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Professionalism and Non-Lawyer Involvement: Regulation of Incorporated Law Firms in Aotearoa New Zealand

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I Introduction

The provision of legal services is a powerful resource that must be regulated to ensure its effectiveness, transparency, reputation and standing in society.[1] Holding a practising certificate can be viewed as including rights and responsibilities. Only lawyers may provide legal services, and this right is regulated through the Lawyers and Conveyancers Act 2006, and corresponding regulation from the New Zealand Law Society. These regulations are designed to protect the public and consumers.[2] They extend not just to lawyers, but also the organisational structures through which they are permitted to operate.

Traditionally, law firms have tended to be structured as partnerships, although they are no longer restricted to this.[3] Lawyers within New Zealand may operate within a law firm that exists either as a partnership or as a company. However, ownership and control of a law firm must remain solely with lawyers, regardless of the firm's structure, placing legal practices at a disadvantage to other businesses within modern New Zealand. Restrictions placed on law firms are often encouraged by concern expressed around non-lawyer involvement leading to a loss of integrity and professionalism in legal services.

This article aims to examine New Zealand's current regulatory schemes around the organisational structures of law firms and consider potential reforms to improve the business position of legal practices in New Zealand. Part II will begin by summarising the organisational structures through which legal services may be provided. Part III will explain some of the specific advantages and disadvantages to operating a law firm as either a partnership or as a limited liability company. This will include an examination of the options and limitation when a firm is raising capital, the risk of partnership collapse, and the likelihood of a loss of professional standards if non-lawyers become involved in law firms. Part IV sets out New Zealand's current regulations around structuring law firms and considers whether, based on the aspects discussed in Part III, New Zealand has reached an appropriate balance when regulating how law firms may operate. Part V looks at comparative approaches, both to international regulation around legal services and domestic regulation regarding similar professions (both patent attorneys and accountants). It will articulate a specific discrepancy within New Zealand's

[1] New York State Bar Association "Report of the Task Force on Nonlawyer Ownership" (17 November 2012), at 3.
[2] Lawyers and Conveyancers Act 2006, s 6.
[3] Section 3.

regulation and consider the need for review. Finally, Part VI considers how New Zealand's law may be reformed to make incorporation a more viable option for law firms in modern New Zealand.

II Different Organisational Structures and Their Consequences

The Lawyers and Conveyancers Act 2006 sets out the organisational structures within which legal services may be provided to the public. Lawyers may operate as sole practitioners, or through a law firm which exists either as a partnership or a company.[4] This article focuses on legal partnerships and incorporated law firms. Sole practitioners and firms owned by sole proprietors are not considered in this article.

A What is a Partnership?

A partnership is defined as a relationship between people carrying on a business in common with a view to profit.[5] In New Zealand, partnerships are governed by the Partnership Law Act 2019. They are formed by partners merely entering into an agreement.[6] There are no formal steps required to create a partnership, and they do not need to be registered.[7] Partnership agreements are essentially private contracts. Persons who have entered into a partnership with one another are collectively called a firm.[8] A partnership typically involves joint ownership of property, sharing gross returns for the business, and provides the effect of receiving a share of the profits.[9] While the Partnership Law Act provides a default set of rules for the operation of partnerships in New Zealand, a specific partnership agreement may tailor the partnership rules to suit their specific needs.[10]

A new partner may not join the partnership, and a partner's interest in a partnership cannot be transferred to another person without the consent of all existing partners.[11] Typically, a partner may dissolve the partnership by giving notice to the other partners.[12] Legally, therefore, if a

[4] Section 9.
[5] Partnership Law Act 2019, s 9.
[6] Peter Watts, Neil Campbell and Christopher Hare *Company Law in New Zealand* (2nd ed, LexisNexis, Wellington, 2016) at 11.
[7] At 11.
[8] Partnership Law Act, s 10.
[9] Watts, above n 6 at 11.
[10] At 12.
[11] At 12.
[12] At 12.

partner were to leave a partnership (e.g., to retire), the existing partnership dissolves and a new partnership must be formed with the remaining partners.

To vary a partnership agreement requires the unanimous consent of the partners.[13] However, partners may unanimously contract out of this requirement in an earlier agreement, for example only requiring a majority of partners to alter the agreement.[14]

At common law, partners owe each other fiduciary duties.[15] Consequently, partners have an obligation of loyalty, fairness and good faith to one another. Under the Act, partners have a number of other imposed statutory obligations, including a duty to provide each other with true accounts and full information.[16]

A partnership is not a legal entity separate from the partners, which means that assets and debts are co-owned by the partners.[17] Partners are an agent of the firm, and act on behalf of other partners.[18] All partners are parties to each contract entered into by the firm.[19] As a result, partners are personally liable for all of the firm's debts.[20] Liability is both joint and several.[21] A partner's liability is unlimited, in that it is not limited by the amount of capital that they have invested into the firm.[22] As a result of the joint and unlimited liability, partnerships are generally unpopular outside of certain professions where their use is required or where there has been a historical requirement such as in law firms.[23]

B What is a Company?

As an alternative to partnerships, a company is another structure through which a business may be run. It is a legal entity in its own right, existing separately from its owners.[24] The company

[13] At 12.
[14] At 12.
[15] See Tamar Frankel *Fiduciary Law* (Oxford University Press, New York, 2010) at 42; *Birtchnell v Equity Trustees Executors and Agency* (1929) 42 CLR 384; and *Chan v Zacharia* (1984) 154 CLR 179.
[16] Partnership Law Act, s 54.
[17] Watts, above n 6, at 11.
[18] Partnership Law Act, s 17.
[19] Watts, above n 6, at 11.
[20] At 11.
[21] At 11.
[22] At 11.
[23] At 13.
[24] At 17.

owns the business.[25] The company itself is owned by shareholders holding shares in the company.[26]

Companies must be registered with the Registrar of Companies.[27] A company is required to have a name, one or more shares, one or more shareholders, and one or more directors in order to be incorporated.[28]

The rules by which companies operate are set out in the Companies Act 1993. Collectively, the Act and the specific constitution will set out the rights and duties of shareholders.[29] The Companies Act provides a default set of rules for New Zealand companies, but many companies create their own individual constitution.[30] Similar to partnership agreements, a company's constitution may alter the default rules that apply to it and its shareholders.[31] The default rule is that these rights and duties may be altered by a special resolution, which requires a 75 per cent vote of shareholders voting on the resolution.[32]

A company is governed by its board of directors.[33] Directors are appointed by shareholders through ordinary resolution, which requires a majority vote.[34] Shareholders may subsequently vote to remove a director from office.[35] In larger companies, the directors generally make big picture decisions, but delegate day-to-day running of the company to a CEO and other managers. In smaller companies (including most incorporated law firms) the directors may also be working in the business.

Shareholders have substantial powers that include adopting, altering, or revoking a company's constitution as well as appointing and removing directors.[36] These powers are enforced through voting rights in ordinary or special resolutions.[37]

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[25] At 17.
[26] At 17.
[27] Section 12.
[28] Section 10.
[29] Watts, above n 6, at 19.
[30] Companies Act 1993, ss 27 and 28.
[31] Section 27.
[32] Section 32.
[33] Section 128.
[34] Section 153.
[35] Section 156.
[36] Sections 32, 153 and 156.
[37] Sections 105 and 106.

As a separate legal entity, a company acts on its own account.[38] Through a director or employee acting as agent, the company itself enters into contractual arrangements and owes and is owed obligations. Income goes to the company, rather than to owners and control over profits is more diffuse. Profits may be paid out to shareholders as dividends or may be retained and reinvested in the firm. Shareholders are not parties to any contracts in which the company enters and have no liability to third parties for the company's debts.[39] Their liability is limited to the amount of capital that they have invested into the company, and for any personal guarantees that they have given to lenders or creditors such as banks.[40]

Shares are easily transferable.[41] They can be bought and sold, subject to a company's constitution. Some smaller companies may specify that shares are only transferable with permission from other shareholders. However, shares typically carry no rights to a withdrawal of the shareholder's interest in the company.[42] An individual shareholder is unable to withdraw their share of the company's assets and cannot generally require the company or other shareholders to buy back their shares. Dissolving a company is the only true way for shareholder to truly get their investment back and requires the support of a majority of at least 75 per cent of shareholders.[43]

III Advantages and Disadvantages of Different Structures

Historically, law firms have operated as partnerships.[44] However, businesses can be structured in a variety of ways to provide different advantages and disadvantages depending on the nature of the business or services to be provided in the specific environment. Therefore, it cannot be assumed that a partnership will be the ideal structure for each and every law firm. Prior to the Lawyers and Conveyancers Act there was a strong push from the legal community to allow the incorporation of law firms.[45] Lawyers wanted more freedom and flexibility to structure their practices.[46] Permitting law firms to structure themselves as they wish may provide more

[38] Watts, above n 6, at 18.
[39] At 18.
[40] At 18.
[41] At 19.
[42] At 19.
[43] At 20.
[44] Brendan Wright "Incorporated Law Firms: The Practical and Ethical Considerations" (2007) 13 Auckland U L Rev 1 at 2.
[45] Phil Goff "Lawyers and Conveyancers Bill" (2003) 8 NZLJ 331 at 332.
[46] At 332.

freedom and flexibility for lawyers and for the profession as a whole. However, there are some obligations and duties that exist within the legal profession that are perhaps not best suited to, or not necessarily fully compatible with certain structures.

For the sake of simplicity, this article will refer to the equivalent of a partner within a partnership as a principal within an incorporated law firm.

A Companies are Convenient Structures

The incorporation of law firms allows them to better align with modern international business practices, because law firms would then be better equipped to compete with other businesses in related areas.[47] An incorporated law firm provides for greater flexibility compared to a partnership. The company's constitution may set out ownership rights and have combinations of distribution rights in the firm's profits as well as control of the firm through the number and types of shares held by principals.[48] Companies are designed to allow for easy changeovers when principals join or leave the firm because of the transferability of shares.[49] For example, shares can be reassigned rather than amending a partnership deed. Furthermore, firms could, for example, give non-voting shares to associates as an incentive to remain with the firm, and to maintain an exceptional work ethic.

Incorporated law firms allow for limited liability, protecting the personal assets of the principals.[50] This is more in line with how other businesses are structured and means that lawyers considering setting up or joining a firm are not daunted with the threat of risking their personal assets. Joining a partnership can be a major personal financial risk. Additionally, companies can have tax advantages compared to partnerships, as the company tax rate sits below the highest personal income tax rates.[51]

B Capital Investment

[47] At 332.
[48] Wright, above, n 44, at 7.
[49] Watts, above n 6, at 19.
[50] Wright, above n 44, at 3.
[51] See Inland Revenue "Tax rates for businesses" <www.ird.govt.nz>; and Inland Revenue "Tax rates for individuals" <www.ird.govt.nz>.

