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Private Firm

Ethics 20/20 Ditches Idea of Recommending Option for Nonlawyer Owners in Law Firms

The ABA Commission on Ethics 20/20 will not recommend any changes to the bar group's policy against nonlawyer owners or investors in law firms, the commission decided at its April 12-13 meeting in Washington, D.C.

In an April 16 statement announcing the decision, Commission Co-Chairs Jamie S. Gorelick and Michael Traynor said, ''Based on the commission's extensive outreach, research, consultation, and the response of the profession, there does not appear to be a sufficient basis for recommending a change to ABA policy on nonlawyer ownership of law firms.''

In other action at the meeting, the commission finalized its recommendations for rule amendments on outsourcing and other topics, which are scheduled to be filed with the ABA in May for consideration by the House of Delegates at the bar group's Annual Meeting in August. See 28 Law. Man. Prof. Conduct 253.

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DAVID J. CARR
ICE MILLER

The commission's decision not to pursue any form of nonlawyer ownership drew quick praise from some quarters. ''It was a bad idea, and it's a good thing they didn't do it,'' Mark W. Foster of Zuckerman Spaeder, Washington, D.C., said in an interview with BNA.

Opponents argue that nonlawyer ownership is unnecessary, threatens the profession's core values, and will lead to external regulation of the legal profession. The commission's proposal would open the door to more extreme forms of nonlawyer ownership, such as passive investment, they say.

But others expressed regret that the commission dropped the idea of allowing nonlawyers who work in law firms to become partners.

''It's unfortunate not to recognize the level of nonlawyer talent that already exists in law firms,'' Tony Williams told BNA. ''Wouldn't it be sensible to recognize there are important people in law firms who don't have J.D. after their names?'' Williams is principal of Jomati Consultants LLP, London.

Still others contend that the commission should have pushed the idea of letting law firms have outside investors, as they are permitted to do in England and Australia. External ownership of law firms will benefit consumers, improve law firm governance, and boost U.S. law as an export business, said Matthew Hudson of MJ Hudson LLP, London.

Proposals Aired in December. In early December, the commission asked for feedback on tentative amendments to Model Rule 5.4 that would allow nonlawyers working in a law firm to have up to a one-fourth ownership interest in the firm.

The commission's discussion draft on ''alternative law practice structures,'' or ALPS, outlined a form of nonlawyer ownership that is even narrower than what is allowed in the District of Columbia, the only U.S. jurisdiction that permits law firms to include law firm partners. The commission had previously decided against endorsing outside investment in firms, publicly traded firms, or multidisciplinary practices. See 27 Law. Man. Prof. Conduct 750.

Commissioners ultimately decided, however, not to recommend any form of nonlawyer ownership. ''The Commission considered the pros and cons, including thoughtful comments that the changes recommended in the Discussion Draft were both too modest and too expansive, and concluded that the case had not been made for proceeding even with a form of nonlawyer ownership that is more limited than the D.C. model,'' Gorelick and Traynor said in their statement.

Choice of Law Issue Still Active. The announcement states that the commission ''will continue to consider how to provide practical guidance about choice of law problems that are arising because some jurisdictions, including the District of Columbia and a growing number of foreign jurisdictions, permit nonlawyer ownership of law firms.''

The commission issued draft proposals on these subjects in December, suggesting possible rule changes

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that could make it feasible for lawyers in jurisdictions that do not allow nonlawyer owners to be partners and share fees with lawyers in jurisdictions that do allow nonlawyer ownership. See 27 Law. Man. Prof. Conduct 750.

The April 16 announcement indicates that the commission welcomes comments on these drafts and will decide at its October meeting whether to submit formal proposals on the choice of law issues for consideration by the delegates in February 2013.

In a comment the commission received on the December discussion drafts, Mike Burke, chair of the ABA Section of International Law, urged that any solution, by rule or comment, should make it clear that a U.S. lawyer in one state, whose ethics rules preclude nonlawyer ownership or fee-sharing, is not in violation of the local rule if the lawyer's partner in another jurisdiction is either not a lawyer at all, or is a lawyer under the other practice, and otherwise meets the ethical standards of that other jurisdiction.

A recent ethics opinion from the New York state bar advised that lawyers who are licensed in New York and primarily practice there may not get around its rules against sharing fees and partnering with nonlawyers by teaming up with a firm organized in a jurisdiction that has more flexible rules. See New York State Ethics Op. 911, 28 Law. Man. Prof. Conduct 190 (2011).

Bar Associations Frown. The commission received more than two dozen comments on its December proposals. Negative reactions outnumbered supportive ones by more than a two-to-one margin.

A comment submitted by the New Jersey State Bar Association decried the ALPS approach as ''a solution in search of a problem, with no discernible benefits for the vast majority of our state's lawyers that would justify the clear potential for harm.''

''Assertions that the proposed amendments to R.P.C. 5.4 are intended to address the reality of global practice do not ameliorate the NJSBA's concerns about the negative impact such changes may ultimately have on the nature of law practice in the United States,'' the bar's comment stated.

