Volume 64 | Issue 3 Article 5

April 1962

Corporate Benefits for Attorneys: Restrictions and Possibilities

Robert Glenn Lilly Jr.
West Virginia University College of Law

West Virginia Law Review

Published by the College of Law of West Virginia University. Official publication of The West Virginia Bar Association.

STUDENT NOTES

Corporate Benefits for Attorneys: Restrictions and Possibilities

"Statutes, cases, and canons of ethics uniformly state that a 'corporation cannot practice law.' Less uniformly, similar principles today apply to the professions of medicine, accountancy, and architecture."[1] These professional people are the only business groups in our economy which cannot freely choose their form of organization.[2] However, a movement is now underway, both at the state and federal levels, to tear down this barrier of inequality.

I. Benefits Denied Attorneys

Because of the attorney's inability to select the corporate form as his business organization he is prevented from qualifying for tax opportunities, business continuity, and business planning otherwise available when business is carried on in the corporate form.[3] The

[1] Note, 12 STAN. L. REV. 746 (1960). W. VA. CODE ch. 30, art. 2, § 5 (Michie 1961), provides that it is unlawful for a corporation to practice law.
[2] Lyons, *Comment on the New Regulations on Associations,* 16 TAX L. REV. 441, 460 (1961).
[3] Jones, *The Professional Corporation,* 27 FORDHAM L. REV. 353 (1959).

major tax benefits denied the professional man are: profit-sharing and retirement plans, pension plans, group life insurance, health and welfare plans, and deferred compensation plans.[4] Main emphasis by reformers is put on the practitioner's inability to set up a pension plan. Such a plan would be a great tax advantage as the lawyer, being considered both employer and employee, could deduct the contributions to the plan with the benefits not taxable until distributed or made available. Beyond the mere fact of postponing the tax, the attorney would more likely be in a lower income tax bracket when payment is made. Lump sum payments from the fund because of death or separation from employment would result in taxation at the advantageous long-term capital gain rates. As a further matter, income earned by the principal accumulation during the period of the plan would be exempt from taxation until distributed.[5]

II. Reasons for Denial of Attorneys' Right to Incorporate

The distinction between the professional man and the corporate employee rests entirely upon the fiction of the corporate entity. Yet this difference is correct "with the conventional powers and attributes now available under existing state laws."[6] The reasons for prohibiting the practice of law in the corporate form are: first, simply that a corporation is not eligible for a license to practice a profession; second, a corporation, as such, cannot be disbarred or suspended; and third, it is feared that the corporate entity would intrude upon the purely personal relationship of the attorney and his client, for not only would the attorney's loyalty be divided, but also middlemen-laymen, the shareholders, would be profiting because of his services to another. Even if original owners were required to be licensed practitioners, inheritance and distribution could eventually bring in the unlicensed. More particularly is the concern that management and control of the corporation in the hands of laymen would result in commercial exploitation of the profession. Finally, there is the problem of misconduct or malpractice, recovery for which could be effectively curbed by the doctrine of limited liability, one of the most common and cherished attributes of a corporation.[7] In summary, the practice of law is limited to individuals qualifed, morally as well as mentally; this right cannot be

[4] Jones, *Should Lawyers Incorporate?*, 11 HASTINGS L.J. 150, 152 (1959).
[5] INT. REV. CODE OF 1954, §§ 404, 501(a), 402(a) (2).
[6] Jones, *supra* note 3.
[7] *Id.* at 354.

inherited, it must be earned. The attorney is an officer of the court with the corresponding oath and duties; his relation with his client involves the highest trust and confidence. A corporation cannot be allowed to do indirectly what an attorney cannot do directly.[8]

Specifically, there is the possibility that the arrangement of the corporate profession would violate several of the Canons of Professional Ethics.[9] In a recent opinion of the American Bar Association's Committee on Professional Ethics[10] it was stated that the substance of the arrangement, rather than the form, determines whether any canon is violated. The mere fact that lawyers use a corporate form of organization would not in itself constitute a violation of any canon. However, the opinion made it clear that each such organization would have to stay within the definite bounds of the pertinent canons.[11]

In spite of these proscriptions it seems that the practitioner will soon be able to attain tax relief similar to that enjoyed by corporate employees. In fact, for some, such equality appears already at hand. Basically, the end can be accomplished either by direct federal legislation granting such relief[12] or through compliance with existing tax laws and regulations. A corollary of the second alternative will be appropriate state action in many, if not in most, instances.

