ABA/BNA Lawyers' Manual on Professional Conduct

26 Law. Man. Prof. Conduct 110 (February 17, 2010)

Model Rules

Speakers Debate Nonlawyers' Role in Firms At First Ethics 20/20 Commission Hearing

ORLANDO, Fla.—Themes that surfaced repeatedly during the ABA Ethics 20/20 Commission's initial public hearing Feb. UU5 were the need for uniformity in lawyers' ethics obligations when practicing across borders, and the importance of allowing innovation in the delivery of legal services.

A particularly controversial issue that came up during the standing-room-only hearing is whether the ABA should recognize any value in allowing nonlawyers to have an equity interest in law firms, as is permitted in the District of Columbia and, to an even greater extent, in Australia and the United Kingdom.

Imploring the commission generally not to recommend yet another set of changes to the Model Rules of Professional Conduct, Lawrence J. Fox, who practices with Drinker Biddle in Philadelphia, condemned in particular the idea of allowing nonlawyers to own law firms.

But according to Richard Granat, who co-chairs the eLawyering Task Force of the ABA Section of Law Practice Management, existing rules limiting ownership of law firms to lawyers impede innovation in the delivery of online legal services, particularly for solo and small law firms.

The commission was launched last summer to recommend updates to the Model Rules in light of changing technology and globalization. See 25 Law. Man. Prof. Conduct 418. The day before the public hearing, the commission held a meeting to hone its focus in light of comments submitted about its preliminary issues outline. See 26 Law. Man. Prof. Conduct 112.

Outside Capital, Management Expertise

Granat told the commission that he operates a virtual law firm in Maryland from his home in Florida. He also is president of DirectLaw Inc., which describes itself as the first “virtual law firm in a box” that enables lawyers to transform their website into an online legal practice and helps solo and small-firm law practices “level the playing field.”

Small law firms need access to outside capital and management skills, Granat said, to take advantage of the large “latent”market that usually goes unserved but whose legal needs can be handled through virtual law practice.

Granat pointed out that the Legal Services Act of 2007 in the United Kingdom allows Alternative Business Structures(ABS) in which outside investors can own a share in a legal services business. American bar leadership should watch these reforms carefully and see what can be adopted in the United States, he contended.

Although the “balkanized” nature of lawyer regulation in the United States would make it difficult to institute these reforms nationwide, “it would be foolish to ignore them as UK firms will have access to management and capital resources that will give them a competitive advantage over the US counterparts,” Granat wrote in materials he submitted to the commission.

‘Terrible Mistake.’

As several speakers pointed out during the commission's public hearing, and also in its meeting the previous day, the District of Columbia's version of Model Rule 5.4 allows nonlawyers to own an interest in law firms.

But at the hearing Fox told the commission that it would be a “terrible mistake” to water down Model Rule 5.4‘s standards on the independence of lawyers. The ABA should not endorse different forms or organizations that compromise the legal profession's values and ethics, he argued.

Commission member Stephen Gillers, who is a law professor at New York University, noted that arguments about Rule 5.4 and nonlawyer ownership of law firms are often made in terms of empirical predictions. Gillers pointed out that there is experience on this issue in Britain, which now allows the D.C. model of nonlawyer ownership for law firms so long as the nonlawyer share is less than 25 percent.

Fox responded by bringing up Arthur Andersen's experience in serving as auditor for Enron, which he described as the best argument against changing Rule 5.4. In response to a statement by Gillers that the mention of Arthur Andersen/Enron is a rhetorical device, Fox said that when the accounting firm's core function of auditing was compromised, “real people lost their leg.”

Solo and small law firms need access to outside capital and management expertise.

Richard Granat
President, DirectLaw Inc.

Gillers pressed Fox to say whether, considering the D.C. and U.K. model, any empirical evidence would change his mind about nonlawyer ownership of law firms. No, said Fox.

Saying that he saw “many shades of MDP”(multidisciplinary practice) in the commission's agenda, Fox reminded the commission that “we had these wars 10 years ago.”A decade ago, the ABA Commission on Multidisciplinary Practice issued a controversial proposal that called for substantial relaxation of the restrictions on lawyers' practice of law within entities that include nonlawyers. The ABA House of Delegates rejected that recommendation in 2000 and disbanded the commission. See 16 Law. Man. Prof. Conduct 367.