The Illinois State Bar Association objected more broadly to all of the ALPS-related proposals the commission floated in December. Their adoption ''would negatively impact the exercise of a lawyer's independent professional judgment and might alter the regulation of the legal profession by the judicial branch of government,'' the ISBA stated in a letter to the commission.

Accompanying that letter was a resolution declaring the ISBA's opposition to the commission's proposals and asking the ABA to reaffirm its policy, adopted in 2000 when the House of Delegates rejected multidisciplinary practices, that ''The sharing of legal fees with non-lawyers and the ownership or control of the practice of law by non-lawyers are inconsistent with the core values of the legal profession.'' See 16 Law. Man. Prof. Conduct 367.

New York Study. In light of the commission's ALPS proposals, the New York State Bar Association launched a task force to evaluate whether the bar association should relax its long-standing policy against nonlawyer ownership of law firms.

Stephen P. Younger, who is chairing that initiative, told BNA that the task force is undertaking a comprehensive study but that its views are not yet final. Younger is a partner with Patterson Belknap Webb & Tyler, New York, and is immediate past president of the NYSBA.

A survey for the project found that the vast majority of the bar's membership—70 to 80 percent—did not favor the nonlawyer ownership model floated by the Ethics 20/20 Commission, Younger said. He applauded the commission for taking the proposal off the table.

Younger said that the task force is still studying both the nonlawyer ownership issue and the Ethics 20/20 Commission's other draft proposal, which would allow lawyers who practice in jurisdictions that permit nonlawyer owners to be partners with lawyers in jurisdictions that do not permit nonlawyer owners.

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TONY WILLIAMS
JOMATI CONSULTANTS

Currently that is not allowed in New York, as Opinion 911 makes clear, Younger explained. The task force is looking at whether the competing position has merit, and its report will address both that issue and the broader nonlawyer ownership issue, he said.

Younger said the task force expects to vote in early June. If it decides to endorse any change in the bar association's existing position, he said, the question would need to be presented to the bar's delegates for debate and possible action.

Independent Judgment at Stake. As part of his practice with Zuckerman Spaeder, Mark Foster advises lawyers and firms about the District of Columbia's unique rule on nonlawyer ownership.

But Foster said he personally believes that allowing nonlawyer ownership in firms is the wrong way for the legal profession to go, due to the potential for interference with lawyers' independent judgment.

''The idea of independent professional judgment is fundamental to the notion of being a lawyer,'' he said.

Foster emphasized that although D.C.'s rule has been on the books for more than two decades, no other U.S. jurisdiction has opted to allow lawyer owners in law firms. If other jurisdictions allow nonlawyer owners, he

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said, ''my prediction is that law firms will be owned by banks.''

Harmful to Core Values. In response to the ALPS discussion draft, nine general counsel of major U.S.-based corporations sent the commission a joint letter expressing their view that ''allowing any form of non-lawyer ownership of law firms will harm the core values of the American legal profession.''

There is no demonstrated need for the proposed change, and no reason to believe that clients will be better served by a profession that is open to nonlawyer ownership, they argued.

''Quite the contrary, we fear that the inevitable chipping away at the profession's professionalism ultimately will do a disservice not just to the business clients we serve, but to all clients who seek the trusted and confidential advice of counsel,'' the letter states.

The corporate counsel also expressed concern that any form of nonlawyer ownership of law firms will undermine the attorney-client relationship. Even under the more limited form the commission was considering, they added, nonlawyer investment ''changes a firm from a group of like-minded attorneys zealously pursuing their clients' interests, into a group with inherently mixed motives and responsibility, where some partners have a professional duty to the client's interests and others do not.''

In addition, they contended that ''the experience of countries such as Australia illustrates that the impulse to start relaxing the longstanding rules upon which the legal profession has been built can quickly lead to a radical transformation of the practice of law.''

Nonlawyer ownership also could make external regulation of the legal profession more likely, the general counsel asserted.

'Recipe for Disaster.' In a comment on the ALPS draft, Indianapolis lawyer David J. Carr, of Ice Miller, wrote that ''Allowing individuals to buy their way into ownership with neither legal training, nor direct ethical accountability, constitutes a recipe for disaster.''

Rather than emulating other countries that allow nonlawyer owners, he contended, the United States ''should continue to serve as a model for other countries in best legal practices.''

After the commission dropped the idea, Carr told BNA, ''I am glad, and proud, that the ABA came to its senses.''

Camel's Nose. The lack of any demonstrated desire for nonlawyer ownership was emphasized in a comment commissioners received from Douglas R. Richmond of Aon Professional Services, Chicago.

Richmond asserted that despite the long existence of D.C.'s Rule 5.4, only a miniscule number of firms in the district include nonlawyer owners—which indicates, he said, that there would be little demand for the stricter approach floated by the commission.

The commission is proposing ''change for the sake of change alone,'' without identifying any client-centered justification and without accounting for potential detriments that may flow from the change, he contended.

Richmond also expressed concern about ''the camel getting its nose under the tent''—that is, that the commission's relatively modest recommendations would ultimately lead to passive outside investment in law firms and multidisciplinary practices. Debating more radical proposals in the future will be far harder if the draft proposals are embraced, he contended.

