ONE SMALL STEP AND A GIANT LEAP: COMPARING WASHINGTON, D.C.'S RULE 5.4 WITH ARIZONA'S RULE 5.4 ABOLITION

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Model Rule 5.4—which prohibits nonlawyer ownership of law firms—has existed for almost 100 years in one iteration or another. Throughout that time, the Rule has been steeped in controversy. Some consider the Rule a necessary fail-safe, protecting the legal profession from complete ethical collapse.[1] *Others consider the Rule to be nothing but a hindrance to legal innovation, artificially inflating the cost of legal services. This Note compares Washington, D.C.'s modified Rule 5.4, allowing nonlawyer ownership in law firms in some circumstances, with Arizona's recent Rule 5.4 abolition, requiring firms that wish to be owned (in whole or in part) by nonlawyers to comply with regular government oversight. All in all, Arizona's*

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1. Research from jurisdictions that have recently changed their rules to allow equity ownership of law firms suggests that this fear, thus far, is largely unfounded. *See* David Freeman Engstrom et al., *Legal Innovation After Reform: Evidence from Regulatory Change*, STAN. L. SCH. 19–20, 45 (Sept. 2022), https://law.stanford.edu/wp-content/uploads/2022/09/SLS-CLP-Regulatory-Reform-REPORTExecSum-9.26.pdf [https://perma.cc/WD37-UCZC] (finding that reforms allowing nonlawyer ownership of law firms in England and Wales "do not appear to have negatively impacted the quality of legal services" nor to have "had a negative economic impact on the traditional U.K. legal market;" and that no ethics complaints have been filed against Arizona firms taking advantage of the Rule change). *See also* Jayne R. Reardon, *Alternative Business Structures: Good for the Public, Good for the Lawyers*, 7 ST. MARY'S J. ON LEGAL MALPRACTICE & ETHICS 304, 349–50 (2017) (reporting that since England and Australia have permitted nonlawyer ownership, "disciplinary complaints against lawyers have remained static or dropped significantly in the years since . . . .").

Rule abolition is more promising because it allows the Arizona legal profession to have its cake and eat it too[2]*: it allows firms to sidestep Rule 5.4 altogether while allowing authorities to monitor firms that choose to do so to make sure they comply with other professional and ethical rules. Thus, as this Note argues, Arizona's Rule abolition does much more to foster innovation than D.C.'s modified Rule. Arizona's Rule change also does much more to carry out the intentions of Rule 5.4 than the D.C. Rule; it better ensures that nonlawyer ownership of law firms does not interfere with the ethical administration of the law. Finally, this Note argues that although Arizona's Rule abolition is a major step in the right direction, much more still needs to be done to lower the cost of legal services—the stated purpose behind Arizona's Rule change.*

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INTRODUCTION

The United States ranks 126th out of 139 countries in terms of accessibility and affordability of its civil courts, placing the nation behind countries such as Honduras, Mozambique, and Afghanistan.[3] In fact, 66% of people in the United

2. This sentence is inspired by the title of another *Arizona Law Review* Note, published 11 years ago. *See* Tyler Cobb, Note, *Have Your Cake and Eat It Too! Appropriately Harnessing the Advantages of Nonlawyer Ownership*, 54 ARIZ. L. REV. 765, 768–69 (2012).

3. *Rule of Law Index*, WORLD JUSTICE PROJECT (2021), https://worldjusticeproject.org/rule-of-law-index/factors/2021/United%20States/Civil%20Justice/ [https://perma.cc/9X79-38RH] (ranking countries based on "national surveys of more than 130,000 households and 4,000 legal practitioners and experts").

States in 2021 had "experienced at least one legal issue in the [previous] four years," and only 49% of those legal issues were resolved as of 2021.[4] Another study conducted in 2010 from New York "revealed that over 95% of people" facing "housing, family[,] and consumer debt" legal issues lacked representation.[5] Additionally, 60% of small businesses reported the need for an attorney, but only 40% of those who needed an attorney hired one.[6] "Today, nearly 80% of civil cases involve at least one party without an attorney—double the percentage of self-represented litigants in 1980."[7]

The mainstream methods of addressing the access to justice problem have failed.[8] For example, nonprofits are incapable of providing low-cost legal services at a sufficient scale because they are required to charge below-market rates, face fundraising limitations, experience negative tax implications from charging on a need-based sliding scale, and are often unable to hire and retain skilled lawyers.[9] Currently, less than "two percent of all American lawyers work in legal aid or public defender jobs and pro bono work accounts for less than two percent of legal effort."[10] Additionally, "providing just one hour of pro bono assistance" per household facing a legal issue "would require over 200 hours of pro bono work per year by every licensed attorney in the country."[11]

Many of these access and affordability issues stem from the current legal regulatory environment.[12] One regulation that has been identified by multiple scholars as the most significant barrier to affordable legal services is the American Bar Association's ("ABA") Model Rule 5.4.[13] This Rule, described in more detail

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4. *Justice Needs and Satisfaction in the United States of America 2021*, THE HAGUE INST. FOR INNOVATION OF L. & THE INST. FOR THE ADVANCEMENT OF THE AM. LEGAL SYS. (2021), https://iaals.du.edu/sites/default/files/documents/publications/justice-needs-and-satisfaction-us.pdf [https://perma.cc/8LYL-T9MJ] (interviewing 10,058 respondents from across socio-economic, racial, employment, and gender backgrounds).

5. Gillian Hadfield, *The Cost of Law: Promoting Access to Justice Through the (Un)Corporate Practice of Law*, 38 INT'L REV. L. & ECON. 43, 43 (2013).

6. DECISION ANALYST & LEGALSHIELD, THE LEGAL NEEDS OF SMALL BUSINESS 4 (2013) https://contractorsorganization.org/wp-content/uploads/2018/03/Legal-Needs-of-Small-Business-2018.pdf [https://perma.cc/BM63-W6KP].

7. Jason Solomon, Deborah Rhode & Annie Wanless, *How Reforming Rule 5.4 Would Benefit Lawyers and Consumers, Promote Innovation, and Increase Access to Justice*, STAN. CTR. L. PRO. 1 (Apr. 2020), https://law.stanford.edu/wp-content/uploads/2020/04/Rule_5.4_Whitepaper_-_Final.pdf [https://perma.cc/5VNJ-2S7A].

8. Gillian K. Hadfield & Deborah L. Rhode, *How to Regulate Legal Services to Promote Access, Innovation, and the Quality of Lawyering*, 67 HASTINGS L.J. 1191, 1193 (2016).

9. R. Mathew Black, Note, *Extra Law Prices: Why MRPC 5.4 Continues to Needlessly Burden Access to Civil Justice for Low-to Moderate-Income Clients*, 25 WASH. & LEE J. CIV. RTS. & SOC. JUST. 499, 530–43 (2019).

10. Hadfield & Rhode, *supra* note 8, at 1193.

11. *Id.*

12. *Id.* at 1194 (listing other regulatory factors that ultimately affect the affordability of legal services, including the requirement that legal providers obtain expensive graduate degrees, pass various exams, and obtain and maintain licenses).

13. *See, e.g.*, Hadfield, *supra* note 5.

below,[14] requires that legal services "be provided by a law firm that is owned, managed, and financed exclusively by lawyers."[15] In jurisdictions where the standard Rule 5.4 has been adopted, nonlawyers cannot have an equity interest in a law firm.[16] Arizona, Washington, D.C., Utah, and Washington State are the only jurisdictions that have either eliminated or modified Rule 5.4, allowing at least some nonlawyer equity interest in law firms under certain circumstances.[17] On January 1, 2021, Arizona eliminated Rule 5.4 and replaced it with a regulatory scheme designed to achieve some of the same goals as Rule 5.4; the new Arizona regulatory scheme, however, allows for ownership, management, and financing of law firms by nonlawyers.[18]

The D.C. Rule allows nonlawyers to enter legal practice partnerships with lawyers if, among other considerations, the partnership or organization's sole purpose is to provide legal services, and the nonlawyer performs professional services that help the organization provide legal services.[19] Despite already having a more relaxed Rule 5.4, Washington, D.C. is contemplating abolishing its Rule, just as Arizona has.[20]

This Note compares Arizona's abolition of Rule 5.4 to D.C.'s modified Rule to understand how each jurisdiction's rule change addresses the access to justice problem. In short, Arizona's Rule change does a better job of attempting to achieve access to justice than D.C.'s Rule. While this is important because it shows that Arizona's Rule change is a significant improvement to the status quo, so much more work still needs to be done to significantly reduce access to justice issues in Arizona.

Part I of this Note provides an overview of the Model Rule 5.4, including its history, benefits, and downsides. One such disadvantage involves the inability of law firms to use financial and legal mechanisms that ultimately lower legal fees for

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14. *See infra* Part I.

15. Hadfield & Rhode, *supra* note 8, at 1194.

16. *See, e.g.*, NEV. RULES OF PROF. CONDUCT r 5.4(b), (d) (NEV. BAR ASS'N 2006) (stating that a lawyer cannot form a partnership with a nonlawyer if any part of the partnership renders legal services, and that a lawyer cannot form any kind of for-profit law practice if a nonlawyer owns any interest therein); MODEL RULES OF PRO. CONDUCT r. 5.4 (AM. BAR ASS'N 2020).

17. *See* D.C. RULES OF PROF. CONDUCT r. 5.4 (D.C. BAR ASS'N 2007); WASH. RULES OF PRO. CONDUCT r. 5.9 (WASH. BAR ASS'N 2015) (allowing for fee sharing and partnership formation with limited license legal technicians subject to certain regulations); ABA Comm. on Ethics & Pro. Resp., Formal Op. 499, 1 (2021) (describing Arizona's Ethics Rule 5.4 change and Utah's regulatory sandbox approach to its Rule 5.4 change) [hereinafter ABA Formal Op. 499].

18. *See infra* Section I.A and Part II.

19. *D.C. Bar Global Legal Practice Committee Seeks Public Comment on Rule of Professional Conduct 5.4*, D.C. BAR (Jan. 23, 2020), https://www.dcbar.org/news-events/news/d-c-bar-global-legal-practice-committee-seeks-publ [https://perma.cc/U4AZ-P4F2].

20. Sam Skolnik, *D.C. Law Firm Ownership Rules May Be in for More Changes*, BLOOMBERG L. (Sept. 3, 2020, 12:21 PM), https://news.bloomberglaw.com/business-and-practice/d-c-bar-law-firm-ownership-rules-may-be-in-for-more-changes?context=article-related [https://perma.cc/3JYH-ZHZ2].

clients. Part II discusses Arizona's Rule 5.4 abolition, including a more detailed account of the history and purpose of abolishing the Rule. Part II also explains the Alternative Business Structure ("ABS") regulatory environment that replaced the original Rule 5.4, how firms in Arizona can use the ABS, and potential legal issues that firms might face when adopting the Arizona ABS. Part III reviews D.C.'s modified Rule 5.4, including its history, use, advantages, and disadvantages. Part IV compares and analyzes the merits of Arizona's Rule 5.4 abolition relative to D.C.'s modified Rule 5.4.

I. OVERVIEW OF RULE 5.4

The ABA's Model Rule 5.4 states that a lawyer may not share legal fees with a nonlawyer and may not form a partnership with a nonlawyer if any "activities of the partnership consist of the practice of law."[21] Moreover, a lawyer may not practice law in a profit-seeking professional corporation or association if a nonlawyer owns any interest in the corporation, is a corporate director or officer of the corporation, or "has the right to direct or control the professional judgment of a lawyer."[22] The Rule's ostensible purpose is to protect lawyers' independent judgment in rendering legal services.[23] Almost all jurisdictions have elected to adopt the ABA's Model Rule 5.4.[24]

A. A Brief History of Rule 5.4 and Its Intended Purpose

Court decisions and legislation from the turn of the twentieth century prohibited the sharing of legal fees with nonlawyers. These developments were responses to "giant corporations . . . employing salaried lawyers to provide legal services to third parties and turn[ing] over the fees to the corporation."[25] In 1928, the ABA codified the prohibition against sharing legal fees with nonlawyers in its professional conduct directive.[26] The early version of what would become Rule 5.4 sought to prevent large banks from taking over the legal industry, and "was probably also aimed at ambulance chasers."[27]

The 1928 Canons of Professional Responsibility were reformulated and recodified when the ABA adopted the Model Code of Professional Responsibility

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21. MODEL RULES OF PRO. CONDUCT r. 5.4 (AM. BAR ASS'N 2020).

