



The Law Society

**Law Society response to the Competition and Markets Authority invitation to comment on the notice on the market study into the supply of legal services in England and Wales**

15 February 2016



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#### Executive Summary

The Society is interested to engage with the CMA's market study into the supply of legal services in England and Wales set out in the Market Study Notice and the accompanying Statement of Scope. Given that there are two proposed consultations, one on separating regulators from their professional bodies and a second on opening up the market for Alternative Business Structures,<sup>1</sup> and a possible broader review of legal services regulation later in this Parliament, it is important to understand the interrelationship of timing between the consultations/review and the market study.

The study is focussed on the market for services to individuals and small businesses, however any proposals for reform may have unintended consequences for other market segments including legal services for large businesses; even within the segment being studied there will be certain legal services (for example conveyancing and litigation) where market forces and public interest considerations are very different to those for other services (such as general legal advice). The CMA is urged to acknowledge these differing factors in its approach.

The market for legal services to individuals and small businesses is fragmented with multiple providers, some subject to professional regulation and some not. Even among solicitors subject to SRA regulation there are a large number of firms and individuals of a range of size and offering a broad range of services. Many consumers and small businesses do have a broad choice of provider for their legal needs. Fixed fees are common, aiding predictability and comparison, and there are price and quality comparison services available. Entry and exit rates are similar to other business sectors.<sup>2</sup>

Solicitors face significant competitive challenges from other solicitors firms. Competition also exists from non-solicitors including other regulated providers (such as licensed conveyancers and barristers) as well as providers not subject to professional regulation (i.e. under the Legal Services Act 2007). The availability of 'legal advice' from 'lawyers' with no qualification and no professional regulation gives rise to consumer confusion and a (misplaced) expectation that all legal service providers offer the same range of protections and that standards are uniformly regulated.

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<sup>1</sup> HM Treasury, cmnd 9164, November 2015

<sup>2</sup> *Understanding barriers to entry, exit and merger*, 2013, Regulatory Policy Institute (George Yarrow and Chris Decker) for TLS and LSB found that entry and exit rates were around 10% for 2-3 years, only a little below average rates across all UK businesses.

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The legal services market like many others is being both stimulated and disrupted, as it always has been, by advances in technological capability which in some areas leads to the commoditisation of legal services.

The scale of unmet legal need is unclear and difficult to measure and define. One significant measure of unmet need is the number of individuals who want to access legal services but cannot afford to do so, regardless of cost. This is where the government has a direct influence in the market as a purchaser of legal services through the legal aid schemes. However, the government has significantly reduced its spend over time and limited the scope of entitlement to legal aid both for criminal and civil cases. This means that where, for example in family law, the level of unmet legal need appears to have increased, this is not a market failure, but a matter of public policy with public welfare consequences.<sup>3</sup>

Many consumers make the rational choice not to use a legal services provider to meet a legal need and, while cost is a factor for some in making this choice, it is not the principal factor – in many cases consumers take the view that they are perfectly capable of handling legal issues themselves or, having identified a legal need, they choose not to pursue (or alternatively, choose to settle) the matter because they make a judgment about the emotional or other costs.

The Society raises awareness of the availability of legal services and strives to broaden and increase access to such services. Our members have their own business imperative to attract and retain clients and everyone who is a consumer of professional services wants those services to be responsive, to present value for money, and to be of good quality. There is evidence from the unregulated sector of risks of pressure on consumers to use paid-for services when they are capable of self-providing. For 'unmet need' to be evidence of market failure, there would have to be evidence of detriment (for example, inefficiencies in business dealings or inefficient outcomes in relation to disputes).

The Society and the solicitors' profession are committed to support the rule of law and maintain values in the public interest. The regulatory system must also take account of broader public interest objectives, or positive externalities. A well-functioning and properly regulated legal services sector generates significant consequential value including: security of transactions (contract and property); supporting lending, investment and innovation; reducing risk; social benefits (for example housing security); and supporting good government.

The independence of lawyers from the state is crucial to underpin an effective legal system and is a critical factor for the international reputation and success of English law firms. The profession must be, and must be seen to be, unfettered in its ability to uphold the law. Only if this is the case can lawyers represent the interests of individuals and businesses fully, particularly in the many areas where individuals' interests can conflict with those of the state.

The CMA's theories of harm identify the risk of regulatory capture without structural separation of legal regulators and professional bodies. We are not aware of credible evidence of any regulatory policy, initiative or enforcement that has been improperly influenced by the profession. Indeed, the involvement of the profession has

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<sup>3</sup> See for example the House of Commons Library: *Briefing Paper 07113 Litigants in Person: the rise of the self-represented litigant in civil and family cases* 14 January 2016 which reports the National Audit Office finding of a 22% increase in cases involving contact with children (Children Act 1989 private law matters) and a 30% increase across all family court cases (including those that remain eligible for civil legal aid) in which neither party had legal representation

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produced value.<sup>4</sup> By contrast, no weight is given in the theories of harm to the much greater risk to the independence and effectiveness of the system where an oversight regulator is appointed by the state.

The Society believes:

a. Solicitors are subject to a rigorous regulatory regime (this includes regulation of all their legal activities; insurance and compensation requirements and redress requirements). Unregulated providers operate largely outside this regime to the confusion and detriment of consumers.

b. The current regulatory regime is not without difficulty in that:

- the oversight regulator is a state appointee who is perceived to lack independence from the state;<sup>5</sup>
- some services are regulated on an activity basis (reserved activities) and others by provider: some providers, such as solicitors, are regulated for all their legal activities (reserved and unreserved) while some are unregulated, providing uneven regulation and giving confusing messages;
- unregulated providers are free to offer important services with no protection beyond general consumer law; and while quality services are important to consumers, consumers have difficulty in assessing quality before they purchase services. Low quality providers are free to drive out higher quality providers, to the detriment of consumers, while delivering services of unreliable quality; and
- paradoxically, the people who are the most qualified and trained are the most regulated and those with no legal training the least regulated.

c. Consumer interests and the wider public interest are best served by a professional title, properly overseen by a professional body. Professional titles are an important hallmark of quality and provide reassurance and guarantees to consumers. The title 'lawyer' should be protected.

### **The Law Society**

2.0 The Law Society of England and Wales (the **Society**) is the professional body for the solicitors' profession in England and Wales, representing over 160,000 members. The Society represents the profession to parliament, government and regulatory bodies and has a public interest role in the reform of the law, maintaining the rule of law and in securing access to justice.

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<sup>4</sup> In 2015, the Society was instrumental in persuading the SRA not to cease the regulation of solicitors who undertake consumer credit activities, as was their original proposal. Had this actually happened, levels of regulation would have increased with solicitors in that part of the market effectively subject to dual regulation: by the FCA for consumer credit work and the SRA for other activities. Part of the Society's influencing success was around its research which showed that the effect on many firms would have been them exiting the market as the levels of regulation undermined the business viability of them doing that work. This in turn would have limited consumer choice and access to such services.

<sup>5</sup> The German Bar BRAK, for instance, formally submitted a Memorandum to the Joint Committee on the Draft Legal Services Bill which touched on the issue of independence (<http://www.publications.parliament.uk/pa/jt200506/jtselect/jtlegal/232/6062624.htm>). The Council of Bars and Law Societies of Europe (CCBE) has also emphasised the importance of the independence of the legal profession in England and Wales (please see paragraph 0 below for further details).

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2.1 The Society is incorporated by Royal Charter, which provides for the Society '*promoting, advancing or protecting the interests, usefulness and efficiency of the Solicitors branch of the legal profession and Members of the Society.*' In addition to the Charter, the Society derives its legal standing from the Legal Services Act 2007 (the **Act**). Under Schedule 4 of the Act, parliament has designated the Society as an Approved Regulator (**AR**) for specified reserved legal activities. The Society previously derived a number of statutory functions from the Solicitors Act 1974, largely superseded by Schedule 16 of the Act.

Parliament granted the Society statutory powers and responsibilities consistent with the model for legal regulation set out by Sir David Clementi in his 2004 *Report of the Review of the Regulatory Framework for Legal Services in England and Wales (Clementi)* which was in large part implemented by the Act. The premise of that report, and of the Act, was that the regulation of the legal profession should not be distanced from the profession itself.

The Society's regulatory functions have been delegated to an independent ring-fenced board. The independent Solicitors' Regulation Authority (the **SRA**) operates with a lay majority with its own budget and keeps its policy considerations and enforcement processes private. All ARs are obliged to exercise their regulatory functions in such a way as to be both compatible with the regulatory objectives of the Act and most appropriate to meet those objectives (Section 28 of the Act). The regulatory objectives are a core concept within the Act, set out at the start in Section 1. They include:

- (a) protecting and promoting the public interest;
- (b) supporting the constitutional principle of the rule of law;
- (c) improving access to justice;
- (d) protecting and promoting the interests of consumers;
- (e) promoting competition in the provision of services within subsection (2);
- (f) encouraging an independent, strong, diverse and effective legal profession;
- (g) increasing public understanding of the citizen's legal rights and duties;
- (h) promoting and maintaining adherence to the professional principles

2.5 The SRA:

- sets the standard of entry to the solicitor profession;
- sets standards of professional conduct and behaviour which are treated as regulatory minimum standards;
- awards the professional title of solicitor; and
- enforces regulation against solicitors, including regulation relating to professional standards (there is no distinction between solicitors' professional standards and the regulatory rules).

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## The market study

The CMA's market study into the supply of legal services (the **Market Study**) comes at a time when changes in the regulatory structure of legal services are being considered as a result of the current consultation ("A Better Deal") launched by HM Treasury (**HMT**) and being taken forward by the Ministry of Justice (**MoJ**), and in particular within this, the consideration of structural separation of the regulators from their professional and representative bodies. The Department of Business, Innovation and Skills (**BIS**) has also launched a number of initiatives to promote innovation and deregulation.<sup>6</sup> The CMA's work should help to ensure a consistent overall approach and that important considerations such as competition, consumer protection and public interest are properly taken into account. In light of this, the government should be encouraged to look at the Act holistically to ensure any detrimental and unintended consequences of change based on a limited review of the market are avoided.

The Market Study's scope is the provision of civil law legal services to individuals and small businesses in England and Wales. We understand why the CMA has chosen to focus on this market segment as smaller consumers are potentially more vulnerable than larger businesses and public bodies. However, there are important limitations to such an approach. The Market Study might give rise to findings that are specific to the sector (or parts of the sector) under investigation from which it would be unwise and dangerous to draw general conclusions about legal services as a whole. So, for example, large commercial law firms compete in a global market with law firms headquartered in other jurisdictions. In some cases English headquartered firms will have substantial operations elsewhere in the world: five of the ten largest law firms in the world, based on gross fee revenue, have their main base of operations in the UK.<sup>7</sup> The legitimacy and standards of the England and Wales regulatory regime, including the authority of the Law Society as AR and standards of education and training, are important factors in that competitive process. There is a close connection between large firms and the City financial sector which means that any change could have implications for London as a global business centre.

Even within the segment for individuals and small businesses, there are very distinct service areas that may differ from each other in terms of supply side and demand side characteristics and the need for broader public protection. So, for example, litigation and advocacy services are not just important consumer services but are integral to the effective operation and credibility of the courts and subject to the authority of the courts. Conveyancing underpins the security of title to land and Probate services are key to the proper administration of death duties and orderly devolution of assets. Conclusions and proposals for change that may seem appropriate in relation, for example, to the provision of generic legal advice might have an adverse impact in the context of other legal service areas. So, while we note the selected case study approach around segments, it is important to take into account that, within the segments being considered, market circumstances and public interest requirements may be different according to the particular service being reviewed.

We set out our initial views on the case studies proposed by the CMA in the Scope of Study document in Annex 1 of this submission. In Annex 2 we provide a summary of proposed or imminent changes to legal services provision. In Annex 3 we enclose the Society's Report on the *Future of Legal Services* (**Future's Report**). All research documents produced for and by the Society referenced in this response are attached to this submission

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<sup>6</sup> <https://www.gov.uk/government/publications/a-better-deal-boosting-competition-to-bring-down-bills-for-families-and-firms> .

<sup>7</sup> See [https://en.wikipedia.org/wiki/List\\_of\\_100\\_largest\\_law\\_firms\\_by\\_revenue](https://en.wikipedia.org/wiki/List_of_100_largest_law_firms_by_revenue). This confirms that 5/10 of largest law firms in the World are headquartered in the UK. The underlying source is the American Lawyer, *2015 Am Law 100*. NB This cannot be accessed directly without a subscription to the publication, which the Society does not have.

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in the enclosed indexed bundle. We shall separately let the CMA have a document setting out our views on the three theories of harm identified by the CMA.

In the following pages, we set out our initial views on the issues raised in the Statement of Scope. We set out some key points on the scope of the study, rather than our detailed position on each and every aspect that the study might cover. We welcome the opportunity for further engagement with the CMA as the study progresses. Please note that this submission and the annexes contain information that is confidential and the CMA should consult us before disclosing the submission and annexes, and information within them, to third parties.

In the remainder of this submission we:

- briefly set out some observations on the markets that are within the scope of the CMA's study (section 0);
- consider the extent of, and reasons for, unmet need for legal services which appears to be an important driver of the CMA's study (section 0), and
- set out a number of essential consumer and public interests that need to be taken into account in assessing the market, including the interaction between the regulatory regime, competition and the protection of consumer and public interests (section 0).

#### **Legal services to individuals and small businesses**

As the CMA recognises, the term 'legal services' encompasses a broad spectrum of services. The Society considers that legal services embraces all activities engaging the application of law to states, institutions or citizens and that legal service providers include the courts and judiciary as well as the solicitors and other regulated professionals, including many working in-house in the private sector, central and local government and the third sector (shown in the below table)<sup>8</sup> and, in our significantly unregulated market, non-regulated providers.<sup>9</sup> As such, services provided by solicitors are just one (important) part of a wider symbiotic system.

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<sup>8</sup> 19.7% of solicitors are in-house and of those 67% practise in the private sector (commerce and industry + accountancy services) Law Society Research Unit (16 Feb 2016) based on SRA data received July 2015.

<sup>9</sup> The definition we use for legal services is derived from the work of Dr George Barker at the ANU Centre for Law and Economics.

	Number of PC-holders	% TOTAL in-house
Commerce and industry	17393	66.3%
Accountancy practice	189	0.7%
Government department	231	0.9%
Local government	4538	17.3%
Court	21	0.1%
Government funded services	215	0.8%
Crown Prosecution Service	1808	6.9%
Advice service	368	1.4%
Educational establishment	484	1.8%
Health services	78	0.3%
Others*	917	3.5%
<b>TOTAL In-house</b>	<b>26242</b>	<b>100.0%</b>
<b>TOTAL All PC-holders</b>	<b>133,367</b>	
<b>TOTAL In-house as % TOTAL All PC-holders</b>	<b>19.7%</b>	

The scope of the CMA's study is the provision of civil law legal services to individuals and small businesses in England and Wales. This is a highly fragmented market segment with a wide variety of regulated and unregulated providers. The table below describes legal service provision by the number and turnover of solicitor, barrister and 'other' (mainly non-regulated) providers. Barrister 'firms' tend to be very small so turnover is a better indication of relative market significance than number of firms. The data relates to all legal services, not just the market segment being examined by the CMA. It can be seen that 'other' providers account for just under one third of the total market. It is not unreasonable to assume that 'other' providers will have a higher share of the individual and small business segment than the segment for services to larger businesses.

	Number of firms				Turnover			
	Solicitor firms	Barrister firms	Other legal services providers	Total	Solicitor firms	Barrister firms	Other legal services providers	Total
2008	44.9%	31.2%	23.9%	100.0%	56.3%	7.9%	35.7%	100.0%
2009	44.4%	32.5%	23.1%	100.0%	57.1%	6.6%	36.3%	100.0%
2010	44.2%	33.2%	22.5%	100.0%	58.3%	8.8%	32.8%	100.0%
2011	44.0%	33.5%	22.5%	100.0%	55.9%	8.8%	35.3%	100.0%
2012	43.0%	33.8%	23.3%	100.0%	58.6%	7.2%	34.2%	100.0%
2013	42.1%	33.8%	24.1%	100.0%	58.1%	10.3%	31.6%	100.0%

Source: Latest ONS Annual Business Survey (released 11 June 2015)

The tables below set out the number of firms and solicitors in England and Wales and their breakdown by type of work. There are more than 7,000 solicitors' firms (and 40,000 solicitors) providing advice to individuals and the smallest businesses. Some of these firms are very small one partner operations while others are large national businesses. The spread of work types is very wide with over 10,000 solicitors practising in each of the top 14 areas.<sup>10</sup>

<sup>10</sup> The vast majority of firms (63.7%) practise in the consumer segment, although the majority of solicitors (54.4%) practise in the business to business market. There is a significant segment (18.4% of firms and 19.6% of solicitors) which have hybrid business and consumer practices.

**Practising certificate holders as at July 31 2015**  
Source: Law Society Group Management Information

**Notes:**

- Work type totals and %s are for Practising Certificate holders only (not all members on the Roll);
- Practising solicitors can report multiple worktypes (the average is 2.75 work types) and this should be borne in mind when viewing %s below;
- July data are the best and historically consistent snapshot of individual practising solicitors and work types during the year;
- Data snapshots at other times (particularly beginning and end of the year) will reflect the practising certificate bulk termination exercise at the end of the year where SRA terminates those practising certificates which have not been renewed

	31 July 2014	31 July 2015	31 July 2015 (% total PC holders)		Work types as at 31 July 2015	Number of solicitors practising work type	% of all work types practised by all solicitors (ranked)
<b>Solicitors on the Roll</b>	<b>160,394</b>	<b>168,226*</b>		<b>Work type</b>	<b>26,374</b>	<b>7.2%</b>	
Solicitors with Practising Certificates (PCs)	130,382	133,367		Business Affairs	24,951	6.8%	
Private practice firms registered in EAW	9,542	9,403		Litigation - General	21,236	5.8%	
Women solicitors with PCs	62,844	65,147	49%	Commercial Property	19,949	5.4%	
Women partners	7,985	8,098		Litigation - Commercial	16,439	4.5%	
Solicitors from minority ethnic groups with PCs	17,831	18,547**	14%	Conveyancing Residential	13,763	3.8%	
Solicitors working in private practice	90,306	91,062	68%	Wills and Probate	13,733	3.7%	
Solicitors employed outside private practice	25,325	26,242	20%	Employment	13,293	3.7%	
New solicitors admitted to the Roll 2014-15	6,345	6,077	5%	Family	13,013	3.5%	
Trainee solicitors commencing contracts 2014-15	5,001	5,457		Corporate Finance	12,956	3.5%	
				Personal Injury	11,611	3.2%	
				"Crime - General, Motor, Juvenile"	11,494	3.1%	
				Mergers and Acquisitions	11,376	3.1%	
				Landlord and Tenant - Residential	10,512	2.9%	
				Advocacy	8,566	2.6%	
				Banking Law	9,105	2.5%	
				Intellectual Property	7,447	2.0%	
				Energy and Natural Resources	7,421	2.0%	
				Children Law	7,199	2.0%	
				Financial and Investment Services	6,261	1.7%	
				Trusts	5,683	1.5%	
				Administrative and Public Law	5,654	1.5%	
				Insurance	4,888	1.3%	
				Computer and IT Law	4,887	1.3%	
				Taxation	4,664	1.3%	
				Professional Negligence	4,390	1.2%	
				Insolvency and Bankruptcy	4,221	1.2%	
				Fraud	4,032	1.1%	
				Immigration and Nationality	3,948	1.0%	
				Construction / Civil Engineering	3,662	1.0%	
				Mediation - Civil / Commercial	3,648	1.0%	
				Medical Negligence	3,511	1.0%	
				Media / Entertainment Law	3,216	0.9%	
				European Community Law	2,870	0.8%	
				Common Law	2,852	0.8%	
				Debt and Money Advice	2,810	0.8%	
				Mediation - Civil / Commercial	2,708	0.7%	
				Planning Law	2,489	0.7%	
				International Law (Non-EC)	2,488	0.7%	
				Consumer Problems	2,476	0.7%	
				Civil Liberties / Human Rights	2,454	0.7%	
				Environment Law	2,191	0.6%	
				Liquor Licensing / Gambling	2,045	0.6%	
				Charity Law	1,922	0.5%	
				Maritime / Shipping / Admiralty	1,808	0.5%	
				Neighbour Disputes	1,512	0.4%	
				Mental Health	1,409	0.4%	
				Transport - Road and Rail	1,270	0.4%	
				Education	1,246	0.3%	
				Immigration - Other	1,138	0.3%	
				Agricultural Law	1,138	0.3%	
				Chancery	1,134	0.3%	
				Welfare Benefits	1,032	0.3%	
				Immigration - Asylum	982	0.3%	
				Mediation - Family	942	0.3%	
				Libel and Defamation	938	0.3%	
				Aviation	469	0.1%	
				Pension Law	368	0.1%	
				Travel and Tourism	22	0.0%	
				Military Law			
				Art Law			

\* 2015 Roll is not comparable with previous years as keeping of the Roll is no longer done on an annual basis.  
\*\* Excludes some BAME solicitors admitted after 31 July 2014 where information is missing from online collection

**Firms' categories of work (2013/14)**

	All firms undertaking this category of work				Firms specialising in this category of work (ie firms where % turnover in this category of work > 30% of total turnover)				
	Total turnover in this category of work (all firms) (£m)	% total	Total number of firms undertaking this category of work	% total	Number of firms where % turnover in this category of work > 30%	% total	Number of solicitors in these firms	Total turnover of these firms in this category of work (£m)	
Business-to-Business (B2B)	Corporate / Commercial	£5,169m	24.2%	2773	29.5%	647	6.9%	20357	£4,090m
	Commercial property / Planning	£1,720m	8.1%	432	4.6%	290	3.1%	2707	£205m
	Intellectual property	£903m	4.1%	497	5.3%	55	0.6%	590	£75m
	ADR/Other litigation	£3,625m	17.0%	4472	47.5%	704	7.5%	13327	£1,842m
	Other B2B	£687m	3.2%	153	1.6%	8	0.1%	1525	£274m
<b>Total B2B</b>	<b>£11,994m</b>	<b>54.4%</b>	<b>6355</b>	<b>67.8%</b>	<b>2230</b>	<b>23.7%</b>	<b>50947</b>	<b>£10,983m</b>	
Business-to-Hybrid (B2H) (mixture of work for businesses and work for consumers)	Employment	£873m	4.1%	3508	37.3%	323	3.4%	1068	£90m
	Personal injury	£2,447m	11.5%	2620	27.8%	926	9.8%	11332	£2,114m
	Other B2H	£935m	4.0%	3938	41.9%	291	3.1%	1051	£124m
	Total B2H	£4,173m	19.6%	5894	62.7%	1736	18.4%	16817	£2,842m
	Family / Children	£980m	4.6%	4387	46.6%	1078	11.5%	5031	£406m
Business-to-Consumer (B2C)	Criminal	£730m	3.4%	2123	22.6%	1044	11.1%	6384	£566m
	Residential conveyancing	£1,264m	5.9%	4671	49.7%	1674	17.8%	8027	£607m
	Probate	£568m	2.7%	3723	39.6%	441	4.7%	1366	£85m
	Wills and trusts	£606m	2.8%	4287	45.6%	198	2.1%	877	£77m
	Total Wills and trusts + Probate	£1,174m	5.5%	8510	89.1%	639m	6.8%	22,43m	£155m
	Immigration	£196m	0.9%	1531	16.3%	700	7.4%	2388	£139m
	Mental health	£42m	0.2%	271	2.9%	68	0.7%	345	£16m
	Discrimination/Civil liberties/Human rights	£20m	0.1%	111	1.2%	9	0.1%	69	£3m
<b>Total B2C</b>	<b>£4,458m</b>	<b>20.8%</b>	<b>7242</b>	<b>77.0%</b>	<b>5888</b>	<b>63.7%</b>	<b>38739</b>	<b>£3,824m</b>	
Business-to-Other (B2O) (work that does not fit into any of the listed categories)	£525m	2.5%	2631	28.0%	197	2.1%	644	£60m	
Don't know split of turnover or total turnover figure not available	£597m	2.8%	538	5.7%	538	5.7%	3083	£597m	
<b>All firms</b>	<b>£21,326m</b>	<b>100.0%</b>	<b>9407</b>	<b>100.0%</b>	<b>9407</b>	<b>100.0%</b>	<b>92136</b>	<b>100.0%</b>	

Source: Law Society Research Unit (4 Feb 2016)

- Notes:  
Figures based on SRA data received July 2015  
Latest figures relate to 2013/14 due lags in producing accounts  
Total number of solicitors figure (92136) is higher than the actual number of solicitors as some solicitors work for more than one firm  
Sum of number of specialist firms is higher than total, as some firms have greater than 30% of their turnover in more than one category of work

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Entry and exit rates for the solicitors' part of the market stand at around 10% for 2-3 years, only a little below average rates across all UK businesses.<sup>11</sup> This suggests that those wishing to enter the market are able to do so and that unsuccessful businesses are not protected from the consequences of their failure.<sup>12</sup>

Consumers have a wide choice of providers, regulated and, for many services, unregulated. According to the Legal Services Consumer Panel (**LSCP**) tracker survey, almost 70% of people who used legal services in the past two years believed that they had a choice of provider.<sup>13</sup>

Fixed-fee and no-win-no-fee legal advice are now widespread allowing customers to know with greater certainty the costs they will face and to compare costs between different providers. According to LSCP's 2015 Consumer Tracker data, 46% of consumers of legal services had had their costs calculated as a fixed fee, up from 38% in 2012. The SRA has reported that fixed-fee arrangements are now more prevalent than hourly-billing in conveyancing, will-writing and immigration law.<sup>14</sup> There is also a strong trend in litigation for the further expansion of fixed fee arrangements such as Damages Based Agreements, which have recently been extended so that they can apply in contentious business, and Conditional Fee Arrangements, which are widely used in the personal injury context. The government has evinced its intention to introduce fixed fees in lower value clinical negligence cases and Lord Justice Jackson has recently announced his view that fixed fees could be introduced for a wide range of litigation (extending fixed fee schemes in the fast track and into the lower ranges of the multi-track).

Consumers can also benefit from after the event insurance which mitigates the risk of bringing an unsuccessful claim particularly in personal injury cases. This can even insure against paying the cost of the insurance cover. This, in particular in conjunction with conditional fee agreements, has led to an increase in the ability of individuals to bring claims in certain areas. Claims against the NHS for clinical negligence, for example, rose when after the event insurance became more widely available.

To help consumers judge the relative merits of providers, in terms of quality as well as price, the Society has developed the Find A Solicitor (FAS) service which seeks to add more information than the base level (SRA) regulatory data to enable consumers to make an even more informed choice about legal services providers. This however remains a challenge as long as many of the same legal services are offered by both the regulated and unregulated sectors to the confusion of consumers.

The Society's Futures Report, which builds on a detailed market assessment, including drivers of change, conducted by the Society between 2012 and 2013, identified significant competitive threats to solicitors in individual and small business markets from: barristers (to whom the public now have direct access); ABS (new entrants and transitioned law firms); legal tech companies; other regulated non-legal businesses (i.e. accountants, banks); other regulated legal (legal executives, licensed conveyancers expanding offerings) and unregulated

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<sup>11</sup> *Understanding barriers to entry, exit and merger*, 2013, Regulatory Policy Institute (George Yarrow and Chris Decker) for TLS and LSB.

<sup>12</sup> In relation to barriers to entry into the legal profession, it is appropriate to distinguish between entry restrictions that relate to quality of service in one way or another, and those which relate to quantity. In general, straightforward quota restrictions – i.e. restrictions on the number of lawyers who can practice in a particular area – are much the more problematic in terms of potentially adverse effects on competition, because they imply a direct restriction on the maximum level of supply. The restrictions relating to entry to the profession are linked to quality standards rather than simple caps on the number of lawyers. (Yarrow and Decker, *Assessing the economic significance of the professional legal services sector in the European Union*, 2012, paragraph 199). Quality barriers do not prevent new entry, and indeed, high quality services promote trust in an industry, and so can have market-expanding effects.

<sup>13</sup> [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Using\\_legal\\_services\\_000.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Using_legal_services_000.pdf)

<sup>14</sup> SRA Risk Outlook, page 10. Report available at <https://www.sra.org.uk/risk/outlook/risk-outlook-2015-2016>.

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providers.<sup>15</sup> The impact of these changes has been considerable, so for example, 30% of the turnover in personal injury cases is now generated by ABS. The abolition by the SRA of the 'separate business rule' is likely to increase the prospect of solicitors owning or managing non-regulated legal service businesses.<sup>16</sup>

We describe below, at paragraph 0, the confusion among consumers that is caused by having regulated and unregulated providers offering the same service but with different standards of consumer assurance and protection. The public is not aware of who is and who is not regulated or of the levels of protection afforded to them. There is no awareness of the concept of reserved legal activities for many consumers (and certainly not those within the scope of this study). Many simply do not realise that giving legal advice, mediation and employment advice are not regulated (or for that matter that immigration advice, claims management and insolvency work are regulated but not reserved activities). This issue is stark in relation to will writing. Consumers therefore have false assurance about standards and the competitive playing field between regulated and unregulated providers is undermined with regulated providers carrying regulatory costs that non-regulated providers benefit from (because consumers assume that all providers are regulated).

Technological change is having a significant impact. The Society's 2014/15 annual law firm study indicates that 14% of firms had replaced some work normally done by non-fee earning staff with automated IT processes in the preceding 12 months.<sup>17</sup> The implication is that this drives down costs to the consumer. The Future's Report sets out the ways in which technology is impacting on legal services. The report concludes that technology is allowing certain types of legal work which are more procedural to be undertaken using technology. This is changing client buyer behavior. Process-driven legal services are being commoditised through automation. In time, with cheaper computing power and better software, increasingly sophisticated services may be automated. Artificial intelligence, 'big data' and communication are areas where revolutionary change is taking place. The effective use of technology has the potential to widen access to justice, by reducing the costs of accessing legal services. However, not all clients will be able to access or use technology and many clients will still require expert legal advice, for example, when using an on-line court. Further, the weight of relevant legislation and new risks (such as cyber crime) means that legal processes become ever more complex in each area of activity

### **Unmet need for legal services**

An important driver of the Market Study appears to be concern that the legal service market is not responding to a significant level of need for legal services. Access to legal services for those who need them is a fundamental requirement of an effective legal system and the Society has over the years engaged in a number of public campaigns to draw the availability of services to the attention of consumers.<sup>18</sup> Similarly, individual solicitors firms have sought in advertising not just to promote their own brands but also to access parts of the market that might otherwise not think about going to a solicitor. Solicitors also engage in a wide variety of *pro bono* and corporate social responsibility work, with a recent survey by the Society finding that 43% have done so in the

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<sup>15</sup> *The Future of Legal Services*, p38-41. <http://www.lawsociety.org.uk/support-services/research-trends/future-of-legal-services/>.

<sup>16</sup> <http://www.sra.org.uk/sra/news/press/sbr-changes-june-2015.page>.

<sup>17</sup> Annual Firm Survey 2014/15: snapshots from the results <http://www.lawsociety.org.uk/support-services/research-trends/annual-firm-survey-2014-15-snapshots-from-the-results/>

<sup>18</sup> See for example: <https://www.lawsociety.org.uk/news/press-releases/law-society-launches-bold-new-advertising-campaign-for-personal-injury/> and <http://www.lawsociety.org.uk/news/press-releases/law-society-launches-use-a-professional-campaign/>

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previous twelve months.<sup>19</sup> The scale and scope of ‘unmet need’ identified depends on how ‘legal need’ is defined and the research takes different, often not comparable, approaches to this. Pleasence and Balmer note:

*“Legal need is a contested concept. It has been used to refer to occasions when people experience legal problems but fail to obtain the services of lawyers to assist with resolution. However, it is generally recognised that legal mechanisms do not always provide the most appropriate route to solving problems that raise legal issues. Attempts to define legal need have therefore come to place emphasis on understanding of options and preferences”.*<sup>20</sup>

We would urge the CMA to consider the definition of unmet legal need carefully. In reality, people do not take legal advice when they encounter legal problems for a range of reasons, many of which do not suggest market failure, vulnerability or damage. In order to classify unmet legal need as an indication of market failure, there would have to be evidence of detriment (for example, inefficiencies in business dealings or inefficient outcomes in relation to disputes).

According to Pleasence and Balmer, the main reason for not seeking legal advice (in relation to justiciable issues) is that the individual thought there was “no need”.<sup>21</sup> Further research, using a broader concept of legal needs undertaken by the Legal Services Board (the **LSB**) has shown that while cost is a reason for some people handling their problems themselves, the main reasons identified included that: they did not think the problem would be difficult to resolve (24%); they had confidence in their ability to handle it alone (17%); or they had enough time to handle it alone (11%).<sup>22</sup> Just as some consumers rationally decide to self-medicate when faced with a minor illness rather than consult a health professional, so consumers make a judgement about their need for legal services and may rationally take the view that they should, for example, seek to negotiate a settlement to a trading dispute themselves and, only if things do not work out commercially, involve a legal adviser.

Indeed, there is evidence from the unregulated market (for example advisers seeking to encourage consumers to make mis-sold PPI claims) of inefficiencies and consumer detriment when advisers seek to persuade consumers to use a service when those consumers are perfectly capable of resolving the issue themselves. There have been numerous campaigns by consumer groups to persuade consumers to undertake PPI claims on their own. An undercover investigation by Which? for instance revealed that almost a third of the claims management companies they spoke to had serious shortcomings including exaggerating success rates, discouraging consumers from pursuing claims themselves or failing to be upfront about charges.<sup>23</sup> The Financial Ombudsman (the **FOS**) has stated that using an adviser makes no difference to the outcome of a complaint.

In the case of PPI, the SRA was alive to the risk and reminded solicitors of their professional obligations regarding clients when handling this work, specifically to inform customers that they would not be able to obtain more compensation than if the customers handled the claim themselves and the need to be clear of the fees they

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<sup>19</sup> See <http://www.lawsociety.org.uk/support-services/research-trends/solicitors-pro-bono-work-2015/>

<sup>20</sup> Pleasence and Balmer, *How people resolve legal problems* (2014)

<sup>21</sup> *Ibid.* Approaching a solicitor, or initiating other legal options, was generally seen as a reluctant choice to be avoided due to:

- (a) A fear of escalating the problem
- (b) the expense involved with solicitors
- (c) a sense that engaging a solicitor is often an open-ended, uncontrolled commitment, and
- (d) a belief that other options would often simply be more effective at resolving the issue.

<sup>22</sup> Legal benchmarking study, 2012, bdr for LSB – p.21-23). The Law Society, with the Legal Services Board and The Legal Education Foundation jointly funded a larger scale repeat of this survey in 2015 (with findings due in March 2016) to enable more detailed analysis by area of law of questions of unmet need and to explore whether or not patterns of behaviour have changed post LASPOA.

<sup>23</sup> <http://www.which.co.uk/money/insurance/guides/claims-management-companies/claims-made-by-cmcs/>

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proposed to charge. In the event, only 1% of PPI claims made in 2013/14 to FOS was handled by a professional (e.g. a lawyer or accountant) while 72% were handled by claims management companies.

Pleasence and Balmer confirm that cost is a 'live issue' among those looking to resolve legal problems but make that point specifically in the context of those choosing between different types of provider. They refer to earlier studies which *'have pointed to cost being only infrequently mentioned as an obstacle to initial action'*.<sup>24</sup> A further point they make, that should not be overlooked, is that public understanding of lawyers' costs is not *'particularly nuanced'*.

- 5.6 In considering cost, it is important to note that there is a significant group of individuals who would not be able to access legal services whatever the price. Such individuals, in terms of the importance of their requirements and extent of their need, are perhaps the most significant category of unmet need. The Pleasence and Balmer report noted that *"the legal services market and civil justice system do not ensure fair and equal access to justice, with deficiencies attributable largely to the difficulty of enabling vulnerable populations with limited capability and resources"*.<sup>25</sup> As is acknowledged in the Statement of Scope, this is not an indication of market failure. These individuals would not be able to afford services under any regime without some form of state or charitable support and are often unable to meet the costs of other important needs such as housing. As outlined above, solicitors address some of this need through *pro bono* and corporate social responsibility work but this can never be a substitute for a properly funded legal aid system. We understand that this is outside the scope of the CMA's enquiry but it is an important contextual issue to be taken into account.
- 5.7 Government actions have a direct impact on the market in this context. Changes to legal aid have meant that there is a new set of consumers who would have previously had legal services they required paid for by the state. Two of the largest areas of provision were family law and employment law. In 2012/13, the last financial year before the changes were made, there were over 200,000 matters started in relation to family law under the legal aid scheme and 15,000 matters started in employment law. The following financial year this had dropped to 43,000 and 6000 respectively.<sup>26</sup> According to the House of Commons Library, the National Audit Office has reported a 22% increase in cases involving contact with children and a 30% increase across all family court cases in which neither party had legal representation. This is as stark an illustration of 'unmet legal need' as any. It is unlikely the number of consumers with these legal problems has fallen this dramatically but they now need to pay for these services. This is a considerable change to the market which is still evolving to provide services to these consumers to the extent that it is possible to do so.
- 5.8 The Society believes that affordable access to legal advice is a basic right for everyone and has put forward recommendations to the government to improve access. Some of these recommendations include solicitors changing the scope of the work they do and unbundling services where possible and supporting *pro bono*

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<sup>24</sup> Ibid – p.102.

<sup>25</sup> Pleasence and Balmer, 2014, *How People Resolve 'Legal' Problems*.

<sup>26</sup> This explains, in part, the number of litigants-in-person in family law cases, noted by the CMA in its Statement of Scope at footnote 15.

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work by legal professionals.<sup>27</sup> Solicitors have a key role to play in the administration of justice but can only be part of the solution.

### **Competition, regulation and the public interest**

The Statement of Scope is almost exclusively focussed on consumer interests. We agree that these are of significant importance but we would ask the CMA to consider legal services also in the context of the wider economic and social value – or “positive externalities” – they provide beyond private individual transactions, thereby contributing to the public good. The legal services market facilitates transactions, investment, innovation, the management of risks and precautionary behaviour in the wider economy that are not likely to be fully reflected in an analysis that concentrates on direct consumer interests alone. Stephen Mayson captured this in his definition of public interest as: *“The public interest concerns objectives and actions for the collective benefit and good of current and future citizens in achieving and maintaining those fundamentals of society that are regarded by them as essential to their common security and well-being, and to their legitimate participation in society.”*<sup>28</sup>

The restricted perspective of the Statement of Scope is highlighted in paragraph 2.8: *“While such restrictions [i.e. regulations] can dampen competition, they may be justified if they are in the public interest and if the restrictions do not go further than is necessary to protect consumers.”* (underlining added).<sup>29</sup> We consider that there will be occasions where the objective of regulation is not just to protect consumers but to protect wider public interests. So, for example, the quality and efficiency of litigation and advocacy services is of fundamental importance to the effective operation of the courts which are the foundation of the rule of law in England and Wales and the lawful settlement of disputes. Similarly, the quality of conveyancing services underpins the security of title to property on which the economic and social system (and future generations) depend. An approach that considers the purpose of legal services regulation to be *purely* about consumer protection, or that consumer protection is always the paramount interest, risks undermining fundamental public interests in the rule of law and administration of justice.

While we consider that the CMA needs to give appropriate weight to wider externalities, we do welcome one important aspect of the Statement of Scope which is the emphasis on quality (in addition to price), and the impact that competition and the regulatory regime can have on positive externalities. The existence of an unregulated sector that provides some important services that compete with the regulated sector is confusing to consumers and risks focussing competition around price (as the only easily comparable measure) to the detriment of quality. Variability in quality of services in a market where final quality is important to consumers but consumers have difficulty in assessing quality before they purchase services (and sometimes, as with will writing, after purchase), is likely to result in low quality providers driving out higher quality providers to the detriment of consumers. It also means that support and redress that are available to consumers in the regulated sector (insurance, compensation fund and access to the ombudsman) are not available to consumers of unregulated providers creating costs and an uneven playing field that makes it hard for consumers to understand what they are getting.

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<sup>27</sup> There are risks in providing unbundled services which could be addressed by regulation to protect consumers who use unbundled services. See TLS Practice Note 'Unbundling Civil Legal Services' <http://www.lawsociety.org.uk/support-services/advice/practice-notes/unbundling-civil-legal-services/> and the Society's work and report on 'Affordable Legal Services' <http://www.lawsociety.org.uk/policy-campaigns/campaigns/access-to-justice/affordable-legal-services/>

<sup>28</sup> Legal Services Institute, *Legal Services Regulation and the public interest* (Legal Services Institute, 2011, revised 2013).

<sup>29</sup> This is mirrored by the CMA's *Theories of Harm* presentation, which notes that *“Our primary focus is on the impact on competition of regulation through recognising the potential trade-off with consumer protection”*.

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We address the following below:

- A. a credible legal system is essential to underpin an effective economy and for a legal system to be credible it requires an independent legal services regime of appropriate quality (this is in addition to the importance of the rule of law, access to and the effective administration of justice as public interests in their own right) (paragraph 0);
- B. an important element of a credible legal system is the role regulated lawyers play in representing the interests of individuals and businesses against the state in its various manifestations (central government; local government; taxation; police; regulators etc.) The actual and perceived independence of the profession from government is a necessity for a competitive market and to protect broader interests (paragraph 0);
- C. the consumer detriments arising from the existence of unregulated or low quality providers offering important legal services (paragraph 0);
- D. the importance of a professional title that can be relied upon by consumers (paragraph 0);
- E. the consumer redress provisions relating to legal service provided by solicitors provide a suitable and necessary level of assurance and customer protection that contributes to confidence in the English legal system; these are not matched in the unregulated sector (paragraph 0); and
- F. why the current regulatory regime is inadequate (paragraph 0).

#### **A. A credible legal system underpins an effective economy**

Before we address some of the wider public interest issues in subsections B – F below, we consider the broader competition and consumer benefits (beyond those accruing to direct consumers of legal services) arising from a well-functioning legal services market. The CMA rightly recognises that the legal sector is important to the UK economy in terms of its direct contribution and that a high quality, independent and well-regulated legal sector underpins the wider UK economy by helping consumers access and enforce their rights under the law and ensuring that businesses can be established and trade with appropriate security and confidence.

In a report for the European Commission, Professor George Yarrow and Dr Christopher Decker found that:

*“The principal conclusion is that economic analysis and evidence suggests that legal services can have wide ranging economic significance through their very close connection with the general institutional architecture of society (sometimes encompassed by a term such as the ‘rule of law’). Moreover, this analysis and evidence suggests that it is not by chance that good economic performance tends to be closely associated with the stable and well-functioning legal systems. Rather the institutions (including laws and norms) of a legal system condition and determine economic performance. Institutions that are stable and credible facilitate economic development and lead to higher levels of economic activity. In addition, although political institutions determine important aspects of the structure of a legal system, and whilst the judiciary determines how given laws are implemented, lawyers actively contribute, through their everyday actions and conduct, to both the shape of a legal system and how effectively it operates and functions.”*

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Attempting to quantify accurately the economic benefit of a well-functioning legal system is difficult. The direct contribution of legal services in terms of value added to the UK economy in the decade up to 2013 was £25.7bn per annum, equivalent to 1.6% of total UK GVA.<sup>30</sup> However, the true benefit of the sector extends much more widely through its “close connection with the general institutional architecture of society.”<sup>31</sup> The CMA cites a Law Society £2.39 output multiplier figure. While this is helpful, an output multiplier does not include other significant measures of value. Most importantly, it does not capture the wider social value resulting from high quality, independent legal services. Our analysis could not quantify the value derived from all external benefits and public goods derived by both purchasers and non-purchasers, for example, the deterrence value of law and the promotion of confidence in trade, investment or the value of legal advice that avoids risk or loss and dispute resolution with or without proceedings.

Recent research conducted for the Society concludes that standard economic theories applied to legal services markets often do not recognise legal services as being in the public good; that is their contribution to society beyond private exchange.<sup>32</sup> This contribution includes:

- Value created through market or exchange effects (property and contract);
- Value created through investment, innovation and risk effects;
- Value created through reducing social cost effects;
- Value created through reducing government failure effects;
- How low quality legal services can drive out good quality legal services; and
- How minimum quality standards create value.

## **B. Independence of lawyers**

Accepting, then, that a credible legal system is a crucial underpinning of a successful economy, it is necessary to consider the key aspects of the functioning of the legal system for that underpinning to work. Yarrow and Decker noted that:

*“Two aspects of the conduct of a legal profession appear to be particularly closely associated with the performance of a legal system, both of which are linked to central themes developed in later sections of this paper. The first aspect relates to the skills and abilities of legal professionals; in short, whether lawyers are adequately trained and resourced to perform the tasks required of them. The second aspect relates to the integrity of the profession, and in particular the extent to which the culture is one of professionalism and independence from external influences, including state influence.”<sup>33</sup> (underlining added)*

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<sup>30</sup> ONS figures (released 1 Feb 2016) <http://www.ons.gov.uk/ons/datasets-and-tables/index.html?pageSize=50&sortBy=none&sortDirection=none&newquery=gva+industry&content-type=Reference+table&content-type=Dataset>.

<sup>31</sup> Ibid.

<sup>32</sup> “A theoretical framework for assessing the value of legal services”, a presentation prepared by Dr George Barker for the Society.

<sup>33</sup> Yarrow and Decker, *Assessing the economic significance of the professional legal services sector in the European Union*, 2012, paragraph 40. We deal with the “first aspect” from paragraph [xx] below.

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The recent research for the Society referred to above notes that enhancing the independence and quality of legal services provides public benefits by lowering legal error and total administration costs.<sup>34</sup>

In this context, independence means independence from outside political and popular interests, in particular, independence from the state.<sup>35</sup> Legal services providers are in the frontline of protecting the interests of individuals and businesses against the state. This is most obvious in relation to the criminal law but it is much wider than this. Individuals may face numerous legal issues in which the state has an opposing interest, for example: state assertion of rights over property and taxation; access to benefits; immigration; employment where the state is the employer; and access to education. For businesses, their interests may be subject to state influence, for example, through regulatory regimes and the activities of regulators, state assertion of rights over property, public sector contracts and taxation. Access to legal advice from advisers who are demonstrably and clearly free of any direct or indirect relationship with the state (and are regulated under a regime free from state influence) is critical.

The important social and economic benefits to society of this independence can be best considered by a counterfactual where there are links between government and lawyers, for example through a regulatory regime in which government is seen directly or indirectly to have an influence in establishing the regulator, making appointments to the regulator, setting regulatory standards, supervising the profession or the enforcement of professional rules. Yarrow and Decker give examples in China and Latin America, where legal processes were not followed and confidence in legal rights broke down. They conclude that independence *“plays a critical role in the maintenance of the rule of law and, as such, is it is something that will be recognized and taken into account by any economic analysis that pays attention to institutional factors.”*<sup>36</sup>

The question of independence in the current regulatory regime in England and Wales has been commented on, often with some concern, by foreign bar associations. The German Bar BRAK, for instance, formally submitted a Memorandum to the Joint Committee on the Draft Legal Services Bill which touched on the issue of independence.<sup>37</sup> The Council of Bars and Law Societies of Europe (CCBE) has also taken a series of positions over the years on legal developments in England and Wales and elsewhere, in which they emphasise the independence of the legal profession.<sup>38</sup>

The global success of English law and English legal services has therefore been underpinned by the independence of the profession. The popularity of English law is an important contributor to the UK's strong position as the most international market globally for legal services: some 27% of the world's legal jurisdictions

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<sup>34</sup> “A theoretical framework for assessing the value of legal services”, a presentation prepared by Dr George Barker for the Society.

<sup>35</sup> In this context when referring to ‘the state’ we are referring to central and local government and other bodies in which government has an interest e.g. through funding, appointment or accountability to ministers.

<sup>36</sup> Yarrow and Decker, *Assessing the economic significance of the professional legal services sector in the European Union*, 2012, paragraph 55.

<sup>37</sup> <http://www.publications.parliament.uk/pa/it200506/jtselect/jtlegal/232/6062624.htm>

<sup>38</sup> See, for example: [http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/ccbe\\_position\\_on\\_req1\\_1182254709.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_req1_1182254709.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/11\\_2007\\_Nov06\\_Report1\\_1194344860.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/11_2007_Nov06_Report1_1194344860.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/ccbe\\_position\\_on\\_non1\\_1182254612.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_non1_1182254612.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/ccbe\\_position\\_on\\_mdp1\\_1182254536.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_mdp1_1182254536.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/EN\\_CCBE\\_response\\_to\\_1\\_1253701378.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/EN_CCBE_response_to_1_1253701378.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/EN\\_CCBE\\_Response\\_to\\_1\\_1253696350.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/EN_CCBE_Response_to_1_1253696350.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/100125\\_CCBE\\_letter\\_t1\\_1264511673.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/100125_CCBE_letter_t1_1264511673.pdf) ;  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/110112\\_Letter\\_Irel1\\_1326374114.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/110112_Letter_Irel1_1326374114.pdf) ; and  
[http://www.ccbe.eu/fileadmin/user\\_upload/NTCdocument/CCBE\\_and\\_ABA\\_letter\\_1\\_1325686329.pdf](http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/CCBE_and_ABA_letter_1_1325686329.pdf).

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use English common law.<sup>39</sup> England is regarded as a natural jurisdiction of choice throughout the world with recent research by TheCityUK finding that companies are twice as likely to choose English law over other governing laws for arbitration. Indeed, more than 20,000 commercial and civil disputes are resolved through arbitration, mediation and adjudication in the UK each year. As TheCityUK reports: *“The impartiality, integrity, quality and depth of experience of legal services and the judiciary found in the UK are particularly well-regarded, both domestically and internationally.”*<sup>40</sup>

Any perception that government may fetter or inhibit the legal profession’s independence impacts on the legal system’s international reputation and threatens the direct economic contribution made by solicitors. Damage to that global standing is likely to impact on GDP and directly affect the prospects of our large commercial and City firms which operate internationally.