III. Federal Legislation As a Solution

The quest for tax equality for the professional man on the federal level is not of present origin. The first organized effort toward enacting federal legislation occurred in 1945. The movement continued with the introduction of a bill for the first time in 1951. In 1956 the enactment of such a bill, then the Keogh-Jenkins Bill, was listed as one of the principal goals of the American Bar Association President, David F. Maxwell.[13]

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[8] *In re* Co-operative Law Co., 198 N.Y. 479, 483-84, 92 N.E. 15, 16 (1910).

[9] Canons of Professional Ethics, Nos. 31, 33, 34, 35, 37, and 47.

[10] Opinion 303, Nov. 27, 1961, 48 A.B.A.J. 159 (1962).

[11] Among others was the expression that the lawyer must remain personally responsible to his client and that no layman should be allowed a beneficial or voting interest in the association.

[12] England in 1956 and Canada in 1957 provided pension plans for self-employed persons. Hosking, *United Kingdom's Experience With Pensions for Self-Employed,* 97 Trusts & Estates 313 (1958); Fairbanks, *Taxation—Pension Plans for Self-Employed Persons,* 35 Can. B. Rev. 564 (1957).

[13] Keogh, *Tax Equity for the Self-Employed,* 47 A.B.A.J. 665 (1961).

A. H.R. 10

In 1961, during the last session of the 86th Congress and again in the first session of the 87th, the House of Representatives passed a bill which would have provided pensions for the self-employed. However, each bill expired with the sine die adjournment of the particular Congress.[14]

The House again has passed a similar bill in the present 2nd session of the 87th Congress, and the Senate for the third time has the bill for consideration with a vote expected on it before April 1 of this year. Greater support is expected particularly since fourteen of the seventeen-member finance committee voted for it. If there is a favorable vote by the Senate, the bill would then go to a House-Senate conference committee to settle differences. Congressmen Keogh predicts that President Kennedy would sign the bill if it passes.[15]

Reasons for the failure of the bill to be enacted into law, other than opposition to the basic idea itself, can best be seen by a comparison and contrast of the House Bill, H.R. 10, with the Finance Committee's substitute.[16] In both, self-employed persons generally are treated as employees for retirement plan purposes and are eligible for coverage in qualified plans. Special averaging provisions are in each to prevent ordinary income taxation when a lump-sum distribution is received by the self-employed pensioner. Note that this is generally less favorable than the capital gain treatment afforded lump-sum payments from qualified pension plans to today's bona fide corporate employee.[17] Normally, under each bill the attorney-beneficiary must be 59½ years of age before becoming eligible for distribution, unless death or permanent disability ensues, and it is mandatory that payments begin before age 70½. The bills differ in the amounts that the self-employed is allowed to deduct and in the coverage for the self-employed's own employees, the House Bill is more liberal in both aspects. The Senate Bill would limit the owner of more than ten per cent of the business to a maximum yearly deduction of 1,750 dollars and would allow other owners

[14] Rapp, *Pensions for the Self-Employed: The Treasury Department-Finance Committee Plan,* 16 TAX L. REV. 227, 246 (1961); 48 CCH STAND. FED. TAX REP.: Taxes on Parade, No. 47, Part II, Oct. 4, 1961.

[15] American B. News, Jan. 15, 1961, p. 2.

[16] Rapp, *supra* note 14, at 252. The full texts of the House Bill and the Senate Finance Committee Bill of 1961 are found in 48 CCH STAND. FED. TAX REP.: Taxes on Parade, No. 45, Part I, Sept. 30, 1961.

[17] INT. REV. CODE OF 1954, § 404.

only one-half of amounts in excess of 1,000 dollars. The House Bill, on the other hand, would allow the ten-per cent owner to deduct 2,500 dollars plus an amount proportionate to contributions for his own employees. Owners of less than ten per cent of the enterprise could deduct an unlimited amount if the plan was non-discriminatory to his employees. Thus the House Bill would allow the self-employed equal treatment with the corporate employee if the plan qualified under the Internal Revenue Code.[18]

The Treasury Department opposes the bill mainly on the basis of loss of revenue.[19] The Treasury also fears that passage would open the door for further remedial legislation in this area.[20] As a condition of withdrawing its objection, the Treasury wants to tighten the present day law on qualified pension plans and repeal various other exemptions to offset partially the expected loss of revenue.[21]