By comparison to other forms of business, law firms have tended to have low requirements for capital.[52] However, this is no longer necessarily the case. There are multiple reasons why having larger amounts of available capital can be beneficial for a law firm, whether operating as a company or as a partnership.

Starting and establishing any type of business, including a new law firm, requires an injection of capital. Additional capital allows an established law firm opportunity to expand through investing in itself. Examples include upgrading technology and communications, increasing the size of a local office, launching an additional office in another location, employing more staff, and accessing professional training, as well as advertising promotions.

A small firm has limited opportunities to compete in the market, as they are restricted by the expertise of the small number of staff and available working hours.[53] Capital is required to grow and the bigger and more varied a firm is, the better its market position, the more efficiently it can deploy resources, and the better placed it is to retain specialist staff.[54] Larger firms allow for a more extensive professional base – better and more efficient staff deployment including legal assistants as well as IT and finance personnel.[55] There is opportunity to economise on the use of office space, and types of hardware.[56] A firm's overall size may also give them cheaper licensing rates for software and cloud-based storage.[57]

Technology has become one of the most important and expensive factors considerations in the provision of legal services. Ongoing capital, not just an initial injection, is required to maintain relevance in technology.[58] A firm's clients will expect their lawyers to be technologically savvy and innovative, with efficient modern business practices to be able to easily and quickly meet client demands.[59] Technological growth continues to be exponential.[60] In many practice areas, a firm needs capital to invest in technology and ongoing funding to maintain relevance.[61] Some

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[52] Richard Susskind *The End of Lawyers? Rethinking the Nature of Legal Services* (Oxford University Press, New York, 2008).
[53] Susskind, above n 52.
[54] Susskind, above n 52.
[55] Susskind, above n 52.
[56] Susskind, above n 52.
[57] Susskind, above n 52.
[58] Susskind, above n 52.
[59] Susskind, above n 52.
[60] Susskind, above n 52.
[61] Susskind, above n 52.

of the outputs include audio, video and data communication, electronic searches, automated billing systems, document automation, historical data scanning and conversion, and the ever evolving and improving use of artificial intelligence.[62] During the age of COVID-19, it has become clear that all firms must be flexible and provide opportunities to work remotely. While working from home, staff must be able to communicate with colleagues and clients and access e-resources. Having the necessary technological capabilities to do so, possibly with short notice, is of the utmost importance to be able to continue providing key legal services for those who need it.

Larger firms are likely to be better placed to trial or experiment with new technologies because they have both the funding to develop and support the technology, as well as having a financial buffer to fall back on if required, while other teams within the firm continue to profit through the more traditional modes of legal practice.[63] Smaller firms are less able to embrace technology and risk being left behind while larger firms benefit from the advances in efficiency and reputation that technology offers.[64] Unsurprisingly, studies have found that larger firms tend to be more innovative than smaller firms.[65] In 2017, 64 per cent of Australian law firms surveyed reported engagement in innovative activity.[66] Many of those firms noted costs to innovation as a barrier to preventing development.[67] Smaller firms have increased difficulty in development as they have far less access to resources and less absorptive capacity to generate innovation.[68] This also reflects the challenges around scaling up smaller firms.[69]

An increase in capital held by a firm may increase access to legal services. Capital may allow firms to invest in technology and find more efficient ways to provide legal services.[70] This may become particularly important as artificial intelligence and other technology becomes more prominent and widely used in society. Increased capital may provide an easier way for law firms to grow and diversify.[71] This could also incentivise further specialisation into specific

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[62] Susskind, above n 52.
[63] Lauren Joy Jones and Ashley Pearson "The Use of Technology by Gold Cost Legal Practitioners" (2020) 2:1 Law, Technology and Humans 57 at 60.
[64] At 60.
[65] At 60.
[66] Vicki Waye, Martie-Louise Verreynne and Jane Knowler "Innovation in the Australian legal profession" (2018) 25:2 IJLP 213 at 224.
[67] At 231.
[68] At 225.
[69] At 225.
[70] Susskind, above n 52.
[71] Jones, above n 63 at 60.

areas of law.[72] Larger firms may also be able to systematise controls of quality and consistency and generate an increase in consumer confidence in their brand.[73]

1 Raising capital within a company

Companies provide an easy approach to accepting outside investment – the issuance of shares.[74] Capital may be provided through family and friends of founders being able to invest in the business. Since investors are not personally liable, their risk is limited. There are other options available, including angel funding and venture capital.

Larger companies may be able to make an initial public offering, i.e., listing on a stock exchange such as New Zealand's Exchange (NZX). However, there are limits before a company can list. They must have an anticipated market capitalisation of $10 million to be eligible to be listed on NXZ.[75] The required legal disclosure statements and associated fees can make this an expensive option for firms.[76] However, if successful, being publicly listed on a stock exchange can be a great source of capital. For example, Australian firm Slater & Gordon raised AU $35 million in their initial share sale on the Australian Securities Exchange (ASX). [77]

2 Raising capital within a partnership

Within a partnership, investments and increases in capital are typically introduced through partner contributions.[78] Partnerships are not well-suited to outside investment.[79] There is no mechanism such as the issuance of shares to easily allow capital to be exchanged for ownership or for a share of profits. This lack of readily available outside capital leaves partnerships with two options for new capital: partner contribution, and debt. This can result in a partnership being restricted by a lack of available investment in their attempts to expand and innovate.

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[72] Susskind, above n 52.
[73] Susskind, above n 52.
[74] Companies Act, s 42.
[75] NZX "NZX Listing Rules" (10 December 2020) <www.nzx.com>.
[76] NZX, above n 73.
[77] Wright, above n 44, at 13.
[78] Toby Brown "Law Firms Raising Capital" (23 August 2012) 3 Geeks and a Law Blog <www.geeklawblog.com>.
[79] Watts, above n 6, at 12.

Raising capital through partner contribution means that partners are often required to buy into the partnership when they become a partner.[80] Some firms allow new partners to 'buy-in' over an extended period.[81] This means that a new partner is able to afford to join the partnership and received a reduced profit share until the cost is met. As a result, their income for the first few years could decrease compared to their previous salary as an associate.[82] The cost of this could perpetuate elitist gatekeeping within the higher levels of the legal profession. It could separate lawyers who can afford to buy into a partnership (possibly having generational wealth to support them) from those that may be managing a mortgage or remaining student debt and cannot afford to take a short-term loss in income. In a typical scenario, older partners nearing retirement would see no benefit from investing in the long-term future of the firm, and younger partners with families and a mortgage cannot afford to.

Furthermore, partners may be hesitant to make large investments in the firm, particularly if it means that they will be significantly decreasing their income until the investment realises its potential. This may prohibit a number of smaller firms from expanding and ultimately limit the efficiency of law firms in New Zealand. If law firms were able to raise capital through the issuance of shares to public investors, partners or principals would not need to supply this capital themselves. Other businesses have this opportunity and often do raise equity to grow or even to survive. There is also the possibility that a partner could leave the firm and withdraw their capital. Partner loss can be a serious risk, particularly to a small firm.

The other option available for partnerships in raising capital is through debt-raising.[83] Outside of partner investment, firms are reliant on securing loans from banks and other lending institutions.[84] These loans often come with covenants requiring, for example, that the firm retains a specific number of partners.[85]

C Risk of Partnership Collapse

[80] See John W Olmstead "Law Firm Capitalization – Should There Be a Buy-In?" (11 October 2017) Olmstead & Associates <www.olmsteadassoc.com>; Dona DeZube "Law Partnership" Monster Jobs <www.monster.com>; and Brenda Jeffreys "The Cost of Making Partner" (October 2017) Law Journal Newsletters <www.lawjournalnewsletters.com>.
[81] Olmstead, above n 80.
[82] Olmstead, above n 80.
[83] Wright, above n 44, at 8.
[84] John Morley "Why Law Firms Collapse" (2020) 75 The Business Lawyer 1399 at 1400 at 1404.
[85] At 1404.

Internationally, it has been shown that the partnership structure of a law firm makes it particularly vulnerable to sudden collapse due to a 'partner run'.[86] This is particularly notable in the United States. Within a partnership, partners are generally easily able to withdraw, taking with them capital, associates, and clients. Within a company, while principals may still take associates and clients when they leave, barriers can be put in place to prevent the loss of capital. A partner's departure from the firm causes damage, and may cause more partners to leave, which adds further damage, and causes more partners to withdraw, and so on.[87] A partner run is self-reinforcing. The essential components in a partner run are that a partner is paid in profits rather than a salary, and that any remaining partners will be personally liable for the debts of the firm.[88]

A partner run begins with the departure of a particularly high-performing senior partner.[89] This partner typically realises that although the firm is still generating a large profit, it is no longer meeting a particular target, and the partner's share of the profits will decrease. This partner leaves the firm for a better offer taking with them other partners and associates, as well as their clients.[90] This departure causes some damage to the firm, including loss of capital, loss of income, and may have implications for the firm's reputation.[91] This damage can then result in the departure of another senior partner, also taking associates and clients, which can worsen the damage, and result in subsequent departures.[92] The loss of highly respected senior partners may change the culture within a firm and result in the departure of other staff.[93] Many clients may follow their lawyers to new firms, which limits the revenue available to the initial firm.[94] A firm may be left with debt and excess office space.[95] Crucially, each departing partner will also take the capital they had invested in the firm.[96] The initial departures may not significantly impact the firm, but if the run continues the situation can change rapidly. The loss in capital will leave the firm relying on bank loans. Loan agreements often require that the firm retains a minimum number of partners, or that a certain number of partners do not leave within a fixed

[86] At 1400.
[87] At 1401.
[88] At 1403.
[89] At 1403.
[90] At 1403.
[91] At 1403.
[92] At 1403.
[93] Larry E Ribstein "The Death of Big Law" (2010) Wis L Rev 749 at 772.
[94] At 772.
[95] At 772.
[96] Morley, above n 84, at 1403.

period. If these covenants are breached and the loan cannot be repaid, eventually the firm will cease practice and dissolve.[97] This reliance on bank loans emphasises the importance of firms being able to raise positive capital. Remaining partners at the time of collapse will be personally liable for all debts owed by the partnership.[98] This further incentivises partners to leave early. Some partners may foresee that the firm is verging on collapse and leave to limit their personal liability.

