

NOTE: The following draft is based on a revision to ABA Model Rule 5.4 that was proposed by the [ABA Ethics 20/20 Commission](#) in a [memo dated 12/2/2011](#). It is intended for discussion only. The footnotes include some observations and possible issues for discussion. Finally, this draft includes only changes to the black letter text. No changes have been made to the comment.

Finally, this proposed rule is not intended to circumvent a discussion of whether such a rule will operate to increase access to justice. It has not yet been established that jurisdictions that permit multidisciplinary practices have experienced a significant increase in access to justice. We still need a robust discussion on this issue.

Underlines represent additions to, and ~~strikethroughs~~ deletions from, current California Rule 5.4.

Rule 5.4 Financial and Similar Arrangements with Nonlawyers

(a) A lawyer or law firm* shall not share legal fees directly or indirectly with a nonlawyer or with an organization that is not authorized to practice law, except that:¹

(1) an agreement by a lawyer with the lawyer's firm,* partner,* or associate may provide for the payment of money or other consideration over a reasonable* period of time after the lawyer's death, to the lawyer's estate or to one or more specified persons;*

(2) a lawyer purchasing the practice of a deceased, disabled or disappeared lawyer may pay the agreed-upon purchase price, pursuant to rule 1.17, to the lawyer's estate or other representative;

(3) a lawyer or law firm* may include nonlawyer employees in a compensation or retirement plan, even though the plan is based in whole or in part on a profit-sharing arrangement, provided the plan does not otherwise violate these rules or the State Bar Act;

(4) a lawyer or law firm* may pay a prescribed registration, referral, or other fee to a lawyer referral service established, sponsored and operated in accordance with the State Bar of California's Minimum Standards for Lawyer Referral Services; ~~or~~

(5) a lawyer or law firm* may share with or pay a court-awarded legal fee to a nonprofit organization that employed, retained or recommended employment of the lawyer or law firm* in the matter; or

¹ The basic prohibition on fee sharing is preserved. The concept is that lawyers should not be sharing fees with nonlawyers. There is a concern that such fee sharing would result in nonlawyer marketing businesses that would direct clients to lawyers who pay the most for the referral, even if the lawyer is not qualified. However, there are six exceptions to the basic rule. A new exception, as proposed by the Ethics 20/20 Commission, is stated in subparagraph (a)(6), which refers to the paragraph (b) requirements.

(6) a lawyer or law firm may share legal fees with a nonlawyer or with an organization that is not authorized to practice law if the lawyer or law firm complies with the requirements set forth in paragraph (b).²

(b)³ ~~A lawyer shall not form a partnership or other organization with a nonlawyer if any of the activities of the partnership or other organization consist of the practice of law.~~ A lawyer may practice law in a law firm in which individual nonlawyers in that firm hold a financial interest,⁴ but only if each of the following requirements is satisfied:⁵

² I've added the full statement of what is permitted so that there is no confusion as to what is being permitted. The Ethics 20/20 version simply provided:

(x) a lawyer or law firm may do so pursuant to paragraph (b).

Although “do so” could be substituted, I think it important that the black letter clarify that permission to “do so” mandates that “the lawyer or law firm complies with the requirements set forth in paragraph (b), all of which requirements are mandatory.

The gist of paragraph (b) is that lawyers and nonlawyers are permitted co-own a law firm, which is defined in the rules as follows:

(c) “Firm” or “law firm” means a law partnership; a professional law corporation; a lawyer acting as a sole proprietorship; an association authorized to practice law; or lawyers employed in a legal services organization or in the legal department, division or office of a corporation, of a government organization, or of another organization.
CRPC 1.0.1(c).

Because sharing in the profits of such a firm requires that the legal fees, which would be the source of profit in such a firm, be shared, there has to be an express exception to the paragraph (a) prohibition as in subparagraph (a)(6).

Issue: Does the definition of “firm or law firm” have to be revised to encompass a company that is providing legal services primarily through technology?

³ **Important note:** Paragraph (b) is substantially more limiting than what was proposed as a “multidisciplinary practice” (MDP) by the ABA MDP Commission in 1999. The Ethics 20/20 was adamant in arguing that this rule was not such an MDP, likely in an attempt to forestall a DOA judgment by the legal profession (the original MDP proposal, made contemporaneously with the Enron debacle, was rejected by the ABA House of Delegates as an invitation for the then Big Five accounting firms to enter the legal market.

⁴ **Issue:** This provision refers to “individual nonlawyers.” Some past proposals have limited the ability to hold a financial interest in the law firm (as defined above) to nonlawyer *professionals*. This is an issue that we should discuss.