22. *Id.*

23. *Id.* cmt. 1.

24. Cobb, *supra* note 2, at 768–69. Ethics rules are promulgated through a jurisdiction's highest court. Letter from Jamie S. Gorelick & Michael Traynor, Co-Chairs, ABA Comm'n on Ethics 20/20, to ABA Entities, Courts, Bar Associations, Law Schools, and Individuals 1 n.1 (Dec. 2, 2011), http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111202-ethics2020-discussion_draft-alps.authcheckdam.pdf [https://perma.cc/8X9F-HNFC].

25. Roy D. Simon, Jr., *Fee Sharing Between Lawyers and Public Interest Groups*, 98 YALE L.J. 1069, 1076–79 (1989) (providing a history of the prohibition against lawyers sharing legal fees with nonlawyers dating back to 1729).

26. *See* CANONS OF PRO. ETHICS Canon 34 (AM. BAR ASS'N 1928); Reardon, *supra* note 1, at 310; *In re* Co-operative L. Co., 198 N.Y. 479 (1910) ("The practice of law is not a business open to all, but a personal right, limited to a few persons of good moral character, with special qualifications ascertained and certified after a long course of study . . . .").

27. Simon, *supra* note 25, at 1079–80.

in 1969.[28] Like the 1928 Rule, the rationale behind the 1969 Model Code of Professional Responsibility Rule was to preserve the integrity of the legal system from the influence of outside money and other conflicts of interest.[29]

Before the Model Rules of Professional Conduct were codified in 1983, the ABA created the Kutak Commission (named for the ABA Commissioner on Evaluation of Ethical Standards, Robert J. Kutak)[30] to recommend changes to the proposed rules.[31] The Kutak Commission's goal "was to reinforce the idea that lawyers served the public good, and helped improve American social, economic, and political structures."[32] The Kutak Commission advocated for a modified Rule 5.4 that allowed for lawyer employment in a firm where a nonlawyer could hold a financial interest or managerial authority if: (1) "the lawyer's independence of professional judgment" with their clients is maintained; (2) the firm maintains fidelity to other confidentiality-based ethics rules; (3) other advertising or personal contact rules are adhered to; and (4) the firm follows Rule 1.5 fee arrangement ethics mandates.[33]

Although the Kutak Commission explained that a prohibition on sharing legal fees "could be viewed as economic protectionism for traditional legal service organizations" that only marginally promoted ethical representation,[34] the ABA delegates rejected the Kutak Rule 5.4 proposal in favor of the traditional approach, which still stands today.[35] The ABA delegates rejected the Kutak Commission's Rule 5.4 out of concern for: (1) lawyers' professional independence when directed by nonlawyers who would not understand "ethical considerations inherent in client representation";[36] (2) a "fear of Sears,"[37] which stemmed from a concern that large corporations would dominate "the legal marketplace";[38] (3) reduced professionalism

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28. Reardon, *supra* note 1, at 310–11.

29. *See id.* at 310–12.

30. Michael S. Ariens, *The Last Hurrah: The Kutak Commission and the End of Optimism*, 49 CREIGHTON L. REV. 689, 689–90 (2016).

31. Cobb, *supra* note 2, at 769–70.

32. Black, *supra* note 9, at 503 (internal quotation omitted). *See also id.* at 503 (noting that the Kutak Commission was created over the backdrop of the Watergate scandal, which shifted "public sentiment toward the belief that the legal profession was openly self-serving").

33. Cobb, *supra* note 2, at 770 n.18.

34. Susan Gilbert & Larry Lempert, *The Nonlawyer Partner: Moderate Proposals Deserve a Chance*, 2 GEO. J. LEGAL ETHICS 383, 386–87 (1988) (noting that the Kutak Commission also explained how the traditional Rule no longer fit in the modern practice of the law where "corporations and organizations, government agencies, and public defender and group legal service organizations employ large numbers of lawyers to perform legal work, although nonlawyers may direct the organization").

35. Cobb, *supra* note 2, at 770.

36. *Id.* at 771.

37. The term "fear of Sears" was coined in an era when the Sears Corporation was a dominant economic figure in the United States (the equivalent of modern-day Walmart or Amazon); the worry was that big corporations would monopolize all aspects of the economy. Dennis A. Rendleman, *Mediation on Model Rule 5.4*, AM. BAR ASS'N (Dec. 2018). https://www.americanbar.org/news/abanews/publications/youraba/2018/december-2018/meditation-on-model-rule-5-4/ [https://perma.cc/JM5N-VSS7].

38. Cobb, *supra* note 2, at 771.

caused by a more commercialized legal profession;[39] and (4) "other negative, but unknown effects on the legal profession."[40]

The ABA again considered revising Rule 5.4 when it created the ABA Commission on Ethics 20/20 (the "20/20 Commission").[41] The 20/20 Commission rejected nonlawyer ownership structures "including a) publicly traded law firms, b) passive, outside nonlawyer investment or ownership in law firms, and, c) multidisciplinary practices."[42] However, the 20/20 Commission's Working Group on Alternative Law Practice Structures (the "Working Group") did recommend a more stringent version of what is now the D.C. Rule 5.4.[43] It was more stringent because it also required nonlawyers to have a subordinate financial and voting interest in the firm.[44] Ultimately, the Working Group's recommendation was rejected, but the ABA did claim "that it would continue its effort to find a way to permit fee splitting between lawyers and nonlawyers."[45]

Rule 5.4's nearly 100-year history, throughout its various iterations, shows that it has always been a controversial rule. Even the ABA, which continues to promote the Rule, has continually looked for alternatives or modifications to the Rule, up to the present day.[46]

B. The Benefits of Rule 5.4

One of the oft cited concerns with lawyers sharing fees with nonlawyers is that traditional law firms will be swallowed up or put out of business by large corporations.[47] While previous generations were concerned with Sears's or big

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39. Candace M. Groth, *Protecting the Profession Through the Pen: A Proposal for Liberalizing ABA Model Rule of Professional Conduct 5.4 to Allow Multidisciplinary Firms*, 37 HAMLINE L. REV. 565, 571 (2014).

40. *Id.*

41. ABA Commission on Ethics 20/20, AM. BAR ASS'N, https://www.americanbar.org/groups/professional_responsibility/committees_commissions/aba-commission-on--ethics-20-20/ [https://perma.cc/56RY-FUE6]. *See also* ROY D. SIMON, JR., SIMON'S NEW YORK RULES OF PROFESSIONAL CONDUCT ANNOTATED § 5.4:38 (2020).

42. SIMON, *supra* note 41, at § 5.4:38.

43. *See* ABA Commission on Ethics 20/20: Initial Draft Proposal for Comment, AM. BAR ASS'N (Dec. 2, 2011) https://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111202-alps_choice_of_law_r_and_r_final.pdf [https://perma.cc/C6EJ-UZW5]. Whereas the D.C. Rule's only additional substantive requirement (apart from nonlawyers being able to own part of a law firm) is that the sole purpose of a firm with nonlawyer ownership must be to provide legal services. *See* D.C. RULES OF PROF. CONDUCT r.5.4 (D.C. BAR ASS'N 2007).

44. SIMON, *supra* note 41 (also noting that the Working Group found four kinds of multidisciplinary practices that " clients were already demanding or might demand in the future: 1) land use law firms that include engineers and architects; 2) intellectual property law firms that include scientists and engineers; 3) family law firms that include social workers and financial planners; and 4) personal injury law firms in which nurses and investigators participate in evaluating cases, evaluating evidence, and developing strategy").

45. Reardon, *supra* note 1, at 317.

46. *Id.*

47. *See generally* Cobb, *supra* note 2, at 771; Simon, *supra* note 25, at 1076–79; Groth, *supra* note 39, at 570–71.

banks' potential domination of the legal market,[48] many contemporary commentators are concerned with the Big Four—Deloitte, PricewaterhouseCoopers ("PwC"), Ernst & Young ("EY"), and Klynveld Peat Marwick Goerdeler ("KPMG")—accounting firms' ability to do the same should the traditional Rule 5.4 disappear.[49] The Big Four accounting firms "already dominate business consulting services in the global market," but Rule 5.4 currently prohibits them from being a one-stop shop for all business *and* legal needs.[50]

The Big Four already offer legal services in other countries; PwC, for example, offered legal services in 124 countries as of 2011.[51] Further, the Big Four are uniquely positioned to take advantage of a Rule 5.4 change because they already serve 49.2% of all public companies through auditing services alone.[52] Additionally, the Big Four already take a multidisciplinary approach to solving problems and "are more adept at assembling teams … of experts in diverse fields";[53] have made significant investments toward reducing consumer costs through innovative service models; typically cultivate relationships with corporate officers;[54] have more robust economic and document analysis capabilities than traditional law firms;[55] and may provide a more enticing environment to attract legal talent.[56] "Moreover, the Big Four does a significant portion of its work at a flat fee."[57]

On a more fundamental level, proponents of the traditional Rule 5.4 argue that for-profit corporations are only concerned with their bottom lines.[58] This argument, however, suggests that for-profit corporations are incentivized to keep legal fees high even while lowering their costs in an attempt to maximize profit.[59] In a competitive market where many firms can lower their costs, this is an unlikely scenario, because at least one firm will lower their legal fees to attract more customers in an attempt to earn more profit, at which point other firms will be forced to lower their legal fees to keep up with the competition.[60]

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48. *See* Simon, *supra* note 25, at 1076–79; Cobb, *supra* note 2, at 771.

49. Elijah D. Farrell, Note, *Accounting Firms and the Unauthorized Practice of Law: Who is the Bar Really Trying to Protect?*, 33 IND. L. REV. 599, 599 n.1, 599–60 (2000).

50. *Id.*

51. Katherine Hollar Barnard, *The Triple Threat Facing Generalist Law Firms, Part 3: The Big Four*, JDSUPRA (Mar. 3, 2021), https://www.jdsupra.com/legalnews/the-triple-threat-facing-generalist-law-5380456/ [https://perma.cc/WBT7-B8AM] (noting that in 2011, Deloitte offered legal services in 97 countries; EY, 29; and KPMG, 73).

52. *Id.*

53. *Id.*

54. *Id.*

55. Farrell, *supra* note 49, at 559–60.

56. *Id.* at 603–04 (noting that the Big Four have the ability to pay lawyers higher salaries and provide less pressure to develop clients).

57. Barnard, *supra* note 51.

58. Farrell, *supra* note 49, at 622.

59. *Id.*

60. *See* Irena Asmundson, *Supply and Demand: Why Markets Tick*, INT'L MONETARY FUND (Feb. 24, 2020), https://www.imf.org/external/pubs/ft/fandd/basics/suppdem.htm ("In perfect competition a firm with lower costs can reduce its price and add enough customers to make up for lost revenue on existing sales.").

Another argument is that the traditional Rule 5.4 protects lawyers' independent professional judgment.[61] This is the primary rationale behind the ABA's current Rule 5.4 and has been the primary reason why attempts to change the Rule have failed thus far.[62] Relatedly, proponents of the traditional Rule 5.4 argue that nonlawyer ownership heightens the risk that lawyers will breach client confidentiality.[63]

Yet another concern is that corporations or other nonlawyer investors in a law firm will be able to fund litigation for their own regulatory, ideological, or personal interests.[64] For example, a religious nonlawyer owner of a law firm with deep pockets might fund anti-abortion causes without having to abide by local rules governing the funding of litigation. Although nonlawyers can already do this in many jurisdictions, many of the regulatory frameworks written to allow for third-party funding of litigation were written for just that: *true* third-party funding.[65] Nonlawyers may be able to sidestep third-party litigation funding regulations by funding litigation as the owners of a law firm. Additionally, nonlawyer owners of a law firm could gain more control over the firm in terms of which kinds of cases the law firm accepts and how the law firm spends money,[66] and they might allow law firms to take on riskier cases because they will have access to equity financing.[67]

One last potential benefit of Rule 5.4 is that it may prevent corporations from gathering otherwise unavailable information about market conditions. Although Rule 1.6 prevents lawyers from divulging client information to nonlawyers and other lawyers who do not represent their client,[68] that Rule may not prevent nonlawyer owners of a law firm—or others in a firm that also provides legal services—from gathering general market data for their own use. For example, an investment or financial services corporation that also provides large amounts of legal services can benefit from general market information held by their legal services department if that department specializes in zoning and real estate. The zoning and real estate department cannot divulge particular information about which clients own or lease which properties, but the department could disclose general market

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61. Farrell, *supra* note 49, at 621.

