UTAH SUPREME COURT AD HOC COMMITTEE

REGULATORY REFORM
Nick Stiles, Co-Chair
Maryt Fredrickson, Co-Chair
Workgroup Meeting: Rule 5.4
December 5, 2025
12:00 – 1:00
Virtual & In-person Meeting
In person: Education Room, Matheson
Meeting LINK

1. Welcome and Approval of November Meeting Minutes (Tab 2)

2. Follow-up on November's Action Items
    a. Connor's report on his meeting with Marquita Brazil, the Program Director of Arizona's ABS Committee
    b. Workshop Proposed Rule Draft (Tab 3) (see also supporting reference material in Tab 4)

3. Deliverables and timeline
    a. Set actionable goals for the workgroup for the next 2 months to prepare a preliminary report.

Tab 1

Current 5.4 Scope

Rule 5.4 Workgroup	
• Research pros and cons of allowing lawyers to partner or share fees with nonlawyers, including any multijurisdictional implications. • Analyze lesson learned from Sandbox ABS entities as well as Arizona's ABS program. • Consider recommendations from experts on legal regulation.	• Examine rule 5.4 language from other states. • Develop a recommendation on whether rule 5.4 should be amended. • Draft proposed rule changes, if any.

Tab 2

Meeting Minutes
Utah Supreme Court's Ad Hoc Committee on Regulatory Reform
Rule 5.4 Meeting Minutes
Friday, November 7, 2025
12:00 – 1:00
Virtual

The Rule 5.4 workgroup met for their first regulatory reform meeting without the AI/Legal Tech working group.

The working group accepted the minutes from the previous joint AI and 5.4 meeting with minor revisions.

Scope

- The Rule 5.4 workgroup will seek to expand or amend Rule 5.4, not eliminate it.
- The workgroup isn't likely looking to recommend an ABS regime like Arizona's. Where Arizona's ABS program is business-centered, Utah's aims to be access-to-justice centered.
- While discussions over AI/Legal Tech will fall to its respective workgroup, that will remain a relevant topic to revisit for the 5.4 workgroup. At some point, the two groups might reintegrate.

Historic learning points

- The Sandbox aimed for innovation. Entities are categories as low-, medium-, and high-innovation.
- There are currently no high-innovation entities in the Sandbox.
- Past discussions contemplated allowing one-stop shops, like accountants and tax lawyers joining to offer combined services.
- Early Sandbox/Standing Order 15 efforts resulted in ABS entities not based in Utah, not serving Utah consumers, and focused more on consumers who could afford a traditional legal services model. There were also lessons learned from entities using the removal of 5.4 restrictions as a source of outside capital for advertising and aggressive marketing/solicitation.

- The working group is aware of the different rules governing the regulation of businesses and the regulation of the practice of law. By constitution and statute, the Supreme Court regulates the practice of law. *See* UTAH CONST. art VIII, § 8; UTAH CODE § 76-17-201.

Jurisdiction Comparison

- The workgroup reviewed Arizona, DC, Puerto Rico, and New York.
- Arizona has taken the most extreme approach by eliminating Rule 5.4.
- DC has the best case study of allowing fee sharing (since 1991); fee sharing was likely permitted for lobbyists and those with multi-jurisdictional practices. But the D.C. rule may be too limited for what this group aims to achieve.
- Puerto Rico is the newest jurisdiction to amend Rule 5.4 (June 2025), and their focus is on pro bono legal services/access to justice. That rule goes in to effect in January 2026. There was a dissent that opposed the new rule.
- New York has initiated workgroups and task forces, but has yet to make any major changes.
- Key features and common denominators:
    - Nonlawyers are still beholden to the same ethical standards as lawyers.
    - Fee-sharing entities must provide legal services.

Other considerations

- Education: for lawyers and for nonlawyers. Ex: when a non-lawyer takes management of a law firm and what that means for a non-attorney. Any CLE requirements? If so, where to house that.
- Enforcement
- Designing metrics for measuring success or impacts, with any rule amendments, at an early stage or drafting, not left for later to add in.

Next Steps

- The group will consider potential pitfalls and guardrails to address them. This may be something to map out with a spreadsheet, of things to include and things to not include. Factors to consider include:
    - Motivation by strictly profit-driven means
    - Improper solicitation of services
    - Quality of services
    - Adherence to ethical standards
    - CLE requirements
    - Enforcement mechanisms
    - Requiring on-staff compliance attorneys for fee-sharing entities

    - Success metrics to see if what we're doing actually helps us achieve those objectives
    - Multi-jurisdictional concerns
- Maryt will begin drafting 5.4 language.
- Connor will look into impact studies in these jurisdictions and other available data.
- Connor will continue to communicate with the other jurisdictions and connections Andrea, Alyson, and the other group members have to those jurisdictions.

Tab 3

Rule 5.4. Professional independence of a lawyer.

(a) A lawyer may provide legal services pursuant to this Rule only if there is at all times no interference with the lawyer's:

(1) professional independence of judgment,

(2) duty of loyalty to a client, and

(3) protection of client confidences.

(b) A lawyer may permit a person to recommend, retain, or pay the lawyer to render legal services for another.

(c) Referral fees are prohibited.

(d) Fee sharing ~~with a~~between lawyers is permissible only as provided in Rule 5.8.

(e) A lawyer or law firm may share legal fees with a nonlawyer only if: [*This may need amended based on how 5.4(f) turns out, so the two do not conflict.*]

~~(1) the fee to be shared is reasonable and the fee-sharing arrangement has been authorized as required by Utah Supreme Court Standing Order No. 15;~~

(1~~2~~) the lawyer or law firm provides written notice to the affected client and, if applicable, to any other person paying the legal fees;

(2~~3~~) the written notice describes the relationship with the nonlawyer, including the fact of the fee-sharing arrangement; and

(3~~4~~) the lawyer or law firm provides the written notice before accepting representation or before sharing fees from an existing client.

(f) A lawyer may practice law in a partnership or other form of organization in which an ownership interest is held, or managerial authority is exercised, by a nonlawyer who performs professional services which assist the organization in providing legal services to clients, but only if:~~with nonlawyers, or in an organization, including a partnership, in which a financial interest is held or managerial authority is exercised by one or more persons who are nonlawyers, provided that the nonlawyers or the organization has been authorized as required by Utah Supreme Court Standing Order No. 15 and provided the lawyer:~~

DC rule

(1) The partnership or organization has as its sole purpose providing legal services to clients [*Puerto Rico limited this to just free legal services to indigent persons--*

="The law office provides for the collective fulfillment of the responsibility to offer free legal services to indigent persons"];__

(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.

Puerto Rico rule

(5) Every non-lawyer with an ownership interest must ensure that the office is operated only by persons admitted to the legal profession in Puerto Rico. The legal practitioner must represent the non-lawyer owner in exercising all voting rights and all other matters related to the law office. They must also ensure compliance with the rules of professional responsibility and notify the Supreme Court once the arrangement begins. By January 15 of each year, they must file with the Clerk of the Supreme Court of Puerto Rico an affidavit stating the number of attorneys in the firm, the dates and amounts of all investments made by the non-lawyer owner, and the profits received by that person in the previous calendar year;

(6) Neither the non-lawyer owner nor any designated agent shall engage in the unauthorized practice of law. Additionally, the only value provided by the non-lawyer owner in exchange for their ownership interest must be money, and the owner or their agents shall not provide any services to the law office, including but not limited to marketing services;

(7) The non-lawyer owner shall not interfere with the independent professional judgment of the legal practitioner or the attorney-client relationship;

(8) Information relating to the representation of a client shall be protected as required by Rule 1.6;

(9) The arrangement described in subsection (2) shall not contravene Rule 1.5;

(10)The legal practitioner informs the client that an ownership interest in the law office is held by a non-lawyer; and

(11) Non-lawyer owners may acquire no more than 49% of the shares of the law office.

