MDPs IN THE GLOBAL ECONOMY

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MDPs (multidisciplinary practices) are the issue du jour in both the legal and accounting professions today. Big Five[1] law practices inspire intense, heated debate between and within the legal and accounting professions. But it is not just the Big Five. Banks and insurance companies hire lawyers to provide estate administration, probate and estate planning services. Labor, environmental and employee benefits consulting firms employ lawyers to provide the same services to their clients that those same lawyers previously provided to clients of the law firms with which they were affiliated.

MDP Defined

Technically, an MDP is an organization owned wholly or in part by nonlawyers offering lawyer-provided services to the public for a fee. In common reference it also applies to "linked partnerships," ostensibly independent law firm and non-legal organizations operating under a management services and / or marketing contract. Many US lawyers equate MDPs and ancillary businesses, erroneously. However, MDPs are not the same as ancillary businesses (authorized under Rule 5.6 of the ABA Model Code), which are non-legal businesses wholly or partly owned by a law firm, as services provided by ancillary businesses by definition do not include legal services.

History of MDPs

MDPs emerged in Germany, following World War II, where tax accountants and lawyers were allowed to practice in partnership together. In France, with a bifurcated profession, counseil juridques (solicitors or office lawyers) could practice in nonlawyer owned organizations, but avocats (barristers or trial lawyers) had to practice in independent law firms. In the mid-1990s, the French professions were merged. Counseil

[1] Big Five "Professional Service" firms include Arthur Andersen, Deloitte & Touche, Ernst & Young, KPMG and PricewaterhouseCoopers.

juridques were "grandfathered" as avocats, creating de jure MDPs overnight in Big Five firms that had employed counseil juridques.

In the UK, where technically MDPs have historically been banned, linked partnerships emerged beginning in 1993 with the formation of Garrett & Co., tied by a management services contract to Arthur Andersen. Percentage-wise, Garrett & Co. is one of the fastest-growing law firms in the UK, with over 200 lawyers at the present time. Since then, English firms have been authorized to use trade names, and KPMG (KLegal) and PricewaterhouseCoopers (Landmark Legal Services) have entered the fray as has Ernst & Young on the backs of two of the original founders of PricewaterhouseCooper's law practice. The Law Society of England and Wales is in the process of liberalizing rules to allow MDPs. Despite the prohibition against MDPs in Scotland, the largest firm in the jurisdiction joined Anderson Legal Services in 1998.

In Spain where MDPs technically are banned, Arthur Andersen in 1996 acquired the largest law firm in the country, J&A Garrigues. Since then, PricewaterhouseCoopers and others have established their own MDP practices, despite the ban.

In the Netherlands, Arthur Andersen and Price Waterhouse (before the Coopers & Lybrand merger) challenged the Dutch legal profession's ban on MDPs in the courts, resulting in a decision upholding the ban by a trial court in Amsterdam. That decision has been appealed to the European Court of Justice, as violative of European Union competition laws. A decision is expected by 2002. However, since then the Dutch bar has negotiated an agreement with Ernst & Young to allow an MDP approach to law practice, provided a majority of the interest in the firm are held by lawyers. It is being done through a linked partnership. Big Five MDPs also exist in one form or another in Norway, Sweden, Finland, Denmark, Ireland, Luxembourg, Belgium, Switzerland, Austria, Greece, Italy and Portugal.

Finally, in Eastern Europe and Russia, Big Five MDPs are primary providers of legal services. In total, over 6,500 lawyers are employed in Big Five MDPs in Europe.[2]

Elsewhere in the world, MDPs have emerged in Australia and New Zealand, and through linked partnerships in some of the more liberal Asian countries, including Hong Kong and Singapore. They are prohibited in Japan, Korea and India. In Latin America, Big Five MDPs have emerged in most country capitals. In Canada, a *de facto* MDP was created by Ernst & Young in the late 1990s, through an affiliation with Donohue & Associates, then a tax boutique in Toronto. Lawyers have been added in both Toronto and Calgary, and Donohue & Associates now claims almost 100 lawyers. The Law Society of Upper Canada, regulatory body for Ontario, has formally allowed MDPs in linked form or where 51% or more of the interests are held by lawyers. Other provinces are following suit.