62. *See* MODEL RULES OF PRO. CONDUCT r. 5.4 cmt. 1 (AM. BAR ASS'N 2020) ("The provisions of this Rule express traditional limitations on sharing fees. These limitations are to protect the lawyer's professional independence of judgment."); Black, *supra* note 9, at 506.

63. Black, *supra* note 9, at 505–06.

64. *See generally* Lili Levi, *The Weaponized Lawsuit Against the Media: Litigation Funding as a New Threat to Journalism*, 66 AM. U. L. REV. 761 (2017).

65. *See id.* at 802–05.

66. Sam Skolnik, *Litigation Finance Companies Eye Law Firm Ownership in Arizona*, BLOOMBERG L. (Nov. 29, 2021, 3:30 AM), https://news.bloomberglaw.com/us-law-week/litigation-finance-companies-eye-law-firm-ownership-in-arizona [https://perma.cc/TA29-F9EZ].

67. This may not be a bad thing.

68. *See* MODEL RULES OF PRO. CONDUCT r. 1.6 (AM. BAR ASS'N 2020) (stating that lawyers cannot disclose "information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted" by certain specifically outlined, policy-concerned exceptions).

trends and bid prices that would otherwise be unavailable or would be available only at a later point in time. Additionally, the law firm could ask its clients to fill out questionnaires to gather information and send them to its nonlawyer owners, and nonlawyers may be able to advertise their other businesses to a firm's clients.[69]

C. Arguments Against Rule 5.4

One of the primary arguments against Rule 5.4 is that it keeps the cost of legal services high.[70] As noted above, affordability is a major factor, if not the primary factor, contributing to access to justice problems for most Americans;[71] for several reasons, nonprofit and low-profit models have failed to solve this problem.[72] As noted below, affordability of justice was the primary reason why the Arizona Supreme Court abolished the Arizona Rule 5.4 in 2020.[73] Included in each argument against the Rule, below, are some of the financial and legal mechanisms that law firms can use to lower legal costs once Rule 5.4 is abolished.[74]

1. Rule 5.4 Raises Legal Costs

Under Rule 5.4, law firms cannot raise outside equity financing.[75] Consequently, law firms must either raise capital through their attorney partners or seek debt financing.[76] However, debt financing contributes to a fragile financial structure and is one of the reasons why some of the world's highest-profile law firms

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69. Although firms would still have to comply with disclosure requirements.

70. Hadfield, *supra* note 5, at 45–48.

71. *See id.* at 44–45.

72. Black, *supra* note 9, at 502. *See* Hadfield, *supra* note 5, at 44 (stating that "legal aid and pro bono work … can never meet the demand for legal help").

73. ARIZ. SUP. CT. TASK FORCE ON THE DELIVERY OF LEGAL SERVS., REPORT AND RECOMMENDATIONS, 6–9 (Oct. 4, 2019) [hereinafter ARIZ. SUP. CT. TASK FORCE].

74. However, it is important to note that Rule 5.4 is not the only Rule that needs to be changed or abolished to lower the cost of legal services. For example, the current ABA Rules substantially limit fee sharing, which impacts a lawyer's use of online coupon sites (such as Groupon) whereby a lawyer could promote special deals and the website would "retain[] a portion of the amount paid by the customer" for the coupon; a website that "collects legal questions from users and routes questions to lawyers who" would answer the legal questions, and the website would receive a portion of the revenue; and any other compensation arrangement where nonlegal entities are paid "based on a percentage of either specific or general law firm profits." Hadfield, *supra* note 5, at 56. This is why Arizona also changed or abolished 12 of its Ethics Rules, including Rule 1.5 which deals with fee sharing arrangements, and other rules that allow for the practice of law by paraprofessionals under certain conditions. Order Amending the Arizona Rules of the Supreme Court and the Arizona Rules of Evidence, *In re* Restyle and Amend rule 31; Adopt New Rule 33.1; Amend Rules 32, 41, 42 (Various ERs from 1.0 to 5.7), 46-51, 54-58, 60 and 75-76, No. R-20-0034 (Ariz. 2020) [hereinafter Ariz. Order No. R-20-0034]. The Arizona Supreme Court also changed 16 Supreme Court Rules and 1 Rule of Evidence (making communications between legal paraprofessionals and a client privileged under certain circumstances), thereby creating a regulatory environment for alternative business structures and legal services provided by paraprofessionals. *Id.*

75. Gillian K. Hadfield, *Legal Infrastructure and the New Economy*, 8 I/S: J. L. & POL'Y FOR INFO. SOC'Y 1, 56 (2012).

76. *Id.*

failed during financial market fluctuations between 2003 and 2008.[77] Therefore, the ability to seek outside equity financing should actually contribute to a more financially stable legal environment as a whole—especially during economic crises.[78] Additionally, law firms already in "dire financial straits that still maintain an otherwise successful practice with a strong client base" could benefit from equity financing that could provide a more sustainable financial lifeline than debt.[79]

In good times, equity financing would allow law firms to expand more easily because the risk and cost of debt financing could be more easily avoided.[80] The greater ease of expansion would benefit law firms in the United States, allowing them to expand globally and compete with law firms in other countries,[81] some of which already have access to equity financing.[82]

Allowing for nonlawyer equity ownership allows for more market participants in the buying and selling of law firm equity and makes transferring law firm equity much cheaper and easier.[83] This mechanism alone provides incentives for law firms to become or change their business structure into a corporation where equity owners can more freely issue and transfer shares to raise capital.[84] In theory, expanding the market for law firm equity would have the additional effect of increasing demand and therefore the prices of law firm equity, assuming the supply of equity remains stable.[85] But in practice, many law firms' equity value might only

77. *Id.*

78. *See id.*; Cobb, *supra* note 2, at 777–78 (noting that the stability equity financing provides allows "'[i]nvestments [t]o be made in long-lived and specialized physical assets, in information and control systems, in specialized knowledge and routines, and in reputation and relationships, all of which [can] be sustained even as individual participants in the enterprise' come and go") (alterations in original).

79. Cobb, *supra* note 2, at 777–78.

80. *Id.* at 776.

81. *Id.*

82. *See* Casey E. Faucon, *Black Market Law Firms*, 41 CARDOZO L. REV. 2283, 2320 (2019).

83. Under the current rules and practice, one must apply to and finish law school, pass a jurisdiction's bar, work in a firm until one earns or creates equity, and only then can one participate in the law firm equity market—and even then, only with those who have also finished the same process.

84. The new Arizona Rule does not completely eliminate equity transaction costs (e.g., shares are still not freely transferable), because one still has to go through a regulatory process to be permitted to own equity in a law firm; and even then, one still has to maintain regulatory compliance. For example, one would likely not be allowed to, under the new Arizona Rule, own part of a law firm if one had one's law license revoked by the Bar for an ethics violation; nor could one in that situation keep their equity ownership in a law firm. So, all market participants must remain in good ethical standing at all times while owning any equity in a law firm. Of course, this is apart from the obvious—that a whole law firm itself must first comply with Arizona regulations allowing for nonlawyer ownership. *See infra* Section II.A.

85. Fundamentally, there are only so many law schools, people who can graduate from them, and people who can pass a jurisdiction's bar and offer legal services.

be worth the size and quality of their partners' client books[86]—which begs more questions: how should law firms be valued in the first place? And relatedly, what are law firms' long-term assets that make them valuable?[87]

These benefits of increased equity transferability would act as incentives to change the dominant corporate structure of law firms from partnership to corporation.[88] Unlike the current partnership law firm model, which divvies up profits on some ratio that "is heavily dependent on the dollars [the partners] themselves generate" each year,[89] the corporate model distributes profit based on equity owned.[90] Thus, because lawyers in a corporate model law firm can earn profits just by owning equity in the law firm, they are incentivized to keep their money in the law firm long-term.[91] This long-term capital, also called "permanent equity," aligns the incentives between older partners looking to retire and newer associates; the older partners gain incentives to reinvest in the firm because their capital can reap dividends and increase in value even if they no longer work in the law firm.[92] Again, a nonworking partner's share of the profits would no longer be

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86. In which case the law firm's equity value would be highly contingent upon partners staying at the firm and maintaining client relations, and investors—assuming such a firm could attract any—would have obvious incentives to change (or create) the firm's long-term strategy.

87. Some of the many things investors might look for include the quality and enforceability of employment contracts and other mechanisms in place to retain talent (including the talent's clients), ability to attract talent, a law firm's institutional ties and communication channels, a firm's brand quality and recognition, the degree to which a law firm has cornered a region's market, the value of the information the law firm has access to, the degree to which a law firm's tasks can be automated or outsourced to paraprofessionals (or others), the degree of value that can be added to a law firm by including other kinds of professionals in the practice of law, etc.

88. *See* James Goodnow, *Is the Problem with Partnerships the Partnership?*, ABOVE THE L. (July 15, 2022, 10:48 AM), https://abovethelaw.com/2022/07/is-the-problem-with-partnerships-the-partnership/ [https://perma.cc/TJ4N-MK79] (explaining that one way in which the partnership models of "Biglaw [are] missing the boat is by not offering its lawyers permanent equity").

89. *Id.* The implication of this idea is this: each partner must work each year to earn their share of the profits. This is unlike the corporate model—do you see Warren Buffett personally drilling for oil or bottling Coca-Cola? No. But he does still earn a percentage of Chevron and Coca-Cola's profits because he owns shares of a company that owns shares in those companies.

90. *Id.*

91. *Id.*

92. *Id.* For example, suppose there is a law firm with many older partners and some younger associates. Additionally, suppose that the younger associates want laptop computers. In a mainstream partnership-style law firm, the partners face disincentives in buying the younger associates laptops because the purchase would eat into the partner's share of profits, and the partners may not stay working long enough in the firm to see their investment reap adequate returns. The partners would be incentivized to make the laptop purchase, however, if they had equity in a firm that appreciated in accordance with the firm's increasing value because the partners would see a return on their investment even if they retired and stopped working. This would be true under the new Arizona Rules even if the partners relinquished their licenses and thus became nonlawyers. See *infra* Section II.A.

tied to their own personal efforts.[93] Additionally, the corporate model gives law firms mechanisms, via types of stock vesting options, that incentivize newer associates to stay in the firm.[94]

Expansion itself may bring the costs of legal services down as larger firms could invest more in identifying "advertising and market approaches that cost-effectively communicate with customers."[95] As Gillian Hadfield explains, many access to justice problems stem from the fact that those who need legal help face substantial costs in searching for legal advice.[96] In fact, many of those who need legal help do not know their problem is a legal one.[97] These legal problems usually stem from more common, everyday tasks such as applying for a job or managing a financial crisis.[98] Access to equity capital can help law firms more effectively reach consumers, thus reducing their search costs.[99]

Additionally, access to equity financing gives law firms greater ability to invest in innovative technology and services.[100] For example, venture capitalists or a technology company with the ability to raise capital through the stock market might invest in a law firm to develop technology for contract drafting or legal research. Alternatively, a law firm might use equity capital to create an application that helps its clients fill out documents remotely or more quickly. Tech companies like LegalZoom would be able to experiment with brick-and-mortar stores that could "bundle easily commoditized services such as wills and trusts [s]imilar to Vision Centers found in Walmart"—making "access to legal services" more "visible to the clients who need the services."[101]

Eliminating Rule 5.4 would allow law firms to more easily attract human capital conducive to innovation.[102] For example, a law firm could attract software engineers by offering them a pathway to a partnership position;[103] a family law firm might attract financial planners or social workers to provide more complete counseling;[104] a personal injury law firm might hire a medical professional to help assess or build cases or a creative writer to help draft demand letters; or "an