~~(1) before accepting a representation, provides written notice to a prospective client that one or more nonlawyers holds a financial interest in the organization in which the lawyer practices or that one or more nonlawyers exercises managerial authority over the lawyer; and~~

~~(2) sets forth in writing to a client the financial and managerial structure of the organization in which the lawyer practices.~~

Comment

[1] The provisions of this Rule are to protect the lawyer's professional independence of judgment, to assure that the lawyer is loyal to the needs of the client, and to protect clients from the disclosure of their confidential information. Where someone other than the client pays the lawyer's fee or salary, manages the lawyer's work, or recommends retention of the lawyer, that arrangement does not modify the lawyer's obligation to the client. As stated in paragraph (a), such arrangements must not interfere with the lawyer's professional judgment. See also Rule 1.8(f) (lawyer may accept compensation from a third party as long as there is no interference with the lawyer's independent professional judgment and the client gives informed consent). This Rule does not lessen a lawyer's obligation to adhere to the Rules of Professional Conduct and does not authorize a nonlawyer to practice law by virtue of being in a business relationship with a lawyer. It may be impossible for a lawyer to work in a firm where a nonlawyer owner or manager has a duty to disclose client information to third parties, as the lawyer's duty to maintain client confidences would be compromised.

[2] The Rule also expresses traditional limitations on permitting a third party to direct or regulate the lawyer's professional judgment in rendering legal services to another. See also Rule 1.8(f) (lawyer may accept compensation from a third party as long as there is no interference with the lawyer's independent professional judgment and the client gives informed consent).

[3] Fee sharing and referral fees are defined in Rule 1.0.

[4] Before engaging in any fee sharing arrangement, lawyers should be familiar with Utah law regarding prohibitions on kickbacks.

[5] Paragraph (e) permits individual lawyers or law firms to enter into business or employment relationships with nonlawyers, whether through nonlawyer ownership or investment in a law practice, joint venture, or through employment by a nonlawyer owned entity. In each instance, the nonlawyer owned entity must be approved by the Utah Supreme Court for authorization under Standing Order No. 15.

[6] Add a comment about the new additions.

[7~~6~~] This rule differs from the ABA Model Rule.

Effective date:

Tab 4

DC Rule 5.4

Rules of Professional Conduct

Rule 5.4: Professional Independence of a Lawyer

(a) A lawyer or law firm shall not share legal fees with a nonlawyer, except that:

(1) An agreement by a lawyer with the lawyer's firm, partner, or associate may provide for the payment of money, 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 who undertakes to complete unfinished legal business of a deceased lawyer may pay to the estate of the deceased lawyer that proportion of the total compensation which fairly represents the services rendered by the deceased lawyer. A lawyer who purchases the practice of a deceased, disabled, or disappeared lawyer may, pursuant to the provisions of Rule 1.17, pay to the estate or other representative of that lawyer the agreed-upon purchase price.

(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;

(4) Sharing of fees is permitted in a partnership or other form of organization which meets the requirements of paragraph (b); and

(5) A lawyer may share legal fees, whether awarded by a tribunal or received in settlement of a matter, with a nonprofit organization that employed, retained, or recommended employment of the lawyer in the matter and that qualifies under Section 501(c)(3) of the Internal Revenue Code.

(b) 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.

(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 professional judgment in rendering such legal services.

Comment

[1] The provisions of this rule express traditional limitations on sharing fees with nonlawyers. (On sharing fees among lawyers not in the same firm, *see* Rule 1.5(e).) These limitations are to protect the lawyer's professional independence of judgment. Where someone other than the client pays the

lawyer's fee or salary, or recommends employment of the lawyer, that arrangement does not modify the lawyer's obligation to the client. As stated in paragraph (c), such arrangements should not interfere with the lawyer's professional judgment.

[2] Traditionally, the canons of legal ethics and disciplinary rules prohibited lawyers from practicing law in a partnership that includes nonlawyers or in any other organization where a nonlawyer is a shareholder, director, or officer. Notwithstanding these strictures, the profession implicitly recognized exceptions for lawyers who work for corporate law departments, insurance companies, and legal service organizations.

[3] As the demand increased for a broad range of professional services from a single source, lawyers employed professionals from other disciplines to work for them. So long as the nonlawyers remained employees of the lawyers, these relationships did not violate the disciplinary rules. However, when lawyers and nonlawyers considered forming partnerships and professional corporations to provide a combination of legal and other services to the public, they faced serious obstacles under the former rules.

[4] This rule rejects an absolute prohibition against lawyers and nonlawyers joining together to provide collaborative services, but continues to impose traditional ethical requirements with respect to the organization thus created. Thus, a lawyer may practice law in an organization where nonlawyers hold a financial interest or exercise managerial authority, but only if the conditions set forth in subparagraphs (b)(1), (b)(2), and (b)(3) are satisfied, and pursuant to subparagraph (b)(4), satisfaction of these conditions is set forth in a written instrument. The requirement of a writing helps ensure that these important conditions are not overlooked in establishing the organizational structure of entities in which nonlawyers enjoy an ownership or managerial role equivalent to that of a partner in a traditional law firm.

[5] Nonlawyer participants under Rule 5.4 ought not be confused with nonlawyer assistants under Rule 5.3. Nonlawyer participants are persons having managerial authority or financial interests in organizations that provide legal services. Within such organizations, lawyers with financial interests or managerial authority are held responsible for ethical misconduct by nonlawyer participants about which the lawyers know or reasonably should know. This is the same standard of liability contemplated by Rule 5.1, regarding the responsibilities of lawyers with direct supervisory authority over other lawyers.

[6] Nonlawyer assistants under Rule 5.3 do not have managerial authority or financial interests in the organization. Lawyers having direct supervisory authority over nonlawyer assistants are held responsible only for ethical misconduct by assistants about which the lawyers actually know.

[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. For example, the rule permits economists to work in a firm with antitrust or public utility practitioners, psychologists or psychiatric social workers to work with family law practitioners to assist in counseling clients, nonlawyer lobbyists to work with lawyers who perform legislative services, certified public accountants to work in conjunction with tax lawyers or others who use accountants' services in performing legal services, and professional managers to serve as office managers, executive directors, or in similar positions. In all of these situations, the professionals may be given financial interests or managerial responsibility, so long as

all of the requirements of paragraph (c) are met.

[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.

[9] The term "individual" in subparagraph (b) is not intended to preclude the participation in a law firm or other organization by an individual professional corporation in the same manner as lawyers who have incorporated as a professional corporation currently participate in partnerships that include professional corporations.