A clear example of a partner run in practice is the United States law firm LeClairRyan. After the firm experienced a rapid expansion, its gross revenue and profitability declined.[99] The decline led to the departures of partners and other attorneys, which rapidly escalated in 2019.[100] Many lawyers left in groups to move to other firms.[101] This included 300 employees who moved to a legal service provider, ULX Partners.[102] By July 2019, the firm had been dissolved.[103]

A notable exception to this model is the law firm Slater & Gordon, which was founded in Melbourne, Australia in 1935.[104] Not only was it the world's first investor-owned law firm, it was also the first large law firm to become insolvent, restructure its debt and continue operations.[105] The investor-ownership structure of Slater & Gordon is a key distinction from partner-owned law firms, which could not have survived such a period of financial difficulty. As an investor-owned business, it was able to continue to pay employees.[106] This meant that principals did not have a reason to leave and take other staff and clients with them while the company was undergoing financial restructuring. Investor-owners are unable to withdraw from the company and withdraw their capital in the way that partners may withdraw from a partnership.[107] Shareholders may be able to sell their shares, but the capital remains in the business.

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[97] At 1403.
[98] At 1403.
[99] Jason Tashea "Too big too soon: How LeClairRyan went under" (21 Jan 2020) ABA Journal <www.abajournal.com>.
[100] Tashea, above n 99.
[101] Tashea, above n 99.
[102] Tashea, above n 99.
[103] Tashea, above n 99.
[104] Morley, above n 84, at 1422.
[105] At 1422.
[106] At 1422.
[107] At 1423.

New Zealand law firms are likely to be less susceptible to a partner run considering the smaller nature of the legal profession (compared to law firms with hundreds of partners across many states). New Zealand law firms are significantly smaller than those seen, for example, in the United States. Partners are more likely to be loyal to each other and to the firm. The combination of this loyalty and a desire to ensure their business is successful contributes to the stability of the firms. Furthermore, in the United States, lawyers are prohibited from using non-compete clauses and other restrictions to prevent partners from leaving.[108] They cannot prevent any partner from withdrawing the capital they have invested in the firm. This rule does not apply in New Zealand, and as such, measures could be taken to restrict withdrawals from the partnership to prevent a partner run. New Zealand partnership firms may be unlikely to include such barriers (such as non-compete restrictions) because partners will want to retain their personal freedom, and do so by refusing to impose restrictions on each other.

D Non-Lawyer Involvement

The incorporation of law firms makes firms more suited for permitting non-lawyer involvement, either as directors or as shareholders. However, there are concerns about non-lawyer involvement revolving around the professional obligations that lawyers are subject to and risks that non-lawyers may not fully understand or appreciate them. Within a company structure, directors are also subject to obligations, which may come into conflict with legal professional responsibilities.

1 Legal and Corporate Obligations

There are various duties and obligations existing within both the legal profession and corporate settings. These obligations stem from both fiduciary duties and statutory duties.

A fiduciary duty is an obligation of loyalty and good faith flowing from the fiduciary to a beneficiary.[109] Fiduciary duties are designed to reduce risk relating to the high levels of power and trust placed in fiduciaries.[110] They are often highly fact-dependent and subject to the individual circumstances.

[108] American Bar Association, Model Rules of Professional Conduct, r 5.4.
[109] Frankel, above n 15, at 106.
[110] At 106.

Fiduciary duties can be characterized as both duties of loyalty to the beneficiary and duties of care relating to the quality of the fiduciary's work and their performance in acting as a fiduciary.[111] The duty of loyalty requires fiduciaries to act for the sole benefit of the beneficiary, and that the fiduciary may not benefit themselves.[112] Fiduciaries must avoid acting within any conflict of the interest of their beneficiary.[113] Breaching a fiduciary duty carries a moral stigma, as well as legal consequences.[114]

Lawyers are well-accepted as being fiduciaries and owing fiduciary duties to their clients.[115] In addition to these fiduciary duties, there are statutory obligations owed by lawyers both to their clients, and to the courts.[116] The Lawyers and Conveyancers Act sets out the fundamental obligations of lawyers.[117] Lawyers are obliged to uphold the rule of law, to act independently when providing legal services, to act in accordance with their fiduciary duties and other duties of care owed by them, and to protect the interests of their clients.[118] They have overriding duties as an officer of the Court.[119] The Client Care and Conduct Rules provide specific direction in upholding these broader obligations.[120] For example, lawyers must not refuse to accept instructions from prospective clients without good cause,[121] must be independent when providing legal services[122] and not act where there is a conflict or risk of conflict, and have strict requirements around protecting confidential information.[123] The Client Care and Conduct Rules also set out factors to be considered regarding fees able to be charged.[124] There is emphasis on upholding the reputation of the legal profession. Within a lawyer's obligations to their clients, there is an utmost duty of honesty to the court and to protect court processes.[125]

Similarly, directors owe both fiduciary duties and statutory duties to the company.[126] The fiduciary duties and statutory duties are essentially the same obligations. Under s 131 of the

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[111] At 106.
[112] At 107.
[113] At 108.
[114] At 104.
[115] At 43.
[116] Lawyers and Conveyancers Act.
[117] Section 4.
[118] Section 4.
[119] Section 4.
[120] Lawyers and Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008.
[121] Rule 4.1
[122] Rule 5.
[123] Rule 8.
[124] Rule 9.1
[125] Lawyers and Conveyancers Act, s 4.
[126] Frankel, above n 15, at 50.

Companies Act, directors are obliged to act in good faith and in the best interests of the company.[127] It is important to note that these duties are owed to the company itself, and not to the shareholders personally. Despite this, the traditional view in corporate law is that a director must exercise their power to maximise shareholder profit. This is supported by the governance powers held by shareholders. Shareholders have consultation rights on major transactions, as well as the power to appoint and dismiss directors, or even dissolve the company.[128] However, it is becoming increasingly accepted that directors may consider other stakeholders while still fulfilling their duties to the company.[129]

2 *Maintaining Professionalism*

Several prominent voices have raised concern that incorporation may lead to non-lawyer ownership and management of law firms, which may undermine professionalism.[130] Their reasoning is that non-lawyers may not have the same regard for the legitimacy of the legal profession and may be more likely to disregard legal ethics because they have not been trained to uphold those professional obligations.[131] The Ontario Trial Lawyers Association argued that the controlling interest in any law firm should be held by lawyers to ensure that core values, such as conflicts of interest, client confidentiality, and the independence of lawyers, are protected.[132] Non-lawyers are not subject to professional discipline for such misconduct. An associated concern is that non-lawyers may inappropriately influence how legal services are offered.[133] They may not fully realise the implications of the ethical and legal obligations owed by lawyers and the firm as a whole while making business decisions. Their primary focus may be on increasing profit, rather than ensuring the firm uphold those responsibilities. Financial pressures could potentially compromise a lawyer's ethical and legal responsibilities to their clients or to the courts.

[127] Companies Act, s 131.
[128] Watts, above n 6, at 20 and 21.
[129] Business Roundtable "Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans" (19 August 2019) <www.businessroundtable.org>.
[130] See Milton C Regan Jr (2008) "Lawyers, Symbols, and Money: Outside Investment in Law Firms" 27:8 Penn St Intl L Rev 407, at 426; and New York State Bar Association, above n 1.
[131] Nick Robinson "When Lawyers Don't Get All the Profits: Non-Lawyer Ownership, Access, and Professionalism (2016) 29: 1 Geo J Legal Ethics 1 at 13.
[132] Ontario Trial Lawyers Association “Submission to Law Society of Ontario on Alternative Business Structures” (15 December 2014) as cited in Andrew Grech and Tahlia Gordon “Should Non-Lawyer Ownership of Law Firms be Endorsed and Encouraged?” (10 May 2015) Creative Consequences <creativeconsequences.com.au>.
[133] Robinson, above 131 at 8.

The implication that lawyers are not focused on trying to make a profit is arguably a naïve one, especially given that law firms worldwide are often ranked based on profitability per partner.[134] However, a lawyer is as an officer of the court, and has a role to maintain the integrity of the legal system.[135] Lawyers may have different goals when owning and operating a law firm, such as ensuring the quality of the work produced and maintaining professional standards.[136] There may already be instances where lawyer partnerships debate taking on a case that would benefit the community and the client but may involve financial or other risk to the firm.[137] Allowing non-lawyers into such a debate may change the dynamic and potentially influence decision-making.[138] Lawyers work within a sometime complex suite of obligations relating to things like confidentiality, anti-money laundering, dealing with client funds, dealing with the courts, communications with other lawyers and their clients, and potential conflicts of interest. Most other professions do not, and non-lawyers who are not trained in these obligations may not understand them fully.[139]

The New Zealand Law Society places a high emphasis on maintaining public trust and confidence in the legal profession and legal system as a whole.[140] Allowing non-lawyer involvement, in particular investment, may undermine this confidence, as the public may regard law firms as placing too much focus on profitability.[141]

The traditional partnership structure of a law firm is one that provides only legal services. The emergence of multi-disciplinary practices will result in larger practices, with more non-lawyers having control of, or access to, confidential information. Internationally, the appearance of multi-disciplinary practices came from the Big Five accounting firms, that are now actively offering legal services in countries such as Australia.[142] Some countries essentially allow accounting firms to engage in legal practice.[143] This practice may result in the increased likelihood that legal rules will not be followed, or confidential information may be shared.

[134] Regan, above n 130 at 426.
[135] Lawyers and Conveyancers Act, s 4.
[136] Regan, above n 130 at 426.
[137] New York State Bar Association, above n 1, at 49.
[138] At 49.
[139] At 49.
[140] Wright, above n 44, at 4.
[141] New York State Bar Association, above n 1, at 141.
[142] Katherine L Harrison (2000) "Multidisciplinary Practices: Changing the Global View of the Legal Profession" 21 U Pa J Intl Econ L 879 at 879.
[143] At 879.