93. Goodwin, *supra* note 88.
94. *Id.*
95. Hadfield, *supra* note 5, at 49.
96. *Id.* at 49–50.
97. *Id.*
98. *Id.*
99. *Id.* at 50 (noting that large-scale branding via internet platforms can help law firms reach customers who can then share their common experiences with the law firm with others, thus providing "reputational guarantees" for legal services and improving "the matching between services and users").
100. Hadfield, *supra* note 75, at 56.
101. *See* Black, *supra* note 9, at 542–43.
102. Faucon, *supra* note 82, at 2316–18; Hadfield, *supra* note 75, at 56.
103. Hadfield, *supra* note 75, at 56. Software engineers could be useful for all kinds of firms—defense, plaintiff, or transactional. Apart from on-boarding software that could help a firm find the best clients or help clients provide information, software engineers can help with the complexities of eDiscovery and "managing, protecting, and presenting electronically stored information." Jay E. Grenig and William C. Gleisner, III 1 eDiscovery & Digital Evidence § 1:1 (Nov. 2022). *See generally id*.
104. Faucon, *supra* note 82, at 2318.

economist might work in a firm with antitrust or public utility practitioners."[105] Moreover, clients could more easily obtain services from firms acting as a one-stop-shop for all their counseling needs; this structure would reduce search costs for clients and would increase the value—and perhaps profits—of firms providing various specialized services.[106] In fact, the ability to attract talent from more diverse backgrounds than just the legal profession is one explanation for why the District of Columbia modified its Rule 5.4: law firms there can attract lobbyists and others with experience and connections in government agencies by offering them partnership positions.[107]

Additionally, law firms can benefit from other professionals with talents in business management or technology by offering them equity—and, again, incentivizing long-term commitment.[108] For example, specialists who focus on making centralized management decisions might allow lawyers to "dedicate their time and energy to practicing their profession . . . ."[109] Likewise, firms would benefit from dedicated technology specialists who could help firms with internet advertising, creating automated client intake applications, helping the firm create electronic visual aids for transactions or trials, etc.[110]

2. Other Arguments Against Rule 5.4

Another commonly cited argument against Rule 5.4 is that it perpetuates an inherently self-serving monopoly on legal services.[111] Besides the impact Rule 5.4 has on the price of legal services, it may contribute to a negative public perception of the legal profession. As noted above, concern for the public perception

105. *Id.*

106. Reardon, *supra* note 1, at 338–39 (noting that data from the United Kingdom supports the contention that ABS firms "provide higher quality services at lower prices").

107. *See* Black, *supra* note 9, at 513–14.

108. *See* Cobb, *supra* note 2, at 778–79 (noting that nothing in the current Rules "prohibit nonlawyers from assuming management roles in law firms and collecting a competitive salary"). *See also* Hadfield, *supra* note 5, at 49 (noting that although many of the legal costs in law firms are fixed and "do not vary as the scale of a practice increases," costs in figuring out the best strategies to run a practice would bring prices down—such as "identifying the best strategies for finding and retaining clients, the optimal systems for pricing, billing and collecting from clients, delivering productive customer service, and reducing errors"). *But see* Reardon, *supra* note 1, at 342–43 (noting that "research in the United Kingdom and in the field of organizational behavior supports the conclusion that employee ownership can provide significant benefits" to organizations via "increased productivity and return on assets") (internal quotation marks omitted).

109. Cobb, *supra* note 2, at 778.

110. Nonprofit law firms might benefit even more from the ability to attract business management talent which requires specialized management knowledge. *See* Black, *supra* note 9, at 531–32 (noting that "nonprofit law firms must comply with reporting requirements that are not relevant to for-profit firms").

111. Thomas D. Morgan, *The Evolving Concept of Professional Responsibility*, 90 HARV. L. REV. 702, 704 (1977).

of the legal profession was one of the main reasons behind the creation of the Kutak Commission.[112]

Abolishing Rule 5.4 may also have positive benefits for lawyer and nonlawyer quality of life. In the long run, innovation in software that helps administer standardized forms or helps lawyers with tasks such as legal research could reduce lawyers' workload.[113] Further, lawyers in a firm able to hire business management experts and invest in client growth would be able to focus on practicing the law instead of juggling multiple roles at once.[114] Moreover, allowing nonlawyer employees to have an ownership interest in the firms in which they work may not only increase their productivity but "has been shown to improve employee attitudes and commitment."[115]

3. Other Rules Already Achieve Rule 5.4's Purported Goals

The "fear of Sears," or the concern that big businesses will take over the legal industry and cause smaller law firms to fail, is already addressed by two other rules.[116] Rule 1.7 prohibits lawyers from representing clients with interests adverse to another client, and Rule 1.9 prohibits lawyers from representing clients if the lawyer previously represented a client in the same or similar matter with adverse

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112. *See* Black, *supra* note 9, at 503. *See generally* Morgan, *supra* note 111, at 708 (noting that "[o]nce one agrees that a layman can choose self-representation, it becomes difficult to argue that he should be unable to seek counsel on legal issues from a nonlawyer").

113. *See Legal Departments Continue to Face an Increased Workload, Budgetary Pressures and Slow Technology Adoption According to Research from Thomson Reuters Institute*, THOMSON REUTERS (Oct. 13, 2022), https://www.thomsonreuters.com/en/press-releases/2022/october/legal-departments-continue-to-face-an-increased-workload-budgetary-pressures-and-slow-technology-adoption.html [https://perma.cc/SXT2-95YQ] (reporting that corporate legal departments are turning to technology to "simplify workflow and manual processes" to cope with increasing work volume and mostly stagnant legal budgets; although the major impediment to technological utilization is the slow pace of technological innovation.).

114. Reardon, *supra* note 1, 342–43.

115. *Id.* at 343. *See also* Robert Saavedra Teuton, Developing Cooperation: Discovering Supportive Legal Frameworks and Policies for Worker Owned Cooperatives 40–43 (Sept. 26, 2018) (Master's thesis, Northern Arizona University), https://openknowledge.nau.edu/id/eprint/5293/1/Teuton_R_2018_Developing_cooperation.pdf [https://perma.cc/HFG5-TUFC]. And these benefits are apart from those stemming from the alignment of short-term and long-term equity interests discussed above; so there may be many more benefits for younger lawyers because older partners would have incentives to invest in newer lawyers' growth, development, and well-being (reduced turnover)—even if older partners know they won't be working at the firm much longer. For more about how to create a happier and healthier law firm environment, *see generally* Joe Regalia and David Wallace, Clients and Lawyers Unite: The Dysfunction of Law Firm Teams Needs A Cure, 48:2 U. DAYTON L. REV. 57 (2022), https://media.licdn.com/dms/document/C4D1FAQFSNK2XwR0FRg/feedshare-document-pdf-analyzed/0/1676757519492?e=1677715200&v=beta&t=AKNBkPsKlfGTINv9cNhu_hUALXa38y2I9BlfHphdhgE [https://perma.cc/M76Z-CJEM] (outlining the challenges and some solutions in fostering a happier and psychologically healthier legal workplace environment).

116. Cobb, *supra* note 2, at 775.

interests to the current would-be client.[117] These Rules make it unlikely that "unchecked growth and domination of the legal marketplace" will come to fruition.[118] One or even a few law firms could not represent all potential clients at once without representing clients, former and current, whose interests are adverse to one another—multiple law firms representing different clients would be a necessity.

The concern that the integrity of the legal profession will be eroded by profit-seeking behavior "is weak."[119] Unless a law firm is a nonprofit law organization, they are already in the business of making a profit, and "pressures to prioritize profits, even at a client's expense, are already pressed upon lawyers."[120] Rules other than Rule 5.4 can still address concerns about ethics in the legal profession, as they do now when profit-seeking incentives are present. Additionally, concern that corporations will try to keep the prices of legal services high while cutting costs is unlikely: corporations cannot avoid the laws of basic economics.[121] Those corporations that find ways to reduce the cost of legal services will do so to compete with other corporations. This competition will drive down the cost of legal services over time.[122]

The concern about lawyers' independent professional judgment "is arguably only voiced by lawyers."[123] Rule 2.1 already states that lawyers "shall exercise independent judgment,"[124] and this Rule would not be eliminated with nonlawyer ownership. Data from England and Australia suggest that allowing nonlawyer ownership in law firms will not undermine lawyers' independent judgment.[125] Using one metric, "disciplinary complaints against lawyers have remained static or dropped significantly in the years since" England and Australia permitted nonlawyer ownership.[126]

However, the concern about a corporation's ability to fund litigation is not unfounded. Although some states have banned third-party litigation financing, many allow and regulate it via their own laws.[127] Currently, litigation financiers enter into contracts with individual clients and law firms and take a share of profit if their party wins (usually plaintiffs) or the firms are paid over a period of time (usually

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117. *Id.*; MODEL RULES OF PRO. CONDUCT rs. 1.7, 1.9 (AM. BAR ASS'N 2020).

118. Cobb, *supra* note 2, at 775.

119. Reardon, *supra* note 1, at 344.

120. *Id.* at 344–45 (2017) (noting that lawyers face incentives to settle a case before trial when they are on a contingency fee case and that billable hour requirements are created to "emphasize maximizing profits").

121. *See* Asmundson, *supra* note 60.

122. *See id.*

123. Reardon, *supra* note 1, at 349.

124. MODEL RULES OF PRO. CONDUCT r. 2.1 (AM. BAR ASS'N 2020).

125. Reardon, *supra* note 1, at 349–50.

126. *Id. See also* Engstrom et al., *supra* note 1, at 19–22 (exploring evidence from England and Wales that suggests that allowing for nonlawyer equity ownership in those jurisdictions has not "negatively impacted the quality of legal services").

127. Jarrett Lewis, Note, *Third-Party Litigation Funding: A Boon or Bane to the Progress of Civil Justice?* 33 GEO. J. LEGAL ETHICS 687, 691 (2018), https://www.law.georgetown.edu/legal-ethics-journal/wp-content/uploads/sites/24/2020/09/GT-GJLE200029.pdf [https://perma.cc/2Y6B-W67E].

defendants).[128] Allowing litigation financiers to have an equity interest in law firms will give them "more say in how firms spend money and which cases they take."[129] Although law firms can be disciplined for bringing frivolous suits, corporations with equity interests in a law firm could skirt jurisdictional laws that only regulate the contractual relationships between litigation financiers, law firms, and party litigants.[130]

II. ARIZONA'S RULE 5.4 ABOLITION

The highest court in a given jurisdiction regulates the practice of law in that jurisdiction.[131] In 2019, the Arizona Supreme Court abolished Arizona Ethics Rule 5.4, which had previously prohibited nonlawyers from any ownership interest in legal services organizations.[132] The rule change stemmed from a November 2018 Arizona Supreme Court Administrative Order establishing the Task Force on Delivery of Legal Services (the "Task Force"). The Task Force was charged with restyling, reviewing, or recommending changes to a number of administrative and ethical rules—including a potential Rule 5.4 change[133]—and noted that the high cost of legal services was a major impediment to low- and middle-income households' ability to access the justice system.[134] Further, the Task Force concluded that Rule 5.4 "no longer serves any purpose, and in fact may impede the legal profession's ability to innovate to fill the access-to-civil-justice gap."[135] So, in August 2020, the Arizona Supreme Court abolished Rule 5.4.[136]

In November 2020, the Arizona Supreme Court replaced Rule 5.4 with a section of the Arizona Code of Judicial Administration that regulates Alternative Business Structures ("ABSs").[137] An ABS is "a business entity that includes nonlawyers who have an economic interest or decision-making authority in a firm

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128. *See, e.g.*, Eileen Bransten, *Litigation Finance 101*, LEXSHARES, https://www.lexshares.com/litigation-finance-101 [https://perma.cc/QG6Y-CTC3]. *See also How Litigation Finance Works*, BLOOMBERG L. (Feb. 24, 2020), https://pro.bloomberglaw.com/brief/how-litigation-finance-works/ [https://perma.cc/4HVG-LB44] (explaining how in the United States in 2020 alone 40 litigation funders invested nearly $2.5 billion in legal cases).

129. Skolnik, *supra* note 66.

130. This is not inherently a bad thing, depending on which side of the particular litigation one advocates for.

131. Gorelick & Traynor, *supra* note 24. *See also In re* Shannon, 876 P.2d 548, 571 (Ariz. 1994) (stating that the Arizona Supreme court has repeatedly declared "that the practice of law is a matter *exclusively* within the authority of the Judiciary").

132. Ariz. Order No. R-20-0034, *supra* note 74.

133. *In re* Establishment of the Task Force on Delivery of Legal Services and Appointment of Members, Admin. Order No. 2018-111 (Ariz. 2018) (noting that "[p]romoting Access to Justice is Goal 1 of the Judiciary's Strategic Agenda") (internal quotation omitted) [hereinafter Ariz. Admin. Order No. 2018-111].

