NEW YORK STATE BAR ASSOCIATION
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New York State Bar Association
Committee on Professional Ethics

Opinion 1081 (1/8/16)

Topic: Unauthorized practice of law; professional independence; fee splitting.

Digest: Lawyers employed by a debt management company may not provide legal services to the company's customers. Whether services are legal services is a question of law that we cannot answer, but if the services *are* legal services, then the inquirers may be aiding a nonlawyer in the practice of law, allowing a nonlawyer to interfere with their independent professional judgment, sharing legal fees with a nonlawyer, and providing incompetent representation to clients, and they may have a personal conflict of interest. If the services *are not* legal services and the clients do not believe they are legal services, then the only applicable ethical rules would be those that apply even where the lawyer does not have an attorney-client relationship, such as the prohibition against conduct involving dishonesty.

Rules: 1.1(a), (b) & (c), 1.7(a), 5.2(b), 5.4(a), (c) & (d), 5.5(b), 5.7(a) & (c), 8.4

Modifies N.Y. State 992

FACTS

1. Two lawyers are employed by a debt management company (the "Company"). The lawyers work under the direction of a nonlawyer who is the managing director of the Company. The main responsibilities of the lawyers are (i) to provide advice to and answer questions from the Company's customers (whom the inquiring lawyers describe as their "clients"); (ii) to contact banks and other credit institutions in an effort to settle customers' outstanding debt for less than the full amount owed; and (iii) counseling customers regarding their rights in litigation. The Company has approximately 700 clients. The lawyers are concerned that they are not able to handle that volume of work, and that consequently their clients will be brought into litigation and risk having judgments taken against them.

2. The Company also has proposed that the salaries of the inquirers be augmented by $100 for each account settled for more than $10,000.

3. The inquirers express concern that they will be unable properly to counsel the Company's clients regarding litigation because of their limited resources and the large number of clients.

QUESTIONS

4. May a lawyer work for a debt management company where the ratio of debt management clients to debt management company lawyers means that the lawyers may not be able properly to counsel the company's clients?

5. May a lawyer working for a debt management company accept a proposed salary structure in which the lawyer will receive an extra payment for each larger account that the lawyer settles? In particular, would that salary structure constitute impermissible fee sharing?

OPINION

Are the Debt Management Company's Services Legal Services?

6. Before we can answer the questions posed, it is important to know whether the services provided by the Debt Management Company are legal services, non-legal services, or a combination of the two. *See* N.Y. State 860 (2011). If any of the services are legal services, then the New York Rules of Professional Conduct (the "Rules") apply. If they are nonlegal services, then some of the Rules may apply, *e.g.*, Rule 8.4 (a lawyer shall not engage in conduct involving dishonesty, fraud, deceit or misrepresentation), but others may not, *e.g.,* rules that specifically require an attorney-client relationship. And if the services are a combination of legal and nonlegal services, then Rule 5.7(a) determines whether the Rules apply. If the services are a combination and the nonlegal services are not distinct from legal services, then the Rules would apply to the nonlegal services as well as the legal services. *See* Rule 5.7(a)(1).

7. The Rules do not define "legal services." Comment [2] to Rule 5.5, dealing with the unauthorized practice of law, states, in part: "The definition of the 'practice of law' is established by law and varies from one jurisdiction to another." As we noted in N.Y. State 860 (2011):

> We do not render opinions on matters of law (and defining unauthorized practice is a matter of law), but we note that Ethical Consideration 3-5 of the former Code of Professional Responsibility gave the following helpful guidance: "Functionally, the practice of law relates to the rendition of services for others that call for the professional judgment of a lawyer. The essence of the professional judgment of the lawyer is the educated ability to relate the general body and philosophy of law to a specific legal problem of a client . . . ."

8. Rule 5.7 contains a definition of "nonlegal services" that applies when lawyers or law firms provide "nonlegal services" to clients. Rule 5.7(c) provides:

> (c) For the purposes of this Rule, "nonlegal services" shall mean those services that lawyers may lawfully provide and that are not prohibited as an unauthorized practice of law when provided by a nonlawyer.