We consider it disappointing that in its Theories of Harm presentation, the CMA notes that there *“may be issues of regulatory capture”* as regards lack of separation between regulators and professional bodies but pays no regard at all to the market consequences of an oversight regulator appointed by the state. There is only one country in Europe with a state legal services regulator, namely Norway. Poland attempted to introduce such a regime but abandoned the idea in the face of criticism from other EU Member States.

Nor is there any evidential base from which it can be determined that concerns about regulatory capture by the profession have greater weight than capture by the state. So far as frontline regulation is concerned, the SRA is for all material purposes independent of the Society as the professional body of solicitors. We are aware of no situation in which it has been suggested that the SRA’s decisions on policy or the enforcement of regulatory standards has been interfered with or undermined by the solicitors’ representative body. Indeed, there is plenty of public evidence to the contrary demonstrating the tensions that exist between the Society and the SRA in relation to how the SRA carries out its regulatory duties.<sup>41</sup>

The tension between separation of regulatory and representative functions and the independence of the profession was considered by Clementi who concluded that:

*“the principle that the legal profession should be independent of Government... is more clearly demonstrated ... where front-line regulatory powers can be exercised at practitioner level.”*<sup>42</sup>

### **C. Quality and Consumer detriment**

Yarrow and Decker’s report, cited above, notes that the skills and abilities of legal professionals are closely linked to the performance of a legal system. Minimum regulation, simplified and applied across all legal services, therefore ought to ensure that these services are provided by appropriately skilled people.

The current regulatory regime applies to some but not all legal service providers, and many legal services (including the broad category of “giving legal advice”) are unregulated.

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<sup>39</sup> TheCityUK, UK Legal Services 2015 (February 2015), available here: [uk-legal-services-2015-legal-excellence-internationally-renowned](#)

<sup>40</sup> TheCityUK, UK Legal Services 2015 (February 2015), available here: [uk-legal-services-2015-legal-excellence-internationally-renowned](#)

<sup>41</sup> See for example, the LSB’s rejection of the SRA’s proposal to reduce the minimum level of compulsory level of solicitors professional indemnity insurance following strong objections from the Society and other stakeholders.

<sup>42</sup> Sir David Clementi, *Report of the Review of the Regulatory Framework for Legal Services in England and Wales* (2004), paragraph 29(b)

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Research carried out by Vanilla Research demonstrates that consumers expect the legal services they purchase to be regulated:

*“There is a view that legal services are different to other sectors (it’s a profession, dealing with the law, and life-changing events), and that there should be sector-wide protections in place”.*<sup>43</sup>

The lack of regulation of all legal services can give rise to significant consumer detriment. In a survey of 2,000 people, Which? found that a quarter of people did not know that claims management companies take a fee. As Martin Lewis from MoneySavingExpert.com said: *“If people make a rational decision to give a huge 30% of what they’re due to a claims handling company in full knowledge they could do it themselves – I’ve no problem. Yet sadly very few are in that position. Many are persuaded under false pretences and the dire lack of regulation means it’s tough to tell legit firms from the rest.”*<sup>44</sup>

#### **D. The value of professional title**

Professional titles such as ‘solicitor’ or ‘barrister’ are hallmarks of quality, easily understood by consumers. Smith, Bailey and Gunn explain that, in relation to the quality of legal service:

*“One major source of quality assurance... should be by way of the admission of appropriate, qualified personnel who are provided with good training. Quality should also be assured, to some extent, by the professional practice rules and the complaints systems for clients.”*<sup>45</sup>

This view is mirrored by the judiciary. In a recent case relating to the failure of Wolstenholmes solicitors, the sentencing judge referred to solicitors firms as businesses *“in which members of the public are entitled to place absolute trust”*.<sup>46</sup>

The Legal Ombudsman has made the same point, noting the disparity between regulated and unregulated activities:

*“One of the clearest examples is with will writing firms. This is not a “reserved activity”—the thing that makes lawyers unique and what they need to be regulated to do. So, although such work is often carried out by lawyers, it is also done by will writing firms who are not regulated and who don’t have to abide by the same standards. This creates a potential confusion about whether or not the service being bought is regulated—and whether the consumer has access to redress from Legal Ombudsman.*

*These cases reveal a mismatch between consumer expectations of what constitutes a “legal service”—which consumers clearly assume implies access to redress—and the reality of the diverse market providing such services. This confusion is not helped by the habit many unregulated companies have of*

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<sup>43</sup> *Risk and the role of regulation*, research report for the Legal Services Consumer Panel by Vanilla Research, January 2013. Available at

[http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf)

<sup>44</sup> <http://www.which.co.uk/news/2012/04/one-in-four-consumers-unaware-claims-management-companies-take-cut-of-their-ppi-claim-284282/>.

<sup>45</sup> Smith, Bailey and Gunn, *The Modern English Legal System*, 5<sup>th</sup> ed, 2007, at 3-034.

<sup>46</sup> Case No.2MA3006 10 June 2014.

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*presenting themselves as though they were traditional law firms, with websites and advertising material branded with the panoply of wigs, gowns and quill pens.*<sup>47</sup>

Even when the services provided by solicitors are not reserved activities, the professional principles still apply and key principles such as the solicitors' integrity and confidentiality are engaged. This underpins quality of services.

Professional title properly overseen by a professional body was acknowledged as important by Clementi who noted that one advantage of leaving the extant front line regulatory functions at practitioner body level was that it was:

*“more likely to increase the commitment of practitioners to high standards; such commitment is important, particularly in the area of professional conduct rules, where rules of behaviour and ethical standards should be seen as an aid to raise standards, not as a constraint to be circumvented.”*<sup>48</sup>

A serious concern is that the title “lawyer” is not legally protected. Anyone can call themselves a lawyer or offer legal services as a lawyer (irrespective of whether they have any legal training or qualifications). This is confusing for the public and in some cases misleading. The LSCP considered that “lawyers” are more trusted than any other profession except teachers and doctors. Customers felt their consumer rights would be best protected in their dealings with “lawyers”. The implication appears to be that consumers think it is reasonable to place their trust in those holding a regulated title. We consider that a key part of the quality assurance provided by regulation comes from having regulated professional titles that carry distinct attributes such as expertise and training to high standards of service.

## **E. Redress services**

As the submissions of the Legal Ombudsman (above, at paragraph 0) show, the confusion as to the level of regulation a legal service provider is subject to extends to a confusion around redress mechanisms to which customers have recourse.

The regulatory regime in England and Wales is known for the high level of protection it offers solicitors' clients. Briefly, the compulsory Professional Indemnity Insurance (PII) requirements in the SRA Indemnity Rules provide considerable indemnity for firms and partners and, therefore, redress to clients:

- (a) The firm's PII will pay all claims up to £2m under the minimum terms and conditions that the SRA require to be included in all PII policies) (£3m for LLPs).<sup>49</sup> There are very limited exclusions where the PII will not pay out. Cover will be given if there has been misrepresentation on the proposal and it protects against fraud and dishonesty save for sole practitioners. In that instance the Compensation Fund is available to make grants to cover loss.

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<sup>47</sup>Written evidence from the Legal Ombudsman to the Justice Committee, September 2011, available at <http://www.publications.parliament.uk/pa/cm201213/cmselect/cmjust/97/97we04.htm>

<sup>48</sup> Sir David Clementi, *Report of the Review of the Regulatory Framework for Legal Services in England and Wales* (2004), paragraph 29 (a).

<sup>49</sup> The SRA Indemnity Insurance Rules 2013 set out at Appendix 1 the minimum terms and conditions of the Professional Indemnity Insurance which all solicitors must purchase. This prescribes the scope of cover, limiting cover, excesses, special conditions, extending the period and run off and exclusions. See <http://www.sra.org.uk/solicitors/handbook/indemnityins/appendix-1/content.page>

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- (b) Top up cover is available for firms which consider that their work needs greater cover, though the full range of the MTC will not apply to top-up.
  - (c) Where the insurance is insufficient, the firms' partners (and, possibly former partners) are liable for any losses.
  - (d) Run-off cover is required for six years.
  - (e) Claims brought more than six years after the closure of the firm are dealt with by the Solicitors Indemnity Fund. This arrangement may only last until 2020 (as it is subject to a decision by the SRA). The SRA is reviewing whether to impose any minimum compulsory insurance requirements and also propose reducing compulsory cover from six years to three. We consider these proposals will create a significant gap in client protection and work against consumer interest. It should be noted that the policy is written on a claims made basis, that is that insurance cover must be in place on the date the claim is made rather than the date the act of negligence occurred. arose.
  - (f) Moreover, complainants can use the Legal Ombudsman service, an alternative to negligence claims at a relatively low level. Complaints of true negligence can be made to the Ombudsman and will be considered; and there is no costs risk for the complainant. The Ombudsman's approach is non-technical so that normal litigation tactics are of limited benefit.
  - (g) The Ombudsman has considerable powers to resolve service complaints including ordering compensation (up to £50,000), reducing the bill and making a firm apologise. Serious cases are referred to the Solicitors Disciplinary Tribunal. Solicitors have to make clear to clients what redress schemes exist in accordance with their professional duties
  - (h) Further clients can use the Legal Ombudsman service as an alternative to negligence claims for values up to £50,000. Complaints of negligence can be made to the Ombudsman and will be considered; there is no costs risk for the complainant. The Ombudsman's approach is non-technical so that normal litigation tactics are of limited benefit.<sup>50</sup>

We note that the CMA has raised concerns about customers' awareness of, and trust in, redress schemes. We understand that this is due to be considered in an upcoming consultation by regulators on what information solicitors should provide to clients about their complaints options and the processes involved.<sup>51</sup> While awareness and trust can always be improved,<sup>52</sup> we consider that a more fundamental issue is that the level of redress available from firms of solicitors is not available from unregulated suppliers; something of which customers are often unaware, as explained above by the Legal Ombudsman.<sup>53</sup> In this context, the key considerations are: (i) whether redress mechanisms exist in relation to the provision of that legal service; (ii) whether customers are able

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<sup>50</sup> <http://www.sra.org.uk/solicitors/handbook/indemnityins/content.page>

<sup>51</sup> <http://www.lawgazette.co.uk/news/solicitors-set-for-new-guidance-on-complaints/5053494.fullarticle>

<sup>52</sup> Consumer confidence in complaining about to a lawyer is in fact similar to other service providers such as accountants and mobile phone companies and only slightly lower than banks (which, by virtue of scale, are not directly comparable to high street solicitors). See Legal Services Consumer Panel (2014) Tracker Briefing 2: Confidence and satisfaction. [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/)

<sup>53</sup> Europe Economics' 2013 report for the OFT on regulatory restrictions in the Legal Profession refers to regulators' requirements PII and compensation schemes for authorised entities as 'on-going compliance costs' which unregulated providers do not incur. (Economic Research into Regulatory Restrictions in the Legal Profession; A report for the Office of Fair Trading by Europe Economics, January 2013. OFT1460)

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to find out what these mechanisms are; and (iii) whether the mechanisms are effective in addressing customers' complaints.

#### **F. The current regulatory regime**

The Act established frontline regulators, owned by the professional organisations (although *de facto* independent from them), with an oversight regulator (the LSB) appointed by government. This was an attempt to ensure appropriate regulatory separation from government while maintaining a separation of regulatory and representative functions. The Society observes that currently:

- there are eleven frontline regulators that add costs to the system and contribute to consumer confusion;
- there is an oversight regulator that is appointed by, and accountable to, the government and is therefore by no measure independent of the state;
- the regime regulates according to activities (for the reserved activities) and extends regulation into a broader range of activities on the basis of professional title but permits unregulated providers to offer services in certain of those broader areas resulting in confusing messages to providers and consumers alike;
- unregulated providers are able to offer services, including in areas of significant importance, without adequate consumer protection thus distorting competition between the regulated and unregulated sectors. Paradoxically, those people who are the most qualified and trained are the most regulated, and people who may not have any legal qualifications or training are the least regulated; and
- the public is not aware of what services, and which providers, are regulated or of the levels of protection afforded to them.

We would welcome the opportunity to engage with the CMA on identifying areas of potential improvement.

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## ANNEX 1: CASE STUDIES

### *Do you agree with our three proposed case studies?*

We comment on the individual proposed case studies below. Before doing so we make one general observation. An important question to be considered in the case studies is how far there is unmet need in each area and, if there is, the extent to which this is an indication of market failure rather than other factors (we discuss this in section 0 of our submission). If there is unmet need, given that there are a significant number of unregulated providers in each of these areas, the question is raised whether the best way of meeting that need is by increasing the volume of providers or by raising standards across the sector so that people have greater assurance as to the quality (and benefits) of advice. We suggest that the study needs to look beyond the simplistic correlation, suggested by some, between appropriate levels of regulation as an alleged barrier to entry and unmet need.

### **1 Will writing and probate services to individual consumers**

There are an estimated 2.2 million new wills prepared in the United Kingdom each year and the market's estimated value is over £606 million.<sup>54</sup>

The drafting of a will seems relatively straightforward to most consumers. They are not in a position to anticipate the range of problems that can arise either by operation of law or by change in their circumstances.

Any failure on the part of the adviser may not be known until after the death of the client. Indeed, it may not even be known then if the failure results in the client's estate being distributed in a way contrary to the client's intentions. Making a will is therefore an important process for ensuring that an individual's wishes are carried out properly after their death. The skill in drafting a will is in drawing out sensitive information from the client and anticipating change and risks and presenting these in a way in which the client can readily understand.

People preparing a will must contemplate a number of undesirable possibilities, for example family break-up or the death or incapacity of friends and relatives. The drafting of a will can involve complex legal and financial issues, often involving technical issues of tax, trusts and property rights. There are issues as to capacity, duress and fraud.

Will writing services provided by a solicitor's firm are regulated ensuring that the client will benefit from the guaranteed protections of: (i) the qualification standards and on-going training requirements placed on solicitors; (ii) an enforceable Code of Conduct; (iii) minimum Professional Indemnity Insurance requirements; (iv) long stop provisions of the Compensation Fund where there is no insurance cover; and (v) access to the Legal Ombudsman. However there is also the benefit of overarching duties placed on all solicitors of professional conduct. All solicitors must act with integrity, failure to do so may well result in a solicitor being struck off the Roll.

For a number of years both regulated and unregulated providers have offered the service. Unregulated providers can write wills regardless of their lack of qualifications, training, insurance cover or any independent

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<sup>54</sup> YouGov Wills and Probate 2015 report.

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oversight. Providers can continue to do so even if they are expelled from any voluntary scheme or, in the case of solicitors, struck off the roll or suspended from practise.

The majority of buyers in this market are unsophisticated and many are vulnerable. They are reliant on the quality and integrity of the person they instruct. It is not clear if consumers are fully able to comprehend the differing levels of protection offered or if at the time of purchase this would have particular importance for them. It is certain that the protection is valued when problems arise.

Unregulated will writers may have no insurance or compensation arrangements. Even if the consumers remembered who they instructed there will be no redress for the majority.

While there are voluntary bodies which unregulated providers can join, such as the Institute of Professional Will writers, the Society of Will Writers and the Society of Trust and Estates Practitioners. The number of different organisations for will writers makes it difficult for consumers to properly understand the level of protection, if any, that they are entitled to for the services they are receiving. In any event these organisations do not offer the same level of assurance as authorised providers operating under an established and scrutinised regulatory regime.<sup>55</sup>

In our view, consumers are not educated about the will writing market and are making uninformed decisions when selecting a will writer leaving them exposed without recourse to the full means of redress they assume they have. Consumers are at risk of having a will drafted by someone who does not understand the complex nature of will drafting (including trust structures and inheritance for example) and therefore drafts an invalid will or a will that does not accurately reflect or will be ineffective in implementing the testator's wishes. A 2015 YouGov survey of wills and probate consumers provides useful insights into this point.<sup>56</sup>

During the passage of the Legal Services Bill, the Joint Committee recommended that will writing be included in the list of reserved activities.<sup>57</sup> This was rejected by the government and the question transferred to the LSB to consider further.<sup>58</sup> The CMA will be aware that in May 2013 the government rejected the LSB's recommendation that will-writing activities should be made subject to regulation. The LSB's recommendations, made in February that year, concluded a two year investigation under section 24 of the Legal Services Act 2007 which, in the LSB's words, 'found comprehensive evidence that the market is working contrary to the interests of consumers who use these critical services.'

In his decision, the then Lord Chancellor agreed that the unregulated will writing sector was causing detriment to consumers and recognised that making will writing a reserved activity might redress this. However, he concluded that there was not enough evidence to demonstrate that this was the best solution and so recommended that alternatives to more regulation be explored.

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<sup>55</sup> The Institute of Professional Will writers has a Code of Practice which is approved by the Trading Standards Institute under its Consumer Codes Approval Scheme; the Society of Will Writers has a Code of Practice, a Client Charter and a requirement for members to hold professional indemnity insurance; and the Society of Trust and Estates Practitioners (STEP) has a set of ethical and professional standards and a Code for will preparation in England and Wales established following the government's call for professional bodies to develop their own codes for will writing.

<sup>56</sup> We subscribe to YouGov's legal channel. Use and reporting is restricted and we have not had time to clear quotes and summaries with YouGov for this submission.

<sup>57</sup> Joint Committee on the Draft Legal Services Bill, session 2005-06, Draft Legal Services Bill, 25 July 2006, paragraph 216.

<sup>58</sup> Government Response to the Report by the Joint Committee on the Draft Legal Services Bill, 25 September 2006, page 17.

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During this period the Society outlined its concerns with the unregulated will writing sector and provided case study examples in responses to the LSCP and LSB's call for evidence into this issue.<sup>59</sup>

## **2 Employment law services to individuals and small businesses**

The Society agrees with the CMA that employment law services is an appropriate candidate for a case study. Focussing on employment law services should afford the CMA insight into an important hybrid market which both consumers and SMEs need to access. Employment law advice is typically needed:

- (a) on entering into an employment relationship, especially at the point that a SME becomes an employer for the first time;
- (b) on business acquisition, merger or disposal;
- (c) in dealing with employment-related disputes within the workplace; and
- (d) in dealing with employment-related disputes at the employment tribunal and through related settlement procedures.

The market for employment law services has undergone considerable change with increasing competition between solicitors, other lawyers, non-legal businesses, trade unions and professional associations, HR professionals and on-line resources. A YouGov report Employment Law 2016 provides useful insights into this market.<sup>60</sup>

In our view, there does not seem to be an unmet legal need in the area of legal advice prior to disputes arising, with there being a significant number of legal service providers available to consumers and businesses.

However, there are potential issues in consumer access to the Employment Tribunal, in which the government is an important market player. The current fees for the Employment Tribunal have caused a significant decrease in the number of cases going before the Tribunal, with a corresponding increase in employment law services businesses (which can be run by non-legal professionals) reported to us by our members. The total number of tribunal claims heard between April 2014 and March 2015 was 61,306, having fallen from 105,803 over the same period in 2013-14 and 191,541 in 2012-13, the last 12-month period before the introduction of tribunal fees in 2013.

The impact of fees has been the subject of parliamentary inquiries and litigation – so far up to the Court of Appeal and possibly to the Supreme Court – and a government review was expected to be published by the end of 2015 but is still awaited. Claimants who have to find the money for tribunal fees have correspondingly less money available to seek legal advice. Where cases do go to the Tribunal, claimants are increasingly representing

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<sup>59</sup> Please see The Law Society responses to the: (i) LSCP's call for evidence for its investigation into will writing - December 2010; (ii) LSCP's call for further evidence for its investigation into will writing - January 2011; (iii) LSB's call for evidence on an investigation into will writing, probate and estate administration - November 2011; (iv) LSB's consultation on will writing, probate and estate administration activities - July 2012; and (v) LSB's second consultation on will writing, probate and estate administration activities - November 2012. Our position on the issues concerned remains the same and so we attach these responses to this submission for the CMA's reference.

<sup>60</sup> We subscribe to YouGov's legal channel. Use and reporting is restricted and we have not had time to clear quotes and summaries with YouGov for this submission

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themselves while, for some time, trade union officials have been representing claimants and human resources (HR) professionals representing businesses.

The Society has made various submissions on the impact of tribunal fees which can be accessed online.<sup>61</sup>

It is unusual for Claimants to pay a fixed fee for representation at a Tribunal. As representation at Tribunal did not fall within litigation it was possible to offer contingency fees to Claimants. Contingency fees enable impecunious Claimants to have representation on the basis that their representative was paid a percentage of any award made. The introduction of Damaged Based Agreements (DBAs) limited the agreements that solicitors could enter into have been available for some years. The availability of DBAs was widened more generally by the civil justice reforms following the Jackson review for use in civil claims (except for family matters). There has however been low take up of such funding arrangements due to, for example, the complexity of the associated regulations. The cap for fees in employment is 35% inc VAT. The cap was brought in just before the increase in VAT from 17.5% to 20% therefore virtually wiping out any profit. This operates to militate against their wider use, particularly given the relatively low level of employment tribunal awards (the median award for unfair dismissal in 2014-15 was £6,995 and the average £12,362).<sup>62</sup> This issue has recently been reviewed by the Civil Justice Council but MoJ action on this report is awaited.<sup>63</sup> Given that the rationale behind such agreements is to promote more effective access to justice (and thus deal with unmet legal need) this may be an additional area that the CMA wishes to consider in the context of cases wider than just employment matters, bearing in mind that non-lawyers are not bound by DBAs.

### **3 Do you agree with the scope of our case study on commercial law services?**

The Society notes that the scope of the proposed case study appears limited to covering trading issues including advice relating to commercial contracts. It is not therefore clear if the case study will focus on these types of trading issues exclusively or take a wider view of commercial law including, for example, aspects of intellectual property and banking law. Clarification of this scope would be helpful. It would also be helpful if the study could specifically consider the scope for legal advice to start up businesses. The Society also believes that a distinction needs to be made between start ups who have often have little capital and limited understanding of the legal services it requires and the more established better financed and experienced small businesses that are well able to select between a range of available advice from banks, accountants, insurers and solicitors, business support networks and government information sites.

The general area of unmet legal need in relation to small businesses was evaluated recently by the LSB in its report on SME's unmet legal need (published in October 2015).<sup>64</sup> While the LSB studied the position in relation to small businesses defined as those employing up to 50 people (and the Market Study focuses on those with ten or fewer) there are likely to be some relevant conclusions. The LSB also noted that this was an area that has previously received little research or investigation.

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<sup>61</sup> <http://www.lawsociety.org.uk/policy-campaigns/consultation-responses/letter-to-the-ministry-of-justice-employment-tribunal-fees-review-team/>

<sup>62</sup> Employment Tribunal award statistics 2014-15, MoJ.

<sup>63</sup> See <https://www.judiciary.gov.uk/announcements/damages-based-agreements-dbas-publication-of-cjc-recommendations/>

<sup>64</sup> LSB, *The legal needs of small businesses* (October 2015).

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The LSB study found that, since their previous survey in 2013: business problems have declined in incidence but remain costly; total annual losses were extrapolated to suggest that the cost to small businesses due to legal problems is £9.79bn; and engagement with legal service providers is limited.

The study found that the number of legal problems faced by small businesses had reduced significantly during the two year period reflecting better trading conditions.as the recession receded. It should also be noted that the sample was re-interviewed and therefore presumably their experience had increased. The most common problems related to trading, employment and taxation. Other businesses were the main source of problems and larger small businesses, and small businesses with BME and disabled business owners-managers, were most likely to experience problems.

The LSB's survey indicates that many small businesses turn to a range of advisors to address legal problems; these include regulated and unregulated legal advisors as well as accountants and financial advisors.<sup>65</sup> The Society would therefore invite the CMA to reflect this in the case study.

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<sup>65</sup> Ibid., p. 54.

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## **ANNEX 2: Imminent regulatory and other environmental changes affecting the profession and the market**

### **Financial protections**

- 1.1 SRA's reform agenda for 'protecting clients' financial interests: the SRA will launch a consultation on proposed reforms to professional indemnity insurance and Compensation Fund arrangements in autumn 2016, with the intention of changes being implemented in autumn 2018 at the earliest.
- 1.2 Insurance Act: the SRA plans to consult during February 2016 on limited changes to the professional indemnity insurance minimum terms and conditions (MTC) with effect from 12 August 2016, consequential on the Insurance Act 2015 coming into effect on the same day.

### **SRA Handbook**

- 1.3 The SRA is undertaking a wholesale revision of the Handbook that will simplify the existing rules and further the SRA's outcomes-focussed approach. The SRA will consult on amendments to:
- (a) The Code of Conduct, Principles and Practice Framework Rules (expected April/May 2016);
  - (b) SRA Accounts Rules (expected April/May 2016);
  - (c) Regulatory Arrangements (Consumer Credit) Rules [2015] (expected 1 April 2016);
  - (d) Code of conduct, principles and regulation framework for organisations (executed Spring 2016; earliest anticipated implementation date Spring 2017); and
  - (e) Remaining Handbook content, including Discipline and Costs Recovery Rules (no date yet specified).

### **Education & Training**

- 1.4 Competence Statement for Solicitors: on 1 April 2015 the SRA published this document, which defines the continuing competences that it requires from all solicitors. This will also be the standard for entry to the profession. It comprises three parts: a statement of solicitor competence, the threshold standard and a statement of legal knowledge.
- 1.5 CPD: on 1 April 2015 the SRA launched a new system of CPD, which they are calling Continuing Competence. Solicitors have until 1 November 2016 to move to the new system. There will no longer be a requirement for a certain number of hours, nor for courses or any specific type of CPD activity. Solicitors must instead consider how best to address their learning needs to maintain their competence.
- 1.6 Solicitors Qualifying Examination (SQE): The SRA is proposing to introduce a new series of centralised assessments, of knowledge and skills to assess the competence of entrants to the profession, in line with the Competence Statement for Solicitors. In its current form this would mean no regulated pathways to entry, or requirements such as the law degree, Legal Practice Course or period of recognised training, which would have a huge impact on those entering the profession, employers and the international reputation of the profession as a whole. The current consultation ends on 4 March 2016, with others planned on further details. Implementation is currently slated for September 2018, although indications are that this may be pushed back to September 2019.

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### **Client information**

- 1.7 The LSB is to release a consultation (expected at the end of February 2016) on what information legal services regulators should be telling lawyers to provide to clients.
- 1.8 The SRA has also indicated that it intends to consult on solicitors' fees and charging structures.
- 1.9 From 15 February 2016, solicitors who are 'online traders' will be required to provide a web link to European Commission's online dispute resolution (ODR) portal as well as the trader's email address. This is a requirement of the EU Regulation on Consumer ODR and the Governments Alternative Dispute Resolution for Consumer Disputes regulations 2015.

### **Practising fees**

- 1.10 The LSB is expected to release a consultation on the rules relating to practising fees, including the practising certificate fee approval process and regulators' treatment of any underspend of the practising certificate fee.

### **FCA senior managers regime**

- 1.11 The FCA is expected to consult on whether in-house solicitors working for banks, building societies and credit unions who have 'overall responsibility' for the organisation's legal function, should fall within the FCA's senior managers regime, and hence require FCA approval to carry out that role.

### **Legal Ombudsman Scheme Rules changes**

- 1.12 The Legal Ombudsman is expected to review its Scheme Rules in 2016.
- 1.13 There is also a possibility that the Legal Ombudsman will submit an application to the Legal Services Board to become an approved alternative dispute resolution (**ADR**) mechanism for the purposes of the EU Directive on Consumer ADR. This would require further changes in the Legal Ombudsman's Scheme Rules and would require solicitors to change the information that they provide to clients.

### **Misconduct and enforcement**

- 1.14 In summer 2016, the SRA plans to release a policy statement following its 'A Question of Trust' consultation, and a framework assessing the relative seriousness of solicitors' actions.

### **Regulatory Independence**

- 1.15 The Ministry of Justice plans to consult in Spring 2016 on removing barriers to entry for alternative business models in legal services, and on making legal service regulators independent from their representative bodies.

### **Legal Services Board plans**

- 1.16 The LSB's draft 2016-17 business plan indicates that it intends to undertake work in the following areas:
- (a) development of a risk-based rationale for regulation;

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- (b) analysis of investment in the legal sector: identifying current sources of capital and establishing how the investor community views the market and any barriers to investment;
  - (c) work with market intermediaries to understand whether there are barriers, regulatory or otherwise, preventing them from entering the legal services sector;
  - (d) review of transitional protections for special bodies;
  - (e) exploration of measures to enhance consumer protection for those using unregulated providers;
  - (f) trading behaviour risks in the legal services market (quality and misuse of personal information in a context of growing use of technology based DIY legal services);
  - (g) consumer vulnerability (identification of areas of highest risk and responding to consumer vulnerability);
  - (h) increasing diversity: explore whether need to focus on particular aspects of regulatory policy e.g. education and training, which could deliver progress in this area; and
  - (i) identifying the benefits/risks associated with regulatory choice i.e. switching regulator (with reference to differences in regulation e.g. entry to regulation, compliance activities and exit from the regulated market).

**Introduction of fixed costs in 'low-value' clinical negligence actions** This is expected in late February.

**Abolition of minor damages for whiplash**

This is expected in late March.

**Raising of the small claims limit for personal injury to £5000**

This is expected in late March.

**EU referendum**

Once the date of a referendum on the UK's membership of the EU is confirmed, there will begin a period of uncertainty that will impact on a number of business sectors, including the legal sector.

If the referendum were to result in a decision to leave the EU, the impact on the legal sector would be far-reaching. There would be a further period of business uncertainty as the terms of withdrawal and of a new relationship with the EU and third parties are negotiated.

The effect on law firms will ultimately depend upon the impact on their client base. Some firms' clients or local economy would be directly affected by a change in the UK's relationship with the EU: the EU is of particular importance to firms who work with the financial services sector, for example. For others, the impact would be less important than general economic conditions such as interest rates, the strength of the property market and economic growth.

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## **Rechtwijzer**

Introduction of on-line mediation in family disputes.

## **Advocacy standards and regulation**

Change anticipated: the government is taking a close interest in this area.

## **Declining volumes of litigation**

This is occurring for a variety of reasons and can be seen most significantly in crime, in the Employment Tribunal, and, possibly, in family and civil cases (certainly, in family disputes, in a reduction in parties being represented by lawyers in). This decline in work is having a major impact on the high street end of the profession.

## **Legal Aid**

The legal aid market remains hugely challenging. On the civil and family side, legal aid has been removed for a substantial proportion of cases. This causes problems on two levels. First, the rates for legal aid work are lower than ever. Secondly, the cuts mean that there is less legal aid work to do, making it ever less worthwhile for firms to incur the fixed costs of maintaining a legal aid contract. On the criminal side, the uncertainty of the past few years has been deeply damaging. The recent decision to abandon “two tier contracts” and to suspend the second of the two recent fee cuts for 12 months has provided some much needed respite, but firms in this sector have little confidence as to what the future might hold. The position is made worse by the threat of further changes such as court closures, additional regulation of advocacy, and the investment required by the digitisation of the courts.

## **Civil Courts Structure Review**

Lord Justice Briggs’ Civil Courts Structure Review final report is due by the end of July 2016.

## **Tribunals review**

There is a Senior President of Tribunals forthcoming review of the tribunal jurisdiction (timetable to be confirmed).



The Law Society

# *A theoretical framework for assessing the value of legal services*

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# Introduction

# The value of legal services derives, ultimately, from the effectiveness of the rule of law, which rests on a holistic definition of legal services

- One of Nobel Prize winner, Douglas North's, key conclusions was that societies can sometimes be locked into poverty and low growth equilibrium due to dysfunctional institutions, such as an absence of the rule of law and an independent high quality judicial system that enforces property rights and contracts. A state's comparative advantage in coercion, and geographic monopoly over coercive power, enables the state to create value by enforcing rule of law and individual rights.
- For the state to deliver on this opportunity, however, legal services need to be independent and of high quality and the concept of legal services needs to include the rules in play, the courts and judiciary as well as the lawyers who provide services. Without this combination of elements, and their quality and independence being assured, disputes will tend to be resolved by 'might-makes-right', or by letting losses stay where they lie. Independent, high quality legal services enable a state to commit credibly to the rule of law, and a just and efficient society.
- An independent judicial system that exercises exclusive control over the use of coercive powers within a nation, according to the rule of law, is an example of an inherently good monopoly. The courts ultimately need to be backed by the threat of coercion in order to ensure the final resolution of disputes. This control over the exercise of coercive powers is the essence of 'legal services', and the ultimate source of the ability of legal services to create value, protecting individual rights and efficient outcomes against abuse of power over time.
- This is what makes legal services different to other markets. Exclusive control over coercion vested in legal services is productive, and is simply a function of the rule of law in operation. This a productive 'monopoly', and merely an adjunct of the state's monopoly over the use of coercive power. The rule of law remains only a concept unless there is an independent judiciary which controls legal services and delegates powers to lawyers acting as officers of the court, who in turn have professional duties to uphold the system of administrative justice and respect client privilege.
- These complementary inputs together serve to manage and exercise the state's authority over the legal use of coercion in a society on a rational, efficient and just basis. This produces sanctioned legal rights and legal obligations that can change economic incentives and improve economic and social outcomes, usually without the need to use the courts' services.

## **Legal Services versus Lawyers' Services**

Legal services is a broader concept than lawyers' services. As discussed in **Annex A** legal services is an output, while lawyers services are just one among other inputs to legal services. Annex A outlines a model of the production of legal services and how it involves a combination of inputs including legal rules, and the services of the judiciary, and lawyers as officers of the courts. This basic idea of legal services creating final value is further captured in simple economic models in **Annexes B and C**.

# Effective rule of law requires exclusive exercise of the state's coercive power by an independent, high quality judiciary and legal profession. This delivers value beyond the immediate private benefits to purchasers

- The economic value which is created by lawyers' services can, theoretically, have three components:
  - The fee income, or the market price paid, multiplied by the volume sold, which is their market value;
  - Private 'surplus' value, which is the value experienced by purchasers over and above price; and
  - 'Social' value, which is the value from any public good, or external benefits derived by non-purchasers as well as purchasers, such as the deterrence value of law.
- Independent, high quality legal services (including lawyers' services) provide value to society over and above their direct contributions to GDP by promoting economic efficiency and reducing risk through the delivery of the rule of law.
- The real value of legal services (including the rules, the courts and judiciary and the lawyers providing services) depends on the extent to which the courts and judiciary are charged with exclusive exercise of the state's coercive power (the ultimate sanctions available in a state), and the independence and quality of legal services.
- Quality and independence are necessary in order to avoid or mitigate error:
  - Independence from executive intervention and control safeguards neutrality, and reduces bias in legal services. This is an essential requirement for effective rule of law and, therefore, economic growth.
  - Quality reduces variance in outcomes, ensuring greater certainty, which is also an essential requirement for effective rule of law and, therefore, economic growth. Where quality is assured by judicially supervised minimum quality standards, there need not be caps on the number of lawyers (as is evident from the historical growth in the numbers of licensed lawyers).
- This article attempts to demonstrate, theoretically, the total economic and social value that legal services can provide beyond private exchange and how this depends on independent and high quality lawyer services. The main text summarises how legal services create value, and why the independence and quality of legal services matter. The annexes provide more detail on how economic value is created by legal services using existing economic models and theory.

How do legal services create value  
and why does independence and  
quality matter?

# Lawyers' services contribute social and economic value through four main mechanisms

The licensed lawyer, as an officer of the court, is a representative with delegated responsibilities from the judiciary in respect of the rule of law. Lawyers' services, in particular, not only enable people to rely on sanctioned rights by ultimately providing access to court services, but can also provide information about rights and the opportunities. The information lawyers make available to clients, whether business or households, about their rights can alone help to reduce both uncertainty and risk. Furthermore, lawyers' information gathering role (based on their education) can avoid the economic inefficiency of many individuals replicating this effort to find and process information about legal rules and their rights and obligations independently.

**Market or exchange effects**  
underpinned by services  
related to property and contract  
law

**Annex D**

**Social cost effects**  
underpinned by services  
related to tort law governing  
harm caused in non  
consensual interactions  
between strangers

**Annex F**

**Investment, innovation and  
risk effects**

underpinned by services  
related to property, contract,  
company and trust law

**Annex E**

**Government failure effects**  
underpinned by services  
relating to public law which  
help ensure that collective  
decision making rules are  
observed

**Annex G**

# Value created through market, investment, innovation and risk effects

**Market or exchange effects**  
underpinned by services  
related to property and contract  
law

**Annex D**

- Through having good quality rules relating to property rights as well as trained lawyers in place to enforce and pursue rights, value is created that is not readily perceived or measured.
- Property and contract legal services reduce transaction costs that would otherwise be incurred because of opportunism by parties to arrangements and the need to find information, thereby facilitating the formation and operation of markets.
- Lawyers enforcing exclusive rights, and triggering sanctions against stealing, thereby create incentives to:
  - invest in and produce goods in excess of personal requirements; and
  - market, and distribute and exchange the additional production.
- Contract legal services facilitate deferred exchange by enforcing promises to pay (e.g. borrowing from banks using collateral)
- The threat of escalating legal services to the courts deters inefficient behaviour and supports the creation of markets and value.

**Investment, innovation and  
risk effects**

underpinned by services  
related to property, contract,  
company and trust law

**Annex E**

- Legal services reduce the risk or variance of returns to investment due to misappropriation and encourage efficient investment as a result
- Property, contract, company, and trust legal services can create value by reducing risk or variance of returns to investment due to misappropriation, thereby increasing investment.
- Legal services not only reduce the downside risks individuals may face from theft, lying and cheating by others, but also limit the upside that individuals may be able to secure by themselves engaging in theft, lying and cheating.
- Annex E demonstrates that in a 'good' legal services environment (low risk legal services), the demand for capital, or what can be paid on a risk adjusted return basis is greater than in a poor (high risk) legal services environment at every level of supply. Economies with good legal services tend to attract more investment and tend to grow faster over time as a result.

# Value created through reducing social cost and government failure effects

**Social cost effects**  
underpinned by legal  
services related based on  
tort and criminal law which  
manage situations in which  
harm is caused in non  
consensual interactions  
between strangers

**Annex F**

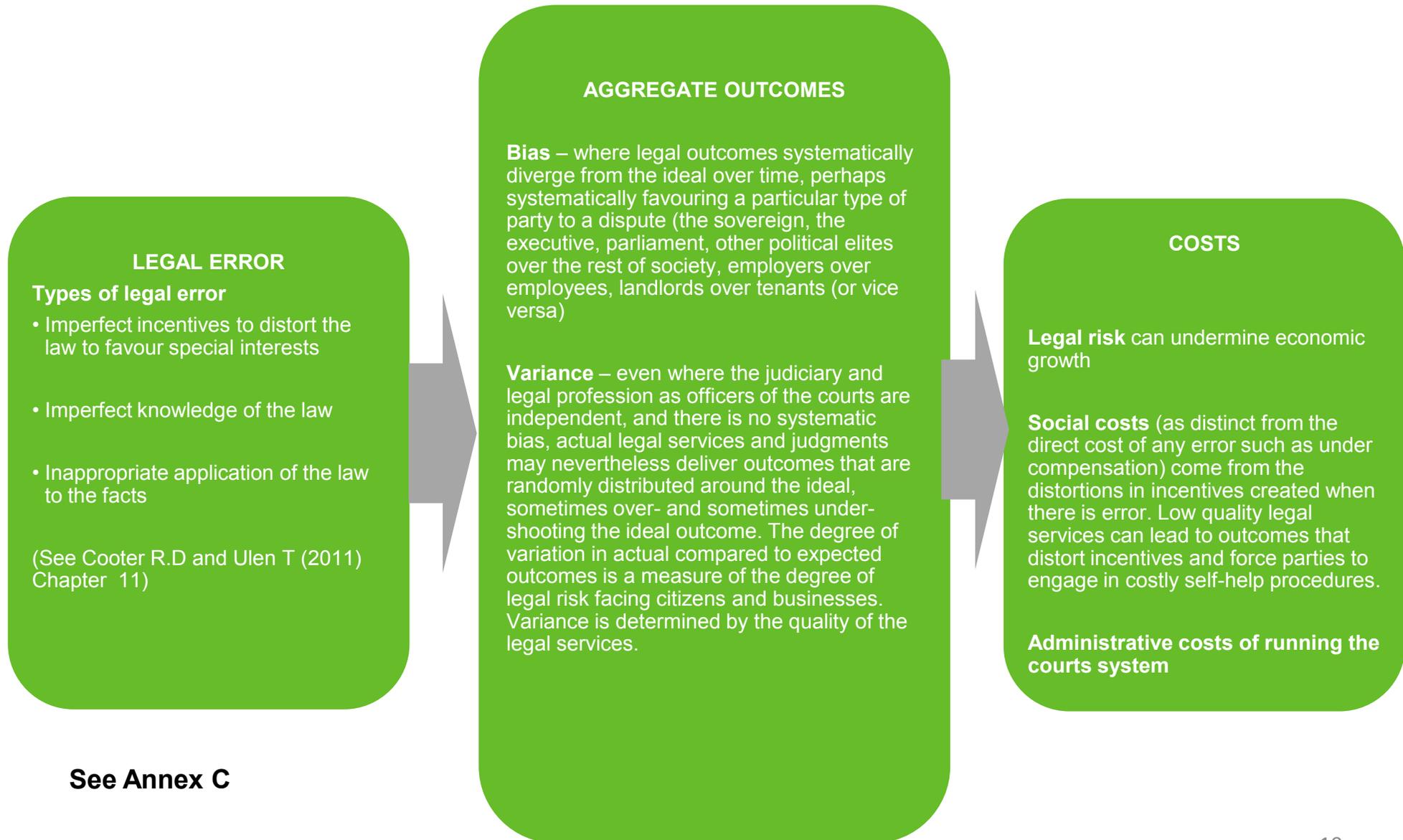
- Legal services create value by reducing the social cost of accidents. In the absence of high quality independent legal services, those who cause harm would not bear the full costs and would choose suboptimal levels of precaution, since precaution is costly.
- Legal services pursuing redress for harm from parties causing damage encourage better levels of precaution, because those in a position to cause harm must take account of the risk and consequences of liability for harm
- If those causing accidents which are capable of a claim in tort law become liable for expected harm up to the point at which they take optimal care, they are incentivised to adopt optimal solutions which minimise total social costs. The same is true for criminal legal services.
- This is otherwise known as deterrent value. Ultimately, value is created by reducing social costs (in the case of tort law, the total of the cost of accidents + prevention costs + administration costs)

**Government failure effects**  
underpinned by legal  
services relating to public law  
which help ensure that  
collective decision making  
rules are observed

**Annex G**

- In the absence of legal services enforcing constitutional and administrative law rules the problem is that those who can secure control of the state, or the favour of the state, can make decisions that benefit them at low cost, while not worrying how their decisions may impose external costs (e.g. taxes) on others. They potentially have incentives to minimise only their own decision costs, perhaps choosing not to consult, or consider others' well being.
- Legal services supporting public law rules can contribute to better outcomes by providing remedies for citizens to enforce collective decision making rules which limit the power of any political elite, for example, in relation to legislation affecting all and not just the elite.
- Legal services supporting constitutional and administrative law can thus not only create private value but also create a public good – that is, the rule of law, which is the pre-eminent public good
- An important condition for these benefits to work is the independence of the legal sector.

# Quality and independence of legal services address legal error that could otherwise result in social and administrative costs...



See Annex C

# ...Enhancing the independence and quality of legal services provides public benefits by lowering legal error and total administration costs

## THE PROBLEM: THE DRIVERS OF SOCIAL (AND OTHER) COSTS OF LEGAL ERROR

**Bias** results from legal services systematically favouring the interests of one type of party to a dispute over another – this is primarily due to lack of independence of legal services.

**Variance** is a measure of the degree of uncertainty or variation around any central tendency or legal risk facing citizens and businesses, which can undermine economic growth – this is primarily due to lack of quality of legal services.

## SOLUTION

**Bias** – requires the separation and independence of legal services supporting judicial power in a state from the control of the legislative and executive branches, to provide checks and balances against the abuse of power. Through an independent judiciary, the state is able to commit, credibly, to promoting social welfare and the public good.

**Variance** – high quality legal services deliver more certain, or low risk, legal outcomes.

**Annex E** demonstrates that the risk adjusted returns on all investment projects will be lower with low quality/high risk legal services, as a consequence, there will be lower investment and therefore lower economic growth with lower quality legal services.

**Annexes H and I** summarise Akerlof's market for lemons theory and Leland's modelling of that theory. It shows how low quality services can undermine value creation and how minimum quality licensing potentially supports the operation of markets, presenting a possible solution to the problem of asymmetric information in consumer markets.

Two aspect of quality are important: the need for high quality and the need for consistent quality.

## OUTCOME

**Economic growth and social and cultural development**

Although granting such independence to legal services and adopting minimum quality standards for lawyers may drive up per unit administrative costs, the point is that quality matters and it is not cheap.

**See Annex C**

# Standard economic theories applied to the legal services market often do not recognise legal services as being in the public good - that is their contribution to society beyond private exchange

- Standard supply and demand curve analysis commonly employed in the analysis of the UK legal services market does not capture the social value created by legal services through deterring inefficient behaviours or facilitating more efficient behaviours. Societal benefits enjoyed beyond direct purchasers (for example, lower theft rates) are, in economic terms, positive externalities. Legal services generate 'externalities', or a public good, because the benefits of legal services extend beyond the immediate relationship of exchange that generates direct economic value.
- The public good nature of legal services can also be considered in terms of avoiding the social costs or public 'bad' of inefficient or bad law. The nature and extent of these public benefits are determined by the degree of independence and quality of the legal services within a state.
- Supply and demand analysis can be adapted to capture the public good derived from legal services enforcing efficient laws showing, theoretically, the extent to which there may be under-provision of legal services (see Annex B). This, in turn, demonstrates the value of social benefits to be derived from increasing the output of legal services (see Annex A) and provides a rationale for subsidising legal services to expand legal services output and internalise the otherwise foregone social value. Annexes B and C further explore how the nature and extent of any public benefits from legal services are determined by the degree of independence and quality of the legal services within a jurisdiction.
- Standard economic models do not address, in any depth, how legal services create value, nor the nature of their fundamental institutional context. The standard approach assumes that legal services can be modelled like any other market where people exchange goods or services.
- While the recent narrative around regulation of legal services has focused on the public interest in consumer protection, too little regard has been paid to the public interest in the rule of law, and therefore the public value of legal services beyond private exchange. The rule of law depends critically on the independence, and the quality of the legal services. The adverse consequences for the public good of weakening the independence and quality of legal services are significant, but not well understood.
- The argument set out here is that, in order for the rule of law to operate effectively, it is necessary for there to be high quality independent legal services and for the judiciary to exercise exclusive control over the ultimate sanctions available within a state (effectively a monopoly over the state's coercive power). Taken together, the economic literature demonstrates that, without high quality independent control over the exercise of coercive power within a state, there is a risk of poorer economic outcomes. See for example North (1983) Acemoglu et al (2001), (2002), (2003), (2005) and (2012); Johnson, N.D. and Koyama, M. (2014), Rodrik, Subramanian, and Trebbi (2004).

# ANNEX A – The Economic Value of Legal Services

## Economic Modelling of Legal Services Value Contribution

Legal services is a broader concept than lawyers' services. Legal services output ( $q_l$ ), is an intangible output which creates final value ( $v$ ) through a monopoly over the ultimate sanctions available in a state held by the judiciary operating through the courts system and with the support of trained lawyers acting as officers of the court. This basic idea of legal services creating final value can be captured as follows

$$V(q_l, q_c)$$

Final value ( $V$ ) enjoyed by individuals is thus assumed to be a function of two outputs: first the output of legal services ( $q_l$ ); and, second, a composite good  $q_c$  which stands for all other goods.

Legal services output ( $q_l$ ) can then be expressed as a function of a number of key inputs as follows

$$q_l = f(R, C, L, \dots)$$

The listed complementary inputs used in producing legal services output include:

R = Legal rules defined by legislation, regulation and court precedent

C = Court services in which judges exercise the coercive power of the state, to develop, interpret and apply legal rules to cases

L = lawyers' services, involving officers of the courts, such as barristers and solicitors representing litigants in trial and co-ordinating a client's legal services

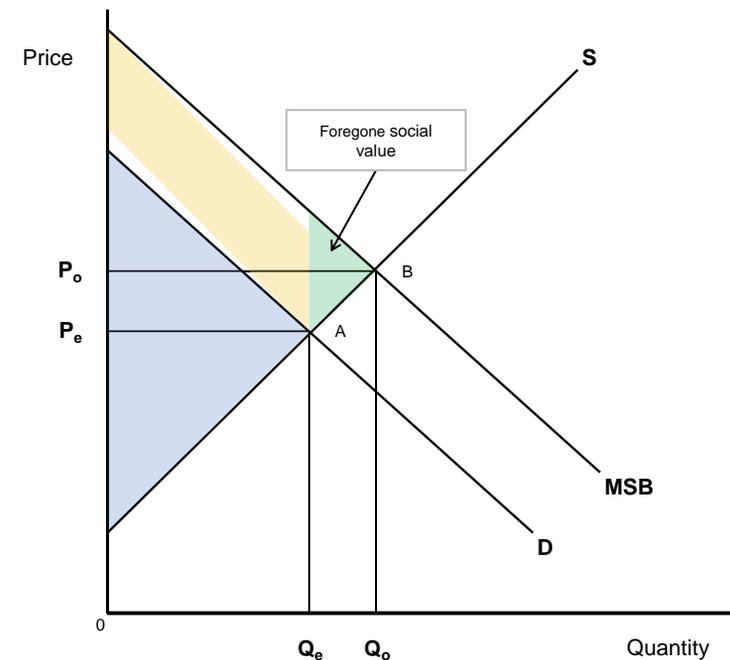
# ANNEX B – The social (public good) value and the risk of under provision of legal services

Any social benefit in addition to the private value of legal services can be represented by a simple amendment to standard demand and supply analysis. The social value of legal services is thus captured in Figure 1 opposite by adding the social value created at any level of consumption of legal services to the private demand curve (D). This generates the marginal social benefit (MSB) of legal services, or social demand curve for legal services, which lies above the private demand curve (D). Based on the arguments in the main text, the height of this MSB curve is driven by the independence and quality of legal services in a state. The greater the independence and quality of legal services in a state, the greater the MSB of legal services (see annex C for rationale)

At the private market equilibrium level of legal services  $Q_e$  (identified by standard analysis) the private surplus value associated with the output  $Q_e$  is shown by the blue shaded triangle. The social surplus value associated with the output  $Q_e$  is shown by the yellow shaded area. This area can be interpreted as the *public good* derived from private transactions in legal services enforcing 'efficient' laws. These social benefits however are not factored in to private decision making about legal services, nor are they measured by the market value of the transactions, which is the price  $P_e$  times total volume sold  $Q_e$  (ie the area in the box 0- $P_e$ -A- $Q_e$ ).