B. *Other Federal Legislation*

The revenue loss resulting if a bill like H.R. 10 were passed would be much greater than if other alternatives restricted to the professional man were used. Only one out of seventeen self-employed persons is from the legal, medical, or dental professions.[22] Other alternatives requiring federal legislation include either an amendment to the Internal Revenue Code permitting lawyers and other professionals to establish pension plans or broadening the definition of employees under section 7701 of the Code to include lawyers. Precedence for the latter is the fact that full-time life insurance salesmen have been so designated.[23] As a further alternative, it is suggested that the objectives of the legislation could best be attained by an amendment of sections 401 through 404 of the Internal Revenue Code to grant self-employed persons the full benefits permitted corporate employees under present qualified pension and profit-sharing plans.[24]

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[18] INT. REV. CODE OF 1954, § 404(a).
[19] At the present time this argument is not so forceful because of the evolutionary effect of state laws which allow corporate benefits. See subsection infra, "State Association Laws."
[20] Rapp, *supra* note 14, at 232, but see, Donohue, *Smathers-Keogh-Simpson Legislation: Retirement Savings for the Self-Employed*, 45 A.B.A.J. 795 (1959), attacking the Treasury's opposition.
[21] Maier & Wild, *Taxation of Professional Firms as Corporations*, 44 MARQ. L. REV. 127, 141 (1960).
[22] Donohue, *supra* note 20, at 798.
[23] INT. REV. CODE OF 1954, § 7701(a) (20).
[24] Maier & Wild, *supra* note 21, at 142.

C. Advantages and Limitations of Federal Legislation

Federal legislation might be viewed by the professional man as unsatisfactory because it results in less than full equality with the corporate employee. As a consequence he might seek equality elsewhere, particularly when matters such as continuity of life, centralized management, and transferability of ownership interests are desired in addition to the benefits of sections 401 through 404.[25] However, all of these proposed federal solutions which would grant the professional man specific corporate benefits rather than general corporate status have the advantage of not impairing the valid objections underlying state laws and canons of ethics which bar the professional groups from incorporating. In the same light, there would not be the objection of the "tax tail wagging the dog,"[26] the choice of an entirely new form of organization merely for the tax advantages and not for the reason that the new form would benefit and improve the business enterprise. Nor would there be the resulting chaos because of the structural and legal changes of the professional firm. Above all, such federal legislation would have the effect of removing the treatment of the professional groups from the uncertain state which now exists and rendering uniform the treatment rather than having a differing status from state to state.

Even though the effort to achieve federal legislation "appears to be nearing fruition,"[27] passage is still not certain and benefits thereunder are somewhat limited. Therefore, other means may be attempted to achieve equality for the professional man.

IV. ASSOCIATIONS AND THE REGULATIONS AS A SOLUTION

Under existing laws there are apparently three forms of organization whereby a group of professional people could obtain organizational and employee benefits comparable to those now available to corporate employees and executives: joint stock company, common law trust, and association.[28] The joint stock company as a solution is doubtful, particularly as there is no precedence. The common law trust, or the Massachusetts business trust, is "well adopted for

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[25] *Id.* at 143.
[26] *Id.* at 127 wherein the author sets forth the proposition that "the different forms of business organization should be accorded the same tax treatment so that . . . election of one form over another will not depend on the tax results obtained. . . . The tax tail is often so important that it wages the dog as to the selection of the proper form of organization."
[27] Rapp, *supra* note 14, at 252; American B. News, *supra* note 15.
[28] Maier & Wild, *supra* note 21, at 128-29.

the use of a professional group which wishes to take advantage of corporate taxation without being a corporation."[29] The association is the organizational form which is predominately being employed by professional men at present in their attempt to gain corporate advantages.

A. Background: Cases, Statutes, and Rulings

The association was used in the leading case of *Kintner v. United States.*[30] In this case a group of doctors had established a clinic organized as an association. Under their agreement all were licensed physicians. The purpose clause provided that the association should be endowed to the extent permissible by law with all the attributes of a corporation and should be treated as a corporation for purposes of taxation. There was a specific provision preserving the confidential relationship between physician and patient. The members were to be employed and considered as employees despite their beneficial interests in the association. The association was to continue until death of the last original member, the interests to be non-transferable. Centralized management in a purely representative capacity was established and annual membership meetings were provided for. Salaries were fixed and to be paid by the association and fees were to be collected by the association. Further, the association assumed necessary expenses of the members, employed non-member doctors, paid social security and withholding taxes, and controlled the doctors' activities generally. Title to property was in the name of the association. All employees were qualified to participate in the pension plan if they were thirty-five years old and had been employed in the association or its predecessor for three years. Finally, the employees were to be given credit for the period of membership in the predecessor partnership in determining their eligibility under section 401 of the Internal Revenue Code.

