THE STORM OVER OUR HEADS: THE RENDERING OF LEGAL SERVICES BY AUDIT FIRMS IN SPAIN*

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May 2000

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forthcoming the *International Journal of the Legal Profession, vol. 7.

THE STORM OVER OUR HEADS: THE RENDERING OF LEGAL SERVICES BY AUDIT FIRMS IN SPAIN

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This article dwells on the thorny debate which is nowadays being held in the Spanish legal profession regarding the rendering of legal services by audit firms. Compared with other countries, the debate in Spain has been rather belated, and it is currently at its zenith due to the discussion of new regulatory measures of the legal profession (*Estatuto General de la Abogacía*)-which would expressly prohibit the joint rendering of legal and audit services by a same firm- and the approval of the so called Olivencia Code on Good Corporate Governance, in which the auditor's duty of independence when certifying the financial statements of Spanish public corporations is stressed.

In this article the different arguments on that debate are analysed, evaluating their soundness. The examination of the different positions gives way to an alternative proposal of regulation which underlines the role of an *informed* market on disciplining excessive auditors' dependence on their clients. Moreover, the potential conflicts of interests should be prevented by the strict observance and enforcement of the respective professional legal and ethical duties.

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JEL Classification: K22, K39, K40, L84, M49
Encyclopaedia of Law & Economics: 5860
Keywords: Spain, MDPs, audit firms, law firms, legal profession, non-audit services, independence, professional services, MAS.

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FINAL DRAFT (May 30, 2000)

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THE STORM OVER OUR HEADS: THE RENDERING OF LEGAL SERVICES BY AUDIT FIRMS IN SPAIN.

1. INTRODUCTION.

In the last few years the legal profession in Spain has been in turmoil. The market for legal services has undergone profound changes and the profession has done its most to adapt to client's new demands, modernising firms and improving the quality of the services rendered[2]. Besides, the Spanish market for legal services is growing at a rate 20% higher than other European markets[3].

The needs of clients have placed two challenges before Spanish attorneys and these have forced law firms into two different forms of association:

The first has to do with *globalisation*. Business have grown transnationally and lawyers have had to attend client's demands of legal services in other countries. This has lead Spanish law firms to increase their size[4] and

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[2] For some general overviews see FERGUSON (1997), STOAKES (1984) and STEWARD (1991). See also «Metamorfosis en la abogacía española», *El País Negocios*, 25 April 1999, 13; «El baile de los bufetes», *Actualidad Económica*, 2155 (11-17 oct. 1999), 48 and 50.

[3] See «Los grandes bufetes crecieron un 18,3 por ciento en 1997, el mejor ejercicio de toda la década», *Expansión*, 27 march 1998, 60; «La demanda de asesoría legal crecerá en España más rápido que en el resto de la UE», *Expansión*, 15 oct. 1999, 60.

[4] For example, recently *Uría & Menéndez* has taken over the law firm *Figaredo & Asociados* (see «Uría & Menéndez absorbe el bufete Figaredo y Asociados», *Cinco Días*, 29 sept. 1999, 30) in 1998 *Uría & Menendez* took over *Bufete Armero* (the later had a revenue in 1997 of 4 million euros), see «Uría & Menéndez in Madrid Merger», *International Financial Law Review* 17 (Nov. 1998). Almost simultaneously, one of its main rivals, *Cuatrecasas*, acquired *Dura* in Alicante and other firms in Portugal, see «Cuatrecasas increases presence in Spain and Portugal», *International Financial law Review* 17 (Oct. 1998); «Cuatrecasas culmina la integración del segundo mayor bufete portugués», *Expansión*, 13 Oct. 1999, 76. Lately *Cuatrecasas* acquired the Spanish branches of the Dutch firm *Loeff Claeys & Verbeke* and merged with other three Latin American firms (see, respectively, *Economist & Jurist*, 36, march/april 1999, 98-99 and *Economist & Jurist*, 35, jan./feb. 1999, 96). *Goméz Acebo & Pombo* reached an alliance agreement with the Portuguese firm *Vieira de Almeida* and with the Brazilian firm *Pinheiro Neto* (see «Expansión internacional de Gómez Acebo & Pombo», *Economist & Jurist*, 36, march/april 1999, 99; «Gómez Acebo & Pombo entra en Latinoamérica de la mano del mayor despacho de Brasil», *Expansión*, 23 feb. 2000, 61). See also «Cremades adquiere una "boutique legal" en Argentina», *Expansión*, 7 april 2000, 67.

also to many kinds of international alliances and networks formed by several firms from different nations[5]. There are some instances of Spanish law firms trying to extend their services in other countries, by establishing there a branch or by taking over a foreign firm.

This worldwide phenomenon affects the legal profession of all countries, which find themselves in fierce competition for clients[6]. In the case of Spain, however, the pressure and competition by foreign law firms has been more relevant due to two important factors[7]. First, the increasing competition by foreign attorneys within the single European market. Secondly, the Spanish legal market is seen by many foreign firms as the access

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On february 14, 1999, *Baker & Mckenzie* reached a merger agreement with the firm *Jiménez de Parga* (see «La norteamericana Baker& Mackenzie absorbe el despacho Jiménez de Parga», *Expansión*, 17 feb. 1999, 61). At the same time, *Garrigues & Andersen* reached a cooperation agreement with the firm *Ribalta y Asociados* that will presumably result in a follow-up merger in three years (see «Garrigues & Andersen continua su crecimiento con la absorción del bufete Ribalta y Asociados», *Expansión*, 3 march 1999, 65). Both deals are reported in *Economist & Jurist*, 36, march/april 1999, 98. On march 2000, *Garrigues & Andersen* announced its plans to expand their business in Portugal and South America, see «El bufete Garrigues & Andersern proyecta expandirse en Latinoamérica y Portugal», *Cinco Días*, 31 march 2000, 26.

[5] For an overall view, see STEWARD (1990).
The best example being the participation in the Alliance of European Lawyers of *Uría & Menéndez*. However, *Uría & Menéndez* abandoned the Alliance in 1998 when *Linklaters & Paines* joined it [see «Linklaters & Alliance confirmed without Uría», *International Financial Law Review* 17 (august 1998), 3-4]. Currently, the Alliance is formed by five European firms: *Linklaters & Paines, De Bandt, van Hecke & Lagae, De Braw Blackstone Westbrock, Lagerlöf & Leman, and Oppenhoff & Rädler*. These five firms have agreed on integrating increasingly themselves leading to a full merger in the near future. But see also, «El bufete Uría & Menéndez inicia su desembarco en Iberoamérica», *Expansión*, 3 Apr. 1998, 56.

[6] In general, see FLOOD (1996, 173 and 188-197). For the situation in: Germany, see ROGOWSKI (1994, 21 and 26; 1995, 123-124); England, see LEE (1992), who also raises the ethical problems that size increases may create; the U.S., see GALANTER and PALAY (1990).

[7] Regarding the competition by British law firms in the Spanish legal market (particularly, *Allen Overy, Clifford Chance*, *Dibb Lupton Alsop* and *Freshfields*) see «Las firmas británicas se cuelan en lo más alto del ránking por prestigio de los bufetes españoles», *Expansión*, 21 apr. 1999, 61; «Dibb Lupton confirma su entrada en España», *Expansión*, 1 oct. 1999, 66 (also *Cinco Días*, 1 oct. 1999, 36). *Linklaters & Paines*, *Simmons & Simmons*, *S. J. Berwin* and *Cameron Mckenna* have also shown their strong interests in opening offices in Spain (see *Economist & Jurist*, 36, march/april 1999). See «El gigante británico Linklaters prepara su desembarco en el mercado legal español», *Expansión*, 9 feb. 1999, 53; «Linklaters cambia de estrategia en España e inicia un potente plan de fichajes», *Expansión*, 30 nov. 1999, 75; «Los despachos británicos Simmons & Simmons y S. J. Berwin & Co. preparan su desembarco en España», *Expansión*, 25 feb. 1999, 53; «El 'top ten' británico Cameron McKenna prepara su entrada en el mercado legal español», *Expansión*, 17 march 1999, 61; «El despacho inglés Allen & Overy cierra la integración del bufete Satrústegui & Asociados», *Expansión*, 27 oct. 1999, 69; «Davis Arnold Cooper estudia abrir un despacho en Barcelona durante el año 2000», *Expansión*, 3 dec. 1999, 66; «Los despachos británicos Eversheds y Cameron McKenna negocian alianzas para entrar en España», *Expansión*, 10 dec. 1999, 67; «El bufete Linklater se refuerza en España», *Expansión*, 7 april 2000, 68; «El bufete británico Simmons & Simmons refuerza su despacho en Madrid», *Cinco Días*, 9 april 2000, 33.
For the competition by U.S. law firms, see «El gigante americano Jones negocia entrar en España de la mano de Tena & Muñoz», *Expansión*, 19 nov. 1999, 62, «Jones Day reforzará su despacho en España e iniciará la entrada en el mercado italiano», *Expansión*, 9 feb. 2000, 61.

gate to the South American legal market. The first challenge has to do with competition among law firms in an increasingly integrated worldwide market for legal services (*intraprofessional competition*).

The second challenge is related to *multidisciplinary services* and the rendering of non-legal services by law firms or the rendering of legal services by non-law firms[8]. Law firms, consulting and auditing firms are becoming multi-product firms. In this case, law firms' competition is not directly with other law firms but with other professionals, mainly audit and consulting firms (*interprofessional competition*)[9].

It is not new that clients' demands often exceed the legal domain, but it is a novel approach that lawyers have been prompt and eager to render those non-legal services, or that audit firms offer their services in the legal domain. In other words, law firms have had no problem in diversifying their services, hiring other professionals (accountants, consultants, etc.) or associating with audit or consulting firms in order to provide other non-legal services[10]. On the other side, audit firms have created their own law divisions or have associated or merged with law firms in order to be able to satisfy client's needs on legal issues[11].

This article aims to analyse the problems raised by multidisciplinary services and, particularly, by the rendering of legal services by audit firms or by the formation of coalitions by audit and law firms to provide legal services. These issues are currently under hot debate in Spain, as the draft of regulation of the legal profession includes some articles that would expressly ban «Multidisciplinary Partnerships» (MDPs) from the practice law.

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8 See MUNNEKE (1992, 561-565). For an interesting essay about the profession's "debate" on diversification, see DEZALAY (1992, 233-269). Another trend of some (small and medium size) law firms towards strong "specialization" in certain areas of the law can also be ascertained (tax, administrative, labor, etc.) -'boutique' practice firms-, but that is not the case of the large law firms or of the legal divisions of the audit firms, which follow a clear "generalization" or "specialization in every area of the law" pattern. See DE ANGULO (1989, 320-321).