9. As we noted in N.Y. State 860, this definition begs the question of what constitutes the unauthorized practice of law, a question of law we cannot answer. It seems likely that some of the activities of the debt management firm, such as negotiating a reduction in the client's indebtedness based on the client's ability to pay (and not on the legal validity of the obligation), do not constitute legal services. Other activities, such as advising clients about legal rights, collections litigation, and litigation risks, probably are legal services. In either case, the inquirers must make the determination. In this connection, the inquirers should consider (among other things) whether the Company's clients are informed (or otherwise are made aware, either expressly or implicitly) that the inquirers are lawyers, whether the advice given to the clients is legal advice, whether the clients believe that they are receiving legal advice, and whether the clients believe that their communications with the inquirers are protected by attorney-client confidentiality. The inquirers should also consider whether they themselves and/or the Company expressly or impliedly inform the credit institutions that they contact on the Company's behalf that they are lawyers.

<u>May the Inquirers Disclaim that They are Providing Legal Services?</u>

10. A second question is whether the Company or the inquirers may disclaim that the Company is providing legal services. N.Y. State 992 (2013) explored business structures in which a lawyer may work with a nonlawyer business person. The lawyer in Opinion 992 was seeking to work with a nonlawyer who planned to establish a "disability office" to help persons with government benefit matters (most of which did not require representation by legal counsel). We concluded that, even if a nonlawyer could perform services without engaging in the unauthorized practice of law, those same services constitute the practice of law when they are performed by a lawyer. *See also* N.Y. State 938 n.2 (2012) (although disability services may be performed by a nonlawyer, different questions would arise if a lawyer were to participate in providing the services, for example by meeting with customers or editing documents drafted by a licensed hearing representative).

11. N.Y. State 992 also said that a lawyer may not circumvent the Rules of Professional Conduct by performing legal services under a designation indicating that the lawyer is employed in a "non-legal capacity" even if a nonlawyer may perform the same services. Specifically, Opinion 992 said:

> Where an attorney is engaged, the client has a reasonable expectation that the attorney has the skills and qualifications beyond that of a non attorney representative, is governed by professional conduct rules, and is subject to civil liability for the representation.

12. We believe that the rationale of N.Y. State 992 would not apply, however, if the client understands that the services being provided are nonlegal services and is not aware that such

services are being provided by a lawyer. *See* N.Y. State 832 (2009) (if the shelf corporations were sold over the internet and the attorney was not identified anywhere on the website as a lawyer, and purchasers never communicated with the lawyer directly and had no opportunity to ask for advice, then the lawyer would not be giving legal advice to purchasers); N.Y. State 557 (1984) (when services are performed by a lawyer *who holds himself out as a lawyer*, they constitute the practice of law). *Cf.* Rule 5.7 (which recognizes that lawyers may provide legal services in one entity and nonlegal services in a separate entity, and that the nonlegal entity will not be subject to the Rules of Professional Conduct if the legal services and nonlegal services are "distinct" and the lawyer gives an appropriate disclaimer or the disclaimer is unnecessary). Of course, if the services would constitute legal services when performed by a nonlawyer, the Company could not avoid the unauthorized practice of law by disclaiming that they are legal services.

Consequences if the Debt Management Company's Services to Clients are Legal Services

13. If the debt management company's services to clients are legal services, then the Company would be providing legal services in violation of the Judiciary Law, which is a crime in New York. *See* Judiciary Law § 485-a (making certain violations of Judiciary Law §§478, 484, 486 and 495 a class E felony); Judiciary Law §495 (providing that no corporation or voluntary association shall (i) practice or appear as an attorney-at-law for any person in any court in this state, (ii) hold itself out to the public as being entitled to practice law, or (iii) furnish attorneys or counsel); Judiciary Law §478 (unlawful for any natural person to furnish attorneys or to render legal services); Judiciary Law §484 (no natural person shall ask or receive compensation for preparing pleadings of any kind in any action brought before any court of record in this state).

14. If the Company's services include legal services, the inquirers may also be in violation of several provisions of the Rules, discussed below.

Aiding Unauthorized Practice; Interference with Professional Judgment

15. Rule 5.5(b) prohibits a lawyer from aiding a nonlawyer in the unauthorized practice of law. If the Company is violating statutes or common law prohibiting the unauthorized practice of law, then the lawyers would be violating Rule 5.5(b).