The Court in the *Kintner* case followed *Burk Waggonner Oil Ass'n v. Hopkins*[31] as authority that nothing precluded Congress from taxing an association as a corporation which transacted its business as if it were incorporated even though unincorporated and considered a partnership under state law. In the *Kintner* case the court found that the clinic more nearly resembled a corporation

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[29] *Id.* at 129.
[30] 216 F.2d 418 (9th Cir. 1954).
[31] 296 U.S. 110 (1935).

than a partnership and thus was entitled to corporate status for taxation. Resemblance and not identity is paramount.[32]

The keystone provision defining a corporation for purposes of taxation is section 7701(3).[33] Since 1917 the statutes have defined the term corporation as including associations but have not yet defined the term association. Case law[34] developed the rule that an association necessarily includes associates and an objective to carry on a business enterprise for joint profit. Since a partnership also has these attributes, further elements were listed in determining corporate status: limited liability, centralized management, continuity of existence, and transferability of interest. If these remaining characteristics are determined to be more corporate than non-corporate, the organization is considered to resemble a corporation and entitled to corporate treatment.

Two years after the *Kintner* decision a revenue ruling was issued which declined to follow the case either in the determination that such an organization was an association or in the allowance of past service in the computation of benefits under a qualified pension plan.[35] It concluded that if a partnership adopted the corporate form to get the benefits of a qualified pension plan, it was still to be considered a partnership for all purposes. However, a clarifying letter to this ruling provided relief to actual incorporations of professional men in a state permitting such incorporates from the impact of the ruling.[36] A later revenue ruling relaxed the original ruling. The Commissioner stated that the "usual tests" would be applied in determining whether a particular organization of professional people had more of the characteristics of a corporation than of a partnership.[37] "The implication was that local law would, at the very most, have only a secondary effect on a determination which would be based in the main on federal standards."[38] However, as a whole the position of the ruling on pension plans for professional people was vague because of the uncertainty of the term "usual tests."

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[32] Morrissey v. Commissioner, 296 U.S. 344, 357 (1935).
[33] INT. REV. CODE OF 1954, identical to Int. Rev. Code of 1939, § 3790.
[34] Morrissey v. Commissioner, *supra* note 32.
[35] Rev. Rul. 23, 1956-1 CUM. BULL. 598.
[36] Letter of clarification from H .T. Swartz, Director, Tax Ruling Division, Internal Revenue Service to Richard L. Mackan, Attorney, Dallas, Texas, March 7, 1957.
[37] Rev. Rul. 546, 1957-2 CUM. BULL. 598.
[38] 6 CCH 1961 STAND. FED. TAX REP. ¶ 5943.

B. The Regulations

Revenue rulings, although reflective of the Service's views, do not have the effect of law as do regulations.[39] In 1960 regulations were promulgated with the intent of clarifying the law.[40] The new regulations are considerably more detailed and at first glance seem to be based upon criteria set forth in *Morrissey v. Commissioner*[41] and subsequent decisions. The regulations provide that the Internal Revenue Code is to decide the tests to be applied in determining the classification in which an organization belongs regardless of the classification of the organization under state law. Following the decision in *Morrissey,* it is provided that resemblance based on the presence or absence of the various corporate characteristics determine the treatment of the organization. However, "the regulations, in two sentences, make local state law rather than federal law controlling in this entire matter of associations taxable as corporations."[42] Although federal law governs in determining the tests to be applied,

> "local law governs in determining whether the legal relationships which have been established in the formation of an organization are such that the standards are met. Thus it is local law which must be applied in determining such matters as the legal relationships of the members of the organization among themselves and with the public at large, and the interests of the members of the organization in its assets."[43]

The practical effect is that even though inability to incorporate under state law does not preclude the organization from being classified as an association, technical requirements under state law may negate the existence of the necessary corporate characteristics despite the agreement of the members.[44] This effect is seen in the subsection "continuity of life"[45] where the regulations provide that if withdrawal of a member causes a formal dissolution under local law, the element of continuity is lacking. This would result despite

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[39] Helvering v. New York Trust Co., 292 U.S. 455, 468 (1934).