9 See BANKS (1997), BOWER (1999), DEZALAY (1992, 171-176), LEE (1992, 39-40), McGARRY (1999), VAN DUCH (1997).

10 For example, in 1984 *Cuatrecasas*, one of the largest law firms in Spain, set up its own audit and consulting firms: *Audihispana* and *Audihispana-Consultores*; however they separated in 1989, see STEWARD (1991, 23). More recently (oct. 1999), the audit firm *Mazars & Asociados* reached a merger agreement with two small law firms (*bufete Plasencia* and *bufete Calavia-Hernández Puertolas*).

In Germany, see ROGOWSKI (1994, 25-26; 1995, 126 and 131). In general, on this diversification trend (in the U.S.) see DEZALAY (1991, 800-803; 1992, 182-188), FITZPATRICK (1989, 465-470), GALANTER and PALAY (1990, 754 ftn. 31 and 807), MacDONALD (1989, 595-596).

11 See ANDREWS (1989, 632-636), CARTY (1996), CANNON (1997); «Accountants and lawyers. Disciplinary measures», *The Economist*, 350/8109 (6 march 1999), 78-79; Mike Yuille and Tim Weekes, «Multidisciplinary Partnerships. Teaming with promise», *Law Society's Gazette*, 94/40, 22 oct. 1997, 27-29.

In case of affiliation, the law firms are known as «Captive Law Firms» (CLFs). This is a frequent vehicle for the association of audit firms and law firms in England, see LSEW (1998, §7.6.1), LSUC (1999; 1998b, 22).

This article intends to overcome the frequent hypocrisy and self-bias that pervade the opinions held by the different sides in this debate[12]. Unfortunately, the economic and market interests come out as an insurmountable obstacle thwarting a truly objective analysis (legal and economic) of the issue[13].

In order to discuss the question posed by the entrance of audit firms to the legal services market, the status of the audit profession and the audit market (2) and of the legal profession and the legal market (4) are briefly studied. The expansion of audit firms to other professional services' markets is best understood as a further growth of the audit firm's non-audit services (3), and has found a strong resistance from the legal profession, which has attempted to prevent the audit firm's invasion of the legal services market (5).

2. THE AUDIT PROFESSION AND THE AUDIT MARKET IN SPAIN.

The true origin of the modern market of audit services in Spain is related to the implementation of the Eight EC Directive on Company Law[14]. Although beforehand some sort of public accountant's control over the financial statements of the corporations existed, the audit market was rather underdeveloped. Only at the end of the eighties, with the *Auditing Act of 1988*[15] and the *Corporation Act of 1989*[16] the situation changed completely[17]. The new *Corporation Act* imposed the obligation of corporations exceeding certain size[18] to

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[12] Two self-explanatory examples of the deceitfulness of the opinions in this debate:
A) In 1996 Antonio Alonso-Lasheras, partner *J. & A. Garrigues*, declared himself contrary to the rendering of legal services by audit firms, in his opinion that would risk the respective freedom and independence of lawyers and auditors, besides he was suspicious about the "obscure" (*sic*) role of audit firms and the problems of captive clientele, see his prologue to Silvia DEL SAZ, *Los Colegios Profesionales* (Marcial Pons, Madrid) 11 and 18. *J. & A. Garrigues* merged *Arthur Andersen ALT* shortly thereafter (see infra note 74).
B) More recently, Tomas Fernández de Pinedo, PWC's partner responsible of strategy and integration within *Estudio Legal*, had de nerve to affirm «I am a lawyer, I have been practising for thirty years and I never joined with an auditor»(!), see «Nunca me he unido a un auditor» (interview with Tomas Fernández de Pinedo) *Cinco Días*, 4 june 1999, 33.

[13] Some of the defendants of MDPs consider that the arguments of their opponents are truly based in the traditional law firms' fear of competition from audit firms, see ANDREWS (1989, 616-621), LÓPEZ CHICHERI (1999, 21).

[14] *Directive EEC 84/253* , of 10 April 1984 (Official Journal L 126, of 12.05.84, 20).

[15] *Ley 19/1988, de Auditoría de Cuentas, approved on 12 July 1988* (BOE nº 169, 15.07.1999) [hereinafter *Auditing Act*].

[16] *Texto Refundido de la Ley de Sociedades Anónimas*, approved by Real Decreto Legislativo 1564/1989, of 22 December 1989 (BOE nº 310, 27.12.1989; BOE nº 28, 01.02.1990) [hereinafter *Corporations Act*].

[17] See GABAS TRIGO (1992), PRADO LORENZO *et al.* (1995, 632 and 634-635)

[18] In accordance with article 51 of the *Fourth EEC Directive on Company Law* (78/660), of 25 July of 1978 (Official Journal L 222, of 14.08.1978, 11), only those corporations that could formulate an abbreviated balance sheet according to article 11 of the Directive could be exempted for the statutory audit. In Spain, article 181 of the *Corporations Act* implemented this exemption and established the financial conditions, allowing

appoint a statutory auditor that should give an opinion about the company's financial statements. The appointment as statutory auditor is reserved to those accountants registered in the "Registro Oficial de Auditores de Cuentas" (ROAC)[19]. In order to become registered in the ROAC there are two main routes.

One is open to accountants who are in possession of a University Degree (generally, but not mandatorily, an economics or business degree). The other one is designed for those accountants who, without a university degree, have a long experience in accounting and auditing. In both cases a period of practice is required and a program of theoretical education must have been followed[20]. Additionaly, there is an official test of professional competence that must be passed before the registration in the ROAC is approved[21]. Apart from individuals, audit firms can also be registered in the ROAC, with the only requirement that a majority of the members be auditors, and that the management of the firm be in charge of an auditor[22].

As in many other European countries, the audit market in Spain is mainly controlled by the "Big Five"[23]. They

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companies the possibility to formulate an abbreviated balance sheet. These conditions are updated from time to time. The last update was in 1997, by article 1 of Real Decreto 572/1997, of 18 april 1997 (B.O.E. nº 104, of 01.05.97).

[19] See art. 6.1 of Ley 19/1988, art. 21 of Real Decreto 1636/1990, of 20 December 1990, which enacts the *Auditing Regulation*, adopted in execution of the *Auditing Act* [hereinafter *Auditing Regulation*].
The *Instituto de Contabilidad y Auditoría de Cuentas* (ICAC), is the competent body within the Spanish Ministry of Economy and Budget, to manage and update the ROAC.

[20] In general, see BLASCO LANG and FERNÁNDEZ ESTELLES (1992, 341-342), NUÑEZ LOZANO (1989, 119-122), PETIT LAVALL (1994, 152-153 and 155), ARANA GONDRA (1995, 296-303 and 307-308). The "experience route" for accessing to the ROAC was introduced in an amendment of the *Auditing Act* by the *1990 General State Budget Act* (D.A. 13ª).
Accordingly, there is an "academic route», requiring a university degree, three years of practice and passing the official test and an "experience route", which requires high school education, eight years of practice, and passing the official test.
Those in possession of a University Degree can do away without some of the theoretical education and the corresponding first phase of the test depending on the specific degrees (arts. 7.4 of *Auditing Act* and 26.2 of *Auditing Regulation*).
Some of the current criticism with the Spanish auditing profession is related to these procedures, which are considered not a sufficient guarantee of competence of the auditors registered in the ROAC. Indeed, this is one of the issues that is planned to be amended in the foreseen amendment of the *Auditing Act*. See, «Las tres corporaciones demandan más control y nivel de formación para acceder a la auditoría», *Cinco Días*, 12 Aug. 1999, 22.

[21] Article 7.4 of the *Auditing Act* and articles 26 and 27 of the *Auditing Regulation*. See BLASCO LANG and FERNÁNDEZ ESTELLES (1992, 343-346), PETIT LAVALL (1994,157-158), ARANA GONDRA (1995, 304-305)

[22] See article 10 of the *Auditing Act* and articles 28 and 29 of the *Auditing Regulation* (except public limited liability companies). See also ARANA GONDRA (1995, 361-371), NUÑEZ LOZANO (1989, 123), PETIT LAVALL (1994, 199-210).

[23] See PEREGRINA BARRANQUERO (1982) for a study of the entry, organization and working procedures of the international auditing firms in Spain. For data about Spain [88% of the audit reports received by the Spanish Securities Market Commission (CNMV) are prepared by the «Big Five»], see GARCÍA-AYUSO

are the statutory auditors of most of the Spanish large corporations, and they certify the financial statements of most of those quoted in the Madrid Stock Exchange (*Bolsa de Madrid*).

3. AUDIT FIRMS AND NON-AUDIT SERVICES.

Professional services go beyond borders according to the audit and consulting firms. Increasingly they describe themselves as worldwide professional advisers, covering any professional area and rendering all kind of professional services[24]. This is the situation of the large audit firms, especially the so called "Big Five"[25]. All of them, started as audit firms, but soon became consulting firms and the same thing happened with most of the professional areas that have entered in (recruitment and personnel selection services, information systems, computer systems and applications, quality control, etc.)[26]. Now the time seems to be ripe for the legal services market.

The success of audit firms in providing non-audit services has been remarkable. The time has come in which non-audit revenues exceed audit revenues (see Table 1)[27]. However, this expansion of the non-audit services (also called *Management Advisory Services* or MAS) has been put into question, as it is thought it may impair the auditor's objectivity[28].

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and SÁNCHEZ SEGURA (1999, 43-46), GARCÍA BENAU et al (1998, 106-108, 117-120, 174); Germany, see ROGOWSKI (1994, 16-17). Generally, see NARASIMHAN and CHUNG (1998, 207-213).

See also data provided in «Bruselas detecta rasgos de concentración en el mercado», *Expansión*, March 25, 1999, 60, which refers to the information collected by the UE Commission in order to approve the merger by *PriceWaterhouse* and *Coopers & Lybrand*.

[24] See CBA (1999c, 33-36).

[25] First they were the "Big Eight". Afterwards, they became the "Big Six", and following the merger of *Price Waterhouse* and *Coopers & Lybrand* they have become the "Big Five" (*Arthur Andersen, Deloitte Touche Tohmatsu, Ernst & Young, KPMG, PricewaterhouseCoopers*). For some annecdotic accounts of their activities, see STEVENS (1981, 1991).

[26] See GREER (1999, 2), NALLET (1999, 21-22). In England, see MUMFORD (1993, 187-189).