Non-lawyer involvement may also undermine some community-oriented ideals within the legal profession.[144] For example, it may decrease the availability of pro bono work or community law offices.[145]

Non-lawyer ownership introduces a possibility that lawyer-directors may be caught in a conflict between their duties owed to shareholders and their duties to clients or to the courts.[146] This places lawyers in an uncomfortable position of having to choose between their obligations. A lawyer's duty to the courts and to their clients is a fundament aspect of New Zealand's legal system.[147] This obligation must prevail against obligations as a director. Even if the priority of legal professional duties is specifically legislated, this is still a complicated area to navigate. Shareholders and non-lawyer directors may still exert undue pressure on lawyer directors. A lawyer's position as director may be tenuous and ultimately, the majority of shareholders have the power to dismiss a director from the board.[148] In a publicly owned firm, even if individual shareholders do not have substantial voting rights, they may sell their shares, therefore decreasing their value, in protest of any decisions that go against their interests.[149]

Worldwide trends suggest that law firms' structure and management must be heavily regulated.[150] Within a New Zealand context, there is an emphasis around not only the integrity of the legal profession, but also public perception of the profession, and the professional conduct rules reflect this.[151]

E Personal Liability vs Limited Liability

A crucial difference between partnerships and companies is that partners are personally liable for the debts of a partnership, while shareholder liability is limited to their investment in the company. The risk of personal liability has many implications within a business. Limited liability encourages the growth of businesses. However, personal liability can be used to ensure the high quality of work coming out of the legal profession. Liability can also play a role in

[144] Robinson, above n 131, at 16.
[145] At 16.
[146] Regan, above n 130, at 425.
[147] Lawyers and Conveyancers Act, s 4.
[148] Companies Act, s 153.
[149] Regan, above n 130, at 425.
[150] At 431.
[151] Lawyers and Conveyancers Act, s 3.

client compensation in the event of malpractice and can damage the public perception and reputation of the legal profession.

1 Encouraging business growth

The limited liability inherent in a company encourages the creation and growth of businesses by removing the personal liability of those who own and manage the company.[152] Limited liability also encourages outside investment in a firm, as shareholder-liability is limited to the amount invested.[153] In a legal context, more lawyers may be willing to set up a firm, as well as increase the capital available to them. This may increase the availability of legal services and be a benefit to society.

2 Incentive to avoid malpractice

The joint and several liability inherent within a partnership provides a powerful incentive for partners to ensure that appropriate care is taken in the provision of legal services, as well as ensuring that their colleagues are not engaging in malpractice.[154] By comparison, the shareholders and directors of a company enjoy limited liability, and therefore cannot be personally liable for the debts incurred by the firm.[155]

The unlimited liability regime in a partnership means that a partner is fully liable for any of their own acts and omissions.[156] As such, they have a clear incentive to ensure that appropriate care is taken in providing legal services to avoid such liability.[157] As partners are jointly liable for the malpractice of each other, unlimited liability also provides an incentive for partners to monitor the services provided by their colleagues.[158] Those incentives are not absolute, as lawyers may be able to partially avoid them. Many lawyers in New Zealand are able to protect their personal assets by shifting ownership to their spouse or to a family trust.[159] Furthermore, most law firms hold professional liability insurance to cover losses caused by malpractice.

[152] Watts, above n 6, at 50.
[153] At 50.
[154] See generally Wright, above n 44, at 3; Susan Saab Fortney "Am I My Partner's Keeper? Peer Review in Law Firms" (1995) 66 U Colo L Rev 329; Robert D Cooter "Economic Theories of Legal Liability" (1991) 5:3 J Econ Perspect 11.
[155] Lawyers and Conveyancers Act, s 17.
[156] Wright, above n 44, at 3.
[157] At 3.
[158] At 3.
[159] At 3.

Concerns have been raised that limited liability may reduce the standard of care displayed by lawyers and result in malpractice, as lawyers will no longer have sufficient incentives to ensure appropriate care is taken in the provision of legal services.[160] Although directors and shareholders are not liable on a joint or several basis for acts or omissions by other directors or shareholders simply because of their position as a director or shareholder, they are still subject to their own professional obligations.[161] The threat of professional discipline remains a powerful incentive to ensure appropriate care is taken to avoid malpractice claims. However, it is possible that limited liability decreases the incentive for principals to monitor the actions of their colleagues.

3 Client compensation

Any shift to allow limited liability legal services may reduce a client's ability to seek financial recourse following malpractice and may further diminish the trustworthiness of the legal profession. This is contrary to aims within New Zealand's legal profession to maintain a reputation of confidence in lawyers, and in the profession as a whole. A potential concern is that a law firm may simply use a company structure solely for limited liability.[162] Allowing lawyers to avoid financial responsibility for malpractice may increase the perception that lawyers use legal concepts and constructs to avoid personal or professional accountability.[163] Clients must be able to have recourse to compensation in the event of malpractice, and the use of limited liability by law firms could undermine this. Clients are more likely to be compensated if firms hold professional indemnity insurance, but although holding insurance is recommended, New Zealand law firms are not required to do so.[164] Allowing limited liability for the owners of law firms puts firms in the same position as other incorporated businesses, such as accountants, where clients have recourse against the firm they engage and not against the firm's owners.

F International Law Firms

Allowing incorporated law firms to be owned by the public (including non-lawyers) could potentially lead to more global firms, as companies are more easily able to operate in multiple

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[160] Susan Saab Fortney "Tales of Two Regimes for Regulating Limited Liability Law Firms in the US and Australia: Client Protection and Risk Management Lessons" (2008) 11:2 Legal Ethics 230 at 235.
[161] Lawyers and Conveyancers Act, s 17.
[162] Wright, above n 44, at 5.
[163] At 5.
[164] Lawyers and Conveyancers Act (Lawyers: Indemnity) Rules 2008, s 4; and New Zealand Law Society "Insurance disclosure" (21 July 2020) <www.lawsociety.org.nz>.

jurisdictions. Operating within a company structure allows for one company to own subsidiaries that operate the local branches of the firm. For example, a parent company registered in Australia may hold shares in a subsidiary based in the United Kingdom creating a multi-jurisdictional law firm.[165] Some international law firms currently have branches within New Zealand,[166] however the New Zealand division must be a legally separate company as owners of law firms must be lawyers by New Zealand's standards.[167] The requirement of holding a New Zealand practising certificate may necessarily exclude some foreign lawyers. Changing ownership conditions could lead to a truly global law firm. Different jurisdictions have various interpretations of the ethical responsibilities within the legal profession. This may create difficulties in applying consistent rules across a range of jurisdictions, especially regarding higher-level management. Within the United States, multi-state firms must adhere to the rules of the most conservative state to avoid breaching any responsibilities. In some jurisdictions there may be instances where obligations are in direct conflict with each other, and issues arise which cannot easily be remedied. Given New Zealand's relative lack of experience in dealing with multiple jurisdictions, this may be an issue that New Zealand is not adequately prepared to deal with at this time.

IV New Zealand's Current Position

There has been a traditional prohibition on non-lawyer involvement in law firms. The Law Practitioners Act 1982 required lawyers to practice within a partnership and maintained a strict prohibition on lawyers entering into partnerships with non-lawyers.[168] This has essentially resulted in a prohibition on non-lawyer involvement in law firms as well as on multi-disciplinary practices within New Zealand. The decision in *Black v Slee* shows that this position can be traced back to 1932.[169] The Court found a partnership agreement between Black (a lawyer) and Slee (an accountant) to be illegal and in breach of the Law Practitioners Act 1931,[170] which prohibited a lawyer from sharing income with a non-lawyer.[171]

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[165] As an example, Slater & Gordon (UK) LLP is a subsidiary of Slater & Gordon Limited, which is incorporated in Australia.
[166] Both DLA Piper and Dentons have New Zealand firms.
[167] Lawyers and Conveyancers Act, s 6.
[168] Wright, above n 44, at 2.
[169] *Black v Slee* [1934] NZLR s 108.
[170]At 110.
[171] Law Practitioners Act 1931, ss 18 and 19.

This prohibition on non-lawyer involvement and ownership was maintained through until the beginning of the 21st century. In 2006, the Lawyers and Conveyancers Act removed the prohibition on allowing law firms to form incorporated companies.[172] The Act now allows owners of multi-lawyer practices a choice between operating as either a partnership or an incorporated company.[173] This reform appears, on the face of it, to significantly increase flexibility for law firms in structuring their ownership. However, the Act still maintains significant restrictions on the ownership and management of legal practices. While Parliament allowed law firms alternative methods of structuring themselves, they also imposed restrictions in line with concerns around non-lawyer involvement, aiming to maintain the integrity and reputation of the legal profession. In doing so, the Act imposed restrictions that do not apply to other limited liability companies.

A Current Regulation on New Zealand Law Firms

Under the Lawyers and Conveyancers Act, all New Zealand law firms must be fully owned and governed by lawyers who are actively engaged in the firm.[174] This means that in a partnership context, all partners must be lawyers. Within a company context, all shareholders and directors must be lawyers. There is a limited exception allowing the immediate family of those lawyers, or certain family trusts, to be shareholders, providing that they only hold shares conferring non-voting rights.[175]

Due to these restrictions on ownership, incorporated law firms are not able to publicly issue and sell shares to raise capital in the way that other companies can. This places incorporated law firms at a significant disadvantage in terms of their ability to raise capital. In modern New Zealand, this is a serious limitation, as discussed in Part III. It is essential and costly for businesses to maintain and progress their technology. Without up-to-date technology, firms risk being left behind, unable to innovate and cope with rapidly changing global conditions and requirements.

In order to prevent potential loopholes regarding forms of beneficial ownership, law firms are not permitted to share income with any person other than a lawyer or incorporated law firm.[176]

[172] Lawyers and Conveyancers Act.
[173] Section 9.
[174] Section 6.
[175] Section 6.
[176] Section 7.

The sole exception to this is that lawyers and law firms may share income with a patent attorney.[177] The purpose of this exception is to account for lawyers in joint practice with patent attorneys who are not lawyers, for example in intellectual property firms. In New Zealand, these joint practices have existed for many years and this exception recognized that.[178] However, the Act does not go so far as to allow patent attorneys to become shareholders, even if they would only hold non-voting shares.

Another significant difference between typical companies and incorporated law firms is that there is a statutory exception to limited liability for theft. Both directors and shareholders can be personally liable for pecuniary loss caused by theft of money or property entrusted to the firm.[179] This does not include shareholders who hold only non-voting shares, and so necessarily excludes any non-lawyer family members.[180] Shareholders of a company are not typically personally liable for anything, which is a material difference. This liability is restricted to the repayment of pecuniary loss as resulting from theft and does not include malpractice claims against the firm. The rule to protect against theft is in line with other professional obligations demanded of solicitors to protect against loss following theft, such as the New Zealand Law Society fidelity fund. In part, this is to ensure continued trust in the legal profession, which is particularly important considering that other professions are unable to operate trust accounts.