Fox also urged the commission not to relax the ethics rules governing current-client conflicts. It's unethical to take a position directly adverse to a client, he asserted.

Philip H. Schaeffer, New York, who is general counsel of White & Case, pointed out that other nations such as Belgium and Germany use a substantial relationship test for current-client conflicts. Schaeffer is serving as the ABA ethics committee's liaison to the commission.

Fox was unswayed by that point.

ABS

Seth Rosner of Saratoga Springs, N.Y., said it would be irresponsible for the commission not to address alternative business structures that are developing outside the United States. Rosner served as a liaison from the ABA House of Delegates to the MDP Commission.

The 20/20 Commission, he said, should focus on the best ways for lawyers and the legal profession in this country to deal with the challenges raised by the new rules in the United Kingdom, such as what U.S.

law firms should do if they have lawyers living and working in Wales.

On the other hand, Rosner advised the commission against bringing MDP back before the ABA House of Delegates for substantive review. It would be “very, very difficult” to get the delegates to embrace a change in the rules on nonlawyer ownership of law firms, he said.

Gillers asked Rosner if he expected that degree of difficulty even for a rule like the one in the District of Columbia that allows nonlawyers to be partners and share fees as long as the firm practices only law. (*See box.*) Rosner said his take is that such a recommendation would not engender the same animosity as a wholesale revisiting of multidisciplinary practice.

Chicago patent attorney Christopher McGeehan told the commission that nonlawyer companies want to bring in legal clients, farm out the work, and pocket the difference. “This is what will happen if nonlawyer ownership” of law firms is permitted, he predicted.

Differing Obligations

In his comments to the commission, Rosner asked the members not to tinker with Model Rule 1.6, which addresses lawyer-client confidentiality. No other model rule has been as contentious as that one, he observed.

But he added that it would be useful for the commission to talk to firms that practice in multiple jurisdictions with varying versions of Rule 1.6 to see how they deal with variations among state lawyer-client confidentiality rules.

In addition, Rosner said, the commission ought to look at whether rules should differentiate on some questions, such as the use of advance waivers, depending on whether the lawyer or firm is dealing with sophisticated clients as opposed to those who see an attorney only a few times in their lives.

Cloud Computing; Virtual Law Practice

In his remarks about virtual law firms, Granat suggested that lack of clarity about confidentiality rules impedes law firms' use of “cloud computing,” which in turn impedes technological innovation in firms of all sizes.

In written materials he submitted, Granat explained that “cloud computing” or “Software as a Service”(SaaS) refers to the use of software that is delivered over the internet to a web browser rather than installed directly as an application on the user's local computer, along with storage of the user's data on an outside server.

Granat's materials posit that law firms can realize numerous advantages from using SaaS, and assert that these arrangements can be highly secure. The materials include a sample hosting agreement and a copy of “Suggested Minimum Requirements for Law Firms Delivering Legal Services Online,” which were developed by the eLawyering Task Force.

Another lawyer who spoke about virtual law practice, Stephanie L. Kimbro, pointed out that ethics opinions on the subject of lawyers' use of the internet tend to be old, discussing fax and e-mail. Broader opinions are needed, she said.

Kimbro operates Kimbro Legal Services, a virtual law firm in North Carolina that primarily provides estate planning. She is the co-founder of Virtual Law Office Technology, which according to its website provides “a secure, software as a service, web-based product that connects solo and small firm law practices with the online consumer.” VLOTech was acquired by Total Attorneys in October 2009.

In written materials she submitted, Kimbro discussed various methods and benefits of virtual law practice,

security recommendations, and ethics and malpractice considerations for virtual law practice.

Implications of New Technology

Granat suggested that ethics rules should be modified "to adjust to an online legal services environment" and "enable U.S. law firms to compete against new legal players." He suggested, for example, that states should:
• drop any mandate that lawyers have a physical office, as well as any requirement that lawyers archive all changes in their web pages;

• adopt rules on providing unbundled legal services, if they haven't yet done so;

• provide a clear definition of unauthorized practice so there's no doubt that a software system isn't the practice of law; and

• modify the rules on referrals and fee-sharing to enable lawyers to use evolving technology without having to worry about facing disciplinary action.

But McGeehan expressed a different view in his remarks. Many internet referral systems are just "virtual runners" that should not be permitted, he contended.