[27] See «Las firmas se vuelcan en consultoría y servicios legales», *Expansión*, 11 march 1999, 99. In general, see also CBA (1999c, 14-17), SOARES (1988, 1514); NOYELLE and DUTKA (1988, 92-115). In 1983 between the 20% and the 40% of the annual gross income of the (at that time) "Big Six" came from tax and management advice services. In 1995 these percentages grew (for the U.S. market) up to around the 60% (see *Accountancy*, feb. 1996, 8-9). In France, see NALLET (1999, 24). In Spain audit firms' income from non-audit services rendered is a 48% of their overall income (data from 1990 to 1996), see ARRUÑADA (1997, 106).

For the particular case of the audit firms' revenues from legal services in Spain, see «Gay afirma que las ganancias del negocio jurídico de las auditoras son un "escándalo"», *Cinco Días*, 4 june 1999, 32.

[28] For a thorough review, see POB (1979). See also, EU COMMISSION (1998, 7): *«Following the Recommendation of the European Parliament, the Comission will guarantee that it is studied with special attention if services different to auditing jeopardize or might jeorpardize the auditor's independence.»* See EU PARLIAMENT (1998, sections 6 and 7).

TABLE I. «BIG FIVE» REVENUES IN SPAIN

	REVENUES YEAR			
FIRMS	**1999**	**1998**	**1997**	**1996**
PriceWaterhouseCoopers	241’61	187'52	-	-
Auditing	80’54	71'52	-	-
Legal and Tax advice	43´30	31'25	-	-
Consulting	113’01	78'73	-	-
Corporate Finance	4’76	6'01	-	-
Arthur Andersen	266’62	229'12 [29]		
Auditing	118’13	61'05		
(Garrigues & Andersen)	97’96	81'2		
Ernst & Young	104’77	84'91	69'06	22'95
Auditing	48’58	41'41	37'21	11'27
Consulting	30’86	23'90	14'96	57'77
Legal and Tax	25’33	19'90	16'89	17'83
KPMG	72’12	62'04	46'88	32'35
Auditing	46’97	41'57	-	-
Legal and Tax	15’04	13'03	-	-
Consulting/Corp. Fin.	10’11	7'45	-	-
Deloitte & Touche	42’44	31'19	24'15	29'14
Auditing	19’64	17'95	15'96	12'47
Consulting	14’37	6'46	2'67	142'12
Tax/Legal services	8’44	6'79	5'53	48'20

Source: E*xpansión*, March 11 1999, 60 and *Expansión*, March 9 2000, 61 (data are in million).

The debate in Spain about the rendering of non-audit services by audit firms has focused on the legal regime of auditors and, specifically, on how it affected the observance of the auditors' duty of independence[30].

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[29] The revenues of *Garrigues & Andersen* are included though formally this is an independent firm within Andersen wordlwide.

[30] In Spain the press and the academic accounts analyze the issue from the audit firms perspective: audit firms are the ones trying to enter the legal services market. Interestingly, DEZALAY (1991, 792) characterizes this as the European pattern of the debate, while in the U.S. the topic is mainly approached from the law firms perspective: associations and mergers between law firms and audit firms also give the possibility to the former of satisfying the auditing needs of their clients. Historical reasons explain why the high status of the law firms (and,

Following article 24 of the Directive 84/253, the *Auditing Act* asserts in its article 8 the general principle of auditor's independence[31]. Afterwards, articles 36 to 41 of the *Auditing Regulation*, established a detailed regime of incompatibilities for the certification of company's accounts and the maximum and minimum appointment periods for the statutory auditors[32]. The general principle of independence, which is followed by a regulation of the concrete situations in which an incompatibility is considered to exist, reads:

> «**1.** Auditors must be independent in the performance of their task from the audited firms or entities.
> **2.** Independence is understood as the lack of interests or influences that may jeopardize the auditor's objectivity
> **3.** To appraise the lack of independence, among other circumstances, the performance of other works that might impair the auditor's impartiality will be taken into account. In any case, it will be considered that independence is lacking where the auditor had performed -during the three years prior to the one to which the audit is referred- other works regarding the material execution of the firm's or entity's accountancy.»[33]

The auditor's duty of independence appears as the guardian of objectivity and impartiality in the examination and certification of the financial statements of his client. The auditor's report is a key to the investors' confidence in the financial markets and to the reliability of the individual company's financial statements for the investors[34].

Leaving apart those situations in which the law expressly establishes that there is an incompatibility and, thus, no discussion may arise, it is generally understood that the fulfilment by the auditor of the duty of independence requires *independence in fact* and *independence in appearance*[35]. The former (*in fact*) is understood as the

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generally, of the legal profession) has only survived in the U.S., but not in Europe (see *id.* 800, 803-804). See also DEZALAY (1992, 189-193), OSIEL (1989, 2050-2053).

[31] For an interesting study of the origin, drafting process and frustrating armonization efforts of the independence rules in the Eigth Directive, see EVANS and NOBES (1998). See also MacGREGOR and VILLIERS (1998, 219). The keys of the Spanish implementation of the Directive are described in BOUGEN and VAZQUEZ (1997).

[32] Generally, see ARANA GONDRA (1995, 313-344), GARCÍA TUÑÓN (1992, 267 and 269-272), NUÑEZ LOZANO (1989, 111-113), PETIT LAVALL (1994, 229-234).

[33] Art. 36 of the *Auditing Regulation*. The first clause of Art. 36 reproduces Art. 8.1 of the *Auditing Act*. The infringement of the duty of independence constitutes a serious offence which is severily punished by the *Auditing Act* (articles 16.2.d) and 17) with fines up to 10% of the income earned by the firm from auditing the year prior to the imposition of the fine or with cancellation of its registration in the ROAC.

[34] This stresses the public interest of the auditor's function. See AICPA (1998, ET section 53, article II); *United States v. Arthur Young & Co.* 465 U.S. 805, 817-818 (1984) and -in Spain- Sentencia del Tribunal Constitucional 386/1993 of 23 december 1993, fdo. jº 3º, in *Repertorio Aranzadi del Tribunal Constitucional 1993*, tomo III, 1185].

[35] See AICPA (1988, ET Section 55, article IV.03), ANDREI (1991, 1082-1083), EU COMMISSION (1996b, 4.8), F.E.E. (1995, 1.2), MARCOS (1997, 183-187), POB (1979, 27), SANTARONI (1982), SOARES

auditor's honesty and his unbiased state of mind. It can only be achieved through the observance and imposition of an ethics code. It rests on the respect of deontological standards and rules that have been established by the profession, and which, if observed, tend to guarantee the auditor's integrity and impartiality, preventing any conflict of interest of the auditor. The latter (*in appearance*), however, depends on the view that clients or interested third parties have of the auditor's position with regard to an individual client. The fulfillment of the condition of independence in appearance requires the auditor (or the audit firm) to avoid the participation in any relationship in which it *might be* reasonably considered that the auditor (or the audit firm) is not independent.

After the enactment of the *Auditing Act*, the discussion about the auditor's independence first pointed to the mandatory rotation system[36], which was repealed in 1995[37], following a strong and consistent criticism by most of the academics[38]. Next, the issue of the rendering of some particular non-audit services by audit firms has easily come to discussion as an obvious risk of conflict of interest due to lack of independence -if appropriate precautions are not adopted[39]. Although some non-audit services are undoubtedly incompatible with auditing (for example, bookkeeping or preparing the financial statements that have to be certified)[40], there are others in which the incompatibility may or may not exist. Consulting, tax and legal services are included among the latter, as there is not a plain and clear-cut rule regarding their compatibility with audit services[41]. In Spain the ICAC

(1988, 1320-1321). The question of determining the criteria of auditor independence and enforcing them is not an easy one [see, for example, ELLIOT and JACOBSON (1992 and 1998)], there is even research pointing at the auditor's psychological impossibility of achieving true independence due to the existence of a *«self-serving bias»* [see BAZERMAN et al. (1997, 91 and 93).

[36] Originally, the system required that statutory auditors were appointed for a minimum of three years and for a maximum of nine years, prohibiting the renewal after the maximum appointment period was achieved. See ILLESCAS ORTIZ (1993, 49).

[37] By the *Limited Liabilities Companies Act* (Ley 2/1995, of 23 March, BOE nº 71, 24.03.95), Disposición Adicional Segunda (18ª) y Sexta.

[38] See IGLESIAS PRADA (1994,11-33), ARRUÑADA and PAZ-ARES (1997), ARRUÑADA and PAZ-ARES (1994).
On the contrary, see VICENT CHULIÁ (1995, 265-266; 1999, 373), VICENT CHULIÁ (1997, 27 ftn.45), PETIT LAVALL (1995, 6903-6911).

[39] See SUBCOMMITTEE ON REPORTS, ACCOUNTING, AND MANAGEMENT (1976, 51-54), COHEN COMMISSION (1978, 93-104), POB (1978).

[40] See AICPA (1988, ET section 101-3, ET-int 101.05); SEC, *Financial Reporting Release* nº 1 (april 15, 1982), §602.02.c.i.

[41] In Spain, none of the authors agree on this point [for a survey see BELLO PERIBAÑEZ (1997, 66-69); CAÑIBANO CALVO and CASTRILLO LARA (1999, 34-36)]. A majority of them consider that the auditor should be banned from rendering other professional services. See GARCIA BENAU and VICO MARTINEZ (1997, 65), PETIT LAVALL (1996), VICENT CHULIÁ (1997,27 ftn.45 and 46). Others, remarkably professor Benito Arruñada, hold that the rendering of additional services by the auditor does not

has expressly ruled, initially, that there is no incompatibility with tax and legal services[42].

However, the question is more complex than the frugality of the ICAC ruling may lead us to think. Everything depends on the kind and nature of the non-audit services provided by the audit firm. Some consulting or management advisory services give reasons for thinking that the auditor may end reviewing his own firm's work or that the auditor may be too involved with the client's affairs and, thus, biased (in favour of the client) in the preparation of his report[43].

The academic discussion on this issue stresses the advantages coming from the rendering of non-audit services by audit firms. Economies of joint production (scope and specialisation), knowledge spillovers and contractual economies appear among the undeniable benefits of the joint rendering of audit and non-audit services by the same firm[44]. On the other hand, the risk of conflict of interest, partiality and lack of independence weigh in favour of somehow restricting that possibility.

Different restrictive solutions have been proposed[45]. These include an absolutely prohibition on audit firms from rendering any kind of non-audit services, to prohibiting the rendering of non-audit services to audit clients[46], or a disclosure policy of the revenues obtained from different activities[47].

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necessarily imply a lack of independence by the auditor. See ARRUÑADA (1999b, 81-98; 1998b; 1998a; 1997, 111-132).

[42] In 1991 the ICAC asserted that "tax advice" was compatible with auditing in the *Norma Técnica de Auditoría* (N.T.A.) 1.3.6 (approved by Resolution of the President of ICAC of 19 january 1991, BOICAC nº 4, January 1991). The so-called *"Normas Técnicas de Auditoría"* (hereinafter N.T.A.) constitute a body of rules and standards adopted by the President of the ICAC, that govern the auditor's legal regime (duties and liabilities) and the auditing procedure.