Figure 1 also identifies the extent to which there may be under-provision of legal services. The socially optimum level of legal services is  $Q_o$  shown at the intersection of the MSB curve and supply curve S. The private market equilibrium however is at  $Q_e$ . There may thus be social benefits from increasing the output of legal services from  $Q_e$  to  $Q_o$ , with the social benefit of such an increase measured by the green shaded triangle entitled **foregone social value**. This forgone public good benefit is often cited as the reason or economic rationale for subsidies to legal services that expand legal services output and internalise the otherwise forgone social value.

Figure 1



The private market equilibrium is A (ie quantity  $Q_e$  of legal services, and price  $P_e$ ). Whereas the socially optimum level of legal services is at B (ie quantity  $Q_o$ ).

This discussion of the public goods and positive externalities from legal services however could also be supplemented by factoring in any social costs, negative effects, or public bad arising from the enforcement of inefficient or bad law. Such social costs appear more likely to occur if laws are introduced that reduce the independence or reduce the quality of legal services. This could be shown in Figure 1 above by adding any social costs to the supply curve to include a marginal social costs curve (MSC) above the private supply curve at every level of legal services. This would imply a lower level of net social value from legal services at equilibrium, and a lower optimum level of output than shown above in Figure 1.

# ANNEX C – Entrusting the state's coercive powers to resolve disputes, to an independent judicial system run and supported by highly trained lawyers, can minimise the social costs of legal error

**The economic objective of the court system is to optimise social welfare or minimise overall social costs.**

As outlined in Cooter and Ulen (2011 Chapter 10) the ideal legal outcome or judgment ( $j^*$ ) in a particular case would be the outcome or judgment that optimises social welfare based on perfect knowledge of the facts and the most appropriate law. Legal error in a case then can be measured as  $e = |j^* - j|$ , where  $j^*$  is the optimum outcome and  $J$  the actual. (The absolute difference is used as an error can occur if an outcome ( $j$ ) is too high or too low).

In the absence of legal services, disputes will tend to be resolved by 'might-makes-right' or by letting losses stay where they lie, which can be a type of wrongly decided dispute. Imperfections in legal services supporting legal decision making by courts, due to incentives to distort the law to favour special interests, or imperfect knowledge of the law, and inappropriate application of the law to the facts can cause such legal error. The independence and quality of legal services in a society determine the nature and extent of error in final legal outcomes.

While the social cost of any legal decision is a function of legal error, a one-to-one correspondence rarely exists. Suppose, for example, a court awards a \$200 judgment when the perfect court would award \$300. The immediate legal error ( $e$ ) is a failure to transfer a further \$100, but this is not the social cost. Social costs come from the distortions in incentives created when a \$200 claim is awarded rather than the correct \$300 claim.. For example the higher award will offer greater deterrence of costly behaviour than the lower award.

This social cost function for a particular case can be written as  $c = c(e)$ . Another type of cost is the 'administrative cost' of running the court system, which is labelled AC.

**The economic objective of the court system is to minimise overall social costs:**

**Minimise SC =  $c(e)$  + AC** for each case

The total social costs of wrongly decided disputes arise from systematic **bias** and **variance** across cases as a whole.

**Systematic bias** occurs where actual legal outcomes ( $j$ ) systematically diverge from the ideal ( $j^*$ ) over time with legal services perhaps systematically favouring the interests of one party to a dispute – such as the executive or parliament, or other political elite, over the rest of society. Therefore  $j^* - J^e \neq 0$ , where  $J^e$  is the expected (or mean) outcome across cases as a whole.

**Variance in legal outcomes** occurs where actual legal outcomes ( $J$ ) vary around those expected ( $J^e$ ). This can occur even when the judiciary and the legal profession as officers of the courts of justice are independent, and there is no systematic bias in legal services. In which case the expected legal outcome ( $J^e$ ) equals the ideal legal outcome ( $j^*$ ) – ie  $J^e = j^*$ . Even with independent legal services actual legal services and judgments ( $J$ ) may nevertheless deliver outcomes that are randomly distributed around the expected ideal judgement, some times over-shooting, sometimes under-shooting the ideal outcome. The same is true without independence of legal services. Also with biased legal services, where actual judgements  $J$  are expected to be biased (i.e.  $J^e$  does not equal  $J^*$ ) the actual outcome may vary around the now expected-biased outcome.

Entrusting the exercise of the state's monopoly over coercive powers to independent legal services (reducing bias) and good quality legal services (reducing variance) licensed by the judiciary can minimise both the costs of error ( $c(e)$ ), and also the administration costs (AC) in the judicial system.

# ANNEX D – Value created through market or exchange effects (property law)

The matrix in Table 1 below helps illustrate the value of property law legal services. It summarises a game with two *players* as shown in the top left cell (Angela and Barbara). As shown in the shaded first column, Angela can choose not to steal, or to steal. Similarly, Barbara can also choose not to steal, or to steal. The shaded “outer” column and row thus capture the available *actions* of each party, who are assumed to make a choice either not to steal, or to steal based on their “*payoffs*” from each action. In the absence of legal services the pay offs to the parties, where both parties do not steal is shown in the cell in the second row, and second column, by the co-ordinates (10,9), where Angela is assumed to derive value, or a payoff of 10 units from the enjoyment of their property, while Barbara is assumed to enjoy 9. This results in combined value, or welfare, of 19 units (10 + 9) where both parties do not steal.

**Table 1: Stealing as a Prisoners Dilemma Game**

	<u>Barbara</u>		
<u>Angela</u>		Does not Steal	Steals
Does not Steal		(10, 9)	(7, 11)
Steals		(12, 6)	(9, 8)

- If Angela does not steal (as shown in the second row), but Barbara does steal (as shown in the last column), the payoffs to the players are shown by the co-ordinates (7,11), in the cell in the second row, and third column. Angela’s payoff is assumed to fall to 7 from 10, because she is not only assumed to “lose” 2 units which are stolen by Barbara, but also because she spends 1 unit of resources on trying to prevent greater theft. The payoff to Barbara on the other hand is assumed to rise to 11 from 9, because she succeeds in stealing 2.
- If Angela now steals in row 3, and Barbara does not steal (as shown in the second column), the payoffs are represented by the co-ordinates (12,6), in the cell in the third row, and second column. The payoff to Angela increases to 12 from 10, because she steals 2, and the payoff to Barbara falls from 9 to 6, because she is assumed not only to “lose” the 2 units which are stolen by Angela, but also because she spends 1 unit of resources on trying to prevent greater theft.
- The problem in the situation modeled so far is that each party realizes that if they steal and the other does not they can be better off, as shown in the cell in the second row, and third column (7, 11), and in the third row, and second column (12, 6) - although in each case total welfare is reduced to 18 from 19 (second row second column). Choosing to steal thus becomes the dominant strategy and leads *both* of the parties to independently choose stealing from each other, and both having to take preventative measures, and results in the equilibrium outcome in the bottom right or southeast corner with even lower total welfare of 17 units (9 + 8).
- Legal services supporting property law however can impose a sanction on people caught stealing and change the payoffs from stealing shown in the above matrix. This can turn the above non-co-operative outcome above into a co-operative one where society is better off. This involves choosing to change the rules of the game. For example if the *expected* sanction for stealing is -4 then this would change incentives and there would be no incentive to steal as any expected gain of 2 would be offset by the sanction -4. This would deter stealing and encourage respect for the property rights of others. The parties then enjoy greater total welfare of 19 in the top left corner (10 + 9) rather than the 17 in the lower right corner (9 + 8). This implies legal services supporting property law can potentially create value of 2 units, which is the difference in total welfare between the top left and lower right cells - nearly a 12% increase in value in this numeric example.
- This value creation effect of legal services is not readily perceived, nor measured, and may be taken for granted because it tends to be invisible, arising from the deterrence effect of intangible legal services. This is an effect of having good quality rules and as well as the lawyers in place to enforce and pursue them.

# ANNEX D continued –Value created through market or exchange effects (contract law)

Table 2 opposite demonstrates how value may be created by exchange of property rights supported by the use of *contract law legal services*. It shows the outcome of a deferred exchange in which Bob sells his car to Adam, relying on Adam’s promise to pay later once Adam receives an inheritance.

- In the initial position shown in column 1, row 1 Bob owns a car, which he values at £3,000,
- In the initial position shown in column 1, row 4 Adam is also assumed to be entitled to an inheritance worth £5,000, which we assume is soon to be paid out when he reaches 21.
- In the initial position then, given Bob values his car at £3,000 and Adam values his inheritance at £5,000 there is a combined or total value of £8,000 (3,000+5,000) as shown in column 1, row 5.
- In the “sold” column (2), if Bob sold the car to Adam it is assumed that the car’s value to Adam would be £4,000 (column 2, row 3). This is more than Bob values the car, which was £3,000 (in column 1, row 1).
- Adam could thus buy the car from Bob promising to pay Bob £3,500. If this transaction went ahead then Bob would have the price paid by Adam of £3,500 (column 2, row 2). Adam would therefore enjoy the £4,000 in value from the car (column 2, row 3), plus the remaining value of his inheritance after paying Bob the price of £3,500, being 1,500.

Thus, summing Adam and Bob’s values in the sold column( 2), the combined or total value increases to £9,000 (= 3,500 + 4,000 + 1,500) from £8,000 as shown in the last row in table 2 opposite.

As outlined in the last slide, legal services related to *property law* can deter theft and support the exclusive rights of Bob to the car originally, so Adam cannot just steal the car without the prospect of legal sanction. Even with property law legal services deterring theft however, there is still the problem of deferred exchange, which legal services supporting *contract law* can overcome.

**Table 2**

	Column 1	Column 2
	Initial Position	“Sold”
Row 1	Car Value to Bob	3,000
Row 2	Price Paid by Adam	-
Row 3	Cars Value to Adam	4,000
Row 4	Adam’s Inheritance	5,000
Row 5	Joint Value/Wealth	8,000
		9,000

Legal services related to *contract law* can facilitate deferred exchange for example by enforcing *promises to pay*. Thus for example legal services may be used to enforce a promise made by Adam to pay from his inheritance which he expects to receive in the future, in exchange for the property right to the car now. Or Adam could borrow from his bank to pay Bob, promising to pay the bank back from his inheritance, perhaps using the security of his inheritance pay-out, or the car itself in exchange with the bank. Such deferred exchanges might not occur however without contract law legal services, and the additional value of 1,000 in the above example would not be created.

The numeric example above thus shows how legal services supporting property and contract law can create additional total value and enable the operation of markets. This value creation effect of legal services is again not readily perceived, nor measured, and may be taken for granted because it tends to be invisible

## ANNEX E – Value created through investment, innovation and risk effects

- It is possible to illustrate the effect of high versus low quality legal services. High quality or good legal services can be assumed to involve low risk, and lead to efficiently defined and enforced property rights, and contractual promises. Low quality legal services on the other hand are assumed to be high risk as they leave scope for socially inefficient behaviours such as stealing, lying and cheating, implying high risk, or high variance in returns to investment.
- Two tables (tables 3, and table 4 on the next page) below can be used to illustrate the impact of the quality of legal services on risk, assuming all other factors affecting risks to the expected return from an investment are known and stay constant.
- Table 3 opposite shows returns to an investment project worth £1bn when it is supported by high quality legal services which eliminate legal risk so there is *no risk* or no variance in expected returns to investment.
- Thus as shown in the second row of table 3, in the second column, there is a 100% probability that the return in each of the three years of the project will be the 100 million per annum as expected, and as shown in columns three to five of row two.
- This gives an expected return per annum of 10% (100m/1,000m) as shown in the last column, row two.
- Finally as shown in the final row in these circumstances risk as measured by the standard deviation of expected return in each year overall is 0%

**Table 3 – High Quality Legal Services and Project Risk**

Type of return	Probability	Year			Expected Return p/a
		1	2	3	
Normal Return	100%	100	100	100	10%
Risk = Standard Deviation of expected return					0%

## ANNEX E continued – Value created through investment, innovation and risk effects

- Table 4 below however illustrates outcomes under low quality or poor legal services. As now shown in column 2 we assume with poor legal services there are three types of return or possible scenarios, with different expected outcomes as shown in the rows 2 to 4 of the table, being:
  - the 'normal return'*, now occurring with an 80% probability as shown in column 2, but as before providing 100 million a year over three years, and giving a 10% expected return p/a on the invested 1 billion, as shown in the final column of row 2.
  - an *advantageous return* shown in row 3 with a 10% probability, as indicated in column 2, where the return secured by the project manager lying, cheating and stealing off others increases to 310 million a year, giving a 31% expected return p/a., as shown in the last column
  - a *disappointing return* shown in row 3 with a 10% probability, as indicated in column 2, where the return falls to negative due to the project manager suffering losses owing to the lying cheating and stealing by others. and investors incur a loss of 110 million in each year, giving a -11% expected return p/a, as shown in the last column of row 4.
- The second to last row of table 4 below shows the weighted average expected return across the above three scenarios in each year is 100 in the poor legal services environment. This weighted average of 100 units per year across the three scenarios in each year, implies an average 10% rate of return p/a, as shown in the final column of the second to last row.

**Table 4 – Low Quality Legal Services and High Project Risk**

Type of return	Probability	Year			Expected Return p/a
		1	2	3	
Normal return	80%	100	100	100	10%
Advantageous	10%	310	310	310	31%
Disappointing	10%	-110	-110	-110	-11%
Average		100	100	100	10%
Risk = Standard Deviation of expected return					9%

- Table Two thus captures a situation where an investment project has the same 10% expected return with poor legal services as the earlier project did with good legal services.
- The problem however is that under the poorer legal services as shown in table 2, while one might expect to make the same 10% return on average, there is greater risk.
- In particular with the poorer legal services there is the chance the project will lose 110 million every year - for a total loss of 330 million over three years.
- Once again the level of risk associated with the legal services can be measured by the standard deviation of the expected annual rate of return from investments they support as demonstrated on the next page. Thus in the example in table 3 on the last page, risk when measured by the standard deviation of the expected annual rate of return is 0%, as shown in the final row of the table 3. By comparison the risk in the example in table 4 above when measured by the standard deviation of the expected annual rate of return is much higher at 9% as shown in the last row of table 4 above - implying higher risk in the latter case under poorer legal services.

## ANNEX E continued – Lawyers’ value – investment and risk effects

In the above examples we measured risk as the standard deviation of the expected annual rate of return. Formally this is measured as:

$$\sqrt{E(R^2) - \{E(R)\}^2}$$

Where

R is the average annual return; and

E(R ) is expected return per annum, the symbol E denoting expected value.

Applying the above formulae to the data in row 2 of table 3,

$$\{E(R)\}^2 = 0.01, \text{ given } E(R) = 10\% = 0.10.$$

To obtain  $E(R^2)$  one must weight the squared returns for each of the expected scenarios. In table 1 there is only one scenario shown in row 2 so

$$E(R^2) = 1 * (0.1)^2 = 0.01.$$

Thus risk is measured as:

$$\sqrt{E(R^2) - \{E(R)\}^2} = \sqrt{[0.01 - 0.01]} = 0$$

that is, there is zero risk with the legal services assumed in row 2 of table 4.

Applying the formulae to table 4

$$E(R) = 10\% = 0.10 \text{ again so } \{E(R)\}^2 = 0.01$$

the same as in the zero risk legal services in table 1. In table 2 however there are three expected scenario presented, so, weighting the squared returns for each scenario gives:

$$E(R^2) = 0.8 * (0.1)^2 + 0.1 * (0.31)^2 + (0.1) * (-0.11)^2 = 0.01882$$

Thus risk is measured as:

$$\sqrt{E(R^2) - \{E(R)\}^2} = \sqrt{[0.01882 - 0.01]} = 0.09315 \approx 9.3\%$$

Thus even though there may be the same expected return, there is greater risk (9.3%) with the lower quality legal services associated with table 4, compared to the zero risk associated with the higher quality legal services in table 3.

## ANNEX E continued – Lawyers’ value - investment, innovation and risk effects

Figure 2 opposite shows the likely economy wide investment effects of poor legal services implied by the above analysis. In figure 2 we show the *risk adjusted return* and costs of capital or investment ( $R$ ) on the vertical axis, and the amount of investment capital ( $K$ ) supplied and demanded on the horizontal.

The supply of capital ( $S_K$ ) is shown as upward sloping from the origin, reflecting the increasing opportunity cost of capital as more is supplied.

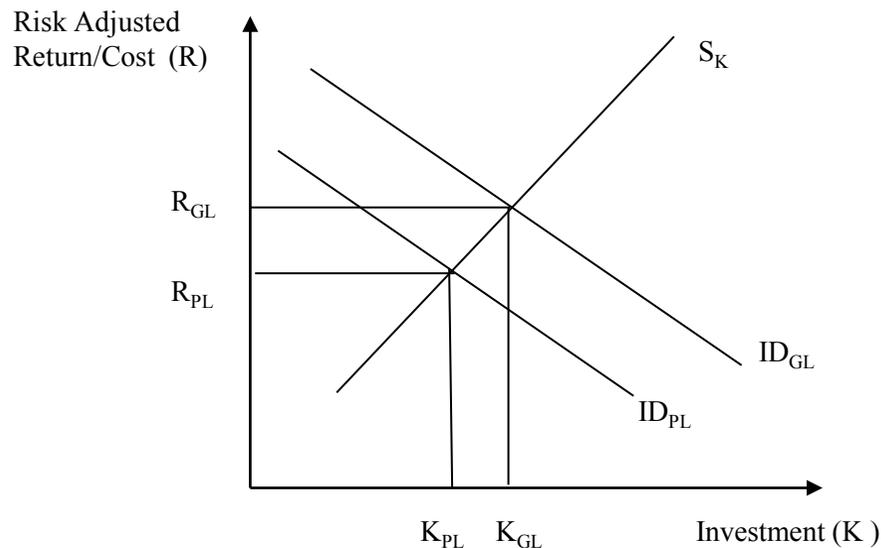
The demand for investment capital ( $ID$ ), is the expected return on a risk adjusted return basis, or what can be paid on a risk adjusted return basis. Demand ( $ID$ ) is shown as downward sloping, reflecting diminishing returns to investment. As shown in Figure 2 with a good legal services ( $GL$ ) environment, (or low risk legal services), the demand for capital ( $ID_{GL}$ ), or what can be paid on a risk adjusted return basis is greater than with poor legal services ( $ID_{PL}$ ) or with high risk legal services - at every level of supply ( $K$ ).

With both good (low risk) legal services and poor (high risk) legal services, the capital market will come to equilibrium where demand ( $ID$ ) equals supply ( $S_K$ ) as follows:

- with good legal services ( $GL$ ) equilibrium is shown at the intersection of  $ID_{GL}$  and  $S_K$  where risk adjusted return to investment is  $R_{GL}$  and the level of investment capital supplied is  $K_{GL}$
- with poor legal services ( $PL$ ) (or high risk legal services) equilibrium is shown at the intersection of  $ID_{PL}$  and  $S_K$  where risk adjusted returns is  $R_{PL}$  and investment capital supplied is  $K_{PL}$

With poor legal services ( $PL$ ) both risk adjusted returns ( $R_{PL}$ ) and investment capital supplied ( $K_{PL}$ ) are lower in equilibrium, due to the higher risk of the legal environment, than in a good legal service environment, where higher risk adjusted returns ( $R_{GL}$ ), and higher levels of investment ( $K_{GL}$ ) are achieved. The economy with good legal services will therefore have more investment and tend to grow faster over time as a result.

**Figure 2 Investment Effects**



# ANNEX F – Value created through reducing social cost effects

Legal services also create value by reducing the social costs of accidents. This can be illustrated using simple algebra to define the expected social costs (SC) of accidents as follows:

$$SC = w.X + p(X). A$$

Where

SC = Expected Social Costs of Accidents

w = cost of precaution

X = level of precaution

p = Probability of Loss from accident (which is a function of precaution X)

A = Extent of loss from accident

The fundamental problem with accidents is that those who cause accidents usually do not bear their full costs (SC), thus they may choose a suboptimal level of precaution (X) as precaution is costly to them (w.X). Legal services affect outcomes by offering remedies to victims of accidents, for example in tort law, which shift the costs of accidents (p(X). A) from the victims back to those who cause accidents.

The scope for inefficiency is demonstrated in figure 3 to the right, based on the above model, where the level of precautions (X) taken by decision makers is measured on the horizontal axis from the origin, and costs on the vertical axis from the origin.

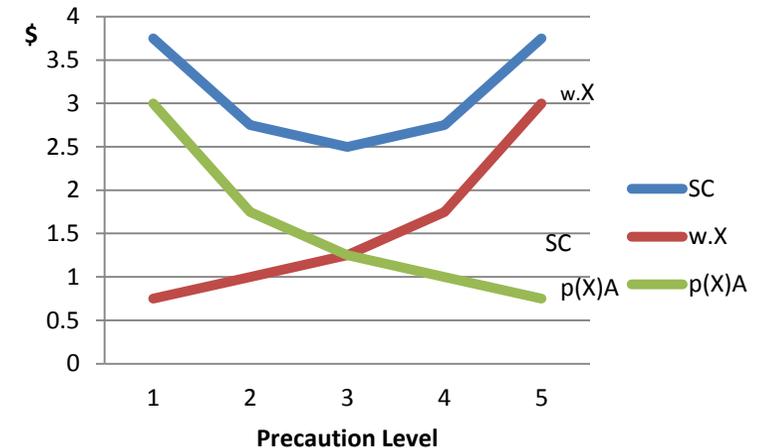
The upward sloping prevention costs curve (w.X) identifies that costs of precautions increase with the level of precaution.

The downward sloping accident costs curve (p.(X).A) identifies the expected costs of accidents falls with the level of precaution.

The expected social costs of accidents curve (SC) is the sum of precaution costs (w.X) and accident costs (p(X).A) at each level of precaution.

The optimal level of precaution in the example shown in Figure 3 is at level 3 where total or social costs are \$2.5.

Figure 3: Legal Services and Social Costs  
Social Costs of Accidents



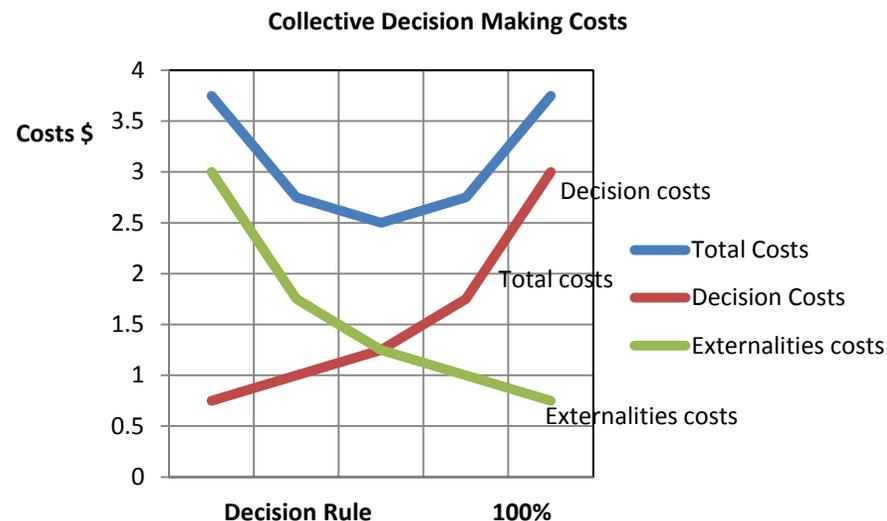
See Calabresi G. (1970) "The Costs of Accidents" Yale University Press

In the absence of legal services the problem is that those who cause accidents may only bear the cost of precaution (w.X) and therefore be concerned only with the curve (w.X), in Figure 3. They potentially therefore have incentives to minimise only precaution costs, perhaps choosing zero precaution, in which case the outcomes observed will be close to the origin, where social costs (SC) are not optimal, being too high. Legal services supporting tort law can contribute to better outcomes by providing remedies to victims. If those causing accidents thereby become liable for the expected harm they cause (p.(X).A) up to the point at which they take optimal care at precaution level 3, they will thereby become concerned not only with the curve w.X, in Figure 3 but also curve p.(X).A. They potentially then have incentives to minimise not only precaution costs, but total social costs (SC), and adopt precautions up to the optimal level 3.

# ANNEX G – Value created through reducing government failure effects

- Figure 4 to the right illustrates the value that can be created by legal services enforcing constitutional and administrative law rules that regulate collective decision making over matters that may affect a community.
- The horizontal axis measures the “decision rule”, which, in this instance, is the percentage of the population given a right to control a particular decision. At the right extreme we assume a 100% or unanimity decision rule holds, where everyone has a veto. Approaching the origin along the horizontal axis, decisions do not require unanimity, and can be made by an increasingly smaller group in the community - and at the extreme, only a small minority of the population, or an elite needs to be involved in the decision for it to be passed.
- The graph then shows how the level of *externalities costs* associated with any decision declines, or how externalities costs are gradually internalised, as the decision rule is increased from requiring only the support of a minority or elite, to requiring unanimity, or 100%, giving all members of the community a veto. At the same time the graph shows how *decision costs* associated with a decision will increase as the decision rule is increased from requiring only the support of a minority or elite, to unanimity, or 100%, - giving all members of the community a veto.
- The *total cost curve* includes the sum of both the externalities costs and decision costs at each decision rule. The total cost curve identifies where the optimal decision rule occurs, that is where total costs are minimised, or the total cost curve reaches its lowest, as the optimal decision rule is where the sum of decision and externality costs are lowest.

Figure 4: Public Law legal Services



(Buchanan and Tullock: 1958) - Chapter 6 Figure 1

- In the absence of legal services enforcing constitutional and administrative law rules the problem is that those who can secure control of the state can make decisions that benefit them at low cost, while not worrying how their decisions may impose external costs (e.g. taxes) on others. They potentially therefore have incentives to minimise only their own decision costs, perhaps choosing not to consult, or consider others well being. In which case the outcomes observed will be close to the origin, where total costs are not optimal, being too high. Legal services supporting public law rules can contribute to better outcomes by providing remedies for citizens to enforce collective decision making rules which limit the power of any political elite for example in relation to legislation affecting all and not just the elite.

# ANNEX H – How low quality legal services can drive out good quality legal services – Akerlof's market for lemons model

- Akerlof's 1971 market for lemons model can be used to explain how low quality or bad legal services will tend to drive out high quality or the good legal services in a market with asymmetric information, and thereby undermine the value creation identified in the main text.
- Suppose (for the sake of clarity rather than reality) that there are just two kinds of solicitors. There are good quality or good solicitors and low quality or bad solicitors (known as 'lemons'). While the good solicitor has higher value, s/he also has to invest and incur higher opportunity costs to be good. With full information, competitive market equilibrium s/he should command a higher market price than the lower quality/ lower cost solicitor.
- Assume that individuals in this market hire solicitors without knowing whether the solicitor they hire will be good or a lemon. However, they do know that, with probability  $q$ , it is a good solicitor and with probability  $(1-q)$  it is a lemon -  $q$  is the proportion of good solicitors and  $(1-q)$  is the proportion of lemons.
- An asymmetry in available information exists: for the sellers (solicitors) have more knowledge about the quality of a solicitor than the buyers, but good solicitors and bad solicitors must still sell at the same price. Since it is impossible for a buyer to tell the difference between a good solicitor and a bad solicitor. This means that the average price will reflect the proportion of bad solicitors.

- Akerlof's theory is that this low average price will drive out the good solicitors. This in turn will lower the proportion of good solicitors, and thus the average market price. Gresham's law where bad money drove out the good, makes a modified re-appearance. For most solicitors traded will be the 'lemons' and good solicitors may not be traded at all. The 'bad' solicitors tend to drive out the good.
- In 1979 Leland developed a model of asymmetric information that generated the Akerlof lemons result and showed that minimum quality constraints (or 'licensing requirements') may be a possible solution to the problem. Although not generally a first-best solution, such constraints will increase welfare in a number of cases.

*'Minimal quality standards (or licensing) will tend to be more advantageous in markets with: (a) greater sensitivity to quality variations ... (b) low elasticity of demand ... (c) low marginal cost of providing quality and ... (d) low value placed on low-quality service' (Leland p1336)*

As a corollary:

*'for markets with suitably low sensitivity to quality, high elasticity of demand, high marginal cost of quality, and/or relatively high value placed on low-quality service, minimal quality standards may not be desirable: .... However, even perfectly competitive markets .... can benefit from licensing if quality is sufficiently important to consumers, relative to its cost of provision...' (Leland p1336)*

- Figure 5, overleaf, shows, graphically, the theoretical maximum value that can be created by minimum quality standards.

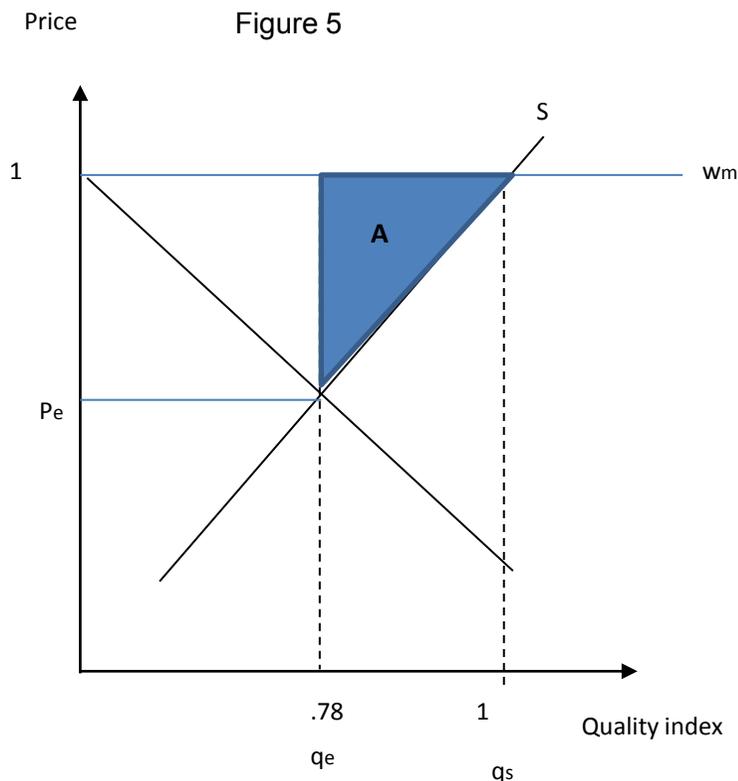
# ANNEX I – How minimum quality standards create value

Figure 5 is taken from Leland (1979) and is based on a specific numerical example.

- The horizontal axis from the origin in the graph measures  $q$ , which is an index of the quality of (legal) services. It can be interpreted as the percentile of potential supply, which has quality  $q$ , or less. Thus, average quality *declines* as  $q$  increases.
- The quantity and quality variables have been rescaled so that supply ( $q$ ) is uniformly distributed on the interval  $[0, 1]$ .
- The vertical axis from the origin in the graph measures price, and value, which is a function of quality  $q$ .
- The downward sloping demand curve ( $p$ ) shows that, with asymmetric information, as  $q$  increases average quality decreases, and so value and the market price consumers are willing to pay falls.
- The upward sloping supply curve ( $S$ ) shows the increasing opportunity cost of supplying a unit of service of quality level  $q$ .
- The horizontal line at the top of the diagram ( $w_m$ ) is the maximum price or value that could theoretically be achieved, or the welfare maximising value at which there would be no 'bad' legal services.
- With asymmetric information and an open market however, the market comes to a market equilibrium at quality  $q_e$  and price  $P_e$ , where the demand curve ( $p$ ) intersects the supply curve ( $S$ ).

The diagram thus illustrates the welfare (or value) loss as the difference in welfare at the market equilibrium  $q_e$  and at the welfare maximization outcome. Given the area under the horizontal blue line  $w_m$  is total available benefits, the net benefits that could be created by minimum licensing standard is the area under this blue line ( $w_m$ ), less the area under the supply curve ( $S$ ) up to the chosen level of  $q$ .

Given that welfare is maximized at  $q_s$ , the total additional value that can be created by minimum quality licensing then is measured by area A, which is the increase in benefits in going from the market equilibrium  $q_e$  with an open market, up to the point where welfare is maximized at  $q_s$ .



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# **Economic Research into Regulatory Restrictions in the Legal Profession**

A Report for the Office of Fair Trading by Europe  
Economics

January 2013

OFT1460

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# 1 EXECUTIVE SUMMARY

## **Key findings**

### **Regulation**

The changes to the regulatory structure for legal services introduced by the Legal Services Act (the Act) and the development of the Legal Ombudsman (LO) have gone a considerable way to addressing the concerns identified by earlier reviews. However the structure of regulation remains complex.

There is some regulatory duplication under the new system but this has not been identified as a major regulatory burden. This may become more of an issue with the growth of Alternative Business Structures (ABS).

### **Market entry**

The introduction of ABS has removed a key barrier to market entry but the policy is still in the early stages of development. The application process both at the licensing body and the individual ABS level can be lengthy and time-consuming for senior staff but we have not identified any clear barriers to entry for ABS. There is no evidence at this stage that additional compliance costs have affected either the range of services being offered or the prices being charged to consumers. It is an open question whether the time and cost of applications is acting as a deterrent.

Demand for barrister training places is well in excess of supply. The availability of pupillage places is driven by market demand for barristers but the process of becoming a Pupillage Training Organisation (PTO) and the development of non-chambers PTOs may be limiting access to the market. The introduction of ABS may help to alleviate the shortfall in pupillage places by introducing more flexibility in the market and external funding.

### **Consumer redress**

The potential for consumer confusion on where to lodge a complaint has been reduced with the creation of the LO but has by no means been eliminated.

A recent YouGov consumer survey suggests that there are around three million users of legal services annually in the UK, of whom 15 per cent indicated they were dissatisfied with legal services on the last occasion they used them. The survey also suggested that only about 13 per cent of dissatisfied users went on

to make a complaint. Evidence from other recent surveys suggests that confusion regarding how to complain could be one reason why dissatisfied consumers do not go on to make a complaint.

## **The historical regulatory context**

- 1.1 In 2001 the Office of Fair Trading (OFT) published a report on competition in the provision of legal and other professional services. The report found that the regulatory framework for legal services was out-dated, inflexible, over-complex and insufficiently accountable or transparent. The OFT raised questions regarding the adequacy of self-regulation and the associated poor record with regard to consumer redress. It also raised concerns regarding restrictions against the setting up of multi-disciplinary partnerships and access to barristers.
- 1.2 Following further consultation the Government introduced legislation to provide for:
  - a new, independent and robust oversight regulator, the Legal Services Board
  - a single complaints-handling and consumer redress body, the Office for Legal Complaints and
  - the facilitation of innovative alternative business structures (ABS), helping the legal sector to become more responsive to consumer needs.
- 1.3 These reforms have been introduced progressively since 2007 with the main institutional changes occurring in 2010 and 2011. The first ABS was licensed in October 2011.

## **Recent developments**

- 1.4 The changes to the legal regulatory structure introduced by the Act have gone a considerable way to addressing the concerns identified by the OFT in 2001 and the Clementi review in 2004. There is now a clear separation between regulation and representative activities in each of the branches of the profession. This separation of functions should remove

the actual or perceived conflict of interest inherent in the previous structure and should enhance consumer confidence in using the regulated services.

- 1.5 The development of the Legal Ombudsman (LO) meets one of the original objectives that there should be a single organisation to address complaints about service that cannot be resolved with the provider.
- 1.6 These are positive developments but the structure of regulation remains complex with distinctions between reserved and unreserved activities, regulated and unregulated activities and separate regulation of individuals and entities.
- 1.7 There is scope for regulatory duplication under the new system where individuals and entities may be subject to more than one regulatory regime depending on the nature of their main business. However the responses we received in our interviews did not highlight this as a major regulatory burden. The lead regulatory responsibility is usually clear. This may become more of an issue with the growth of ABS.
- 1.8 The main area of the legal services market not subject to regulation is the provision of unreserved activities by unregulated individuals or entities. Will writing is the best known example of an unreserved activity. Any extension of regulation to this or other activities would need to be justified both in terms of the rationale for intervention – for example, correcting for information asymmetry – and by identifying benefits that outweigh the cost of regulation.

## **Restrictions on entry or development**

- 1.9 Two aspects of regulation that we identified as potentially restricting entry or development are the process for becoming authorised to provide training to barristers and the application processes for becoming ABS licensing bodies and becoming a licensed ABS.

### **Pupillage places**

- 1.10 We found that for every pupillage place there are on average six applicants, compared to a three to one ratio for solicitor training contracts. While pupillage places are driven by market demand for

barristers, the process of becoming a Pupillage Training Organisation may be limiting access to the market. There is evidence to suggest that the role of non-chambers Pupillage Training Organisations and the scope for barristers to supervise more than one pupil at a time (as is the case for solicitors) could be explored further to ensure that these do not present unnecessary barriers to entry to the profession.

- 1.11 The introduction of ABS may help to alleviate the shortfall in pupillage places by introducing more flexibility in the market and external funding. This is an issue that could be monitored going forward. The report from the Legal Education Training Review (LETR)<sup>1</sup> at the end of 2012 will also provide a more detailed analysis of training.
- 1.12 There is a current debate about moving from the traditional title based qualification and regulatory model to an approach based on qualification for specific activities. This could improve risk based regulation and allow greater flexibility for firms to enter the market. Such issues may warrant further exploration following the forthcoming report on legal education and training by the LETR.

### **Licensing and regulation of ABS**

- 1.13 At the entity level the introduction of ABS has removed a key barrier to market entry. The policy is still in the early stages of development and only 16 ABS had been approved at the time of this study. So far the emphasis of the new ABS has been on making non-lawyers partners and increasing their offering of legal services rather than the development of a wider range of services.
- 1.14 Data on the application processes, both at the licensing authority level and the firm level are limited but we estimate that on average it costs between £27,000 and £160,000 more to gain authorisation as an ABS compared to the traditional model. It is important to view these estimates in the context of the very recent introduction of the application process — there could be an element of learning by doing

<sup>1</sup> The SRA, BSB and IPS have jointly commissioned an independent review of legal education and training (LETR) with a final report due at the end of 2012

which would suggest that our figures overestimate the cost in the medium to long term.

- 1.15 Overall, while there appear to be no clear barriers to entry for ABS, it remains an open question whether the time and cost of applications is acting as a deterrent. This remains an area that may warrant monitoring in the future given the relative novelty of the reforms.
- 1.16 While multiple regulation of the individual is not a new phenomenon and unlikely to raise any significant issues, multiple regulation at the entity level would be a new dimension resulting from the option for ABS to offer both legal and non-legal services. Having to engage with multiple regulators could substantially increase costs and potentially undermine the concept of a one stop shop for consumers.
- 1.17 We found that, so far, multiple regulation does not appear to be an issue, as new ABS have not tended to extend their service offering beyond legal services. Over time the emphasis may shift away from ownership changes to ABS that provide the wider range of services envisaged at the policy development stage. This may result in the application process taking longer. In order to pre-empt any concerns, Memoranda of Understanding could be developed to clarify the relationships between key regulators and formalise mutual recognition.
- 1.18 There is no evidence at this stage that additional compliance costs have affected either the range of services being offered or the prices being charged to consumers. This could be reviewed going forward when the new system of ABS has had more time to develop.

## **Consumer redress**

### **Potential issues**

- 1.19 The potential for consumer confusion on where to lodge a complaint has been reduced with the creation of the LO but has by no means been eliminated.
- 1.20 There are a number of potential issues with the new system. In particular:

- the LO only covers authorised persons and entities (whether they are providing reserved or unreserved legal services) – this can raise particular issues where consumers are provided with a single packaged service which can involve authorised and unauthorised providers and potentially relate to services covered by another sector ombudsman, and
- the approved regulators or the organisations to whom they have delegated the power to regulate are still responsible for conducting complaints – this requires consumers to be able to distinguish between service and conduct complaints.

1.21 As a result of these factors in some cases consumer detriment may go unaddressed. In addition uncertainty in the process may increase costs to consumers and complaints handlers. Our survey work and other evidence suggests that there may be confusion about the complaints process and this could put consumers off complaining when they otherwise would have done so. In addition the new system requires, as the old system did, that consumers are provided with sufficient information about how the complaints procedure works. There is evidence that the new complaints process is not well understood, that consumers do not recall having the process explained to them by providers of legal services and that uncertainty about the process is amongst the reasons for consumers not complaining.

### **Consumer satisfaction**

1.22 A recent YouGov consumer survey suggests that around 33 per cent of the population of England and Wales have used legal services since 2007, this equates to around three million people using legal services annually. Of these around 15 per cent (approximately 460,000) suggested they were not satisfied with the overall service provided the last time they used them. The survey results suggest the vast majority of users who indicated they were dissatisfied did not go on to make a formal complaint about the service they received. The very small number of dissatisfied customers who go on to make a complaint is a potential concern because:

- it is indicative that on a significant number of occasions consumers receive poor service but do not go on to seek redress<sup>2</sup> and
- complaints from dissatisfied consumers represent an important source of intelligence in an industry, such as legal services, characterised by significant information asymmetry and with limited repeat purchasing.

1.23 The finding that large numbers of dissatisfied consumers do not go on to make a complaint is replicated in the results of a consumer survey commissioned by the LSB in 2011. This survey found that 66 per cent of dissatisfied consumers did not go on to complain.<sup>3</sup>

1.24 Although only a proportion of complaints made are upheld by the LO, this indicates a significant level of consumer detriment which has not been subject to any form of review or redress due to a lack of awareness or confusion over the complaints handling process.

### **Redirection of complaints**

1.25 Evidence from approved regulators and the LO indicate that complaints often need to be referred on to an alternative body resulting in some additional cost to consumers and complaints handlers.

### **Policy options**

1.26 One possibility for addressing consumer uncertainty about how or where to complain would be to make clear to consumers in all publicity provided by regulators and law firms that there is now a single post-box system where the Legal Ombudsman acts as the single point of contact

<sup>2</sup> Albeit only a proportion of those consumers who were dissatisfied would have their complaint upheld should they have decided to make a formally complaint.

<sup>3</sup> The survey results are not directly comparable as the LSB use a sample that consists only of dissatisfied consumers and because the sample pre-screening process used to identify dissatisfied customer differs from how the YouGov survey identifies dissatisfied customers. However, the findings confirm that a significant proportion of dissatisfied consumers do not go on to use the formal complaints process.

for all consumer complaints that cannot be resolved at the 'in-house' level.

- 1.27 The Legal Ombudsman is in a position to refer on the complaints to other organisations if appropriate. This would be similar to the model adopted in Scotland under the Scottish Legal Complaints Commission (SLCC). The possibility for a single unified timetable for all regulators/ombudsmen and a formal system for them to talk to each other could also be explored.

## **Scotland and Northern Ireland**

- 1.28 The reform of legal regulation is at very different stages in Scotland, Northern Ireland and England and Wales. While Scotland has made some moves towards the system adopted in England and Wales, there remain key differences both in terms of the market structure and the regulatory framework. Meanwhile Northern Ireland has experienced limited change in the regulatory framework over the last five-10 years.
- 1.29 Legal Services (Scotland) Act 2010 introduced the possibility of ABS being licensed but at present no regulatory body has been authorised to issue licences. The scope proposed for ABS in Scotland is more limited than in England and Wales. Advocates cannot participate in ABS and there is a limit on the extent of non-lawyer ownership.
- 1.30 The professional regulatory bodies continue to combine regulation and representational functions although separate disciplinary bodies exist to assess serious cases of misconduct.
- 1.31 The SLCC was set up in 2008 as a 'one-stop shop' for complaints and provides an initial filter to separate service complaints, which it handles and complaints about conduct which are referred on to the appropriate regulator.
- 1.32 In the case of Scotland it is too early to identify the costs and benefits of the reforms and these may warrant further examination once the changes have been fully implemented.
- 1.33 In Northern Ireland, in the absence of any significant policy reform, the focus of any on-going work should continue to consider issues of access, market entry and the legitimacy of the complaints process.

## 2 INTRODUCTION

2.1 Europe Economics was commissioned by the OFT to conduct research into regulatory restrictions in the legal services market. The aim of this research is to increase the OFT's understanding of how the sector has evolved since the OFT's 2001 report 'Competition in Professions' in respect of specific categories of regulatory restrictions in the legal services market.

### Objective of the study

2.2 Our research and this report aim to assist the OFT:

- in its competition advocacy work by providing economic evidence on the costs and benefits of certain regulatory restrictions from a consumer welfare perspective
- in identifying competition and consumer issues in relation to which the OFT can add significant value by taking competition and/or consumer enforcement action or conduct a tightly scoped market study, and
- in stimulating and influencing the on-going debate around liberalisation of professional services and empowering consumers both at national and supranational level. In particular, the research is designed to maximise the impact of any submissions the OFT will make in the context of consultations relating to professional services generally and the legal services market specifically.

2.3 In order to achieve this, the research has focused on identifying and assessing the economic impact of restrictions in the legal services sector. Specifically the research has sought to identify:

- Duplication of regulation and conflict between regulation carried out by different regulatory bodies relating to:
  - consumer redress and
  - the operation of alternative business structures (ABS) in England and Wales and

- regulations affecting entry into the market for legal services, including training requirements for barristers in England and Wales.

2.4 In addition, legal services in Northern Ireland and Scotland have been considered with a view to identifying unduly restrictive regulation, rules and practices that may give rise to consumer detriment.

## **Approach to the study**

2.5 We have adopted a fourfold approach to collecting relevant material for this report. At the start of the project we carried out a literature review. We used this to identify:

- the objectives which the current regulatory structure set out to achieve, with particular reference to consumer redress and market development
- the main approaches adopted by different regulatory bodies, and
- problems that have been identified as the new structures have been put into operation.

2.6 Relevant material has been drawn from Government publications, including impact assessments and other statements linked to the development of policy, regulators' policy statements and academic and professional commentary. A bibliography is provided in Annexe 1.

2.7 The literature review provided the input for a mapping exercise showing the structure of legal regulation and consumer complaint procedures. It was also used in drawing up questionnaires to send to the main regulatory and consumer complaint handling bodies. As far as possible standard questions were put to each of the regulators and ombudsman organisations but, where necessary, questions were customised to take account of differences, for example in training requirements. Separate questionnaires were sent to organisations in Scotland and Northern Ireland. Examples of the questionnaires are provided in Appendices 2 and 3.

2.8 These questionnaires were then followed up with a number of telephone interviews to discuss issues in more detail and to obtain qualitative views. Interviews were carried out with the Legal Services Board, the

Law Society, the Bar Council, the Bar Standards Board, the Faculty of Advocates, the Legal Ombudsman and the Financial Ombudsman. We also interviewed two recently accredited ABS and a number of consumer organisations.

- 2.9 The study also involved a short consumer survey to establish consumers' recent experience in the use of legal services, their awareness of complaint procedures and experience in the handling of complaints. The survey was carried out in June 2012 as part of the Ipsos Omnibus Survey and the results are included in this report. The questions used in that survey are set out in Annexe 5. We have also drawn on the results of other relevant consumer surveys to explore the issues of consumer experience of legal services and the complaints process.
- 2.10 Quantitative and qualitative information collected through these four channels have been used to identify the ways in which regulation and the handling of consumer complaints may have negative or positive effects on consumers and, where possible, to provide our own quantification of these effects.

## **Structure of the report**

- 2.11 The first section of the report looks at the current arrangements for regulation of legal services and complaint handling. We set out how arrangements differ depending on the nature of the service and on the individual or entity providing the service and set out illustrative 'maps' showing overlaps in existing regulatory arrangements and those areas which are not regulated.
- 2.12 The next section examines restrictions on entry into the legal services market. We set out an analytical framework and draw on evidence from our research to assess the effects of possible barriers. We consider barriers at both the entity and individual level. A similar approach is adopted in reviewing development in the use of ABS.
- 2.13 A separate analytical structure has been prepared for reviewing the handling of consumer complaints. Evidence for this section is drawn both from our questionnaires and interviews with regulators and ombudsmen and from the Consumer Survey.

- 2.14 The current structure of the regulation of legal services in Scotland and Northern Ireland is summarised in a separate section of the report.
- 2.15 Drawing together the result of the analysis in the previous sections we then set out our assessment of the impact of possible changes to regulation and consumer complaint handling looking in particular at effects on consumers from clearer procedures and reduced barriers to entry. This feeds into the conclusions section of the report.