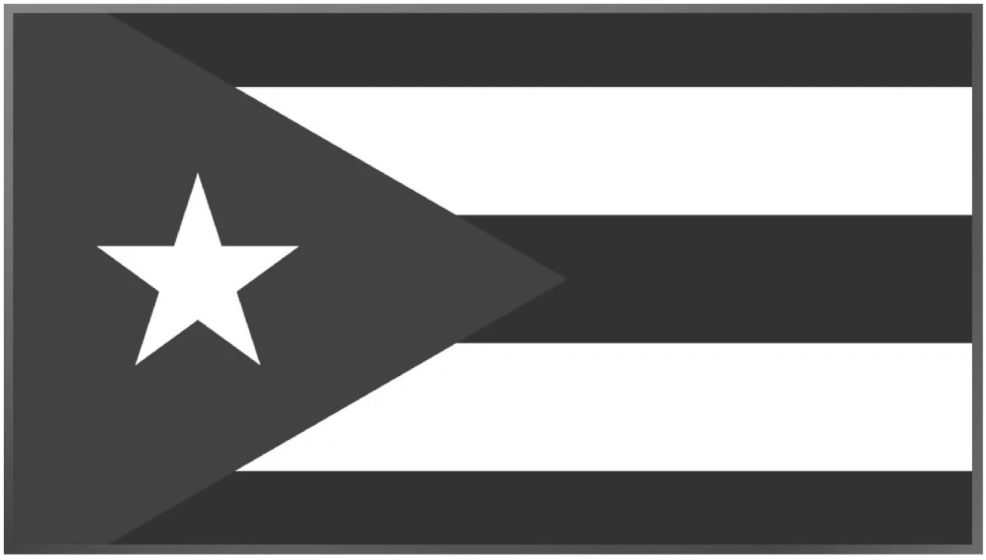
[10] Some sharing of fees is likely to occur in the kinds of organizations permitted by paragraph (b). Subparagraph (a)(4) makes it clear that such fee sharing is not prohibited.

[11] Subparagraph (a)(5) permits a lawyer to share legal fees with a nonprofit organization that employed, retained, or recommended employment of the lawyer in the matter. A lawyer may decide to contribute all or part of legal fees recovered from the opposing party to a nonprofit organization. Such a contribution may or may not involve fee-splitting, but when it does, the prospect that the organization will obtain all or part of the lawyer's fees does not inherently compromise the lawyer's professional independence, whether the lawyer is employed by the organization or was only retained or recommended by it. A lawyer who has agreed to share legal fees with such an organization remains obligated to exercise professional judgment solely in the client's best interests. Moreover, fee-splitting in these circumstances may promote the financial viability of such nonprofit organizations and facilitate their public interest mission. Unlike the corresponding provision of Model Rule 5.4(a)(5), this provision is not limited to sharing of fees awarded by a court because that restriction would significantly interfere with settlement of cases, without significantly advancing the purpose of the exception. To prevent abuse of this broader exception, it applies only if the nonprofit organization qualifies under Section 501(c)(3) of the Internal Revenue Code.

Puerto Rico Rule 5.4(b)

LawSites
Tracking Technology and Innovation for the Legal Profession

Puerto Rico Allows Non-Lawyer Ownership of Law Firms



*By **Bob Ambrogi** on June 19, 2025*

I **wrote yesterday** about the Puerto Rico Supreme Court's adoption of the duty of technology competence, done as part of its promulgation of new rules of professional conduct to replace a code of ethics that had governed lawyers' professional conduct in Puerto Rico since 1970.

While Puerto Rico modeled its new **Rules of Professional Conduct** on the **American Bar Association's Model Rules**, it diverged from the ABA in two significant respects.

One, as I explained in yesterday's post, was to add a separate rule devoted to the duty of technology competence, rather than address the duty through a comment to the general rule on competence, as the ABA does.

The other — and potentially more significant — divergence was to revise Rule 5.4 to allow non-lawyers to have ownership interests in law firms.

Until now, only Arizona and the District of Columbia have allowed non-lawyer ownership of law firms. D.C. has allowed this since 1991, and Arizona **eliminated the ban on non-lawyer ownership** in 2020.

Utah also allows non-lawyer ownership, but only of entities approved within **its regulatory "sandbox" program**.

Puerto Rico's Rule 5.4

Puerto Rico's new conduct rules retain Rule 5.4's general prohibition against a lawyer sharing fees with a non-lawyer. But with respect to ownership, it adds a new section (b) that reads as follows (translation via ChatGPT):

> **(b)** A legal practitioner may practice in a law office where an ownership interest is held by a non-lawyer only if:
>
> 1. The law office provides for the collective fulfillment of the responsibility to offer free legal services to indigent persons;
> 2. Every non-lawyer with an ownership interest must ensure that the office is operated only by persons admitted to the legal profession in Puerto Rico. The legal practitioner must represent the non-lawyer owner in exercising all voting rights and all other matters related to the law office. They must also ensure compliance with the rules of professional responsibility and notify the Supreme Court once the arrangement begins. By January 15 of each year, they must file with the Clerk of the Supreme Court of Puerto Rico an affidavit stating the number of attorneys in the firm, the dates and amounts of all investments made by the non-lawyer owner, and the profits received by that person in the previous calendar year;
> 3. Neither the non-lawyer owner nor any designated agent shall engage in the unauthorized practice of law. Additionally, the only value provided by the non-lawyer owner in exchange for their ownership interest must be money, and the owner or their agents shall not provide any services to the law office, including but not limited to marketing services;
> 4. The non-lawyer owner shall not interfere with the independent professional judgment of the legal practitioner or the attorney-client relationship;
> 5. Information relating to the representation of a client shall be protected as required by Rule 1.6;
> 6. The arrangement described in subsection (2) shall not contravene Rule 1.5;
> 7. The legal practitioner informs the client that an ownership interest in the law office is held by a non-lawyer; and
> 8. Non-lawyer owners may acquire no more than 49% of the shares of the law office.

Not Supported By Rules Committee

Although the overall development of the new conduct rules was accomplished through the work of a special, court-appointed committee, that committee had not recommended this change to Rule 5.4.

The Supreme Court did not provide a rationale or explanation of its decision to change the rule on non-lawyer ownership. However, it did say that it will conduct an evaluation of the new rule's effectiveness three years after it takes effect.

The court assigned the task of conducting that assessment to the same committee that drafted the recommended rules, now renamed as the Committee on Rules of Professional Conduct.

One Justice Dissented

While the court did not elaborate on its reasons for adopting the new Rule 5.4, one member of the court, **Associate Justice Luis F. Estrella Martínez**, wrote a detailed dissent discussing various components of the new conduct rules, including Rule 5.4.

Justice Estrella Martínez wrote that he did not agree with this change "due to the potentially harmful consequences it may bring."

(Here again, translations are via ChatGPT.)

"[A]llowing this source of funding in Puerto Rico law firms could represent a significant risk to the autonomy and independence of the professional judgment of the attorneys within them," he wrote.

Justice Estrella Martínez expressed concern that investors in law firms would typically be driven by purely economic interests, "which does not guarantee an improvement in the availability or quality of legal services for the people of Puerto Rico."

He also raised the concern that the court lacks disciplinary authority over investors who are not attorneys. "As a result, such investors could influence legal decisions without being subject to the same ethical and professional responsibilities as attorneys," he wrote.

While acknowledging the models adopted in Arizona, D.C., and Utah, he thought Puerto Rico should have waited to observe their experiences before adopting this change.

"So far, we have not seen these sectors partner with law firms to litigate on behalf of the environment or vulnerable populations," he wrote.

"We must not allow the principle of access to justice to be used as a pretext to perpetuate inequality or to excessively commercialize the practice of law."

(Here is the full, translated text of the portion of the dissent that addresses Rule 5.4.)