A ruling of the ICAC in 1991 also established, although did not reason why, that audit firms' legal or/and tax advice to audit clients was admissible (see Consulta nº 5, BOICAC nº 5, may 1991, 102-103). Recently the same conclusion was affirmed in another case by a civil court judgement, see «Los tribunales defienden la compatibilidad de los servicios de asesoría fiscal y de auditoría», *Expansión*, 2 March 2000, 61. These holdings have been strongly criticized by some authors, arguing the conflict of interest is obvious, see GARCÍA TUÑON (1992, 270-272) and PETIT LAVALL (1994, 231-232). For the begining of a more thoughtful analysis, see ARANA GONDRA (1995, 328-330).

[43] See ICAEW (1996, 4.55-4.64 and 4.67-4.78).

[44] See ANTLE et al. (1997, 17-18), ARRUÑADA (1999b; 1997, 95-104), POB (1979, 17-21).

[45] In general, see HILLISON and KENNELLEY (1988, 37-39), also surveyed by ARRUÑADA (1999b, 140-143).

[46] See BRILOFF (1984, 508-509), SUBCOMMITTEE ON REPORTS, ACCOUNTING AND MANAGEMENT (1976, Recommendation 8), SOARES (1988, 1550-1553).

[47] See SUBCOMMITTEE ON REPORTS, ACCOUNTING AND MANAGEMENT (1976, Recommendation 9). This would be the disclosure made by audit firms to their professional organizations or monitoring organs [see POB (1979, 42-43)]. Besides, the client companies should reveal in the annual report accompanying their financial statements, the amounts paid -in all headings- to its audit firm, otherwise the auditor could disclose that information in his/her report.

The two alternative prohibitions seems to go to far. Potential conflicts of interest might perfectly, and more efficiently, be prevented by the auditor's personal integrity and honesty, by the firm's specific policies, by the audit profession and by the legal system[48]. All these factors, coupled with a disclosure rule[49], should lead the auditor (and his firm) to avoid any potential conflict of interest.

Generally, at least within the large audit firms, the auditor's reputation (goodwill) provides a general safeguard against the excessive dependence of one of its clients[50]. Indeed, an audit firm can adopt internal rules and policies in order to preserve the (highly valued) independence. This can be coupled with the introduction by the accounting profession of additional ethic rules dealing with the provision of non-audit services[51], with educational programs and quality controls (peer reviews), and with the enforcement and disciplining of violations of the profession's deontological code. Finally, the system of auditor's liability should be designed in such a way that encourages independent and unbiased professional behaviour[52].

However, a more general problem remains unsolved. If the revenues the auditor or the audit firm receives from an individual client for the rendering of (any kind) professional services are *excessive,* it could be that the

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This approach was adopted by the SEC in the *Accounting Series Release nº 250* (42 Fed. Reg. 29,110), approved on 29 june 1978 (*Disclosure of Relationships with Independent Public Accountants*), requirig the disclosure (in the audited company's statement) of the fees paid for non-audit services to the audit firm in case they exceed in more than 3% the audit fees. See LOSS and SELIGMAN (1989, 738-739), POB (1978, 40-41), RECKERS and STAGLIANO (1980). For the effects of these disclosures, see SCHEINER (1984). On 28 january 1982 the SEC abroged ASR nº 250 (through ASR nº 304, codified in *Financial Reporting Release nº 1*, §604, 7 Fed. Sec. L. Rep. [CCH] ¶¶ 73,295 to 73,301, pages 62,921 to 62,925).
See also §11-12, 2 section i.f. of norwegian *Aksjeselskapsloven* (of june 4, 1976, as amended in 1997) nº 59 and §7-31, 1 section i.f of norwegian *Regnskapsloven* (of may 13, 1977, as amended in 1998); section 283 of the *South African Companies Act 69 of 1991*; CADBURY COMMISSION (1992, 5.10, 5.11, and Summary of Recommendations 8); EU COMMISSION (1996a, 80-81; 1996b, 4.13); section 390B of *English Companies Act of 1985* and S.I. (1991) nº 2128. For an empirical study of the possitive effects of the English disclosure see LENNOX (1998). In Spain, a similar policy has been suggested, for example, by Pablo Picazo, «Los grandes retos de la auditoría», *Expansión*, 15 march 1997, 39.

48 Some of the possible options -for the firms and for the profession- are suggested in ARRUÑADA (1999b, 99-108; 1997, 132-140).

49 See ARRUÑADA (1999c, 522-527; 1999b, 154-155; 1997, 201-202) for a possible formulation of such a rule (ratio of total fees from single client and total fee income).

50 See EASTERBROOK and FISCHEL (1984, 675; 1991, 282), F.E.E. (1995, 3.3.2), FISCHEL (1987,1052). The auditors' reputational interest is larger than the profits from slisphod or false certification of financial statements.

51 See, for example, *Organizational Structure and Function of the SEC practice section of the AICPA Division for CPA firms*, §IV.3(i) (1978).

52 For example, in the U.S. the rendering of non-audit services might be considered an additional element in the liability judgment against the auditor, see «CPAs who perform management consulting services may face increased exposure to controlling person: Liability under the federal securities law», *Washington and Lee Law Review* 44 (1987), 1079-1102.

auditor becomes too dependent on this client, impairing its independence to certify its financial statements. This specific situation is expressly acknowledged, though in general terms, by the *Norma Técnica de Auditoría* (N.T.A.) 1.3.8[53]:

> «It should be specially taken care of the independence when the fees received in all headings from a client represent a substantial fraction of the gross overall income of the auditor or of the audit firm. For this purpose, it will be considered as an individual client the group of firms or entities that are connected by a control relationship -direct or indirect-, similar to the one provided in article 42.1 of the Commerce Code for corporate groups or when the firms are controlled, directly or indirectly, by the same entity or individual person.»

Preventing a breach of the rule of independence due to excessive financial dependence on a client might be approached through a diversification rule[54]. This rule would prohibit the concentration of a large fraction of the revenues of the firm within an individual client[55]. It seems appropriate to introduce some flexibility in the rule with regards to starting audit firms (for example, using a multi-year period in the calculation of the income obtained from the same client). The rule should be adjusted according to the overall revenue of the firm, the limit threshold should be variable, lower for larger firms[56].

In fact, the Code on the governance of listed corporations (so-called *Olivencia Code*), approved in 1998 by the Special Commission for the Study of an Ethics Code for Corporation's Boards of Directors, when analising the Board of Directors' relationship with the auditors, deals with the auditor's independence in this manner,

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53 See GUYON (1977, §9). The rule is similar in France, where article 46 of the *Code des devoirs et intérêts professionels* (adopted by *Délibération du Conseil National des Commissaires aux Comptes* of 21 october 1976) vaguely requires the auditor to avoid that income from a company or group of companies represent a substantial portion of its overall income so that it might affect its independence. See also IFA (1998, section 8.7), SASSO (1999, 235).

54 On the contrary, see ARRUÑADA (1999c, 522-524; 1999b, 147-148; 1997, 196-197).

55 A rule of this kind was included in article 11(3) of the original proposal of Eight Directive on EEC Company Law (Official Journal C 112, of 13.05.78, 6-10), see EVANS and NOBES (1998, 499).
For the first formulation of this proposal in the Spanish academic literature, see PAZ-ARES (1996, 76-79); see also, CAÑIBANO CALVO and CASTRILLO LARA (1999, 33). A recent proposal in the same direction has been made by some professional organizations («Los economistas auditores piden crear un baremo de facturación para garantizar la independencia», *Cinco Días*, 5 jul. 1999, 29).

56 So that, for example, a 5% income received from the same client could be considered excesive for a «Big five» firm but not for a small or medium size firm, see PAZ-ARES (1996, 79, ftn. 13).
In other systems, more experienced with this sort of diversification rules, the discussion focuses on determining the limit threshold [see, for example, APB (1992, §4.8), CNCC/COB (1997, A.2.1.5), EU COMMISSION (1995, 4.3; 1996a, 76-77), F.E.E. (1988, V.3), ICAEW (1996, 4.1-4.9), HAMPEL COMMISSION (1998, 6.8)]. For a survey see ARRUÑADA (1999b, 145-147). In Germany §319.II(80) of the *Handelsgesetzbuch* fixed a 50% threshold, which is too high to effectively work as a diversification rule, see HERZIG and WATRIN (1995, 799-800). In 1998 the so-called *KonTRaG* (*Gesetz zur Krontrolle und Transparenz im Unternehmensbereich*, gesetz von 06.03.98, BGBI, I 1998, 786) changed the maximum fee income to 30%.

recommending[57]:

> «The Board of Directors and the Audit Committee monitor situations which might jeopardize the independence of the company's external auditors and, specifically, they should check the percentage of the audit firm's total revenues represented by the fees paid to it under all headings, and professional services other than auditing should be publicly disclosed.»[58]

Afterwards, the «Board of Directors' Model Regulation», prepared by the Comisión Nacional del Mercado de Valores (CNMV) in accordance with the *Olivencia Code* deals with the relationships with auditors in section 44. The relevant portions of this section read:

> «2. The Board of Directors will refrain from hiring those audit firms in which the fees that it foresees to pay, under all headings, are more than 5% of its income during the last year.
> 3. The Board of Directors will publicly disclose the overall fees that the corporation has paid to the audit firm for services other than auditing.»

The *Olivencia Code* and the CNMV's Model Regulation are not mandatorily imposed, but only recommended to the publicly listed companies, it is still soon to evaluate the acceptance they have received[59]. Although some criticisms have already been asserted with regards to the treatment of these issues on the report[60], more than anecdotal evidence indicates that most of the large quoted corporations are somehow adapting their internal regulations to the report[61].

4. THE LEGAL PROFESSION AND THE LEGAL MARKET IN SPAIN.

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[57] See OLIVENCIA COMMISSION (1998, II.11.2). The wording of this section, and of the subsequent recommendations, have a clear inspiration in PAZ-ARES (1996, 76-79). It should be added that professor Cándido Paz-Ares was one of the members of the Special Commission.

[58] OLIVENCIA COMMISSION (1999, Recomendation 21).

[59] Although it has been critized for following a "recommendation approach" instead of mandatorily enacting dispositions that listed companies must obey, it should be noted that the CNMV has *strongly encouraged*, directly or indirectly, Spanish listed corporations to follow the recommendations contained in the Olivencia Code (see *Carta Circular 11/1999, of 17 december 1998, on public disclosure about the compliance with the Code of Corporate Governance*).