### 3 ARRANGEMENTS FOR REGULATION AND CONSUMER COMPLAINTS

#### The historical regulatory context

- 3.1 In 2001 the OFT published a report on competition in the provision of legal and other professional services.<sup>4</sup> The report found that the regulatory framework for legal services was out-dated, inflexible, over-complex and insufficiently accountable or transparent. The report raised questions regarding the adequacy of self-regulation and the associated poor record with regard to consumer redress. It also raised concerns regarding restrictions against the setting up of multi-disciplinary partnerships and access to barristers.
- 3.2 As a result, the Government launched a consultation in 2002,<sup>5</sup> followed by a series of Government reports<sup>6</sup> and independent reviews, most notably the Clementi Report (Clementi (2004)).<sup>7</sup> Clementi confirmed that oversight regulation of front-line bodies (for example, the Law Society and the Bar Council) was inconsistent. Governance arrangements did not separate regulatory from representative functions, which was found to be a potential source of consumer detriment, as were the numerous and inconsistent procedures for complaints handling. Finally, restrictions on

<sup>4</sup> Office of Fair Trading (2001) 'Competition in the Professions – A Report by the Director General of Fair Trading'.

<sup>5</sup> Department for Constitutional Affairs (2002), 'A Lord Chancellor's Department Consultation Paper: In the Public Interest? A Consultation following the Office of Fair Trading's report on Competition in Professions'.

<sup>6</sup> Department for Constitutional Affairs (2003) 'Response to the Consultation Paper: 'In the Public Interest'', Department for Constitutional Affairs (2003), 'Competition and Regulation in the Legal Services Market – A Report Following the Consultation 'In the Public Interest?''

<sup>7</sup> Clementi, David (2004) 'Review of the Regulatory Framework for Legal Services in England and Wales – Final Report'. Report for the Secretary of State for Constitutional Affairs.  
[www.legal-services-review.org.uk/content/report/index.htm](http://www.legal-services-review.org.uk/content/report/index.htm)

the ownership and composition of legal practices were thought to act as barriers to entry and competition.<sup>8</sup>

3.3 Accepting these challenges, the Government published a White Paper in 2005, in which it set out several proposals for reform.<sup>9</sup> The three planks upon which reforms were to be built were:

- a new, independent and robust oversight regulator, the Legal Services Board
- a single complaints-handling and consumer redress body, the Office for Legal Complaints, and
- the facilitation of the innovative ABS, helping the legal sector to become more responsive to consumer needs.

3.4 Following consultation a full regulatory impact assessment was conducted by the Ministry of Justice (MoJ) in 2006 and the Legal Services Bill was introduced into Parliament in the same year.<sup>10</sup> The Bill received Royal Assent in 2007.

### **Changes in regulation since the Legal Services Act (2007)**

3.5 The current regulatory structure thus has its legal basis in the Legal Services Act (2007), (the Act). The Act seeks to liberalise and regulate the market for legal services in England and Wales by encouraging competition and facilitating access to consumer redress. Separate provisions apply in Scotland and Northern Ireland.

3.6 The Act brought about three key changes to the legal services market. The first relates to the establishment of new rule-making structures.

<sup>8</sup> Clementi, David (2004) 'Review of the Regulatory Framework for Legal Services in England and Wales – Final Report'. Report for the Secretary of State for Constitutional Affairs. [www.legal-services-review.org.uk/content/report/index.htm](http://www.legal-services-review.org.uk/content/report/index.htm)

<sup>9</sup> Department for Constitutional Affairs (2005) 'The Future of Legal Services: Putting Consumers First'.

<sup>10</sup> Ministry of Justice (2006) 'Legal Services Bill: Full Regulatory Impact Assessment'.

These include the establishment of approved regulators and a separation of regulating bodies' representational and regulatory functions. The second change relates to consumer redress. In its impact assessment, the MoJ argued that the primary rationale for regulation of the legal services market was information asymmetry. As legal services are purchased infrequently and often in stressful circumstances, consumers find it difficult to assess quality before, during and even after such services are delivered. Improved channels for consumer redress would mitigate the effects of this asymmetry ex-post. The third key change is the reduction of entry barriers. This refers primarily to the introduction of ABS.

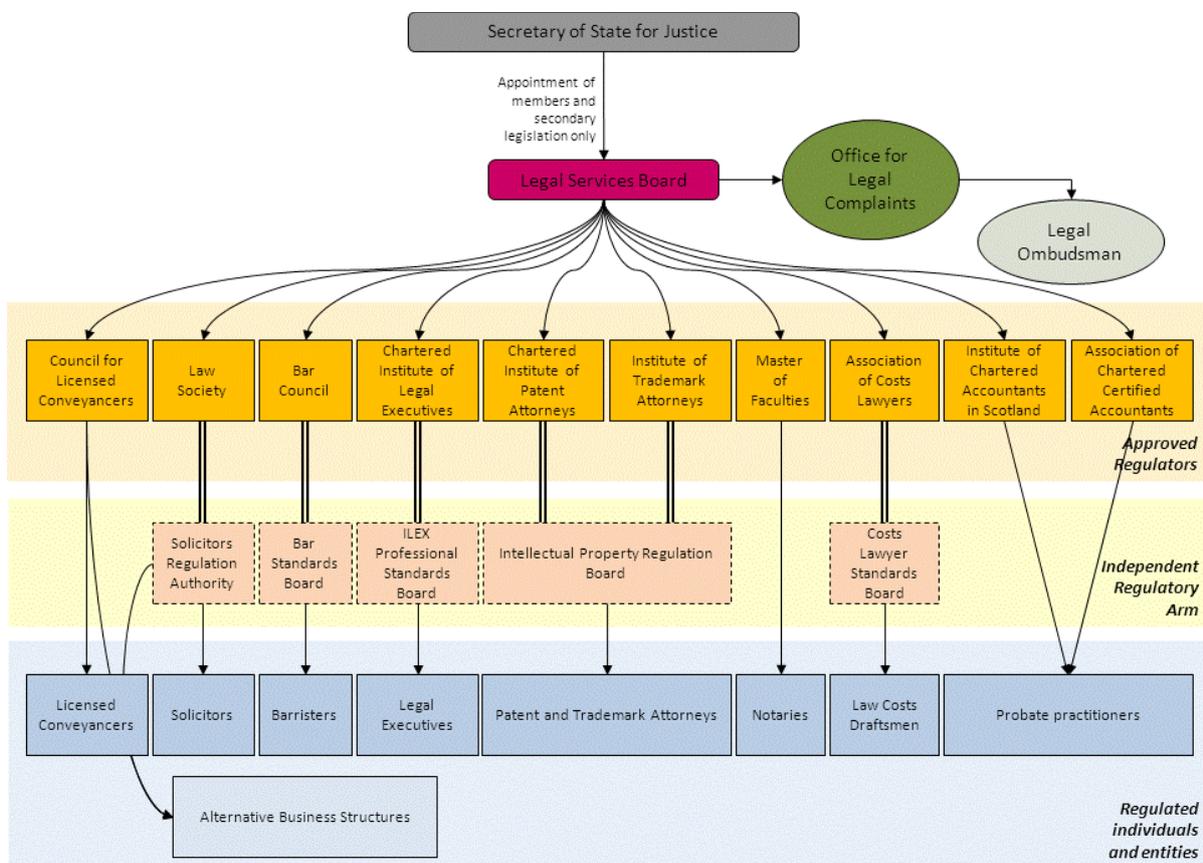
- 3.7 The means through which these three changes – rule-making structures, consumer redress and restrictions on entry – are addressed by the Act are discussed in turn.

### **Rule-making structures**

- 3.8 One of the Government's objectives in reform was simplification of the 'regulatory maze' that existed in the legal professions. Clementi (2004) argued that the system was flawed, complex and inconsistent. One principal recommendation was that oversight regulatory arrangements be restructured to reduce complexity and facilitate consistency. A second recommendation was that regulatory functions be separate from representative functions – there could be a conflict of interest if a professional body also represented the individuals or entities it sought to regulate, reducing consumer confidence in the system.
- 3.9 The Act sought to tackle both issues. First, it established the Legal Services Board (LSB), which is responsible for overseeing 10 separate bodies, the Approved Regulators. These regulators themselves regulate all lawyers practising throughout the jurisdiction. The Board also oversees a new organisation, the Office for Legal Complaints, which handles consumer complaints about lawyers. Second, it requires approved regulators to separate fully their regulatory and representative functions. All regulatory decisions should be taken by an independent regulatory arm, who may seek intervention of the LSB should it feel that any action or inaction on the part of the relevant professional body is damaging to its independence or effectiveness.

3.10 The results of these reforms are illustrated in Figure 3.1. The Secretary of State for Justice appoints members of the Legal Services Board, which regulates 10 approved regulators and the Office for Legal Complaints. Where required, the approved regulators delegated their regulatory functions to an independent regulatory arm. For example, as a professional body, the Law Society retained its representational functions and delegated its regulatory functions to the Solicitors Regulation Authority (SRA). Each approved regulator itself regulates one lawyer-type entity and/or individual. Referring to the previous example, the SRA regulates solicitors.

**Figure 3.1 Result of regulatory reforms in legal profession**



Source: Europe Economics

## Consumer redress

3.11 Changes to the rule-making structures were made in the interest of the public. Indeed, the LSB's overriding mandate is to ensure that regulation in the legal services sector is carried out in the public interest and that

the interests of consumers are placed at the heart of the system.<sup>11</sup> In addition to complexity and inconsistency in the regulatory structure, similar and related complexity and inconsistency was found in the complaints handling system.

- 3.12 MoJ (2006) had identified several problems with complaints handling in the regulatory structure prior to the introduction of the Act. Each legal discipline had separate complaints procedures and there were multiple overseeing authorities, each responsible for varying degrees of external oversight of complaints handling.<sup>12</sup> Additionally, as before, regulating bodies were responsible for regulating members, representing their interests and handling complaints, resulting in a perceived or actual lack of independence in complaints handling.
- 3.13 In order to address these problems, the Act introduced a new complaints-handling structure and abolished the then-existing Legal Service Ombudsman and the Office of Legal Services Complaints Commissioner. Under the revised structure the LSB oversees a new organisation that handles consumer complaints about lawyers, the Office for Legal Complaints (OLC). In turn, the OLC is responsible for setting up and running an independent ombudsman scheme which aims to resolve complaints between consumers of legal services and providers of such services. Consequently, the OLC established the Legal Ombudsman, responsible for resolving consumer complaints against lawyers.<sup>13</sup>
- 3.14 It is important to note that the Legal Ombudsman's jurisdiction is limited to complaints about the service provided. Where complaints are about professional misconduct, jurisdiction lies with the approved regulators

<sup>11</sup> Legal Services Board (2009) 'About Us' See [www.legalservicesboard.org.uk/about\\_us/index.htm](http://www.legalservicesboard.org.uk/about_us/index.htm)

<sup>12</sup> Including the Legal Service Ombudsman, the Legal Services Complaints Commissioner, the Secretary of State for Constitutional Affairs, the Master of the Rolls, the Court of Facilities, the Financial Services Authority, the Patent Office and the Immigration Services Commissioner

<sup>13</sup> Memorandum of Understanding between the Legal Services Board (LSB) and the Office for Legal Complaints (OLC). [www.legalservicesboard.org.uk/about\\_us/our\\_relationships/pdf/20091217\\_lsb\\_and\\_olc\\_mou.pdf](http://www.legalservicesboard.org.uk/about_us/our_relationships/pdf/20091217_lsb_and_olc_mou.pdf)

(and other statutory regulators if appropriate). This distinction between service and conduct may not always be clear to consumers.

3.15 Generally, professional misconduct involves a breach of the code of conduct which is relevant to that lawyer. For example, barristers must abide by the code of conduct set by the Bar Standards Board (BSB). Examples of professional misconduct include:

- misleading the court
- failing to keep information confidential
- acting dishonestly or in a way that damages the profession's reputation
- discriminating against you because of your race, sex, disability, religion or belief, sexual orientation, gender reassignment, age or marital/civil partnership status.

3.16 Conversely, aspects of poor service include:

- delayed or unclear communication
- problems with fees, or
- loss of documents.<sup>14</sup>

3.17 It does not include dissatisfaction with the outcome of a court case.

3.18 For all complaint-types, the LSB has required legal service providers to maintain in-house complaints handling procedures. In the first instance consumers are required to file a complaint in-house with the provider of the service. Only if the complaint cannot be resolved with the service provider can the consumer take the issue to the Legal Ombudsman in

<sup>14</sup> See, for example, consumer complaints handling information provided by the Bar Standards Board: [www.barstandardsboard.org.uk/complaints-and-professional-conduct/concerns-about-a-barrister](http://www.barstandardsboard.org.uk/complaints-and-professional-conduct/concerns-about-a-barrister) and the Solicitors Regulation Authority: [www.sra.org.uk/consumers/problems/report-solicitor.page](http://www.sra.org.uk/consumers/problems/report-solicitor.page)

respect of a complaint about service or to the relevant approved regulator for a complaint about professional conduct.

## Restrictions on entry

- 3.19 OFT (2001) found evidence of restrictions on multi-disciplinary partnerships, which limited competition in the legal sector. In his independent review, Clementi (2004) investigated this in more detail and also found restrictions on partnerships between different legal disciplines and between legal and non-legal disciplines. For example, individuals practising a non-legal discipline with non-legal skills which are nevertheless essential to running a modern legal practice (for example, IT or finance) could not act as principals in those businesses. Additionally, barristers could not enter into partnerships with each other, and neither barristers nor solicitors could enter into partnerships with other professionals (lawyers and non-lawyers). Finally, barristers could not generally deal directly with the public, instead having to do so through solicitors.<sup>15</sup>
- 3.20 Consequently, following a cost-benefit analysis by MoJ (2006), the Act now allows for the licensing of ABS, whereby lawyers and providers of non-legal services can establish firms offering services covering multiple disciplines and non-lawyers can act in management roles. It was anticipated that allowing ABS would increase competition between existing suppliers and potential competition from new suppliers and forms of supply. ABS must apply for a licence allowing them to provide legal services. The LSB gives separate authorisation to independent regulatory bodies to issue licences for the operation of ABS. At present only the SRA and the Council for Licensed Conveyancers (CLC) have received this authorisation.
- 3.21 While the Act allowed for ABS, the provisions did not come into force immediately. On 31 March 2009, Legal Disciplinary Practices (LDPs) with a maximum non-lawyer ownership of 25 per cent were allowed, and restrictions on full ABS were only lifted on 6 October 2011.

<sup>15</sup> Clementi, David (2004) 'Review of the Regulatory Framework for Legal Services in England and Wales – Final Report'.

- 3.22 OFT (2001) also questioned the extent to which entry qualifications and professional development requirements restricted entry to the legal services market. Academic and professional qualifications help the consumer assess the quality of a legal service ex-ante, a task rendered difficult by the presence of information asymmetry. Such qualifications also allow service providers to distinguish themselves and signal higher quality to the consumer. Excessive requirements on entry qualifications and professional development may restrict the number of service providers (for example, barristers and solicitors) who are able to practice, therefore acting as a restriction on market entry.
- 3.23 OFT (2001) found no evidence that entry qualifications and professional development requirements unduly restricted entry at the time. Nevertheless, an effective competitive environment is characterised by a balance between the quality and the quantity of service providers and services provided, and this balance needs to be kept under review. As such, Section 4 of the Act places the duty on the LSB to help the approved regulators maintain and develop standards of education and training of regulated persons. For example, the Board may issue guidance on, or examples of, good education and training practices or principles of professional conduct that have been developed for a reserved legal activity by one approved regulator to all approved regulators.
- 3.24 Indeed, the LSB is increasingly focused on education and training, the role these play in market functioning and the impact on consumers. Education and training standards and entry requirements have changed since OFT (2001). For example, the LSB recently approved a Bar Course Aptitude Test (BCAT), now to be required of all aspiring barristers. The test will be compulsory for entry to the Bar Professional Training Course (BPTC), requiring students to meet a minimum standard specified by the BSB. The SRA has announced it will remove the minimum salary requirement on training contracts, allowing solicitor firms greater flexibility on trainee pay subject to the requirements of the minimum wage legislation. These changes are too recent to have had a clear impact at this stage.
- 3.25 The SRA, BSB and ILEX Professional Standards (IPS) have jointly commissioned an independent review of legal education and training (LETR) with a final report due at the end of 2012. The LETR is wide

ranging covering both regulated and non-regulated legal services. It will cover all stages of legal education and training, including the academic stage(s) of qualification, professional training and continuing professional development of the regulated professions. It will identify both the scope for deregulation of existing training requirements and whether there is a case for bringing aspects of the non-regulated sector within a scheme of regulation. The stated objective of LETR is to ensure that England and Wales has a legal education and training system which advances the regulatory objectives contained in the Legal Services Act 2007, and particularly the need to protect and promote the interests of consumers and to ensure an independent, strong, diverse and effective legal profession.<sup>16</sup>

- 3.26 The Act has also led to a move away from individual based regulation towards entity-based regulation. More specifically, legal professionals no longer have sole ownership and management responsibilities (non-lawyers may now own and/or manage ABS). As a result, while education and training of legal professionals as individuals remain central to the well-functioning of the market, increasing focus is now being placed on how the entity will ensure services provided are of the appropriate quality standards, for example, how the entity will train and educate its workforce to ensure those standards are met.<sup>17</sup>
- 3.27 Regulators are increasingly moving to outcomes-focused regulation, where they set desired outcomes (for example, quality standards) and assess an entity's risk of not achieving those outcomes (as opposed to setting rules and regulations).<sup>18</sup> Each entity will need to decide the type of workforce (for example, solicitors, paralegals, financial advisers) that it needs in order to deliver any chosen activity, where activities carry different risks. Each entity will also need to ensure these decisions

<sup>16</sup> Details of the review are available at <http://letr.org.uk/about/what-is-letr>

<sup>17</sup> LSB (2012), 'Education and Training: Its Role in Regulation?' [online]. Available at: [www.legalservicesboard.org.uk/Projects/workforce\\_development/pdf/20120221\\_education\\_and\\_training\\_its\\_role\\_in\\_regulation\\_final.pdf](http://www.legalservicesboard.org.uk/Projects/workforce_development/pdf/20120221_education_and_training_its_role_in_regulation_final.pdf) [Accessed: 28 August 2012].

<sup>18</sup> Such a regulatory approach is already being adopted by the SRA, although it is still at the early stages of implementation

support the outcomes specified by the regulator. Training will thus depend increasingly on the activity being provided and not only the individual providing it.

- 3.28 Training and education is only one element of the activities-based regulation debate, which argues for using risks to differentiate regulatory approaches between activities. The key driver is the desire for liberalisation – allowing non-lawyers to qualify to conduct specific activities (for example, will-writing and estate administration, now being considered to be included as a regulated activity) and improve competition in the market.<sup>19</sup> It is too early to establish whether activities-based regulation will reduce barriers to entry (for example, by allowing non-lawyers to conduct specified activities) or increase them (for example, by requiring such non-lawyers to obtain qualifications which they would have otherwise not needed to obtain).

## **Regulatory and complaints mapping in legal services**

### **Regulatory mapping**

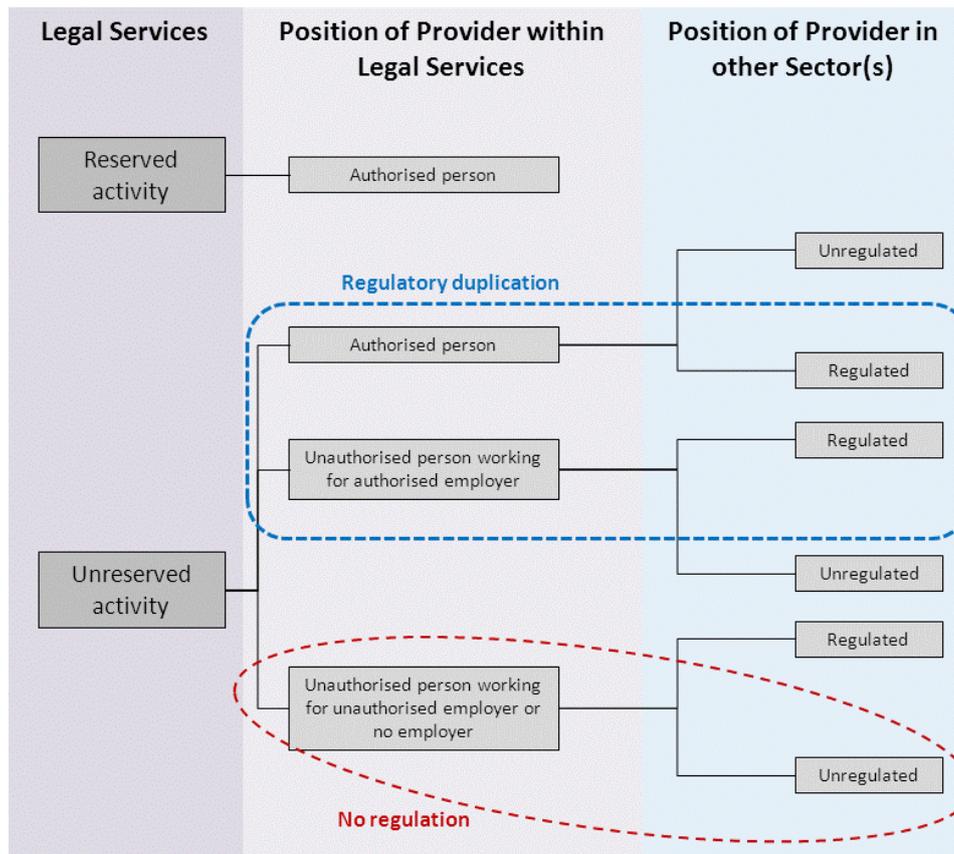
- 3.29 The Act distinguishes between reserved and unreserved legal activities. It identifies six reserved activities, also referred to as the ‘inner circle of legal services’, as follows:

- exercise a right of audience
- conduct of litigation
- reserved instrument activities
- probate activities
- notarial activities
- administration of oaths.

<sup>19</sup> LSB (2012), ‘Activities Based Regulation: An Introduction’, [online]. Available at: [www.legalservicesboard.org.uk/about\\_us/board\\_meetings/pdf/paper\\_12\\_35\\_activity\\_based\\_regulation.pdf](http://www.legalservicesboard.org.uk/about_us/board_meetings/pdf/paper_12_35_activity_based_regulation.pdf) [Accessed 28 August 2012]

- 3.30 Unreserved activities can be classified into regulated and unregulated activities. Regulated activities are those regulated by a statute other than the Act. Examples include immigration advice, claims management services and insolvency work. Unregulated activities are those which are not regulated by any statute (including the Act). Examples of these include preparation of wills, advice and representation at a police station and advice about mental health.
- 3.31 Reserved activities can only be conducted by authorised persons, while unreserved activities can be conducted by authorised, unauthorised and unregulated persons alike. Authorised persons are individuals or entities which have been authorised to conduct reserved activities by the appropriate authorised regulator. These regulators are supervised by the LSB. Examples of authorised persons include solicitors and barristers. Unauthorised persons are not authorised themselves, but are employed by an authorised person. Unauthorised persons may conduct all legal activities except reserved activities. Unregulated persons are also not authorised, nor are they employed by an authorised person. Unregulated persons may also conduct all legal activities except reserved activities, although it should be noted that if an activity is regulated then the person is, by extension, regulated.
- 3.32 Unreserved activities may also be conducted by persons outside the legal services sector. For example, mortgage-related legal activities may be conducted by a bank. The bank is regulated by relevant financial statutes and the Financial Services Authority (FSA). In this case the person, for instance, the bank, is unregulated within the legal services sector but is regulated within the financial services sector. Finally, a person conducting unreserved activities may be unregulated within the legal services sector and unregulated within other sectors. A person conducting only will-writing activities, for example, falls under this category.
- 3.33 The interaction between these different types of activities and the level of regulation is illustrated in Figure 3.2 below.

**Figure 3.2: Regulatory mapping**



Source: Europe Economics

3.34 Persons conducting legal activities may therefore be regulated by one or more of the following:

- The Act in the case of reserved activities.
- Other legal-sector statutes relevant to the activity being conducted.
- The legal-sector regulatory body that has given that person a license to conduct the activity.
- Other-sector statutes relevant to the person conducting the activity.
- Other-sector regulatory bodies relevant to the person conducting the activity.

3.35 Where multiple statutes and/or regulatory bodies regulate a person and/or activity, there exists regulatory duplication. Where a person and activity are not covered by any statute or regulatory body within and

outside of the legal services sector, there exists no regulation. The consequences of this are clearly manifested in the way consumer complaints are handled.

### **Mapping of complaints process**

- 3.36 The Legal Ombudsman has jurisdiction over all complaints on the service provided by authorised persons, while authorised regulators have jurisdiction over all complaints concerning professional conduct of authorised persons. As such, consumer complaints concerning authorised persons are directed to one of these two bodies, irrespective of whether the activity is reserved or unreserved.
- 3.37 As reserved activities can only be conducted by authorised persons, any complaint concerning a reserved activity will be directed to either the Legal Ombudsman or to the appropriate authorised regulator. However, as unreserved activities may be conducted by authorised persons, unauthorised persons, persons which are unregulated within the legal services sector, persons which are regulated in other sectors and/or persons which are unregulated in other sectors, there are multiple channels for consumer redress.
- 3.38 For example, if a consumer has been provided unreserved legal services by a bank, complaints could be referred to the Financial Ombudsman Service (FOS). However if a solicitor was also involved in the service provision, then the consumer may be referred to either the FOS or the Legal Ombudsman. Additionally, as the definition of an unauthorised person is a person who is not authorised but whose employer is authorised, there is a theoretical possibility that complaints concerning the unauthorised person who might, for example, have been providing a non-legal service may be referred to the Legal Ombudsman or authorised regulator via the authorised employer.
- 3.39 As not all activities are regulated, there may not be a relevant regulatory body for that activity. Where an authorised person, unauthorised person or a person regulated within another sector conducts unregulated activities, the consumer may file a complaint with one of the several regulatory bodies both inside and outside the legal services sector (for example, the Legal Ombudsman in the case of unregulated activities conducted by authorised persons, and other bodies in the case of

unregulated activities conducted by unauthorised persons or persons regulated within other sectors). The potential for overlap resembles that above. However, a number of unregulated activities are increasingly conducted by unregulated persons (for example, will-writing). Where neither the activity nor the person is regulated in any sector, there exists no regulation and therefore no regulated complaints handling system. The relationship between the different types of services offered and the complaints process are illustrated in Figure 3.3 below.

Figure 3.3: Complaints channels mapping by service type

Legal Services	Position of Provider within Legal Services	Position of Provider in other Sector(s)	Complaints Channel				
			First-tier	Second-tier			
			In-house	Legal Ombudsman & Authorised Regulators (LSA 2007)	Other Legal Services Regulator (by Statute)	Other Sector Ombudsman or Regulator	No Ombudsman or Regulator
Reserved activity	Authorised		✓	✓			
		Regulated	✓	✓	✓	✓	
Regulated activity	Authorised	Unregulated	✓	✓	✓		
		Regulated	✓	✓*	✓	✓	
	Unauthorised	Regulated	✓	✓*	✓	✓	
		Unregulated	maybe^		✓	✓	
	Unregulated	Regulated	maybe^		✓		
		Unregulated	✓	✓			
Unreserved activity	Authorised	Unregulated	✓	✓			
		Regulated	✓	✓		✓	
	Unauthorised	Regulated	✓	✓*		✓	
		Unregulated	✓	✓*			
	Unregulated	Regulated	maybe^			✓	
		Unregulated					✓

\*As unauthorised persons are employed by authorised individuals or entities, and the entity regulator takes jurisdiction over the individual regulator (if existing), complaints against unauthorised persons under this definition ultimately fall under the jurisdiction of the Legal Ombudsman.

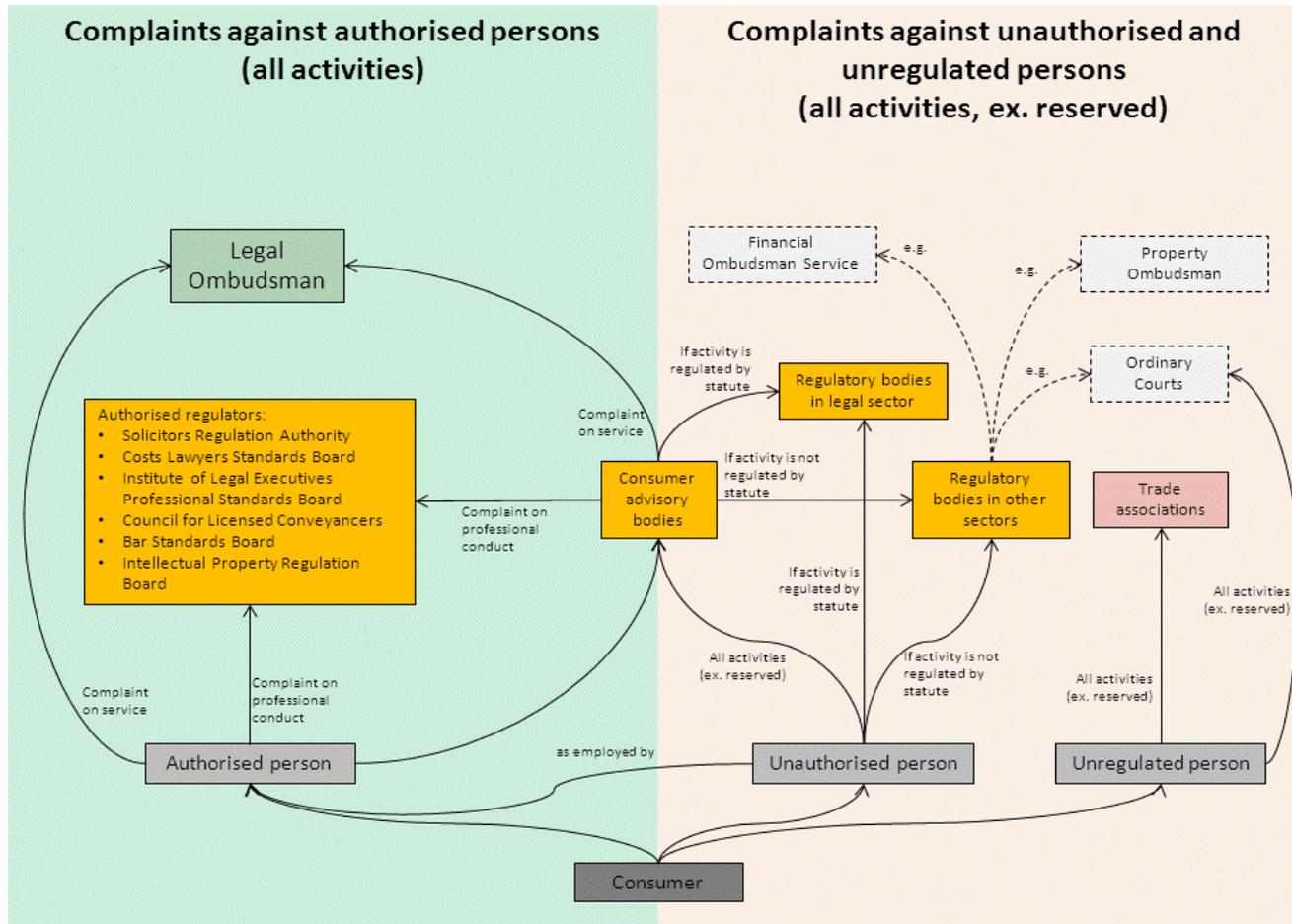
^Where the activity is unreserved and the provider within legal services is unregulated, then first-tier complaints procedures will depend on the relevant statute that governs that activity and/or service provider, either within legal services or in other sectors.

Source: Europe Economics

3.40 Figure 3.3 and Figure 3.4 provide a very simplified portrayal of the many possible channels for consumer redress. At first-tier, consumers refer their complaint to the person or entity providing the service (light grey). At the second-tier, complaints are referred to the appropriate regulating

and/or advisory bodies inside and/or outside legal services, and/or to the relevant trade association. Regardless of the person or activity, consumers may refer to a consumer advisory body, which will normally refer them to either the Legal Ombudsman or the appropriate authorised regulator. In cases where both the activity and the person are unregulated, consumers may be able to refer complaints to the relevant trade association (for example, the Society of Will Writers). In the case of complaints to a trade association the complaints procedure will generally depend on the practices of the individual association. Indeed, compensation is rarely provided in these cases. Alternatively, consumers may refer their complaints to ordinary courts, which may entail additional time and cost.

Figure 3.4: Complaints Channels



Source: Europe Economics

3.41 While the above figures illustrate typical regulatory interactions and complaints channels, one should note there may exist further complications in practice. For example, the figures suggest that complaints concerning reserved activities will be directed to either the Legal Ombudsman or the relevant authorised regulator. However, in practice many reserved activities are conducted as part of a larger package of services. For example, while conveyancing is a reserved activity, house purchasing typically involves services from an estate agent, a mortgage finance provider, a surveyor and a solicitor – oversight may be shared between the Legal Ombudsman (in the case of lawyers), the Ministry of Justice (in the case of mortgages and property) and the FOS (in the case of financial services), among others. The extent of the overlap will depend on both the type of activity and type of person conducting it.

## 4 RESTRICTIONS ON ENTRY/EXPANSION

### Introduction

- 4.1 Legal services are characterised by information asymmetries between practitioners and consumers, who tend to purchase these services infrequently and often under traumatic and/or stressful circumstances, such as divorce, death, house buying or prosecution. As a consequence restrictions on market entry have been a feature of the legal profession since the profession started and in many cases are necessary to ensure consumers are protected.
- 4.2 One feature of this market is the classification of services into reserved and unreserved activities. As discussed in the previous section only authorised persons are allowed to provide reserved services. Educational and training requirements for becoming an authorised person reinforce this distinction and contribute to the protection of consumers.
- 4.3 Research conducted by the OFT in 2001 also found evidence of restrictions on the types of organisations that could operate in the market, which further restricted entry and competition in the industry. In particular restrictions on multi-disciplinary partnerships were identified. Clementi (2004) investigated this in more detail and also found restrictions on partnerships between different legal disciplines, as well as between legal and non-legal disciplines.<sup>20</sup>
- 4.4 These restrictions on the structure of organisations providing legal services were thought to represent an unnecessary barrier to entry and expansion within the industry. Changes were therefore introduced in order to facilitate market entry. In particular, the Act sought to facilitate market entry by allowing for ABS and removing restrictions on the management of firms providing legal services (by non-lawyers).

<sup>20</sup> Clementi, David (2004) *Review of the Regulatory Framework for Legal Services in England and Wales – Final Report*. Report for the Secretary of state for Constitutional Affairs. Retrieved from [www.legal-services-review.org.uk/content/report/index.htm](http://www.legal-services-review.org.uk/content/report/index.htm)

4.5 In this section we examine if and how the current regulations are restricting entry into the market for legal services. In particular we focus on:

- identifying statutory requirements and other restrictions which give rise to barriers to entry into the profession by imposing burdens specifically on new entrants, and
- identifying and assessing education and training requirements relating to the barrister profession, with a view to allowing the OFT to reach an evidence-based view as to whether certain requirements may be disproportionate should they unnecessarily restrict access to the profession to the detriment of consumer welfare.

4.6 We first identify the scope for such problems and use this to construct the analytical framework, describing the mechanisms through which such restrictions may impact on consumer welfare.

4.7 We then present our analysis of the empirical and qualitative information collected via the surveys and interviews. We assess the extent to which the potential detriment identified in the analytical framework may have materialised.

## **Potential benefits and costs of restricted entry**

### **Potential benefits**

4.8 Goods and services may be categorised according to our ability to assess their levels of quality. The quality of 'search' goods and services may be observed prior to purchase. The quality of 'experience' goods and services may be observed immediately after a purchase. In the case of 'credence' goods and services quality may only be observed sometime after purchase, if at all.

4.9 Many professional services, including legal services, are considered to be 'credence' goods.<sup>21</sup> Such services may be too technically complex for

<sup>21</sup> That legal services are considered to be credence goods is widely accepted. See also Cabrillo and Fitzpatrick (2008), *The Economics of Courts and Litigation*, Cheltenham: Edward Elgar

the consumer to discern quality. Similarly, the quality of the service may not be directly related to the outcome – for example, a lawyer may lose a case despite his best efforts.

- 4.10 Where a consumer cannot discern the quality of services provided, there exists an information asymmetry between the consumer and the service-provider. This may lead to market failure, as the latter has incentives to undercut quality without reducing price. Alternatively, as the individual providing the service is also the one who diagnoses the consumer's requirement, he or she may have an incentive to bias his recommendation towards a service that is more profitable for the provider. Regulation in such markets is designed to overcome such problems of asymmetric information.
- 4.11 As such, within legal services, certain activities are classified as 'reserved' so that only authorised persons may provide them. The types of services classified as reserved have evolved over a number of years.<sup>22</sup> While the rationale for classifying individual activities as reserved has, historically, been unclear, recent analysis by the Legal Services Institute (2011), suggests that by and large such services deserve their reserved status.<sup>23</sup>
- 4.12 Restricting certain activities in this way is intended to ensure the quality of the service provision and protect the independence of the services provided, both of which are key for consumer protection in this sector.
- 4.13 Closely linked to the classification of certain services as reserved activities is the issue of training requirements for individuals to qualify to provide legal services. Both solicitors and barristers for example have to go through a rigorous training process in order to qualify to operate in

Publishing Limited, Chapter 3, Bonroyet. al (2010), 'Credence goods, experts and risk aversion', Grenoble Applied Economics Laboratory (GAEL) Working Papers 201005,

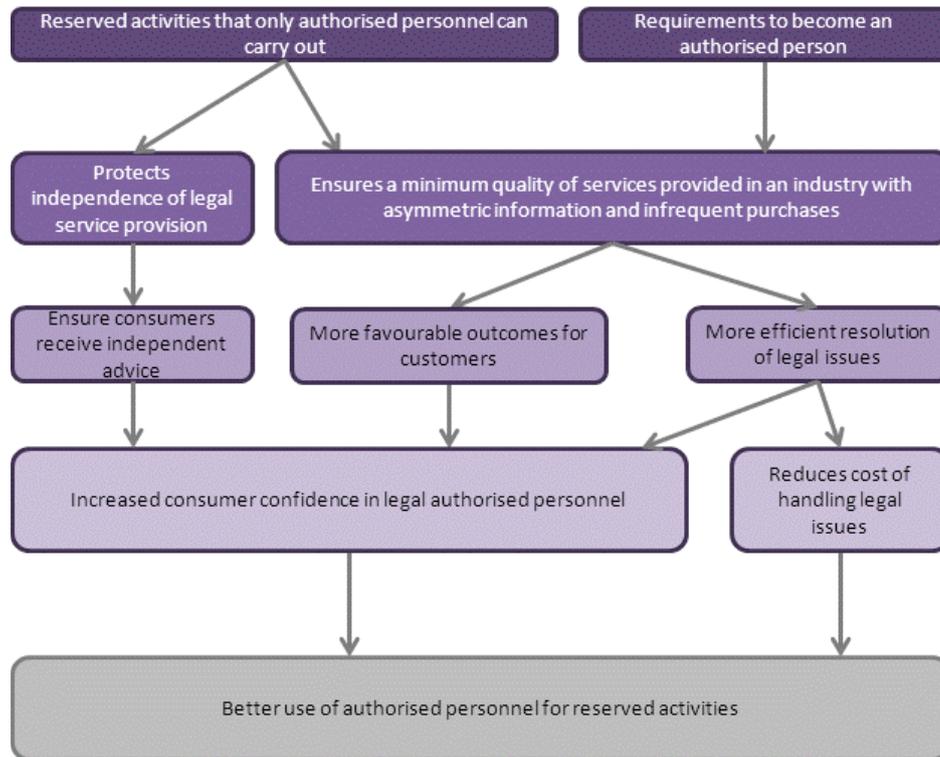
<sup>22</sup> Legal Services Institute (2011) 'The Regulation of Legal Services: What is the Case for Intervention?'

<sup>23</sup> Legal Services Institute (2011) 'The Regulation of Legal Services: What is the Case for Intervention?'

the sector and carry out reserved services. There are three main elements to the training process: academic, vocational and practical.

- 4.14 The academic training usually involves obtaining a degree in law. Subsequently, solicitors' and barristers' training requirements differ. Solicitors are required by the Law Society, to complete a Legal Practice Course, followed by a two-year Training Contract obtained with a law firm. Solicitors are accepted into the Law Society following completion of this training. Meanwhile, barristers must take the Bar Professional Training Course (BPTC), designed by the General Council of the Bar to develop practical skills necessary for court work. On successful completion of the Bar Exams, the student can then be called to the Bar by their Inn of Court. There are four Inns of Court, and membership is mandatory in order to become a barrister (membership involves paying a fee and attending a number of sessions at the Inn). In order to practice alone, barristers must complete a 12 months' 'pupillage' at a set of chambers where they learn from experienced barristers.
- 4.15 Such requirements to become qualified legal professionals and authorised persons ensure a minimum quality of legal professionals and reinforce quality standards created by the classification of reserved activities.
- 4.16 High quality service provision and independent advice should ensure that consumers are appropriately represented and as such receive independent advice and more favourable outcomes, both of which create consumer confidence in qualified persons. Also services provided by qualified individuals would expect to result in a more efficient resolution of any legal issues, potentially reducing the cost of handling such issues. This would further enhance confidence in legal professionals.
- 4.17 These potential benefits of restrictions on market entry are illustrated in Figure 4.1 below.

**Figure 4.1: Potential benefits of restrictions on market entry**



Source: Europe Economics

## Potential costs

4.18 While such restrictions may be necessary and desirable, there is scope for entry to be unduly restricted under this system.<sup>24</sup> Key factors considered in our research are:

- existing requirements on the ownership of firms and approvals processes for entry to the market at the firm level, and
- regulations hindering the growth and development of pupillages for barristers.

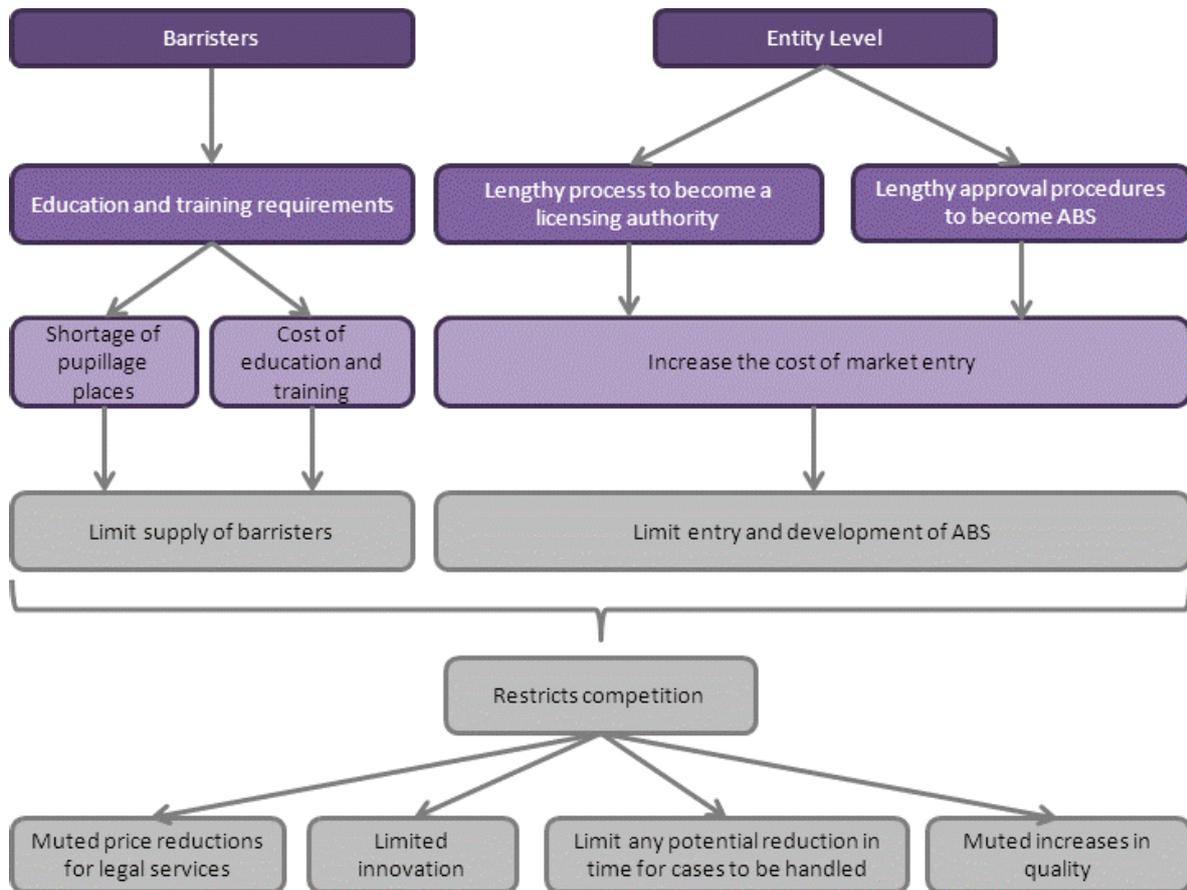
4.19 While classifying activities as reserved creates benefits in terms of consumer protection, the restriction also potentially creates costs for

<sup>24</sup> To note it is beyond the remit of this study to explore whether or not such restrictions are indeed appropriate.

consumers by limiting the scope for competition in the provision of those services. The need to become an authorised person increases the costs associated with providing reserved services and restricts the number of persons that can provide the services. While in certain areas such costs may be justified in order to ensure quality, there is the potential for authorisation processes to create unnecessary barriers to entry, both at the individual and entity level.

- 4.20 At the individual level a shortage of training places, in particular pupillages for barristers, and the cost of training may represent barriers to entry.
- 4.21 At the firm level, even following the reforms introduced in the Act, limits on market entry and expansion still potentially exist. New authorisation procedures have been introduced for ABS. These cover both the approval of licensing authorities and the approval by those authorities of individual ABS. These procedures are new and still under development but if they prove to be lengthy or more costly than approval procedures for the traditional business structures such as solicitor partnerships, this could limit the development of ABS and their entry into the market. Equally lengthy processes involved in becoming a licensing authority may further hamper the development of such business structures by limiting the number of bodies able to approve ABS.
- 4.22 Ultimately any requirements that restrict supply either at the entity level or the individual level will limit any potential for increased competition and access for consumers envisaged with the introduction of the Act. As a result any anticipated price reductions, increases in quality and innovation, and impacts on the time for consumers to have their case handled may be more muted than originally envisaged by the reforms.
- 4.23 These limitations and the potential costs associated with them are summarised in Figure 4.2 below.

Figure 4.2: Potential costs of restrictions on market entry



Source: Europe Economics

4.24 Given the existence of information asymmetries as discussed in the previous section, there are clear benefits to requiring authorised legal professionals to meet certain standards. The question we explore here is whether these requirements or the way the system is currently structured creates costs by unnecessarily restricting the ability of individuals and companies (particularly ABS) to enter the market.

## Barristers

4.25 As described above, a typical course of entry for prospective lawyers includes a three-year degree in law (or other degree followed by a conversion course), postgraduate/professional training courses (for example, Bar Professional Training Course (BPTC) for barristers or Legal Practice Course (LPC) for solicitors), and practical training (for example, pupillage for barristers or training contract for solicitors).

## Pupillage places

- 4.26 According to data from the Bar Council, while applications for pupillages have risen from 2,802 in 2008/2009 to 2,865 in 2010/2011<sup>25</sup> (a two per cent increase), the number of registered pupillages has fallen by around 15 per cent. In 2007/2008, there were 562 First Six pupillages (pupillages covering the first six months of training) and 555 Second Six pupillages (pupillages covering the second six months of training). By 2010/2011, these figures had dropped to 446 (a 21 per cent reduction) and 477 (a 14 per cent decrease), respectively.<sup>26</sup> This implies that for every pupillage place available there were on average six applicants in 2010/2011.
- 4.27 These data suggest a growing discrepancy between the number of applicants and the number of pupillages available. Indeed, there is strong competition for pupillage places. Each year, BPTC graduates and those who did not obtain pupillage the previous year(s) apply for pupillage. BPTC graduates may apply for pupillage for up to five years after passing the course (keeping in mind that roughly one-third of BPTC graduates are international students returning to their home countries with no intention of applying for a pupillage).
- 4.28 The data are not sufficient to generate any firm conclusions and must be viewed in the context of the wider economic environment over the period. In particular, the UK economy has experienced long periods of negative growth since 2009. Budget cuts in legal aid have resulted in reductions in the amount of publicly funded work, particularly on criminal and family work. Growing economic pressure is also driving practitioners to request referral fees, which barristers cannot agree to. Arguably, request for referral fees is diverting family and criminal work, traditionally given to pupillage members, away from aspiring barristers to

<sup>25</sup> Bar Council, 'Statistics: Pupil barrister s'. See [www.barcouncil.org.uk/about-the-bar/facts-and-figures/statistics/#PupilBarStats](http://www.barcouncil.org.uk/about-the-bar/facts-and-figures/statistics/#PupilBarStats)

<sup>26</sup> Bar Standards Board (2011), 'An analysis of the backgrounds of pupils registered in 2009/10' See [www.barcouncil.org.uk/media/18139/pupillage\\_report\\_registered\\_2009\\_10.pdf](http://www.barcouncil.org.uk/media/18139/pupillage_report_registered_2009_10.pdf)

solicitor-advocates.<sup>27</sup> <sup>28</sup> BSB research suggests that only 16 per cent of the self-employed barristers' workload has increased in the past 12 months, while almost one in four reported that their workload had decreased over the past 12 months.<sup>29</sup>

## **Pupillage training organisations**

- 4.29 Although wider factors potentially affecting demand for barrister services may explain, at least to some extent, the shortage of pupillages, the process for becoming a Pupillage Training Organisation may also be a contributing factor. The Access to Justice Act (1999) introduced the option for those wishing to train as a barrister to do their full 12 months of pupillage in employment, as opposed to doing a pupillage entirely at the independent bar or spending six months in chambers and six months in a firm. It was anticipated that relaxing the rules in this way would help address the shortage of pupillage places available.
- 4.30 Under the rules non-chambers can apply to become Pupillage Training Organisations (PTO). Though pupillages are still driven by demand for barrister services, the system may be undermined by unduly lengthy accreditation processes for organisations to become PTOs and offer pupillages in employment. In particular, the Bar Association for Commerce, Finance and Industry (BACFI) has highlighted the existence of burdensome and lengthy accreditation processes for organisations to become Pupillage Training Organisations (PTO).
- 4.31 A total of 325 chambers and 30 employed Bar organisations together provide pupillage training. All chambers and other pupillage training organisations (PTOs) have to meet certain standards before a placement

<sup>27</sup> Bar Council (2011), 'Guidance on the Prohibition of Referral Fees' See [www.barcouncil.org.uk/media/101378/referral\\_20fees\\_20guidance\\_1\\_.pdf](http://www.barcouncil.org.uk/media/101378/referral_20fees_20guidance_1_.pdf)

<sup>28</sup> From April 2013 solicitors will also be banned from soliciting referral fees in personal injury cases.