134. ARIZ. SUP. CT. TASK FORCE, *supra* note 73.

135. *Id.* at 15.

136. Ariz. Order No. R-20-0034, *supra* note 74.

137. *See In re* Arizona Code of Judicial Administration § 7-209: Alternative Business Structures, Admin. Order No. 2020-173, 1–2 (Ariz. 2020) [hereinafter Ariz. Admin. Order No. 2020-173].

that provides legal services."[138] For example, an ABS might be a firm in which a nonlawyer is an equity partner with other lawyers. The nonlawyer partner may be someone who provides nonlegal expertise, such as a software developer, marketer, lobbyist, or business manager. Additionally, an ABS could be a firm that is wholly owned by nonlawyers but employs lawyers to provide legal services. ABSs may also include multidisciplinary practices, which are firms that offer "both legal and nonlegal services separately in a single entity" (e.g., a company that provides both access to capital and bankruptcy legal services).[139]

In May of 2021, only three firms had taken advantage of the Arizona Rule change; by April 2021, eight firms;[140] by October 21, 2022, a total of 29 firms had leveraged the new regime.[141] Three big-tech legal service providers—LegalZoom, Axiom, and Elevate[142]— have taken advantage of the ABS structure.[143] One firm that used the Rule change was a traditional law firm that is now 50% owned by nonlawyers; another was not a traditional law firm before the Rule change but wished to include legal services alongside its tax and accounting services.[144] At least one of the firms is a subsidiary of another business that will passively invest in the firm.[145] One firm will operate as a personal injury and mass tort law firm, another is a boutique business law firm, and a third "will have subscription-based bilingual legal services" available for small businesses and consumers.[146] Seven of the

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138. *Id.* at 1; Reardon, *supra* note 1, at 308–09 (providing three definitions of an ABS).

139. SIMON, *supra* note 41.

140. *ABS Directory*, ALT. BUS. STRUCTURES PROGRAM (April 18, 2022), https://www.azcourts.gov/Portals/0/ABS/2021%20Directory/ABS%20Directory%204-18-222.pdf?ver=KIy2UAVCbcrmyTWeBR4KjA%3d%3d [https://perma.cc/B9EN-6MN7].

141. *ABS Directory*, ALT. BUS. STRUCTURES PROGRAM (Nov. 16, 2022).

142. LegalZoom is a publicly traded online platform that provides legal services to "millions of consumer" clients online. Engstrom et al., *supra* note 1, at 26–27. However, before taking advantage of Arizona's Rule change, it could not directly employ lawyers, so it had to enter into contractual relationships with independent lawyers who then provided services to clients. *Id.* LegalZoom is able to mass market legal services on the internet and establishes a fee for legal services that are usually flat fees. *Id.* LegalZoom then charges the independent attorneys a marketing fee. *Id.* These kinds of online legal services have raised ethics concerns; but notwithstanding those concerns, the ABA has endorsed LegalZoom. *Id.* Additionally, LegalZoom already owns a law firm in the United Kingdom. Elevate is a corporate-facing law firm that also operates in the United Kingdom. *Id.*

143. *Id.* at 37.

144. Lyle Moran, *Permitting Alternative Business Structures Could Spur Tech Innovation, Arizona Justice Says*, ABA J. (Mar. 8, 2021, 5:20 PM), https://www.abajournal.com/news/article/permitting-alternative-business-structures-could-spur-tech-innovation-arizona-justice-says [https://perma.cc/WP8D-V2JC].

145. Sara Merken, *Arizona Approves Five More Entities for New Legal Business*, REUTERS (Aug. 27, 2021, 1:24 PM), https://www.reuters.com/legal/legalindustry/arizona-approves-five-more-entities-new-legal-business-structure-2021-08-27/ [https://perma.cc/XBZ9-3CAJ].

146. *Id.*; *ABS Directory*, ALT. BUS. STRUCTURES PROGRAM (Sept. 27, 2022), https://www.azcourts.gov/Portals/26/ABS/Directory/ABS%20Directory%209-27-2022.pdf?ver=Nnqjpxy-Vs7La-pjanyIrg%3d%3d [https://perma.cc/R83M-7HVS].

approved ABS business, as of September 2022, had addresses outside of Arizona: Idaho, Colorado, Utah, California, Texas, Illinois, and Washington, D.C.[147]

In one study of nineteen firms that took advantage of Arizona's Rule change as of June 30, 2022, most aimed to serve consumers and small businesses.[148] In this same study, the top three legal sectors represented were business, end-of-life planning, and injury, respectively.[149] Most of the nineteen Arizona law firms analyzed in the study sought more than 50% or more nonlawyer ownership.[150] Ten out of nineteen of these firms "are organized and managed as traditional law firms."[151] Five of nineteen are "entities with nonlawyer ownership or structured as a for-profit corporate entity" offering primarily law-related services—companies like LegalZoom, Axiom, and Elevate.[152] And four of the nineteen firms are non-law companies expanding into the legal field—"companies whose primary business sits outside the legal sector but [seek to] offer 'one-stop-shop' multidisciplinary professional services or begin to build a legal vertical."[153]

A. The ABS Regulatory Environment

The Arizona Supreme Court created an entirely new regulatory environment for the practice of law when it abolished Rule 5.4 and changed or abolished 12 other Ethics Rules, 16 Supreme Court Rules, and 1 Witness Rule.[154] This new regulatory environment is what governs ABSs.[155]

ABSs are regulated by the Arizona Administrative Office of the Courts, a state-funded office.[156] The ABS program receives funding from "monies received for licensure fees, costs, and civil penalties."[157] And the ABS program is overseen by a Director who not only performs administrative functions but also has the power to "direct division staff to conduct investigation[s] into alleged acts of misconduct or violations in relation to initial licensure, renewal of license or licensure after a

147. *Id.*
148. Engstrom et al., *supra* note 1, at 22, 41.
149. *Id.* at 42.
150. *Id*. at 43.
151. *Id.* at 37.
152. *Id.*
153. *Id.* at 37–38.
154. *See* Ariz. Order No. R-20-0034, *supra* note 74. This new regulatory environment includes a modified rule for fee sharing arrangements and the practice of law by paraprofessionals—professionals that are not full attorneys but are qualified to practice in designated fields.
155. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 1 (the Arizona Supreme Court defines an ABS as "a business entity that includes nonlawyers who have an economic interest or decision-making authority in the firm and provides legal services in accord with Supreme Court Rules 31 and 31.1(c)").
156. *Id.* at 2.
157. *Id.*

period of revocation."[158] Moreover, the Director can refer matters to the Arizona State Bar and can initiate compliance audits of an ABS license holder.[159]

B. How Firms Can Use the ABS Structure

A law firm seeking to become an Arizona ABS must first apply for a license.[160] The licensure process includes an initial application,[161] supporting documents,[162] fees payable to the Arizona Supreme Court,[163] and a background check.[164] The application is designed to analyze a firm on two levels: as a business entity and in terms of personnel.[165] Additionally, the questions in the application are designed to ensure that ABSs comply with the regulatory scheme established by the Arizona Supreme Court in its Administrative Order.[166]

On the business entity level, the license application asks, among other things, about the general nature of the business the ABS will conduct.[167] Additionally, the application asks how the ABS will advance one or more regulatory objectives, including "promoting the public interest, promoting access to legal services, advancing the administration of justice and rule of law, encouraging an

158. *Id*. However, keep in mind that although the ABS program has the power to investigate and makes recommendations to the Arizona Supreme Court to license or renew licenses, the Arizona Bar is ultimately responsible for disciplinary decisions. *Id.* at 5 (stating that the "State Bar of Arizona is responsible for receiving, processing, investigating, seeking interim suspension of and prosecuting disciplinary matters against [an] ABS and an ABS's members, and shall carry out this responsibility according to the Supreme Court Rules applicable to members of the state bar."). Therefore, sanctions can be entered by a presiding disciplinary judge, hearing panel, or by the Arizona Supreme Court, *id.* at 19, like in other bar related disciplinary matters. *See The Discipline Process*, STATE BAR OF ARIZONA, https://www.azbar.org/for-lawyers/lawyer-regulation/discipline-bar-charges/the-discipline-process/ [https://perma.cc/38CY-YFN8] (last visited Feb. 18, 2023).

159. *Id.*

160. *Id.* at 5.

161. *Id.* at 5–11 (An applicant may be subject to a personal credit review independent of the mandated background check upon submission of a completed application. Additionally, the reviewing committee may request an informal interview with an applicant to clarify information submitted with the application or to investigate allegations of misconduct "received after the applicant's original licensure expired.").

162. *Id.*

163. *Id.* at 6, 22–23 ("Fees are not refundable or waivable," and vary by size of an ABS that does not otherwise qualify as a traditional law firm, profit status (non-profit versus for-profit), location (international versus national and whether an organization is located in Arizona or outside of Arizona if the organization is a non-profit), and whether an ABS's primary business is to provide legal services—therefore a "traditional law firm" under the regulatory framework—or not otherwise a traditional law firm.).

164. *Id.* at 5–11, 22–23 (the background check includes a "readable fingerprint card or affidavit in lieu of a fingerprint card" and a criminal background check).

165. *See generally Application for Initial License of Alternative Business Structure*, ARIZ. SUP. CT. (July 2021), https://www.azcourts.gov/Portals/0/ABS%20Application%20for%20Initial%20License%20%28Sample%29.pdf [https://perma.cc/RV5K-JG79].

166. *Compare* Ariz. Admin. Order No. 2020-173, *supra* note 137, at 5–11 *with* ARIZ. SUP. CT., *supra* note 165.

167. ARIZ. SUP. CT., *supra* note 165.

independent, strong, diverse, and effective legal profession," and "promoting and maintaining adherence to professional principles."[168] This inquiry is consistent with Arizona's purported socio-legal goals in abolishing Rule 5.4.[169] Moreover, the application seeks to preserve some of the protections the traditional Rule 5.4 sought to provide when it asks how the ABS's governance structure and policies will ensure that: (1) legal services are provided to consumers in a way that is consistent with lawyers' professional responsibilities; (2) proper standards of work are maintained; (3) "the lawyer makes decisions in the best interest of clients"; (4) the other Arizona Rules regarding confidentiality are maintained; and (5) business practices "do not interfere with a lawyers' duties and responsibilities to clients."[170] Further, the application asks about the relationships the ABS might have with other entities, such as with a parent corporation of the ABS and entities that may assist or partner with the ABS,[171] the presence of shareholder or voting agreements that would affect decision-making,[172] the list of individuals who would derive a profit from the operations of the ABS,[173] and sources of finance the ABS intends to use.[174] These questions are consistent with the Arizona Supreme Court Order establishing the ABS regime and also aim to maintain the goals of Rule 5.4 after its abolition.

On the personnel level, the initial ABS application requires information about "Authorized Persons," which are defined as persons or entities holding "equal to or more than 10 percent of all economic interests in the" ABS or a person with decision-making authority within the ABS.[175] Apart from general background information such as whether an Authorized Person has ever been found guilty of a felony or misdemeanor,[176] the application probes the character and fitness of all Authorized Persons through questions about involvement "in a business that has

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168. *Id.*

169. *See* ARIZ. SUP. CT. TASK FORCE, *supra* note 73.

170. ARIZ. SUP. CT., *supra* note 165, at 5–9 (The ABS must also describe how it "will comply with Arizona's Rules of Professional Conduct for lawyers, Code of Conduct for Entities and for Owners and Managers." Additionally, the ABS must explain the procedures it plans on using to ensure confidentiality of client information and for checking for conflicts of interests. Further, the ABS must describe policies and procedures to "ensure no inducements are offered to clients or potential clients for choosing the business's course other than for the best interest of the client.").

171. *Id.* at 8 (including the entity an ABS may share staff, premises, or data with). *See also* Ariz. Admin. Order No. 2020-173, *supra* note 137, at 14 (mandating that an ABS "fully disclose all relationships to any parent company or organization, and currently paid or unpaid officers, directors, owners, and boards of directors, and any and all company subsidiary dba's operating in any state").

