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# NOvA (NoGo) or Multi-Disintegrating Partnerships

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Multi-disciplinary partnerships (MDPs) have been a contentious issue for national and state bars for recent years. The English Law Society has finally agreed to promote them, in a limited fashion.[2] Although the House of Delegates of the American Bar Association voted against them, certain states are going to permit them.[3] No jurisdiction has yet embraced them fully and openly.

The stereotypical model of an MDP is a merger between an accounting firm and a law firm. This could be at the small end of the spectrum, e.g., high street practices, or at the multinational end, e.g., a large City of London or New York law firm and one of the major global accounting firms. The most aggressive moves for MDPs have come from this latter segment. The former Big Five accounting firms—PricewaterhouseCoopers, KPMG, Andersen, Ernst & Young and Deloitte Touche—have considered and attempted to start their own law firms, all with a view to integrating them into MDPs so as to offer one-stop shopping to their clients.

While the dream of becoming masters of the universe preoccupied the Big Five, events, to paraphrase Harold Macmillan, acted against them. Two, especially, carry enormous significance and though on opposite sides of the Atlantic they are intertwined: first, the collapse of the energy trading company Enron in 2001, and the subsequent conviction of the Andersen firm in Texas for the wilful destruction of documents connected to Enron's audits. This has led to draconian legislation by the US Congress, and signed into law by President Bush, regulating audit and accounting firms. The second is the European Court of Justice (ECJ) decision in the *NOvA* case,[4] which enables national and state bars to prohibit the formation of multi-disciplinary partnerships by their members.

It certainly seems as though an unstoppable tsunami of globalisation has met a powerful Canute. Of course, for how long the tide is halted—and the economic recession helps—is an

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[2] See J Flood, "The Cultures of Globalization: Professional Restructuring for the International Market" in Y Dezalay & D Sugarman (eds), *Professional Competition and Professional Power: Lawyers, Accountants and the Social Construction of Markets* (London, Routledge, 1995), and "Capital Markets: Those Who Can and Cannot Do the Purest Global Law" in R Applebaum, W L F Felstiner & V Gessner (eds), *The Legal Culture* of *Global Business Transactions* (Oxford, Hart Publishing, 2001).

[3] For example, New York and the District of Columbia, but with many restrictions.

[4] Case C-309/99 *J C J Wouters, J W Savelbergh and Price Waterhouse Belastingadviseurs BV v Algemene Raad van de Nederlandse Orde van Advocaten (NOvA)*, [2002] *European Court Reports* 1–21.

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open question. One way to begin to foretell the future is to enquire more closely into these two potentially cataclysmic events.

## 1. NOvA

In 1952 the *Advocatenwet* established the Netherlands bar and its association (*Nederlandse Orde van Advocaten*). The bar was given the power to regulate itself and also "visiting lawyers" (foreign lawyers practising in the Netherlands). Its primary purpose was to protect the public interest by ensuring the proper practice of the legal profession and maintaining the independence of the bar. Forty years later in 1993, the *NOvA* adopted the regulation, *Semenwerkingsverordening*, on joint professional activities. The regulation prohibited the formation of professional partnerships where the primary purpose was not the practice of law. Yet members of the Dutch bar could form such partnerships when other professional categories had been accredited by *NOvA*. Those so far accredited included notaries, tax consultants, and patent agents. Accountants, however, were specifically excluded from accreditation. The 1993 regulation also laid down particular requirements on ethics, maintaining separate case files, and ensuring the continuation of lawyer-client privilege.

In the mid-1990s two Dutch lawyers attempted to become partners in the accounting firms of Arthur Andersen and Price Waterhouse, which described themselves as "tax consultants" in the Netherlands. *NOvA* declared both lawyers were in breach of the 1993 regulation as the two firms were primarily accountants, an unacceptable category, in addition to being tax consultants, an accredited category. The lawyers and the firms appealed on the grounds that *NOvA's* decision was incompatible with the Treaty provisions on competition, right of establishment and freedom to provide services.[5] The European Court of Justice held that, even though *NOvA* was an association of undertakings within the meaning of Article 85(1) of the EC Treaty, the 1993 regulation, prohibiting MDPs, did not infringe the article as it was necessary for the proper practice of the legal profession. The court maintained it was essential to ascertain the context of the regulation and the objectives it was attempting to achieve. The ECJ stated the objectives are

> "connected with the need to make rules relating to organisation, qualifications, professional ethics, supervision and liability, in order to ensure that the ultimate consumers of legal services and the sound administration of justice are provided with the necessary guarantees in relation integrity and experience".[6]

The court was concerned that lawyers and accountants had divergent roles that could lead to conflicts. Whereas lawyers were cast in an advisory role, accountants had a supervisory role that arose from their audit activity, to declare to the public that the certified accounts were reliable. Accountants' central audit activity could therefore possibly compromise the integrity of the lawyer-client privilege. The general dean of the Dutch bar added a further twist, that an MDP "would have more resembled 'the marriage of a mouse to an elephant

[5] Case C-309/99 at para 30.
[6] *Ibid* at para 97.

