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The complex interrelationship between law and accounting reveals itself in many forms and presents numerous questions which have been provocative of long continued debate and discussion. Among the questions arising most frequently are these:

1. To what extent has the law developed from principles of accounting?
2. To what extent have the law and the rulings of administrative bodies operating under the law determined accounting principles?
3. How much law should an accountant know for purposes of professional practice?
4. How much accounting should the lawyer know for *his* practice?
5. What are the bounds and limits of practice respectively of the two professions? Can coöperation be substituted for the present unfortunate competition?

In the short space here available it is impossible to discuss fully all of these questions. Attention is therefore centered primarily on the fourth—that relating to the lawyer's training in accounting. However, when necessary for a more complete discussion of this primary topic, reference is made to the other questions mentioned. In the footnotes are references to competent discussions of these other questions not fully treated here.

There is practically universal agreement among practicing lawyers that the services required of the lawyer today (outside of a very few specialized fields) demand a certain amount of accounting training for most competent performance.

A quotation from a letter received from a practicing attorney presents the case very clearly:

"The changing nature of the functions of an attorney have steadily increased the importance of a knowledge of the subject (accounting). I admit that when I was a boy and thought about becoming a lawyer, I had in my mind's eye the picture of a robust gentleman in a Prince Albert coat, who could thrust his hand between the first and second buttons, counting from the north, and, shaking his hoary locks, could shatter the circumambient atmosphere with glowing periods.

"It now develops, forgetting for the moment court work, that about two-thirds of my time with clients is taken up in answering questions which really should be put to a business man. While the knowledge of law is useful, and indeed necessary, in drawing a contract, of equal importance to the modern client is the ability to understand his business necessities and the hazards which may arise.

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"The intricate national legislation in connection with income, inheritance, and other forms of taxation, and the tendency of the states to enter the same domain, emphasizes the importance of a clear conception of accounting.

". . . I might make the matter the subject of an article, in which I could give some very interesting experiences with regard to blunders, sometimes ludicrous and sometimes tragic, which I have seen lawyers make in the trial of cases, and which would have been impossible had the law schools included even a four months' course in the fundamentals of accounting."

Other expressions by members of the bar read as follows:

"It has been my observation that training in the elements of bookkeeping and accountancy are very valuable to a trial attorney. For some years prior to becoming a member of this court [a state supreme court] I was one of the judges of a circuit court. While holding that position I many times noticed that the lawyer who is familiar with books of account has a great advantage over an opponent unfamiliar with such matters. The advantage soon comes to the notice of the jurors, and they place trust and confidence in the attorney who can quickly extract information from the account books. In fact, so much of the litigation, which is profitable to the attorneys, requires the examination of account books that all attorneys who expect to try cases ought to possess a knowledge of accountancy."

"From my twelve years' experience at the bar and in various types of legal work, particularly as pertains to railroad law and banking law, and from the standpoint of the practicing attorney, I am convinced that a knowledge of accounting is very, very important; not that the attorney himself must always, of necessity, prepare the figures or statements, but he certainly should be able to understand what they mean and how they are computed."

To supplement the preceding quotations taken from personal letters of practicing lawyers and judges, below are presented several brief statements which are fairly typical of the opinions held by members of the profession. Each one presents a slightly different angle of the question:

"Accounting is especially valuable in the examination of witnesses in the trial of cases; also for the intelligent understanding of a client's business and business problems."

"In the field of the patent law: (1) deals of all kinds for the manufacture and for sale of articles, machines, etc., whether on a royalty or other basis, require a thorough understanding of accounting, (a) for the negotiation of the deals, and (b) for the drafting of definite, certain and workable contracts; and (2) in connection with recoveries for infringement, a large body of law has been built up, which is generally referred to as 'the law of patent accounting.' The recovery is absolutely dependent upon a knowledge of accounting, and such knowledge is necessary to the application of the law itself. This has special reference to 'cost accounting' and to such items as the proper classification of

items of cost and the spreading of overheads, as well as such items as depreciation and depletion."