[2] The European Lawyer, London, Issue 6, November 2000, page 21.

In the US the situation is more complicated. MDPs are banned in every jurisdiction except Washington, DC, where nonlawyers can be owners in law firms, but 51% of the interest in the firm needsto be in the hands of lawyers. It is estimated that Big Five firms in the United States currently employ more than 5,000 lawyers, providing services to clients, for a fee. However, due to the ban on MDPs, Big Five firms generally claim these lawyers are not involved in law practice, per se, but rather in "consulting" or in the practice of "tax" or "M&A," not law. The Big Five view in the United States appears to be that law practice reserved to independent law firms consists only of appearance in court on behalf of clients.

Supporters and Opposition

Although viewed as a disagreement between accountants and lawyers, supporters of MDPs include not only CPAs, but also those lawyers who would work for or believe others should have the right to work for nonlawyer-owned organizations. Opposition comes primarily from two sources: the organized bar, and the Securities and Exchange Commission.

Opposition to MDPs by the organized bar is based on four principles, each of which is disputed by proponents of MDPs. They are:

1. Unauthorized Practice of Law (UPL). Opponents claim that provision of services by lawyers in Big Five firms and other MDPs represents UPL. However, UPL statutes generally are designed to protect the public against attempts at providing legal advice or services by nonlawyers. On that basis, MDPs are not engaged in UPL — the services are being provided by lawyers licensed in the jurisdiction in which they operate.

2. Lawyer Independence. Opponents of MDPs claim that lawyer independence is threatened by sharing of fees and profits between lawyer and nonlawyer owners. Proponents of MDPs claim that a lawyer in a private law firm faces equal threat or conflict between best interests of the client and the interests of the firm, as do lawyers in an MDP. Private law firms also scrutinize carefully fees collected by the lawyers and such scrutiny could influence the lawyers' handling of the client's case.

3. Conflicts of Interest. MDPs opponents claim that there is an inherent conflict of interest between an auditor's duty to disclose client information and a lawyer's duty to conceal it. MDP proponents claim that "Chinese Walls" or "screens" can be employed to avoid such a problem, just as they are in law firms which obtain client waivers and create such devices to protect against conflicts.

4. Compromise of Client Privilege. Opponents of MDPs claim that client privilege might be compromised by the duty of auditors to disclose confidential information which lawyers are obliged to protect. Proponents

claim that the fact that client privilege can only be waived by the client renders this issue moot.

ABA Position

Although the American Bar Association (ABA) does not regulate lawyers, it is quite influential over the state agencies who do so, mostly the state Supreme Courts. The ABA Model Rules are in effect at least in part in most of the 50 US jurisdictions.

In 1998, Philip Anderson, ABA President, appointed a Commission on MDPs which conducted hearings during 1998 and 1999. At the ABA Annual Meeting in Atlanta in 1999 it issued its report, allowing but providing for special regulation of MDPs. The issue was remanded by the ABA House of Delegates to the Commission for further study, among other things to demonstrate market demand for MDPs (despite the fact that 5,000 lawyers currently employed in US Big Five firms represent approximately two billion dollars in fees). Further hearings were held in 1999 and 2000, and a revised proposal was submitted by the Commission in the spring of 2000. In the meantime, the New York State Bar submitted a competing proposal to continue the ban on MDPs which was presented to the House of Delegates as an alternative to the Commission's proposal. The alternative proposal proposed by the New York State Bar was adopted by the House of Delegates at the ABA Annual Meeting in New York in July of 2000 to the exclusion of the Commission's proposal. That resolution also dissolved the ABA Commission. In effect, it preserves the status quo, and to many observers, it was the worst possible decision, effectively a "cop out." It preserves an environment of uncertainty in which *de facto* MDPs thrive without <u>any</u> effective regulation, assuring that the issue will return with even higher stakes at some point in the future.