B Practical Differences Between Incorporated Law Firms and Partnerships

The Lawyers and Conveyancers Act has made little impact on the structure of New Zealand law firms. By comparison with other jurisdictions, such as Australia and England, relatively few New Zealand law firms have taken up the opportunity to incorporate, choosing instead to remain as partnerships. This begs the question: do these heavy regulations offset the advantages of allowing law firms to incorporate?

The key difference between incorporated law firms operating with these restrictions and partnerships is that incorporated law firms offer limited liability. The personal assets of the principals are protected against claims against the company.[181] This means that principals are

[177] Section 7.
[178] Baldwin Shelston Waters “Submission to the Justice and Electoral Committee on the Lawyers and Conveyancers Bill 2003”.
[179] Lawyers and Conveyancers Act, s 18.
[180] Section 18.
[181] Section 17.

no longer jointly and severally liable for the breaches of fiduciary duty or negligence of their colleagues. Many law firms maintain professional indemnity insurance, so personal liability would only be an issue where the insurance was declined or exceeded.

Within any well-managed law firm, the provision of legal services by junior staff must be supervised by senior lawyers such as partners or principals. In New Zealand, all legal work must be supervised by a lawyer who is entitled to practise on their own account.[182] An incorporated law firm may not have the same hierarchy as a partnership, and as a result, the chain of responsibility may look different in an incorporated law firm. However, the same professional standards apply across all New Zealand firms, regardless of structure.

Essentially, incorporated law firms must operate in a similar way to partnerships, but with limited liability. Given that law firms tend to act like companies with a strong emphasis on profit, the contrasting dynamic has yet to play out.

C Business vs Profession

An ongoing question regarding incorporated law firms is whether a law firm is a profession or a business. A profession is typically viewed as a career involving self-sacrifice because the interests of the client must come before those of the professional.[183] There is a requirement of higher education, and a diligently maintained skill set. A business is a means of generating wealth and income for the owner.[184] A business may prioritise their own financial interests. While this distinction is intangible and may appear inconsequential, it can alter the tone of lawyers and impact public perception of legal services.

Lawyers tend to refer to themselves as the legal *profession* and many larger law firms in New Zealand are structured as a partnership.[185] However, most firms tend to functionally operate in a manner similar to a company.[186] For example, many firms have a high focus on productivity and billable hours.[187] There is immense competition both within and between law firms, for clients as well as legal talent.[188] Law firms are often ranked based on productivity and profit,

[182] Section 30.
[183] Frankel, above n 15, at 134.
[184] At 134.
[185] Watts, above n 6, at 13.
[186] Wright, above n 44, at 16.
[187] At 18.
[188] Wright, above, n 44, at 16.

which does not fit with the language typically used to describe the legal profession.[189] Law firms themselves tend to use language weighted towards professionalism, even if sometimes technically inaccurate. For example, PwC Legal operates as an incorporated company, however, refers to its shareholders and directors as 'partners'.[190] Firms appear to have shifted their focus from legal services to law firm profits. This could raise issues regarding prioritising profit over ethical obligations.[191]

There has always been an innate tension in the legal profession between profession and business. The recent drift appears to be towards business. The prohibition on non-lawyer involvement in law firms may well be the final obstacle in place to prevent legal services moving too far towards a business-run model. The critical distinction between lawyer management and non-lawyer management is that all lawyers are subject to disciplinary action for misconduct, whereas non-lawyers do not face such consequences. However, even if non-lawyers were permitted to own law firms and possibly exert such pressure on lawyers, lawyers would still be subject to their existing rules and obligations.

V Comparative Approaches to Regulation

A Comparisons with International Legal Practices

The restrictions on the ownership of legal practices seen within New Zealand are not an isolated approach. International jurisdictions provide an interesting comparison to New Zealand's current regulations. Some provide alternatives to New Zealand's strict prohibition of non-lawyer ownership of law firms, with specific regulation in place to mitigate any risks that may arise.

For example, New South Wales, Australia, did not allow law firms to structure themselves as incorporated companies until 2001.[192] England and Wales permitted non-lawyer involvement in incorporated law firms from 2011.[193] Other jurisdictions also appear to be lessening

[189] Regan, above n 130, at 426.
[190] PwC "PwC Legal Services" (2021) PwC <www.pwc.co.nz>.
[191] Wright, above n 44, at 18.
[192] Andrew Grech and Tahlia Gordon "Should Non-Lawyer Ownership of Law Firms be Endorsed and Encouraged?" (10 May 2015) Creative Consequences <creativeconsequences.com.au> at 2.
[193] Jakob Weberstaedt "English Alternative Business Structures and the European single market" (2014) 21:1 International Journal of the Legal Profession 103 at 103.

restrictions imposed on law firms. In early 2021, in the United States, Arizona and Utah removed prohibitions on non-lawyer ownership of law firms.[194]

These jurisdictions often cite policies aiming to lower law firms' costs, in the hope that non-traditional forms of legal practice will reduce the cost of providing legal services.[195] This could increase the supply of such services for the public, particularly in jurisdictions with high levels of unmet demand and accessibility issues for legal assistance.[196]

New Zealand has adopted a more conservative approach that retains traditional limitations on law firms. In time, the experience of international incorporated law firms will surely impact future government policy relating to the legal profession.

1 Australia

In New South Wales, the Legal Profession Uniform Law Act 2014 provides regulation to legal practice in a manner similar to the Lawyers and Conveyancers Act. The key distinction is that New South Wales allows non-lawyer ownership of law firms.[197] This means that non-lawyers may join law firms as either partners, or shareholders and directors. Incorporated law firms may be publicly listed, and legal services can be offered alongside non-legal services such as in multi-disciplinary practices.

Despite allowing non-lawyer involvement, incorporated law firms in New South Wales are still subject to strict regulation. Management oversight must remain with an appropriately licenced lawyer. At least one director of an incorporated legal practice must be a 'solicitor director', who must ensure that the professional rules of conduct are upheld.[198] That director is responsible for managing the provision of all legal services through the firm, as well as implementing appropriate management systems.[199] They are also responsible for reporting misconduct. There is evidence to suggest that internal management structures are a more efficient measure in regulating provisions of services rather than external audits.[200]

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[194] Karen Rubin “Non-Lawyer Ownership of Law Firms Is Trending – But Is it a Good Idea?” (22 March 2021) Ohio State Bar Association <www.ohiobar.org>.
[195] Rubin, above n 194.
[196] Rubin, above n 194.
[197] Wright, above n 44, at 13.
[198] At 25.
[199] At 25.
[200] At 26.

The approach taken in New South Wales directly contrasts that of New Zealand. It allows for greater freedom in structuring and owning a law firm, opting away from a total prohibition of non-lawyer involvement in favour of directly targeting specific risks associated with non-lawyers. For example, concerns around non-lawyer management disregarding professional standards are managed by a requirement for a solicitor-director and appropriate internal monitoring. However, Australia does not have a specific regulation in place to prevent or mitigate the risk of undue pressure from shareholders.

Another issue identified regarding non-lawyer involvement is conflicting professional duties. In New South Wales, legislation specifies that in the event of conflict between a director's fiduciary obligations, duties to the courts take precedence, followed by duties to clients, and finally to shareholders.[201] This provides clarity for solicitor directors, and appears to remove liability directors would face from shareholders in the event of a conflict. The acceptance of conflicts of interest seemingly undermines the entire concept of fiduciary duties. However, as long as shareholder investors in law firms understand their rank in the priority of obligations, there should be no material harm. Regardless, this remains a viable option for New Zealand, should regulations be altered to allow for non-lawyer shareholders.

Australian law firms are required to carry professional indemnity insurance.[202] This may counter some concerns regarding limited liability and go towards ensuring that clients are able to gain compensation in the event of malpractice. New Zealand firms are not required to carry insurance.[203] Despite this, the New Zealand Law Society has set out what it considers to be 'minimum standards of insurance' and firms are required to disclose the amount of insurance that they do hold.[204] Some clients may not fully realise the implications when told that their lawyer does not hold indemnity insurance. Given that New Zealand allows law firms to exist with limited liability, firms should be required to hold at least the minimum standards of professional indemnity insurance.

[201] Regan, above n 130, at 424.
[202] Fortney, above n 160, at 231.
[203] Lawyers and Conveyancers Act (Lawyers: Indemnity) Rules 2008, s 4.
[204] Section 4; and New Zealand Law Society, above, n 164.

The approach taken in New South Wales appears to be a more appropriate balance to regulation than seen in New Zealand. It allows for more freedom in running a law firm and permits the advantages of incorporation, such as increased ability to raise capital, while mitigating risks associated with non-lawyer involvement and safeguarding professional obligations.

2 *England and Wales*

The provision of legal services in England and Wales is regulated through the English Legal Services Act 2007.[205] The Act reformed regulatory restrictions on the structure and ownership of law firms. Prior to the Act, there were restrictions prohibiting non-lawyers owning or investing in businesses that provide legal services.[206] The Act regulates the provision of legal services through both Legal Disciplinary Practices (LDPs) and Alternative Business Structures (ABSs), both of which permit non-lawyer involvement.[207] Law firms, whether LDPs or ABSs, are able to be structured as sole practitioners, companies, partnerships, and limited partnerships.[208]

Legal Disciplinary Practices must be fully owned by lawyers.[209] This means that non-lawyers are only permitted as directors where the LDP is a company – they may not be shareholders, or partners in a partnership. LDPs are only permitted to provide legal services, so cannot be multi-disciplinary practices. Management of an LDP must be made up of at least 75 per cent lawyer-managers, and up to 25 per cent non-lawyer managers are permitted.[210] All entities with a non-lawyer manager must be licenced to provide legal services.[211]

ABSs allow for more widespread non-lawyer involvement. They can be fully owned by non-lawyers and can provide non-legal services alongside legal services.[212] Regulations are in place to ensure that the legal professional obligations are met. The key requirement is ABSs must be licenced through a regulatory body, such as the Solicitors Regulation Authority (SRA).[213]

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[205] Legal Services Act 2007 (UK).
[206] Weberstaedt, above n 193, at 103.
[207] At 103.
[208] At 111.
[209] Solicitors Regulation Authority "Legal Disciplinary Practices" (25 November 2019) <www.sra.org.uk>.
[210] Solicitors Regulation Authority, above n 209.
[211] Legal Services Act, s 72.
[212] Section 72.
[213] Section 72.