⁵ Similar to subparagraph (a)(6), the following phrase has been added to the Ethics 20/20 language:

(b) A lawyer may practice law in a law firm in which individual nonlawyers in that firm hold a financial interest, but only if each of the following requirements is satisfied:

Again, this language is intended to emphasize that each of the requirements is mandatory.

(1) the firm’s sole purpose is providing legal services to clients;⁶

(2) the nonlawyers provide services that assist the lawyer or law firm in providing legal services to clients;⁷

(3) the nonlawyers state in writing that they have read and understand the Rules of Professional Conduct, the State Bar Act and other laws regulating lawyer conduct and agree in writing to undertake to conform their conduct to the Rules, the State Bar Act and other laws regulating lawyer conduct;⁸

⁶ Subparagraph (a)(1) limits these co-owned firms to those whose “sole purpose” is the provision of “legal services” to clients.

Issues: (1) Do we need to define “legal services”?

(2) Is it necessary to include the term “to client”? For example, if the “legal services” are provided through an app, is a lawyer-client relationship formed even if the lawyer or lawyers in the firm never review the services that the app provides?

⁷ Subparagraph (a)(2) address to some extent a concern expressed by members of ATILS regarding whether a tech solution can retain the protection of the privilege or work product in providing services. So long as the nonlawyers, whether through their own efforts or through apps they have designed, are assisting lawyers in providing services to the firm’s clients, the protections of privilege and work product should be preserved.

For example, with respect to privilege, see Evid. Code 952, which provides:

As used in this article, “confidential communication between client and lawyer” means information transmitted between a client and his or her lawyer in the course of that relationship and in confidence by a means which, so far as the client is aware, discloses the information to no third persons other than those *who are present to further the interest of the client* in the consultation or *those to whom disclosure is reasonably necessary for the transmission of the information or the accomplishment of the purpose for which the lawyer is consulted*, and includes a legal opinion formed and the advice given by the lawyer in the course of that relationship. (Emphasis added)

However, this rule would not address the stated concern as to a nonlawyer’s business that is engaged in providing legal services through technology, unless that business is majority owned by a lawyer.

Issue: Should nonlawyer ownership be limited to nonlawyers who “assist” the lawyers of the firm in providing legal services?

If not so limited, e.g., the firm is a true MDP (i.e., providing legal, accounting, etc., services independent of one another), which could open the door wider than intended. See Sam Skolnik and Amanda Iacone, [Big Four May Gain Legal Market Foothold With State Rule Change, Bloomberg \(4/11/19\)](#).

Compare the rule revision proposal of the ABA MDP Commission in their [Appendix A](#).

⁸ Under subparagraph (b)(3), the nonlawyers must agree to undertake to conform their conduct to that of lawyers under the Rules of Professional Conduct, the State Bar Act, and the other laws that govern lawyer conduct (e.g., Evidence Code, Probate Code, Penal Code, etc.)

Issue: Is it necessary to require that they have “read” the rules & other lawyer or sufficient that they “understand” the conduct requirements imposed on lawyers by these laws?

(4) the lawyer partners in the law firm are responsible for these nonlawyers to the same extent as if the nonlawyers were lawyers under Rule 5.1;⁹

(5) the nonlawyers have no power to direct or control the professional judgment of a lawyer, and the financial and voting interests in the firm of any nonlawyer are less than the financial and voting interest of the individual lawyer or lawyers holding the greatest financial and voting interests in the firm, the aggregate financial and voting interests of the nonlawyers does not exceed [25%] of the firm total, and the aggregate of the financial and voting interests of all lawyers in the firm is equal to or greater than the percentage of voting interests required to take any action or for any approval;¹⁰

(6) the lawyer partners in the firm make reasonable efforts to establish that each nonlawyer with a financial interest in the firm is of good character, supported by evidence of the nonlawyer's integrity and professionalism in the practice of his or her profession, trade or occupation, and maintain records of such inquiry and its results;¹¹ and

(7) compliance with the foregoing conditions is set forth in writing.¹²

Issue: The provision requires nonlawyers agree to “undertake to conform their conduct.” Should the provision provide that the nonlawyers agree “to conform their conduct.” In other words, we’re not asking you to attempt to conform your conduct but telling you that you must agree to do so.

⁹ Subparagraph (b)(4) clarifies that managerial and supervisory lawyers are still responsible for the nonlawyers, even though they might be co-owners in the firm. There could be circumstances where a particular nonlawyer might have a larger ownership share in the firm. Nevertheless, the lawyer would still ultimately be responsible for that nonlawyer as if the nonlawyer were a nonmanagerial partner/shareholder or a subordinate lawyer.

Issue: This concept probably needs to be fleshed out in a comment to the rule.