Bob Ambrogi

Bob is a lawyer, veteran legal journalist, and award-winning blogger and podcaster. In 2011, he was named to the inaugural Fastcase 50, honoring "the law's smartest, most courageous innovators, techies, visionaries and leaders." Earlier in his career, he was editor-in-chief of several legal publications, including The National Law Journal, and editorial director of ALM's Litigation Services Division.

Blog Post

Goodbye Rule 5.4: Legal Ethics Change in Arizona

By Joel Truett

At the beginning of this year Arizona Ethics Rule 5.4 formally ended. The Arizona Supreme Court announced the elimination of the rule last year, and has since gone into effect on January 1, 2021. The rule prohibited partnerships between lawyers and non-lawyers working together where any part of their services involved the practice of law.

In the United States, model ethics rules for lawyers are proposed by the American Bar Association, but the laws governing lawyers are enacted on a state-by-state basis. This means that the rules about how lawyers can behave change from one state to the next. The provisions enacted in Rule 5.4, however, were uniformly accepted in every state until this year. This makes Arizona the first state to cast off its restrictions on attorney/non-attorney partnerships.

The American Bar Association's Model Rule 5.4 cites the protection of a lawyer's professional judgement as the justification for the rule. The idea being that if a lawyer is working with a non-lawyer in providing legal services, the lawyer should ideally be making decisions based on the best interests of their client, without interference from any outside actor that could negatively influence the advice the lawyer gives.

While that may sound reasonable at first, the rule may at best be considered an unwieldy attempt to prevent bad behavior that is already illegal apart from the rule. At its worst, the rule serves as an artificial barrier restricting competition in the field of law in a self-serving scheme that benefits established lawyers while harming clients looking for new services. For those reasons, Arizona was right to eliminate the rule, and other states should follow suit.

To be charitable, Rule 5.4 takes a heavy-handed approach to solving a problem that could be addressed by other means. In its current form, as worded on the ABA's website, the rule is an absolute prohibition on partnerships between lawyers and non-lawyers in business activities that involve the provision of legal advice. Instead of allowing for the punishment of wrongdoing when or where it occurs, the rule instead elects to completely prevent potentially beneficial forms of economic activity on the mere possibility that some nondescript harm may result from it.

While a state bar may have very legitimate reasons for wanting to prevent obstructions to lawyer's professional judgement, a rule completely banning partnerships, as does rule 5.4, makes for an over-restrictive means to achieve that end. The rules already have plenty of guidelines about how a lawyer must behave when giving legal advice. These guidelines serve the stated purposes of 5.4 without imposing such burdensome restrictions. For example, lawyers must act in the fiduciary interest of their clients, and already have duties to place client interests above their own. The elimination of Rule 5.4 does nothing to prevent the enforcement mechanisms present in other ethical rules from applying. Consequently, if a lawyer in Arizona working under the law as it is today happens to place the business interests of their non-lawyer partner above their client's interests, that lawyer will be in violation of ethical rules, and will be subject to state penalties. The law therefore continues to operate as it should.

Moreover, Rule 5.4 reduces client options when selecting legal and consulting services. There are significant potential benefits available to clients in the provision of legal services by a firm that combines the skills of lawyers with those of non-lawyers. While lawyers are (hopefully) well-educated and capable individuals, no person can embody perfection in all the multitude of skills that a client may want when receiving a consultation. Professionals in other fields have valuable insights that may be usefully amplified if used in conjunction with legal services. Easing Rule 5.4 will allow for the creation of new businesses to provide these insights, while also increasing public access to legal resources overall.

Lastly, the elimination of Rule 5.4 does not mean the end of regulation of legal practice in Arizona. Business entities providing joint services must still apply for a license to do so in the state. The Supreme Court of Arizona approved its first two applicants this March.

At its best, the elimination of Rule 5.4 will provide Arizonans with access to new and unique legal services that can't be replicated in any other state in the nation. While Arizona may be the first state to eliminate Rule 5.4, it is not alone in the country or in the world in doing so. Washington D.C. permits non-lawyer ownership of law practices, and England has allowed the same since 2007. It is a welcome sight to see Arizona join those jurisdictions in removing restrictions on legal partnerships.

5.4 workaround via existing rule

ABAJOURNAL

LAW FIRMS

McDermott acknowledges 'fielding inbound interest' from outside investors as it listens to new ideas

BY DEBRA CASSENS WEISS (HTTPS://WWW.ABAJOURNAL.COM/AUTHORS/4/)

NOVEMBER 18, 2025, 9:03 AM CST

McDermott Will & Schulte said it is "fielding inbound interest" from outside investors after the Financial Times reported that the law firm is considering splitting off its

McDermott Will & Schulte said it is "fielding inbound interest" from outside investors after the Financial Times (https://www.ft.com/content/3a9d3c27-a692-4389-961c-f4893a80b3b7) reported that the law firm is considering splitting off its back-office work into a managed service

back-office work into a managed service organization in which private equity could own a stake. (Image from Shutterstock)

organization in which private equity could own a stake.

McDermott chairman Ira Coleman told Law360 (https://www.law360.com/articles/2409986), Law.com (https://www.law.com/americanlawyer/2025/11/12/mcdermott-considers-taking-on-private-equity-investment) and Bloomberg Law (here (https://news.bloomberglaw.com/business-and-practice/mcdermott-will-schulte-considers-outside-investment-in-firm) and here (https://news.bloomberglaw.com/business-and-practice/mcdermotts-outside-investor-talks-augur-big-law-transformation)) that it has been approached, although "this is all very preliminary."

"As one of the fastest-growing, most successful modern law firms, we are constantly approached and we always listen to new ideas," Coleman said. "This is how we find the best opportunities to attract and retain the industry's top talent and what our clients expect from us."

Splitting off back-office operations, such as billing, marketing, information technology and human resources would avoid issues created by ethics rules that ban fee sharing and nonlawyer ownership of firms, Law360 explains. The model is already in use by medical practices and accounting companies, according to the Financial Times and Law.com.

Litigation funder Burford Capital has invested in U.K. firms with similar structures, according to Law360. Burford chief development officer Travis Lenkner said other firms are also considering the idea.

"From our conversations with leading global firms, it's clear that larger, more sophisticated firms are actively exploring how to use MSOs to secure long-term competitiveness," Lenkner told Law360.

Private equity company Renovus recently announced that it has acquired three organizations that provide back-office services to the legal sector, Bloomberg Law reports. The three organizations will be combined into one company that will have outsourcing contracts with a majority of the nation's 200 top-grossing firms, according to Renovus managing director Lee Minkoff.

"All major law firms are having these conversations," Minkoff said. "They're not saying we should do it, they're saying, well, we need to learn what it means and what it looks like and what others are doing."

But legal sector analyst Jordan Furlong warned that lawyers have to be aware of the implications.

"This is not getting another line of credit from your bank," Furlong told Bloomberg Law. "You are severing a significant chunk of your law firm and handing it over to a third party. That is not a decision I would take lightly if I were running a law firm."