SEC Position

The most significant opposition to MDPs in the United States comes from the SEC, in the form of the Independence Commission appointed by Chairman Arthur Levitt. That Commission focused on conflicts of interest, from two perspectives. One is the personal interests of partners, employees and family members of employees and partners of Big Five firms presented by their ownership of shares in companies audited by the Big Five firm, in violation of current SEC rules. In 1999, over 4,000 violations of that stock ownership prohibition were identified at PricewaterhouseCoopers, and it was recognized that other Big Five firms were likely to experience the same problem, were they scrutinized. The interesting reaction of the Big Five to the PWC situation was not to call for divestment of those interests, but rather to suggest that the rules be changed to allow such ownership. That reaction fueled the argument by lawyer-opponents of MDPs that accountants view conflicts much less seriously and more liberally than do lawyers.

The other conflict subject of the SEC Independence Commission review was that between the auditor and its firm's advisors, primarily in the form of management advisory or consulting services offered by Big Five firms to audit clients. The SEC's proposal that would prohibit provision of such services to audit clients was challenged by the Big Five,

ultimately resulting in a position that would require only disclosure on the part of the Big Five. Still, it led to divestiture and hiving off of consulting services wholly or in part at Arthur Andersen, PricewaterhouseCoopers, Ernst & Young and KPMG.

The Status Quo

The result of all of this is that official bans on MDPs continue, but MDPs also continue to thrive in a *de facto* form. The organized bar has opposed MDPs in only one instance, in Texas, where a complaint alleging unauthorized practice of law by Arthur Andersen filed by the Texas Bar was later withdrawn. Regulators appear to be fearful of the consequences of challenging the Big Five due to not only their economic strength (and the "war chests" purportedly reserved to meet such legal challenges) but also to the implicit threat that such a challenge would be met with a counter-claim alleging violation of anti-trust laws. The Big Five are likely to defend attempts at limiting their activity legally by coloring them as attempts by the organized bar at economic protectionism, an accusation likely to fall on sympathetic ears in the public.

The Future

In the final analysis, ultimate resolution of the MDP issue will depend upon client and public demand for such services. It is predictable that the MDP movement will be publicly supported because:

1. Clients want choice. The American Corporate Counsel Association (ACCA) officially adopted a position in favor of MDPs as providing more choice, despite all of the regulatory impediments which highlight the potential harm to public and clients arising from such organizations. ACCA, consisting of in-house lawyers in corporations, is the most sophisticated, organized group of consumers of legal services in the world, and likely to recognize the "dangers" of MDPs quicker and more thoroughly than any other group.

2. Clients want one-stop shopping for multidisciplinary services, as evidenced by the industry convergence between banking, insurance and stock brokerages, and the early successes of MDPs where they have been permitted to practice.

3. Clients want global capability in professional service providers, as evidenced by the success of international and global independent law firms, and early successes of Big Five global MDPs.

The stage is set for the MDP issue to mature as pressures in the 50 jurisdictions in the US increase. Ultimately, what the US does on this issue will have an influence worldwide. It may well be that resolution of the issue will depend upon the form of the MDP, and that linked partnerships and liberalization against prohibition of trade names will resolve the issue. Ernst & Young's support of its Washington, DC linked partnership, McKee Nelson, Ernst & Young, may well become the model. The alternative would be to maintain the name of the independent law firm, identifying it permanently as a member of the worldwide legal services provided by one of the Big Five firms. In any event, it will be difficult to hold

back the clock on this issue in the US permanently, given the popularity overseas of MDPs and increasingly within the United States, albeit in a *de facto* sense, so far.

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