"A better training along this line would cut down many unintentional embezzlements and would better qualify lawyers to compete with banks in the settlement of estates and also to become more prominent in banking organization."

"The lawyer whose practice includes any substantial amount of advisory work for business enterprises, whether corporations or partnerships, has frequent need for an ability to understand and analyze financial statements. In legal specialties such as income tax practice, utility rate regulation, and corporate mergers and consolidations, a mastery of accounting principles is almost indispensable. Here the lawyer will often have an expert accountant associated with him and without some knowledge of accounting methods and terminology, he finds it difficult to utilize to the full the services of the expert.

"But, even apart from such specialized branches of the practice where the need for accounting is obvious, lawyers very generally recognize the value of an understanding of accounting in dealing with such questions as corporate dividends, income bonds, blue sky laws, corporate franchise taxes, qualification of foreign corporations, and partnership liquidations. Not least among the benefits resulting from such an understanding is the habit of visualizing business operations and financial condition in the form of the financial statements in common use. This habit very definitely facilitates the understanding of the legal rules involved in some of the rather complicated aspects of these problems."

These statements clearly indicate the correlation between law and accounting. One explanation of this interrelationship between these two fundamentally dissimilar fields is presented by A. A. Berle, Jr. and Frederick S. Fisher, Jr., after exhaustive research to determine the extent to which the courts have undertaken to impose rules of accounting as rules of law:

". . . day by day, lawyers and courts predicate legal effects on the results of accounting. It may fairly be said that rules of accounting are for many purposes rules of law; or, conversely, that rules of law entail rules of accounting. The respective tasks of a lawyer and accountant here intermingle so closely that neither can proceed without the other. To a much larger degree than perhaps either profession realizes, this intermingling has already taken place. Courts have in fact and in form laid down rules which bind the accountants, or they have themselves adopted accountants' conventions. The accountant, once his rules have found their way into the body of law, becomes legally obliged to follow them in his further work."[1]

Not only do the courts adopt and lend sanction to accounting principles as exemplified in accounting practice, but also the reverse is equally true—that the law, and administrative bodies created by the

[1] Berle and Fisher, *Elements of the Law of Business Accounting* (1932) 32 COL. L. REV. 573, 578. Consult this article for a very competent discussion of this interesting subject and for an appended digest of cases.

law, themselves in turn influence materially the development of accounting principles and practice. Most of the states have passed recently one of several types of so-called unfair trade practice acts. While these laws vary greatly among themselves in many respects, most of them have one element in common—a provision for a "fair" price which is related in some respect or other to a (frequently unstated) concept of cost. Accountants, and accounting-trained lawyers, should know that "cost" is a very complex and intricate term, that no definition of cost is possible except in terms of a specific purpose, and that even for a single purpose a satisfactory definition is most difficult to achieve. To empower an administrative board or commission to enforce an unfair trade practice act which does not define cost carefully and at great length, and from the point of view of a single specific objective, is to grant this commission the authority to "make law" on accounting matters, whether or not this be the intent of the original act.

The layman would assume—would have a right to expect—that the corporation statutes of the respective states would have a determining influence upon the principles and practices of corporation accounting. Unfortunately this is not entirely true, for: (a) orthodox legal concepts of accounting matters as they appear in many state corporation acts do not conform closely to generally accepted accounting principles and practices; (b) in the corporation acts of the several states there are many different treatments of accounting matters; and (c) often the use of accounting terminology is so loose and varied that the exact meaning and intent of the law remains uncertain. Even in the Illinois Act, in the formation of which there was a definite attempt to conform to good accounting practice, there is a substantial amount of ambiguity and uncertainty, and according to some authorities, at least one case of contradictory clauses.[2]

Today there are several dozen important administrative agencies, federal and state, which render final decisions, and therefore "make law" on accounting matters. One of these, the Securities and Exchange Commission, operating under the Securities and Exchange Act, has set forth formally and informally a number of "requirements" for registrants and is daily rendering "decisions" on disputed points of accounting practice. Normally these requirements and decisions are based on generally accepted accounting principles insofar as it is possible to determine what (if any) accounting principles are generally accepted. In any case, however, without review by any competent authority, they become authoritative, and for all practical purposes are written into