[60] See SANZ PARAISO (1999, 404-405), criticizes the diversification rule of the Commission's Code, proposing the re-introduction of a mandatory rotation rule and suggesting a general prohibition of the rendering of non-audit services by audit firms. Contrary to what he says, none of these measures were supported by the Cadbury Report, indeed, quite the opposite happened, as it clearly and expressly rejected both. See CADBURY COMMISSION (1992) in 5.10 and 5.11- for the rejection of the prohibition of the rendering of non-audit services by audit firms-, and 5.12, for the rejection of the mandatory rotation.

[61] In http://www.cnmv.es/delfos/ (visited on 01.07.2000) it is possible to read the company's reports (not only those publicly held or quoted) on the implementation and compliance with the *Olivencia Code*. See also CNMV, *Annual Report 1998*, 41. However, apparently everything points at a low level of compliance with the Code's disclosure rules, see «El ´Código Olivencia´ha tenido un escaso impacto en la transparencia empresarial», *Expansión*, 11 March 2000, 69.

In order to be able to act as a lawyer, Spanish Law requires him/her to be licensed as such by any of the regional bar associations (*Colegios de Abogados*)[62]. Of course, attorneys can join themselves to practice law within a law firm[63]. At the national level it exists the Spanish Bar Association (*Consejo General de la Abogacía Española* or CGAE), which represents and coordinates the activities of all the local associations.

Traditionally the spanish legal market has been pervaded by solo-practitioners or classic law firms of middle size (around ten lawyers). The situation seems to have radically changed in the nineties when a wave of mergers and acquisitions increased the medium size of spanish law firms[64].

A handful of local traditional firms in Madrid and Barcelona have grown among the largest law firms in Spain (namely *Uría & Menéndez, J. & A. Garrigues, Cuatrecasas, Goméz Acebo & Pombo*). As noted before, these firms have found in the last few years increasing competition among themselves and with other foreign firms that have established their branches in Spain. However, the main challenge to the large Spanish law firms comes from the entrance of audit firms in the legal services market[65].

5. THE RENDERING OF LEGAL SERVICES BY AUDIT FIRMS: MULTIDISCIPLINARY PARTNERSHIPS.

Complex economic and business transactions are not purely legal and it would be difficult to find a transaction in which only law and regulation were involved. The overlapping of different professional disciplines has become clearer. The legal aspects are not necessarily the most important (although it is understandable lawyers may tend to consider them so). The multidisciplinary aspects involved in any business transaction have grown in the modern times; environmental, political, psychological and social issues need to be analysed and conveniently taken into account[66]. This has lead to many multidisciplinary jobs, requiring collaboration from

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[62] Art. 436 of Ley Orgánica 6/1985, of 1 july 1985, del Poder Judicial (BOE nº 157, 264, of 2.07.85 and 04.11.85); Arts. 10.1 and 15 of *Estatuto General de la Abogacía Española* [adopted by *Real Decreto 2090/1982*, of 24 July (BOE nº 210, of 02.09.82) hereinafter EGAE]. Apart from a Law Degree (*«Licenciatura en Derecho»*), the other main requirement is the payment of the admission fees to the local bar association. See SANS ROIG (1995, 125).

[63] art. 34 EGAE. Although, it has always remained unsettled which legal form the firm could adopt. The form more commonly used is the partnership (*sociedad colectiva* or *sociedad civil*) and the private limited liability companies.

[64] See supra notes 2 and 3 and Jordi Amado and Glòria Moles, «Un sector en ebullición», *Expansión*, 5 march 1999, 67. But see Lupicinio Rodríguez, «Megabogacía», *Expansión*, 13 dec. 1999, 62-63, for a strong plea in defence of middle size law firms.

[65] For an overall view of this situation, see MARTI BALDELLOU and HARILLO (1993, 117-118).

[66] See ANDREWS (1989, 623).

different professionals.

Although this may lead only to different unrelated professional firms working together, no one disputes that it would be easier to provide all the services within the same firm. Disparate services would be rendered in only «one-stop shop»: more convenient for the client and also for the different professionals[67]. The benefits for clients stick out a mile, as they save the costs of acquiring information about other firms or contracting with them. The arrangement is also profitable for the professionals, who, apart from obtaining most of the same savings as the clients, are able to easily and efficiently monitor the quality of the different specialised professional services provided[68].

Audit firms competitive advantage as business advisers and their worldwide network of offices places them in an excellent position in their quick entrance in the legal services market[69].

Tax advice and tax law.

As in many other countries, in Spain, tax services have been the scenario where the competition among law firms and audit firms first began[70]. In tax law the interplay between law and finance appears with particular clarity[71]. In contrast to the licensing requirements to practice law or to work as a statutory auditor, in Spain tax advisers are not licensed as such or required to fulfill any specific condition. Anyone with a substantial up-to-date knowledge of the tax rules and procedures may work as a tax adviser. However, in case of controversial tax law issues that are brought to the courts, if the tax advisor wants to act and argue his case before the court

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67 A similar phenomenon of integration or joint-rendering of separate and different banking services can be ascertained, but even there the issue is far from settled, see DREXHAGE (1998) and FEATHERSTONE (1997).

68 See GILSON (1990, 893-896), HADFIELD (2000, 22-27). Particularly, given the nature of legal and auditing services -in which there is an information barrier about the quality of the services provided- these professionals have a very strong incentive to provide an overall good quality. That is why the MDP is preferred if compared with a mere "referral system".

69 See QUINN (1997, 160-161). This international component of auditing firms implies auditing firms are able to give coordinated advice in many locations about many legal systems, dealing also with non-legal issues. Their competitive advantage is clear. See Juan Luis Marchini Bravo, «Globalización, regulación, auditores y abogados», *Expansión*, 3 march 1999, 66.

70 In general see EBURNE (1991). For the competition in the area of international taxation, see NYSBA (1999, 31-32) and PICCIOTTO (1993, 40-43). For Germany, see ROGOWSKI (1994, 26) and for the United Kingdom see DEZALAY (1991, 795) and FLOOD (1989, 582). This constitutes one of the areas in which the interplay between lawyers and accountants first occurred, see SUGARMAN (1995, 233).

71 Not only in tax law, but also in takeovers, mergers and acquisitions (M & A). Investment bankers also play a relevant role in this area. See DEZALAY (1995; 1992, 194-196), and in Spain, «Auditoras y bufetes restan mercado a los bancos de inversión en el negocio de fusiones y adquisiciones», *Expansión*, 30 sept. 1999, 69.

he is required to be a licensed attorney.

The coverage of this new sector by audit firms was fast and effective; it proved to be an excellent complement to their audit services. Indeed, the paradox has been that no real competition has been opposed by lawyers. Audit firms easily won that battle. Most of the tax law work in Spain is done by legal departments or legal affiliates of audit firms[72].

However, tax law opened the doors of the legal services market to the audit firms. They did not think twice and most of them extended quickly their services all over the legal field, establishing full-fledged legal departments or affiliating with "independent" law firms[73]. They started rendering services not only in relation to (or to) audit clients, but in open competition with Spanish law firms (see Table II)

[74]. Moreover, there has also been some audit firms that associated or merged with traditional law firms to improve their position in the Spanish legal services market[75]. In the last few years the audit firms' revenues for their legal services have grown substantially[76].

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72 See MARTI BALDELLOU and HARILLO (1993, 115-116) Although, recently law firms seems to be, somehow, retaking a portion of the market, EBURNE (1991,15).

73 See FLOOD (1995, 150, 156-157) -who graphycally characterizes accountants as "brokers between professionals"-, MORELLO (1997, 198-203), STOAKES (1986). Although currently most of the large audit firms that render consulting and legal services have placed different activities within separate firms, this has been done to comply with distinct national regulatory requirements or to keep-up appearances, as the (theoretically) independent professional firms remain strongly connected, belonging to the same group of firms. That is one of the few reasonable points raised by COLEGIO DE ABOGADOS DE BARCELONA (1996, 26). In France, see MIKOL and STANDISH (1998, 547).

74 In Spain all the «Big five» have legal departments or associated law firms. In fact, in 1996 the legal arms of five of the (then six) biggest accounting firms ranked among the top ten law firms in the country by revenue, see FERGUSON (1997, 39). In 1997, the medium profile of the Spanish audit firms (bear in mind that the data are heavily influenced by the dominance of the «Big Five») was 45'6% audit services, 27'8% consulting, and 22% legal services (see *Expansión*, 15 Jan. 1999, 52).

75 The paradigmatic (and pioneering) merger being between *Arthur Andersen ALT* and *J&A Garrigues* in January 1996 [see «Spanish merger marks watershed», *International Financial Law Review*, 15 (Oct. 1996) 3-4; «Andersen/Garrigues merger is completed», *International Financial Law Review*, 16 (March 1997) 3-4]. In 1998 Pricewaterhousecoopers *JF* also merged with *Estudio Legal*, the Madrid branch and the intellectual and industrial property division of *Mullerat & Roca*, thereby becoming the second largest law firm in Spain (see «PricewaterhouseCoopers cierra su unión con el despacho Estudio Legal y la fracción madrileña de Mullerat & Roca», *Expansión*, 29 dec. 1998, 53; *Economist & Jurist*, 35, Jan./Feb. 1999, 96).

76 For the «Big Five» see supra Table I. Data for middle and smaller size audit firms in 1998 are provided in «Las firmas se vuelcan en consultoría y servicios legales», *Expansión*, 11 March 1999, 60 (overall, the growth was larger for consulting -22'6%-, followed by tax & legal services -17'19%-; revenues for audit services only increased 11'06%).

TABLE II. LAW FIRMS REVENUES IN SPAIN

Law firms	*1999*	*1998*	*1997*
1. Garrigues & Andersen	98	78'7	62
2. Cuatrecasas	63’1	45'1	34'9
3. Uría & Menéndez	45	32'9	27'5
4. PWCo Jurídico y Fiscal/ *Landwell*	43’3	31,3	-[77]
5. Ernst & Young D. Jur. Trib.	28’5	22'3	18'4
6. Elzalburu	27’4	25’1	-
7. Gomez Acebo & Pombo	23’7	21'5	19'1
8. Clifford Chance	21	15	11'1
9. KPMG Abogados	16’4	14'6	10'2
10. P. & A. Cons. Jur. Trib.	18’5	10'2	6'2
11. Hispajuris	14’8	11'2	9'7
12. Bufete Barrilero	12’1	9'6	8
13. Iusfinder	11’7	10’4	11'7
14. Baker & Mckenzie	10’4	8'2	9'8
15. Alzaga, Caro, Marañon, Sánchez Terán Asoc.	10’2	9	8'1

Source: ***Expansión*, April 23 1999, 59 and *Expansión*, April 14 2000, 68 (data are in million).**

Most Spanish law firms were not happy at the arrival of the newcomers. The representatives of the legal profession have assumed also this position, considering that the rendering of legal services by audit firms would compromise the lawyer's independence and integrity[78], giving rise to a potential conflict of interest.