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than a union of partners of equal stature' ".[7] Despite the expected economies of scale and the desires of clients to receive integrated professional services in a globalising world, the court found that the obligations of professional conduct

> "require of the members of the Bar that they should be in a situation of independence vis-à-vis the public authorities, other operators and third parties, by whom they must never be influenced. They must furnish . . . guarantees that all steps taken in a case are taken in the sole interest of the client".[8]

The ECJ held the view that accountants in the Netherlands were not beholden to comparable duties. It is debatable, in determining the aim of the 1993 regulation, whether the ECJ actually understood the nature and range of services offered by accounting firms (especially the Big Four) since the court focused exceptionally on audit.[9] The court asserted

> "The Bar in the Netherlands was entitled to consider that members of the Bar might no longer be in a position to advise and represent their clients independently and in the observance of strict professional secrecy if they belonged to an organisation which is also responsible for producing an account of the financial results of the transaction in respect of which their services were called upon and for certifying those accounts."[10]

Thus the prohibition on MDPs by *NOvA* was upheld by the ECJ, through the mechanism of protecting core values of the legal profession. The effect is that individual member states of the European Union can determine the regulation of their legal professions and those of "visiting lawyers". The global effect, however, is likely to be minimal. States that erect barriers to combinations of professional activities will find themselves seriously weakened when their legal professions try to compete against those that have more laissez-faire attitudes to professional organisation and regulation. The Bars and Law Societies of the European Union (CCBE) have long endorsed the position taken in the judgment, but nonetheless recognised that the decision will be open to challenge in the future.[11]

## 2. ENRON and its Aftermath

In late 2001 Enron, an energy trading corporation with strong links to the White House, filed for Chapter 11 protection with debt of $63.3 billion, the largest bankruptcy in corporate history. Essentially, Enron had inflated its profits through dubious off-balance sheet financing ruses. Their witting accomplices in their pursuit of greater profit were Andersen, then one of the Big Five and Vinson & Elkins, one of the largest law firms in the US.[12] As the insolvency unravelled, Andersen was increasingly implicated. Eventually a partner in Andersen's

[7] *Ibid* at para 78.

[8] *Ibid* at para 102.

[9] M Power, *The Audit Society: Rituals Of Verification* (Oxford, Oxford University Press, 1999). D Brock, M Powell, and C R Hinings (eds), *Restructuring the Professional Organization: Accounting, Health Care and Law* (London, Routledge, 1999).

[10] Case C–309/99 para 105.

[11] CCBE, "Analysis of the NOvA 1 Judgement and Guidance to Bars on Professional Rules Following the NOvA 1 Decision" <http://www.ccbe.org/documents/analysisguidance_en.pdf>, and J. Fish, "Ethical Issues Affecting MDPs from a European Perspective" in K Raes & B Claessens (eds), *Towards a New Ethical Framework for a Legal Profession in Transition?* (Antwerp, Intersentia, 2002).

[12] B Malkin, "IBN Feature: Legal/Accounting Repercussions from Enron", <http://www.envoynews.com/iba/e_article000072235.cfm>

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Houston office directed that documents detailing the firm's Enron activities be shredded. Under US law this is illegal. Andersen's partner admitted his guilt and the entire firm was convicted. Andersen imploded. Various offices were cherry picked by other firms. Andersen had also been particularly aggressive in adding law firms to its roster of international services. In Spain and Scotland, for example, it had persuaded the largest law firms to join with it. Vinson & Elkins has, however, managed to avoid discussing its role with the US Securities and Exchange Commission (SEC) in advising Enron on off-balance financing under the rubric of not wishing to breach lawyer-client privilege. But the firm has been sued by Enron shareholders for aiding and abetting the off-balance transactions that fraudulently inflated Enron's profits.[13]

The then Big Five accounting firms had been increasingly successful in cross-selling professional services on the back of their audit function,[14] to the extent, in Andersen's case, that Andersen Consulting was earning bigger fees than its parent accounting half. Divorce resulted and Accenture was born. This melding of activities came under the scrutiny of SEC in the Clinton administration. Arthur Levitt, the then SEC chairman, lobbied Congress to prohibit this mix and cross-selling. The accounting lobby, led by attorney Harvey Pitt, resisted the SEC challenge, yet some of the Big Five began to divest themselves of their consulting arms. For example, Ernst & Young sold its consultancy to Cap Gemini, KPMG spun off its consulting business, and PwC sold PwC Consulting to IBM.[15] Bush's SEC chairman, Harvey Pitt, has until recently taken a more relaxed view on audit and consulting than his predecessor until, that is, Enron's bankruptcy and Andersen's demise.