172. ARIZ. SUP. CT., *supra* note 165, at 8.

173. *Id.*

174. *Id.*

175. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 1, 13 (Economic interest also includes the right to use intangible property based in whole or in part on the firm's gross revenue or profits. Moreover, decision making authority is further defined as one who can (1) make legally binding decisions on the ABS; (2) "control or participate in the management or affairs of the ABS;" or (3) make decisions affecting the day-to-day or long-term management, policy, and operations of the ABS.).

176. ARIZ. SUP. CT., *supra* note 165, at 6.

declared bankruptcy,"[177] the commission of "material misrepresentation, omission, fraud, or corruption in business or financial matters,"[178] and conduct "showing incompetence or a source of injury and loss to the public."[179] Presumably, the inquiry into Authorized Persons' character and fitness seeks to hold potential nonlawyer owners to a similar standard that lawyers must face in their character and fitness evaluations. And ABS program officials will likely investigate the proposed capital and decision-making structures of license applicants to make sure investors are not seeking to skirt authorized person requirements through obscure capital or organizational structures.

Besides listing its Authorized Persons, an initial ABS applicant must also appoint and list a Compliance Lawyer and a Designated Principal.[180] A Designated Principal is merely someone who communicates with the ABS licensure division staff about "any administrative, procedural, or operational issues."[181] A Compliance Lawyer must be an Arizona lawyer, a manager or employee of the ABS, not have been subject to discipline by any state bar during the previous ten years, and must possess the legal credentials and experience to ensure ethical obligations and standards of professionalism are complied with.[182] Apart from ensuring that lawyers within an ABS comply with ethical and professional responsibilities,[183] Compliance Lawyers must also ensure Authorized Persons comply with the ABS regulatory scheme and must notify the Arizona State Bar if they reasonably believe the ABS has substantially breached regulations.[184]

The ABS Code of Conduct holds all members of an ABS responsible for adhering to the professional and ethical codes of conduct of the regulatory scheme.[185] Additionally, ABS members who are also members of the Arizona State Bar—not just the Compliance Lawyer—must adhere to the ethical and professional obligations of the legal profession; this hearkens back to the purported goals of Rule 5.4 of maintaining the integrity of the legal profession.[186] Noncompliance with the

177. *Id*. at 8.
178. *Id.* at 6.
179. *Id*.
180. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 14–16.
181. *Id.* at 14.
182. *Id.* at 15.
183. *Id.* at 15–16
184. *Id.* (compliance lawyers who fail to carry out their duties are subject to suspension and other sanctions).
185. *Id.* at 23–25 (Some of the codes of conduct all ABS members must adhere to include: not representing clients if the representation would create a conflict of interest as defined in other ethics rules; not engaging in conduct that would compromise the professional independence of lawyers or other legal service providers; maintaining records of compliance with ABS regulations; maintaining "effective governance structures, arrangements, systems, and controls" to ensure compliance with the Rule; monitoring "financial stability and business viability[;]" and separating the property of legal services clients from the ABS's property).
186. *Id.* at 24. Under this rule, Arizona ABSs can only employ Arizona lawyers who hold an Arizona bar license if those lawyers are employed to provide legal services. *Id.* However, the reverse may not be true: an Arizona barred lawyer employed by an Arizona ABS may be able to provide legal services in another jurisdiction if they work with an attorney

regulatory scheme or code of conduct by an ABS or any of its members can result in any of the disciplinary actions that an Arizona-licensed attorney would be subject to.[187] For example, an ABS that fails to give notice of an impending merger or acquisition—regardless of whether the other business is also an ABS—is subject to disciplinary action such as a license suspension.[188]

Once division staff have reviewed and verified an application for completeness,[189] the Committee on Alternative Business Structures ("the Committee") recommends whether to issue an initial license.[190] The Committee can recommend denial on grounds that an Authorized Person has committed a misrepresentation in business or financial matters,[191] that an Authorized Person has ever violated a rule or decision by a professional regulatory entity,[192] or that an Authorized Person is "incompetent or a source of injury and loss to the public."[193] An applicant is entitled to a hearing to appeal the Committee's denial recommendation.[194] Alternatively, an applicant can wait 12 months after a denial of licensure by the Supreme Court and reapply.[195] But the applicant must address the issues that resulted in the original denial of licensure.[196]

In a recommendation for approval, the Committee must state whether the ABS furthers one of the Arizona Supreme Court's regulatory objectives for the ABS program[197] and whether the ABS's governance structure ensures adequate

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licensed in that other jurisdiction. *See infra* note 206 and accompanying text. But even if an Arizona barred lawyer, who is barred in another jurisdiction, does not violate any Arizona rules for working in an Arizona ABS that provides legal services in the other jurisdiction, they would likely violate the other jurisdiction's Rule 5.4 if their work had any relation to the Arizona ABS. And lawyers that are Authorized Persons who violate ethics rules in other jurisdictions must report ethics violations in other jurisdictions to the ABS program—putting their ABS's license in jeopardy. *See id.* at 8, 12–13. Just to be clear, notwithstanding the last example, there is nothing stopping a lawyer barred in Arizona and another jurisdiction from providing legal services in Arizona while employed in an Arizona ABS.

187. *Id.* at 19–22 (Thus, an ABS or any of its individual members could face a sanction, admonition, probation, or monetary penalties—among other things—for noncompliance with ABS regulations or the code of conduct. However, the regulations do specify how an ABS can reinstate its license after a suspension or license revocation.).

188. *See id.* at 15, 22–23 (Merger or acquisition fees are equivalent to fees for an initial licensure. The same is true for fees for reinstatement of a license after suspension or revocation.).

189. *Id.* at 6, 8 ("division staff shall advise the applicant of deficiencies").

190. *Id.* at 7–8.

191. *Id.* at 8.

192. *Id.* (searching also for any disciplinary actions relating to professional or occupational licenses or certificates—without a qualifying that search to only Arizona).

193. *Id.* at 7.

194. *Id.* at 9.

195. *Id.* at 10. The procedure to be reinstated after an ABS license that has already been granted and has been revoked is different—in that case, an ABS must wait 3 years before it can apply for reinstatement. *Id.* at 19.

196. *Id.*

197. *Id.* at 7 (these include social goals such as "promoting access to legal services").

safeguards against regulatory infringement.[198] Once a license is granted and after approval from the Arizona Supreme Court, the license will expire after a year unless a license holder files "a timely and complete renewal application," in which case "the existing license does not expire until the administrative process for review of the renewal" is complete; but unlike the initial license process, renewals can be denied by the Committee alone.[199]

Without permission, ABSs in Arizona cannot do business within Arizona under an assumed name; i.e., they cannot use any other name than that which appears on the ABS license.[200] An ABS, however, can use the label "Arizona licensed" in its name or title—a label no other business can adopt to induce the public to believe the business holds a valid Arizona ABS license.[201] Additionally, a list of every ABS in Arizona must be maintained online for public access.[202] Presumably, public notices and disclosures have been instituted as yet another safeguard ensuring that members of the public know if they are dealing with an ABS. However, it is unclear (and doubtful) that members of the public know or care about the ramifications of being represented by a law firm owned even in part by nonlawyers.

C. Legal Issues for Arizona Firms Using the ABS Structure

If a conflict arises between the ABS regulatory framework and other professional codes of conduct, the regulatory framework and Supreme Court Rule 42 shall prevail.[203] Supreme Court Rule 42 includes ABA Model Ethics Rules 1.6 governing confidentiality, and Rules 1.7, 1.8, and 1.10 governing conflicts of interest.[204]

One of the most significant legal issues for ABSs is their ability to work with clients in other jurisdictions.[205] Arizona ABSs would not be able to provide legal services, on their own, to clients in jurisdictions with the traditional Rule 5.4—

198. *Id.* (such as ensuring that lawyers provide legal services to consumers with "independence consistent with the lawyers' professional responsibilities").

199. *Id.* at 4, 12–13. The ABS regulatory scheme also sets out a procedure for submittals of untimely renewal applications which requires a finding of good cause for the untimely filing. Importantly, the Committee can deny a license renewal for criteria Authorized Persons are scrutinized for in the initial licensure phase. *Id.* at 8, 13.

200. ARIZ. SUP. CT., *supra* note 165, at 12 (permission must come in the form of a certificate filed with the Division Staff "setting forth the name under which business will be transacted").

201. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 11.

202. *Id.* at 3, 14 (other ABS information subject to the public includes final compliance audit reports and whether an ABS has professional liability insurance). *See also ABS Directory*, ALT. BUS. STRUCTURES PROGRAM (Jan. 19, 2022), https://www.azcourts.gov/Portals/0/ABS%20Directory%20as%20of%20January%2019%2C%202022.pdf [https://perma.cc/32JN-3FGX] (listing the ABSs licensed in Arizona as of January 19, 2022, along with the ABSs' license numbers, business addresses, and other contact information such as emails and phone numbers).

203. *Id.* at 25.

204. *Compare* ARIZ. R. SUP. CT. 42, *with* MODEL CODE OF PRO. CONDUCT rs. 1.6–1.8, 1.10.

205. This is also a major concern for lawyers in Washington, D.C. and may be one reason why ABSs are not more common there. *See* Cobb, *supra* note 2, at 783.

which constitutes the vast majority of states—even if the lawyers in the ABS were separately licensed in that non-Arizona jurisdiction. However, the ABA has opined that a lawyer practicing in another U.S. jurisdiction could share fees with a lawyer who practices in a firm that includes a nonlawyer partner.[206] Additionally, a lawyer or law firm in a traditional Rule 5.4 jurisdiction could passively invest in an Arizona ABS and refer clients to that ABS as long as they complied with disclosure requirements in Model Rule 1.8(a).[207]

Yet another major issue is the potential dilemma that an ABS Compliance Lawyer might face when reporting a "substantial breach of the regulatory requirements of [the ABS] code or the ethical and professional obligations of lawyers."[208] According to Andrew Halaby, an attorney at Greenberg Traurig in Phoenix, Arizona, a law firm that has reviewed "dozens of ABS initial license applications," it is very usually the case that an ABS's corporate counsel and Compliance Lawyer are the same person.[209] Thus, a Compliance Lawyer as a corporate counsel is in an attorney-client relationship with the ABS that employs him or her; and a Compliance Lawyer's "reporting duties plainly conflict with the ABS's [attorney-client] privilege."[210] One line of reasoning that solves this dilemma is to assume that any information that must be disclosed necessarily "falls outside the privilege" because "information that must be reported cannot, as a matter of law, have been made in confidence."[211] Accordingly, when an ABS attorney reports to their Compliance-Lawyer-Corporate-Counsel of a substantial regulatory or ethical breach, because the disclosure is mandatory the moment the communication happens, it is not made in confidence and therefore is not covered by the attorney-client privilege.[212]

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206. ABA Comm. on Ethics & Pro. Resp., Formal Op. 464, 2 (2013) [hereinafter ABA Formal Op. 464].

207. *See* ABA Formal Op. 499, *supra* note 17, at 2–3. However, a truly passive investor-lawyer who might want to stay clear of the ABS scheme's Authorized Person requirements would have to make sure they did not own more than 10% of the ABS—either by themselves or through other entities they may own or control. *See supra* note 175 and accompanying text. Relatedly, but as a somewhat esoteric matter, even passive investor-lawyers must be mindful of the "rarely invoked Model Rule 5.7," which subjects a lawyer to the Rules of Professional Conduct when for exercising control over an entity that provides "law-related services;" and that control can be "individually or with others if the lawyer fails to take reasonable measure to assure that the person obtaining the law-related services knows that the services are not legal services" without the protections of the client-lawyer relationship. Keith R. Fisher, ABA Ethics Opinion Cracks Open Door to ABS, ABA (Dec. 15, 2021), https://www.americanbar.org/groups/business_law/publications/blt/2021/12/aba-ethics-opinion/ [https://perma.cc/873X-XGW2]; MODEL CODE OF PRO. CONDUCT r. 5.7 (a).

208. Andy Halaby, *Arizona ABS Compliance Lawyers and the Attorney-Client Privilege*, GREENBERG TRAURIG 3–4 (Sept. 26, 2022), https://www.gtlaw.com/en/insights/2022/9/arizona-abs-compliance-lawyers-and-the-attorney-client-privilege [https://perma.cc/43SM-F8SL].

209. *Id.* at 4 n.23.

210. *Id.* at 6.

211. *Id.* at 7.

212. *Id.* at 7–8.