Any English law firm requires a licence if there is non-lawyer involvement in terms of ownership or management.[214] This includes where a non-lawyer is a partner (in a partnership) or either a shareholder or director (in a company). Licences are granted by approved regulatory bodies in respect of particular reserved legal activities, such as the right of audience, conducting litigation, or administering oaths.[215] The SRA does not limit the different structures that an ABS may operate as (i.e., partnership, company, limited partnership), but requires an ABS to meet minimum requirements in order to gain a licence.[216]

All ABSs must appoint a Head of Legal Practice and a Head of Finance and Administration, both of whom are responsible to the Solicitors Regulation Authority.[217] The Head of Legal Practice must be a lawyer and is responsible for ensuring the maintenance within the firm of licensing terms regarding the legal professional and ethical duties of lawyers.[218] The Head of Finance and Administration is not required to be a lawyer, and is responsible for ensuring compliance with licensing terms regarding the treatment of money held by the firm, including money held on trust for clients.[219] The SRA has rebranded these positions to Compliance Officer for Legal Practice (COLP) and Compliance Officer for Finance and Administration (COFA).[220] It requires both LDPs as well as ABSs to fill these positions.[221]

For a non-lawyer to hold a material interest in an ABS (such as holding at least 10 per cent of shares or having significant voting influence) that individual must be approved by the licensing authority.[222] Unlike Australia, the SRA must be satisfied that these non-lawyer owners and managers 'fit and proper' to assume the role.[223]

The regulation in England and Wales is similar to that of New South Wales. Both allow non-lawyer ownership; however, the Alternative Business Structure in England and Wales is more rigidly and widely regulated to ensure a stricter legal control of the business. The firm itself,

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[214] Section 72.
[215] Section 18.
[216] Grech, above n 192, at 4.
[217] Sections 91 and 92.
[218] Section 91.
[219] Section 92.
[220] Solicitors Regulation Authority "Responsibilities of COLPs and COFAs" (25 November 2019) <www.sra.org.uk>.
[221] Solicitors Regulation Authority, above n 220.
[222] Legal Services Act, sch 13.
[223] Schedule 13.

as well as its lawyers, are licensed and regulated and each firm must have a designated COLP and COFA. In both jurisdictions, law firms, primarily incorporated law firms, are taking advantage of the freedom to include non-lawyers as shareholders and directors, however the full effects of these regulations have not yet been established.

3 United States

Concerns around non-lawyer ownership or control of law firms can be seen further in other jurisdictions. The United States Model Rules of Professional Conduct prohibits the control of lawyers' professional judgement by non-lawyers.[224] In each jurisdiction, regardless of specific management, all lawyers within a firm are subject to their professional rules of conduct regardless of the organisational structure of a business and may be subject to professional discipline.

Many states have permitted law firms to be organised outside of a traditional partnership, such as an incorporated company, but maintained restrictions on non-lawyer involvement.[225] Even without non-lawyer involvement, the courts have found ways to protect the integrity and reputation of the legal profession. Although this is no longer the case, Illinois has previously found shareholders in incorporated law firms to have joint and several liability for malpractice within the firm.[226] This essentially defeated the limited liability aspect of forming a company.

In 2020 the Arizona Supreme Court voted to adopt changes to the regulation of legal services to remove rules prohibiting fee sharing and non-lawyer involvement in a law firm.[227] Also using the title 'Alternative Business Structure', firms are entitled to apply for a licence through the state's Supreme Court Committee on Alternative Business Structures.[228] The change permits non-lawyers to have ownership or management interests in a law firm.[229] At least one lawyer must be appointed, as either a manager or an employee, to sit as a compliance officer

[224] American Bar Association, Model Rules of Professional Conduct, r 5.4.
[225] American Bar Association Commission on Ethics 20/20 Working Group on Alternative Business Structures "Issues Paper Concerning Alternative Business Structures" (5 April 2011).
[226] Robert Hillman (2003) "Organizational Choices of Professional Service Firms: An Empirical Study" 58:4 The Business Lawyer 1387 at 1392.
[227] Arizona Supreme Court "Alternative Business Structures (ABS) Questions & Answers" (2021) <www.azcourts.gov>.
[228] Arizona Supreme Court, above n 227.
[229] Arizona Supreme Court, above n 227.

to ensure legal ethical requirements are maintained.[230] This is very similar to what can be seen in England and Wales.

Other states are beginning to follow suit. States such as Utah and California have begun trialling 'regulatory sandboxes' to test co-ownership and non-lawyer involvement within law firms working within a similar model to Arizona.[231] Further states are considering taking similar steps.[232]

B Comparisons with Domestic Professions

The New Zealand legal profession can also be compared with other professions that exist domestically, such as accountants and patent attorneys.

1 Accountants

The legal profession is often compared to the accounting profession. Lawyers and accountants provide professional services in a similar manner, and to similar clients. Only Chartered Accountants are able to offer accounting services to the public.[233] Regulation of the accounting profession falls within the New Zealand Institute of Chartered Accountants Act 1996, which delegates power to the Institute of Chartered Accountants (NZICA).

NZICA permits the provision of accounting services through a number of structures, including both partnerships and companies.[234] It allows accountants to provide accounting services in a firm with non-accountant involvement, however, it requires control at the ownership level to be retained by accountants (whether through voting shares, or other mechanisms providing them with the power to exercise control such as in a partnership).[235] No resolution may be passed unless agreed by a majority of shareholders who are chartered accountants.[236] While control at the ownership level must be held by accountants, accountancy practices are able seek outside investment.

[230] Arizona Supreme Court, above n 227.
[231] Rubin, above n 194.
[232] Sam Skolnik "N.Y., Others Mull Moves to Allow Companies to Co-Own Law Firms" (24 November 2020) Bloomberg Law <www.news.bloomberglaw.com>.
[233] Rules of the New Zealand Institute of Chartered Accountants, r 10.
[234] Appendix IV, r 2.
[235] Appendix IV, r 2.2.
[236] Appendix IV, r 4.

Non-accountant principals, whether partners, shareholders or directors, must be considered to be a 'fit and proper person' by the NZICA.[237] Accountants at the relevant firm are responsible for ensuring non-accountant compliance with the Act, as well as the associated Rules, and Code of Ethics.

There is a distinction between lawyers and accountants in that accountants do not owe fiduciary obligations to their clients.[238] Their services require independence from the client and impartiality that may conflict with the client's interests.[239] Accountants are not supposed to serve their clients' interests, they are instead to ensure the accuracy of their client's accounts.[240] While clients do entrust some power to their accountant this is not sufficient to be recognised as establishing a fiduciary relationship. However, they still are bound by a Code of Ethics and have professional obligation of independence.

2 Patent Attorneys

Another interesting difference to the regulations of law firms is seen in the regulations regarding patent attorney services. Patent attorneys are similar to lawyers in that they must be appropriately qualified, and provision of work is heavily regulated. Such regulation comes under the Patents Act 2013. Until recently, the provision of patent attorney services was limited to individuals registered as patent attorneys, or a partnership solely comprising of individuals registered as patent attorneys.[241]

The Patents (Trans-Tasman Patent Attorneys and Other Matters) Amendment Act 2016 created a joint regulation regime for New Zealand and Australian patent attorneys. This included altering regulations regarding structures in which New Zealand patent attorneys may provide services to be consistent with Australia. Under this amendment, patent attorney services may be provided from either a partnership in which at least one partner is a registered patent attorney or a company that is registered as a patent attorney.[242] A patent attorney company requires that at least one of its directors is a registered patent attorney.[243] There are no restrictions on who may be a shareholder. In part, this was to allow for effective cooperation and competition

[237] Appendix IV, r 3.
[238] Frankel, above n 15, at 112.
[239] At 112.
[240] At 113.
[241] Patents Act 1953, s 103 [as at 13 September 2014].
[242] Patents Act 2013, s 271.
[243] Section 60.

between New Zealand and Australian patent attorneys, particularly regarding the usefulness of allowing outside investment to increase capital.

Ultimately, those changes allowed for more freedom and flexibility when patent attorneys structure their businesses. These regulations more closely resemble the regulations on law firms in New South Wales rather than those in New Zealand. These changes came into effect after the enactment of the Lawyers and Conveyancers Act. Given that the starting point in both cases was lawyer-only and patent attorney-only partnerships, this suggests an increased willingness by Parliament to reconsider and lessen regulations regarding the organisational structures in which professional services may be provided.

3 Inconsistency in non-lawyer involvement

Despite the extensive restrictions faced in the organisational structure of law firms, a point of contention has become obvious. The sole exception to the prohibition on lawyers or law firms from sharing income allows income to be shared with patent attorneys.[244] The reasoning for this is quite clear: to allow for intellectual property firms to operate effectively, being able to provide both legal and patent services. Law firms and patent attorney firms may combine their total profit ensuring that partners or principals in each firm gets their appropriate share of the business's profit. There is no restriction of income sharing from patent attorney firms, so their profits may be freely shared with a law firm. It also allows income from each firm to be used to invest in the business as a whole.

When the Lawyers and Conveyancers Act first came into effect, patent attorney (for the purpose of income sharing) was defined as a person registered as a patent attorney.[245] At that time, patent firms were limited to operating as partnerships, where any income would be owned by the partner individually.[246] The Patents (Trans-Tasman Patent Attorneys and Other Matters) Amendment Act extended the definition of 'patent attorney' to include a patent attorney company. The Lawyers and Conveyancers Act was amended accordingly to allow income to be shared directly between the companies, ensuring that patent attorney shareholders have more control over that profit, for example being able to retain it in the patent attorney company.

[244] Lawyers and Conveyancers Act, s 7.
[245] Lawyers and Conveyancers Act, s 6 [as at 12 December 2012].
[246] Patents Act 1953, s 103 [as at 13 September 2014].

Potter IP is an example of a New Zealand intellectual property firm. It includes two separate companies: Potter IP Law Limited (an incorporated law firm), and Potter IP Limited (an incorporated patent attorney firm).[247] Patent services are provided by patent attorneys employed by the patent attorney company, and legal services are provided by lawyers employed by the incorporated law firm.[248] The firms are operated and managed together, with directors of both firms working collectively. A similar concept can be envisaged using two partnerships, or even a partnership and a company, working closely together as one business.

The 2017 amendment means that a law firm may be able to enter into an agreement in which it will share its income with a patent attorney company in exchange for the patent attorney company paying the law firm's costs. This patent attorney company may have directors or shareholders that are neither patent attorneys nor lawyers. It may be a subsidiary, or even be publicly listed. These two companies can then effectively operate as a single business. While the law firm must still have lawyer directors, this essentially results in a multi-disciplinary practice, in which non-lawyers could potentially exert pressure on lawyers or even lawyer directors. Given the lack of discussion from either Parliament or the Law Society regarding this scenario, it appears that permitting this sort of situation may not have been intentional.