<sup>29</sup> Pike G, Robinson D. 'Barristers' Working Lives: A Biennial Survey of the Bar 2011'. Report, Bar Council and Bar Standards Board, February 2012. Available at [www.barcouncil.org.uk/media/99583/barristers\\_working\\_lives\\_06\\_02\\_12\\_web\\_2.pdf](http://www.barcouncil.org.uk/media/99583/barristers_working_lives_06_02_12_web_2.pdf)

may be approved. An estimated 2,460 supervisors were eligible to have a pupil in 2010.<sup>30</sup>

- 4.32 Providers must advertise all pupillage vacancies on the Pupillages website, unless they apply for a specific exemption.<sup>31</sup> On 6 August 2012, this site was advertising 334 pupillages for a start year in 2013. Of these, 291 (87 per cent) were for pupillages at chambers whilst 43 (13 per cent) were for pupillages at other PTOs. A total of 147 different entities were advertising for pupillages, 133 chambers (90 per cent) and 14 other PTOs (10 per cent).<sup>32</sup>
- 4.33 If we presume that barristers in the employed bar (20 per cent of barristers) are just as interested in taking on pupillages as self-employed barristers at chambers (80 per cent), but are, for regulatory reasons deterred from becoming PTOs, then we find that pupillages are currently overrepresented at chambers. If the number of pupillages at chambers remained constant and the number offered by other PTOs increased until they represent 20 per cent of the total there would be a nine per cent increase in the number of pupillages. In other words restrictions to pupillages may be leading to fewer pupillages being offered than there might otherwise be.
- 4.34 Aspiring PTOs must apply to the Bar Standards Board Qualification Committee. The Qualifications Committee Panel normally deals with all applications within eight weeks of receipt and notifies applicants of its decision within 10 days of a decision. A £200 application fee is applicable. Aspiring PTOs will not be granted permission to provide pupillage without approved pupillage supervisors. Applications for

<sup>30</sup> Wood, Derek, John Carrier, Andrea Clerk, and Valerie Shrimplin (2009). 'From Pupillage to Professional: Is Pupillage Fit for Purpose?' UK Centre for Legal Education. UK Centre for Legal Education. See [www.ukcle.ac.uk/resources/employer-engagement/pupillage](http://www.ukcle.ac.uk/resources/employer-engagement/pupillage)

<sup>31</sup> Pupillage Portal. See [www.pupillages.com](http://www.pupillages.com), Bar Standards Board. 'Pupillage funding and advertising waivers'. See [www.barstandardsboard.org.uk/regulatory-requirements/for-chambers-and-education-providers/education-and-cpd-providers/pupillage-training-organisations/pupillage-funding-and-advertising-waivers](http://www.barstandardsboard.org.uk/regulatory-requirements/for-chambers-and-education-providers/education-and-cpd-providers/pupillage-training-organisations/pupillage-funding-and-advertising-waivers)

<sup>32</sup> Pupillage Portal [www.pupillages.com](http://www.pupillages.com)

accreditation as a pupil supervisor are made to a barrister's own Inn of Court. A period of training is required, of a recommended four to five hours, within each Inn. Approved pupil supervisors are registered with the BSB on the recommendation of the relevant Inn.<sup>33</sup>

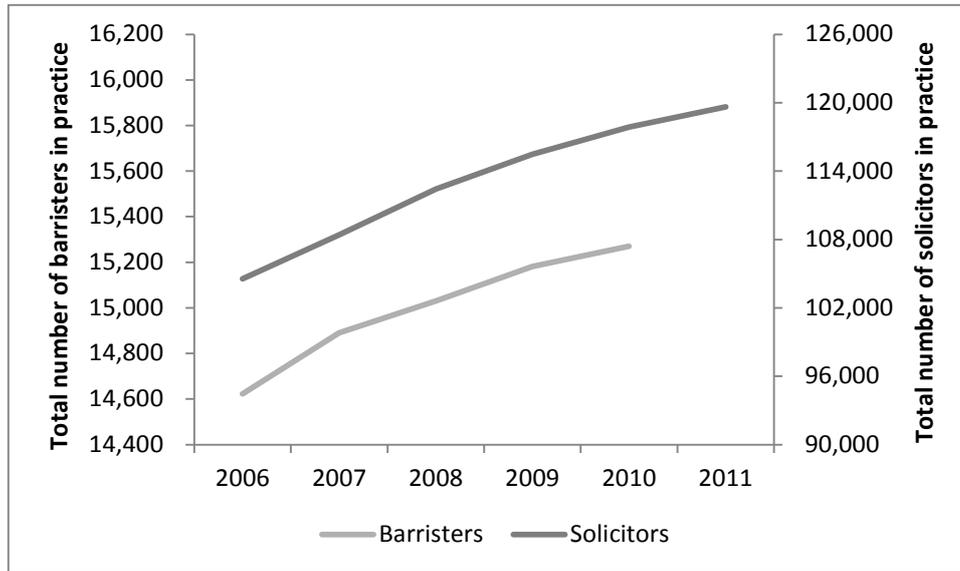
### **Comparing training arrangements for barristers and solicitors**

- 4.35 A solicitor firm must also apply to be authorised to enter into training contracts with trainees, however the application process differs. The firm applies directly with the SRA. The firm must nominate a training principal who is ultimately responsible for all training contracts, however the principal need not undertake any training himself to be nominated for this position, although he must meet minimum experience requirements. A £100 application fee is applicable.
- 4.36 A key difference in the two schemes is that pupil supervisors may only supervise one pupil at a time, whereas solicitor firms may enter into contracts with two trainees per partner or senior solicitor with a current practising certificate and four previous practising certificates. Additionally, the solicitor firm must pay for the trainees' Professional Skills Course (PSC).<sup>34</sup>
- 4.37 Between 2007 and 2011, the number of solicitors increased by on average 2.74 per cent annually. Meanwhile the number of barristers increased at a much slower rate, at 1.09 per cent annually between 2007 and 2010 (see Figure 4.3).

<sup>33</sup> Bar Standards Board (2011), Pupillage Handbook.  
[www.barstandardsboard.rroom.net/assets/documents/Pupillage%20HANDBOOK%20August%202011%20FINALc.pdf](http://www.barstandardsboard.rroom.net/assets/documents/Pupillage%20HANDBOOK%20August%202011%20FINALc.pdf)

<sup>34</sup> Solicitors Regulation Authority (2008), Training trainee solicitors - The Solicitors Regulation Authority requirements, Education and Training Unit.

Figure 4.3: Number of practicing barristers and solicitors



Source: Law Society and Bar Council Annual Reports

4.38 To become a solicitor, students must enrol with the SRA prior to taking the LPC examinations. Once they have completed their LPC, they must undertake a training contract to formally qualify as a solicitor. SRA annual reports suggest there are roughly half as many traineeships registered each year as there are students enrolled in the SRA. Both figures have declined in the last several years. In 2009/10 there were 8,098 students registered with the SRA, down from 11,558 (in the Law Society) in 2007/08 (a 30 per cent decline). There were 4,874 new traineeships registered in 2009/10, down from 6,303 in 2007/08 (a 23 per cent decline). These figures suggest a shortage in supply for traineeships. Indeed, the SRA warns that '...the number of employers able to offer training contracts may be dictated by economic factors and can be significantly lower than the number of LPC graduates...'.<sup>35</sup> Indeed according to estimates from the Law Society Annual Statistical report (2010), there were almost three times as many applicants for each available vacancy in 2010.<sup>36</sup> While a discrepancy therefore also exists

<sup>35</sup> Solicitors Regulation Authority (2012) 'SRA | Legal Practice Course (LPC) Solicitors Regulation Authority.' See [www.sra.org.uk/students/lpc.page](http://www.sra.org.uk/students/lpc.page)

<sup>36</sup> Bassett, Kate (2011) 'Law: Overview' Prospects. See [www.prospects.ac.uk/industries/law/overview.htm](http://www.prospects.ac.uk/industries/law/overview.htm)

for solicitors as for barristers in the final stage of training, the disparity between applicants and available places is smaller.

- 4.39 If we assume a similar discrepancy between applicants and places for pupillages as exist for solicitor training contracts there would be 107 per cent more pupillage places available, with the number of places available more than doubling from 462 up to 955.

### **Cost of training**

- 4.40 The cost of training to become a barrister compared to other legal professionals may further impact on the scope for entry. For example, a typical three-year law degree costs roughly £2,000 per annum, recently increased to between £5,000 to £9,000 under new fee guidelines.<sup>37</sup> Alternatively one could do a law conversion course, at a cost of between £3,000 and £9,000.<sup>38</sup> The BPTC then costs between £9,500 and £15,750 to complete.<sup>39</sup> In contrast, it costs solicitors £8,500 to £13,000 for the LPC.<sup>40</sup>
- 4.41 The Law Society of England and Wales recommends that trainee solicitors earn a minimum salary of £18,590 in central London and £16,650 outside London.<sup>41</sup> According to the Association of Graduate Recruiters (AGR), median starting salaries in 2009 were £37,000 in

<sup>37</sup> [www.lawsociety.org.uk/careersinlaw/becomingasolicitor/costs.page](http://www.lawsociety.org.uk/careersinlaw/becomingasolicitor/costs.page), [www.bpp.com/undergraduate-course-details/d/undergraduate/LLB/97](http://www.bpp.com/undergraduate-course-details/d/undergraduate/LLB/97)

<sup>38</sup> Law Society. 'The costs of qualifying'. See [www.lawsociety.org.uk/careersinlaw/becomingasolicitor/costs.page](http://www.lawsociety.org.uk/careersinlaw/becomingasolicitor/costs.page), Law Society. 'Advice for undergraduates – financial considerations'. See <http://juniorlawyers.lawsociety.org.uk/node/14963>

<sup>39</sup> Data relates to 2010/2011 fee rates. See: [www.barstandardsboard.org.uk/qualifying-as-a-barrister/bar-professional-training-course/bptc-frequently-asked-questions/#fees](http://www.barstandardsboard.org.uk/qualifying-as-a-barrister/bar-professional-training-course/bptc-frequently-asked-questions/#fees)

<sup>40</sup> Law Society. [www.lawsociety.org.uk/careersinlaw/becomingasolicitor/costs.page](http://www.lawsociety.org.uk/careersinlaw/becomingasolicitor/costs.page), <http://juniorlawyers.lawsociety.org.uk/node/14963>

<sup>41</sup> To note, the SRA has announced there will be no minimum salary requirement as of August 2014

London. Both starting salary and progression depends on the size of firm and type of work. Pupil barristers earn a minimum of £12,000 per annum, although some earn up to £40,000. Initial earnings after training range from £20,000 - £90,000.<sup>42</sup>

- 4.42 There is little to suggest, therefore, that the cost of undertaking training is significantly different for individual barristers as compared to individual solicitors.
- 4.43 There is, however, a difference in who bears the economic risk in each training model. Trainee solicitors apply to a number of firms and are usually employed on a fixed-term contract for two years, after which the firm decides whether or not to retain the trainee. The risks (for example, poor performance and associated costs) are therefore largely borne by the firm, at least during the employment period. There is, of course, a risk of unemployment following completion of a training contract. However given the larger size of solicitor firms, and thus a greater potential to manage staffing and demand risks, given the investment the company has already made on that individual there exists an incentive to retain them.
- 4.44 With pupillages, however, it is likely that the individual bears more of the risk. For instance, limits on places makes it much more difficult to obtain a pupillage than a training contract, and the aspiring barrister will be required to invest substantially in his/her education with less certainty that he/she will be employed as a pupil at the end of it. Additionally, since barristers are self-employed, not only is there no guarantee of employment from the pupil master at the end of the pupillage, but also for success self-employment requires a network and reputation which may only be obtained in time. As a result, the career prospects and more importantly future income stream of a barrister pupil are less certain than for a trainee solicitor. Though this may be offset to some extent but higher subsequent earnings (high risk-high reward).

<sup>42</sup> 'Law: Overview' [www.prospects.ac.uk/industries/law/overview.htm](http://www.prospects.ac.uk/industries/law/overview.htm)

## Implications

- 4.45 These findings do not provide a definitive indication that the market needs to be altered. A full study of the market for barristers and the training process would be required to draw any firm conclusions in this respect. Furthermore, the introduction of ABS and increased direct access for consumers to barristers may create a rise in demand for barrister services and increase the number of pupillage places available. Since ABS are still in their infancy and most remain in the application process it is too early to explore whether or not this is the case. It is an issue that could be monitored going forward. The report from the LETR at the end of 2012 will also provide a more detailed analysis of training provision and future requirements.
- 4.46 Indeed, feedback from student members of the Law Society highlights key effects that ABS may have on access to the profession. Raikundalia (2011) explains that postgraduate courses such as the LPC and PSC are tailored for a single employer-category – the large London based firm. For example, the lack of sandwich courses whereby students can work for firms whilst completing the postgraduate course may discourage entry into the profession. Thus, the entrance of large players in the High Street arena under the ABS system may help introduce more flexibility in the market. Equally, where large multi-disciplinary firms (for example, the Big Four accounting firms) choose to provide legal services parallel to their existing services, these firms may offer funding or study loans to their graduates as a means to attract the highest performers.<sup>43</sup>
- 4.47 In contrast, Barnes (2011) argues that access will not be driven by the entrance of big brand names but by existing law firms which, with access to external funding, may expand beyond the limitations set by partners' funds and debts, thereby improving access to aspiring

<sup>43</sup> Raikundalia, S (2011): What effect will alternative business structures have on access to the profession? *Law Society*. See <http://juniorlawyers.lawsociety.org.uk/files/essay-comp-2011-sheena-raikundalia.pdf>

solicitors.<sup>44</sup> Robinson (2011) provides a more general perspective, saying that ABS will increase the number and/or size of players in the market, as well as a greater diversity of business structures. The presence of non-traditional enterprises (for example, the Co-operative Legal) may encourage students of non-traditional backgrounds (those lacking financial support, elite degrees and family connections) to pursue a career in law.<sup>45</sup>

- 4.48 Some comments in our interviews suggested that the high level of qualifications required are not necessary for many of the services provided, and that obtaining pupillage (barristers) or training contracts (solicitors) limits the growth of qualified personnel. A review of whether or not training requirements are excessive goes beyond the remit of this study. However, such a suggestion, alongside the large numbers not finding pupillages, the high cost of training given that the trainees bear the risk, the current debate within industry over activity-based regulation, and changes in the wider regulatory environment of the legal profession (for example, abolition of referral fees), suggest that these may be issues warranting further examination following the forthcoming report on legal education and training by LETR.

## Entity level

- 4.49 At the firm level a major change introduced by the Act was the scope for multi-disciplinary practices (MDPs). Initially these took the form of Legal Disciplinary Practices (LDPs) – bringing together lawyers and non-lawyer managers to provide legal services – and more recently ABS – allowing professionals from different sectors to work alongside each other. This process is still in the early stages: ABS have only been allowed since October 2011 and the first regulator authorised to license

<sup>44</sup> Barnes, A (2011): What effect will alternative business structures have on access to the profession? *Law Society*. See <http://juniorlawyers.lawsociety.org.uk/files/essay-comp-2011-alex-barnes.pdf>

<sup>45</sup> Robinson, C (2011): What effect will alternative business structures have on access to the profession? *Law Society*. See <http://juniorlawyers.lawsociety.org.uk/files/essay-comp-2011-christopher-robinson.pdf>

ABS was only established in May 2011. The SRA only opened to applications for authorisation on 3 January 2012. This makes it difficult fully to assess the extent to which the benefits of the current system may be undermined by any limitations on access, in particular the extent to which lengthy processes and regulatory requirements may exist.

- 4.50 The LSB (2011)<sup>46</sup> account of market trends found that by June 2011 there were 393 registered LDPs,<sup>47</sup> only 3.7 per cent of all firms in England and Wales. One of the reasons behind this relatively low take-up may have been anticipation of more flexible ownership arrangements offered through the then pending liberalisation of ABS. Large firms might have also refrained from applying due to lower requirements for capital as well as concerns that foreign regulatory regimes may prohibit members practicing through LDP-type structures. Indeed, according to LSB (2012)<sup>48</sup> over 180 applications to become an ABS had been received by the SRA by end of March 2012.
- 4.51 There are currently only two licensing authorities for ABS, the SRA and the CLC. As of 1 August 2012 16 ABS had been authorised by these two bodies, 14 by the SRA and two by the CLC.<sup>49</sup>

<sup>46</sup> Legal Services Board (2011) 'Research note: The legal services market' See [www.legalservicesboard.org.uk/news\\_publications/latest\\_news/pdf/research\\_note\\_on\\_the\\_legal\\_services\\_market.pdf](http://www.legalservicesboard.org.uk/news_publications/latest_news/pdf/research_note_on_the_legal_services_market.pdf)

<sup>47</sup> 220 of these had non-lawyer managers – equivalent to just over half (56 per cent) of all LDPs.

<sup>48</sup> Legal Services Board (2012) 'Market impacts of the Legal Services Act – Interim Baseline Report' See [www.legalservicesboard.org.uk/what\\_we\\_do/Research/Publications/pdf/market\\_impacts\\_of\\_the\\_legal\\_services\\_act\\_interim\\_baseline\\_report.pdf](http://www.legalservicesboard.org.uk/what_we_do/Research/Publications/pdf/market_impacts_of_the_legal_services_act_interim_baseline_report.pdf)

<sup>49</sup> Solicitors Regulation Authority. 'SRA Licenses 15<sup>th</sup> ABS' 6 Aug. 2012. See [www.sra.org.uk/sra/news/press/sra-licenses-15th-abs.page](http://www.sra.org.uk/sra/news/press/sra-licenses-15th-abs.page). Council for Licensed Conveyancers. 'CLC issues second ABS license.' 6 Jul. 2012 See [www.conveyancer.org.uk/News32.php](http://www.conveyancer.org.uk/News32.php). To note, by mid-September 2012 this had risen to five ABS authorised by the CLC and 32 ABS authorised by the SRA. This report and any estimates or analysis of new ABS relies on information on the 16 ABS that had been approved as of 1 August only.

- 4.52 Feedback from regulators and industry, however, indicates that there could be challenges with the application process both at the licensing body level and at the ABS level. The process of becoming a licensing authority can be lengthy and time consuming for senior staff. This may serve to limit the number and types of bodies that take on this role — potentially limiting the scope for competition at the licensing level.
- 4.53 Whether or not this would ultimately restrict entry at the firm level is unclear, though the fewer the licensing authorities the more limited the range of ABS may be, particularly if authorising bodies focus on specific types of ABS in their licensing regime. For example, the BSB is currently exploring the potential to become a licensing authority for ABS (they are expected to submit an application towards the end of the year). It is unlikely that they will replicate ABS scheme set up by others, such as the SRA, rather the focus will be on ABS providing an alternative structure to carry out the same type of work as currently self-employed barristers.
- 4.54 At the firm level, evidence from recent applicants suggests that the application process can take between 10 and 18 months to complete — depending on the nature of the application. Based on feedback from industry and data on the cost of time,<sup>50</sup> we estimate that it costs between £27,000 and £160,000 more to gain authorisation to become an ABS than to gain authorisation under the traditional model.<sup>51</sup> This is a

<sup>50</sup> Salary data from the Law Society of Scotland are used due to the availability of more up to date survey data (2011). The most recent similar salary figures for England, published by the Law Society, are from 2008 (see: [www.lawsociety.org.uk/secure/file/180549/e:/teamsite-deployed/documents/templatedata/Publications/Research%20fact%20sheet/Documents/salarydata08\\_v1.pdf](http://www.lawsociety.org.uk/secure/file/180549/e:/teamsite-deployed/documents/templatedata/Publications/Research%20fact%20sheet/Documents/salarydata08_v1.pdf))

<sup>51</sup> This estimate includes salary costs, additional systems costs, external costs and application costs. Cost of entry as a law firm are calculated as salary costs and SRA new company authorisation costs. The range of the estimate is influenced by differences in the size of firms gaining authorisation to become an ABS, with costs to larger firms higher than for smaller firms. For instance, the application cost charged by the SRA is dependent on applicant size, leading to differences of more than 10 times between the cost of applying for small firms and large firms. Similarly, salary costs of applying were found to be five times greater for a large firm than a small firm.

substantial increase. Further cost could be incurred if it is necessary to be authorised by more than one regulator.

- 4.55 This estimate must, however, be taken in context. In particular, the development of ABS and the application procedures are still in the early stages and high costs may in part reflect a learning process. As such this may overestimate the cost of becoming an ABS in the medium to long term.
- 4.56 More generally, feedback suggests that financial standing and compliance procedures represent particularly onerous requirements for a new entrant (including ABS) and for businesses wishing to expand their service provision. These have become more onerous since the introduction of the Act. Meanwhile, businesses wishing to expand their service provision are being hampered by requirements on management structures (this is apparently less of a problem for new entrants).

## Conclusions

- 4.57 In this section we consider if and how the current regulations are restricting entry into the market for legal services. We focus particularly on any unnecessary burdens on new entrants and training requirements relating to the barrister profession.
- 4.58 We note that a key feature of the legal services market is the need to regulate the provision of certain services, known as reserved activities. While this enhances consumer welfare the associated restrictions may create scope for consumer harm. In particular we identify certain processes for becoming authorised to provide training to barristers and the application processes for becoming ABS and ABS licensing bodies as being potential sources of harm.
- 4.59 We find that for every pupillage place there are on average six applicants, compared to a three to one ratio for solicitor training contracts. While pupillage places are driven by market demand for barristers, the process of becoming a Pupillage Training Organisation may be limiting access to the market.

- 4.60 Using data on the relative proportion of practising barristers that are in employment versus those that are self-employed, we estimate that there could be potentially nine per cent more pupillages than are currently being offered with in-employment pupillages being under represented. If we assume a similar discrepancy between pupillage places and applicants as exist for solicitors seeking training contracts, we estimate that there would be more than double the current number of pupillages available.
- 4.61 While this does not prove that unnecessary barriers to entry exist for barristers, it does suggest that the area could warrant further exploration. The introduction of ABS may help to alleviate the shortfall in pupillage places by introducing more flexibility in the market and external funding. This is an issue that could be monitored going forward. The report from the LETR at the end of 2012 will also provide a more detailed analysis of training provision and future requirements.
- 4.62 There is a current debate about moving from the traditional title based qualification and regulatory model to an approach based on qualification for specific activities. This could improve risk based regulation and allow greater flexibility for firms to enter the market. Such issues may also warrant further exploration following the forthcoming report on legal education and training by the LETR.
- 4.63 At the entity level the introduction of ABS has removed a key barrier to market entry identified initially by the OFT (2001) and later by Clementi (2004). The policy is still in the early stages of development ABS having only been allowed since October 2011 and the first licensing body having only been established in May 2011. As a result only 16 ABS had been approved at the time of this study. So far the emphasis of the new ABS has been on making non-lawyers partners and increasing their offering of legal services, for example moving into reserved legal activities.
- 4.64 Data on the application processes, both at the licensing authority level and the firm level are limited. However, based on feedback from industry we estimate that on average it costs between £27,000 and £160,000 more to gain authorisation as an ABS compared to the traditional model and can take 10 – 18 months to complete. It is however important to

view these estimates in the context of the very recent introduction of the application process — there could be an element of learning by doing which would suggest that our figures overestimate the cost in the medium to long term.

- 4.65 Overall, while there appear to be no clear barriers to entry for ABS, it remains an open question whether the time and cost of applications is acting as a deterrent. This remains an area that may warrant monitoring in the future given the relative novelty of the reforms.

## **5 REGULATION OF ABS**

### **Introduction**

- 5.1 As discussed in Section 2 and the previous section ABS were introduced under the Act, largely in an attempt to reduce restrictions on market entry and improve consumer access to barristers.
- 5.2 In this section we consider the extent to which duplicative and/or conflicting regulations relating to the operation of ABS are undermining the benefits of such business structures. In particular we seek to identify circumstances in which the simultaneous regulation of ABS by a number of regulators may have an adverse impact on innovation and the efficiency of ABS' operations and ultimately reduce the benefits consumers derive from the existence of multi-disciplinary 'one-stop-shop' businesses, and examine the extent to which this is the case and the implications for consumer welfare.
- 5.3 We first identify the scope for such regulatory duplication and the existence of unregulated areas based on the mapping from the previous section. We use this to construct the analytical framework, describing the mechanisms through which such restrictions may impact on consumer welfare.
- 5.4 We then present our analysis of the empirical and qualitative information collected via the surveys and interviews. We assess the extent to which the potential detriment identified in the analytical framework may have materialised and thus the extent to which they are eroding the anticipated benefits of introducing ABS.

### **Potential benefits and costs of ABS**

#### **Potential benefits**

- 5.5 As described earlier the benefits of ABS were chiefly aimed at improving market entry. The benefits were explored by the Ministry of Justice in the 2006 impact assessment. In particular it identified:
- better scope for risk sharing among new entrants

- access to a wider pool of capital due to allowing external investment
- increases in efficiency by market valuation that follows from floating a stake in the stock market, and
- a better ability to compete internationally.

5.6 The scale of these benefits may be expected to vary depending on the size of the organisation and the range of services they offer. For example smaller businesses would be less likely to operate on an international level.

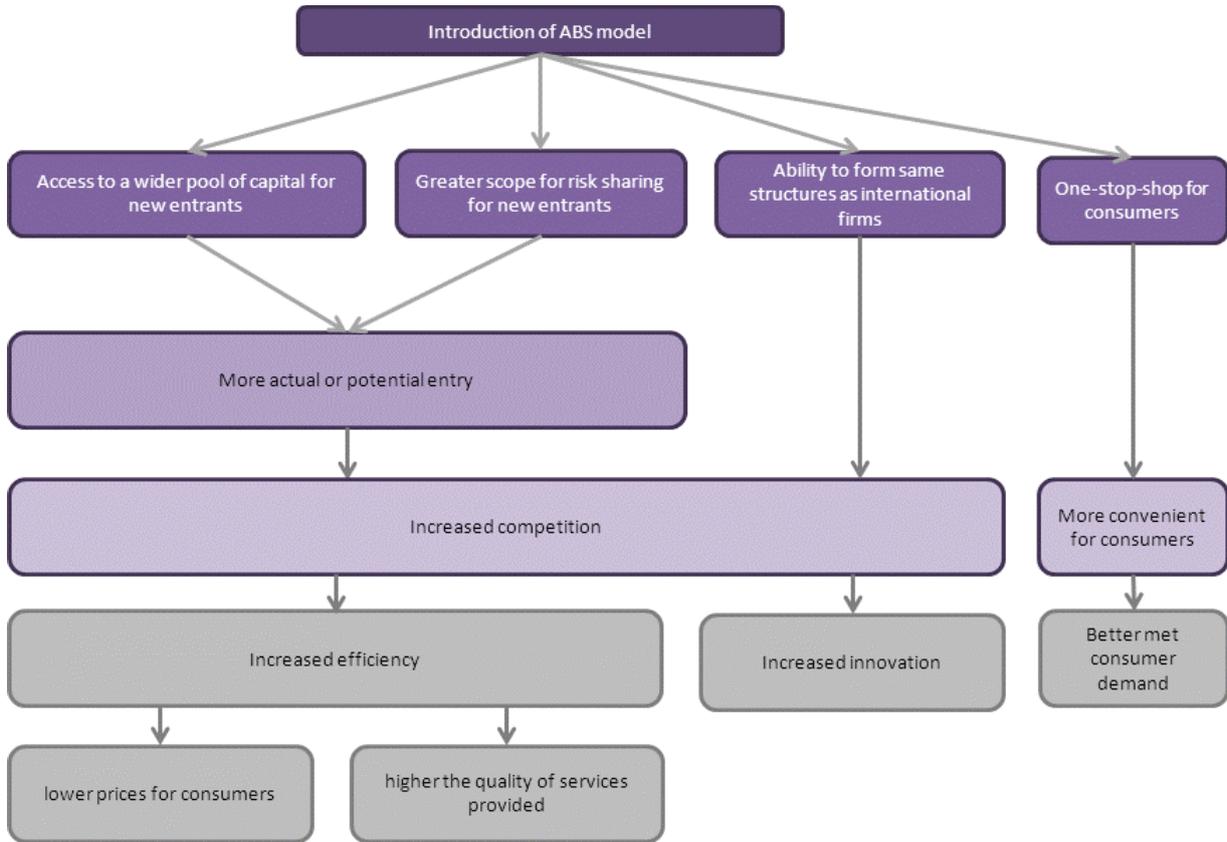
5.7 In turn these effects would increase competition between existing suppliers and potential competition from new suppliers and forms of supply. Ultimately this was expected to result in greater efficiency in the sector and more innovation. Consumers would benefit from lower prices and/or higher quality service provision.

5.8 In addition to these competitive benefits, the introduction of ABS was also expected to offer greater convenience for consumers seeking a one-stop shop.

5.9 Wider potential benefits identified included, an increase in training opportunities for law students from under-represented groups, and the provision of types of legal services currently not financially viable due to the increased efficiencies from information sharing with other business areas.

5.10 The potential benefits for consumers are illustrated in Figure 5.1 below.

**Figure 5.1: Potential benefits for consumers of ABS structures**



Source: Europe Economics

5.11 It is not within our remit to attempt to replicate the original Impact Assessment and estimate the benefits of ABS. Given the relative novelty of ABS there is little new information in this respect. Despite the fact that to date the ABS that have been approved have generally not altered their service offering, and all have restricted their business to legal services, there is nothing to suggest that the type of multi-disciplinary practices originally envisaged will not appear. As such there is no indication that the anticipated benefits will not be realised. Rather we focus, here, on the scope for any such benefits to be eroded by the way in which the system has been set up.

### Potential costs

5.12 Potential issues with the current system for regulating ABS may be undermining the realisation of such benefits. Potential costs were identified as part of the 2006 impact assessment. The costs identified by the MoJ included:

- a risk of confusion and increase in compliance costs for ABS firms, and an increase in operational costs for regulators in order to coordinate regulation across regulators and resolve issues of conflicting, overlapping or inadequate regulation
- a risk of disclosure of clients' confidential information due to outside ownership, and
- the possible withdrawal of several small firms who would become inefficient with the coming of ABS firms.

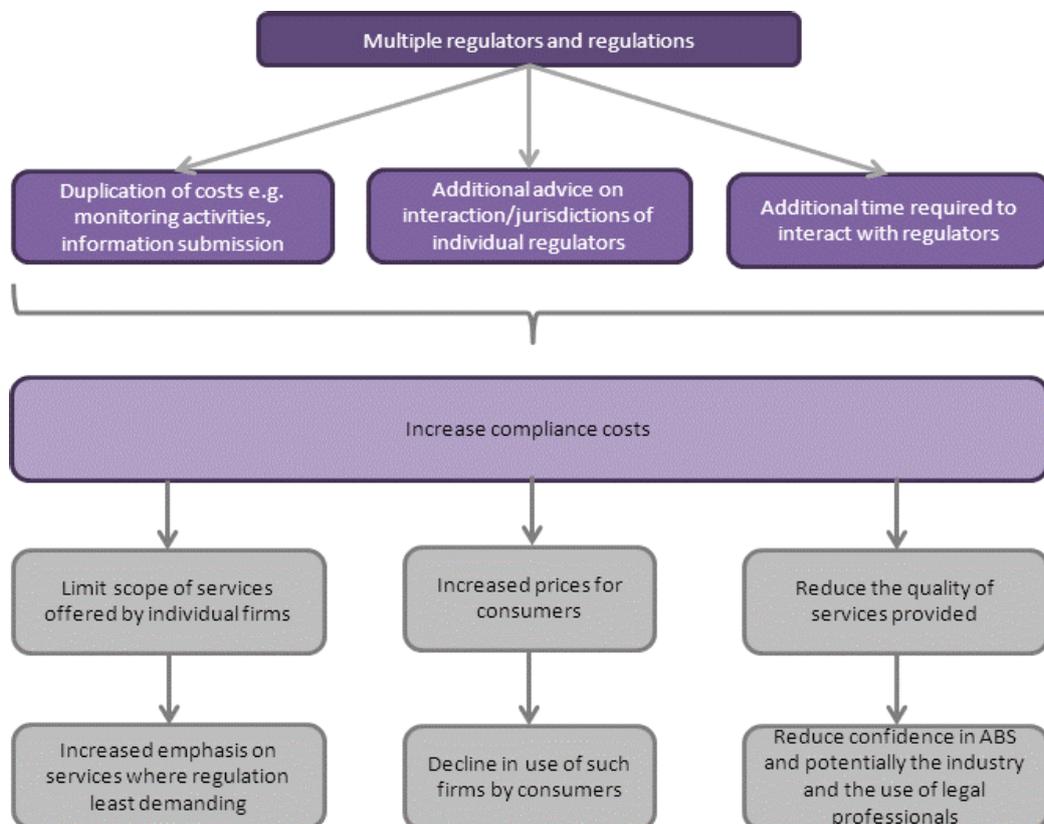
5.13 In our interviews concerns were expressed about the position of barristers operating within an ABS. In particular, it was suggested that by working within business entities like ABS, no two barristers within one entity would be able to represent both sides of a case due to conflicts of interest, potentially undermining the benefits of increased consumer access, as consumer choice could be reduced.

5.14 One thing is certain, however; as illustrated by the regulatory mapping exercise in section 2, risks do exist for regulatory duplication. Specifically, ABS that offer reserved services and/or regulated unreserved services will be regulated by a legal services regulator. In addition to this, an ABS that provides financial advice, for example, alongside legal service will be regulated by the FSA. As regulation takes place both at the service and individual level, the types of professionals that work within the ABS will also determine which and how many regulators the organisation as a whole must be mindful of.

5.15 Since ABS can provide multiple services there is significant scope to be regulated by more than one regulator and a variety of legislation. This could result in higher compliance costs compared to situations in which an organisation is regulated by a single regulator. In particular, there could be a duplication of costs (for example, monitoring activities), inconsistent advice between regulators and time spent abiding by multiple rules. These additional compliance costs could be passed onto consumers by reducing the scope and/or quality of services provided, or through higher prices.

5.16 These potential costs and the associated impacts are summarised in Figure 5.2 below.

**Figure 5.2: Potential costs of current system for regulating ABS**



Source: Europe Economics

### To what extent is multiple regulation an issue?

5.17 While the benefits of ABS were discussed at length in the original Impact Assessment, we explore here whether the regulatory structure under the Act may undermine these benefits by creating additional compliance costs that cause companies for example to limit the scope of services they offer or affect the price or quality of services offered.

5.18 There are two types of regulatory overlaps:

- vertical overlaps – where the authorised person is regulated by a body which is regulated by a second body

- horizontal overlaps — where the authorised person is regulated by two bodies.

5.19 Horizontal overlaps are the primary concern in this context. Within this group there are two further distinctions:

- multiple regulation of the individual — an authorised individual working in an LDP or ABS may be regulated at the entity level by a different body than they are at the professional level, and
- multiple regulation of the entity — an ABS may be regulated at the entity level by more than one body, in addition to any distinct regulation at the individual level.

### **Multiple regulation of the individual**

5.20 Multiple regulation at the individual level does not appear to be a significant challenge — all employees of a law firm are bound by the regulator of that law firm. A second body generally only becomes involved if disciplinary action has to be taken against an individual, whereupon the relevant approved regulator for the individual may be required to intervene.

5.21 While legal professionals in the more niche areas may find themselves regulated by more than one approved regulator, this seems to be less of an issue for professionals working as solicitors and barristers. For example, the Faculty Office estimates that '80 per cent of their members (713 out of 885) are solicitors and, as such, regulated by the SRA as well'.<sup>52</sup> Similarly, data from the Legal Services Board suggest that currently more than 25 per cent of licensed conveyancers and legal executives are subject to more than one LSB approved regulator, compared to less than 10 per cent of solicitors and barristers (the largest group of legal professionals).

<sup>52</sup>Nick Smedley (2011), 'The smaller approved regulators: An assessment of their capacity and capability to meet the requirements of the Legal Services Act 2007, with analysis and recommendations', submitted by Nick Smedley to the Legal Services Board, June 2011

- 5.22 The CLC acts as a principal legal regulator for relevant ABS and LDPs, however solicitor managers and owners of these entities are also regulated by the SRA and Chartered Legal Executives are regulated by the IPS. Additionally, the CLC is authorised (and itself supervised by) the FSA to regulate CLC practices acting as intermediaries in the provision of financial services incidental to the provision of conveyancing and probate services. Similarly, the CLC supervises CLC Practices in Anti-Money Laundering processes (subject itself to the supervision of HM Treasury).
- 5.23 Although the BSB does not regulate entities, barristers regulated by the BSB are permitted to practise as employees or managers of entities regulated by other approved regulators. Currently 50 barristers are recorded as being managers of what its Code calls 'recognised bodies' (for instance, LDPs regulated by other approved regulators). Currently no barristers are recorded as being managers of 'licensed bodies' (for instance, ABS firms). Managers are defined as partners in partnerships, members of LLPs or directors of companies. It is likely that these firms will be regulated by the SRA. There are no data on how many barristers are simply employees of LDPs or ABS. Industry feedback suggests that there is little appetite amongst barristers to join ABS, as many barristers enjoy their self-employed status.
- 5.24 The Bar Standards Board (BSB) is currently consulting on a new Code of Conduct, which if approved would enable it to regulate both barrister only entities (BOEs) and legal disciplinary practices (LDPs).
- 5.25 The CLC has regulated Recognised Bodies since 2000 which are permitted to be wholly owned by non-lawyers and managed by non-lawyers provided (since 2009) that at least one manager is a licensed conveyancer. The CLC has also permitted other lawyers to own and manage Recognised Bodies, provided that at least one manager is a licensed conveyancer. For these purposes, the CLC has treated the Recognised Bodies it regulates as LDPs.

### **Multiple regulation of the entity**

- 5.26 While multiple regulation at the individual level is fairly commonplace, the introduction and growth of ABS will add an additional dimension by creating the scope for multiple regulation at the entity level.

5.27 According to the LSB, much of the duplication and challenges to avoid duplication stretch across regulators outside of legal services. To this end, the LSB have produced a memorandum of understanding<sup>53</sup> aimed at facilitating information sharing between regulators to avoid harmful effects of regulatory overlap. Various sections of the Act are important here. Section 52 addresses regulatory conflicts between approved regulators, stating that the entity requirement prevails over the individual requirement. A common example includes a legal executive working within a SRA regulated solicitor firm. Meanwhile, Section 54 deals with regulatory conflicts outside of the approved regulators, for example dual SRA/FSA regulated entities, stating that regulatory arrangements of an approved regulator must make provisions for coordination between regulators as is reasonably practicable. Individuals working both as a notary and a solicitor are also relevant, however there are few of them. A study by Centre for Consumers and Essential Services (CCES) in 2011<sup>54</sup> estimates that around 70 solicitors' firms are dual regulated by the FSA and SRA.

5.28 An estimated 180 entities had applied for ABS status by the end of March 2012, and as of 1 August 16 ABS had been authorised. Based on available information on the existing ABS the range of services offered by individual ABS varies dramatically with some becoming ABS simply to allow a non-lawyer partner, with no substantive change in their service offering, while others have diversified into reserved activities that they historically out-sourced. To date the ABS that have been authorised, however, all remain within the legal services context. As such they are likely to fall within the scope of only the authorising body (for instance, the SRA or CLC). Whether or not this will vary going forward is unclear. Nonetheless, we pose the question as to whether any additional cost of complying with an extra regulator may limit the scope of services offered

<sup>53</sup> Solicitors Regulation Authority 'Agreement allows more information sharing'. 3 May. 2012  
See [www.sra.org.uk/sra/news/press/memorandum-understanding-signed.page](http://www.sra.org.uk/sra/news/press/memorandum-understanding-signed.page)

<sup>54</sup> Centre for Consumers and Essential Services (2011) 'Mapping potential consumer confusion in a changing legal market- report for the Legal Ombudsman' *University of Leicester*, See [www.legalombudsman.org.uk/downloads/documents/publications/Consumer\\_confusion\\_report.pdf](http://www.legalombudsman.org.uk/downloads/documents/publications/Consumer_confusion_report.pdf)

by ABS or result in higher fees, undermining the benefits of such structures to consumers.

### **Estimated cost of multiple regulators to ABS**

- 5.29 It is important to distinguish between one-off and on-going compliance costs. One-off costs are those that are only incurred once (for instance, in making the transition to becoming an ABS), for example changes to systems and processes required for compliance under the relevant regulations. On-going costs are those that are continuous as a result of being subject to a new regulator (for instance, that will be incurred on a recurring basis) such as reporting or administrative costs.
- 5.30 The additional one-off compliance costs associated with becoming an ABS are largely addressed in the previous chapter on market entry (estimated at an additional £27,000 to £160,000 to gain authorisation as an ABS). As such we focus primarily on on-going costs of compliance here. One aspect of one-off costs of compliance that has not been addressed, however, is the scope for different regulators to require different processes/codes of conduct, which could require an ABS to establish two differing systems for conducting their work.

### **Sources of on-going compliance costs**

- 5.31 For each regulator, the ABS faces or will face certain types of on-going costs of compliance, primarily:
- an annual registration fee
  - annual reporting requirements
  - annual CPD requirements
  - monitoring.
- 5.32 The scale and cost associated with each of these core compliance functions will vary by regulator. Some regulators rely on more informal interaction with the regulated entities, while others require more formal interaction. It is not clear, however, that the compliance burden would differ greatly under the different approaches.

- 5.33 In addition to the basic fees certain regulators may also require authorised entities to pay for professional liability insurance and contribute to a compensation scheme. These would represent additional on-going compliance costs.
- 5.34 Though the registration fee would not differ for firms of a similar size, the scale of any additional on-going compliance costs will be affected by the extent and nature of any regulation they were subject to prior to becoming an ABS, due to the additional administrative and procedural requirements. For example a firm that was originally completely unregulated may face higher additional compliance costs compared to one already subject to some form of regulatory oversight which required them to meet certain standards and abide by a specified code of conduct.
- 5.35 For instance, in the case of barristers there are no entity costs as barristers are self-employed and share administration costs within chambers only. Costs of compliance for barristers are primarily related to practising certificates. Barristers must acquire a practising certificate on an annual basis, the cost of which reflects the cost of regulating them. The chambers is required to submit information on an annual basis regarding compliance and first-tier complaints handling to the Bar Standards Board, and a sample is required to provide more in-depth feedback in order to ensure accuracy. The emphasis is on more informal contact with barristers, though it is not clear that this is any less burdensome than for authorised persons regulated in a more formal way.
- 5.36 Meanwhile, a company that has previously been unregulated (though may be subject to some form of voluntary regulation) would ex ante face much lower costs of compliance, if indeed any at all. For example a will-writing company may or may not be a member of the Institute of Professional Willwriters (IPW). If it is, it would already be required to comply with the IPW code of conduct (approved by the OFT). The company would also already face an annual fee and be required to submit certain information on an annual basis. As such, though the cost of compliance may not be as high as under a formal regulatory regime, they would already face some cost of compliance and may already have systems and processes in place that would require little modification to meet the standards of formal regulators. In contrast a company

previously subject to no such regime would face higher additional costs when becoming an ABS. Industry estimates that annual compliance costs for an ABS could be 10 per cent higher than under the previous regulatory regime. One of the drivers of this change in the cost of compliance was identified by an industry source as the change in number of regulators reported to.

- 5.37 Equally companies that invest more in installing time-saving systems at the outset, though they incur higher one-off costs, would be likely to experience lower on-going compliance costs. Research from other sectors indicates that initial investment in automated systems tends to be more common in larger organisations, where such outlays may be more relevant given the scale of the compliance task and firms have access to the finance to pay for such projects.<sup>55</sup> The continuing development of IT and open source material may, over time, reduce this distinction.

### **Estimates of the additional on-going compliance cost**

- 5.38 Estimating the additional compliance cost is complex, not least because fees are generally based on an individual organisation's turnover. Table 5.3 below illustrates the rates charged by the SRA and CLC. Meanwhile the BSB charges fees on the basis of seniority, with a junior barrister paying in the range of £60 to £67, and a senior barrister contributing upwards of £1,000.<sup>56</sup>

<sup>55</sup> See for example Europe Economics (2009), 'Study on the Cost of Compliance with Selected FSAP Measures', a report for DG Internal Market

<sup>56</sup> To note these fees are accurate as of July 2012. The Bar council is currently reviewing the fee arrangements, however.

**Table 5.3: Fee rates for regulators**

Turnover	CLC	SRA
£0 - £19,999		£100 + 0.80% of turnover
£0-£100,000	1.4% of turnover	
£20,000 - £149,999		£260 + 0.47% of turnover > £20,000
£100,001-£500,000	£1,400 + 1.3% of turnover > £100,000	
£150,000 - £499,999		£871 + 0.46% of turnover > £150,000
£500,000 - £999,999		£2,481 + 0.44% of turnover > £500,000
£1,000,000 - £2,999,999		£4,681 + 0.41% of turnover > £1,000,000
£500,001-£3,000,000	£6,600 + 1.1% of turnover > £500,000	
> £3,000,000	£34,100 + 1.0% of turnover > £3,000,000	
£3,000,000 - £9,999,999		£12,881 + 0.28% of turnover > £3,000,000
£10,000,000 - £29,999,999		£32,481 + 0.24% of turnover > £10,000,000
£30,000,000 - £69,999,999		£80,481 + 0.22% of turnover > £30,000,000
£70,000,000 - £149,999,999		£168,481 + 0.20% of turnover > £70,000,000
£150,000,000 - £9,999,999,999		£328,481 + 0.07% of turnover > £150,000,000

Source: CLC Fees Framework 2011 and SRA 2011/2012 fee structures

5.39 Based on feedback from industry we assume that, on average:

- an organisation will need to invest one to two days of a full time employee to put together the annual report

- each legal professional is required to complete 13 hours of Continuous Professional Development (CPD) each year <sup>57</sup>
- an organisation is inspected by the regulator once every three years, and
- professional indemnity insurance is required (though contributions to compensation funds are not necessarily).

5.40 Given these assumptions and data from the Law Society of Scotland regarding the cost of time of legal professionals,<sup>58</sup> we estimate the average annual cost of compliance per regulator (excluding the required fee and any insurance or compensation contributions) to equate, depending on the size of the organisation, to between £900 and £2,100.

## Implications

5.41 As part of the survey of industry regulators and complaint handlers we sought feedback on potential methods for reducing the costs of multiple regulators having power over ABS. It was suggested that firms may find it easier to keep legal services and financial services separate, for example, as full integration would complicate compliance, although integration may be the most efficient business model.

5.42 There is no evidence at this stage to suggest that these additional costs of compliance have influenced decisions in terms of which services to provide. Feedback from industry suggests rather that to date these have primarily been commercial decisions by organisations keen to offer a broader range of services that complement their original offering. Eight of the first 16 ABS, or 50 per cent, also appear only to have changed their organisation in terms of management or ownership; the services offered have not changed. One explanation for this is that the application

<sup>57</sup> Average of CPD requirements for SRA (16 hours), CLC (six-16 hours), IPW (six-20 hours) and BSB (12 hours). CPD requirements lead to both costs of CPD courses as well as lost earnings from time attending.

<sup>58</sup> The Law Society of Scotland, Benchmarks and Cost of Time report. Available at: [www.lawscot.org.uk/media/494553/benchmarks\\_and\\_cost\\_of\\_time\\_survey\\_2011.pdf](http://www.lawscot.org.uk/media/494553/benchmarks_and_cost_of_time_survey_2011.pdf)

process for ABS seeking to diversify services takes longer, and so non-lawyer partner requests have tended to be approved first.<sup>59</sup> As more applications are processed the landscape in terms of the range of services offered by ABS may well change.

- 5.43 There is also no evidence at this early stage to indicate that fees have increased as a result of any additional compliance costs. Price information is very limited and clearly the small number of ABS currently in operation are unlikely to influence aggregate price data. That said, data from the ONS experimental prices index (based on 161 legal practices),<sup>60</sup> Guideline Hourly Rates (GHRs) determined by the Master of the Rolls for Civil Costs,<sup>61</sup> and an annual hourly rates survey of larger corporate solicitors firms, undertaken by Jim Diamond (JDS),<sup>62</sup> indicates there is evidence of only a small percentage increase in hourly rates between 2007/8 and 2010/11.<sup>63</sup> Similarly, research conducted by Charles River Associates in 2010 indicated that average conveyancing fees for private consumers remained largely constant between 2003 and

<sup>59</sup> Note all LDPs with non-lawyer partners are automatically required to apply for ABS.

<sup>60</sup> Legal Services Board (2012) 'Market Impacts of the Legal Services Act – Interim Baseline Report'. Page 58. April 2012. Report available at The ONS index measures the cost of legal services delivered by all types of legal service providers with more than 10 employees, to business consumers of legal services. This index reports a 2.8 per cent increase in prices between 2009/2010 and 1.5 per cent for Q1 2010/11. Report available at [www.legalservicesboard.org.uk/what\\_we\\_do/Research/Publications/pdf/market\\_impacts\\_of\\_the\\_legal\\_services\\_act\\_interim\\_baseline\\_report.pdf](http://www.legalservicesboard.org.uk/what_we_do/Research/Publications/pdf/market_impacts_of_the_legal_services_act_interim_baseline_report.pdf)

<sup>61</sup> Legal Services Board (2012) 'Market Impacts of the Legal Services Act – Interim Baseline Report'. Page 58. April 2012.