[40] Treas. Reg. § 301.7701 (1960).

[41] 296 U.S. 344, 359 (1935).

[42] Ray, *Corporate Tax Treatment of Medical Clinics Organized as Associations,* 39 TAXES 73, 78 (1961); that the treatment is the same as previously, see Bittker, *Professional Associations and Federal Income Taxation: Some Questions and Comments,* 17 TAX L. REV. 1, n.8.

[43] Treas. Reg. § 301.7701-1(c) (1960).

[44] Lyons, *supra* note 2, at 458.

[45] Treas. Reg. § 301.7701-2(b) (1960).

an agreement of the members providing that such withdrawal would not cause dissolution and the further element that the business was in fact continued by the remaining members. In another subsection the regulations provide that transferability is lacking "if under local law a transfer of a member's interest results in even the [formal] . . . dissolution of the old organization and the formation of a new organization."[46]

Seven examples are given in the regulations to illustrate the application of the rules. The first two examples concern doctors forming organizations; the third, attorneys. The examples and other sources indicate that if two of the corporate characteristics of limited liability, continuity, transferability, and centralized management are satisfied and two others are not, the organization will be classified as a partnership.[47] However, two characteristics plus a modified form of transferability may suffice.[48] Under the regulations, modified transferability is present when a member may dispose of his interest only after offering it to other members.[49] Since the lawyer is precluded from enjoying the corporate advantage of limited liability because of ethical and statutory restrictions, an organization of attorneys would have to satisfy the requirements of centralized management, continuity of life, and at least a modified form of transferability. If such could be established under state law, there is no reason why a legal partnership may not avail itself of the benefits of the regulations as freely as would a medical partnership.[50]

The regulations and examples result in the "complete dominance of local law over federal law . . . which is quite foreign to the usual rule with respect to federal tax matters."[51] The importance placed on local law seems to conflict with the *Kintner* case and other decisions which held that local law, although not to be ignored, was not to control the test or standards of classification.[52] Furthermore, the regulations are confusing in that the two examples on doctors and the one on lawyers make no reference to the effect

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[46] Treas. Reg. § 301.7701-2(e) (1960).
[47] 6 CCH 1960 STAND. FED. TAX REP. ¶ 8973.
[48] *Ibid.*
[49] Treas. Reg. § 301.7701-2(e) (1960).
[50] Stutsman, *How to Organize Professional Men for Corporate Tax Status Under Kintner*, 11 J. TAXATION 336, 339 (1959).
[51] Ray, *supra* note 42, at 84.
[52] Helvering v. Coleman-Gilbert Associates, 296 U.S. 396 (1935); Helvering v. Combs, 296 U.S. 365 (1935); Swanson v. Commissioner, 296 U.S. 362 (1935); Morrissey v. Commissioner, 296 U.S. 344 (1935); Galt v. United States, 175 F. Supp. 360 (D.C. Tex. 1959).

of local law on the agreement of association. Taken as a whole the regulations are themselves contradictory.[53] The term partnership is not limited to its common law meaning, and the classes into which the organizations are to be placed along with the tests and standards to be applied in deciding the classification are to be determined under the Internal Revenue Code; but the legal relationships are to be determined under local law. This is "a new, single legalistic test in place of the old, multiple, realistic test set forth in the *Morrissey* case."[54] In addition, the regulations appear "to elevate form over substance."[55] Actual practice and conduct of carrying on the business despite technical dissolution should better indicate continuity rather than local law.[56] Finally, the regulations could act as a deception to the taxpayer who might believe his organization would qualify as an association because of analogy with the examples when in fact it would not so qualify because not allowable under local law.[57]

An organization in a state under the Uniform Partnership Act cannot qualify as an association under the regulations.[58] Under these laws a partnership will lack the corporate characteristics of continuity of business, centralized authority, limited liability, and transferability[59] which are the four features distinguishing an association from a partnership for federal income tax purposes.[60] Forty states have adopted the Uniform Partnership Act[61] which includes West Virginia.[62] Thus, without change in the particular states laws, professionals in only one-fifth of the states could possibly obtain benefits under the regulations which is far removed from any degree of uniformity that the regulations profess at the outset. "It is highly improper to deal at a local level through the state legislatures with a problem which is essentially a child of the federal tax laws."[63]

[53] Ray, *supra* note 42, at 84.