[2] See Frese, *Property Rights of Stockholders under the 1933 Illinois Business Corporation Act* (1935) 10 ACCOUNTING REV. 136; Payne, *The Effect of Recent Laws on Accountancy* (1935) 10 ACCOUNTING REV. 84, 89.

the body of the law. Two divergent views as to the desirability of this sort of "law-making", and its probable effect on accounting practice and on the law of business accounting, are presented below—the first by a lawyer and the other by an accountant; both discussions refer to the Securities and Exchange Commission. Strangely enough, it is the lawyer who expresses concern for accounting doctrine.

". . . There is always danger, where accounting rules are made by specialized administrative tribunals, that the resulting body of doctrine may be lop-sided, if not positively dangerous; however conscientiously the rulings have been made from the point of view of the administrators making them.

"Even more of a problem is the process by which these decisions —now become authoritative—are made.

". . . Now, this, it is submitted, is not a satisfactory state of affairs. Specifically,

1. Decisions so made are not recorded or available to others as a guide of conduct or a basis of informed criticism and comment;
2. They are by no means necessarily uniform, reasoned, systematic, or grounded on anything other than the feeling of the examining staff;
3. They are not reviewed by any competent authority, nor susceptible of being so; and
4. There is no procedure leading to the conclusion that such decisions are valid precedent rather than purely arbitrary determination, depending on the capability and integrity of the commission staff at any given moment.

"Yet there, at the present writing, is the mechanism by which rules of accounting are determined, and for all practical purposes, written into the living law, by the administrative agency having the greatest degree of control over the accounting profession save in a few specialized fields. Had the common law been developed in any such fashion, its major glory—the constant self-criticism which it engendered, and which has at all times been its safe-guard, its forward light, and its intellectual fertility—would never have come into existence. The criticism of process is fundamental. . . . The plain fact remains that effective accounting rules are made *in camera,* without system, without effective submission to criticism, with little guaranty against arbitrary determination, and without the continuous and open self-examination which much go into rulings which attain to the sanction and dignity of law."[3]

On the other hand, the accountant quoted below anticipates beneficial rather than ill effects on accounting principles and practice:

"The general effect of these regulations will undoubtedly be to strengthen the hands of all who are concerned in good accounting. Company accountants and public accountants will be able to point to these requirements in support of what they regard as necessary for accurate statement and full disclosure. While the Commission has endeavored to make its regulations liberal, practical, and adaptable to the greatly varied conditions of business, yet it is reasonable to believe that account-

[3] Berle, *Accounting and the Law* (1938) 13 ACCOUNTING REV. 9.

ing principles, as embodied in the published statements of corporations, will look more like the accounting principles taught in colleges than ever before. And this will be true whether or not the statements are filed with the Commission; it would be absurd to suppose that in the circumstances reports to stockholders, or any other publications by business corporations, could show any material divergences from statements filed with the Commission. Company and public accountants all over the country have that idea clearly in mind."[4]

Conclusions that follow from the foregoing discussion are that practically all business legislation and regulation should "tie in" at some point with accounting principles and practice; and, therefore, that it behooves the lawyer who contemplates any substantial amount of business practice to become familiar, to some degree, with business accounting.

The accounting profession is much younger than the legal profession, but it has grown very rapidly during the forty or fifty years of its active history. The interrelationship between law and accounting has become constantly more complex during this whole period. In spite of the fact that the two professions are fundamentally dissimilar there are many situations which involve mixed questions of law and accounting fact. Of necessity, therefore, the activities of lawyers and accountants must overlap at many points.