Write a letter to the editor, share a story tip or update, or report an error. *(/contact?referrer=https://www.abajournal.com/news/article/mcdermott-acknowledges-fielding-inbound-interest-from-outside-investors-as-it-listens-to-new-ideas)*

Dissent on Puerto Rico's 5.4 rule

CHAPTER V - MATTERS RELATED TO THE PRACTICE OF LAW AND LAW FIRMS

Rule 5.4. Professional independence of the lawyer

The Rule approved by this Court sets forth the following:

(a) A person who practices law or a law firm shall not share legal fees with a person not authorized to practice law, except that:

1. They may enter into an agreement with their law firm, partners, or associates to provide for the payment of money to their estate or to specific individuals for a reasonable period of time after their death;
2. They may purchase the law practice of a deceased, incapacitated, or judicially declared absent lawyer pursuant to Rule 1.17, through payment of the agreed purchase price to the estate or legal representative of that lawyer;
3. They may include non-lawyer employees in a compensation or retirement plan, even if the plan is partially or entirely based on a profit-sharing arrangement;
4. They may share court-awarded fees with a nonprofit organization that hires, employs, or recommends them to handle a matter; and
5. They may share profits with a non-lawyer owner of a law firm, provided they comply with subsection (b) of this rule.

(b) A person who practices law may do so in a law firm in which an ownership interest is held by a person who is not a lawyer only if:

1. The law firm provides for the collective responsibility of offering free legal services to indigent persons;
2. Any non-lawyer who holds an ownership interest in the law firm must ensure that the firm is operated solely by an attorney admitted to practice law in Puerto Rico. The lawyer must represent the non-lawyer owner in exercising any voting rights and in all matters related to the firm. The lawyer must ensure compliance with professional responsibility rules and notify the Supreme Court once the agreement begins. By January 15 of each year, they must file a sworn statement with the Clerk of the Supreme Court of Puerto Rico detailing the number of lawyers in the firm, the dates and amounts of all investments made by the non-lawyer owner, and the earnings received by that person in the previous calendar year;
3. The non-lawyer owner or their agent shall not engage in the unauthorized practice of law. Moreover, the only contribution from the non-lawyer owner to the firm must be monetary; they or their agents may not provide any services to the firm, including but not limited to marketing services;
4. There shall be no interference by the non-lawyer owner with the professional judgment of the lawyer or with the attorney-client relationship;
5. Client-related information shall be protected as required by Rule 1.6;
6. The agreement in subsection (2) does not violate Rule 1.5;
7. The lawyer must inform the client that a share of the law firm is owned by a non-lawyer;
8. Non-lawyer owners may not hold more than 49% of the firm's equity.

(c) A lawyer shall not allow a person who recommends, employs, or pays them to provide legal services for another to direct or control their professional judgment in rendering such services.

(d) The Supreme Court shall evaluate the effectiveness of subsection (b) of this rule no later than three years after it goes into effect.

As can be seen, this provision allows attorneys to share equity in a law firm with individuals who are not authorized to practice law in Puerto Rico. In other words, this rule allows non-lawyers to financially invest in law firms in the country. Given the above, I am not in agreement with the implementation of this rule due to the potentially harmful consequences it may bring.

First, allowing this source of funding in Puerto Rico law firms could represent a significant risk to the autonomy and independence of the professional judgment of the attorneys within them. In fact, this was one of the main concerns of both the Special Committee and the Secretariat, which did not recommend the approval of this regulatory provision after its draft departed from the ABA Model Rule 5.4.

In the past, we have rejected third-party interference in the decisions, strategies, or advice provided by the attorney responsible for representing someone who comes to a law office. For example, investors not subject to professional ethical standards might be inclined to pressure for a settlement that favors their interest in fee-sharing, rather than continuing litigation to achieve the best outcome for the client. Therefore, this could be interpreted as interference in the legal decisions, strategies, or advice related to a particular case or client.

Additionally, according to findings from the Secretariat, in practice, investors are typically driven by purely economic interests, which does not guarantee an improvement in the availability or quality of legal services for the people of Puerto Rico. In fact, arguments favoring a more flexible Model Rule 5.4 may distract from more effective strategies to improve access to justice. In our jurisdiction, the Regulation for the Assignment of Court-Appointed Attorneys in Puerto Rico, as well as organizations that provide free legal services and the Access to Justice Fund (created by law), promote and ensure access to justice without economic motivations. These mechanisms do indeed facilitate and guarantee access to justice free from financial interests.

Another concern reinforcing my position is the even more troubling fact that we lack disciplinary authority over investors who are not attorneys in Puerto Rico. In my view, this situation creates a gap in oversight and accountability because, although Rule 5.4 establishes criteria for allowing third-party investment in law firms, there is no built-in mechanism to regulate their disciplinary conduct or ethical boundaries. As a result, such investors could influence legal decisions without being subject to the same ethical and professional responsibilities as attorneys. This could create conflicts of interest and put the quality of legal services provided to the public at risk.

Moreover, adopting this rule distances us from the model established by the ABA, and therefore from the Special Committee's mandate to harmonize our ethical rules with the ABA Model Rules. See *In re Proy. Conducta Prof. y Regl. Disc.*, 189 DPR 1032 (2013). The ABA currently maintains its stance that lawyers and law firms should neither share fees with non-lawyers nor allow non-lawyers to invest in law firms. In fact, the vast

majority of U.S. jurisdictions continue to apply ethical provisions similar to ABA Model Rule 5.4, which addresses the same subject as our Rule 5.4.

That said, I acknowledge that the jurisdictions of Arizona and the District of Columbia modified their Rule 5.4 to lift the absolute ban on lawyers sharing equity in a law firm with non-lawyers. North Carolina presents a particular situation by allowing a non-lawyer to hold a leadership or officer position in a legal services corporation, as long as they do not have the authority to direct or control the conduct of the attorneys in the firm. Meanwhile, Utah implemented a pilot program in August 2020, valid through 2027, to assess the feasibility of easing the restriction imposed by Rule 5.4. However, the preliminary results of this experience in Arizona, D.C., and Utah's pilot program have not shown evidence of improved access to justice; instead, they confirm that investors are in fact driven by purely economic interests, as previously indicated.

For these reasons, I agreed with the initial draft proposed by the Special Committee and the Secretariat, which was not approved by a majority of this Court. Specifically, the rule read as follows:

> **(a)** A person practicing law or a law firm shall not share legal fees with a non-lawyer, except that:
>
> 1. They may enter into an agreement with their law firm, partners, or associates to provide for the payment of money to their estate or to specified individuals over a reasonable period of time after their death;
> 2. They may purchase the law practice of a deceased, incapacitated, or judicially declared absent lawyer in accordance with Rule 1.17, by

paying the agreed purchase price to the estate or another representative of the lawyer;

3. They may include non-lawyer employees in a compensation or retirement plan, even if the plan is based in whole or in part on a profit-sharing agreement;
4. They may share court-awarded fees with a nonprofit organization that retained, employed, or recommended them to handle the matter.

(b) A lawyer shall not form a partnership with a non-lawyer if any of the activities of the partnership consist of the practice of law.

(c) A lawyer shall not allow a person who recommends, employs, or pays them to provide legal services for another to direct or control their professional judgment in rendering such services.

(d) A lawyer shall not provide legal services through a professional corporation or association authorized to practice law for profit if:

1. A non-lawyer owns any interest in the organization, except that a representative of the estate of a lawyer may hold the shares or assets of the law firm for a reasonable time during estate administration;
2. A non-lawyer is a director, officer, or holds a similar position of responsibility in the organization;
3. A non-lawyer has the right to direct or control the professional judgment of the lawyer.

In summary, the prior version, which was not approved by a majority of this Court but closely mirrored the ABA Model Rule 5.4, reaffirmed the known limitations on fee-sharing and the prohibition against third-party investment in law firms. These restrictions are primarily intended to preserve the independence and professional judgment of lawyers, preventing any external influence that could compromise their ethical duties and client representation. They also ensure that the provision of legal services is governed solely by professional standards, not by economic interests foreign to legal practice.
For that reason, ABA Model Rule 5.4 has long served as an effective safeguard against ethical concerns regarding the professional independence of lawyers, and its validity was recently reaffirmed by the ABA House of Delegates. In my opinion, relaxing or eliminating Rule 5.4 will not solve the problems its advocates claim to address; instead, it may create significant risks for the legal profession.