[54] *Ibid.* However, that the regulations are in conformity with past case law see Bittker, *supra* note 42.

[55] Saltz, *Associations*, 38 TAXES 187, 191 (1960).

[56] *Ibid.*

[57] *Id.* at 193.

[58] Ray, *supra* note 42, at 74. However, Kintner v. United States, 216 F.2d 418 (9th Cir. 1954) was decided in Montana which had adopted the U. P. A.

[59] 48 CCH STAND. FED. TAX REP.: Taxes on Parade, No. 44, Part I, Sept. 13, 1961.

[60] Treas. Reg. § 301.7701-2(a) (1960).

[61] 48 CCH STAND. FED. TAX REP., *op. cit. supra* note 59. The states which have not adopted the U. P. A. are: Alabama, Florida, Georgia, Hawaii, Iowa, Kansas, Louisiana, Maine, Mississippi, and New Hampshire.

[62] W. VA. CODE ch. 47, art. 8A, § 1 (Michie 1955). Also,

[63] Saltz, *supra* note 55 at 193.

C. State Legislation As an Answer

In 1961, in answer to the regulations, fifteen states upset long established traditional and statutory proscriptions and passed "professional association laws" or amended the pertinent provisions of their Uniform Partnership Acts.[64] These statutes have the common characteristic of not altering the law applicable to the relationships between the attorney and his client including liability of the lawyer which might arise out of his professional services. Their intended effect is to place professional men on an equal tax basis with employees of corporations generally. Some of these laws have already been held within the proper ethical bounds[65] but as yet there have been no decisions determining that such laws satisfy the requirements of the regulations. However, these laws apparently stand a good chance of so qualifying.[66]

West Virginia has neither passed nor introduced such a bill at this time. In fact, there has been very little evidence of an interest in a "professional's corporation act" at present or in the near future. The subject was not considered at the extraordinary session of the 1962 state legislature which would postpone any such action until at least the next regular legislative session in 1963.

State legislation is thought to provide a potentially workable and reasonable method of accomplishing tax equality among professional men, although, in theory, true equality could more simply and better be accomplished by an act of Congress.[67] As a further practical matter, state laws force federal action with the result that Congress may ultimately pass a "professional's corporation law" due in part to

[64] 49 CCH STAND. FED. TAX REP.: Taxes on Parade, No. 8, Part I, Jan. 24, 1962. The respective state statutes are reproduced, at ¶¶ 507-805. Ten states allow professionals generally to incorporate, including attorneys: Alabama, Connecticut, Florida, Georgia, Illinois, Ohio, Oklahoma, Pennsylvania, Tennessee, and Wisconsin. Texas seems to include professionals generally although coverage is not clear. In addition, Colorado allows law corporations. Three states have statutes limited to medical professions: Arkansas, Minnesota, and South Dakota.

[65] *In re* the Florida Bar, 133 So. 2d 554 (Fla. 1961).

[66] 48 CCH STAND. FED. TAX REP., *op. cit. supra* note 59. That they will likely not so qualify see Eber, *The Pros and Cons of the New Professional Service Corporation,* 15 J. TAXATION 308 (1961); Bittker, *supra* note 42, at 3, "because of ambiguities in their status under state law." Opinion 303, *supra* note 10, where it is stated that there is some doubt whether the various statutes will result in such associations being classified as corporations for federal income tax purposes and in addition it is expressed that the members of the Committee have "grave doubts" of the wisdom or feasibility of lawyers adopting the association form.

[67] Jones, *Should Lawyers Incorporate?,* 11 HASTINGS L.J. 150, 153 (1959).

pressures of the states' laws.[68] This pressure was seen in 1948 with the passage of the husband and wife split-income tax laws.