AJ Park is another New Zealand intellectual property firm also comprising two companies: AJ Park Law Limited and AJ Park IP Limited.[249] AJ Park IP Limited is an incorporated patent attorney firm, which is wholly owned by IPH Limited (which is a publicly listed company on the ASX, based in New South Wales, Australia).[250] While AJ Park Law Limited is wholly owned by lawyer shareholders,[251] IPH described the deal as an *acquisition* of the entire firm. More specifically, it announced that it had reached an agreement "to acquire the New Zealand intellectual property firm AJ Park by an acquisition of its patent attorney business and the benefit of its trade mark and legal businesses."[252] It is implied that IPH (through the patent attorney company) will have significant influence working with the lawyer directors.

[247] Potter IP "Our structure" <www.potterip.com>.
[248] Potter IP, above n 247.
[249] AJ Park "Our firm" (2021) <www.ajpark.com>.
[250] AJ Park, above n 249.
[251] AJ Park, above n 249.
[252] IPH Limited ASX Announcement: "IPH acquires AJ Park – the leading IP firm in New Zealand" (11 October 2017).

This essentially places New Zealand intellectual property firms in the position where they allow non-lawyer involvement, both in management and ownership, but do not have the specific safeguards to non-lawyer ownership as seen in other jurisdictions, such as a designated compliance officer, or requirements around state licencing. That is not to say that such firms are not regulated – the law firm itself still must have lawyer directors. However, this is inconsistent with the rest of New Zealand's current regulation which does not appear to tolerate any form of non-lawyer involvement. This exception to non-lawyer involvement leaves New Zealand intellectual property firms in a similar position to Australia, without the express provision that a lawyer's ethical professional obligations should take priority to other corporate responsibilities. Although lawyer directors will not actually have any obligations to the patent attorney company or their shareholders (potentially including a parent company), they will be working in a multidisciplinary practice, with the income of the law firm being shared with a corporate entity, presumably through a contractual relationship.

The New Zealand Law Society has set circumstances in which and conditions under which lawyers and incorporated law firms may share income with patent attorneys.[253] Under these regulations, law firms that intend on sharing income with patent attorneys under this exception are required to provide notice of their intention to do so to the Law Society.[254] Nothing in those rules prohibits the above scenario.

The above scenario clearly demonstrates an inconsistency in current regulation around the organisational structures of law firms. It is in direct conflict with the overarching idea within New Zealand regulations, which seek to prevent non-lawyer involvement in law firms. It emphasises one of two ideas. The first is that it suggests that prohibitions on non-lawyer involvement are overly onerous and no longer required. The alternative is that non-lawyer involvement poses risks that law firms are not prepared to manage, in which case patent attorney regulations should be looked at to remove this possibility.

The more likely scenario is the former, that prohibitions on non-lawyer involvement can no longer truly be justified, given the benefits possible for the development of the legal profession. However, a level of regulation must still remain to ensure the integrity of the legal profession.

[253] Lawyers and Conveyancers Act, s 94.
[254] Lawyers and Conveyancers Act (Lawyers: Income Sharing With Patent Attorneys) Regulations 2008, s 5.

VI Options for Reform

Given the differing advantages and disadvantages of both partnerships and companies, it is clear that the structuring and operation of law firms is not a one-size-fits-all situation. In particular, the benefits of allowing incorporation, particularly around raising capital, suggest that it should be a more viable possibility for New Zealand law firms. A more appropriate balance to New Zealand's regulation must be implemented – allowing law firms to operate as incorporated companies, without having stripped the structure of key benefits. This will require legislative and regulatory reform.

Every jurisdiction that has recently 'opened up' to allow non-lawyer ownership has included measures to protect the ethical obligations of the legal profession. There is merit to concerns that non-lawyer involvement and control, whether through ownership or governance, may influence the integrity of the legal profession. The legal profession is currently balanced towards business over profession, and maintaining high levels of lawyer involvement and control ensures that people making decisions have appropriate training on legal ethics and are keenly aware of the importance of their obligations.

If Parliament is willing to reconsider non-lawyer involvement in law firms, it must consider the scale and depth of this involvement: whether to restrict non-lawyers to what is essentially passive investment with no control, or to allow non-lawyer control at ownership and governance levels. This will determine whether any additional mechanisms are required to ensure legal professional standards are upheld.

A Retaining Lawyer Control of Law Firms

A key benefit of incorporation that cannot be utilised within New Zealand law firms is the increased ability to raise capital. If the aim is to increase the ability of law firms to raise capital, concerns around non-lawyer influence or control could be met by restricting non-lawyer control. Firms could allow non-lawyer ownership and either restrict this ownership to a minority of shareholder control or prohibit non-lawyer ownership of voting shares by allowing non-lawyers to hold only non-voting shares. To retain control at this level would also require that the directors of incorporated law firms be restricted to lawyers only. This would ensure lawyer control of firms at both an ownership and a governance level.

The default rule regarding shares in a company is 'one share, one vote'.[255] However, this can be modified by the company's constitution, which may specify that particular shares do not include voting rights, or have fewer votes than other shares.[256] As such, companies may offer lower-value non-voting shares. Creating dual class of shares is often designed to allow specific shareholders to retain control.[257] Classes of shares with unequal voting rights are created by shareholders who do not want to give up control but want public equity for financing.[258] Should incorporated law firms begin to permit non-lawyer ownership, there are two ways that different classes of shares could be used to retain lawyer shareholder control of the firm.

The first possibility to be considered would be to allow non-lawyer ownership, but limit non-lawyers to holding only non-voting shares. A company could issue shares to non-lawyer investors that hold no voting rights. This would ensure that all of the shareholder votes are held by lawyers. This would be similar to current regulations allowing non-voting shares to be held by family members or family trusts of lawyers within firms.

The second possibility would be to restrict non-lawyer ownership to a minority of shareholder control, as seen in New Zealand's regulation of accountants. This could be done through retaining a majority of the shares in lawyer shareholders, or by issuing shares with comparatively fewer voting rights than the shares held by lawyers. For example, shares issued to lawyers could be worth 10 votes each, while shares issued to non-lawyers could be worth one vote each. Legal practices could use dual class shares to maintain control through holding the higher-value voting shares within an inner circle of highly ranked lawyers at the firm. By limiting voting rights, the company effectively separates control from ownership. This would make it easier for lawyers to retain control at an ownership level.

In both instances, non-voting or dual class shares would entitle shareholders to invest in a law firm, and receive dividends for that investment, but would remove control that may be used to influence directors. This would afford law firms the opportunity to raise more capital than

[255] Companies Act, s 36.
[256] Section 36.
[257] Dorothy S Lund "Nonvoting Shares and Efficient Corporate Governance" (2019) 71 Stan L Rev 687 at 693.
[258] At 693.

merely through partner or principal contributions without introducing a risk of non-lawyer control or decision-making.

Dual class shares have been used by media companies such as the New York Times.[259] The claim was that this structure allowed them to retain their journalistic integrity without risk of shareholder pressure.[260]

However, there are issues associated with non-voting shares. There is a perception that non-voting shares are a financial risk for shareholders.[261] Refusing to cede shareholder control signals mistrust. There are concerns that dual classes of shares allow for subpar corporate governance standards on the part of directors.[262] They allow company founders to maintain control, despite other shareholders effectively having provided the majority of a company's capital. Those holding higher-value shares retain control despite being in a position of less financial risk. The United States Security and Exchange Commission has expressed disapproval of the use of dual class shares.[263] Furthermore, use of such shares does not appear to be *genuine* use of a company structure, which promotes 'one share one vote' and shareholder control rather than founder control.

While use of multiple classes of shares may be an option for allowing non-lawyer involvement to raise capital, the inherent mistrust in dual classes of shares may limit the willingness of potential investors. Therefore, it may be necessary to consider a wider scope for non-lawyer involvement, that can be regulated through other mechanisms.

B Allowing Non-lawyer Control and Governance

Further non-lawyer influence could be permitted through dropping restrictions altogether on non-lawyer shareholders and through the allowance of non-lawyer directors. This is likely to require obligations regarding legal professional responsibilities could be bolstered. Various possibilities must be examined. These include using existing legal and corporate regulation or making use of specific aspects of existing international models.

[259] At 704.
[260] At 704.
[261] At 693.
[262] At 693.
[263] At 711.

1 Using existing legal and corporate regulation

There could be clear guidance in place ensuring that the legal profession obligations of a law firm (including those of its lawyers and the legal profession as a whole) are held above typical corporate governance obligations. As seen in Australia, legislation could clearly specify the priority of obligations in the event of conflict – i.e., legal obligations must be held above the interests of shareholders. An incorporated law firm could clearly state this in its constitution and use the constitution to modify the default rules of the Companies Act to signal their commitment to ensuring that legal obligations are maintained. The constitution could specify the objective of the firm and would be difficult to change without a near-unanimous shareholder vote. Legislation, as well as the particular company's constitution, could emphasise that profit maximisation is to be balanced by other objectives, such as ensuring that lawyer's professional obligations are maintained.

However, while this may reduce risks of confusion regarding potentially conflicting obligations owed by directors, it does not do enough to mitigate risks around non-lawyer control. In particular, regardless of whether or not the board includes lawyers, non-lawyer shareholders may use their position, particularly their voting rights, to threaten directors into complying with their wishes by removing them from the board. Shareholders maintain some governance powers through their voting rights and will not face misconduct discipline in the event that a lawyer prioritises profit over their professional responsibilities. Overall, regulation in this form is not sufficient. New Zealand would require targeted regulation such as that seen in other jurisdictions to mitigate the risks associated with non-lawyer involvement. Any structure of law firm permitting non-lawyer control in an ownership or governance sphere will need to have external regulations on the internal management systems in place, such as those seen internationally.

2 Using aspects of international approaches to regulation

Regulations as seen in England and Wales may be seen as a step too far in the context of New Zealand law firms. Requiring all law firms to apply for licences to practice law may create excessive administrative duties on a regulatory body. If such administration were to become overly burdensome, the licensing and regulation of law firms may become 'check-list' regulation rather than ensuring that each firm is appropriately representing the legal profession.