<sup>62</sup> Legal Services Board (2012) 'Market Impacts of the Legal Services Act – Interim Baseline Report'. Page 58. April 2012.

<sup>63</sup> To note these price measures relate mainly to prices paid by business consumers, as opposed to individual consumers.

2010, although this is in the context of a wider economic downturn and depression of the housing market in the UK.<sup>64</sup>

- 5.44 Given that existing ABS are relatively new and remain limited to legal services (as highlighted earlier) this is not necessarily surprising, and may change in the future.

## Conclusions

- 5.45 In this section we consider ABS, specifically the extent to which duplication of regulation or conflict between regulations may undermine the benefits of such business structures. In particular we identify the scope for regulatory overlaps, both in terms of:

- the regulation of the professional, and
- the regulation of the entity.

- 5.46 While multiple regulation of the individual is not a new phenomenon, and unlikely to raise any significant issues, multiple regulation at the entity level would be a new dimension resulting from the option for ABS to offer both legal and non-legal services. Having to engage with multiple regulators could substantially increase compliance costs and potentially result in higher prices for consumers, lower quality service provision or even limit the range of services offered, undermining the concept (and benefits) of a one stop shop for consumers.

- 5.47 We find that so far — for the first 16 ABS — multiple regulation does not appear to pose an issue, since to date the new ABS have not tended to extend their service offering beyond legal services. Given that LDPs with non-lawyer partners are obliged to apply for ABS status this trend is likely to continue in the short-term at least. That said, an estimated 180 entities had applied for ABS status by March 2012. Over time we may see the emphasis shifting away from simple ownership changes to ABS that represent more the diversity envisaged at the policy development

<sup>64</sup> Legal Services Board (2012) 'Market Impacts of the Legal Services Act – Interim Baseline Report'. Page 59. April 2012.

stage. For those seeking to diversify their service offering the application process is likely to take longer.

- 5.48 We estimate that the on-going costs of compliance for each additional regulator would be between £900 and £2,100 excluding the fee and any contributions to compensation funds – both of which tend to be calculated in relation to the size of the firm. The scale of the additional compliance costs would also be affected by the extent to which the firm was previously regulated – a company that already has many of the necessary processes in place will be less likely to have to alter their approach substantially. Similarly the scale of the initial one-off investment in compliance functions will affect the scale of any on-going compliance costs.
- 5.49 There is no evidence at this stage that such additional compliance costs have affected either the range of services being offered or the prices being charged to consumers. This should, however, be reviewed going forward when the new system of ABS has had more time to develop.

## 6 CONSUMER COMPLAINTS

### Introduction

- 6.1 A number of problems were identified with the complaints process in 2006. The Ministry of Justice 2006 impact assessment in particular raised the following issues:<sup>65</sup>
- there were separate complaints and discipline systems for each legal discipline
  - there was a multiplicity of overseeing authorities,<sup>66</sup> each responsible for varying degrees of external oversight of complaints handling
  - professional bodies like the Law Society and the Bar Council were responsible for regulating members, representing their interests and handling complaints, thus leading to a lack of independence in complaint handling
- 6.2 In order to address these problems, as described in Section 2, an independent Legal Ombudsman was set up in 2010 and a single-entry and tiered structure for consumer redress introduced. In the first year and a half after the Legal Ombudsman was set up, it received around 110,000 contacts, leading to the acceptance of around 12,000 cases.<sup>67</sup>
- 6.3 In this section we consider the impacts of this new consumer redress framework. Specifically we consider whether and to what extent the design of this system undermines the intended benefits of the more streamlined process. Jurisdictional overlaps between redress mechanisms and the existence of unregulated individuals/activities can

<sup>65</sup> Ministry of Justice (2006) 'Legal Services Bill: Full Regulatory Impact Assessment', p.9-10.

<sup>66</sup> Including the Legal Service Ombudsman, the Legal Services Complaints Commissioner, the Secretary of State for Constitutional Affairs, the Master of the Rolls, the Court of Facilities, the Financial Services Authority, the Patent Office and the Immigration Services Commissioner

<sup>67</sup> The Office for Legal Complaints (2012) 'Annual report and accounts: For the year ending 31 March 2012'

create confusion for consumers and businesses in this area and are likely to result in suboptimal levels of consumer confidence as well as artificially increased costs.

- 6.4 We first identify the scope for any duplication in the complaints process and the areas without consumer redress processes based on the mapping from Section 2. Using this we construct the analytical framework, describing the mechanisms through which such restrictions may impact on consumer welfare.
- 6.5 We then present our analysis of the empirical and qualitative information collected via the surveys and interviews to assess the extent to which the potential detriment identified in the analytical framework may have materialised.

## **Potential benefits and costs of the complaints system**

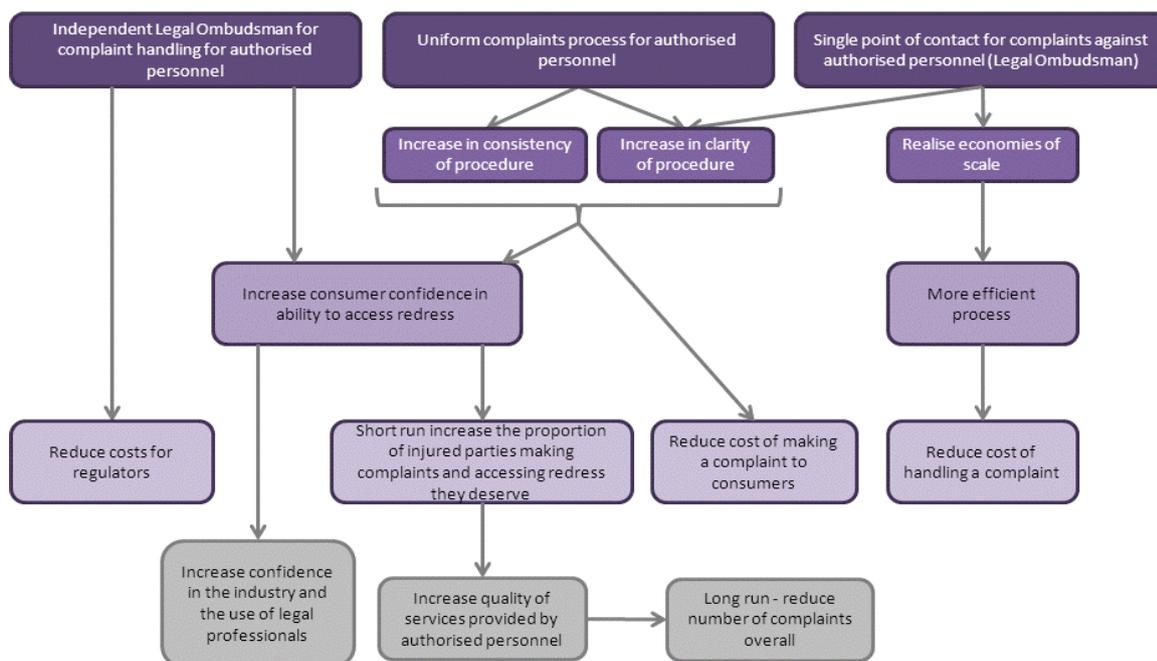
### **Potential benefits**

- 6.6 In the 2006 impact assessment the Ministry of Justice identified a number of potential benefits of the proposed new system for handling consumer complaints.
- increased consistency in the way that complaints are handled
  - greater clarity in the way complaints are handled
  - potential economies of scale and more efficient handling of complaints.
- 6.7 These benefits would be likely to increase consumer confidence and reduce the cost to consumers of making complaints and the cost of handling complaints (particularly for regulators who would no longer be involved in complaints handling and would only incur a cost via the financial contribution to the running of the Legal Ombudsman).
- 6.8 Ultimately, confidence in the industry as a whole would benefit, and aggrieved parties would be better able to access the redress they deserve. While this could in theory in the short run increase the number of complaints received, in the medium to long run a more efficient

effective complaints process and clearer information to consumers about complaints made would stimulate higher quality service provision, which should ultimately result in fewer complaints being made.<sup>68</sup>

6.9 These expected benefits are illustrated in Figure 6.1 below.

**Figure 6.1: Potential benefits of complaints process introduced by THE ACT (2007)**



Source: Europe Economics

## Potential costs

6.10 Although the reforms introduced by the Act aimed to eliminate confusion in the regulatory structure, recent studies have shown there is still some scope for confusion. These relate to three particular areas:

- the role of the Legal Ombudsman – in particular, the distinction between reserved and unreserved activities and between authorised and unauthorised persons

<sup>68</sup> On the other hand, as identified by the Ministry of Justice in its 2006 impact assessment, such a rise in the number of complaints would increase the workload for suppliers of substandard services which could in turn create a risk that service providers would become ‘cautious’ in not agreeing to take on complex or difficult cases.

- the role of other regulating and advisory bodies – in particular, the ease with which consumers are able to identify which regulating body to refer complaints to
- the tiered process – in particular, the transition of an in-house, first-tier complaint into a second-tier complaint.

- 6.11 In addition to these concerns, the separation of responsibilities for conduct complaints and service complaints, previously both handled by the approved regulators, may make it difficult for consumers to identify the appropriate body to address their complaint to if the in-house process fails.
- 6.12 The mapping of the consumer redress process presented in Section 2 illustrates the potential for duplication in the redress framework and an absence of redress processes in certain areas which can create these types of uncertainty. The key issue is that the Act only applies to authorised persons. Since unauthorised persons are allowed to provide unreserved legal services a key consequence of the Act is that there may be different redress procedures for different types of providers offering the same (unreserved) services.
- 6.13 In some cases, where the legal service is unreserved and unregulated and is provided by an unauthorised and unregulated person, there may be no specific route for accessing redress except via trade bodies or the ordinary courts. Equally where an unreserved service is regulated in other legislation and is provided by an authorised person who is also regulated in another sector, there may be various routes for accessing consumer redress.
- 6.14 Such absences and duplications in the complaints process could have a number of negative effects on the effectiveness of the system. In particular they could result in:
- consumer detriment not being addressed at all, and
  - uncertainty for consumers in how to make a complaint.
- 6.15 Uncertainty created by the system could deter aggrieved parties from seeking redress, ultimately resulting in consumer detriment going

unaddressed. Equally such uncertainty could increase the cost of making a complaint and increase costs for complaints handlers if they have to re-refer complaints incorrectly lodged with them. Meanwhile the lack of any redress process potentially increases the cost of using unauthorised providers (as compared to authorised providers) and reduces confidence in the industry more broadly (particularly if consumers cannot easily distinguish between authorised and unauthorised providers).<sup>69</sup>

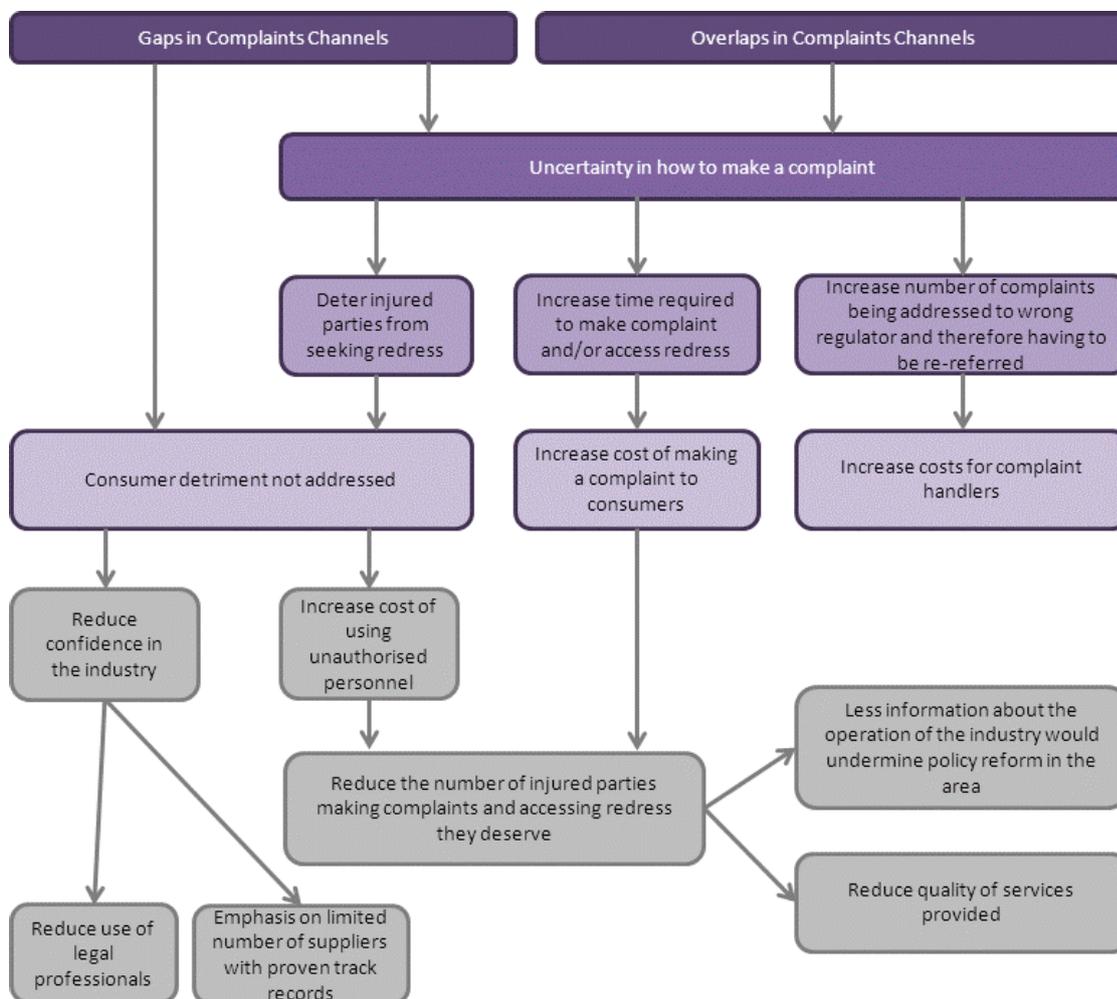
- 6.16 Ultimately these costs and a reduction in confidence could encourage consumers to use legal professionals less, and/or rely on a small number of suppliers with a proven track record. Equally, the number of aggrieved parties seeking redress would be likely to be lower than expected initially, undermining any increase in the quality of services provided which the reforms were expected to create and reducing the information available to policy-makers regarding the operation of the industry. One role of the Office for Legal Complaints is to gather intelligence from its work to inform policy development by the Legal Services Board.<sup>70</sup>
- 6.17 These effects may not, however, be symmetric across all types of service providers (for instance, authorised and unauthorised, and regulated and unregulated persons) or all types of services (for instance, reserved and unreserved, and regulated and unregulated). In part the extent to which the impacts vary between different types of providers and services will depend upon the extent to which consumers distinguish between different types of legal services and legal providers. If consumers have a clear understanding of the difference between authorised and unauthorised persons for example, it could be that while unauthorised persons may be used less, authorised persons may be used more for all types of services.

<sup>69</sup> Or, in the context of the Act reforms, fail to produce the increase in confidence the restructuring was intended to create

<sup>70</sup> Legal Ombudsman Memorandum of Understanding with the Legal Services Board, December 2009. Available at: [www.legalombudsman.org.uk/downloads/documents/work\\_other\\_bodies/20091217\\_lsb\\_and\\_olc\\_mou-FINAL.pdf](http://www.legalombudsman.org.uk/downloads/documents/work_other_bodies/20091217_lsb_and_olc_mou-FINAL.pdf)

6.18 These potential impacts and their associated costs are summarised in Figure 6.2 below.

**Figure 6.2 Potential costs of current complaint handling process**



Source: Europe Economics

## The Potential for Overlap and Uncertainty in Complaints Handling

### Overview of use of legal services

6.19 The consumer survey we conducted as part of the study was administered to a representative sample of 2,012 individuals as part of an IpsosMORI Capibus survey in June 2012 ('Our Survey' – references to survey results in this chapter including tabulated data refer to this

survey unless otherwise stated).<sup>71</sup> The survey covered a number of aspects of the consumer experience of legal services since the introduction of the Legal Services Act 2007. The full set of questions can be found in Annex D. The main findings are considered here with a particular focus on the responses from consumers in England and Wales.<sup>72</sup>

6.20 In addition our analysis draws on the results of a number of other related surveys. Notably a recent YouGov survey commissioned by the OFT,<sup>73</sup> ('OFT/YouGov (2012)') the Legal Service Consumer Panel 2012 Tracker Survey<sup>74</sup> ('LSCP (2012)') and a YouGov survey on First tier complaint handling commissioned by the Legal Services Board in 2011 ('LSB/YouGov (2011)').<sup>75</sup>

6.21 Our survey identified 677 UK respondents (34 per cent of all participants) who had used services provided by a legal professional since 2007, including a number who had used a service on more than

<sup>71</sup> The survey respondents were stratified by a number of demographic and social criteria and the final results were weighted so that they are representative of the adult population of the United Kingdom (UK). Unless otherwise stated, all of the results in this report have been weighted in this way. One consequence of this is that the counts in some tables do not sum precisely to the totals shown and the percentages in some tables do not sum precisely to 100 per cent. Also percentages shown in the tables exclude those respondents who stated that they did not know the answer to a question or refused to answer it.

<sup>72</sup> Additional analysis on responses from Scotland and Northern Ireland is provided in Chapter 8.

<sup>73</sup> The OFT commissioned a short survey looking at satisfaction with legal services and use of the complaint process as a complement to the IpsosMORI Capibus survey. The survey was administered to 2246 people as part of the YouGov online omnibus survey in November 2012.

<sup>74</sup> The LSCP survey was published in March 2012 and was administered to 1410 respondents who had used legal services in the previous two years:  
[www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/CIR\\_final\\_full%202012%2007%2025.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/CIR_final_full%202012%2007%2025.pdf)

<sup>75</sup> YouGov (2011) commissioned by the LSB, 'First Tier Complaints Handling':  
[www.legalservicesboard.org.uk/what\\_we\\_do/Research/Publications/pdf/final\\_report\\_for\\_lsb\\_ftch\\_09\\_06\\_11.pdf](http://www.legalservicesboard.org.uk/what_we_do/Research/Publications/pdf/final_report_for_lsb_ftch_09_06_11.pdf)

one occasion. The corresponding figure was 33 per cent for England and Wales. These responses are summarised in Table 6.3.

**Table 6.3: Have you used a legal professional in a personal capacity since 2007?**

UK constituent countries	Count/per cent				
	Never	Yes, once	More than once but fewer than five times	More than five times	All
England	1109	356	184	36	1685
Scotland	105	39	22	4	170
Wales	79	12	7	0	98
Northern Ireland	42	8	9	0	59
United Kingdom	1336	415	222	40	2012
<b>of which:</b>					
England and Wales	1188	368	191	36	1783
England	66%	21%	11%	2%	
Scotland	62%	23%	13%	2%	
Wales	81%	12%	7%	0%	
Northern Ireland	71%	14%	15%	0%	
United Kingdom	66%	21%	11%	2%	
<b>of which:</b>					
England and Wales	67%	21%	11%	2%	

Base size: 2,012 UK adults – excludes one respondent who answered don't know

Source: Europe Economics' consumer survey

6.22 One third of participants from England and Wales using legal services since 2007 is equivalent to an average of approximately seven per cent of the population of England and Wales or three million adults using legal services per annum over this period.<sup>76</sup> Some of these used legal services more than once over this period. The total number of occasions on

<sup>76</sup> 44.9 million adults were usually resident in England & Wales in mid-2010. Source: ONS [www.ons.gov.uk/ons/rel/pop-estimate/population-estimates-by-marital-status/mid-2010/index.html](http://www.ons.gov.uk/ons/rel/pop-estimate/population-estimates-by-marital-status/mid-2010/index.html)

which legal services were used over the five year period is estimated at about 32 million, an average of 6.5 million uses a year.<sup>77</sup>

6.23 The results of the OFT/YouGov (2012) survey identified similar levels of usage with 33 per cent of respondents indicating they had used legal services since 2007.

6.24 Amongst those respondents who had used the services of legal professionals since 2007, the most commonly mentioned services were conveyancing or mortgage services and wills or probate. The breakdown is shown in Table 6.4.

**Table 6.4: Number surveyed in England and Wales that had used different legal services since 2007**

Service used	Number of respondents	Per cent	Confidence Interval
All persons in England and Wales using legal services	595		
Conveyance/mortgage	246	41%	+/-4%
Will or probate	176	30%	+/-4%
Acting on behalf of you in your dealing with other people or bodies	144	24%	+/-3%
Representing you in legal proceedings such as court action or hearings	90	15%	+/-3%
Advice on interpretation of the law or other codes and how it applies to your circumstances	88	15%	+/-3%
Preparation of contracts or other documents (excluding wills)	82	14%	+/-3%
Certificate/notarisation of documents	26	4%	+/-2%
Divorce	4	1%	n/a
Accident/compensation claim	3	0%	n/a
Other – not specified	6	1%	n/a
Total count	863		
Average per person	1.45		

Base size: 595 UK adults

Source: Europe Economics' consumer survey

6.25 The survey results can also be analysed by demographic features. However sample sizes are small for some categories and these

<sup>77</sup> Tables showing the derivation of these estimates are provided in Annex F.

breakdowns should be interpreted with caution. Full tables for demographic breakdowns are given in Annex F.

- 6.26 The demographic breakdowns suggest that there is higher usage of legal services by males than females. There is also a distinction between individuals from different age groups. Among age groups, people younger than 25 are predominantly non-users of legal services, with only 12 per cent reporting to have used them at all. Similarly, only 11 per cent of people older than 60 years old have used them more than once since 2007, the highest usage was in the 45 – 59 age groups.
- 6.27 The use of legal services is also correlated with income. Only 12 per cent of individuals reporting incomes lower than £6,500 have used legal services since 2007. On the other hand, 47 per cent of earners of £25,000 or more have used legal services at least once. The correlation between use of legal services and income is uniform across all services. Earners of £25,000 or more use at least 43 per cent of the services in each category.

### Consumer satisfaction and complaints

- 6.28 The OFT/YouGov (2012) survey and the LSCP survey directly explore whether users of legal service were satisfied with the services they received. The results from the OFT/YouGov survey are reported in Table 6.5 below.

**Table 6.5: Satisfaction levels of users of legal services since 2007**

	Overall satisfaction with legal service at most recent time of use				
	Very satisfied	Satisfied	Neither satisfied nor dissatisfied	Dissatisfied	Very dissatisfied
Total	25%	44%	16%	11%	4%

Base size: 746

Source: OFT/YouGov survey (2011)

- 6.29 The results of the OFT/YouGov survey suggest that 15 per cent (95 per cent confidence interval: 12.5 per cent, 17.5 per cent) of users of legal service since 2007 were dissatisfied with the overall service they received the last time they used them. This equates to approximately 460,000 users of legal services in England and Wales annually. In

addition a further 16 per cent of respondents gave a neutral response suggesting they were neither satisfied nor dissatisfied with the overall level of service they received.

6.30 These results are broadly consistent with those from the LSCP (2012) survey which asked respondents who had used legal services in the previous two years about their level of satisfaction across a range of service measures and about their overall level of satisfaction. With regard to overall satisfaction eight per cent of respondents to the LSCP survey indicated they were either 'dissatisfied' or 'very dissatisfied' with the service they received, with a further 19 per cent responding that they were 'neither satisfied or dissatisfied'. For the questions on the various aspects of service<sup>78</sup> numbers of respondents indicating dissatisfaction ranged between seven per cent and 12 per cent, with the range of respondents who were neither satisfied or dissatisfied ranging between 17 per cent and 26 per cent.

6.31 In the published write up of the LSB/YouGov (2011) publication of their survey into first tier complaints handling the LSB stated that 'it is also clear that the majority of dissatisfied customers do not complain about their initial issue with the legal service'.<sup>79</sup> The survey results suggested that 66 per cent of dissatisfied users did not go on to complain. As we noted above there is the potential for consumer detriment and a loss of intelligence for regulators in an industry such as legal services when large number of dissatisfied users do not go on to complain. The OFT/YouGov (2012) survey asked respondents who had used legal service and were dissatisfied whether they then went on to complain. In this case an even higher proportion – 87 per cent - indicated they did not go on to make a formal complaint.<sup>80</sup>

<sup>78</sup> For example 'communication', 'professionalism', 'quality of advice', e.t.c.

<sup>79</sup> Chris Kenny, Chief Executive of the LSB in the forward to YouGov (2011) commissioned by the LSB.

<sup>80</sup> The difference between the values from the two surveys is likely to be explained by differences in the sample construction. In particular The LSB/YouGov survey was only administered to respondents who had been pre-screened for dissatisfaction, whereas the

6.32 Our survey sought views on satisfaction with service over the whole period since 2007 including views from people who had used legal services more than once. 70 per cent of respondents indicated that they were always satisfied – a similar percentage to the OFT/YouGov response for most recent use of legal services. 19 per cent were satisfied more often than not and 11 per cent were only satisfied half the time or less.

### **Consumer awareness of the complaints process**

6.33 The LSB/YouGov (2011) survey found that only 13 per cent of respondents were told about the first-tier in-house complaints procedure and only eight per cent were told about the second-tier process. Of those who were not informed about complaints procedures upon engagement, only a third were informed subsequently. However, the majority of consumers that did receive information from their service provider found it gave clear instructions on what to do and who to complain to.

6.34 Our survey supports the finding that a significant proportion of people did not have the complaints process explained to them by their service provider indicating that, following the 2007 reforms, uncertainty remains a key issue in the complaint and redress process. Awareness of the process for making a complaint about the legal services provided under the new system was moderate, 62 per cent<sup>81</sup> of respondents claimed they had been aware of the process before using the service but over a third (39 per cent)<sup>82</sup> of those who were aware of the process did not feel they fully understood it.

OFT/YouGov survey was administered to a representative UK sample and the question on complaints was only put to a subset of the sample who indicated they had used legal service and had been dissatisfied. We note that the 2012 LSCP tracker survey found that only 21 per cent of dissatisfied users made a formal complaint to their service provider.

<sup>81</sup> 368 respondents. Percentage excludes two respondents who answered don't know

<sup>82</sup> 145 respondents. Percentage excludes two respondents who answered don't know

**Table 6.8 Awareness in England and Wales of the process for making a complaint about the services**

	Number of respondents*	Per cent	Confidence Interval
All persons in England and Wales who used legal services	593		
I was unaware of the process	225	38%	+/-4%
I was aware but did not fully understand the process	145	24%	+/-3%
I was aware of the process and felt that I understood it	223	38%	+/-4%

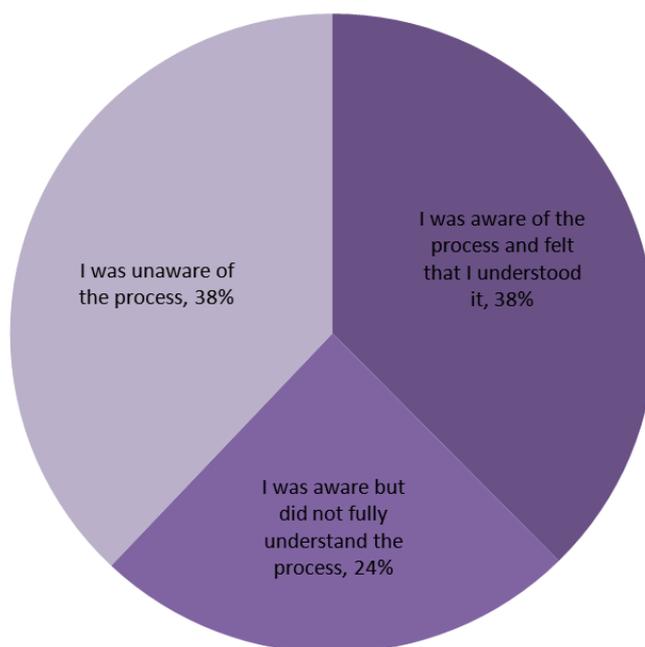
\* Excluding two respondents who answered don't know

Source: Europe Economics' consumer survey

6.35 Of those respondents that were aware of the process and felt they understood it, almost two thirds (65 per cent)<sup>83</sup> noted that legal service providers had made the complaint process clear to them on all occasions. However, around one in three respondents noted that clarity of the complaints process was not provided in all cases, of which around half recorded that the complaints process had not been made clear on any occasion.

<sup>83</sup> 127 respondents. Percentage excludes two respondents who answered can't remember

**Figure 6.9 Consumer awareness of complaints process in England and Wales prior to using legal professional**



Note: Percentage of the 595 respondents who had used a legal professional in a personal capacity since 2007, excluding two respondents who answered don't know

Source: Europe Economics' consumer survey

6.36 The more experience consumers had with using legal professionals, the more likely they were to be aware of the complaints process prior to using the service. Whilst 48 per cent of consumers who had used legal professionals more than five times were aware of the complaints process and felt they understood it, only 33 per cent of consumers who had never used a legal professional before felt this way.

6.37 A study by the Centre for Consumers and Essential Services (CCES) in 2011<sup>84</sup> examined the extent to which uncertainty was manifest under the new regime, focusing on the transition of an in-house complaint into a second tier complaint. They found that one of the contributing factors towards consumer confusion was the fact that the Legal Ombudsman

<sup>84</sup>Centre for Consumers and Essential Services (2011) 'Mapping potential consumer confusion in a changing legal market- report for the Legal Ombudsman' *University of Leicester*. See [www.legalombudsman.org.uk/downloads/documents/publications/Consumer\\_confusion\\_report.pdf](http://www.legalombudsman.org.uk/downloads/documents/publications/Consumer_confusion_report.pdf)

only has jurisdiction over authorised persons, for instance, persons authorised by a relevant approved regulator.

6.38 Studies by GfK (2010) and AIMR (2010) into issues concerning complaints procedures at the Legal Ombudsman tier also found evidence of uncertainty under the new system.<sup>85</sup> <sup>86</sup> The report found that spontaneous knowledge of the Legal Ombudsman and complaints procedures for the legal profession was limited. There was a general expectation of an ombudsman-like body to exist for legal services, but respondents were sceptical of its efficiency and impartiality.

6.39 In addition to suggesting some lack of awareness of the complaint process our survey provides some evidence that confusion about the complaint process may prevent consumers from complaining when otherwise they may have done so. Our survey asked those legal service users who had indicated they may not have been entirely satisfied with the service received why they did not complain about the service.<sup>87</sup> 33 per cent<sup>88</sup> of this group of respondents indicated that their reasons for not complaining were 'I did not know I could' or 'I did not know who to complaint to' or 'I did not know how to make a complaint' suggesting they might have made a complaint if they had a greater understanding of the process for making one. These results are comparable to those found

<sup>85</sup> GfK (2010) 'Research on Consumers' Attitudes towards the Purchase of Legal Services, research report for Solicitors Regulation Authority' [www.sra.org.uk/documents/consumer-reports/consumer-research-2010-purchase-attitudes-final.pdf](http://www.sra.org.uk/documents/consumer-reports/consumer-research-2010-purchase-attitudes-final.pdf)

<sup>86</sup> Acute Insight Market Research (2010) 'Identifying Law Firms Subject to Consumer Complaints to the Legal Ombudsman', See [www.legalombudsman.org.uk/downloads/documents/consultations/Consumer\\_research\\_report\\_1\\_10224.pdf](http://www.legalombudsman.org.uk/downloads/documents/consultations/Consumer_research_report_1_10224.pdf)

<sup>87</sup> Although our survey did not ask directly about level of dissatisfaction question IM07 did ask user of legal service since 2007 if they had always been satisfied with the service they received. 30 per cent (153 survey respondents) of users of legal services gave responses that indicated they had not always been satisfied with the service they received, although there is some potential for ambiguity in how respondents who had used legal services only once since 2007 would interpret the question posed.

<sup>88</sup> 51 respondents

in the LSB/YouGov (2011) survey. This survey found that nine per cent of respondents did not complain because they did not really understand the complaints procedure, nine per cent did not complain because they did not know how to and seven per cent did not complain because they did not know they could.

- 6.40 Overall these data suggest that uncertainty regarding the complaints process could be an important driver in consumers' decision to not complain.

### **Consumer satisfaction of complaints handling process**

- 6.41 The LSB/Yougov (2011) survey did identify an improvement in consumer satisfaction in the handling of complaints following the introduction of the Legal Ombudsman: 51 per cent of respondents who made a first tier complaint post October 2010 were satisfied with complaint handling, up from 36 per cent for pre October 2010 complaints.
- 6.42 Similarly, of the 23 respondents to our survey who had gone on to complain or seek redress, over half (56 per cent)<sup>89</sup> expressed generally positive views on the complaints process.<sup>90</sup> However, over a third (41 per cent)<sup>91</sup> still noted some dissatisfaction, largely associated with the clarity in the reasons given for the outcome of the complaint and the consultation process.
- 6.43 The LSB/YouGov survey found that the main causes of dissatisfaction with the complaints procedure were the amount of time the matter took (43 per cent) and poor quality service (42 per cent).

<sup>89</sup> 13 respondents

<sup>90</sup> Noting that they were 'Very satisfied' or 'Fairly satisfied'

<sup>91</sup> Nine respondents

## Complaint referral

- 6.44 Identifying the appropriate organisation to complain to is also difficult for consumers and complaints bodies alike, because of:
- the need to distinguish between service and conduct issues, and
  - the fact that consumers are normally provided a single, packaged service (which may include services regulated by other sectors).
- 6.45 There is evidence that complaints are incorrectly directed to the Legal Ombudsman. Compared to the 8,420 complaints the Legal Ombudsman accepted they had to redirect 13,533 complaints to first tier in-house processes ('premature complaints'). Equally, 839 of the complaints received were outside the Legal Ombudsman's jurisdiction and 477 were made too late, that is outside of the time limits set out in the ombudsman scheme rules. Feedback from complaint handlers also suggests that a significant number of complaints also had to be re-directed to the approved regulators.
- 6.46 Meanwhile regulators operating in other sectors also face confusion. The Financial Ombudsman Service was established by law to resolve individual disputes between consumers and financial businesses. Their role is to examine complaints about a wide range of financial matters, including complaints about financial services provided by authorised professional firms, complaints about financial businesses acting as executors/administrators/trustees and complaints about will-writing services provided by banks. While FOS does not record the number of consumers referred to other ombudsman schemes or whether the consumers that contact them were sign-posted to them by other ombudsman schemes, we were told that complaints about Legal Expenses Insurance was an area where there could be confusion about which organisation should handle the complaint. Such confusion may increase with the growth in MDPs.
- 6.47 Furthermore, different bodies have different rules concerning time-scales and handling processes. For example, the Legal Ombudsman allows less time for a consumer to make a complaint than the FOS. Not only may this add to the confusion, but this may be problematic in cases where

consumers are referred from one body to another, by following the guidance of the wrong body the complainant may miss the time limit for the actual body with whom they should be lodging their complaint, and any time delay in the referral process may render the complaint invalid by the time it reaches the appropriate body. Additionally, different schemes charge different fees and allow for different maximum awards of compensation. These differences may make it more advantageous or disadvantageous for consumers to file a complaint with one body rather than another, creating the potential for distortions.

### **Estimated cost**

- 6.48 Aside from the benefits of having an independent ombudsman scheme to address service issues, as illustrated in the original impact Assessment, the new system with a separate Legal Ombudsman shifted responsibility for the handling of complaints mostly away from legal sector regulators onto the Legal Ombudsman. Hence, there have been cost savings for the previous complaints bodies, including some bodies which are now no longer operational under the new system.
- 6.49 While this reduction in costs has been in part offset by the additional running cost for the Legal Ombudsman, we estimate that the introduction of the Legal Ombudsman has reduced the cost of complaints handling in the legal services sector by around £18 million per annum, a 51 per cent reduction on the old system.<sup>92</sup> With a total legal services industry turnover of £25 billion,<sup>93</sup> the annual cost of complaints (both in terms of the LO and the complaints processes run by

<sup>92</sup> This figure is based on the original estimates by PriceWaterhouseCoopers financial analysis to support the draft Legal Services Bill 2006, of the annual cost of previous complaints system, estimated to be £32,515,000, and their estimate of the expected cost savings to previous complaints bodies from the introduction of the Legal Ombudsman of £29,916,000. We have also drawn upon the Legal Ombudsman Annual Report 2012 to identify the annual cost of running the Legal Ombudsman. Both of these figures were inflated to 2011 prices using Eurostat HCIP data for the UK (price index of 102.3 for 2006 and 119.6 for 2011).

<sup>93</sup> Office for National Statistics (2010). 'Results of the 2010 Services Turnover Survey' Available at [www.ons.gov.uk/ons/rel/ppi2/services-producer-price-indices/results-of-the-2010-services-turnover-survey-/art-results-of-the-2010-sts.html#tab-Survey-results](http://www.ons.gov.uk/ons/rel/ppi2/services-producer-price-indices/results-of-the-2010-services-turnover-survey-/art-results-of-the-2010-sts.html#tab-Survey-results)

the approved regulators) represents only 0.1 per cent of the industry's annual turnover.

- 6.50 Our consumer survey work suggests that there are a significant number of complaints not being lodged. Although only a proportion of complaints made are upheld by the LO, this may mean that there is a significant level of continuing consumer detriment which has not been subject to any form of review or redress due to a lack of awareness or confusion over the complaints handling process.
- 6.51 This only provides a partial indication of the economic loss that consumers may have suffered from poor service. Further consumer detriment may also arise from complaints dropped after being referred on to a second complaint body and complaints timed out because of delay.
- 6.52 Such uncertainty may also raise the cost of making a complaint for consumers, and in fact increase the cost for complaint handlers in terms of time spent referring consumers to the relevant bodies.

### **The Absence of Complaint Processes**

- 6.53 As illustrated in Section 2 there are legal services that are unreserved and unregulated. Examples of these include preparation of wills, advice and representation at a police station and advice about mental health. Where these are provided by an unauthorised and unregulated person, there may be no specific route for accessing redress except via trade bodies or the ordinary courts.
- 6.54 The potential for a lack of a redress process is highlighted in the study by Centre for Consumers and Essential Services (CCES) in 2011:<sup>94</sup>

'If the consumer uses a will writing company, then there is no recourse to the Legal Ombudsman. There are two trade

<sup>94</sup> Centre for Consumers and Essential Services (2011) 'Mapping potential consumer confusion in a changing legal market- report for the Legal Ombudsman' *University of Leicester*, [www.legalombudsman.org.uk/downloads/documents/publications/Consumer\\_confusion\\_report.pdf](http://www.legalombudsman.org.uk/downloads/documents/publications/Consumer_confusion_report.pdf)

associations that a will writing company might belong to: the Institute of Professional Will Writers (IPWW) and the Society of Will Writers (SWW). The former seems to cover around 200 firms and operates an OFT approved Code of Practice, which requires its members to have a complaints procedure. If the consumer is not happy with the outcome, they may either refer the matter to the IPWW, who will help 'to reach a mutually acceptable outcome' or they may instead refer the matter to the Estate Planning Arbitration Scheme, the results of which are binding on the parties (and there is an upper limit of £10,000).

If the will writer is a member of the SWW, which is much larger than the IPWW, then that association may become involved. Complaints may be resolved through conciliation or, if more serious, the SWW will consider whether or not to discipline the will writer. The SWW, however, has no powers to order compensation. If the will writer is not a member of either organisation, then there is no means of recourse, outside the normal channels of consumer law.'

6.55 Even if there is some scope for redress via a trade body in this instance, '...for consumers using will packs or online providers, there is no specific means of redress, outside the ordinary law...'.<sup>95</sup> Indeed research commissioned by the SRA found that:<sup>96</sup>

'Consumers were generally surprised and concerned to learn that some legal services were not regulated. They were not aware of

<sup>95</sup> Centre for Consumers and Essential Services (2011) 'Mapping potential consumer confusion in a changing legal market- report for the Legal Ombudsman' *University of Leicester*, [www.legalombudsman.org.uk/downloads/documents/publications/Consumer\\_confusion\\_report.pdf](http://www.legalombudsman.org.uk/downloads/documents/publications/Consumer_confusion_report.pdf)

<sup>96</sup> Solicitors Regulation Authority (2011), 'Consumer attitudes towards the purchase of legal services: An overview of SRA research findings', February 2011. The research was carried out by GfK, and the findings are based on interviews with 40 consumers who had either recently purchased legal services, or were intending to purchase them.

how to tell the difference between an unregulated and regulated provider.<sup>197</sup>

- 6.56 Although the existence of unregulated activities and practitioners is well documented, there is little existing evidence as to the number of consumers that may be using such services and who are, therefore, susceptible to a lack of access to a redress system. Based on our survey of consumers approximately two per cent have used an unauthorised person to provide unreserved services since 2007. Around one third of these consumers used unauthorised providers for employment issues and a third for will-writing services.
- 6.57 Only 10 per cent<sup>98</sup> of consumers that used unauthorised providers for unreserved services were dissatisfied with the service they received.
- 6.58 The consumer survey data suggest that overall less than one per cent of all consumers are in danger of suffering as a result of a lack of redress system (for instance, less than one per cent are using unauthorised providers for unreserved activities and have been dissatisfied with the outcome).
- 6.59 According to our survey, three out of the four consumers that were dissatisfied with the service they received did attempt to seek some form of redress. One in three found the redress process to be less than satisfactory, and none reported being satisfied with it.

## Conclusions

- 6.60 In this section we explore the scope for overlaps in the consumer redress system and also areas where there is a lack of access to redress systems following the Act. The shift to an independent Legal Ombudsman for service complaints in 2010 was aimed at reducing

<sup>97</sup> Solicitors Regulation Authority (2011), 'Consumer attitudes towards the purchase of legal services: An overview of SRA research findings', February 2011. The research was carried out by GfK, and the findings are based on interviews with 40 consumers who had either recently purchased legal services, or were intending to purchase them.

<sup>98</sup> Three respondents

potential conflicts of interest, and interest, and rationalising and streamlining the complaints process, ultimately improving the quality of service provision in the industry and consumer welfare.

6.61 A number of potential issues with the new system exist. In particular:

- the LO only covers authorised persons and entities (whether they are providing reserved or unreserved legal services) — this can raise particular issues where consumers are provided with a single packaged service which can involve authorised and unauthorised providers (and potentially relate to services covered by another sector ombudsman), and
- the approved regulators or the organisations to which they have delegated the power to regulate are still responsible for conduct complaints — this requires consumers to be able to distinguish between service and conduct complaints.

6.62 This implies that in some cases consumer detriment may go unaddressed, either because the legal service provider is not authorised and therefore is not covered by the LO, or because uncertainty about the complaints process deters consumers from lodging a complaint. In addition uncertainty in the process may increase the costs to consumers and complaints handlers of making and addressing complaints.

6.63 There is evidence to suggest that consumers are still confused about the complaints process, and such confusion may grow with the development of multi-disciplinary practices.

6.64 Our consumer survey and the OFT/YouGov survey suggest that around seven per cent of the population of England and Wales use legal services every year. The OFT/YouGov survey suggest that around 15 per cent of users were dissatisfied with the services they received last time they used legal services which equates to approximately 460,000 users of legal services in England and Wales annually. There is also evidence from the LSB/YouGov (2011) and our own survey that the majority of dissatisfied users do not go on to complain about the service they received

- 6.65 One of the reasons that dissatisfied consumers do not go on to make a complaint could be confusion regarding the complaints process. Evidence collected via our consumer survey in the UK supports this, indicating that, following the 2007 reforms, uncertainty remains a key issue in the complaint and redress process. Awareness of the process for making a complaint about the legal services provided under the new system was moderate, 62 per cent of respondents claimed they had been aware of the process before using the service but over a third (39 per cent) of those who were aware of the process did not feel they fully understood it.
- 6.66 In addition when respondents who indicated they may not have been entirely satisfied with the legal service received were asked why they did not complain a significant proportion (33 per cent) suggested one of the reasons for not doing so was some aspect of uncertainty regarding the complaint process. This is supported by research conducted by YouGov in 2011 which found that 25 per cent of respondents did not complain because of uncertainty about the complaints procedure. Although only a proportion of complaints made are upheld by the LO, this indicates a significant level of consumer detriment which has not been subject to any form of review or redress due to a lack of awareness or confusion over the complaints handling process.
- 6.67 Evidence from approved regulators and the LO indicate that complaints often need to be referred on to an alternative body. For example compared to the 8,420 complaints the Legal Ombudsman accepted, they had to redirect 13,533 complaints to first tier in-house processes ('premature complaints'). Equally, 839 of the complaints received were outside the Legal Ombudsman's jurisdiction and 477 were made too late, that is outside of the time limits set out in the ombudsman scheme rules. Feedback also suggests that a significant number of complaints had to be re-directed to the approved regulators.
- 6.68 Equally, there are legal services that are unreserved and unregulated, such as will writing and advice about mental health. Where these are provided by an unauthorised and unregulated person, there may be no specific route for accessing redress except via trade bodies or the ordinary courts.

## **7 POSSIBLE CHANGES TO CURRENT SYSTEM IN ENGLAND AND WALES**

### **Introduction**

- 7.1 In this section we consider possible changes to the current system aimed at addressing any issues identified in earlier sections associated with market entry, the regulation of ABS and the complaints handling system in England and Wales.
- 7.2 Regulators should generally try to restrict their intervention to a minimum, because competitive markets will use resources wherever they have the highest value, unless there is a market failure. Where such a market failure has been identified an Impact Assessment should be the first stage in any policy assessment in order to identify the possible policy options and estimate the potential impacts of the individual options.
- 7.3 The aim here is not to try to identify market failures and conduct a full Impact Assessment. We simply draw upon our analysis in previous sections to propose areas for further consideration or policy changes that might be worth further consideration, both in terms of the need for such changes and the impact of any such changes.
- 7.4 In particular many of the issues considered in this report relate to relatively recent changes in the legal services sector. As such, in many cases it would be premature and inappropriate to try to set out proposals for policy interventions.

### **Restrictions on entry/expansion**

- 7.5 Our analysis in Section 3 identifies the potential for entry barriers both at the individual and the entity level. In particular we identify a large discrepancy between the number of pupillages available and the number of applicants. This discrepancy is higher than that for solicitor training contracts. While this may be a reflection of demand for barrister services, there is evidence to suggest that the role of non-chambers Pupillage Training Organisations and the scope for barristers to supervise more than one pupil at a time (as is the case for solicitors) could be

explored further to ensure that these do not present unnecessary barriers to entry to the profession.

- 7.6 As a first step a more detailed review of the training and qualification systems would seem proportionate, within the context of new business structures, primarily ABS. An independent review is already being carried out by the LETR which will report at the end of 2012. Given the potential importance of ABS on the market for legal services, any further review would be most useful once these structures have had a chance to develop more fully and the findings of the LETR have been considered.
- 7.7 An additional consideration might also be the scope for more focused education and training. According to the LSB, the current regulatory framework follows a traditional title-based regulatory model where qualifications drive the title, activities that an individual can undertake and regulatory burdens imposed. As an example, a solicitor setting up a will-writing business must undertake a three-year law degree (or another degree followed by a one-year Graduate Diploma in Law (GDL)), a one-year Legal Practice Course and a two-year training contract, followed by three years in practice before setting up a will-writing or criminal defence business. Once qualified, individuals can (subject to accreditation in some areas) offer any legal services regardless of experience or specific training.
- 7.8 The LSB believes a more targeted regulatory framework could help reduce risk, improve the quality of regulation and allow greater flexibility for firms to enter the market offering legal services. An example of this would be qualifications for practice based on activities undertaken.
- 7.9 At the entity level of access, more time is required before any clear assessment can be made of the impact of multiple regulation on market entry, and the broader impact of ABS on access. At this stage therefore it would be inappropriate to consider further policy and/or regulatory changes.

## **Regulation of ABS**

- 7.10 As set out in Section 4 to date there is no evidence that the regulatory structure for ABS significantly affects firms' compliance costs, or any associated impacts on price, quality or the range of services offered by existing ABS. That said, as of 1 August 2012 only 16 ABS had been authorised. It remains an open question whether the time and cost of applying to become an ABS is acting as a deterrent and a barrier to entry. At this stage, therefore the most prudent course of action would be to review these issues once the new system of business structures has become more ingrained and more ABS exist.
- 7.11 In order to pre-empt any concerns, Memoranda of Understanding could be developed to clarify the relationships between key regulators such as the FSA, ACA, RIBA and the SRA and CLC, and formalise a mutual recognition of regulation.

## **Consumer redress**

- 7.12 One of the concerns about the current consumer redress system is that confusion over the appropriate organisation to handle the complaint could result in consumer detriment not being addressed. One possibility for addressing this would be to introduce a post-box system whereby a specific organisation acts as the single point of contact for all consumer complaints that were unable to be resolved at the 'in-house' level. In theory this could be any organisation, for example the Legal Services Board, the Legal Ombudsman or even a consumer organisation such as the Citizen's Advice Bureau.
- 7.13 The most natural place to house this filtering process, however, may be with the Legal Ombudsman, as it already forms part of the complaints process and will have connections with other complaint handling organisations. The LO would then refer on the complaints to the appropriate organisation, for example to other sector regulators or (if a misconduct issue) to the relevant approved regulator, or address the complaint themselves if it relates to a service issue, similar to the model adopted in Scotland under the SLCC.