Consistent with the above, judges must adopt a critical and pragmatic view toward the true motivations of certain economic sectors interested in co-owning law firms. Nonetheless, starting from a place of good faith, there are alternative solutions that better respect the ethical principles governing our profession, which must be preserved in our jurisdiction.

The jurisdictions of Arizona, D.C., and Utah have chosen to explore this model; let us observe their experiences and cautiously analyze the effects of possible over-commercialization of the law, the influence of powerful economic sectors, and the challenges this could pose to access to justice. So far, we have not seen these sectors partner with law firms to litigate on behalf of the environment or vulnerable populations.

We must not allow the principle of access to justice to be used as a pretext to perpetuate inequality or to excessively commercialize the practice of law. For these reasons, I respectfully dissent from this rule.

Ethics opinion for lawyers practicing ABS entities in DC, AZ, and UT

NEW YORK CITY BAR

COMMITTEE REPORTS

Formal Opinion 2024-4: Lawyers Associating with Alternative Legal Business Entities

Date
July 18, 2024

SUMMARY

The **Professional Ethics Committee** issued a formal opinion regarding New York lawyers associating with Alternative Legal Business Entities. Although the New York Rules of Professional Conduct as well as the ethics rules of almost all other U.S. jurisdictions prohibit nonlawyer ownership of law firms, some jurisdictions have adopted rules and regulatory programs that permit Alternative Legal Business Structures (ABS) to provide legal services. The opinion finds that a New York lawyer may hold a financial interest in an ABS provided the lawyer is not practicing law through the ABS and is merely a financial investor. A lawyer must also be mindful of the bounds of NY Rule 8.5 and NY Rule 5.4, which set the parameters for a lawyer's ability to associate and do business with an ABS while the lawyer is admitted in New York.

REPORT

FORMAL OPINION 2024-4: LAWYERS ASSOCIATING WITH ALTERNATIVE LEGAL BUSINESS ENTITIES

TOPIC: A New York lawyer holding a financial interest in an Alternative Legal Business Entity.

DIGEST: A New York lawyer may hold a financial interest in an Alternative Business Structure (ABS) that is lawfully operating in a jurisdiction that permits ABS entities to provide legal services. A New York lawyer is not permitted to practice law as part of an ABS if the predominant effect of the New York lawyer's conduct will be felt in New York, but the New York Rules do not prohibit a lawyer or law firm from entering into ongoing business arrangements with an ABS provided the ABS and the New York firm are operating as legally separate entities.

RULES: 5.4; 8.5

QUESTION: May a New York lawyer hold a financial interest in an ABS that is lawfully operating in a jurisdiction that permits such entities to provide legal services? May a New York lawyer enter into business arrangements beyond a financial interest with an ABS that is lawfully operating in a jurisdiction outside of New York?

OPINION: A New York lawyer may hold a financial interest in an ABS provided the lawyer is not practicing law through the ABS and is merely a financial investor. A lawyer must also be mindful of the bounds of NY Rule 8.5 and NY Rule 5.4, which set the parameters for a lawyer's ability to associate and do business with an ABS while the lawyer is admitted in New York.

Introduction

Although the New York Rules of Professional Conduct (the "New York Rules") as well as the ethics rules of almost all other U.S. jurisdictions prohibit nonlawyer ownership of law firms, some jurisdictions have adopted rules and regulatory programs that permit Alternative Legal Business Structures (ABS) to provide legal services. In broad terms, an ABS is an entity that is authorized to practice law but that has at least one nonlawyer who shares in the proceeds of the firm.[1]

The District of Columbia Rules of Professional Conduct have permitted ABS entities since 1991, subject to certain limitations. *See* D.C. R. Prof. Cond. 5.4. Arizona took steps in 2021 to eliminate its version of Rule 5.4 altogether and to

create a regulatory scheme to allow ABS entities, subject to certification and regulation by the Supreme Court of Arizona. Also in 2021, the Utah Supreme Court established a "regulatory sandbox" program to allow for ABS entities under certain conditions. The United Kingdom has permitted ABS law firms since at least 2007. *See* Legal Services Act, 2007 c. 29, § 71 et seq. (U.K.).

The purpose of this opinion is twofold. *First*, this opinion will identify common themes running through the various ABS-related ethics opinions issued by the American Bar Association ("ABA") and New York ethics committees. *Second*, this opinion will address why we believe the New York Rules permit a New York lawyer to hold a financial interest in an ABS that is legal in the jurisdiction where it is operating.

I. Relevant Rules and Ethics Opinions Related to ABS Ownership

As earlier ethics opinions have observed, some other U.S. jurisdictions permit ABS law firms, and a New York lawyer may wish to practice with an ABS lawfully operating in one of those jurisdictions. There are two New York Rules that must be considered in determining whether a New York lawyer may have an ownership interest in an ABS.

Rule 5.4

Rule 5.4 of the New York Rules addresses nonlawyer ownership of law firms. NY Rule 5.4(a) states that a "lawyer or law firm shall not share legal fees with a nonlawyer." NY Rule 5.4(b) states that "a lawyer shall not form a partnership with a nonlawyer if any of the activities of the partnership consist of the practice of law." In the same vein, NY Rule 5.4(c) prohibits a nonlawyer owner from "directing or regulating the lawyer's professional judgment in rendering legal services," while NY Rule 5.4(d) says that a lawyer may not form "a professional corporation or association" if a nonlawyer owns any interest in it, or is a "corporate officer or director thereof", or has the right to direct or control its operations.[2] Accordingly, it is well settled that the New York Rules prohibit a lawyer from practicing law in New York through an ABS (*e.g.,* as the resident New York partner in an ABS based in Arizona).

NY Rule 5.4, however, does not end our analysis. Whether a lawyer admitted in New York may have an ownership interest in an ABS may turn on which ethics rules apply to the lawyer's conduct.

Rule 8.5

NY Rule 8.5(a) provides that:

> A lawyer admitted to practice in this state is subject to the disciplinary authority of this state, regardless of where the lawyer's conduct occurs. A lawyer may be subject to the disciplinary authority of both this state and another jurisdiction where the lawyer is admitted for the same conduct.

NY Rule 8.5(a) is meaningfully different, however, from Rule 8.5(a) of the ABA Model Rules of Professional Conduct (the "Model Rules"). Specifically, Model Rule 8.5(a) contains the following additional language: "A lawyer not admitted in this jurisdiction is also subject to the disciplinary authority of this jurisdiction if the lawyer *provides or offers to provide* any legal services in this jurisdiction." (Emphasis added.) NY Rule 8.5(a) does not include this language. In other words, unlike the jurisdictions that have adopted Model Rule 8.5(a), NY Rule 8.5(a) applies the New York Rules only to a lawyer who is actually "admitted to practice" in New York, not to a non-New York lawyer who merely "provides or offers to provide" legal services in New York.[3]

In the case of a lawyer licensed in multiple jurisdictions, NY Rule 8.5(b)(2)(ii) provides that:

> the rules to be applied shall be the rules of the admitting jurisdiction in which the lawyer principally practices; provided, however, that if particular conduct clearly has its *predominant effect* in another jurisdiction in which the lawyer is licensed to practice, the rules of that jurisdiction shall be applied to that conduct.