In a report presented in 1933 to the Essex County (New Jersey) Bar Association by a joint committee of lawyers and accountants, the following were noted as examples of activities requiring the services of both accountants and lawyers:

1. Planning the type of legal entity to conduct a new business, having in mind the subject of Federal, State, and Municipal taxes.
2. Upon incorporation of businesses, the opening of books of account and installation of accounting systems.
3. Problems involved in the dissolution of partnerships and corporations.
4. Problems involved in the consolidation, merger, and reorganization of corporations.
5. Preparing accounting and cost systems in connection with the Federal Securities Act and with the National Industrial Recovery Act.[5]
6. Determination of extent of damages and profits in patent and other infringement suits.
7. Public Utility rate cases.
8. Determining losses covered by fire insurance policies and preparation of proof of claim.

[4] Sanders, *Influence of the Securities and Exchange Commission upon Accounting Principles* (1936) 11 ACCOUNTING REV. 66.

[5] Note that the reference to N.I.R.A. is no longer pertinent and that reference to the Securities and Exchange Act might now be added.

9. Matters arising in receivership and bankruptcy cases, including examination of books and records of the bankrupt and an analysis of financial statements.

10. Determination of rights of life tenant and remainderman, especially with regard to distribution of corporate dividends.

11. Income tax matters, including presentation of cases before the Commissioner of Internal Revenue and before the United States Board of Tax Appeals.

To the foregoing list of "coöperative" activities may be added others suggested by lawyers and public accountants who have expressed opinions on this matter. Their suggestions include the following:

1. The preparation or interpretation of lease contracts, particularly where valuation of property or the determination of income is involved, or where there are lease security deposits.

2. Problems relating to the declaration of dividends.

3. The preparation of documents creating trusts, either living or testamentary.

4. Preparation of evidence for presentation in court where accounting records constitute an important part of the evidence.

5. The preparation of uniform legislation, particularly where it affects the interpretation of such terms as surplus, earned surplus, capital surplus, stated capital, dividends, insolvency, and many other matters which relate to both accounting and law.

6. Preparation of registration statements for the Securities and Exchange Commission.

There are undoubtedly many other points at which lawyers and accountants should unite their activities in the endeavor to render to clients a service which is complete and adequate for the specific purpose at hand. However, the examples listed above constitute a fair sample, and in themselves offer substantial proof of the necessity of coöperation between these two professions. Furthermore, they give some indication of the type of accounting training useful to a lawyer.

A natural result of this overlapping is that lawyers feel that accountants are encroaching upon their practice. For several years committees representing the American Bar Association and the American Institute of Accountants have been discussing, at joint meetings and by correspondence, the bounds and limits of practice of the two professions which these associations represent.[6] They have endeavored to agree upon a joint statement regarding the relationship between the practice of the lawyer and of the accountant in the fields where they meet. Some progress has been made, but they have not yet been able to come to an agreement upon certain sections of this statement, particularly that section

[6] Byerly, *Relationship between the Practice of Law and of Accounting* (1938) 66 JOURNAL OF ACCOUNTANCY 154.

dealing with tax practice. On this phase of the problem the American Bar Association committee on unauthorized practice of the law has stated definitely its opinion that it is within the practice of the law, rather than accounting, to engage in any of the following activities:

1. To give advice regarding the validity of tax statutes or regulations or the effect thereof in respect of matters outside of accounting procedure.

2. To determine legal questions preliminary or prerequisite to the making of a lawful return in a lawful manner.

3. To prepare protests against tax adjustments, deficiencies, or assessments.

4. To represent a taxpayer at a conference with administrative authorities in relation to matters outside of accounting procedure.

5. To prepare claims for refund of taxes.

6. To prepare petitions, stipulations, or orders incident to the review of assessments by the United States Board of Tax Appeals or any like administrative tribunal.

7. To conduct the trial of issues before the United States Board of Tax Appeals or any like administrative tribunal.

Accountants have voiced strong objections to the views presented above. The committee of the American Institute of Accountants has expressed the opinion that it is impossible to set forth broad rules establishing a dividing line between the practice of law and the practice of accounting, particularly in tax cases, for there is a complex interrelationship between law and accounting in this field. This committee has suggested as an alternative procedure the adoption of a "case method" of dealing with the problem. It suggests that the Bar Association refer to the Institute, or to state accounting societies, cases in which accountants have engaged in alleged improper practices. The accounting organizations might then investigate these cases and prevent a recurrence of the offense. The bar committee, apparently, has received this proposal favorably, and it is probable that some such coöperative machinery will be attempted, first in the State of New York.