It should be noted that there is a substantial difference between the lawyer's duty of independence and the auditor's duty of independence[79]. In fact, it could be said the requirement of the lawyer's independence is somehow *rethorical*, as the lawyer is required to act in the best interest of his client in compliance with the Law[80]. Therefore, the lawyer needs to become involved in the affairs of his client, working on his defence within the borders legal system. However, acting on behalf and in defense of his client, the lawyer should devote himself solely and exclusively to the client's interest, avoiding any interferences or potential conflicts with

[77] In 1997 the revenues of the firms that merged in *Estudio Legal* were the following (in million): PW JF- 16'92; *Coopers & Lybrand*- 11'87, *Estudio Legal*- 6'6. There are no data available about the revenues of the fraction of *Mullerat & Roca* that joined *Estudio Legal*. In 1999 PWCo (currently *Landwell*) increased its revenues 38% up to 43'4 million euro (see «Landwell aumentó su facturación un 38% al integrar Estudio Legal», *Cinco Días*, 11 feb. 2000, 24; «Landwell aumenta sus ingresos en un 40%», *Expansión*, 11 feb. 2000, 67).

[78] See CGAE (1999b) and CBBE (1999).

[79] See, extensively, NALLET (1999, 106-107), NYSBA (1990, 12-14).

[80] The issue is a complex one, as the lawyer is also believed to develop a substantial communitarian dimmension or public task at the same time he/she zealously serves the interest of its individual client. For one thorough exposition of the lawyers' essential qualities and skills, see KRONMAN (1993, 123, 128-134, specially 144-153). See also OSIEL (1989, 2013-2022).

other personal interests or with his firm's interests[81].

Thus, the legal profession regulations require, following article 42 of the *Estatuto General de la Abogacía Española* (EGAE) that the attorney:

> «in the fulfillment of his/her task, will act with absolute freedom and independence, without other limitations that those imposed by the Law, by moral and ethical rules».

The ethical rules stress the lawyer's duty of independence and loyalty in the performance of his services:

> «**1.1.** Under the rule of law, the intellectual and moral independence of the lawyer is an essential condition for the practice of his/her profession, as it is for the courts. Lawyer's independence, that should permanently be preserved, is the guarantee that the client's interests will be defended with objectivity.»
> «**6.4.** The lawyer has the obligation to fully inform his client of all those situations that may affect his independence, like family, friendship, economic or financial relationships with the contrary party or his agents.»[82]

The International Bar Association's *International Ethics Code* also stresses the lawyer's duty of independence:

> «Lawyers will preserve independence.
> Lawyers practising on their own account, or in partnership where permissible, shall not engage in any other business or occupation if by doing so they may cease to be independent.»[83]

In the last meeting of the CGAE, the law profession dealt expressly (and strongly) with this issue in one of its reports («La abogacía española en la Unión Europea»)[84]. The relevant portions read as follows:

> «**Fifth.** The legal scheme of incompatibilities requires further clarification, in a rule with appropriate legal force, to avoid competition disloyalties, situations of captive clientele or offers that cause confusion to the clients and risks for the duty of confidentiality, for the independence and for the prohibition of conflict of interests.»
> «**Sixth.** Appropriate actions should be taken against the mercantile companies, incorporated by persons outside of the law profession whose main aim or market is the rendering of legal services...»

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[81] This profile of the lawyer's duty of independence is emphasized in CCBE (1988, §§2.1.1. and 2.7), which was adopted by the CGAE on 22 September 1989 (and, thus, applicable to Spanish lawyers). See also, ABA (1995, Rule 1.7; 1983, Cannon 5), CCBE (1999, 1).

[82] Extracted from *Código Deontológico de la Abogacía Española*, approved by the meeting of local associations' presidents («asamblea de decanos») on the 28th and 29th, may 1987.

[83] IBA (1998, rule 3).

[84] The meeting was held in Sevilla, on 10-13 march 1999. The full text of the meeting can be read in CGAE (1999b). The fragment in the text is taken from *Otrosi* (Information Bulletin of the Madrid Bar Association), April 1999, 14-15.

Theoretically, the reasons for the rejection of audit firms rendering legal services are that this may entail the risk of unauthorised practice of law and that it might compromise their duty of independence and integrity as lawyers. The argument is that both professions cannot be practised by the same firm (or by affiliated firms) without compromising their corresponding legal and ethical duties.

Audit firms rendering legal services: Benefits and Costs.

Contrary to other legal systems[85], Spanish law does not expressly prohibit neither regulate the rendering of legal services by audit firms[86]. The issue is discussed under the heading of the so called *"multidisciplinary partnerships"* or MDPs.

Under what circumstances can a firm supply integrated legal and accounting services to their clients?, what kind of arrangements could cover this service supply?, can lawyers and other professionals share fees?, can they form a partnership together?.

The answers to some of these questions are not clear. Despite of the concerns of the legal profession, some of these issues remain unregulated. However, there are others which have expressly been dealt with by Spanish law. Sharing fees by lawyers and other professionals is forbidden[87], but lawyers are not prevented from the formation of a partnership with other professionals[88]. Current law provides a wide leeway for the collaboration or joint-work by lawyers and other professionals, even within the same partnership or firm.

For a long time the «Big five» have profited from this situation, and have been rendering legal services. Some

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[85] For an overall view of the problem see ALONSO AYALA (1999), DE ANGULO (1989, 331-334), MULLERAT (1999, §IV).
In general, see EU COMMISSION (1996a, 74). The most restrictive regimes are the french, belgian and italian, but even in these countries the prohibitions can be slanted through the use of a separate entity. See SASSO (1999, 226) for Italy, and MIKOL and STANDISH (1998) for an analysis of the regulation in France and the United Kingdom (the former -due to article 220.4º of the Loi 1966, of 24 july- is more restrictive, but see supra note 70 *in fine*). See also CNB (1998, 1994).
In Germany, according to §3 of the *Rechtsanwaltsverordung*, audit firms can only render legal services on tax and corporate law if it is required for (or connected with) their auditing work. On the other hand, no harmonization is sought by the EU on this issue, see article 11.5 of Directive 98/5/EC, of 16 february 1998 (Official Journal L 77, of 14.03.99, 36). For the *status quaestionis* in the U.S., see ABA (1998).

[86] See MULLERAT (1999, §IV.3.A), although he clarifies this statment.

[87] The lawyers' prohibition of sharing fees with non-lawyers is established, *inter alia*, in CCBE (1988, §3.6.1). In the U.S., see ABA (1995, Rule 5.4.a; 1983, DR3 -102.A; 1969, Cannon 34), NYSBA (1999, 22-23), ROACH and IACOBUCCI (1998a, 32 and 49). In England, see *Solicitors' Practice Rules,* rule 7(1) (1990).

[88] Contrary to the situation in the U.S., see ABA (1995, Rule 5.4.b; 1983, DR 3-103; 1969, Cannon 33); NYSBA (1999, 24-29). But see GILBERT and LEMPERT (1988).

of these services are ancillary to the auditing and consulting services, thus, being provided as a part of an integrated and coordinated product[89]. But most of the legal services performed by the «Big five»'s legal departments, divisions or subsidiaries are offered as a separate and independent service.

As noted, this growth of the audit firms in the legal services domain has encountered strong opposition by the Spanish Law profession[90]. The arguments posed against audit firms providing legal services are several, ranging from the possible conflict of interest to the anti competitiveness of the audit firms entrance in the legal market[91]. Doubtless, there may be situations in which the joint rendering of different professional services might originate a conflict of interest or an incompatibility. In such cases, measures should be taken in order to prevent the conflict from appearing[92]. Firms may, by themselves, internally regulate the relationships among different departments (or firms within the same group)[93]; they may even classify certain transactions as too risky, requiring prior disclosure of the potential conflict and the client's express consent. In extreme situations the rendering of some of the services must be discontinued, but generally there are other risk minimizing devices that may work perfectly.

Perhaps the nature of the legal work or service rendered by the professional firm can provide a good hint on ascertaining potential conflicts of interest[94]. Technical issues, routine tasks or recurring legal services, normally without involving litigation, seem not to pose major risks of conflict of interest[95]. On the other hand, things may be different when the services are not recurring or are exceptional. In this situation, the probability of conflict

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[89] See MARCOS (2000). Arruñada largerly overestimates the complementarity of auditing and other services provided by audit firms, see ARRUÑADA (1999b, 72-74; 1997, 96-98). Although it may well be [see KLARSKOV and JEPPESEN (1998)] that in the current auditing framework the boundaries between auditing and other professional advisory services are blurred, but that is something different.

[90] Extensively, see DEZALAY (1992). See also Neil Rose, «MDP limits», *Law Society's Gazzette*, 94/42, nov. 1997, 1 and 4; «Pugna entre auditores y abogados», *Expansión*, 5 march 1999, 66.

[91] In general, see MORRISSEY (1988).

[92] There is a risk of conflict of interest or interference with the lawyer's professional independence, but the benefits to the public (in terms of social value and competition) outweigh the potential harm [see ABA (1999b, §II.4], as it happens with nonlawyer ownership or management of law firms, see ADAMS and MATHESON (1998), ANDREWS (1989), NIELSEN (1981), GILBERT and LEMPERT (1988, 410).

[93] This could be done by some explicit provisions in the contractual or partnership agreement, and these provisions would be independent of the observance and aplicability of the respective professional ethical rules. Indeed, it could perfectly be that in those issues more disputed (confidentiality, attorney-client privilege, ecc.) the content of such provisions is made compulsory, see BARREAU DU QUÉBEC (1999, 82-84, 88-89).

[94] See SIMMONS (1998b, 3). In their analysis of lawyers' advertising HAZARD Jr., PEARCE and STEMPEL (1983) draw a similar distintiction between "standardizable" services, that can be provided by a routinized production system, and "individualized" services, that require close personal attention from an attorney. Advertising will be very positive and beneficial in the former, without adding nothing in the latter.

[95] See FEE (1995, 4.2.2).

may increase, discouraging the rendering of the service by the MDP.

In any case, the conflict of interest issue should be dealt with by strong enforcement of the rules requiring the lawyer to serve the best interest of his client. Besides, a disclosure rule of the conditions and prices at which different services are provided would provide enough consumer protection, helping the professionals and their clients in a sound valuation of any potential problems arising from the joint rendering of different services[96].