This mandatory reporting requirement and lack of an attorney-client privilege will probably lead to less reporting to the Compliance Lawyer in general.[213] Preemptively, ABSs should remind employees that the Compliance Lawyer has a duty to disclose substantial ethical violations and that the Compliance Lawyer is the ABS's lawyer (this is doubly true if the Compliance Lawyer and corporate counsel are the same person).[214] Further, the Compliance Lawyer tasked with disclosing a major ethical violation should only disclose the bare amount of factual information necessary to convey that an ethical breach has occurred.[215]

Another legal issue that could arise involves an ABS sharing general client information with investors. Although Arizona Rule 1.6 prohibits lawyers from sharing client information without a client's informed consent,[216] it is unclear whether this rule would protect aggregated client information that cannot be used to identify specific clients.[217] For example, an ABS might try to provide its investors with recommendations on what to do based on client information. Imagine an ABS that specializes in zoning and real estate services providing its investors with information about which real estate parcels it should buy at specified price ranges.[218] On one hand, using relevant, aggregate client information to provide reports to investors is not necessarily divulging individual client information outright; on the other hand, client information would be necessary for compiling those reports.[219]

Finally, the entire ABS regulatory system in Arizona may be prohibited under the structure of Arizona's Constitution,[220] which separates the judicial and legislative branches.[221] This potential controversy stems from the fact that the Arizona Supreme Court instituted a regulatory regime that impacts the very nature of the corporate structure of ABSs—more than the mere regulation of the legal profession.[222] While the Arizona Supreme Court has the power to regulate the legal profession[223] and also performs oversight and adjudicatory functions to oversee and

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213. *Id.*

214. *Id.*

215. *Id.* at 7–10 (advocating for eliminating the mandatory reporting requirement). Another solution is for the Arizona Bar to give guidance on this issue and ensure that ABSs or their conduct will only be scrupulously inspected if notice is given about grave or serious violations or notice of violations are given persistently and systematically.

216. ARIZ. RULES OF PROF. CONDUCT r. 1.6.

217. *See* ABA Formal Op. 499, *supra* note 17, at 5 (noting that "the issue of disclosure of confidential information by an ABS is a developing area of law and beyond the scope of this opinion").

218. A law firm could also gather information by distributing questionnaires to its clients and providing the information received to its investors.

219. *See* ARIZ. RULES OF PROF. CONDUCT r.1.6(a) (stating that "[a] lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent").

220. Maya Steinitz, *The Partnership Mystique: Law Firm Finance and Governance for the 21st Century American Law Firm*, 63 WM. & MARY L. REV. 939, 991–2 (2022).

221. ARIZ. CONST. art. III (stating that "[t]he power of the government of the state of Arizona shall be divided into three separate departments, the legislative, the executive, and judicial . . . .").

222. Steinitz, *supra* note 220, at 970.

223. *See supra* Part II.

interpret the law,[224] it does not have general *legislative* powers, which are reserved for the Arizona Legislature.[225] And by instituting the ABS structure, the Arizona Supreme Court has changed the corporate legal environment as applied to ABSs.[226] For example, shareholder primacy, a decades-old corporate legal concept, requires that directors and officers of a corporation maximize shareholder profits.[227] In an Arizona ABS, the duties imposed by the corporate shareholder primacy rule conflict with "Arizona's legal ethics, which are premised on stakeholder primacy."[228] Consequently, a corporate ABS's board is under additional legal duties—apart from its obligation to make legal decisions to maximize shareholder profit—to ensure that the ABS fully complies with Arizona's legal ethics rules. In essence, Arizona's Supreme Court created a new corporate structure, analogous to a benefit corporation that many states, including Arizona, have authorized through their legislative branches.[229] The Arizona Supreme Court could find it has the implied right to create or otherwise regulate corporate structures that practice law—which in and of itself is not an inherent right—as the head regulator of the legal profession in Arizona.

III. OVERVIEW OF WASHINGTON, D.C. RULE 5.4

Washington, D.C.'s Rule change was considered after the ABA rejected the Kutak Commission's recommendations.[230] The group assigned to explore the D.C. Rule change was known as the Jordan Committee[231] and was particularly concerned with the notion that nonlawyers could only be employees in a law firm—even if the nonlawyer had substantial experience in their field and was a professional with all the necessary certificates (such as an accountant or psychologist).[232] As a result, the District of Columbia was the first U.S. jurisdiction to allow nonlawyer ownership in a law firm.[233]

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224. *See supra* Part II.

225. ARIZ. CONST. art. III.

226. Steinitz, *supra* note 220, at 946.

227. *Id.*

228. *Id.* (noting that the Court may resolve this conflict by interpreting the ABS regulations as more specific than general corporate principles such as shareholder primacy—and thus prevail over the corporate principles. However, this presupposes that the Court has the authority to enact business legislation under the Arizona Constitution.).

229. *Compare* ARIZ. REV. STAT. § 10-2431 (mandating that an Arizona benefit corporation's board of directors shall consider the board's actions or inactions on the corporation's shareholders, community and societal factors, local and global environment, etc.) *with* Ariz. Admin. Order No. 2020-173, *supra* note 137, at 23–25 (stating that all members of an ABS, lawyers and nonlawyers alike, must adhere to the ethical rules, and that ABSs must "maintain effective governance structures, arrangements, systems and controls to ensure 1) compliance with the requirements of the [Rules]; and 2) . . . [that] anyone employed, associated with, or engaged do not cause or substantially contribute to a breach of the ethical rules").

230. Gilbert & Lempert, *supra* note 34, at 393.

231. The committee was named after Robert Jordan of Steptoe & Johnson. *Id.* at 392.

232. *Id.* at 393. *See also* Black, *supra* note 9, at 513 (noting that one theory as to why D.C. changed its Rule 5.4 is so that D.C. law firms could better leverage the interpersonal connections of lobbyists and government officials).

233. Black, *supra* note 9, at 513.

Washington, D.C.'s Rule 5.4 allows nonlawyer and lawyer partnerships in the practice of law if: (1) the law firm's sole purpose is to provide legal services to clients;[234] (2) anyone with managerial authority or a financial interest in the law firm abides by the Washington, D.C. Rules of Professional Conduct;[235] (3) the lawyers with managerial authority or financial interest in the law firm "undertake to be responsible for" nonlawyer partners' conduct "to the same extent as if" the nonlawyers were lawyers under Rule 5.1;[236] and (4) all of the previous conditions of this Rule are solidified in writing.[237] Additionally, a lawyer in such a firm must maintain their independent professional judgment in rendering legal services.[238] The purpose of this Rule is to permit nonlawyers to work with lawyers to deliver legal services "without being relegated to the role of an employee,"[239] which was one of the main concerns of the Jordan Committee.[240]

A. How D.C. Firms Have Used the Modified Rule 5.4

Unlike Arizona, Washington, D.C. does not keep statistics about firms' use of its modified Rule 5.4.[241] It is therefore hard to gather data about how many D.C. firms have used the modified Rule 5.4 and in what ways.[242] Some commentators, however, note that few D.C. firms have used D.C.'s modified Rule because of "ambiguities concerning the ability for firms outside of D.C. to share fees with firms that have nonlawyer" partners.[243] Nonetheless, at least one member of the "Big Four" accounting firms—PwC—opened a law firm in D.C. to assist its U.S. clients with international business issues.[244]

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234. D.C. RULES OF PROF. CONDUCt r.5.4(b)(1) (D.C. BAR ASS'N 2007).

235. *Id.* r. 5.4(b)(2).

236. *Id.* r. 5.4(b)(3). Washington, D.C.'s Rule 5.1 states that lawyers with managerial authority over other lawyers must take efforts to assure those under their supervision conform to the other rules of professional conduct, and holds them accountable for not doing so. *Id.* r. 5.1. A lawyer can also be liable under D.C.'s Rule 5.1 if the lawyer also had specific knowledge of the conduct, orders it, or ratifies it. *Id.*

237. *Id.* r. 5.4(b)(4).

238. *Id.* r. 5.4(c).

239. *See Id.* r. 5.4 cmts. 3, 7. For an example of a D.C. law firm with a nonlawyer partner, see Sam Skolnik, *D.C. Nonlawyer Partner Rule Spurs Interest as States Mull Change*, BLOOMBERG L. (Oct. 30, 2019, 1:55 AM), https://news.bloomberglaw.com/us-law-week/d-c-nonlawyer-partner-rule-spurs-interest-as-states-mull-change [https://perma.cc/F2T4-76X7] (reporting about a nonlawyer partner in a law firm that "is a public relations expert and former CNN journalist").

240. Gilbert & Lempert, *supra* note 34, at 393–94.

241. Skolnik, *supra* note 239 (noting that some law firms, according to a D.C. bar spokeswoman, did use the D.C. Rule change when it took effect in 1991).

242. *See id.* (implying that some law firms that have used D.C.'s Rule are based outside of D.C.).

243. Cobb, *supra* note 2, at 783.

244. Faucon, *supra* note 82, at 2286–87. *See also* Skolnik, *supra* note 239 (reporting that "ethics lawyers and bar officials also said they know of a number of instances in which Rule 5.4 has been utilized. This includes at least one Big Four accountancy and at least one former AmLaw 100 law firm.").

B. Advantages and Downsides of the D.C. Rule 5.4

The D.C. Rule 5.4 change represents a modest alteration to the traditional Rule and has not undermined the legal profession,[245] but it contains some serious limitations: (1) firms must solely engage in providing legal services; (2) firms are unable to raise capital outside debt financing or through individual partners; (3) it is ambiguous if firms can form partnerships with firms in other jurisdictions; and (4) it is uncertain if confidentiality requirements for nonlawyer professionals conflict with legal ethics. Other concerns are addressed in the next section when comparing the D.C. and Arizona Rules.

D.C. Rule 5.4(b)(1) severely limits firms' ability to provide anything but legal services.[246] Therefore, multidisciplinary practices, where consumers can hire one firm to perform multiple services (such as hiring one firm for both legal zoning issues and architectural restructuring services), are not permitted.[247] However, the Rule does not define the term "legal services," which might result in a limited definition without more guidance.

Additionally, the D.C. Rule does not "permit an individual or entity to acquire all or any part of the ownership of a [law firm]."[248] This means that law firms cannot raise any equity capital from outside investors. Consequently, D.C. law firms must adhere to the traditional means of law firm capital fundraising: individual partners and debt financing.

As noted above, some commentators believe that more firms haven't taken advantage of the D.C. Rule because firms don't know whether they can share fees with firms in other jurisdictions.[249] However, the ABA issued an opinion in August 2013 concluding that it would be permissible to split legal fees between firms that reside in traditional Rule 5.4 jurisdictions and firms that have lawful nonlawyer partners.[250] Unfortunately for D.C. law firms, the ABA opinion did not say that a single D.C. firm with nonlawyer partners and offices in multiple jurisdictions can take fees for itself.[251] Thus, because the vast majority of jurisdictions still adhere to

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245. *See* Skolnik, *supra* note 239.

246. D.C. RULES OF PROF. CONDUCT r. 5.4(b)(1) (D.C. BAR ASS'N 2007).

247. *See id.* r. 5.4 cmt. 7 (2019) (stating the "the [R]ule 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," etc.).

248. *Id.* r. 5.4 cmt. 8.

249. Cobb, *supra* note 2, at 783.

250. ABA Formal Op. 464, *supra* note 206, at 1–5 (noting that forcing clients to hire D.C. firms separately would "likely annoy clients and add unnecessary complexity to a common arrangement with no constructive purpose," and that an outright prohibition on non-D.C. firms being able to work D.C. firms with nonlawyer partners would "unreasonably impair the ability of lawyers to work alongside" other lawyers who "may be best suited to serve a particular client or resolve a particular matter").