Thus, it appears that several years of negotiation between the representatives of these two professions have produced only a tentative agreement to "coöperate" in a "case method" of dealing with "improper" accounting practice. In the opinion of the writer, this constitutes some evidence that the fields of law and of accounting are not exactly separable, that there is a "no man's land" of practice which will always be a field for: (a) lawyers and accountants coöperating in joint practice, or (b) practitioners with adequate training in both professions, armed with admission to the bar and with a C. P. A. certificate, or (c) lawyers with *some* accounting training, or accountants with *some* legal training,

whichever "get there first". It is doubtful that there is any way of solving satisfactorily this problem of so-called "improper practices" of either lawyers or accountants.

In a few specialized fields there are distinct opportunities for simultaneous practice of law and accounting. The best of these opportunities lie in various fields of taxation and in the handling of trusts and receiverships. There are several outstanding examples of this type of practice. In many cases the individual engaging in joint practice has been admitted to the bar and also holds a C. P. A. certificate; in other cases one or the other of these formal qualifications is lacking. It would seem that law students who display a special interest in and aptitude for the accounting and financial aspects of legal business problems should be encouraged to consider the opportunities in this dual field and to secure the necessary accounting and business training to engage in it. In such joint practice, however, even in these highly specialized fields, there is the distinct probability that one or the other of the two professions will become the major one.

The discussion to this point should be sufficient to show that it is no longer necessary to "sell" the lawyer on the need for some knowledge of accounting. Only a few years ago this point of view was not generally accepted; traditionally the training of lawyers did not include accounting—nor does it yet, universally, but largely because facilities for providing this training economically (from the point of view of time requirements) have not been easily available. There are so many fields in which the lawyer should be proficient, and there is so little time available in his few years in the law school, that not everything can be included. Small wonder, then, that accounting, which in the usual school of business course requires perhaps twenty or more semester hours, has not always been included as an essential course.

The change in the attitude of lawyers toward accounting training is seen to arise from several causes:

First, the increasing complexity of the modern business and economic situation has brought about an evolutionary change in the nature of services required of the lawyers. This trend is evidenced by the lawyers' opinions already quoted.

Second, the lawyers' lack of accounting training has been a prime factor in the loss of certain types of practice to accountants, and in the growth of public accounting services of a nature approximating legal services. This condition, now so greatly deplored by lawyers, would not have developed, in all probability, had lawyers been thoroughly trained in accounting.

Third, with the development of accounting into a recognized profession, there has been a corresponding improvement in accounting train-

ing. There is now a sharp distinction between bookkeeping, as taught in most high schools and business colleges—designed to give vocational training for minor clerical positions—and accounting as taught at a collegiate and professional level.

Fourth, the time required for such training has been greatly reduced. The need for general accounting training for students of business, of law, and of engineering, etc., has caused the development of specialized courses for each of these student groups. For example, in one major educational institution, there are four accounting programs: one for accounting specialists, including a total of eight or ten or even more accounting courses; one for general business students, composed of three courses; a single course for the students of economics in the social science division; still another single course for students in the law school. While all of these programs start at the same point—with an explanation of the fundamental principles of double entry accounting—they differ vastly in point of view, amount of emphasis on technique and procedure, kind and amount of case and problem material, number of topics discussed, speed and inclusiveness of "coverage", and in many other respects.

In the course for law students, the only one pertinent to this discussion, the so-called accounting process—the principles of double entry and basic accounting procedures—is disposed of in about four to six class sessions, about one-fourth the time required for the general business students and perhaps only one-tenth of the time required by the accounting specialists. In this course for lawyers practically no attention is given to the various types of journals, ledgers, and other books of entry. On the other hand greater emphasis is given to partnership and corporation accounting, to statement analysis, and to certain other topics than in the other courses.