(Emphasis added.)

New York and ABA Ethics Opinions

The ABA and ethics committees in New York have issued several ethics opinions regarding lawyers working for and owning interests in ABS entities. We briefly summarize some of the key opinions below.

A seminal opinion is New York State Opinion 889 (2011), which permitted a lawyer admitted in both New York and the District of Columbia (which permits

certain types of ABS entities) to become part of an ABS law firm in the District of Columbia provided that the predominant effect of the lawyer's practice was in the District of Columbia. New York State Opinion 889 further stated that this conclusion would not change if the lawyer conducted "occasional New York litigation" so long as "the lawyer and the law firm, now and in the foreseeable future, have their principal place of business in the District of Columbia and ... the bulk of their revenue is derived from matters unrelated to the State of New York."

One year later, New York State Opinion 911 (2012) concluded that a New York lawyer was not permitted to practice law principally in New York as an employee of an ABS firm based in the U.K. (which generally permits ABS entities). Both New York State Opinions 889 and 911 were based on the New York State Bar Association Committee's analysis of NY Rule 8.5. New York State Opinion 889 analyzed NY Rule 8.5(b) to determine the "predominant effect" of the conduct of lawyers admitted in *both* New York and the District of Columbia, while New York State Opinion 911 analyzed NY Rule 8.5(a) and concluded that because the inquiring lawyers were admitted *only* in New York, the New York Rules clearly applied.[4]

New York State Opinion 1038 (2014) similarly concluded that a New York lawyer who practiced primarily in New York could not join a D.C. law firm with nonlawyer members "as a partner" or by "forming a 'wholly owned subsidiary law firm' in New York to be 'independently managed/operated' by the New York lawyer."

In New York City Opinion 2015-8, this Committee addressed whether a New York lawyer may ethically share fees with a law firm in another jurisdiction that is permitted to have (and has) nonlawyer owners. We concluded that such an arrangement was permissible. *Accord* ABA Formal Op. 464 (2013) (approving fee-sharing between a law firm located in a Model Rules jurisdiction and an ABS firm located in a jurisdiction that permits ABS entities). Similarly in New York City Opinion 2020-1, we concluded that the New York Rules did not prohibit a New York law firm from entering into an ongoing business relationship with an ABS entity where the two firms regularly act as co-counsel on matters together and share fees pursuant to a standing agreement, but the two firms remain separate legal entities.

Further, in addressing a question similar to the one we address here, ABA Formal Op. 499 (2021) concluded that a lawyer admitted in a Model Rules jurisdiction could become a "passive investor" in an ABS firm. (We use the term "Model Rules Jurisdiction" to mean a jurisdiction that has adopted Model Rule 5.4, which prohibits non-lawyer ownership of for-profit law firms and prohibits fee sharing between lawyers and nonlawyers.) ABA Formal Op. 499 defined a "passive" investment as one where the lawyer "contributes money to an ABS with the goal of receiving a monetary return on that investment." ABA Formal Op. 499 added that "[p]assive investment does not include scenarios in which the investing lawyer practices law through the ABS, manages or holds a position of corporate or managerial authority in the ABS, or is otherwise involved in the daily operations of the ABS." In other words, ABA Formal Op. 499 reasoned, simply making a monetary investment in an ABS entity would not subject the lawyer to regulatory scrutiny in a Model Rules jurisdiction under Model Rule 8.5(b), but actively participating in the day-to-day operations of an ABS entity might subject the investing lawyer to regulatory scrutiny.

Shortly after the ABA issued ABA Formal Op. 499, New York State Opinion 1234 (2021) concluded that a New York lawyer may not merge practices with an out-of-state law firm owned directly or indirectly by nonlawyers, even if such ownership is permissible under the rules applicable in the out-of-state law firm's home jurisdiction (the ABS jurisdiction), unless (a) the New York lawyer is also admitted in that jurisdiction; (b) the New York lawyer principally practices in that jurisdiction; and (c) the predominant effect of the work is in the ABS jurisdiction.

New York State Opinion 1234 also noted, in passing, that "New York is not among the jurisdictions that allow nonlawyer [ownership of law firms]" and that "New York Rule 5.4(d) prohibits a New York lawyer from practicing in an entity authorized to practice law for profit if a nonlawyer owns *any* interest." *See* New York State Opinion 1234, ¶ 13 (citing New York City Opinion 2020-1). In our view, New York State Opinion 1234 is consistent with the opinions cited above. New York State Opinion 1234 merely reinforces the conclusion that a New York lawyer cannot *actively* participate in the activities of an ABS firm – whether by becoming a partner in an ABS firm or by "merging" with an ABS firm – unless the New York lawyer's conduct has a predominant effect in

another jurisdiction that permits fee sharing with nonlawyers *and* the New York lawyer is also admitted in that jurisdiction.

The above rules and ethics opinions lead to several important conclusions.

First, a New York lawyer is not permitted to practice with an ABS entity if the predominant effect of the New York lawyer's practice is clearly felt in New York. *See, e.g.,* New York State Opinion 911; New York State Opinion 1234. These opinions are based on the conclusion that under NY Rule 8.5(b), if the "predominant effect" of the lawyer's conduct is clearly felt in New York, then the New York rules will govern the lawyer's conduct regardless of where the ABS entity is located.[5]

Second, Model Rule 8.5 does not prohibit a lawyer from investing in a lawful ABS entity when the investment is a passive one. *See* ABA Formal Op. 499.

Third, a New York lawyer is permitted to enter into an arm's-length fee-sharing agreement with an ABS firm provided the New York law firm and the ABS are operating as legally separate entities. *See* ABA Formal Op. 464; New York City Opinion 2015-8; New York City Opinion 2020-1. Such a fee-sharing arrangement may be ongoing – it does not need to be reinvented on a case-by-case basis. *See* New York City Opinion 2020-1.

II. May a New York Lawyer Ethically Invest in an ABS?

New York ethics committees have not yet answered whether a lawyer admitted in New York (a non-ABS jurisdiction) may passively invest in an ABS firm in a jurisdiction that permits out-of-state lawyers to invest in an ABS. The conclusion in ABA Formal Op. 499 is based largely on a reading of Model Rule 8.5(b)(2), which states that where a lawyer's conduct is not related to a matter pending before a tribunal, the applicable ethics rules are "the rules of the jurisdiction in which the lawyer's *conduct occurred or*, if the *predominant effect* of the conduct is in a different jurisdiction, the rules of that jurisdiction shall be applied to the conduct." (Emphasis added.) ABA Formal Op. 499 therefore concluded:

> [U]nder Rule 8.5(b)(2), the predominant effect of a Model Rule Lawyer's passive investment in an ABS would be in the jurisdiction(s) where the ABS would be permitted. That conclusion follows from the fact that the

> investment is passive and is made in order to fund the activities of an ABS in a jurisdiction that permits such entities. Assuming the Model Rule Lawyer's investment is genuinely passive, the lawyer cannot be deemed to be practicing law in the ABS-permissive jurisdiction, just as a lawyer who is an investor in a mutual fund that includes widget company stock in its portfolio is not deemed to be making widgets. Accordingly, when the Model Rule Lawyer is passively investing, the only relevant "conduct" and the only meaningful "effect" of that conduct occurs in the ABS-permissive jurisdiction.