251. *See id.* at 4 (stating that the division of legal fees "by a lawyer or law firm in a Model Rules jurisdiction with a lawyer or law firm in another jurisdiction that permits the sharing of legal fees with nonlawyers does not violate Model Rule 5.4(a) simply because a nonlawyer could ultimately receive some portion of the fee under the applicable law of the other jurisdiction").

some version of the traditional Rule 5.4, D.C. law firms cannot expand outside their own jurisdiction.[252]

Further, the D.C. Rule does not clarify how firms should proceed when a disclosure conflict arises between nonlawyer professionals' ethical rules and ethical rules governing attorneys.[253] For example, a law firm in D.C. could have a social worker partner subject to mandatory reporting requirements, but the D.C. Rule flatly imposes other rules of professional conduct on all persons with "managerial authority or holding a financial interest" in the firm; such rules may require nondisclosure of certain information in conflict with the social worker's reporting requirement.[254] Accordingly, different professional and legal disclosure and nondisclosure requirements may conflict and may produce legal ambiguities or frequent rule violations by D.C. law firms.[255]

Perhaps because the D.C. Rule modification was so modest,[256] or maybe because of some of the aforementioned potential legal ambiguities, the D.C. Bar is considering abolishing Rule 5.4 altogether.[257] In a 2020 press release, the D.C. Bar asked firms for comments about whether there was a demand for integrated legal and nonlegal services, whether the D.C. Rule was too restrictive, how third-party litigation funding would be impacted by a rule change, and how the D.C. Rule has been beneficial for clients.[258]

IV. COMPARING ARIZONA'S RULE 5.4 ABOLITION WITH WASHINGTON, D.C.'S RULE 5.4

The Arizona Rule requires compliance with an entire regulatory scheme, whereas the D.C. Rule only requires a firm to comply with a fixed set of rules. The Arizona ABS scheme is fluid in that licensed ABSs must continually (at least annually after the initial licensure is authorized) work with the Arizona Supreme Court and division staff of the ABS licensing program to maintain its license.[259] The Arizona ABS scheme is regulated by a government organization that imposes its own rules and oversees all ABSs, and thus, like any organization, the ABS regulatory system is more subject to change.[260] The D.C. Rule, however, is more

252. *See* Black, *supra* note 9, at 513–14.

253. Faucon, *supra* note 82, at 2333.

254. D.C. RULES OF PROF. CONDUCT r. 5.4(b)(2) (D.C. BAR ASS'N 2007); Faucon, *supra* note 82, at 2333. *See also* D.C. RULES OF PROF. CONDUCT r.1.6(e) (D.C. BAR ASS'N 2007) (listing the circumstances in which a lawyer may reveal information relating to the representation of a client).

255. Faucon, *supra* note 82, at 2333.

256. This is true especially in terms of not allowing outside equity investing and not allowing true multidisciplinary practices that provide more than just legal services.

257. Debra Cassens Weiss, *DC Bar Considers Relaxing its Already-Lenient Rules to Allow Nonlawyer Ownership of Law Firms*, ABA J. (Jan. 27, 2020, 10:40 AM), https://www.abajournal.com/news/article/dc-bar-considers-relaxing-its-already-lenient-rules-to-allow-nonlawyer-ownership-of-law-firms [https://perma.cc/VHM6-74JN].

258. D.C. BAR, *supra* note 19.

259. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 12–13.

260. Change can be minute, like a change in the information asked in forms or applications, or it can be larger. Changes can occur gradually, as the regulatory system develops, or can happen more quickly.

fixed and static, because it does not require a governmental organization to administer.

The D.C. Rule and Arizona ABS Regulations both impose ethical obligations on nonlawyers within firms owned or managed in part by nonlawyers,[261] and both impose some duty on lawyers within the firm to oversee nonlawyer conduct.[262] The Arizona Regulations, however, more comprehensively assure nonlawyer compliance with ethical obligations. From the outset, an Arizona firm must explain how its members will comply with legal ethics obligations when it applies for licensure.[263] This requirement must be repeated annually with each licensure renewal.[264] Further, each ABS must be monitored by a Compliance Lawyer who has an affirmative duty to report any breaches of the ABS Code of Conduct and other legal professional responsibilities.[265] Therefore, the Arizona Regulations provide a much more rigorous and continuous system for ensuring compliance with legal professional responsibilities.

Unlike the Arizona Regulations, the D.C. Rule does not impose any disclosure requirements. Thus, consumers of legal services in D.C. would not know if their law firm was owned by nonlawyers unless they asked or the firm advertises as such.[266]

Two of the most important differences between the Arizona regulations and the D.C. Rule relate to the scope of what firms in each jurisdiction can identify as their purpose and the ability of firms to raise capital through passive investment. First, D.C. firms with nonlawyer owners can only have one purpose: providing legal services.[267] This means that D.C. firms cannot be truly multidisciplinary practices like Arizona ABSs can. For example, a D.C. architecture firm cannot also have a division that provides legal services unless the firm ceased providing architectural services. There is no such restriction in the Arizona Regulations. Further, the D.C. Rules do not allow for passive investments in law firms,[268] whereas the Arizona Rules allow them.

The major differences between the D.C. Rule and Arizona Regulations stem from each of their respective purposes. The drafters of the D.C. Rule were primarily concerned with the inability of nonlawyers to become partners in a law

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261. *See* Ariz. Admin. Order No. 2020-173, *supra* note 137, at 23–25 (stating all members of an Arizona ABS must adhere to the ethical codes of conduct); D.C. RULES OF PROF. CONDUCT r. 5.4(b)(2) (D.C. BAR ASS'N 2007) (stating that nonlawyers with managerial and ownership interest in the firm must abide by the D.C. Rules of Professional Conduct).

262. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 23–25; D.C. RULES OF PROF. CONDUCT r. 5.4(b)(3) (D.C. BAR ASS'N 2007) (stating that the lawyers with managerial authority or financial interest in the law firm "undertake to be responsible for" nonlawyer partners' conduct "to the same extent as if" the nonlawyers were lawyers).

263. ARIZ. SUP. CT., *supra* note 165, at 5–9.

264. Ariz. Admin. Order No. 2020-173, *supra* note 137, at 12.

265. *See id.* at 15–16.

266. The lack of disclosure requirements in Washington, D.C. also makes research about D.C. firms owned in part by nonlawyers much more difficult.

267. D.C. RULES OF PROF. CONDUCT r. 5.4(b)(1) (D.C. BAR ASS'N 2007).

268. *Id.* r. 5.4 cmt. 8.

firm merely because of their nonlawyer status,[269] whereas the purpose of the Arizona Regulations was to promote access to justice and legal innovation.[270] The schemes' respective purposes explain the differences in ability to raise capital (presumably allowing Arizona firms to invest in innovative technologies) and what firms in each jurisdiction can make their purpose (again, D.C. firms' main purpose must solely be to provide legal services).

V. CONCLUSION AND RECOMMENDATIONS

Arizona's Rule 5.4 abolition is a major step in the right direction in terms of expanding access to justice and promoting legal innovation. The Arizona regulation doesn't merely abolish Rule 5.4; it also replaces it with something that can fulfill the Rule's purported goals: maintaining legal ethics in the practice of law.[271] Because of robust oversight and continuing ethical assessments required for annual licensure renewal, Arizona ABSs might likely be *more* aligned with legal professional standards than regular law firms. Moreover, any change within reason should be welcome considering the state of access to justice in the United States.

Without more affirmative requirements for ABSs to help expand access to justice, it is unlikely that the Arizona Regulation alone will make a significant impact on such an expansion in the short term. Most of the entities that had an ABS license as of March 2022 were estate planning and business firms.[272] Most of the firms that had taken advantage of the Rule change since September 2022 were either business, estate planning, or personal injury firms.[273] These firms are unlikely to be the kind of firms that lower the cost of legal services simply because they can attract nonlawyer partners unless these firms can attract enough capital investments to develop technology that significantly lowers their cost of providing legal services. Even the ability to acquire large amounts of capital investments to invest in legal technology is doubtful because of the jurisdictional limits Arizona firms must comply with—namely, they can only practice in Arizona.[274]

Although a majority of ABSs as of June 2022 were "developing some kind of technological innovation,"[275] more needs to be done to promote technological innovation in Arizona ABSs.[276] Utah, which amended its Rules around the same

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269. Gilbert & Lempert, *supra* note 34, at 393–94.

270. Ariz. Admin. Order No. 2018-111, *supra* note 133 (noting that "[p]romoting Access to Justice is Goal 1 of the Judiciary's Strategic Agenda") (internal quotation omitted).

271. *Id.*

272. *ABS Directory*, ALT. BUS. STRUCTURES PROGRAM (Feb. 2022), https://www.azcourts.gov/Portals/0/ABS/2021%20Directory/ABS%20Directory%20February%202022.pdf?ver=p_SGja8K2SLAQq-upQXa7g%3d%3d [https://perma.cc/K86P-PXYZ].

273. Engstrom et al., *supra* note 1, at 22, 42.

274. However, if ABA Formal Opinion 464 is followed, law firms in other jurisdictions can partner with Arizona ABSs and split legal fees with them. *See* ABA Formal Op. 464, *supra* note 206, at 1–5.

275. Engstrom et al., *supra* note 1, at 22, 44.

276. For many reasons stated above, current legal nonprofits will never be able to fill the access to justice gap for low-income people. *See supra* Introduction. But advanced

time as Arizona, provides an example of one way to do this. Utah firms can apply for an Unauthorized Practice of Law ("UPL") Waiver, which allows "entities using nonlawyers or software to practice law."[277] This waiver provides protections to software developers and nonlawyers that provide "generalized legal information and basic scrivening help."[278] Indeed, a Stanford Law School analysis of Arizona and Utah law firms that took advantage of the different rule changes showed that the Utah UPL waiver appeared "to be critical to serving lower-income populations," and that only Utah saw firms seeking to serve primarily "low-income people."[279] In fact, one-third of Utah firms sought to use the UPL waiver.[280] In the long term, software has the greatest potential to reduce the cost of legal services because it has the potential to cut boundless human hours completely out of the resolution of legal problems.

One area where the Arizona Regulation could make a significant difference in promoting access to justice is in third-party litigation. Because investors can invest and influence litigation through ownership in a law firm, investors can use their expertise in third-party litigation to help their law firm develop procedures, such as intake and screening practices, that maximize their chances for the greatest return on investment. Additionally, these investors might have access to more information that can help them refine their third-party litigation investment practices in Arizona and elsewhere.

To increase the impact of the Rule 5.4 abolition on access to justice, ABSs should be required to provide minimum hours of pro bono legal services.[281] These pro bono hours can be imposed based on firm size.[282] Alternatively, firms should be able to substitute pro bono legal services for consulting qualified nonprofit or governmental organizations. The consulting services could be aimed at implementing more efficient or effective legal practices—including providing software. Firms that develop legal technology with access to capital could provide these services at greater benefit to society than those merely offering pro bono legal services.

To clear up any potential legal ambiguity concerning the constitutionality of the ABS scheme,[283] the Arizona ABS business structure should be solidified in

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technology could greatly improve nonprofit firms' ability to fill the access to justice gap. For a discussion on one such technology, artificial intelligence, see generally Maoyu Wang, 5 ARIZ. L.J. EMERGING TECH. 1 (forthcoming Spring 2023).

277. Engstrom et al., *supra* note 1, at 6.

278. *Id.* at 16.

279. *Id.* at 7, 40.

280. *Id.* at 39.

281. Other Arizona ethics rules will ensure that pro bono hours are met competently and diligently. *See* ARIZ. R. SUP. Ct. 42 (requiring competence and diligence, among other things).

282. Licensure fees are already adjusted based on firm size. *See* Ariz. Admin. Order No. 2020-173, *supra* note 137, at 22–23.

283. This stems from the fact that the Arizona Supreme Court developed its own corporate form without having explicit legislative powers to do so outside of its recognized power to regulate the legal industry. *See* Steinitz, *supra* note 220, at 939, 991.

an Arizona statute.[284] Lastly, consumers of an ABS's products or services should be granted causes of action (even if only limited ones) to sue the ABS for failure to promote access to justice or violation of ethical duties or the ABS code of conduct.[285] This would provide yet another level of oversight to ABS ethical compliance, and would help ensure ABSs adhere to the intent of the ABS regulations: to promote access to justice.

All things considered, the Arizona ABS scheme is a significant, positive advancement. It is the first Rule 5.4 modification adopted by any jurisdiction that allows for equity investment from people outside the firm while also providing firms with access to equity capital for innovation and economic stability (unlike the D.C. Rule). Additionally, the Rule also allows firms to be truly multi-disciplinary (again, unlike the D.C. Rule). Indeed, these benefits make Arizona law firms among the most structurally flexible legal firms in the United States. This flexibility is a prerequisite to innovation in the legal field, moving the legal field in a giant leap in the right direction to see new horizons and possibilities.

284. *Id.* at 992.
285. *Id.* at 1006–07.