In short, the law student is given a different kind of an accounting course from that offered to other groups of students—one that lays emphasis on principles and problems pertinent to the study and practice of the law. And not the least important feature of such a course is the relatively short time required for a comprehensive survey of those parts of the whole accounting field which are most essential for the lawyer. A single course of perhaps four or five semester hours has been found to be adequate for the purpose. This development has done much to remove one major obstacle to accounting training for lawyers—the excessive time requirements of non-specialized accounting courses.

There is no complete agreement among lawyers as to how much knowledge of the various phases of accounting is desirable for law practice. The majority of lawyers seem to agree that "the more knowledge the better", but there is the question of marginal utility. Just how much

time can a law student afford to take from other pre-legal and legal subjects to devote to accounting? A few lawyers are definitely in favor of a complete accounting training: "as much as a C. P. A."; "thoroughly well informed"; "he can't have too much"; "there is no limit"; etc. At the other extreme are many who insist on only a "knowledge of the fundamentals", "a general working knowledge", "enough to know what it is all about", etc. The predominating opinion is to the effect that a lawyer should be able not to *do,* but to *understand,* what is done; he should be able to analyze and interpret statements, and have sufficient knowledge to work intelligently with accountants who perform the actual accounting work. More training is required, of course, for specialized corporate or other commercial work.

Conclusion

Frequent reference has been made to the increasing complexity of business and to the additional legislation and governmental regulation which in recent years have still further complicated the problem of business activity. In many cases there are few or no guiding precedents, and forward steps must be very carefully planned and executed. Mistakes can be avoided only if advantage is taken of all available sources of information. The combined judgments of accountant, lawyer, and client afford little enough assurance against errors of policy or procedure. The value of the lawyer in connection with these joint decisions will be materially increased if he has been trained to appreciate their financial as well as the legal implications.

An analysis from an accounting point of view not only aids in the understanding and statement of rules of law, but also would probably have saved the courts from laying down certain rules now recognized as unfortunate. Especially in the case of partnerships and corporations there are many instances of decisions which have resulted apparently from an inability or failure on the part of counsel and court to analyze the problem as an accountant would. And there are many instances also, of problems with which the courts have apparently had great difficulty and upon which the reasoning in their opinions is obscure and unsatisfactory, but which become much easier of satisfactory solution in the light of accounting principles. To be sure, the courts have had to work out many of these problems before accounting had reached anywhere near its present state of development, but today not only may many old rules of law be profitably restated, but whole groups of new problems may be solved more readily and confidently if counsel are equipped with an understanding of the fundamental techniques of accounting and if the courts are able and willing to follow counsel in such analyses. Recent opinions suggest that judges in increasing num-

bers are welcoming this type of assistance. And the fact that law students who have had training in accounting usually master the difficult problems of corporation law more easily than do students without such training is further evidence that an understanding of accounting principles is of value in the analysis and solution of many legal problems.

It has been noted that accounting principles have long served as non-legal precedents for legislation and court decisions on financial and business matters. The accounting-trained lawyer is in a peculiarly strategic position to exercise his influence in hastening this evolutionary process. By so doing he performs a distinctive social service, for many glaring inequities should disappear as still more of our fundamental accounting principles are embodied in formal legislation and legal precedent.

The suggestion is not intended that the accountant's approach would facilitate the handling of all the legal problems with which the lawyer and the accountant are both concerned. There are many points at which the accountant has little light to throw on the problem, as in the case of the apportionment of "income" between life tenant and remainderman. Here, as frequently, the only help the accountant can offer is to point out practical advantages or disadvantages of alternative rules with respect to the relative complexity of the computations and bookkeeping which they entail. In such matters the law must govern the accounting practice. And on the other hand, the simultaneous consideration of the legal and accounting aspects of certain problems may suggest the necessity of important modification of accounting practice in order to reflect the results of the legal rules.