It is also argued that the audit firms position as the auditors of their clients places them in a privileged position to "sell" other services[97]. Indeed the Lawyer's Ethics Code deals somehow with this issue, stating:

> «**6.12.** The Lawyer cannot unfairly take clients.
> Among the acts of unfair taking of clients are:
> **a)** to use direct or indirect publicity means, whether by self initiative or accepting offers from third persons.
> [....]
> **c)** to entrust third persons with obtaining clients, whether their work is remunerated or not.
> **d)** any acts analogous to the previous».

Therefore -so the reasoning goes- the audit firms would be capable of exercising a power to determine the client's demand of other professional services. The anti-competitive threat of this "*steering*" and *"feeding"* strategy in which the auditor may recommend clients to purchase additional services provided by his firm (including legal services) would be real, and measures would need to be adopted to prevent it[98].

However, this is nothing peculiar to the audit services or audit firms, as it may be observed in many professional relationships[99]. Lawyers could also do it[100]. In fact, it is something that comes from the character of professional services as "credence goods", provided by an expert who also determines the buyer needs[101].

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96 See Mario Alonso Ayala, «Abogados y auditores: ¿incompatibles?», *Expansión*, 24 feb. 1999, 62, who also proposes that the rendering of audit and legal services act as an aggravating circumstance in case of professional liability due to conflict of interest.

97 See COLEGIO DE ABOGADOS DE BARCELONA (1996, 26-27), LSEW (1987, 3.8.II.ii), NALLET (1999, 49), SUBCOMMITTEE ON REPORTS, ACCOUNTING AND MANAGEMENT (1977, 16).

98 The idea that the anticompetitive menace may come from the audit firm judging other lawyers work (see Emilio Cuatrecasas, «Lo que no se quiere entender», *Expansión*, 16 of march 1999, 62) is problematic as it assumes client stupidity.

99 Of course, the peculiarity in case of auditors is that they maintain a stronger position in that «feeding» strategy: they can exert greater pressure towards the client as they are required to certify the client's financial statements.

100 See CBA (1998a, 18-19); ROACH and IACOBUCCI (1998b, 26-27 and 31), who propose disclosure to the client of lawyer's financial interests in any ancillary business activities.

101 See HADFIELD (2000, 22-27).

In other words, when any professional has a large discretion in serving the client's interest and there is a substantial information asymmetry regarding the quality of the service provided (technical expertise)[102], it would be easy for the professional to advice the client about the necessity of buying additional services provided by his firm.

This risk could promptly be counteracted if a competitive market for the different professional services existed. If the customer is able to compare the price and quality of the service provided by different service suppliers it would be easy for him to avoid any possible *"feeding"*[103].

Apart from these risks, there are undeniable benefits coming from the gathering different professionals in the same firm and the joint rendering of diverse professional services[104]. As it was seen with regards to non-audit services, the synergies and economies (technological and contractual) coming from the joint-rendering of services by a firm to the same client may be substantial[105].

On certain occasions, the transfer of information between the diverse professionals working in the MDP may be barred by the respective confidentiality duties of auditors and lawyers[106] and, specially, by the attorney-client privilege[107]. Generally the establishment of adequate "screening devices" and control procedures within the firm may serve to prevent undesirable information flows between different professionals, but in certain situations they may not work, and (once those are identified) incompatibility should be legally imposed[108].

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102 For a similar characterization of the lawyer-client relationship, which however, may be extended to the auditor-client relationship, see BOWER (1982, 331 and 342), HAZARD Jr., KONIAK and CRAMTON (1994, 474-476), STHEPEN and LOVE (1999, §3). In general, see ARRUÑADA (1999a, 1-2).

103 See BOWER (1982, 342-343), CBA (1998b, 19), MORRISSEY (1988, 5).

104 See NYSBA (1999,10), ROACH and IACOBUCCI (1998a, 60-61).

105 Knowledge spillovers are substantial, see BOWER (1982, 333), but also contractual efficiencies (*id.* 334). See also ARRUÑADA (1999c, 514-515).

106 The absurd (but widely extended) belief that accountants do not have a duty of confidentiality needs to be rectified, it may be less strict than lawyer's, but that does not mean they do not have one. See SIMMONS (1998b, 1-2).

107 See article 1.3 of *Código Deontológico de la Abogacía Española*; CCBE (1988, §2.3), ABA (1995, Rules 1.6 and 1.8.b; 1983, DR4-101; 1963, Cannon 37), DAVIES and MIKELS (1999, 21), FBA (1999, 22-26), GREER (1999a, 4-9), HAZARD , Jr., KONIAK and CRAMTON (1994, 241-243), LSUC (1998b, 31-35, 40-43), NALLET (1999, 47 and 109), NYSBA (1999, 15-18), ROACH and IACOBUCCI (1998a, 34-36, 52-54; 1998b, 34-40). there have been also proposals of expanding the privilege to non-lawyer professionals working in the MDP, see CBA (1999a, 12-18), FLSC (1999, 7-8), BARREAU DU QUÉBEC (1999, 40-43).

108 Recently PWCo was accused by *Mazda Motor España S.A.* of providing *Landwell* (PWCo's legal services "affiliate") auditing information about the firm that was passed later on to the japanese firm *Mazda Motor Corporation* (Landwell´s client), which was having a sour dispute with the controlling shareholders of *Mazda Motor España, S.A*. (see «Price se enfrenta a la primera denuncia en España por falta de independencia de auditores y abogados», *Expansión*, 15 Jan. 2000, 1, 2 and 37; «PWC, acusada por Mazda España de pasar información de la auditora a la rama legal», *Cinco Días*, 17 Jan. 2000, 11). *Mazda Motor*

Finally, the joint rendering may increase the quality of services and generate professional rivalry promoting creativity and innovation of the overall services provided by the firms to their clients[109].

Proposal of regulation of the legal profession.

The recent draft of regulation of the legal profession (*«Estatuto General de la Abogacía»*) includes various prescriptions designed to deal implicitly with the rendering of legal services by audit firms[110].

Indeed, Article 21 of the proposal establishes the following prohibitions for lawyers:

> «to share premises or services with other incompatible professionals, risking the professional secret (c)»
> «to have associative ties with professionals, public officials or positions incompatible with the exercise of the legal profession or prohibited to lawyers (d)».

Besides, article 22 asserts the absolute incompatibility between the practice of law and the *«professional exercise in association with any of the positions, activities or professions incompatible with the legal profession(c)»*. This broad disposition that would impede the joint working with any professionals held incompatible with lawyers is somehow absurd as it cannot be said that auditors are *per se* incompatible with lawyers. That is something that should be ascertained in each situation depending on the concurring circumstances[111].

Article 29 of the proposal regulates multi professional firms that practice law. First of all, this possibility is restricted to those professionals who would not be incompatible with lawyers. Furthermore, the conditions that would be imposed to the formation of a multiprofessional firm that also renders legal services are:

> - that non licensed lawyers accept by writing the ethical and disciplinary obligations of lawyers.
> - that lawyers are liable for the ethical and disciplinary infringements of non-lawyers.
> - that lawyers may veto any decision to be adopted by the firm.

España filed several claims against PWCo and *Landwell* before the ICAC, the Madrid Bar Association, the civil courts (see *Expansión*, 9 feb. 2000, 61), and the antitrust authority. In few days the Madrid Bar Association denied *Mazda*'s claim (see «El Colegio de Abogados archiva la denuncia de Mazda contra PwC por falta de pruebas», *Expansión*, 27 Jan. 2000, 65; «Archivada la primera denuncia por falta de independencia entre abogados y auditores contra PricewaterhouseCoopers», *Cinco Días*, 27 Jan. 2000, 27).

[109] See MORELLO (1997, 246-247).

[110] See MULLERAT (1999, §3.B).

[111] See ALONSO AYALA (1999, 80). On the contrary, see CNB (1998, 1994); LSEW (1998, §23.2); MULLERAT (1999, §VII), the latter two consider that there is clash of regulatory cultures, particularly a conflict of legal duties.

On January 14, 1999, the Council of State (*«Consejo de Estado»*), delivered its mandatory report about the proposal of new regulation[112], making several observations and objections to the text of the proposal. Observations 10 and 16 deal specifically with those provisions of the proposal related to the issue of the rendering of legal services by audit firms. These observations criticise the normative realm of the regulation, and the lack of precision and ambiguity with which the legal rules have been drafted. They are considered too vague, leaving a wide gap that might easily be interpreted as restricting the competition on the legal services market.

The Council of State considered that the principle of "incompatibility" that can be directly extracted from articles 21 and 22 cannot be accepted, as it is too broad and it affects other professions other than the lawyers and, thus, should not be included in a proposal of regulation of the law profession[113]. The regulation should constrain itself to those aspects that put in danger the correct practice of law[114].

Although the articles of the Regulation objected by the Council of State were promptly modified -in order to adapt them to the observations made and to fulfill the conditions required[115]- the Ministry of Justice has followed a reticent position on the approval of the regulation. This backwardness seems to be based on the objections that other Ministries have posed to the current proposal, specially to the rules dealing with professional incompatibilities and multidisciplinary companies[116].

The delay in the approval of the regulation by the Government pushed the legal profession (CGAE) to threaten the approval of self-regulatory rules that would establish the incompatibility of the joint practice of law and

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[112] According to article 22.3 of the Ley Orgánica 3/80, of 22 April 1980, del Consejo de Estado, the Council of State must deliver a report of any regulation that executes an Act. In this case, article 6, numbers 2 and 3 the Ley 2/1974, of 13 february, sobre Colegios Profesionales (BOE nº 40, of 15.02.74) is being executed .

[113] For a similar analysis, see CBA (1999a, 28-31), ROACH and IACOBUCCI (1998b, 16-18).

[114] See CONSEJO DE ESTADO (1999, 35-38 and 44-46); «El Consejo de Estado condiciona la prohibición de que auditores y abogados trabajen juntos», *Expansión*, Jan. 15 1999, 52. It is suggested that the forthcoming Ley de sociedades profesionales (*Act on Professional Companies*) should be the proper place were to regulate most of these aspects.

[115] See «El Estatuto de la Abogacía incluirá las indicaciones del Consejo de Estado», *Expansión*, 13 feb. 1999, 45. In case the Council of State raises any objections in the Report (as it did in fact), art. 130. 3 of the Regulation of the Council of State (approved by Real Decreto 1674/1980, of 18 July, and modified by Real Decreto 1405/1990, of 16 November 1990), establishes that corrections are necessary if the proposed text wants to be approved "in accordance with the Council of State".

[116] Mainly, but not exclusively, by the Ministry of Economy, see «Economía interviene en el Estatuto de la Abogacía por las presiones de los auditores», *Cinco Días*, Feb. 24 1999, 30; «Economía defiende la unión de auditores con abogados y bloquea el Estatuto», *Cinco Días*, May 20 1999, 34.

audit services, precluding the rendering of legal services by audit firms[117]. The CGAE searched an expeditious channel to arrive at the prohibition of the joint-exercise of the legal and the audit professions, even if it had to be decided by the courts[118].