- 7.14 Currently, the LO only offers a one stop shop for service complaints. Based on estimates for such a scheme explored in the original IA, extending its remit in this way could add an additional £400,000 to the cost of running the LO. The £400,000 cost estimated related to transferring the call handling functions of the Consumer Complaint Services of the Law Society to form a 'Post-box' giving a 'single point of entry for all complaints against legal practitioners, with complaints passed to relevant FLRs to deal with.'<sup>99</sup>
- 7.15 The estimated cost of a Legal Services Board (LSB) and Office for Legal Complaints (OLC) in the IA, tasked with such a rerouting function, was £23.8 million,<sup>100</sup> compared to the actual cost of the Legal Ombudsman in 2011/2012 of £17.3 million – a £6.5 million difference. If we instead look at just the cost estimate for the OLC of £19.6 million, the difference is smaller at £2.3 million, but still significantly larger than the £0.4 million figure. This difference may be related to a number of factors in addition to the removal of the call rerouting function.
- 7.16 Depending on the actual cost of making the LO a one-stop shop, it may be economically efficient to do so. If however, the cost is substantially higher, an alternative might be simply to require providers to clarify at the outset of any engagement with a customer which regulatory/ombudsman service they would be governed by in the event of a complaint.
- 7.17 The possibility for a single unified timetable for all regulators/ombudsmen and a formal system for them to talk to each other could also be explored. Equally, firms' schemes could be required to have a set time limit before escalation to regulator/ombudsman.
- 7.18 A final area where policy changes may usefully be considered is the issue of third party complaints. Though not addressed as part of our

<sup>99</sup> PricewaterhouseCoopers. (2006) 'Financial Analysis to support the draft Legal Services Bill'. 22 May 2006. PwC

<sup>100</sup> £3.6million for the LSB and £16.8 million for the OLC converted to 2011 prices based on Eurostat HICP data for the UK – with 2006 price index of 102.3 and 2011 price index of 119.6.

analysis, this seems to represent an area where consumer redress is not accounted for. Third party complaints currently lie outside the remit of the LO, however, 1,560 complaints made since October 2010 have been third party complaints.<sup>101</sup> At present, evidence suggests coordination between legal services complaints-handling and other sector complaints-handling bodies is informal. While memoranda of understanding between regulating authorities are presently being drafted in England and Wales, drafting has not yet commenced in Scotland.

## Conclusions

- 7.19 At this stage, given the potential for substantial changes in the market for legal services with the recent introduction of ABS, it would seem premature to consider further policy intervention or de-regulation, particularly with respect to ABS. Rather the most prudent strategy would be to review the scope for barriers to entry at the individual level, in particular with respect to barristers and pupillage training organisations, and, once the new system has been able to develop, review any issues around the regulatory framework for ABS that might be affecting market entry at the entity level.
- 7.20 While the Legal Ombudsman role is also relatively new, and it remains too early to identify any robust trends, the scope for clarifying the redress processes and aligning the different schemes, including comparison with the SLCC model, could be explored further.

<sup>101</sup> Legal Services Consumer Panel (2012), 'Consumer Impact Report 2012'. Available at: [www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/CIR\\_final\\_full%202012%2007%2025.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/CIR_final_full%202012%2007%2025.pdf) .

## 8 SCOTLAND AND NORTHERN IRELAND

### Introduction

8.1 In this section we consider the cases of Scotland and Northern Ireland. While at differing stages in the reform process to that of the regulatory model in England and Wales, we consider the current environment and recent policy reforms in order to identify key issues for consumer detriment going forward.

### Relative experience with legal professionals in Scotland and Northern Ireland

8.2 The results from the consumer survey suggested that there is no real distinction in the frequency of usage of legal services at a regional level.

**Table 8.1: Percentage of surveyed that used legal services since 2007**

		Group size*	Never	Once	More than once but fewer than five times	More than five times
Region	UK	2,012	66%	21%	11%	2%
	ENGLAND + WALES	1,783	67%	21%	11%	2%
	SCOTLAND	170	62%	23%	13%	2%
	NORTHERN IRELAND	59	71%	14%	15%	0%

\* Excluding respondents who answered don't know

Source: Europe Economics' consumer survey

8.3 Our survey also shows that there are no significant differences in satisfaction with the use of legal services depending on the geographical location.

**Table 8.2 Percentage of surveyed according to satisfaction**

		Group size*	Never	No less often than not	About half the time	More often than not	Yes, always
Region	UK	672	1%	3%	4%	18%	76%
	ENGLAND + WALES	592	2%	3%	6%	19%	70%
	SCOTLAND	64	0%	3%	4%	18%	76%
	NORTHERN IRELAND	17	0%	0%	12%	29%	59%

\* Excluding respondents who answered don't know

Source: Europe Economics' consumer survey

8.4 The lack of significant differences between the groups may be explained in part by the relatively small sample sizes in Scotland and Northern Ireland.

## Market for legal professionals

### Scotland

8.5 The key players in the legal services profession in Scotland include advocates, solicitors and conveyancing and executry practitioners. All advocates are registered with the Faculty of Advocates (much like the Bar Council in England and Wales), while solicitors and conveyancing, and executry practitioners are registered with the Law Society of Scotland (much like the Law Society and the CLC in England and Wales).

**Table 8.3 Membership in The Law Society of Scotland (as of 31 October 2011)**

Members holding practising certificates	10573
Private practise principals	3557
Consultants	283
Associates	1266
Assistants	2553
Local authorities	564
Central Government	925
Other in-house	540
Other	885
Members not holding practising certificates	469

Source: The Law Society of Scotland, Annual Report

- 8.6 A new professional body was established in 2009 – the Association of Commercial Attorneys. This association represents commercial attorneys dealing with construction law. As a newly formalised category of lawyers, there is very limited information on commercial attorneys' role in the market. They have been consequently omitted from this analysis.
- 8.7 In 2012, just over 460 individuals were registered with the Faculty of Advocates, of whom approximately one fifth are Queen's Counsel. In 2011, 11,042 individuals were registered with the Law Society of Scotland (down from 12,936 in 2010). Of these, 10,573 held practising certificates and 469 did not hold practising certificates. Scottish solicitors do not have grant of rights of audience to higher-level courts such as the High Court of Justiciary and the Court of Session. However, under Section 24 of the Law Reform (Miscellaneous Provisions) Scotland Act 1990, suitably qualified solicitors were for the first time in Scotland granted rights of audience in the Supreme Courts in Scotland as well as in the House of Lords and the Judicial Committee of the Privy Council as solicitor advocates. Although they are regulated by the Law Society they have distinctive career paths and are represented by The Society of Solicitor Advocates. They are regarded as a 'competitive constraint' on Advocates who are regulated by the Faculty of Advocates.

## Training

- 8.8 The training process for solicitors and advocates in Scotland is similar to those in England and Wales. All aspiring lawyers must complete an LLB (three years accelerated or four years part time) or sit the Society's professional exams. These exams involve entering into a three-year pre-Diploma training contract with a Scottish solicitor and studying for the Society's professional exams. The Law Society has undertaken a review of Scottish legal education. In the academic session 2011/2012 the Diploma and the traineeship will become Professional Education and Training stages (PEAT1 and PEAT2) comprising a post-graduate vocational stage in a simulated environment and a work-based stage in a workplace setting. PEAT aims at facilitating the development of legal skills and will integrate these with legal knowledge and ethical behaviour.

- 8.9 Subsequently, all aspiring lawyers must undertake a Mandatory Diploma in Professional Legal Practice (part time or full time). The costs vary between providers. UK and EU students should budget at least £6,000 for fees, materials and textbooks.<sup>102</sup>
- 8.10 Aspiring advocates must then matriculate as an Intrans, which requires payment of a number of fees: a Court Fee of £180, a Matriculation fee of £150, and Entry Money of £850.<sup>103</sup> They must then pass the Faculty's examinations (fees are £150 + VAT per examination paper) and confirm their professional training (21-24 months) has been completed prior to the commencement of devilling. Once two years of training is completed, advocates may commence training requirements as required by the Faculty (eight to nine months), referred to as devilling. Subsequently, they are admitted as members of the Faculty of Advocates.
- 8.11 Following the Mandatory Diploma, aspiring solicitors must enter a two-year training contract. From June 2011, the recommended rate for first year trainees are £16,200 (up from £15,965 in 2010) and £19,400 for second year trainees (up from £19,107 in 2010). The Law Society of Scotland registered 488 training contracts in 2011.<sup>104</sup>

## Northern Ireland

- 8.12 The key players in the legal services profession in Northern Ireland are solicitors and barristers. All barristers are registered with the General Council of the Bar while solicitors are registered with the Law Society of

<sup>102</sup> Law Society of Scotland (2012). 'Guidance Note for Students: Part 1/The Diploma in Professional Legal Practice'. Available at [www.lawscot.org.uk/media/472949/guidance%20note%20for%20students%202012-2013.pdf](http://www.lawscot.org.uk/media/472949/guidance%20note%20for%20students%202012-2013.pdf)  
'The Future of Diploma in Legal Practice Funding'.  
[www.lawscot.org.uk/media/443187/future%20of%20diploma%20funding.pdf](http://www.lawscot.org.uk/media/443187/future%20of%20diploma%20funding.pdf)

<sup>103</sup> Faculty of Advocates (2009) 'Regulations as to Intrans'. Scotland. Available at: [www.advocates.org.uk/downloads/becoming\\_training/regintrans\\_2009.pdf](http://www.advocates.org.uk/downloads/becoming_training/regintrans_2009.pdf)

<sup>104</sup> Law Society of Scotland (2011). 'Trainee Statistics'. Retrieved from: [www.lawscot.org.uk/media/212372/trainee%20statistics%202011.pdf](http://www.lawscot.org.uk/media/212372/trainee%20statistics%202011.pdf)

Northern Ireland. In this respect, the profession is similar to England and Wales. However, the regulatory structure is quite different.

- 8.13 There are approximately 500 solicitor-firms in Northern Ireland, with around 2,200 solicitors. About 50 per cent of solicitors are single partner/practitioners, (compared to only five per cent operating as sole practitioners in England and Wales). Less than 30 per cent work in firms of five or more partners (compared to 70 per cent in England and Wales). Most of these firms are situated in the larger cities.
- 8.14 Barristers can be divided into those in independent private practice, working as sole practitioners, and those who are employed by companies and other organisations. The majority of barristers work in private practice. In 2005, there were around 560 barristers in private practice in Northern Ireland.<sup>105</sup> Their numbers had almost doubled over the previous 15 years. In 2011, there were 600 barristers in private practice.<sup>106</sup> Employed barristers, by giving up their sole practitioner status, lose their right of audience before the courts. All barristers in Northern Ireland operate from the Bar Library in Belfast.<sup>107</sup>

## Overview of regulatory systems

### Scotland

- 8.15 Following developments in England and Wales, there was a debate in Scotland on reform of the legal services profession. The Scottish Government set up a Research Working Group (RWG) to review the

<sup>105</sup> Department of Finance and Personnel (2006). 'Legal Services in Northern Ireland: Complaints, Regulation, Competition', Legal Services Review Group. Norwich: The Stationary Office. Retrieved from [www.dfpni.gov.uk/legal\\_services.pdf](http://www.dfpni.gov.uk/legal_services.pdf)

<sup>106</sup> Office of Fair Trading (2011). 'Bar Council of Northern Ireland Modifies its Rules to Address OFT Concerns'. 5 Jan. 2011. Retrieved from [www.oft.gov.uk/news-and-updates/press/2011/02-11](http://www.oft.gov.uk/news-and-updates/press/2011/02-11)

<sup>107</sup> Department of Finance and Personnel (2006). 'Legal Services in Northern Ireland: Complaints, Regulation, Competition', Legal Services Review Group. Norwich: The Stationary Office. Retrieved from [www.dfpni.gov.uk/legal\\_services.pdf](http://www.dfpni.gov.uk/legal_services.pdf)

Scottish legal services market and the introduction of alternative business structures (ABS) in Scotland. The resulting 2006 report<sup>108</sup> recommended the implementation of sections 25 to 29 of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1990.<sup>109</sup> These sections set out arrangements by which rights to conduct litigation and rights of audience can be granted in Scotland to members of a professional or other body, for instance, to bodies whose members are not necessarily legally qualified. The sections were implemented on 1 March 2007.<sup>110</sup>

8.16 One key issue in the debate, as in England and Wales, concerned the fact that regulation preventing the formation of ABS in Scotland consequently restricted choice to consumers. Which?, for example, submitted a super-complaint to the OFT in May 2007 requesting:

- removal of the current regulatory restrictions on solicitors and advocates working together, or bringing together lawyers and other professionals to provide legal and other services to third parties
- removal of the prohibition on consumers having direct access to advocates, and
- the creation of an independent Scottish Legal Services Board, responsible for the regulatory control of the Scottish legal bodies and consumer protection.<sup>111</sup>

<sup>108</sup> Working Group on the Legal Services Market in Scotland. 'Report by the Research Working Group on the Legal Services Market in Scotland'. Edinburgh: Scottish Executive, 2006. Print. Retrieved from [www.scotland.gov.uk/Resource/Doc/111789/0027239.pdf](http://www.scotland.gov.uk/Resource/Doc/111789/0027239.pdf)

<sup>109</sup> Scottish Government (2011) 'Rights of Audience'. Scottish Government, 4 May 2011. Retrieved from [www.scotland.gov.uk/Topics/Justice/legal/Rights-of-Audience-1-1#a2](http://www.scotland.gov.uk/Topics/Justice/legal/Rights-of-Audience-1-1#a2)

<sup>110</sup> Scottish Government (2011). 'Background: Reform of the Legal Profession'. Scottish Government, 10 May 2011. Retrieved from [www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background](http://www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background)

<sup>111</sup> Scottish Government (2011). 'Background: Reform of the Legal Profession'. Scottish Government, 10 May 2011. Retrieved from [www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background](http://www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background)

- 8.17 The OFT concluded in favour of greater liberalisation and recommended that the system be reformed. In its response, the Scottish Government noted that while it believed reform was needed, it did not believe the Scottish legal system needed the radical changes being implemented in England and Wales.<sup>112</sup>
- 8.18 The Law Society of Scotland (the Society, which regulates solicitors) and the Faculty of Advocates (the Faculty, which regulates advocates) subsequently undertook consultations on the matter, resulting in two papers. The Society published a policy paper in April 2008<sup>113</sup> in which it argued that it was in the interests of the public and profession to permit ABS for a more modern and competitive legal service. Scottish firms needed to be able to compete with larger firms outside Scotland. Recent merger activities may be regarded as a sign for this need for restructuring.
- 8.19 It was agreed that an appropriate regulatory framework needed to be established to maintain the core values of the legal profession. The Faculty published its response in May 2008,<sup>114</sup> which favoured maintaining an independent referral Bar. The Faculty did not wish advocates to participate in ABS at that time, although it did not object to solicitors being able to do so, and any advocate wishing to join an ABS should be able to do so by becoming a solicitor advocate.<sup>115</sup>

<sup>112</sup> Scottish Government (2011). 'Background: Reform of the Legal Profession'. Scottish Government, 10 May 2011. Retrieved from [www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background](http://www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background)

<sup>113</sup> 'The Public Interest: Delivering Scottish Legal Services'  
[www.lawscot.org.uk/media/54432/abs\\_policy.pdf](http://www.lawscot.org.uk/media/54432/abs_policy.pdf)

<sup>114</sup> Faculty of Advocates (2008). 'Access to Justice: a Scottish Perspective: A Scottish Solution' Available at [www.advocates.org.uk/downloads/news/accesstojustice.pdf](http://www.advocates.org.uk/downloads/news/accesstojustice.pdf)

<sup>115</sup> Scottish Government (2011). 'Background: Reform of the Legal Profession'. Scottish Government, 10 May 2011. Retrieved from [www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background](http://www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background)

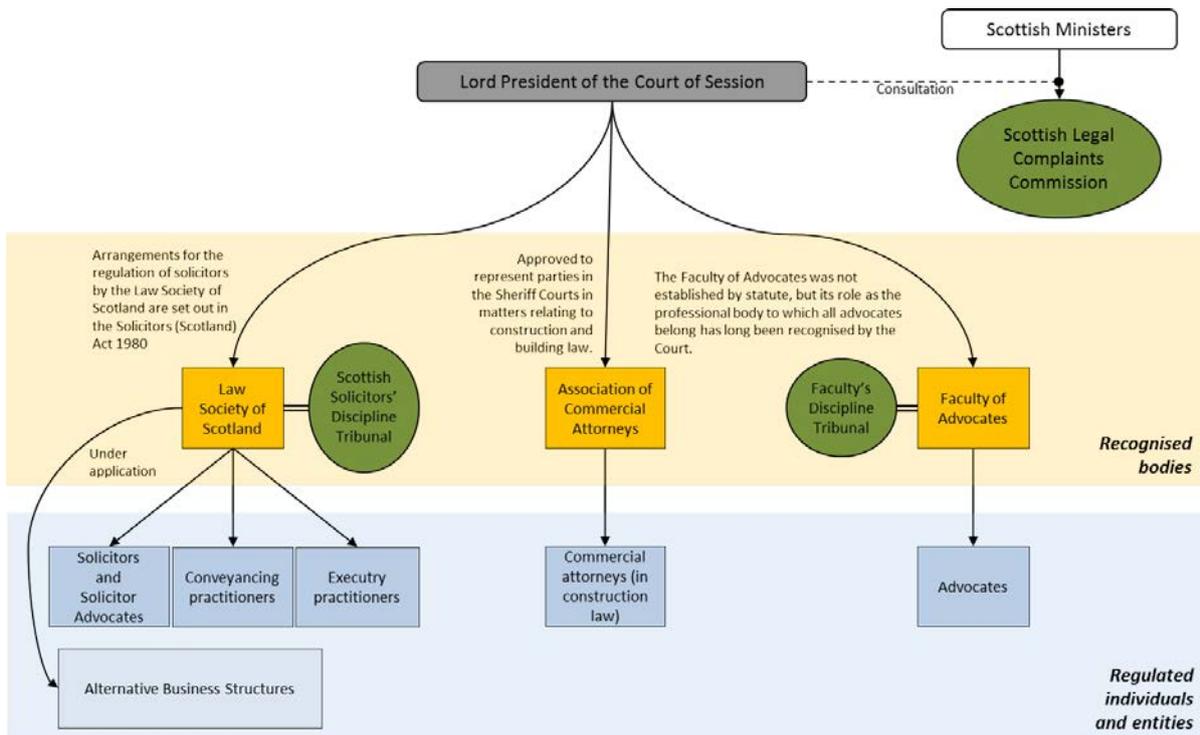
- 8.20 The debate culminated in the Legal Services Bill, announced in September 2008, introduced to Parliament in September 2009 and passed as the Legal Services (Scotland) Act in September 2010. This Act allowed for the introduction of ABS in Scotland, subject to appropriate regulation to maintain public protection and quality of service. A Bill Reference Group (BRG)<sup>116</sup> was set up in autumn 2008 to support policy development alongside the Scottish Government's consultation in January 2009. Of the 47 responses, two thirds were from organisations (for example, law firms, representative bodies and consumer bodies) and one third from individuals. Responses were broadly supportive of the introduction of ABS with a minority claiming ABS could threaten the independence of the legal system and there was not sufficient evidence to support its introduction.<sup>117</sup>
- 8.21 Under the new ABS proposals for Scotland, there may be a maximum of three approved regulators with the ability to issue licences for the setting up of inter-disciplinary firms. There was no need felt to set up a Legal Services Board equivalent as the structure of organisation in the Scottish legal sector was seen to be much simpler than the English set up. One of the significant differences in the Scottish ABS model is the minority outside ownership provision which limits external ownership of ABS in Scotland to 49 per cent.<sup>118</sup>
- 8.22 The current regulatory framework is illustrated in Figure 8.4.

<sup>116</sup> The BRG included representatives from the Society, the Faculty, Consumer Focus Scotland, the Scottish Legal Aid Board ('SLAB'), the OFT, and Professor Alan Paterson of Strathclyde University. Issues considered included how best to protect the core values of the legal profession and ensure high quality of service, how to regulate firms which combine legal and other professional services, and how best to support access to justice in the new environment. Discussions were also held with key stakeholders such as Which? and the Institute of Chartered Accountants of Scotland ('ICAS').

<sup>117</sup> [www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background](http://www.scotland.gov.uk/Topics/Justice/legal/17822/10190/profession-reform-1-1/Background)

<sup>118</sup> Law Society of Scotland(2010) '*Society Welcomes Compromise on ABS Ownership*'. Law Society of Scotland, June 2010. Available at [www.lawscot.org.uk/news/press-releases/2010/june-/news\\_20100616\\_1](http://www.lawscot.org.uk/news/press-releases/2010/june-/news_20100616_1)

**Figure 8.4 Regulatory structure in Scotland**



Source: Europe Economics

8.23 The impact of the legislation on advocates and solicitors differ. For advocates, the legislation formalises the regulatory framework that already existed in Scotland but was not set out in statute – it does not make any further changes to the environment in which advocates in Scotland operate, contrary to solicitors, as it does not allow advocates to engage in multidisciplinary practices (ABS). With the exception of additional administrative processes, the expected impact of the legislation on advocates is minimal.

8.24 Approved regulators will only be able to regulate ABS in accordance with regulatory schemes approved by the Scottish Government (following consultation with the OFT) and the Lord President of the Court of Session. No such schemes have yet been approved and, whilst the Society are in the process of drafting such a scheme (in accordance with their declared policy of applying to become an approved regulator), that draft scheme is in the early stages of consideration and discussion both internally and with the Scottish Government. Additionally, the Scottish Government are still in the process of drafting and promulgating regulations to allow implementation of parts of the new legislation.

- 8.25 Consequently, no legal businesses – solicitors, advocates and others – in Scotland have yet experienced any change to regulatory requirements as a result of the legislation. There will be few changes to the way in which traditional practices in Scotland are regulated - the principal sources of legislative requirements for such practices remain the Solicitors (Scotland) Act 1980 (as amended) and the Legal Profession and Legal Aid (Scotland) Act 2007 (as amended). Although the new legislation does contain provisions which affect regulation of the traditional profession (for example, the Society as regulator of the traditional profession has an obligation to act in a way which is compatible with the new regulatory objectives) these are primarily at a 'principles' level and have not yet resulted in any significant differences in the detailed regulation to which the traditional profession is subject.
- 8.26 A centralised Scottish Legal Complaints Commission (SLCC) was established in 2008 to handle all consumer complaints. As in England and Wales, the first tier of the complaints system is in-house for instance, directly with the relevant solicitor or advocate. Where the complaint cannot be resolved in-house, it is submitted to the SLCC regardless of whether it is a complaint about service or professional conduct. The SLCC determines whether it is a complaint on service, in which case it is kept by the SLCC, or conduct, in which case it is referred to the Faculty of Advocates or the Law Society of Scotland (very serious conduct complaints are referred by the Law Society to the Scottish Solicitor's Discipline Tribunal, an independent body which mainly deals with serious disciplinary issues and appeals made by solicitors to the Law Society). As such, the SLCC represents a one-stop point of contact for consumers and removes the need for them to identify the nature of the complaint and the appropriate body to lodge the complaint with.

### **Northern Ireland**

- 8.27 The legal services system in Northern Ireland is largely self-regulating. Solicitors are governed by the Solicitors (Northern Ireland) Order 1976 (the Order 1976). Under the Order 1976, the Law Society acts as the regulatory authority governing the education, accounts, discipline and

professional conduct of solicitors.<sup>119</sup> In exercising its regulatory function, the Law Society of Northern Ireland is subject to the oversight and supervision of the Lord Chief Justice for Northern Ireland. It is also subject to oversight from the Lay Observer in relation to complaints-handling.<sup>120</sup> Until the implementation of the review of the judicial system envisaging the devolvement of powers to the Justice Minister, the system in Northern Ireland had not undergone any significant changes. Regulation of solicitors rests with the department of Finance and Personnel. The Finance Minister himself expressed strongly his discontent with the current regulation.<sup>121</sup>

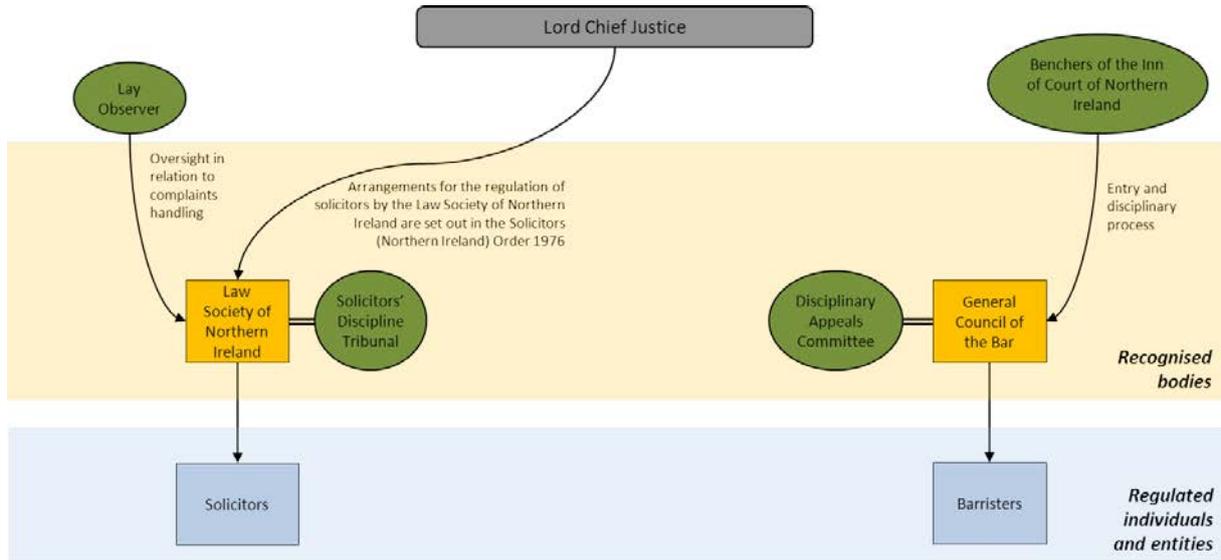
- 8.28 Statute does not provide a basis for regulation of barristers, which is self-regulated by the General Council of the Bar. It has the authority to set rules concerning conduct, professional practice, entry to the profession, on-going training and professional development, and any other area relating to the practice of a barrister in Northern Ireland. It is assisted by an organisation known as the Benchers, who are members of the Inn of Court of Northern Ireland (the Inn). The Benchers of the Inn have control over the entry into the Bar and ultimate control of the disciplinary process.
- 8.29 The regulatory structure of the legal services profession in Northern Ireland is illustrated in Figure 8.5.

<sup>119</sup> Law Society of Northern Ireland (2012). 'Role of Law Society'. Retrieved from [www.lawsoc-ni.org/role-of-the-law-society](http://www.lawsoc-ni.org/role-of-the-law-society)

<sup>120</sup> Department of Finance and Personnel (2006). 'Legal Services in Northern Ireland: Complaints, Regulation, Competition', Legal Services Review Group. Norwich: The Stationary Office. Retrieved from [www.dfpni.gov.uk/legal\\_services.pdf](http://www.dfpni.gov.uk/legal_services.pdf)

<sup>121</sup> Finance Minister Sammy Wilson (26 August 2010). Retrieved from [www.northernireland.gov.uk/news/news-dfp/news-dfp-august-2010/news-dfp-260810-wilson-highlights-need.htm](http://www.northernireland.gov.uk/news/news-dfp/news-dfp-august-2010/news-dfp-260810-wilson-highlights-need.htm)

**Figure 8.5 Regulatory structure in Northern Ireland**



Source: Europe Economics

8.30 In December 2005 the Government established the Legal Services Review Group to recommend to the Minister of Finance and Personnel how the legal professions in Northern Ireland should be regulated.<sup>122</sup> As part of the review, published in 2006, the Legal Services Review Group considered a number of regulatory prohibitions in detail. In particular:

- associations between barristers are not permitted, nor are associations between barristers and solicitors
- legal disciplinary practices and multi-disciplinary practices (for instance, alternative business structures) are also prohibited, as is the external ownership of law firms.

8.31 However, the Review came to the conclusion that removing these prohibitions could reduce competition rather than raise it. In particular, allowing barristers to form associations would, by bringing them together in larger units, reduce competition amongst them. This also rules out the possibility of barristers forming legal disciplinary practices

<sup>122</sup>Department of Finance and Personnel (2006). 'Legal Services in Northern Ireland: Complaints, Regulation, Competition', Legal Services Review Group. Norwich: The Stationary Office. Retrieved from [www.dfpni.gov.uk/legal\\_services.pdf](http://www.dfpni.gov.uk/legal_services.pdf)

with solicitors and of multi-disciplinary practices. An additional argument provided against multi-disciplinary practices is that the idea is largely untested and subject to regulatory confusion – the regulation of professionals from different backgrounds and services within a single firm could undermine the regulation of professional standards, subject practitioners to conflicts of interest, and raise issues of confidentiality.

- 8.32 The Review recommended maintaining self-regulation whilst introducing greater oversight of professional bodies and a thorough revision of the consumer complaints-handling system in Northern Ireland, for reasons outlined in the next section, as the risk of consumer detriment as a result of these systems is high. In 2011 the Bar Council of Northern Ireland modified its rules to address OFT concerns with respect to competition on the level of fees charged and to facilitate practice for barristers from outside Northern Ireland.

## **Potential sources of consumer detriment**

### **Scotland**

#### **Restrictions on entry and exit**

- 8.33 While data are not sufficient to generate any firm conclusions, industry feedback suggests that to date there have tended to be sufficient devil masters to meet the demand from prospective advocates. There is, however, a potential issue for market entry in terms of the employment status of advocates. Advocates are only allowed to be self-employed and can only access customers via referrals from solicitors. As a result, there is a high degree of financial uncertainty surrounding their earning ability once qualified. Many advocates, therefore, have traditionally acted as solicitors for a number of years prior to training to become an advocate. In this way they can ensure that they have sufficient contacts and a reputation with those responsible for referring clients to them (for instance, solicitors) to create a viable income stream. The fact that advocates were excluded from the new ABS system means that the development of such practices will not help to address such access issues.

- 8.34 At the entity level, legislation allowed the introduction of ABS, limiting non-lawyer ownership to 49 per cent (compared with no ownership cap in England and Wales) and prohibiting advocates from participating. However, as there are currently no approved regulators in Scotland, there are currently no approved ABS (though certain organisations have expressed an interest in such business structures). This makes it difficult to assess the impacts of the new system on barriers to entry.
- 8.35 While such limitations on ABS may be justified to ensure quality, partial-liberalisation may continue to create costs for consumers by limiting the scope for competition in the provision of legal services. Any requirements that restrict supply of legal services may limit any potential for increased competition and access for consumers, originally envisaged by the reforms. Certainly, the restrictions suggest that there will be a less dramatic impact on barriers to entry than one might expect in England and Wales.
- 8.36 Scotland has limited the number of licensing authorities to three, although only one – the Law Society – has applied for authorisation to licence. The fewer the licensing authorities, the more limited the range of ABS may be, particularly if authorising bodies focus on specific types of ABS in their licensing regime. This is especially the case in Scotland, where advocates are prohibited from participating in ABS and therefore any licensing authority will be additionally limited to licensing ABS structures composed mainly of solicitors. It is very likely that ABS will carry out the same type of work as solicitors currently perform.

### Regulation of ABS

- 8.37 The potential for multiple regulation, once ABS exist, is the same as in England and Wales. At this stage, it is unclear whether entity requirements will take precedence over individual requirements, as is provided in the Legal Services Act 2007 for England and Wales. This provision has significantly reduced the potential for complexity in the regulation of ABS in England and Wales, and its absence may result in a significantly more complex regulatory structure than presently.
- 8.38 The extent of consumer detriment will depend on the take-up of ABS. Industry feedback suggests advocates enjoy their self-employed status,

so it is unlikely there will be a push to open ABS to advocates as well as solicitors. It appears, for now, that ABS will be limited to solicitors' involvement and even then we cannot say what take-up will be like. If Scotland follows what appears to be the current path of England and Wales, entities may apply for ABS status primarily in order to allow a non-lawyer partner, subject to the 49 per cent ownership restriction, with no change in services provided. If this is the case, it is unlikely that regulatory duplication will have any significant effects on consumer detriment.

## Consumer complaints

- 8.39 Complaints against legal services in Scotland are channelled through the Scottish Legal Services Complaints Commission (SLCC).<sup>123</sup> The SLCC operates as a 'one-stop shop' for complaints which have not been resolved at the first tier level directly with the supplier of the service. The SLCC then decides whether the complaint is about the service provided, in which case it will investigate and reach a decision on the complaint, or whether it is about professional conduct, in which case it will be referred on to the relevant professional body. This approach means that consumers do not have to make their own judgment about whether a complaint is about service or conduct, a factor that has been identified as a possible source of confusion in the England Wales complaints process.
- 8.40 If the complaint regards conduct rather than service, it is referred to the appropriate body – the Law Society of Scotland, Faculty of Advocates or the Association of Commercial Attorneys. The Law Society of Scotland carries out an initial investigation and can decide to prosecute more serious cases before the Scottish Solicitors' Discipline Tribunal (SSDT). The most severe sanction available to the SSDT is to strike an individual off the Roll of Solicitors, which effectively removes the individual's right

<sup>123</sup> Previously, unresolved complaints could be taken to the Scottish Legal Services Ombudsman (SLSO) where staff investigated how the complaint had been handled by the professional body. The office of the SLSO was abolished to make way for the SLCC.

to practise as a solicitor in Scotland.<sup>124</sup> Similarly, the Faculty of Advocates also carries out an initial investigation through its internal Complaints Committee, which may refer a complaint for determination and/or disposal to the Faculty's Disciplinary Tribunal. The Tribunal may suspend or expel an advocate from the Faculty.<sup>125</sup>

- 8.41 The independence of the SLCC is similar to that of the Office of Legal Complaints and by extension the Legal Ombudsman. However, unlike England and Wales, there has been limited separation between representational functions and regulatory functions of the professional bodies currently regulating solicitors, advocates and commercial attorneys until the recent appointment of the Regulatory Committee in the Law Society of Scotland which includes non-solicitors. This committee is responsible for monitoring the Society's regulatory work and for considering new rules and regulations for solicitors. The Society's current regulatory sub-committees will report through it, rather than directly to the Society's Council. While service complaints are assessed by the SLCC, conduct complaints remain under the jurisdiction of the professional bodies.
- 8.42 The Society's Disciplinary Tribunal is independent in governance, however cases are passed through the Law Society before they are referred to the Tribunal, and only very serious cases and appeals are referred. The independence of the Faculty's Disciplinary Tribunal is unclear. Nevertheless, cases are also passed through the Faculty before they are referred to the Tribunal. As such, there remains a potential conflict of interest concerning conduct complaints, and therefore this may be a source of consumer detriment.

<sup>124</sup> Scottish Solicitors' Discipline Tribunal. 'About SSDT'. Available at [www.ssd.org.uk/about/index.asp](http://www.ssd.org.uk/about/index.asp)

<sup>125</sup> Faculty of Advocates 'Summary of Complaints Procedures'. Available at [www.advocates.org.uk/complaintsprocedures.html](http://www.advocates.org.uk/complaintsprocedures.html)

## Northern Ireland

### Restrictions on entry and exit

- 8.43 There have been no changes in the restrictions to entry in Northern Ireland since the 2006 review, therefore the extent of consumer detriment resulting from restrictions on entry has not changed – at the individual and entity levels.
- 8.44 At the entity level, the 2006 Review came to the conclusion that removing restrictions on entry to ABS could reduce competition rather than raise it – allowing barristers to form associations would, by bringing them together in larger units, reduce competition amongst them. It was concluded that, given the limited size of the market in Northern Ireland, introducing ABS would simply reduce the number of existing participants rather than increase entry of new participants, thus increasing the potential for consumer detriment by reducing access.

### Regulation of ABS

- 8.45 ABS remain prohibited in Northern Ireland and for this reason regulatory duplication brought about by ABS is not a source of consumer detriment.

### Consumer complaints

- 8.46 Where a client is dissatisfied with a solicitor, he will file a complaint in-house first. If that is unsatisfactory, the client can file a complaint with the Law Society of Northern Ireland. Clients may alternatively complain directly to the Lay Observer or to the Solicitors' Disciplinary Tribunal, although this rarely occurs. The roles of these three organisations are set out below.
- 8.47 The Law Society has delegated the majority of its powers regarding complaints handling under the Solicitors' (Northern Ireland) Order 1976, as amended, to the Client Complaints Committee. The Committee oversees and controls the investigation of complaints relating to unprofessional conduct and inadequate service. The Committee is not independent of the Law Society, although some independent lay members participate in the consideration of clients' complaints.

- 8.48 In serious cases of professional misconduct, the Law Society refers the complaint to the independent Solicitors' Disciplinary Tribunal. In this respect, the system is very similar to Scotland. The Solicitors' Disciplinary Tribunal is statutorily constituted with the status and powers of the High Court. Members of the Tribunal are appointed by the Lord Chief Justice after consultation with the Law Society.
- 8.49 Finally, the Lay Observer can influence good practice in complaint handling. When the Lay Observer disagrees with the Law Society, he can ask the Society's Professional Conduct Committee to assess the complaint. He can also refer cases to the Solicitors' Disciplinary Tribunal.
- 8.50 The Bar Council's complaints procedure was revised in 2003. The Bar Council may investigate any aspect of professional behaviour through its Disciplinary Committee. Two of the five or seven members of the committee are lay members, chaired by a judge. Appeals from decisions of the Disciplinary Committee are referred to the Disciplinary Appeals Committee, composed of three Benchers and a lay person, appointed from a panel determined by the Lord Chief Justice. Both Committees may admonish, fine or suspend barristers. There is no external oversight of the complaints-handling process or of other aspects of the regulation of the Bar. Unlike in England, Wales and Scotland, where public oversight arrangements for the Bar exist, the Lay Observer for Northern Ireland has no remit in relation to the Bar.<sup>126</sup>
- 8.51 The Solicitors' Disciplinary Tribunal and the Bar Council's Disciplinary Appeals Committee are independent in governance, however cases are passed through the Law Society and through the Bar Council before they are referred to the respective disciplinary groups. As such, there remains a potential conflict of interest concerning conduct complaints, and therefore this may be a source of consumer detriment.
- 8.52 Additionally, unlike England and Wales, it is not compulsory for lawyers in Northern Ireland to have in-house complaints procedures (although

<sup>126</sup> Department of Finance and Personnel (2006) [www.dfpni.gov.uk/legal\\_services.pdf](http://www.dfpni.gov.uk/legal_services.pdf)

many do) and it is not compulsory for them to notify clients of these procedures.

## Conclusions

- 8.53 In this section we have carried out a brief review of the regulatory structure for the legal profession in Scotland and Northern Ireland identifying recent changes and aspects which might result in consumer detriment.
- 8.54 The reform programme is at very different stages in Scotland, Northern Ireland and England and Wales. While Scotland has made some moves towards a system similar to that adopted in England and Wales, there remain key differences both in terms of the market structure and the regulatory framework. Meanwhile Northern Ireland has experienced limited change in the regulatory framework over the last five -10 years.
- 8.55 New legislation introduced the possibility of ABS being licensed but at present no regulatory body has been authorised to issue licences. The scope for ABS in Scotland is more limited than in England and Wales. Advocates cannot participate in ABS and there is a limit on the extent of non-lawyer ownership.
- 8.56 The professional regulatory bodies continue to combine regulation and representational functions although separate disciplinary bodies exist to assess serious cases of misconduct.
- 8.57 The SLCC was set up in 2008 as a 'one-stop shop' for complaints and provides an initial filter to separate service complaints, which it handles and complaints about conduct which are referred on to the appropriate regulator.
- 8.58 In the case of Scotland it is too early to identify the costs and benefits of the reforms. That said there are a number of areas that would warrant further examination in the future, once the changes have been fully implemented:
- The impact on entry barriers created by the structure of the ABS system, in particular the number of licensing authorities permitted,

and the limitations on ownership by non-lawyers. As the two systems develop comparison between ABS development in Scotland and England and Wales should become possible.

- The existence of any barriers to entry to the advocate profession created by continued restrictions on client access to advocates and the way in which advocates are allowed to organise themselves.
- The scope for multiple regulation of ABS to limit the range of services offered and the price and/or quality of the services provided. Again comparison between Scotland and England and Wales may be of value.
- The impact of the lack of independence of the professional bodies handling consumer complaints about conduct on confidence in the redress system, and the scope for consumer detriment to go unaddressed.

8.59 In Northern Ireland, in the absence of any policy reform the focus of any on-going work should continue to consider issues of access, market entry and the legitimacy of the complaints process.

## **9 CONCLUSIONS**

### **Recent developments**

- 9.1 The changes to the legal regulatory structure introduced in England and Wales by the Act have gone a considerable way to addressing the concerns identified by the OFT (2001) and Clementi (2004). There is now a clear separation between regulation and representative activities in each of the branches of the profession with regulatory functions progressively increasing the independence of their activity from the parent body which carried out representative work. This separation of functions should remove the actual or perceived conflict of interest inherent in the previous structure and should enhance consumer confidence in using the regulated services.
- 9.2 The LSB has overseen this development and has also driven the move towards outcomes based regulation. This is intended to provide stronger but less intrusive regulation but is still in an early stage of development with some additional costs as new systems are developed.
- 9.3 The LSB has now authorised two regulators to provide licences for ABS but that is a recent development and, at the start of August 2012, only 16 ABS had been licensed. ABS provides great opportunity for new business structures to develop, for innovation in the range of services supplied and in the way competition develops in the market. So far change in business structure has been the main driver in seeking an ABS licence but other developments are expected to follow.
- 9.4 The development of the Legal Ombudsman also meets one of the original objectives that there should be a single organisation to address complaints about service that cannot be resolved with the provider.

### **Regulatory overlaps and unregulated services**

- 9.5 These are positive developments but the structure of regulation remains complex with distinctions between reserved and unreserved activities, regulated and unregulated activities and separate regulation of individuals and entities. A full review of the merits of these distinctions is beyond the scope of this study but we have sought to identify any

overlaps both in regulation and the handling of consumer complaints and areas where a lack of regulation means that there are limited options for consumer redress.

- 9.6 On the regulatory side unreserved activities provided by unregulated individuals or entities are effectively unregulated. Will writing is the best known example. The LSB is considering whether will writing should be brought within the reserved activities. Any extension of regulation to this or other activities would need to be justified both in terms of the rationale for intervention – for example, correcting for information asymmetry – and by identifying benefits that outweigh the cost of regulation. That sort of impact assessment is outside the scope of this report.
- 9.7 We have also identified regulatory duplication where individuals and entities may be subject to more than one regulatory regime depending on the nature of their main business. However the responses we received from our interviews did not highlight this as a major regulatory burden. The lead regulatory responsibility is usually clear. This may become more of an issue with the growth of ABS. These businesses may face additional regulatory costs in reporting to more than one regulator as the range of services expands.
- 9.8 The potential for consumer confusion on where to lodge a complaint has been reduced with the creation of the LO but has by no means been eliminated. The distinction between authorised and unauthorised individual and entities and between poor service and professional misconduct is not always clear to the consumer and it can take time for a complaint to be directed to the right body. Overlap between different Ombudsmen – for example, the LO and FOS – has not been a major issue so far but could become more significant as ABS develop. The LO and the FOS are working together to address this development. Unreserved activities provided by unregulated bodies fall outside the scope of the LO and this remains an area where there is no formal consumer complaints process, unless covered by trade association codes of conduct.

## **Restrictions on entry or development**

- 9.9 We have reviewed two aspects of regulation that might be restricting entry or development. These are the process for becoming authorised to provide training to barristers and the application processes for becoming ABS licensing bodies and becoming a licensed ABS.

## **Pupillage places**

- 9.10 We find that for every pupillage place there are on average six applicants, compared to a three to one ratio for solicitor training contracts. While pupillage places are driven by market demand for barristers, the process of becoming a Pupillage Training Organisation may be limiting access to the market.
- 9.11 Using data on the relative proportion of practising barristers that are in-employment versus those that are self-employed, we estimate that there could be potentially nine per cent more pupillages than are currently being offered with in-employment pupillages being under represented. If we assume a similar discrepancy between pupillage places and applicants as exist for solicitors seeking training contracts, we estimate that there would be more than double the current number of pupillages available.
- 9.12 While this does not prove that unnecessary barriers to entry exist for barristers, it does suggest that the area could warrant further exploration. The introduction of ABS may help to alleviate the shortfall in pupillage places by introducing more flexibility in the market and external funding. This is an issue that could be monitored going forward. The report from the LETR at the end of 2012 will also provide a more detailed analysis of training provision and future requirements.
- 9.13 There is a current debate about moving from the traditional title based qualification and regulatory model to an approach based on qualification for specific activities. This could improve risk based regulation and allow greater flexibility for firms to enter the market. Such issues may also warrant further exploration following the forthcoming report on legal education and training by the LETR.

## **Licensing of ABS**

- 9.14 At the entity level the introduction of ABS has removed a key barrier to market entry. The policy is still in the early stages of development with only 16 ABS approved at the time of this study. So far the emphasis of the new ABS has been on making non-lawyers partners and increasing their offering of legal services.
- 9.15 Data on the application processes, both at the licensing authority level and the firm level are limited. However, based on feedback from industry we estimate that on average it costs between £27,000 and £160,000 more to gain authorisation as an ABS compared to the traditional model. It is however important to view these estimates in the context of the very recent introduction of the application process — there could be an element of learning by doing which would suggest that our figures overestimate the cost in the medium to long term.
- 9.16 Overall, while there appear to be no clear barriers to entry for ABS, it remains an open question whether the time and cost of applications is acting as a deterrent. This remains an area that may warrant monitoring in the future given the relative novelty of the reforms.

## **Other ABS issues**

- 9.17 We have considered the extent to which duplication of regulation or conflict between regulations may undermine the benefits of ABS. In particular we identify the scope for regulatory overlaps, both in terms of:
- the regulation of the professional, and
  - the regulation of the entity.
- 9.18 While multiple regulation of the individual is not a phenomenon, and unlikely to raise any significant issues, multiple regulation at the entity level would be a new dimension resulting from the option for ABS to offer both legal and non-legal services. Having to engage with multiple regulators could substantially increase compliance costs and potentially result in higher prices for consumers, lower quality service provision or

even limit the range of services offered, undermining the concept (and benefits) of a one stop shop for consumers.

- 9.19 We find that so far - for the first 16 ABS - multiple regulation does not appear to pose an issue, since to date the new ABS have not tended to extend their service offering beyond legal services. This trend is likely to continue in the short-term at least. Over time we may see the emphasis shifting away from simple ownership changes to ABS that represent more the diversity envisaged at the policy development stage. For those seeking to diversify their service offering the application process is likely to take longer.
- 9.20 We estimate that the on-going costs of compliance for each additional regulator would be between £900 and £2,100 excluding the fee and any contributions to compensation funds – both of which tend to be calculated in relation to the size of the firm. The scale of the additional compliance costs would also be affected by the extent to which the firm was previously regulated – a company that already has many of the necessary processes in place will be less likely to have to alter their approach substantially. Similarly the scale of the initial one-off investment in compliance functions will affect the scale of any on-going compliance costs.
- 9.21 There is no evidence at this stage that such additional compliance costs have affected either the range of services being offered or the prices being charged to consumers. This should, however, be reviewed going forward when the new system of ABS has had more time to develop.

## **Consumer redress**

- 9.22 The shift to an independent Legal Ombudsman for service complaints in 2010 was aimed at reducing potential conflicts of interest, and interest, and rationalising and streamlining the complaints process. Ultimately improving the quality of service provision in the industry and consumer welfare.
- 9.23 A number of potential issues with the new system, however, exist. In particular:

- the LO only covers authorised persons and entities (whether they are providing reserved or unreserved legal services) — this can raise particular issues where consumers are provided with a single packaged service which can involve authorised and unauthorised providers and potentially relate to services covered by another sector ombudsman, and
- the approved regulators or the organisations to whom they have delegated the power to regulate are still responsible for conduct complaints — this requires consumers to be able to distinguish between service and conduct complaints.

9.24 This implies that in some cases consumer detriment may go unaddressed, either because the legal service provider is not authorised and therefore is not covered by the LO, or because uncertainty about the complaints process deters consumers from lodging a complaint. In addition uncertainty in the process may increase the costs to consumers and complaints handlers of making and addressing complaints.

9.25 There is strong evidence to suggest that consumers are still confused about the complaints process, and such confusion may grow with the development of multi-disciplinary practices.

9.26 Survey evidence suggests that around 15 per cent of users were dissatisfied with the services they received last time they used legal services. There is also survey evidence that the majority of dissatisfied users do not go on to complain about the service they received

9.27 One of the reasons that dissatisfied consumers do not go on to make a complaint could be confusion regarding the complaints process. Uncertainty about the complaints process remains a key issue in the complaint and redress process. Survey evidence suggests that between a quarter and one third of those not fully satisfied with the service received did not complain because of uncertainty about the process.

9.28 Although only a proportion of complaints made are upheld by the LO, this indicates a significant level of consumer detriment which has not been subject to any form of review or redress due to a lack of awareness or confusion over the complaints handling process.

- 9.29 Evidence from approved regulators and the LO indicate that complaints often need to be referred on to an alternative body. Evidence collected via our survey of consumers in the UK supports this, indicating that, following the 2007 reforms, uncertainty remains a key issue in the complaint and redress process.
- 9.30 There are legal services that are unreserved and unregulated, such as will writing and advice about mental health, where there may be no specific route for accessing redress except via trade bodies or the ordinary courts.