Commission members questioned Granat and Kimbro about how virtual law practice works and how clients can be sure that the lawyer providing services is competent, not conflicted, and authorized to represent them.

"We should be thinking about how to export our values."

Lawrence J. Fox

Commission member George W. Jones Jr. wondered if the anonymity of a person providing legal services on the internet can create difficulties if the client needs to find the person who provided the services. Jones is a partner in Sidley Austin in Washington, D.C.

Kimbro explained that when VLOTech sets up a virtual law firm for lawyers, they must identify themselves on their websites. State bar ethics advisers are coming up with ways to require attorneys to include contact information when they provide services over the internet, she said. The individual state bars are responsible for going after attorneys not in good standing, she added.

Granat said that unlike lawyers who have true virtual law practices, lawyers who respond to inquiries from consumers on sites such as Answers.com are said to be providing only "legal information" rather than giving "legal advice," so these lawyers do not check conflicts and supposedly do not form an attorney-client relationship with the consumer.

Good Guys, Bad Guys

In her comments to the commission, professor Laurel Terry of Penn State Dickinson law school recommended that in general the commission should "get out of the way of innovations."

How to "catch the bad guys" should be a priority issue for the commission, Terry said. It should "get out in front" on the issue of reciprocal discipline and see "what might impede catching the bad guys in other jurisdictions," she said.

In this regard, Terry noted that the European Union is in the process of creating an “e-justice portal”and that, as part of the U.K. reforms, lawyers are being assigned an ID number. “Our system has to be able to talk to their system,” she said.

Terry also urged the commission to be proactive about “encouraging the good guys.” Australia is implementing a self-assessment system for law firms, she noted.

She also suggested revisiting the idea of shifting from a rule-based system of regulation to a regulatory system based on principles.

Exporting Values and Views

Fox and Terry both mentioned, in different terms, the importance of communicating the U.S. legal profession's views to the rest of the world.

Fox said the ABA should explain the U.S. legal profession's rules to the rest of the world rather than making a “rush to the bottom” and adopting the “lowest common denominator” of other regulatory regimes. “We should be thinking about how to export our values,” he declared.

Terry urged the commission to consider how the ABA and the U.S. legal profession can best comment on and participate in the global discussion of law firms and legal services. “We're not at the table and we're not even talking,” she remarked, saying that there needs to be a permanent communication method.

Terry explained that no single entity within the ABA other than the House of Delegates is empowered to communicate policy for the entity on global issues involving legal services, yet the House of Delegates structure is not “nimble” for the purpose of commenting on key documents under consideration elsewhere around the globe. Citing the complicated nature of globalization issues, Terry said she wouldn't be comfortable with having an ABA task force commenting officially on such documents.

By Joan C. Rogers

The Ethics 20/20 Commission's website is http://www.abanet.org/ethics2020/.

Written comments that witnesses provided for the public hearing can be viewed at http://www.abanet.org/ethics2020/submissions.pdf.

District of Columbia Rule 5.4(b) Allows Some Nonlawyers to Have Financial Interest in Law Firms

“A lawyer may practice law in a partnership or other form of organization in which a financial interest is held or managerial authority is exercised by an individual nonlawyer who performs professional services which assist the organization in providing legal services to clients, but only if:

“(1) The partnership or organization has as its sole purpose providing legal services to clients;

“(2) All persons having such managerial authority or holding a financial interest undertake to abide by these Rules of Professional Conduct;

“(3) The lawyers who have a financial interest or managerial authority in the partnership or organization undertake to be responsible for the nonlawyer participants to the same extent as if nonlawyer participants were lawyers under Rule 5.1;

“(4) The foregoing conditions are set forth in writing.”

COMMENT

"[7] As the introductory portion of paragraph (b) makes clear, the purpose of liberalizing the Rules regarding the possession of a financial interest or the exercise of management authority by a nonlawyer is to permit nonlawyer professionals to work with lawyers in the delivery of legal services without being relegated to the role of an employee. ...

"[8] Paragraph (b) does not permit an individual or entity to acquire all or any part of the ownership of a law partnership or other form of law practice organization for investment or other purposes. It thus does not permit a corporation, an investment banking firm, an investor, or any other person or entity to entitle itself to all or any portion of the income or profits of a law firm or other similar organization. Since such an investor would not be an individual performing professional services within the law firm or other organization, the requirements of paragraph (b) would not be met."