

# Accountants and Their Confidentiality Statute

By Laurence R. Donaldson



## Fast Facts:

- Because there was no accountant privilege at common law, MCL 339.732(1), being in derogation of the common law, must be strictly construed.
- Regardless of what the *client* did previously, the *accountant* is bound to obtain written permission before producing information gained in the course of an engagement, even in the face of subpoena.
- Before you subpoena a CPA's files, check to see if MCL 339.732(1) will be a bar to obtaining the information you seek.

You are involved in a divorce case and have questions about one spouse's reported income or distributions made to him or her from a closely held business. Or in a dispute between the owners of a business over a buy-out of one by the other. Or a dispute between the seller and the buyer over the value of an item or a business sold. Or you are seeking discovery into the claimed economic losses suffered by the opposing party. Or there is some issue regarding what might have appeared on someone's tax return. What to do? I know, you say, let's subpoena the accountant's work papers and files.

Before you do that, it is best to fully understand the meaning of the accountant confidentiality statute, MCL 339.732. That statute is part of article 7 of the Occupational Code, which governs public accounting and licensing of a certified public accountant (CPA). MCL 339.732(1) states:

Except by written permission of the client or the heir, successor, or personal representative of the client to whom the information pertains, a licensee, or a person employed by a licensee, *shall not disclose or divulge* and *shall not be required to disclose or divulge* information relative to and in connection with an examination or audit of, or report on, books, records, or accounts that the licensee or a person employed by the licensee was employed to make. Except as otherwise provided in this section, the information derived from or as a result of professional service rendered by a certified public accountant is confidential and privileged. [Emphasis added.]

There was no accountant privilege at common law, so the statute, being in derogation of the common law, must be strictly construed.<sup>1</sup> Two exceptions to the statutory privilege, one seen frequently and the other less frequently, are important in the situations that this article considers.<sup>2</sup> They will be discussed further below.

What are the practical implications of the statute? Some argue that since the information sought has been discussed in other places, the CPA's client has waived confidentiality. Some argue, This is a subpoena; it is a court order you have to obey. Some argue that the court has issued a discovery order directing the party to provide the information. All those arguments will, and should, fail with respect to the CPA. Regardless of what the *client* did previously, the *accountant* is bound to obtain written permission before producing information gained in the course of an engagement, even in the face of subpoena. Without that permission, the accountant's only course of action is to appear as the subpoena requires, but decline to produce records or give testimony (a waste of everyone's resources). Threatening the accountant

with contempt may get him or her to appear, but it will not get you the information you are seeking.

An important part of MCL 339.732(1) is the language “shall not be required to disclose or divulge.” Note that the statute does not add “unless you are ordered to do so by a circuit court judge” or “unless you receive a subpoena.” It is my opinion that a trial judge has no authority to order a CPA to produce or testify without written permission, since that would require violation of the statute and subject the CPA to adverse action, either from the client or the State Board of Accountancy. Of course, the court always has the power to rule that a party has waived the privilege and must provide the written permission on pain of some evidentiary or issue preclusion for failure to do so. I am aware that at least one family court judge in the Oakland Circuit Court has ruled from the bench during trial that she could not order testimony from a CPA whose nonparty client had declined to give permission.

So what is the solution when you believe there is information important to your client’s cause in the hands of a CPA? First, request the information directly from the CPA’s client. Second, if the information relates to a party, seek written permission from the party. If necessary, and if appropriate, seek a court order. The court may compel the party to either produce the information directly or give written permission to get it from the CPA, or it may rule that the party will be precluded (by an order in limine against that party) from using any of that information itself at a later trial. If the CPA’s client is a person or an entity not a party to the case, request or subpoena the information directly from that person or entity. It is likely not privileged in their hands.

The two exceptions to MCL 339.732(1) mentioned earlier sometimes help. For example, if the CPA’s clients are a husband and wife who file joint tax returns or the client is an entity owned 50-50 by two people, both of whom were actively involved and worked with the CPA, then *Harwood v Randolph Harwood, Inc*<sup>3</sup> may help. Basically, *Harwood* held that since both individuals (or the individuals and the company) are “the client,” neither can invoke the statute against the other. In such a case, the CPA is bound to comply if subpoenaed. Keep in mind, however, that if the owners/clients are not parties to the lawsuit, if a party was only a part-owner, or if one party to the action is not a client, that analysis doesn’t work and the CPA still needs written permission. Often, in divorce matters, the parties earlier filed joint returns, but in more recent years filed separately. In that case, if a CPA prepared the joint returns and now prepares one party’s separate returns, written permission is needed to obtain the separate returns.

The other exception is the “crime-fraud exception.” If otherwise privileged information constitutes evidence of a present, ongoing crime or an act of criminal fraud, the court may hold that the privilege does not apply. But in a criminal investigation, the exception only allows access to the CPA’s information that refers to an ongoing or future wrongdoing. A CPA’s information regarding past misconduct is still covered by privilege.<sup>4</sup> It is my opinion that even the attorney general is bound by the statute and cannot lawfully execute a criminal search warrant against an accountant

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seeking evidence of past misconduct of the CPA’s client. At least one judge in the Ingham Circuit Court has so ruled in a case in which the crime-fraud exception was alleged and found not to apply, citing *People v Paasche*<sup>5</sup> and the statute.

In federal court diversity matters applying Michigan law, the statute applies.<sup>6</sup> But in federal investigations by such agencies as the Department of Justice, Department of Labor, and Internal Revenue Service and in federal grand jury matters, the state statute does not apply.<sup>7</sup> However, in an IRS/taxpayer dispute, there is a statutory provision that may keep some of the taxpayer’s information in the accountant’s file privileged.<sup>8</sup> You should undertake a detailed analysis in such cases.

In short, before you subpoena a CPA’s files, check to see if MCL 339.732(1) will be a bar to obtaining the information you seek. ■



*Lawrence R. Donaldson, a senior shareholder in Plunkett Cooney PC’s Mount Clemens office, has devoted his career to the defense of accounting and legal malpractice cases. He is a former chair of the State Bar Standing Committee for Lawyers Professional Liability Insurance and former president and chairman of Michigan Lawyers Mutual Insurance Company. He served eight years on the State Board of Accountancy and is counsel to the Michigan Association of Certified Public Accountants.*

## FOOTNOTES

1. *People v Simon*, 174 Mich App 649, 658; 436 NW2d 695 (1989).
2. This article will not address the limited applicability exceptions found in MCL 339.732(2) and (3).
3. *Harwood v Randolph Harwood, Inc*, 124 Mich App 137; 333 NW2d 609 (1983).
4. *People v Paasche*, 207 Mich App 698, 707; 525 NW2d 914 (1994).
5. *Id.*
6. *Berdon v McDuff*, 15 FRD 29, 31-32 (ED Mich, 1953).
7. *Couch v United States*, 409 US 322, 335; 93 S Ct 611; 34 L Ed 2d 548 (1973).
8. 26 USC 7525(b).

CONFIDENTIAL

19:5  
22:4  
23:0  
23:1  
23:5  
06:0  
9:3