16. Rule 5.4 contains a number of provisions intended to ensure the professional independence of a lawyer. *See* Rule 5.4, cmt. [1]. Rule 5.4(a) provides that a lawyer "shall not share legal fees with a nonlawyer," with exceptions not applicable here. If the Company's clients are paying the Company for legal services rendered by the inquirers, then the inquirers would be violating Rule 5.4(a). Rule 5.4(c) provides that "a lawyer shall not permit a person who . . . employs . . . the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services ...." If the lawyers here work under the direction of a nonlawyer, they may be violating Rule 5.4(c). *See* N.Y. State 1068

(2015) (discussing whether a lawyer could join with a claims recovery firm in an agreement to offer legal services to the public to be performed by the lawyer and the claims recovery firm on a systematic and continuing basis).

Lawyer Workload

17. Rule 1.1 contains provisions to protect clients against incompetence. Rule 1.1(a) states that a lawyer should provide competent representation to a client; Rule 1.1(b), prohibits a lawyer from handling a legal matter that the lawyer knows or should know he or she is not competent to handle; and Rule 1.1(c) prohibits a lawyer from intentionally failing to seek the objectives of the client through reasonably available means permitted by law and the Rules, and from prejudicing or damaging the client during the course of the representation. In N.Y. State 751 (2002), an opinion decided under the former Code of Professional Responsibility, we responded to an attorney for a government agency who believed that more matters were being assigned to individual attorneys than could be competently handled by those attorneys. We cited the Code provisions equivalent to those now in Rule 1.1 and concluded that it was a lawyer's duty to avoid accepting more matters than the lawyer could competently handle and to reduce his or her workload if it had become unmanageable. *See also* ABA 347 (1981). The obligation of a lawyer to act competently has not changed under the Rules.

18. In N.Y. State 751, we noted that, if the question of whether the lawyer could provide competent representation in light of the lawyer's workload was an arguable question of professional duty, then under the Code's equivalent of Rule 5.2(b), the lawyer could act in accordance with a supervisory lawyer's reasonable resolution of that question. If the supervisor is a nonlawyer, then Rule 5.2(b) would not apply, and the inquirers would need to make their own judgment as to whether they can represent all of their 700 clients competently.

Bonus Compensation

19. If the services provided are legal services, then the proposed bonus compensation proposal also raises questions about conflicts of interest. Under that proposal, the lawyers would receive $100 in additional compensation for each account settled for more than $10,000. That arrangement would create a potential personal conflict of interest for the lawyers under Rule 1.7(a)(2), which prohibits a lawyer from representing a client if "there is a significant risk that the lawyer's professional judgment on behalf of a client will be adversely affected by the lawyer's own financial ... interests." If the additional $100 would encourage the lawyer to settle a matter on terms less favorable to the client in order to qualify for the bonus, then the compensation arrangement would violate Rule 1.7 unless the conflict is consentable under Rule 1.7(b) and the lawyer obtains the client's informed consent, confirmed in writing.

Consequences If the Debt Management Company's Services to Clients are Not Legal Services

20. If the services to the clients of the Company are not legal services, and if neither the inquirers nor the Company holds the lawyers out as providing legal services to the Company's clients, then the provisions of the Rules on aiding in the unauthorized practice of law, fee sharing, interference with professional independence, competence and personal conflicts of interest would not apply. Nevertheless, the lawyers would remain subject to all Rules that do not depend on the existence of a legal representation or an attorney-client relationship. For example, the lawyers could not engage in illegal, dishonest, fraudulent or deceptive conduct and could not state or imply an ability to achieve results using means that violate the Rules or other law. See Rule 8.4(c), (e).

CONCLUSION

21. Lawyers employed by a debt management company under the direction of a nonlawyer managing director may not provide legal services to the company's customers. If the services *are* legal services, the inquirers may be aiding a nonlawyer in the practice of law, allowing a nonlawyer to interfere with their independent professional judgment, sharing legal fees with nonlawyers, and providing incompetent representation to clients, and they may have personal conflicts of interest. If the services *are not* legal services and the clients do not believe they are legal services, then the only applicable ethical rules would be those that apply even where the lawyer does not have an attorney-client relationship, such as the prohibition against conduct involving dishonesty.

(26-15)