The ability to be able to remove a firm's authority to practice law is a powerful tool, especially considering that non-lawyers are not subject to discipline for professional misconduct. In Australia, even where law firms do not hold a licence that could simply be revoked, if a solicitor director fails to maintain an appropriate management system for ensuring legal obligations are met, the Legal Services Commissioner may remove their practising certificate.[264] While the non-lawyers will not directly face misconduct charges, if a new solicitor director is not appointed, the firm will face involuntary liquidation.[265]

The inclusion of a solicitor director, as seen in Australia, or compliance officers for legal practice and for financial matters, as seen in England and Wales, to ensure compliance with legal standards may be an appropriate means through which to mitigate risk of non-lawyer control over a law firm. Using compliance officers allows this responsibility to be delegated to employees within the firm and appears to narrow the focus of specific responsibilities compared to a solicitor director. However, this responsibility may be better suited to lawyer-directors who are managing the firm. A compliance officer may face pressure from non-lawyer directors in a stronger manner than would be faced by a solicitor director based on their employment status.

C Proposed Reform

To adequately integrate the benefits of operating as an incorporated law firm, New Zealand should strongly consider reform of the Lawyers and Conveyancers Act and corresponding regulation. Reform may allow for non-lawyer involvement and investment in law firms. Any concerns around legal professional standards can be mitigated through a number of targeted regulations. Since incorporated law firms are already required to be registered with the New Zealand Law Society, it should not be necessary for each individual law firm to be licensed.

Non-lawyer shareholders and directors could easily be permitted with risks mitigated. There should be no restriction on non-lawyer shareholders, however, a requirement for one or two lawyer directors would be mandated. This is because non-lawyer involvement in terms of shareholding is less of a risk than non-lawyer involvement in management of the firm. Corporate pressure coming from shareholders can be managed by directors who are responsible

[264] New York State Bar Association, above n 1, at A-12.
[265] At A-12.

for any breaches in legal duties, ensuring that the shareholder interests do not impact how legal services are provided on a day-to-day level. Lawyer directors would also be responsible for implementing a management system to protect legal professional obligations in a similar manner to the position required in Australian incorporated law firms.

Non-lawyer directors should be required to pass a 'fit and proper person' test through the Law Society and could receive specific training on legal obligations and professional responsibilities owed by the firm. This would be to ensure that no inappropriate pressure is passed down to legal employees on how they should provide their services. The extra level of caution around non-lawyers in management positions rather than ownership positions is because pressure coming into a firm from shareholders may be less personal and less threatening than pressure on a particular lawyer (especially a junior lawyer) from a director or from their bosses.

Lawyer directors should be restricted to lawyers who are actively engaged and practising within the firm, to ensure that they are appropriately involved to manage any issues that may arise regarding misconduct. Non-lawyer directors should be restricted in that they may not be director of more than one law firm (at a time) to ensure that no issues of conflict or confidentiality can arise between firms.

Should issues arise around the management of legal professional obligations, the lawyer director could have their practising certificate revoked, which may leave the firm in breach of the requirement. A new lawyer director must be appointed, or risk the firm being shut down by the Law Society. Although non-lawyers will have face this misconduct consequence, a mechanism could be developed through which they are deemed unfit to participate in the management of a law firm.

For the avoidance of any doubt, it could be specified, in both legislation and each incorporated law firm's constitution, that legal obligations must be maintained and that professional responsibilities will be held in priority to typical corporate duties owed to shareholders. To manage concerns around loss of client compensation where more firms have limited liability, law firms should be required to hold a minimum standard of professional indemnity insurance.

These regulations would mean that specific exceptions permitting patent attorneys to cooperate and share income with lawyers would no longer be required. Regulation could specify that a

company may be both an incorporated law firm and a registered patent attorney. Intellectual property firms could operate as either a single structures, with at least one lawyer director and one patent attorney director. Any issues that may arise from the beneficial ownership of law firms as outlined in Part V may be managed through the requirement that non-lawyer or non-patent attorney directors pass a 'fit and proper person' test. This may provide further certainty of the integrity of the legal profession without posing a burden on those directors or the companies themselves, especially considering that they operate in direct competition with Australian intellectual property firms.

D Practical Issues around Non-Lawyer Investment

1 Personal liability for theft

Regardless of specific regulation to protect the integrity of the legal profession, a potential barrier to allowing any form of non-lawyer ownership in New Zealand law firms exists within provisions that specify that shareholders and directors of incorporated law firms are personally liable for theft. Shareholders and directors can be personally liable for loss caused by theft, for example, of money in a trust account.[266] This does not include shareholders that only hold non-voting shares.[267]

The importance of protections against theft for legal clients is evident within New Zealand's legal profession, particularly after law firm Renshaw Edwards stole nearly $30 million from their clients in 1992.[268] It is arguable that theft of client funds by lawyers is less likely to occur in modern New Zealand, given the increasingly electronic nature of financial transactions and monitoring requirements of trust accounts. Lawyers are required to contribute to the Law Society's fidelity fund, and this would remain regardless of whether they practised in a firm owned by lawyers or by non-lawyers. However, it is unclear how the particular provision requiring personal unlimited liability would translate to include non-lawyer shareholders or directors.

[266] Lawyers and Conveyancers Act, s 18.
[267] Section 18.
[268] New Zealand Law Society "A moment in time: The Wellington legal profession on display" (28 January 2020) <www.lawsociety.org.nz>.

Investors often consider a range of risk factors in their investments.[269] However, there is a distinction between investing in a company versus an incorporated law firm. Investors typically only risk the capital they have invested in a company, and do not open themselves up to the personal liability and risk the loss of their personal assets,[270] whereas in an incorporated law firm any investor holding voting shares – even a small parcel – could be fully liable for the repayment of stolen client funds.[271] While some potential investors to a law firm may be willing to take on the risk of personal liability, assuming the potential for a high return and the low likelihood of significant theft occurring, many investors may be less likely to invest in such a business knowing that there is a risk of personal liability. Instead, they would simply find another business to invest in without that financial threat.

A possibility would be to restrict non-lawyers to hold only non-voting shares, which would permit the continuance of this theft liability scheme. However, this may put an unfair and inconsistent onus on lawyer shareholders and directors who may want to be compensated, insured or indemnified for the potential personal liability. Alternatively, the provision could be limited to directors, as those best placed to ensure appropriate systems in place within the firm to prevent the theft. However, placing directors in a position of personal financial risk, especially given that they do not financially benefit from dividends, may be seen as unfair.

While other jurisdictions, including both Australia and England and Wales have a form of fidelity fund for compensating clients for theft of monies held by a law firm, New Zealand appears to be isolated in the existence of this provision.[272] If New Zealand were to reform regulations around the structure and ownership of law firms, the removal of this theft liability would need to be seriously considered.

2 Non-lawyer investment may not lead to material change

A final, more practical point is that merely allowing non-lawyer involvement in law firms will not necessarily achieve mass benefit for all New Zealand law firms. The types of firms likely to obtain external investment are the firms that are less likely to need it.[273] The law firms that

[269] Financial Industry Regulatory Authority "The Reality of Investment Risk" Financial Industry Regulatory Authority <www.finra.org>.
[270] Watts, above n 6, at 18.
[271] Lawyers and Conveyancers Act, s 18.
[272] Legislative Counsel Panel on Administration of Justice and Legal Services "Fidelity Fund" (22 April 2002).
[273] New York State Bar Association, above n 1, at 8.

may benefit more from non-lawyer investment are firms that are unlikely to receive it.[274] Investors are naturally cautious, and tend to invest in companies that are well-performing or displaying obvious potential – they will likely be drawn to larger law firms, less in need of outside capital.[275] Within Australia and England, many of the best-performing incorporated law firms are those specialising in personal injury.[276] New Zealand's ACC scheme specifically excludes this highly profitable specialisation.[277] Smaller firms that may require capital are less likely to be viewed as a good investment, and will be unable to reap the benefits of non-lawyer involvement and investment in law firms.[278] Furthermore, regardless of the potential of the firm, investors may be more reluctant to invest where it is clear that their interests as shareholders will never be the top priority of the directors.

This is not to say that reform of the organisational structures of the legal profession is not necessary. Reform is likely to provide for more flexibility and opportunities for law firms than currently available. However, ultimately, within New Zealand, removing restrictions on non-lawyer investment is unlikely to provide the degree of benefit some proponents might anticipate.

VII Conclusion

Under the Lawyers and Conveyancers Act, New Zealand law firms have flexibility in how they choose to structure their business. They may exist as either a partnership or an incorporated company. The Act allows incorporated law firms to structure and operate in a manner similar to non-legal businesses. The use of a company structure has the potential to introduce new elements into the legal profession such as the ability to raise capital, eliminating some layers of partner accountability and more global opportunities. These elements have been severely limited by specific regulation excluding the involvement of non-lawyers, reflecting a reluctance to allow non-legal influence within an incorporated law firm. Such restrictions sought to mitigate any risk that may compromise the public's view of the sanctity of the legal profession. Few New Zealand firms have taken the opportunity to become incorporated law firms despite the pressure they exerted to push for the change, and partnerships remain the

[274] At 9.
[275] At 9.
[276] Grech, above n 192, at 8.
[277] Accident Compensation Act 2001, s 317.
[278] New York State Bar Association, above n 1, at 8.

dominant structure in which law firms are run, suggesting that current regulations allowing incorporated law firms are not satisfactory.

By comparison with international regulations around law firm ownership, as well as to domestic regulations to comparable professions, the New Zealand legal profession is significantly restricted by its prohibition on non-lawyer involvement. This limits how a law firm may raise capital, which is essential to allow firms to grow and diversify. In particular, firms must invest in technology, and find different and more efficient ways to provide legal services. Artificial intelligence and other technologies are changing the face of business, and law firms must be able to keep up. Reforms to regulations surrounding the organisational structures of law firms are essential for the legal profession to survive and thrive within a modern business society.

A closer analysis of the Lawyers and Conveyancers Act, alongside corresponding regulations, demonstrates potential shortcomings and inconsistencies in how law firms are permitted to organise. This further emphasises the need for reconsideration and reform.

Both Australia and England and Wales have implemented regulatory schemes permitting non-lawyer involvement and ownership in legal practices. In particular, New South Wales has utilised an arguably more appropriate approach to regulation, targeting restrictions towards specific risk management.

New Zealand must reconsider non-lawyer involvement in law firms. Reform could include specific mechanisms to target areas of concern to protect the legal profession from non-lawyer influence through ownership or governance. In particular, New Zealand could benefit from regulation allowing non-lawyer shareholders and directors, with appropriate oversight from lawyer directors who are responsible for the compliance of all legal professional standards.

International trends suggest that allowing non-lawyer involvement in law firms is becoming increasingly common. Reform could align New Zealand with other jurisdictions, and better position New Zealand law firms in both local and global markets.

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