ABA Formal Op. 499 at 3; *see also* ABA Formal Op. 504 (2023) (concluding that a lawyer lawfully practicing as part of an ABS firm may practice *pro hac vice* in a non-ABS jurisdiction because the "predominant effect" under Model Rule 8.5(b) of the lawyer's conduct as it relates to ownership of the ABS firm would be the jurisdiction where the law firm structure was established and that permitted such conduct).[6]

We agree with the conclusion in ABA Formal Op. 499, albeit for slightly different reasons. Because the language of Model Rule 8.5(b) differs from the language of NY Rule 8.5(b)(2), the New York version requires a narrower application. As noted, Model Rule 8.5(b)(2) applies to "*any other conduct*" outside of the lawyer's home jurisdiction that is not related to a matter pending before a tribunal. (Emphasis added.) NY Rule 8.5(b)(2)(i)-(ii), by contrast, provides that for any multijurisdictional conduct: (i) if the lawyer is licensed to practice *only* in New York then the New York Rules will apply regardless of where the predominant effect will occur, but (ii) if the lawyer is licensed to practice in *both* New York *and* another jurisdiction, then the "predominant effect" test comes into play.

We do not believe that NY Rule 8.5(b) requires that the New York Rules apply to a lawyer's passive investment in an ABS if the lawyer is admitted only in New York. Were the New York Rule read to require such a result, then that same conduct – making a passive investment in an ABS operating in another jurisdiction – would be governed by different ethics rules depending on whether the New York lawyer was admitted only in New York or also admitted in the jurisdiction where the ABS operated. We cannot discern any legitimate basis for such a distinction. Further, such a distinction is inconsistent with the purpose of NY Rule 8.5(b). *See* NY Rule 8.5 Cmt. [3] (the purpose of NY Rule

8.5(b) is "to resolve ... potential conflicts" between the rules of multiple jurisdictions, and the premise of Rule 8.5(b) is that "minimizing conflicts between rules, as well as uncertainty about which rules are applicable, is in the best interest of clients and the profession (as well as the bodies having authority to regulate the profession).").

We therefore reach a similar conclusion to ABA Formal Op. 499. As a threshold matter, because the lawyer's proposed investment in the ABS is not, by itself, the practice of law, we do not believe that an application of NY Rule 8.5 is necessary in the first instance. As ABA Formal Op. 499 reasoned: "Assuming the Model Rule Lawyer's investment is genuinely passive, the lawyer cannot be deemed to be practicing law in the ABS-permissive jurisdiction, just as a lawyer who is an investor in a mutual fund that includes widget company stock in its portfolio is not deemed to be making widgets." We agree with this reasoning. Put simply, an otherwise lawful passive investment in a company is not the practice of law subject to regulation under the ethics rules. Although NY Rule 8.5 is not limited to conduct involving the practice of law – for example, it may require the application of NY Rule 8.4(c) to dishonest, deceitful or illegal conduct of a New York lawyer outside of the practice law and committed outside New York – the underlying conduct must also implicate a specific Rule of Professional Conduct. As detailed below, that is not the case here because NY Rule 5.4 is meant to address conduct involving the practice of law.

In our opinion, NY Rule 5.4 does not apply to a lawyer's passive investment in an ABS. As detailed above, NY Rule 5.4 provides that a New York lawyer shall not: (i) share legal fees with a nonlawyer (NY Rule 5.4(a)); (ii) "form a *partnership* with a nonlawyer if any of the activities of the partnership constitute the practice of law" (NY Rule 5.4(b)) (emphasis added); and (iii) "*practice with* or in the form of an entity authorized to practice law for profit" if a nonlawyer holds an interest in the entity (NY Rule 5.4(d)) (emphasis added). A financial investment in an out-of-state ABS does not fit any of these criteria.

With respect to NY Rule 5.4(a), we do not believe that a lawyer would be "sharing legal fees" with a nonlawyer simply by collecting a return on the lawyer's investment from the ABS. NY Rule 5.4(a) addresses the obligations of the lawyers who are sharing the fees, not the activities of the non-lawyers

receiving a share of the fees. The New York lawyer's role in the ABS as a passive investor is identical to that of the nonlawyer passive investors. As noted, the lawyer is not practicing law through the ABS or providing legal services to the ABS's clients. Model Rule 5.4(a) in ABS jurisdictions, like New York's version of the rule, addresses the actions of the lawyers who are practicing in the ABS, but unlike New York's rule permits the lawyers to share fees with the nonlawyer investors. Those fees paid to the ABS were not for services rendered by the New York lawyer or over which the New York lawyer had any direction or control and so NY Rule 5.4(a) is not implicated. Conversely, if the lawyer was involved in providing or directing the legal services, Rule 5.4(a) would be implicated and NY Rule 8.5(a) would require the application of NY Rule 5.4(a).[7]

With respect to NY Rules 5.4(b) and 5.4(d), we believe they are similarly inapplicable to a passive financial investment in a permissible out-of-state ABS. A financial investment in an ABS does not constitute a "partnership" with a nonlawyer for the purposes of practicing law. NY Rule 1.0(m) defines a "partner" as a "member of a partnership, a shareholder in a law firm organized as a professional legal corporation or a member of an association authorized to practice law." *See also* Roy D. Simon, *Simon's New York Rules of Professional Conduct Annotated* § 1.0:41 (Thomson Reuters 2022) ("The related term 'partnership' is not defined in Rule 1.0, but it should likewise be read to encompass every form of association included in the definition of 'partner.'"). An outside investor in an ABS is none of these. Although the lawyer may nominally be termed a "shareholder," the lawyer would not be practicing law through the ABS firm, would not have any involvement in the ABS firm's representation of clients, and would not otherwise hold himself or herself out as practicing law through the ABS firm. In other words, so long as the lawyer is not practicing law through the ABS, there is no meaningful difference between a lawyer's investment in an ABS entity and an investment in any other number of companies.[8] Similarly, a lawyer who is a mere investor is not "practicing" in the form of an entity authorized to practice law and therefore is not subject to NY Rule 5.4(d). As detailed above, a passive investment does not constitute the practice of law. It is merely an economic investment in a business venture. Accordingly, NY Rule 5.4(d) is not applicable.

The purpose of NY Rule 5.4 is to protect the lawyer's "professional independence of judgment." *See* NY Rule 5.4, Cmt. [1]. Where the lawyer is not practicing law through the ABS, we do not see any attribute of a New York lawyer's financial investment in an ABS entity that would risk compromising the lawyer's professional independence. Any legal practice that the lawyer maintains would be entirely separate from the lawyer's investment. It would therefore be impossible for any nonlawyer affiliated with the ABS entity to attempt to influence the lawyer's decision making on behalf of clients of the lawyer's New York law practice.

Under these circumstances, we are of the opinion that the New York Rules do not apply to a New York lawyer's holding a passive financial interest in a legal ABS entity operating in another jurisdiction because NY Rule 5.4 does not address such an investment.

Conclusion

A lawyer admitted in New York is permitted to hold a financial interest in an ABS entity that is lawfully operating in another jurisdiction (*i.e.,* a jurisdiction that permits ABS entities to practice law) provided the New York lawyer-investor is not practicing law through the ABS entity. A New York lawyer is not permitted to practice as part of an ABS firm if the predominant effect of the New York lawyer's conduct is in New York. Finally, a New York lawyer or law firm is permitted to enter into ongoing business arrangements with an ABS firm to work on client matters together provided the ABS firm and the New York firm are operating as legally separate entities.

FOOTNOTES

Committees

Subject Areas

Issues

Share