¹⁰ Subparagraph (b)(5) is probably the most controversial provision, at least from the perspective of nonlawyers. The apparent intention here is to limit outside influence on the independent professional judgment of lawyers. Exercising independent judgment on behalf of clients is a core duty of the legal profession. This provision attempts to limit the financial pressures that might arise when majority stakeholders in a firm attempt to influence lawyers to take a position at odds with the client’s interest.

Issue: We should discuss this provision. The kind of limitations on ownership might be a first small step that will more likely garner acceptance than would a proposal for a full-blown MDP.

See also note 7, above.

¹¹ Subparagraph (b)(6) appears to require that the lawyers in the firm conduct some sort of background check on the nonlawyers.

Issue: Is this overkill? Is there some other way of doing this? For example, if the nonlawyer is a member of a professional organization and in good standing, would a background check be necessary.

Regardless, if this provision were to be retained, it would likely require a comment to flesh out the kind of effort the lawyers in the firm would have to make.

¹² Subparagraph (b)(7) simply requires that the firm keep a written record to demonstrate that it has complied with all the requirements of paragraph (b).

(c) A lawyer shall not permit a person* who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's independent professional judgment or interfere with the lawyer-client relationship in rendering legal services.

(d)¹³ A ~~lawyer shall not practice with or in the form of a professional corporation or other organization authorized to practice law for a profit if:~~

~~(1) a nonlawyer owns any interest in it, except that a fiduciary representative of a lawyer's estate may hold the lawyer's stock or other interest for a reasonable* time during administration;~~

~~(2) a nonlawyer is a director or officer of the corporation or occupies a position of similar responsibility in any other form of organization; or~~

~~(3) a nonlawyer has the right or authority to direct or control the lawyer's independent professional judgment.~~

(e) The Board of Trustees of the State Bar shall formulate and adopt Minimum Standards for Lawyer Referral Services, which, as from time to time amended, shall be binding on lawyers. A lawyer shall not accept a referral from, or otherwise participate in, a lawyer referral service unless it complies with such Minimum Standards for Lawyer Referral Services.

(f) A lawyer shall not practice with or in the form of a nonprofit legal aid, mutual benefit or advocacy group if the nonprofit organization allows any third person* to interfere with the lawyer's independent professional judgment, or with the lawyer-client relationship, or allows or aids any person* to practice law in violation of these rules or the State Bar Act.

Comment

[1] Paragraph (a) does not prohibit a lawyer or law firm* from paying a bonus to or otherwise compensating a nonlawyer employee from general revenues received for legal services, provided the arrangement does not interfere with the independent professional judgment of the lawyer or lawyers in the firm* and does not violate these rules or the State Bar Act. However, a nonlawyer employee's bonus or other form of compensation may not be based on a percentage or share of fees in specific cases or legal matters.

[2] Paragraph (a) also does not prohibit payment to a nonlawyer third-party for goods and services provided to a lawyer or law firm;* however, the compensation to a nonlawyer third-party may not be determined as a percentage or share of the lawyer's or law firm's overall revenues or tied to fees in particular cases or legal matters. A lawyer may pay to a nonlawyer third-party, such as a collection agency, a percentage of past due or delinquent fees in concluded matters that the third-party collects on the lawyer's behalf.

Issue: Question whether this provision would have a similar effect as a lawyer failing to keep adequate trust account records, e.g., failure to keep adequate records is a violation in itself and even if records are kept, but are inadequate, that is also a violation and evidence of the violation.

¹³ Because the prohibitions in former paragraphs (b) and (d) have been subsumed in new paragraph (b), former paragraph (d) is deleted except for former subparagraph (d)(1) regarding the fiduciary of a lawyer's estate.

[3] Paragraph (a)(5) permits a lawyer to share with or pay court-awarded legal fees to nonprofit legal aid, mutual benefit, and advocacy groups that are not engaged in the unauthorized practice of law. (See *Frye v. Tenderloin Housing Clinic, Inc.* (2006) 38 Cal.4th 23 [40 Cal.Rptr.3d 221]; see also rule 6.3.) Regarding a lawyer's contribution of legal fees to a legal services organization, see rule 1.0, Comment [5] on financial support for programs providing pro bono legal services.

[4] This rule is not intended to affect case law regarding the relationship between insurers and lawyers providing legal services to insureds. (See, e.g., *Gafcon, Inc. v. Ponsor Associates* (2002) 98 Cal.App.4th 1388 [120 Cal.Rptr.2d 392].)

[5] Paragraph (c) is not intended to alter or diminish a lawyer's obligations under rule 1.8.6 (Compensation from One Other Than Client).