D. Advantages and Disadvantages of Qualifying As An Association

An attorney, before changing his form of organization to an association in those states whose laws allow such change, should consider the disadvantages inherent in the corporate form as well as the disadvantages which might be present in the particular situation. The attorney's pension plan will not qualify if it discriminates in his favor against other employees.[69] Personal holding company taxes[70] as well as accumulated earnings taxes[71] should be considered. Double taxation, once at the corporate level and again at the individual level, might result in increased taxes. Double taxation could occur if salaries did not meet the test of reasonableness.[72] Revenue agents particularly watch for this in closely held corporations. One possible answer would be to loosen the standard of reasonableness.[73] Another solution would be subchapter S.[74] Under this latter possibility undistributed income of the association is considered as if it were divided among the owners; thus, reasonableness of compensation would be immaterial for purposes of salary deduction.[75] Subchapter S would not presently deprive one of pension benefits but in the light of proposed regulations and proposed legislation in Congress "which would tend to strip a subchapter S of the privilege of claiming deductible fringe benefits . . . subchapter S might not prove to be a satisfactory tax alternative."[76] Another privation could be the taxing authorities disregarding the corporate entity in transactions with owners.[77] In addition, there is the possibility that the establishment of the corporate entity would be disregarded as being created solely for the purpose of reducing income tax.[78] It should also be kept in mind that though achieving status of a corporation

[68] Jones, *The Professional Corporation*, 27 FORDHAM L. REV. 353, 371 (1959).

[69] INT. REV. CODE OF 1954, § 401(a) (3) (B).

[70] INT. REV CODE OF 1954, § 541. See Eber, *supra* note 64 for a discussion of the personal holding tax aspect.

[71] INT. REV. CODE OF 1954, § 531.

[72] INT. REV. CODE OF 1954, § 162(a) (1).

[73] See Klamath Medical Serv. Bureau, 29 T.C. 339 (1957).

[74] INT. REV. CODE OF 1954, §§ 1371-77.

[75] Note, 12 STAN. L. REV. 746, 763 (1960).

[76] Jones, *Should Lawyers Incorporate?*, 11 HASTINGS L.J. 150, 152 (1959).

[77] Jones, *The Professional Corporation*, 27 FORDHAM L. REV. 353, 371 (1959).

[78] *Ibid.*

will not itself necessarily result in the imposition of taxes,[79] a change of mind probably will be a taxable event.[80] Finally, it is to be remembered that state fees and taxes would likely be imposed on these organizations doing business in the corporate form.[81]

Of course, many advantages accompany the corporate form; otherwise, there would be little sense in agitating for the organizational characteristics. Besides fringe benefits such as pension plans[82] association would: allow fiscal year choice, provide for centralized management and pooling of skills, permit reduction or addition of associates without dissolution and continuity of practice by successors, establish a market cash value for qualified eligible successors, come under the lower corporate tax ceiling, and provide additional flexibility for estate planning.[83]

CONCLUSION

The lawyer walks a tightrope between the tax law and the general law. He wants to be sure not to violate local corporate laws or canons of ethics, but he wants his organization to qualify as an association for tax purposes. The regulations are dangerous[84] even in those states which have passed laws to meet the situation. Specific federal action would relieve this unwanted sporting element but

> "unfortunately Congress, which is composed mostly of lawyers, hasn't done too much for the lawyers specifically. There are not any panaceas, any special provisions, of which lawyers are the designated beneficiaries, as there are special provisions, for example, benefiting cattle raisers and people who grow Christmas trees,"

unless the fact that benefits will ultimately be reaped by lawyers because of continued and increased complexity of the Internal Revenue Code could be so considered.[85] However, with federal legis-

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[79] INT. REV. CODE OF 1954, § 351. Though changing from a partnership to a corporation is not necessarily a taxable event, there are certain pitfalls which would result in a taxable exchange, especially if accounts receivable of a cash-basis taxpayer are involved. INT. REV. CODE OF 1954, § 751. For a discussion of this possibility see Eber, *supra* note 66, at 309-10.
[80] INT. REV. CODE OF 1954, §§ 331, 1001, 1002.
[81] 49 STAND. FED. TAX REP., *op. cit. supra* note 64, at 27.
[82] See corresponding text, *supra* note 4.
[83] Eber, *supra* note 64.
[84] *Ibid.*
[85] Sanger, *Tax Problems of Lawyers*, 42 CHICAGO B. RECORD 127 (1960).

lation there would be the objection that the benefits would be limited.

Perhaps the lawyer and other professional men would be more satisfied if a liberal compromise were reached giving unambiguous full benefits. However, this cannot be expected overnight first at the federal level because of the resulting loss of revenue and second at the state level because of the deep-rooted objection to a corporation practicing law. Decisions as in the *Kintner* case, state legislation, and proposed federal legislation that have occurred are large steps forward in giving the professional man tax equality. The strongest misgiving would seem to be the fact that the impact of the federal income tax is strong enough to change tradition.

Robert Glenn Lilly, Jr.