the past and continued to make agents from state tax commissions, as well as the Bureau of Internal Revenue, available to assist individuals in the preparation of their income tax returns. The court held that the Constitution was violated by the provision prohibiting any person other than a member of the Bar or a licensed certified public accountant from making and preparing income tax returns as an unreasonable exercise of the police power, arbitrarily discriminatory, not in the promotion of public welfare and without reasonable relation to the advancement of public convenience, prosperity, health, morals or safety.

It must be noted at this juncture that there is no statutory prohibition in Arizona against an individual practitioner, either trained as an accountant or not, from establishing a John Doe tax service to prepare income tax returns. There would appear to be no reason to treat a corporate entity, which renders a similar service, differently.

Ultimately dispositive on this question, however, is the case of State v. Bookkeepers Business Service Co., 382 S.W.2d 559 (1964), which held that a corporation engaged in the preparation of income tax returns (among other services) was not practicing public accounting within the statutory meaning in the State of Tennessee. The Tennessee statutes prohibited public accounting practice by a corporation in T.C.A. § 62-141. Further, § 62-127 of the Tennessee Code Annotated, defined the practice of public accounting as including "compiling

tax returns". These sections are in direct contrast to the situation as it exists within the State of Arizona, where there is no statutory definition of public accounting. Notwithstanding the specific wording of the statute, the Tennessee court interpreted the section as not prohibiting the preparation of income tax returns by a corporation on the following reasoning.

The court stated that jurists have consistently held that legislation prohibiting noncertified accountants from practicing the profession of accountancy are invalid, infringing upon the rights of contract and having no bearing on or relation to the general public welfare.

"In the present case, it is clear that the defendant held itself out to the public as qualified to render, and did render to more than one employer, several of the services enumerated in the above code section, notably, the installing of a bookkeeping system, the recording and presentation of financial information or data, and preparation of tax returns. It is equally clear that, in doing so, the defendant did not represent itself as skilled in the knowledge, science and practice of accounting or as a 'public accountant' or a 'certified public accountant.' To the contrary, the defendant, in both its literature and solicitation of business, emphasized that it performed bookkeeping and similar technical services only, and did not do any auditing, verification of accounts, or certification of financial statements.

"We conclude, therefore, that the Chancellor correctly held that the business activity of the defendant did not constitute the practice of public accountancy."

Although the Attorney General of Tennessee argued to the contrary, maintaining the practice of income tax preparation did constitute the practice of public accounting and was

in fact prohibited to a corporation, the court stated at page 566:

"Admittedly, the Act is subject to this construction. However, the effect of such a broad construction, in our opinion, would make the statute unconstitutional as an unwarranted regulation of private business and the right of a citizen to pursue the ordinary occupation of bookkeeper and/or accountant. . . ."

The court also cited wording from the Journal of Accountancy, December, 1960, which said:

" . . . But the courts and the Treasury Department have indicated their disapproval of granting to anyone the exclusive right to perform bookkeeping and similar technical services, and to prepare Federal income tax returns.

"Accordingly it appears that the traditional function of certified public accountants--the auditing and expression of opinion on financial statements, on which third parties may rely--remains as the only function endowed with sufficient public interest to justify legal restriction of the right to perform it to certified public accountants and licensed public accountants." (Original emphasis.)

Note should be taken of the portion of the quotation above concerning the traditional function of the certified public accountant as the audit of and expression of opinion on financial statements (upon which third parties may rely) as being the only function sufficiently endowed with public interest to justify regulation.

Further reason for the negative answer to the Board's question is the information garnered in a survey conducted by the Executive Secretary, pursuant to the request of this office. That survey requested information concerning the

current law and/or board policy as to whether or not the preparation of income tax returns constitutes the practice of public accounting in the several states.

Responses from over sixty per cent of the states indicate unanimously that the preparation of income tax returns is not regarded as public accounting, either by statutory exclusion or Board of Accountancy interpretation and/or policy. These states include such notables as California, Colorado, Florida, Massachusetts, New Jersey, Michigan, New Mexico, New York, Oregon, Texas and Utah. Of the states surveyed, reference should be made to the States of California and Massachusetts for the following reasons.

Opinion No. 61-44 previously issued by this office was based, in part, upon the opinion of the Attorney General of the State of California, No. 46-315. The State Board of Accountancy of the State of California indicates that their opinion is no longer controlling, as it lacked definiteness and enforceability.

The State of Massachusetts is the only state responding to the survey which indicated that the Board drew a distinction between the preparation of individual tax returns as opposed to corporate or partnership returns. The Massachusetts Board stated that it had adopted a policy that the preparation and signing of corporate and partnership income tax returns constitutes the practice of public accountancy, in that these returns contain financial statements.

This latter distinction is one which must be made by the State Board as a policy matter, based upon its obvious competence and expertise in determining what does and does not constitute the practice of public accounting.

It is the opinion of this office that the preparation of income tax returns in general does not constitute the practice of public accounting, and, therefore, may be performed by corporate entities other than professional corporations. Any distinctions drawn between the eligibility of

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such corporations to prepare only individual income tax returns as opposed to corporate or partnership returns containing financial statements, certified or uncertified, must be made by the Board of Accountancy.

Respectfully submitted,


GARY K. NELSON
The Attorney General

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