It's Already Happening. But Tony Williams of London expressed disappointment that the commission dropped the idea of allowing nonlawyers who work within law firms to be partners. Williams provides consulting services to the legal profession and previously served as managing partner of Clifford Chance and Arthur Andersen Legal.

Williams pointed out that many firms in the United States have nonlawyers in key positions, such as chief financial officers and chief operating officers, who are viewed as important parts of the management team and attend partners meetings. Remuneration for these people is generally tied to the performance of the firm, so that ''allowing them to become partners would regularize what is already happening,'' Williams said.

Whether the ABA wishes to open up to other models of nonlawyer ownership, such as passive investment, is a different issue, Williams commented. But to reject all approaches to nonlawyer ownership, he said, shows a lack of confidence in lawyers' being able to function in other environments, and ignores what would be useful to clients. Making sure that services are available in the way clients want at a credible price matters too, he remarked.

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THOMAS M. GORDON
RESPONSIVE LAW

As for the argument that nonlawyer owners will press lawyers to ignore professional standards, Williams said ''to suggest that only lawyers have ethics is a bit insulting for the rest of society.'' Law firms understand the value of protecting their reputation, and ''any sensible professional will know that the highest professional standards are good business,'' he added.

External Investment. In an email to BNA, Matthew Hudson took the position that bar associations and U.S. states ''are being surprisingly misguided'' on the issue of external investment in firms.

Hudson previously managed foreign offices for a couple of large U.S. law firms in Europe, and is the founder of MJ Hudson, a law firm that advises the ''alternative asset'' industry and intends to take advantage of the U.K.'s Legal Services Act, which permits outside investment in law firms.

In Hudson's view, external ownership will bring in competition and new ideas about product delivery, which will lead to better pricing, better access, and more transparency to the consumer.

He also asserted that ''having the rigors of external shareholders will introduce far greater governance and internal management'' in law firms. The United Kingdom and the United States are fighting it out to be the law of choice for commercial contracts and dispute resolution, but the U.S. has allowed the U.K. to get ahead of the game, he said.

As for the idea that investors' profit motives will damage law firms and the services they provide, Hudson called that ''pretty hilarious.'' If that is the concern, then all law firms should be made not-for-profit organizations,'' he suggested.

Hudson said in his experience all law firms try to make as much profit as they can. ''I cannot see how having external investors would change that,'' he said. If anything, he suggested, investors would try to increase their capital value by growing revenues and profits, which might well mean reducing fees to build market share.

Regarding the resistance to nonlawyer ownership in the United States, Hudson said the U.S. legal profession ''wants to protect its cartel.'' But states will end up competing with each other, he added, and ''those that change their laws now will have a business advantage against other States.''

''Ultimately all of the US will adapt and bring in external law changes—I predict this will happen within 5 years,'' Hudson told BNA.

'Matter of Time.' In an interview with BNA, Thomas M. Gordon of Responsive Law in Washington, D.C., said it's disappointing but not surprising that the ABA would reject nonlawyer ownership. ''It's now a decade into the 21st century and the commission rejected a proposal that would bring us up to the 1980s,'' he said.

Gordon said he believes the Ethics 20/20 Commission should have gone further and recommended allowing passive investment in law firms. Access to capital will promote innovations in delivering legal services, he contended.

His prediction is that ''it's only a matter of time'' until law firms are allowed to have nonlawyer owners. ''But it's going to be a tough fight,'' he said.

Indeed, a federal district court last month dismissed a lawsuit by the Jacoby & Meyers law firm challenging the barrier to private equity investment in New York Rule of Professional Conduct 5.4. The constitutional challenge cannot be heard in federal court because other, unchallenged provisions of New York law also prevent law firms from including nonlawyer owners, the court held. See 28 Law. Man. Prof. Conduct 143.

Better to Have Tried. Reflecting on the commission's decision to pull back on the issue of nonlawyer ownership, law professor Thomas D. Morgan of George Washington University pointed out that ABA commissions define success in terms of what they can get the House of Delegates to accept.

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LETTER FROM GENERAL COUNSEL
OF NINE MAJOR U.S. COMPANIES

They tend to see a defeat in the House as a failure, he said, ''even if by bringing a good idea before lawyers today, they may make later acceptance of an idea more likely.''

The commission may be right that it would not have won this time around, he said, ''but I think their failure even to try is unfortunate.''

According to Morgan, many ABA members believe that the ABA Commission on Multidisciplinary Practice failed when it produced a report that was outstanding but proposed going further than the ABA delegates were prepared to go.

But far from failing, Morgan said, the MDP Commission succeeded in laying the groundwork for changes in Great Britain, Australia, and potentially other parts of the world. ''I only wish the Ethics 20/20 Commission were equally willing to risk 'failure' in ABA terms, but reap success in the larger sense,'' he said.

BY JOAN C. ROGERS

Full text of the commission's announcement is at http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20120416_news_release_re_nonlawyer_ownership_law_firms.authcheckdam.pdf.