The announced self-regulatory measures were adopted by the general assembly of the CGAE on 18 June 1999, and although they deal with the topic of legal practice in agreement with other professionals, they have not been able to expressly and directly forbid law practice by audit firms[119].

The new regulation, which is applicable after 1 July 1999, permits attorneys to reach an agreement to collaborate with other professionals *«not incompatible with the practice of law»*, with the requirements -among others less important- to disclose and notify the agreement in an special register within each local bar association[120], and also that the non-lawyers submit a written compromise to abide to the ethical rules of the law profession[121].

6. CONCLUSION.

The current situation in Spain provides an excellent opportunity for a change in the approach to the regulation of the interprofessional competition and the possibility of forming MDPs.

Law and accounting need not be considered watertight compartments anymore[122]. There is nothing wrong with firms that provide legal and auditing services at the same time, to the same client. Of course, despite the

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[117] See «Los abogados se revelan contra Justicia y tratan de aprobar el Estatuto por su cuenta», *Expansión*, May 26 1999, 51; «La abogacía aprobará la separación de los auditores sin el permiso de Justicia», *Expansión*, June 11 1999, 74.

[118] «El Consejo de la Abogacía amenaza con denunciar a bufetes ligados a auditores», *Cinco Días*, May 26 1999, 38.

[119] See «Los abogados españoles deciden autorregularse», *Cinco Días*, June 11 1999, 32; «Los abogados reiteran la incompatibilidad con los auditores, pero no la pueden imponer legalmente», *Cinco Días*, June 21 1999, 30; «La nueva autorregulación de los abogados no incluye la incompatibilidad con los auditores», *Cinco Días*, June 18 1999, 32.

[120] See «La Abogacía obliga a los despachos a comunicar sus alianzas con profesionales 'no abogados'», *Expansión*, 5 Nov. 1999, 58. See *Otrosí* 13 (march 2000) 67-68 for the Resolution approving the creation of the "MDPs Register" by the Madrid Bar Association.

[121] Tercera. b), «Normas de ordenación de la actividad de la abogacía», *Otrosí* , 6 July 1999, 15. Besides, the attorney participating in the agreement assumes the liability in case of infringement of the deontological rules by the non-lawyers (*id.*, Tercera. f). That is also one of the conditions imposed by the Rules 5.3 and 5.4(b).3 of the Bar Association of the District of Columbia, see also GILBERT and LEMPERT (1988, 396). This restriction operates as a constrain to the emergence of MDPs, see AAI (1999, 1).

[122] On the contrary, see LEVINSON (1990, 259-260). In Spain, see Luis Martí Mingarro, «Defender y auditar: dos tareas distintas», *Expansión*, 6 oct. 1999, 67 (who stresses the need to draw a "clear an categorical frontier" between both professions).

formation of a multidisciplinary firm, the licensing requirements and the legal and ethical duties of the different professionals must be strictly observed and enforced[123].

In the last few years there has been a change in the domain and scope of the law and accounting professions, that found themselves within a powerful dynamic evolution, whose consequences and effects are still difficult to foresee[124].

The legal profession needs to adapt the practice of law to current client's needs[125]. A change of attitude is necessary: of course, zealously serving the client's interest in compliance with the laws continues to be the only aim of lawyers. However, the traditional discourse depicting lawyers as the "guardians" of justice and the law profession as something disparate to other professions, with some peculiar essence or ethical standards that preserve the legal services out of a market[126], needs to be relinquished. Lawyers are not different to other professionals[127]. Their legal and ethical duties might be[128], but that does not require preserving them from a "market" or from competition. In fact, there is competition among individual lawyers and law firms, and nothing should insulate them from the competition of other professionals[129].

Restrictions to multidisciplinary partnerships formation and to the practice of law by audit firms should

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[123] See FLOOD (1989, 590-592).

[124] See FREEDMAN and POWER (1991, 787-791) [new comercialism and questioning of traditional professional organizations and structures].

[125] See AAI (2000, 8-10); McGARRY (1999); MEEKS (1991, 1042).

[126] See FBA (2000, 12). However, for a recent restatement of the old fashioned discouse in Spain see CGAE (1999, 15 and 17) or MULLERAT (1999, §VIII).

[127] For a (somehow) different view (*«distinctiveness of law as a separate profession»*), see LEVINSON (1990, 243 and 262; 1988, 804). This issue is also stressed, as it is considered to be put in risk by increasing competition, mergers of law and audit firms and MDPs by Joaquín García Romanillos, «Abogados: ¿sin fronteras?», *Expansión*, 5 march 1999, 60.

[128] Due to the «requirements of a properly functioning judicial system in a constitutional democracy», see CBA (1999c, 21).

[129] See «Join 'em or beat 'em», *Law Society's Gazzette,* 94/22 (4 june 1997), 13. This position is held also by MARTI BALDELLOU and HARILLO (1993, 122-123). This seems to be a shared conclussion reached by national bar associations and law societies worldwide, see, for example, BARREAU DU QUÉBEC (1999), CBA (1999b, 1999d, 1998b, 1998c, 1998d), FLSC (1999), LSUC (1998a, 1998b), LSEW (1998), NYSBA (1999). For the IBA see «IBA faces up to multidisciplinary partnerships», *International Financial Law Review* 17, Oct. 1998, 4-5 (resolutions 5 and 6 of the Vancouver meeting, june 1998).

It is often argued that rules restricting the formation of MDPs by lawyers constitute a form of economic protectionism of the legal profession, see AAI (2000, 13-15); MORELLO (1997, 236 and 250). However, it has also been considered that the opening of the legal services market to the audit firms, due to the big five domination, might lead to a «Big five» MDPs' oligopoly that would eliminate the advantages initially foreseen, see CBA (1999c, 45), MORELLO (1997, 241).

disappear (as it seems it will finally happen) from the Spanish draft of regulation of the legal profession[130]. It is not only that this regulation is not the proper *forum* for introducing those prohibitions and limitations (which indeed it is not), it is moreover that the approach followed is deeply mistaken. The restrictions proposed do not protect the consumers or the public interest, they constitute an attempt to preserve some sort of economic protectionism of lawyers over the legal services market. Audit firms should be allowed to practice law in competition with law firms, MDPs may be formed and ownership of law firms by other professionals should be permitted. There is nothing wrong with these things in themselves. Lawyers and law firms should adapt to this new scenario, committing themselves to the provision of legal services of better quality than audit firms[131]. In any case, lawyers practising law within an audit firm or law partners of MDPs must strictly follow the regulation and ethical code of the law profession. It may be considered their duty of loyalty, confidentiality and integrity in the defense of their client's interests are even stronger than to traditional law firms[132]. Indeed, as potential conflicts of interest might become more prevalent, the respective professional organizations or the legislator may introduce some rules to address them[133].

In this situation, two measures seem adequate. They concern the auditors, trying to secure their independence from the client. The measures proposed are though to deal with joint-rendering of audit and non-audit services, but they may even be useful (at least the first) even for ordinary audit firms that do not render non-audit services. First, a flexible and variable diversification rule should be introduced, since this would prevent audit firms from an excessive financial dependence on an individual client. Secondly, following the English model, a disclosure obligation should be established. The obligation would be imposed to corporations, and it would be particularly effective in publicly quoted corporations. They would be required to disclose the total income paid

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[130] See «Justicia renuncia a la separación de auditores y juristas en el futuro Estatuto de la Abogacía», *Expansión*, 9 sept. 1999, 50. On the other hand, one of the largest local associations (the catalonian) has taken a more lenient approach to the issue (see «La abogacía catalana apoya la creación de sociedades multidisciplinares con auditoras», *Cinco Días*, 4 oct. 1999, 33), this has led to the approval on february 16, 2000 of a new "Regulation on Law Partnerships" (see «La abogacía catalana liberaliza las sociedades profesionales», *Cinco Días*, 18 feb. 2000, 34; «El Consejo catalán liberaliza la creación de sociedades», *Expansión*, 18 feb. 2000, 67; «Los abogados catalanes pueden crear despachos multidisciplinares, pero deben suministrar más información a los colegios», *Cinco Días*, 25 feb. 2000, 2000). This Regulation (*Reglament de societats professionals d'avocats*) is available on www.icab.es (visited on 21.03.2000).

[131] See DAVIES and MIKELS (1999, 20); Rachel Berresford, «Beat 'em or join 'em», *Lawyers Journal*, 9 (july 30, 1999), 1.

[132] See LCA (1998, §§ 3, 4.a), CBA (1999b, 30-31).

[133] See AAI (2000, 15-16); MUNNEKE (1992, 606-607). Some of the conflicts of interest may arise due to conflicting duties of the respective professional ethic codes, in that case harmonization must be sought, see BARREAU DU QUÉBEC (1999, 49-51), SIMMONS (1998a, 1-2).

to their audit firms, under all headings, and whether the rendering of non-audit (including legal) services by their firm acting as statutory auditor (or any of its affiliates) was approved by the audit committee and/or by the Board of directors.

On the other hand, regarding the legal profession, given the increased competition from audit firms in the legal services market, it should try to develop some basic and simple (fair) rules to govern the practice of law by audit firms and MDPs[134]. The recommended rules would inform the public about the different arrangements through which legal services can be provided, objectively describing the risk and protections available, and the governing legal and ethical rules, in each case[135]. This would allow traditional independent law firms that practice law only to differentiate their product from MDPs or audit firms that practice law among other different services[136].

ACKNOWLEDGEMENTS:
I wish to thank the helpful comments and interesting suggestions that María Alvarez, Brendan Doyle, Trude Erwik, Javier García de Enterría, Angel Rojo, Aníbal Sánchez, Avron Sheer (the editor), Ignacio Tirado and an anonymous referees provided to previous drafts of this article. Of course, the remaining mistakes are of my own responsibility.
Financial Support by grant AP95 09404511 (within the *Programa de Formación de Profesorado Universitario*) of the Spanish Ministry of Education and Culture is herein gratefully acknowledged.

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134 See proposals included in NYSBA (1999, 29).

135 See «La Unión Internacional de Abogados aprueba los criterios mínimos para el ejercicio profesional multidisciplinar», *Noticiario Jurídico Aranzadi*, 25 nov. 1999, nº 40, 3 (resolution of the UIA adopted in New Delhi on nov. 3, 1999).

136 A similar proposal was made by BOWER (1997, 166-168). See also, CBA (1998a, 32-33); NALLET (1999, 105-106) and David Andrews, «One stop to profit», *Law Society's Gazette*, 94/26 (2 july 1997), 15.

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