As more corporations filed for Chapter 11 and others revealed evermore corporate fraud, the accountancy business was seen as culpable. Congress responded with the Sarbanes-Oxley Act 2002—a stringent regulatory framework that will even have effect overseas. If a company has a listing on an American stock exchange, any accounting firm that plays a role in producing an audit will have to register with a new US oversight board and adhere to American rules.[16] The law also bars auditors from cross-selling consulting services to audit clients.

Lawyers, too, are obligated under section 307 of the act to act as corporate watchdogs reporting material violations of the securities laws or breaches of fiduciary duty to the chief legal counsel or the chief executive officer, and if they fail to respond, the lawyers should report the evidence to the board of directors.[17] Harvey Pitt claimed that,

> "Sarbanes-Oxley reflects some skepticism about the degree to which the legal profession can police itself, by making explicit the Commission's ability, *and our obligation*, to regulate how lawyers appear and practice before us, including minimum standards of professional conduct for corporate lawyers."[18]

[13] M Rozen, "V&E Reacts to Enron Shareholders' Latest Allegations", *Texas Lawyer*, 17 June 2002, <http://www.law.com/jsp/article.jsp?id=1024078842414>. The firm once counted Enron as its largest client. In 2001, Vinson & Elkins billed Enron $36 million—more than 7 percent of the firm's revenue" M Flood, "Lawyers Proud Of Role At Enron. Firm Touts Expert Legal Work Despite Corporate Debacle", *Houston Chronicle*, 16 August 2002, < http://www.chron.com/cs/CDA/story.hts/special/enron/1538107>.

[14] In 2001 Andersen earned $27 million from Enron in non-audit fees. *Ibid*.

[15] *Economist* "Professional Services: Goodbye Monday", *Economist*, 3 August 2002, p. 56.

[16] *Economist* "Audit Firms: Tough New World", *Economist*, 3 August 2002, p. 63.

[17] I Schacter and A Scheibe, "Why Lawyers Should Not Become Corporate Watchdogs", *International Financial Law Review*, September 2002, p. 12.

[18] H Pitt, "Speech by SEC Chairman: Remarks Before the Annual Meeting of the American Bar Association's Business Law Section", 12 August 2002, <http://www.sec.gov/news/speech/spch579.htm>

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This may well put a severe dent in the attorney-client privilege as lawyers are being cast as the protectors of the shareholders against the management. As Pitt put it,

> "Lawyers for public companies represent the company as a whole and its shareholder-owners, not the managers who hire and fire them . . . Attorneys must be vigilant in protecting the interests of their true clients."[19]

But the SEC chairman went even further when he chided lawyers,

> "The question every corporate lawyer is taught to ask at the outset of a representation is, 'Who is my client?' Contrary to popular belief, this is not so they'll know where to send bills. Rather, it is so they'll know whose interests they are sworn to protect. When a corporation hires a lawyer, the lawyer represents the corporation and its shareholders. Being ever mindful of this answer can help protect lawyers from the fate visited upon the accounting profession."[20]

Enron, therefore, has effectively killed the attractiveness of the MDP as the preferred mode of professional organisation, for the time being. However, some of the law firms that joined Andersen then fled have not reverted to their single status, instead preferring to link with other accounting firms. It is likely that Enron and its aftermath may impose a temporary moratorium on the formation of MDPs, but it is impossible to stifle innovation in the organisation and delivery of professional services, including legal services, in an aggressively competitive and integrated world. Although lawyers and accountants are the most affected, we can envisage new agglomerations of professional services such as banks, law firms, insurance companies and accounting firms eventually emerging.

## Conclusion

For some the coincidence of *NOvA* and Enron may be a happy one; one that is a death knell for multi-disciplinary partnerships. For others it will be a temporary blip in the trajectory of a complex, corporatised and globalised world. While the ECJ has enabled national bars to restrict MDPs (in a time when no one really wants them) and the SEC is establishing itself as a new global super-regulator, commerce and finance will continue to demand sophisticated professional services. We can be sure that corporate memories are short over economic cycles. As the recession recedes, the repercussions of Enron and its acolytes will fade and dissipate. Governments and national bars will realise that *NOvA* may serve to protect them in the short term, but if the Anglo-American professional axis is perceived to be outmanoeuvring their professions, they will relax their stance.[21] In the global sphere, competitive forces will dominate.

[19] *Ibid*.
[20] *Ibid*.
[21] The Lord Chancellor's Department has already announced a consultation process based on the Office of Fair Trading's critique of competition in the professions, which will liberalise the UK legal profession further. See *In the Public Interest*, CP 07/02, July 2002.