## **Scotland and Northern Ireland**

- 9.31 The reform of legal regulation is at very different stages in Scotland, Northern Ireland and England and Wales. While Scotland has made some moves towards the system adopted in England and Wales, there remain key differences both in terms of the market structure and the regulatory framework. Meanwhile Northern Ireland has experienced limited change in the regulatory framework over the last five-10 years.
- 9.32 Legislation in Scotland introduced the possibility of ABS being licensed but at present no regulatory body has been authorised to issue licences. The scope for ABS in Scotland is more limited than in England and Wales. Advocates cannot participate in ABS and there is a limit on the extent of non-lawyer ownership.
- 9.33 The professional regulatory bodies continue to combine regulation and representational functions although separate disciplinary bodies exist to assess serious cases of misconduct.
- 9.34 The SLCC was set up in 2008 as a 'one-stop shop' for complaints and provides an initial filter to separate service complaints, which it handles and complaints about conduct which are referred on to the appropriate regulator.
- 9.35 In the case of Scotland it is too early to identify the costs and benefits of the reforms. That said there are a number of areas that would warrant further examination in the future, once the changes have been fully implemented:

- The impact on entry barriers created by the structure of the ABS system, in particular the number of licensing authorities permitted, and the limitations on ownership by non-lawyers. As the two systems develop comparison between ABS development in Scotland and England and Wales should become possible.
- The existence of any barriers to entry to the advocate profession created by continued restrictions on client access to advocates and the way in which advocates are allowed to organise themselves.
- The scope for multiple regulation of ABS to limit the range of services offered and the price and/or quality of the services provided. Again comparison between Scotland and England and Wales may be of value.
- The impact of the lack of independence of the professional bodies handling consumer complaints about conduct on confidence in the redress system, and the scope for consumer detriment to go unaddressed

9.36 In Northern Ireland, in the absence of any policy reform, the focus of any on-going work should continue to consider issues of access, market entry and the legitimacy of the complaints process.

## GLOSSARY

**Alternative Business Structures (ABSs):** Firms managed, owned or controlled by a mix of lawyers and non-lawyers offering legal services.

**Authorised Person:** An individual or firm who or which is authorised by an approved regulator to undertake a reserved legal activity.

**Bar Professional Training Course (BPTC):** A graduate course completed by those wishing to practise as a barrister in England and Wales.

**Bar Standards Board (BSB):** Regulates barristers called to the Bar in England and Wales in the public interest.

**Barrister Only Entity (BOE):** Business owned and managed by a barrister or barristers.

**Barrister:** A lawyer regulated by the Bar Standards Board, often specialising in courtroom representation, drafting pleadings, and expert legal opinions.

**Chartered Institute of Legal Executives (CILEx):** Professional body and provider of legal education.

**Citizens Advice Bureau:** Service that provides free, independent, confidential and impartial advice to everyone on their rights and responsibilities.

**Conveyancing:** The processes involved in buying, selling or re-mortgaging a property to transfer its legal title from one person to another.

**Council for Licensed Conveyancers (CLC):** Regulating body for licensed conveyancers in England and Wales. Recently extended its regulatory services to probate and Alternative Business Structures.

**Financial Ombudsman Service (FOS):** UK based independent service for settling disputes between financial service providers and their customers. Deals with complaints from consumers about most financial matters.

**Financial Services Authority (FSA):** Regulator of all providers of financial services in the United Kingdom.

**ILEX Professional Standards (IPS):** The independent regulator of members of the Chartered Institute of Legal Executives (CILEx). It oversees the education, qualification and practice standards of Chartered Legal Executives and promotes proper standards of professional and personal conduct.

**Inns of Court:** Located in London, the professional associations for barristers in England and Wales. All such barristers must belong to one such association.

**Legal Disciplinary Practice (LDP):** A type of law firm where solicitors work alongside other types of lawyers (for instance, licensed conveyancers) and a restricted number of non-lawyers.

**Legal Executive:** A lawyer regulated by ILEX Professional Standards.

**Legal Ombudsman (LO):** An independent body set up to deal with complaints of poor service about all lawyers and law firms of England and Wales. The service to consumers is free. LO was set up in 2010 by the Office for Legal Complaints under the Legal Services Act 2007.

**Legal Services Act 2007 (LSA):** An Act of Parliament of the United Kingdom that seeks to liberalise and regulate the market for legal services in England and Wales, to encourage more competition and to provide a new route for consumer complaints.

**Legal Services Board (LSB):** The independent body responsible for overseeing the regulation of lawyers in England and Wales. It is a non-departmental public body sponsored by the Ministry of Justice. The Board was created by the THE ACT in 2007.

**Office for Legal Complaints (OLC):** The board of the Legal Ombudsman. The OLC ensures that they and the LO promote the regulatory objectives set out in the Legal Services Act 2007.

**Probate:** A legal permission provided by a Probate Registry for someone to deal with someone else's estate after they die.

**Pupillage Training Organisations (PTO):** Barristers' chambers or other approved legal environment that provides pupillage training. Pupillage is a period of 12 months practical work and experience under the supervision and guidance of an established practitioner. It is an indispensable qualification for practice at the Bar of England and Wales.

**Recognised body/sole practitioner:** A body recognised by the SRA under Section 9 of the Administration of Justice Act 1985, a recognised sole practitioner is a solicitor authorised by the SRA to practice as a sole practitioner.

**Regulatory Objectives set out in the Act:** (1) protecting and promoting the public interest (2) supporting the constitutional principle of the rule of law (3) improving access to justice (4) protecting and promoting the interests of consumers of legal services (5) promoting competition in the provision of legal services (6) encouraging an independent, diverse, and effective legal profession (7) increasing public understanding of the citizen's legal rights and duties (8) promoting and maintaining adherence to the professional principles.

**Reserved Legal Activities:** Services that can only be conducted by authorised personnel. Activities are defined as: (1) exercise of rights of audience (2) conduct of litigation (3) reserved instrument activities, being certain activities concerning land registration and real property (4) probate activities (5) notarial activities and (6) administration of oaths.

**Scottish Legal Complaints Commission (SLCC):** Receives all complaints about legal practitioners in Scotland. Commission resulted from the Legal Profession and Legal Aid (Scotland) Act of 2007.

**Society of Will Writers:** A non-profit, self-regulatory organisation that both promotes the need for a valid will and acts as a self-regulatory body by vetting practitioners through stringent membership requirements, proficiency standards, and on-going training.

**Solicitor Regulation Authority (SRA):** The regulatory body for more than 120,000 solicitors in England and Wales. The SRA was launched in January 2007, when The Law Society delegated its regulatory powers to the new organisation.

**Solicitor:** A lawyer who has been admitted as a solicitor by the SRA and whose name appears on the roll of solicitors. Solicitors provide expert legal support and advice to clients.

**Student Training Framework:** Handbook created by the Council for Licensed Conveyancers which outlines the process to be awarded a Practising License.

**The Bar Association for Commerce, Finance, and Industry (BAFCI):** Represents the interests of employed and non-practising barristers providing legal services in commerce, finance, and industry. BAFCI provides representation, education, and support to barristers working in a commercial environment, organizes seminars and events throughout the year

**The Bar Council:** A professional association for barristers in England and Wales. Established in 1894, it acts as a disciplinary body and a regulatory body through the Bar Standards Board, also represents the interests of barristers.

**The Law Society:** The representative body for solicitors in England and Wales.

**Unauthorised person:** An individual who has not been authorised by the SRA or other approved regulator to carry on a legal activity.

**Unreserved Legal Activities:** Services that fall outside the realm of reserved activities, can be conducted by those who are not authorised legal professionals, activities include will-writing, immigration and medical.

**Unregulated person:** An individual who has not been authorised by the SRA or other approved regulator and is thus not regulated by the Authority.

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## **B QUESTIONNAIRE FOR REGULATORS AND PROFESSIONAL BODIES**

### **Regulation**

How has the burden of regulation changed since implementation of the LSA?

How has the oversight role of the LSB affected regulation? Positive? Negative?

How has the division between regulatory and representative responsibilities affected individual lawyers? Has this led to a clearer distinction in the role of separate organisation?

Is regulation by more than one body a burden for individual lawyers or entities? Has this got worse since LSA 2007? Is it more of an issue for ABS than for traditional firms? What effect has this had on the cost of compliance? (prompt +/- 5 per cent, 10 per cent etc)

Are there regulatory gaps that should be filled? (prompt – will writing, representation at tribunals)

Does the distinction between reserved/unreserved activities cause confusion?

Alex, do we still need this after clarification from the Law Society [What is the distinction between unauthorised and unregulated persons (versus authorised, who provide reserved legal activities)? From our understanding, authorised may provide reserved legal activities, unauthorised may not provide reserved legal activities but are employed by an authorised person and unregulated is someone who may not provide reserved legal activities and is either self-employed or not employed by an authorised person.]

Are there areas where regulation could be improved?

### **Consumer complaint**

How well informed are consumers about how to make a complaint about legal services? Has awareness improved in recent years?

Has creation of Legal Ombudsman improved the ability of consumers to get complaints heard and get redress?

Has creation of Legal Ombudsman reduced the cost to consumers of getting complaints heard and getting redress?

Has creation of Legal Ombudsman improved the service provided to consumers when dealing with complaints?

Has creation of Legal Ombudsman reduced the cost to regulators of dealing with complaints?

Are there overlaps between different complaint handling regimes? (prompt for example, Financial Ombudsman, Property Ombudsman). If so how should they be dealt with?

Are there gaps in complaint handling?

Does creation of ABS alter the need for complaint handling?

Any suggestions for improvement?

Barriers to entry

Are there particular regulatory hurdles that are seen as a barrier to entry or expansion? (prompt – financial requirements, management requirements) Has ABS reduced the regulatory barriers?

What challenges do firms face in achieving ABS status?

How much does it cost for firms to achieve ABS status?

How much additional entry would there be of ABS firms if this cost was removed?

Have regulatory requirements for a new entity increased or reduced in the past five years?

How much does it cost to train as a solicitor/barrister/other authorised personnel?

How much additional entry do you think there would be as solicitors/barristers/other authorised personnel if the regulatory requirements for these positions were removed?

Is the availability of well qualified lawyers a constraint on growth?

Is the availability of training course or training places in practices a constraint on growth?

How strong is competition in the market for legal services? Are some services more competitive than others?

Can you give examples of innovation in the provision of legal services that has improved the choice available to consumers?

How does competition affect the quality of services?

## **C QUESTIONNAIRE FOR OMBUDSMEN/CONSUMER GROUPS**

### **Complaint handling**

How difficult/easy do think it is for consumers to make complaints about legal services?

How aware are consumers about how to make a complaint?

How aware are consumers about the different complaint channels, for example financial and legal services? For example, complaints about service and complaints about professional conduct?

How much time do consumers spend on average on identifying the correct complaints channel?

How much time do consumers spend on average on submitting a complaint and their subsequent communications with the Legal Ombudsman?

Do you think there is duplication or overlap between complaint handling for legal services?

Do you think that there are gaps in complaint handling for legal services?

Are consumers given enough information about how to make a complaint? (prompt – by the provider of the service, through other publicity)?

Are consumers deterred from complaining because of complexity of the process or lack of understanding?

Have changes since LSA 2007 improved/worsened/made no difference to consumers' ability to complain about service? And to get redress where services is shown to be poor?

How likely is it that a bad experience with complaint handling leads to a reduction in a consumer's use of legal services in the future?

What changes would you like to see in the way complaints about legal services are handled?

## Service to consumers

Have the changes since LSA 2007 had an effect on the level of service provided to consumers by lawyers?

Have the new business structures arrangements, particularly ABS, led to innovations in the provision of legal services?

How significant a benefit are these changes for consumers?

Have the changes led to any corresponding shift in service prices?

How sensitive are consumers to changes in the prices of legal services?

Are there further changes in regulation you would like to see to improve service to consumers?

## D CONSUMER SURVEY QUESTIONS

### ASK ALL: IM01

Have you ever personally used a legal professional, for example solicitor, barrister, licensed conveyancer, or a legal executive in a personal or professional capacity?

Yes, once

Yes, more than once but fewer than five times

Yes, more than five times

Never

(SP allow DK)

### ASK ALL: IM02

Have you used a legal professional in a personal capacity since 2007? How many times have you used legal professionals since 2007? Please treat multiple contacts with regards to one specific issue as one instance of using a legal professional.

INTERVIEWER: Please probe for best estimate

Yes, once

Yes, more than once but fewer than five times

Yes, more than five times

Never

(SP allow DK)

### ASK ALL CODING 1-3 (YES) at IM02: IM03

Since 2007 what type of legal services have you used? Select as many as relevant.

Advice on interpretation of the law or other codes and how it applies to your circumstances

Acting on behalf of you in your dealing with other people or bodies

Representing you in legal proceedings such as court action or hearings

Preparation of contracts or other documents (excluding wills)

Certificate/Notarisation of Documents

Will or Probate

Conveyance/Mortgage

Other [please specify]

(Multi code allow DK, REF)

**IM04**

Before using the legal service(s) were you aware of the process for making a complaint about the service if you were unhappy with it? And if so, did you feel you understood the complaints process?

I was unaware of the process

I was aware but did not fully understand the process

I was aware of the process and felt that I understood it

Ask IM05 to all coding 3 at IM04: **IM05**

Was the process for making a complaint made clear to you by your provider of legal services?

On all occasions

On most occasions

On some occasions

On no occasions

Can't remember

ASK ALL CODING 1-3 (YES) at IM02: **IM06**

If you are unhappy with the quality of legal services you have used, you are able to complain to an independent body if you felt the provider did not satisfactorily resolve your complaint? Are you aware of this?

Yes

No

Ask IM06b if respond No to IM06: **IM06b**

Would knowing that you can complain to an independent body if you are unsatisfied make you more or less likely to use legal service in the future?

More likely

Make no difference

Less likely

Don't know

ASK ALL CODING 1-3 (YES) at IM02: **IM07**

Can you tell me if you were always satisfied with the service you received? Would you say...

**Yes always**

**More often than not**

**About half the time**

**No less often than not**

**Never**

(Single Code allow DK)

ASK IM08 if you responded no to question IM07 (**No = we'll net the codes 2+3+4+5**): **IM08**

Did you ever seek advice from anyone about how to complain or seek redress?

Who in particular did you ask? Please mention all that apply.

No – did not seek advice

Yes, Friends/family

Yes, the provider of the service you wanted to complain about

Yes, Citizens Advice Bureau

Yes, Consumer organisation e.g. Which?

Yes, Your employer

Yes, Trade Union

Yes, Legal regulator

Yes, Legal Ombudsman

Other – please specify

(Multi Code allow DK)

**IM09**

Did you ever complain or seek redress?

Yes

No

(Single Code allow DK)

ASK IM10 if code Yes at IM09: **IM10**

How easy or difficult was it to identify the correct body to lodge your complaint with?

Very easy

Fairly easy

Neither easy nor difficult

Fairly difficult

Very difficult

(Single Code allow DK)

ASK IM11 if code Yes at IM09: **IM11**

How satisfied or unsatisfied were you with the complaints process?

Very Satisfied

Fairly satisfied

Neither satisfied nor dissatisfied

Fairly dissatisfied

Very dissatisfied

Don't know

Ask IM11b if respond Not satisfied at IM11 (codes 3-5): **IM11b**

If not, what was the reason you were not satisfied with the complaint process?

INTERVIEWER: select all from the following list that are applicable)

The complaint process was unclear

I had difficulty finding the right person or body to complain to

Time taken to resolve the complaint

You did not feel properly consulted

The reasons for the outcome of the complaint were not made clear

Other - please specify

**Ask all coding no (2, 3, 4 or 5 at IM07) AND code No at IM09 (for instance, not satisfied but did not complain): IM12**

For those instances where you were unsatisfied with the service you received but did not complain/seek redress, why did you not? Please select as many as relevant

I did not know I could

I did not know who to complain to

I did not know how to make a complaint

In light of the potential cost of pursuing a complaint I did not think it was worthwhile

I did not think it was worthwhile given the amount of my time the process would require

You tried to complain but could not find the right body to complain to

I did not trust the complaints process

Other – please specify

(Multi Code allow DK)

ASK ALL CODING 1-3 (YES) at IM02: **IM13**

Have you ever decided to use an alternative to a legal professional since 2007? For example a will writer does not have to be a solicitor, or you may have used a representative from a trade union for example rather than a solicitor in an employment issue.

Yes

No but have considered it

No and have never considered it

(Single code allow DK)

Ask IM13b if code YES at IM13: **IM13b**

On the occasion that you have decided not to use a legal professional, what activity was it for?  
Please mention each occasion if used more than once.

Will writing

Representation for an employment issue

Advice about mental health issues and detention

Other – please specify

(Multi code allow DK)

Ask IM13c if code YES at IM13: **IM13c**

Why did you choose not to use legal services? If you could answer in order of the main reason followed by the next and so on

Too costly

Lack of time

I was advised not to use a legal professional

I was unsure how to find reliable services

I was unsure how to engage a legal professional

I did not have confidence in the providers of legal services

I did not feel that I would be able to make a complaint if things went wrong

My need for legal services was resolved by other means [please state]

I did not consider using a legal professional

(Multi code allow DK)

**IM14**

On the occasion that you decided to use an alternative to a legal professional, were you satisfied with the service you received?

1. On all occasions I was broadly satisfied
2. On at least one occasion I was unsatisfied but took no further action
3. On at least one occasion I was unsatisfied and made a complaint and/or sought redress

ASK IM15 if answered 3 to IM14: **IM15**

How satisfied or unsatisfied were you with the complaint process?

Very satisfied

Fairly satisfied

Neither satisfied nor dissatisfied

Fairly dissatisfied

Very dissatisfied

Don't know.

CLOSE for all CODING 1-3 (YES) at IM02

Ask IM16 to all coding 4 (NO) to IM02: **IM16**

Which of the following best applies to you as to why you have not used a legal professional since 2007?

A situation did not come up where I felt the need to use them

I have been in a situation where I could have used them but chose not to

I used an alternative to a legal professional, e.g. a will writer that was not a solicitor, Citizen's Advice Bureau, Trade Union representative

(Single code allow DK)

Ask IM17 if code '2' at IM16: **IM17**

Why did you choose not to use legal services? If you could answer in order of the main reason followed by the next and so on...

Too costly

Lack of time

I was advised not to

I was unsure how to find reliable services

I was unsure how to engage a legal professional

I did not have confidence in the providers of legal services

I did not feel that I would be able to make a complaint if things went wrong

My need for legal services was resolved by other means [please state]

I did not consider using a legal professional

Other [please specify]

(Multi code allow DK, REF)

Ask IM18, IM19 and IM20 if code '3' at IM16: **IM18**

You mentioned that you decided to use an alternative to a legal professional, what activities was it for? Please mention each occasion if used more than once.

Will writing

Representation for an employment issue

Advice about mental health issues and detention

Other – please specify

(Multi code allow DK)

### **IM19**

And what were the main reasons why you decided to use the alternative to a legal professional? If you could answer in order of the main reason followed by the next and so on...

Too costly

Lack of time

I was advised not to

I was unsure how to find reliable services

I was unsure how to engage a legal professional

I did not have confidence in the providers of legal services

I did not feel that I would be able to make a complaint if things went wrong

I did not consider using a legal professional

(Multi code allow DK, record in order mentioned, REF)

### **IM20**

On the occasion that you decided to use an alternative to a legal professional, were you satisfied with the service you received?

On all occasions I was broadly satisfied

On at least one occasion I was unsatisfied but took no further action

On at least one occasion I was unsatisfied and made a complaint and/or sought redress

ASK IM21 IF code 3 at IM20: **IM21**

How satisfied or unsatisfied were you with the complaint process?

Very satisfied

Fairly satisfied

Neither satisfied nor dissatisfied

Fairly dissatisfied

Very dissatisfied

Don't know.

CLOSE

## E COMPARISON OF SURVEY RESULTS: EUROPE ECONOMICS, YUGOV, GFK, AIMR, CCES

	Europe Economics	YouGov	GfK	aimr	CCES
Source		YouGov (2011) 'First-tier Complaints Handling' Legal Services Board	GfK (2010) 'Research on Consumers' Attitudes towards the Purchase of Legal Services. A research report for Solicitors Regulation Authority'	Acute Insight Market Research (2010) 'Identifying Law Firms Subject to Consumer Complaints to the Legal Ombudsman',	Centre for Consumers and Essential Services (2011) 'Mapping potential consumer confusion in a changing legal market - report for the Legal Ombudsman' University of Leicester
Website		<a href="http://www.legalservicesboard.org.uk/what_we_do/Research/Publications/pdf/final_report_for_lsb_ftch09_06_11.pdf">www.legalservicesboard.org.uk/what_we_do/Research/Publications/pdf/final_report_for_lsb_ftch09_06_11.pdf</a>	<a href="http://www.sra.org.uk/documents/consumer-reports/consumer-research-2010-purchase-attitudes-final.pdf">www.sra.org.uk/documents/consumer-reports/consumer-research-2010-purchase-attitudes-final.pdf</a>	<a href="http://www.legalombudsman.org.uk/downloads/documents/consultations/Consumer_research_report_110224.pdf">www.legalombudsman.org.uk/downloads/documents/consultations/Consumer_research_report_110224.pdf</a>	<a href="http://www.legalombudsman.org.uk/downloads/documents/publications/Consumer_confusion_report.pdf">www.legalombudsman.org.uk/downloads/documents/publications/Consumer_confusion_report.pdf</a>
Summary		Large, quantitative survey. Some similar figures to those researched by our survey.	All qualitative and not particularly relevant to the areas we are looking at – so not much useful to be taken from it.	All qualitative and not particularly relevant to the areas we are looking at – so not much useful to be taken from it.	
Year	2012	2011	2010	2011	2011
Sample	2013 face to face interviews with omnibus	300,000 YouGov panel – online survey	40 face to face in-depth interviews (one hour), 20 amongst recent purchasers and 20 with those intending to purchase	12 mini-group discussions (58 consumers in total) - 10 mini-groups with a broad-based general public and 2 mini-groups with those who identified themselves as very	Literature review and semi-structure interviews with: Citizens Advice, Financial Ombudsman Service, LSB, Legal Services Consumer Panel, Legal Ombudsman, Ministry of Justice, and

				dissatisfied with solicitors	Which?
Excluded	Ages 0-17	Ages 0-17		<p>In addition to the standard exclusions (marketing/market research, journalism, PR), we excluded from the main general public sample those:</p> <ul style="list-style-type: none"> <li>- who say they would never be likely to use a solicitor on the grounds that their level of interest in the issues was likely to be very low,</li> <li>- who have recently been in dispute or are dissatisfied with a solicitor on the grounds that they might hijack the group discussion seeking to gain support for their hostile viewpoint, and</li> <li>- who regularly dealt with solicitors as part of their work/business (such as police, estate agents, other legal professionals, court officials, etc.) on the grounds that they would have a 'professional'</li> </ul>	

				perspective on the issues.	
Quality of service	70 per cent were always satisfied with service, 20 per cent had been happy more often than not, 5 per cent satisfied about half the time, 3 per cent satisfied no less often than not and one per cent never satisfied.				
First-tier complaints	12 per cent of those not always happy with the legal service provided subsequently went on to complain or seek redress. 87 per cent of respondents found it very easy or fairly easy to identify the correct body to lodge their complaint with. Reasons for not complaining included feeling that the time required was not worth taking (27 per cent), not aware of being able to complain (25 per cent), cost (12 per cent).	33 per cent made a formal complaint to their service provider, and 33 per cent raised their concerns with the service provider but did not make a formal complaint, 22 per cent did nothing. Reasons for doing nothing included feeling it wasn't worth it (34 per cent), being so fed up with the whole process they just let it go (34 per cent), cost (24 per cent) and time (12 per cent). Main cause of dissatisfaction with complaints procedure was			

		<p>delays to the amount of time the matter took (43 per cent) and poor quality of service (42 per cent).</p> <p>Satisfaction with the first-tier complaints process has increased from pre October 2010 (36 per cent) to post October 2010 (51 per cent) – provides some evidence that complaints systems are improving with LO.</p> <p>Outcomes of first-tier complaints: fully upheld (31 per cent), partially upheld (30 per cent), rejected (21 per cent) and heard nothing back (14 per cent).</p>			
Second-tier complaints		<p>Only 28 per cent of complainants who were dissatisfied with the outcome of their first-tier complaint subsequently made a second-tier complaint.</p>			
Sources of advice					<p>'It is estimated that 95 per cent of advice provided by CABx is legal advice, and</p>

					over 50 per cent of CABx currently have contracts with the LSC.'
Service providers		Solicitor organisations (72 per cent), other groups, for example, banks, trade unions (nine per cent), licensed conveyancers (four per cent) and barristers (three per cent)			
Areas of law	All - Conveyancing (38 per cent), probate (31 per cent) and acting on their behalf in dealings with other people (24 per cent)	Relating to complaint - Conveyancing (23 per cent), probate (10 per cent) and family matters (10 per cent)			
Expectations regarding complaints and redress system	62 per cent aware of the process for making complaint before using the service 56 per cent had been made aware of the complaint process by the legal service provider 73 per cent aware that they were able to complain to an independent body in case they felt the provider had not satisfactorily resolved their complaint.	13 per cent were told about the in-house complaints procedure 8 per cent were told about the second-tier complaints procedure	'There was minimal knowledge of the redress available in response to a complaint about a legal service. Responses were therefore based on generalised assumptions, and expectations for redress were generally low.'	'There were indications that consumers were often initially reluctant to complain about services/products fearing that the process might become too drawn out, demanding and frustrating. People generally only got engaged with the process of complaining when they felt there was no alternative. Some gave up when they found they would not get satisfaction	

				<p>fairly easily. Others were reluctant to let go when they felt their complaint was justified.'</p> <p>'Spontaneous awareness of the Legal Ombudsman was very limited.'</p> <p>'There was widespread anticipation that involving the Legal Ombudsman would entail a lot of impenetrable forms and the process itself could take a (very) long time.'</p>	
Jurisdictional problems					<p>'There seem to be around 70 solicitors' firms that are dual regulated by the FSA and the SRA and FOS refers some legal expenses insurance claims to the LO when they are about the legal services provided.'</p> <p>'the Legal Ombudsman has estimated that around 9 per cent of the contacts which it signposts to other organisations are referred specifically to the Claims management Regulator and to the professional bodies</p>

					for will writers.'
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## F ADDITIONAL MATERIAL FROM CONSUMER SURVEY

### Annual use of legal services

#### Part 1: Usage of legal professionals

##### Question IM02: Have you used a legal professional in a personal capacity since 2007?

Overall about one third of UK adults (34 per cent) had made use of legal professional services at least once since 2007.

##### Have you used a legal professional in a personal capacity since 2007?

UK constituent countries	Count/per cent				
	Never	Yes, once	More than once but fewer than five times	More than five times	All
England	1109	356	184	36	1685
Scotland	105	39	22	4	170
Wales	79	12	7	0	98
Northern Ireland	42	8	9	0	59
United Kingdom	1336	415	222	40	2012
<b>of which:</b>					
England and Wales	1188	368	191	36	1783
England	66%	21%	11%	2%	
Scotland	62%	23%	13%	2%	
Wales	81%	12%	7%	0%	
Northern Ireland	71%	14%	15%	0%	
United Kingdom	66%	21%	11%	2%	
<b>of which:</b>					
England and Wales	67%	21%	11%	2%	

Base size: 2,012 UK adults – excludes one respondents who answered don't know

If we assign scale mid-point values to each category it is possible to arrive at approximate estimates for the overall usage of legal professional services. The survey design has no scale point corresponding to using a legal professional five times and the

category for 'more than five times' is unbounded. For the purpose of the estimation, the values shown in Table 2 have been used.<sup>127</sup>

Under these assumptions, a rough estimate of the average use of legal professional services over the five-year period since 2007 emerges at just over 0.7 per UK adult.

**Have you used a legal professional in a personal capacity since 2007? Approximate estimates of average usage**

Per cent/average use					
UK constituent countries	Never	Yes, once	More than once but fewer than five times	More than five times	Average <sup>128</sup>
Assumed usage	0	1	3.5	7	
England	66%	21%	11%	2%	0.74
Scotland	62%	23%	13%	2%	0.84
Wales	81%	12%	7%	0%	0.38
Northern Ireland	71%	14%	15%	0%	0.67
United Kingdom	66%	21%	11%	2%	0.73
<b>of which:</b>					
England and Wales	67%	21%	11%	2%	0.72

Combining these results with figures for the adult populations of the constituent countries of the United Kingdom allows estimates of the total usage of legal services since 2007, and approximate usage per year. On this basis it is estimated that UK adults make use of legal professional services about 7.4 million times each year.

<sup>127</sup> We recognise that other assumptions about these values could be made, but the overall results of the analysis are not very sensitive to these.

<sup>128</sup> Assumed usage in each category multiplied by number of respondents in each category.

**Estimated average usage of legal professionals in a personal capacity since 2007 and total usage based on adult populations for UK 2010**

<b>UK constituent countries</b>	<b>Average usage</b>	<b>Adult population (millions)</b>	<b>Total usage (millions)</b>	<b>Usage per year (millions)</b>
England	0.74			
Scotland	0.84	4.3	3.6	0.7
Wales	0.38			
Northern Ireland	0.67	1.4	0.9	0.2
United Kingdom	0.73	50.6	37.0	7.4
<b><i>of which:</i></b>				
England and Wales	0.72	44.9	32.4	6.5

Adult refers to a person aged 16 and over

Sources: ONS; NISRA; Mid-2010 Population Estimates for Scotland

## Demographic analysis of use of legal services

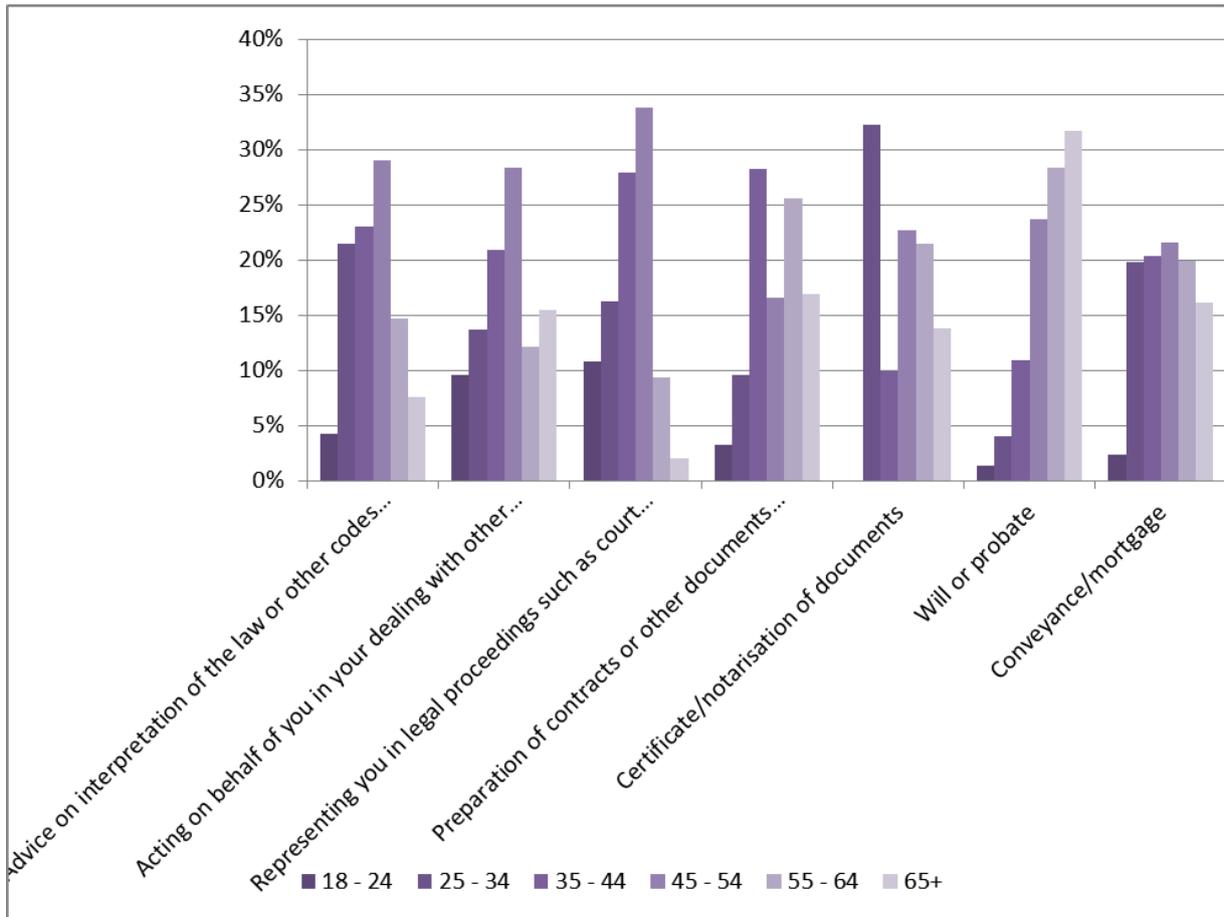
### Percentage of surveyed in England and Wales that used legal services since 2007

	Group size*	Never	Once	More than once but fewer than five times	More than five times	
Total	1,783	67%	21%	11%	2%	
95 per cent confidence interval		+/-2%	+/-2%	+/-1%	+/-1%	
Age	18 - 24	247	88%	8%	3%	1%
	25 - 34	302	68%	21%	8%	2%
	35 - 44	308	63%	26%	9%	2%
	45 - 54	307	58%	21%	17%	3%
	55 - 59	110	53%	20%	23%	4%
	60 - 64	147	60%	29%	10%	1%
	65 +	362	68%	20%	10%	2%
Sex	Female	912	69%	20%	10%	1%
	Male	871	64%	22%	12%	3%
Income level	UP TO £6,499	107	88%	6%	2%	3%
	£6,500 - £11,499	218	75%	16%	7%	2%
	£11,500 - £17,499	216	66%	24%	9%	1%
	£17,500 - £24,999	122	68%	20%	9%	2%
	£25,000 PLUS	517	53%	26%	18%	3%
Qualification	No formal qualifications	303	80%	15%	5%	1%
	Secondary	796	67%	22%	9%	1%
	Still studying	11	100%	0%	0%	0%
	University	538	56%	23%	17%	4%
	Other	134	70%	20%	9%	2%

\* Excluding the one respondent who answered don't know and those who did not disclose the relevant personal details

Source: Europe Economics' consumer survey

### Types of service in England and Wales by age group



Source: Europe Economics' consumer survey

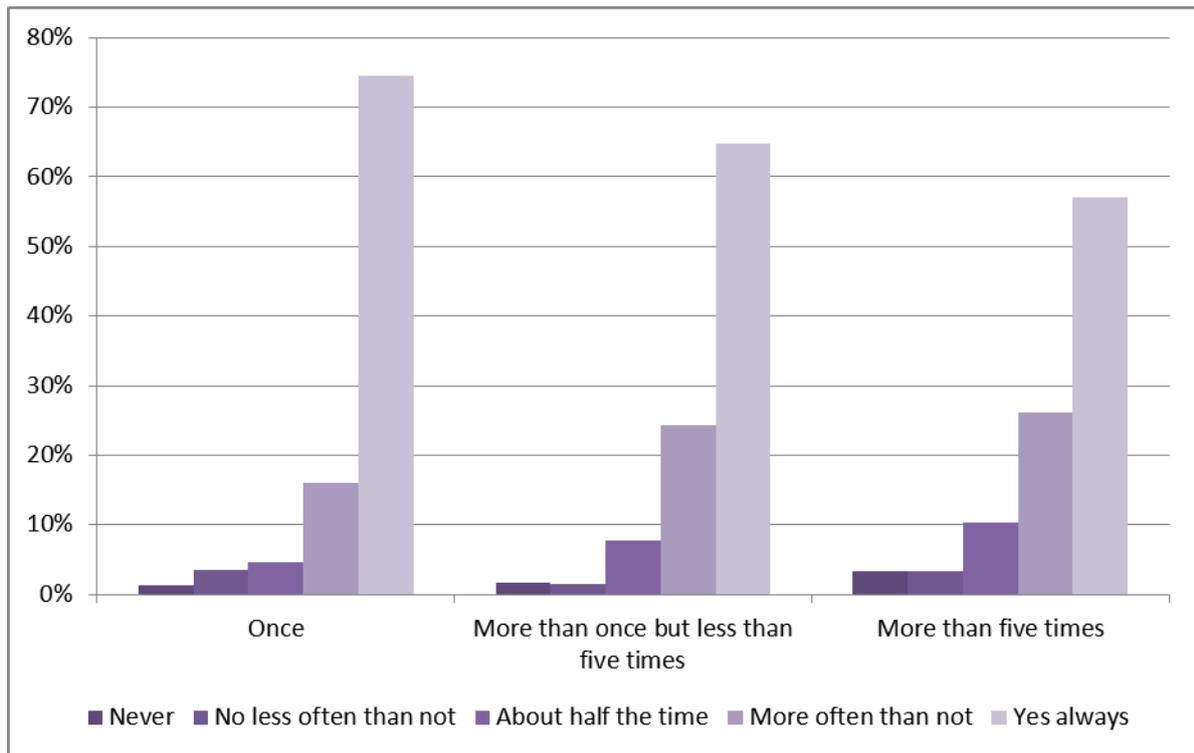
## Percentage of surveyed in England and Wales according to satisfaction

		Group size*	Never	No less often than not	About half the time	More often than not	Yes, always
Total		592	2%	3%	6%	19%	70%
95 per cent confidence interval			+/- 1%	+/-1%	+/-2%	+/-3%	+/-4%
Age	18 - 24	30	5%	0%	0%	18%	77%
	25 - 34	95	0%	6%	7%	15%	72%
	35 - 44	114	2%	4%	3%	27%	64%
	45 - 54	128	3%	1%	11%	22%	61%
	55 - 59	52	0%	4%	5%	15%	76%
	60 - 64	59	1%	2%	5%	14%	78%
	65 +	113	0%	1%	5%	17%	77%
Sex	Female	282	2%	2%	7%	19%	70%
	Male	310	1%	3%	5%	20%	71%
Income	Up to £6,499	12	12%	3%	13%	0%	72%
	£6,500 - £11,499	54	0%	4%	16%	17%	63%
	£11,500 - £17,499	73	0%	6%	8%	28%	57%
	£17,500 - £24,999	38	0%	3%	1%	14%	83%
	£25,000 plus	243	1%	2%	5%	19%	73%
Qualification	No formal qualifications	61	0%	4%	5%	14%	78%
	Secondary	257	2%	4%	7%	20%	68%
	University	233	2%	2%	7%	20%	69%
	Other	40	0%	0%	0%	18%	82%

\* Excluding the three respondents who answered don't know and those who did not disclose the relevant personal details.

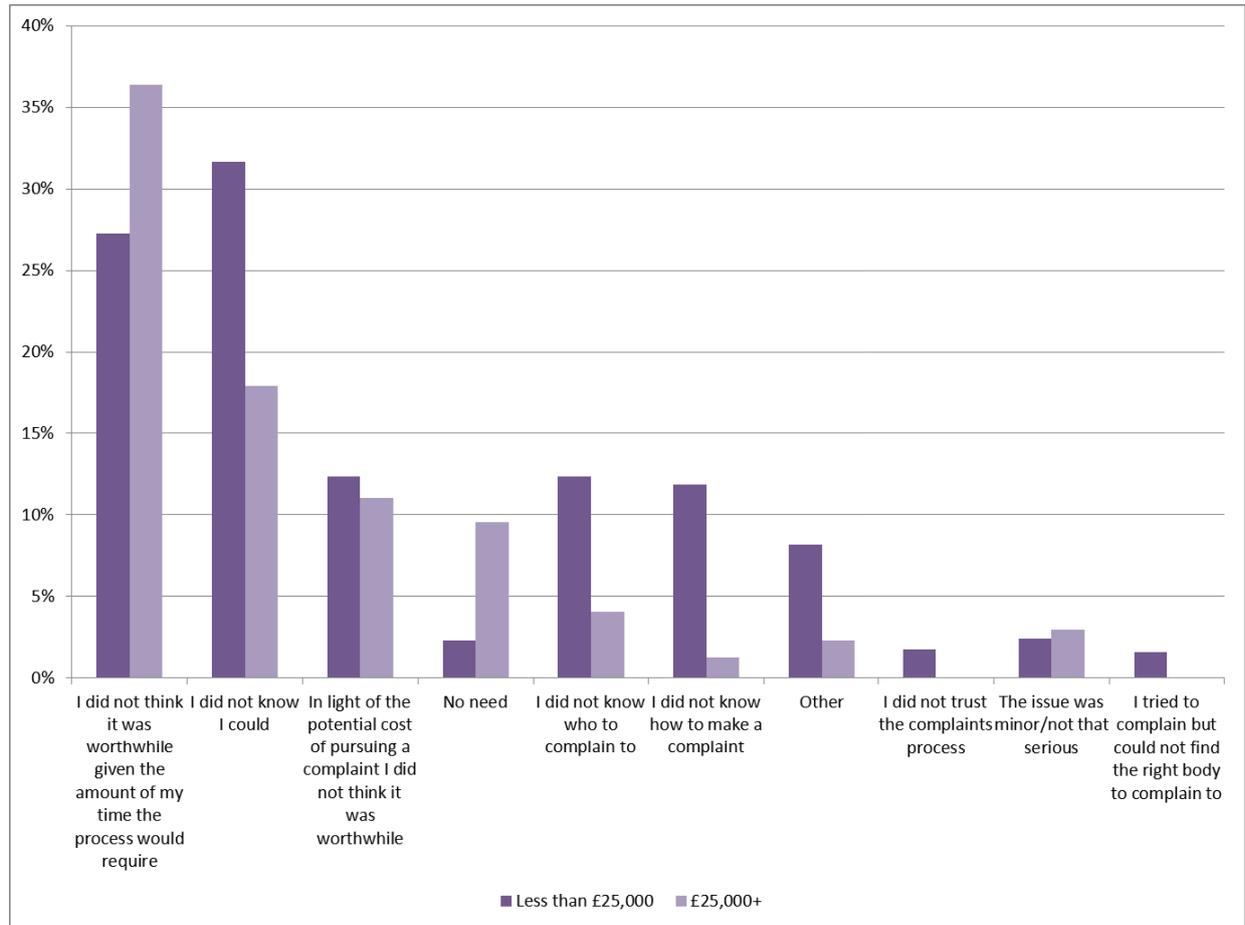
Source: Europe Economics' consumer survey

**Satisfaction of Consumers in England and Wales broken down by frequency of use since 2007**



Source: Europe Economics' consumer survey

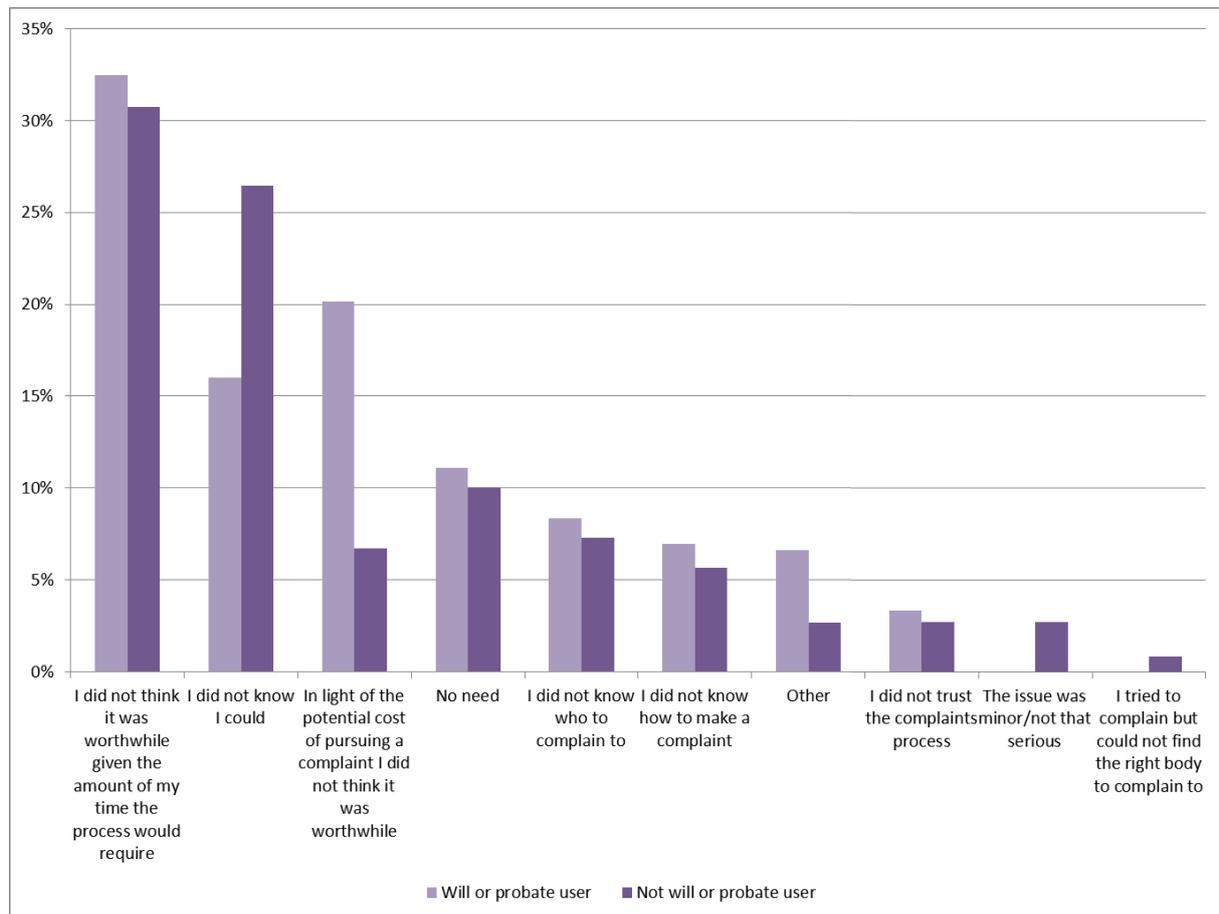
**Reasons why consumers in England and Wales did not complain when dissatisfied with the service received, by income category**



Note: Percentage of the 58/52 respondents in England and Wales who did not complain or seek redress who had incomes up to £24,999/£25,000 +. Respondents were asked to select as many as relevant, so percentages do not add up to 100 per cent.

Source: Europe Economics' consumer survey

**Reasons why consumers in England and Wales did not complain when dissatisfied with the service received by whether they were users of will or probate**

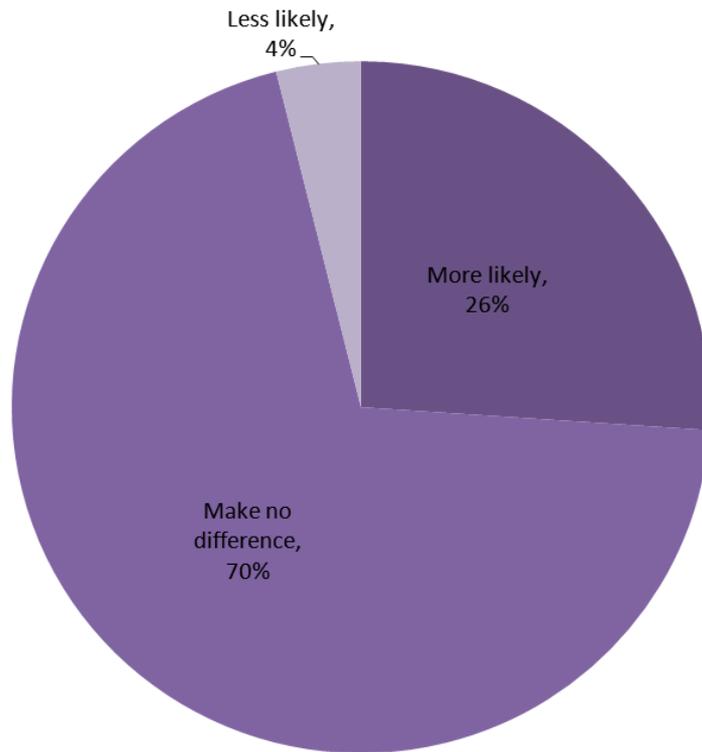


Note: Percentage of the 45/107 respondents in England and Wales who did not complain or seek redress who were users of will or probate/not users of will or probate. Respondents were asked to select as many as relevant, so percentages do not add up to 100 per cent. To note the distinction between wills and probate were made in order to distinguish between reserved and unreserved activities.

Source: Europe Economics' consumer survey

9.37 The majority (72 per cent) of respondents who had used legal services had been aware that they would have been able to complain to an independent body in the case that they felt the provider had not satisfactorily resolved their complaint. Where consumers were not aware of this, while two thirds indicated that this knowledge would not make a difference to their choice to use a legal service in the future, just under a third (26 per cent) indicated that this knowledge would make them more likely to use a legal service in the future.

**Figure 6.12 Likelihood of using a legal service in England and Wales once aware of ability to complain to an independent body**



**Note:** Percentage of 165 respondents who were not aware that if you were unhappy with the quality of legal services used, you are able to complain to an independent body if you felt the provider did not satisfactorily resolve your complaint

**Source:** Europe Economics' consumer survey

**Summary of reasons why consumers in England and Wales did not complain when dissatisfied with the service received**

	All respondents who did not complain or seek redress	Income category		Users of will or probate?	
		Up to £24,999	£25,000 +	Yes	No
Number of respondents	153	58	52	45	107
I did not think it was worthwhile given the amount of my time the process would require	31%	27%	36%	32%	31%
I did not know I could	23%	32%	18%	16%	26%
In light of the potential cost of pursuing a complaint I did not think it was worthwhile	11%	12%	11%	20%	7%
No need	10%	2%	10%	11%	10%
I did not know who to complain to	8%	12%	4%	8%	7%
I did not know how to make a complaint	6%	12%	1%	7%	6%
I did not trust the complaints process	3%	2%	0%	3%	3%
The issue was minor/not that serious	2%	2%	3%	0%	3%
I tried to complain but could not find the right body to complain to	1%	2%	0%	0%	1%
Other	4%	8%	2%	7%	3%

Note: The number of respondents across different income categories does not add up to 153 due to some respondents replying 'Don't know' or 'Refused' to this question.

Source: Europe Economics' consumer survey

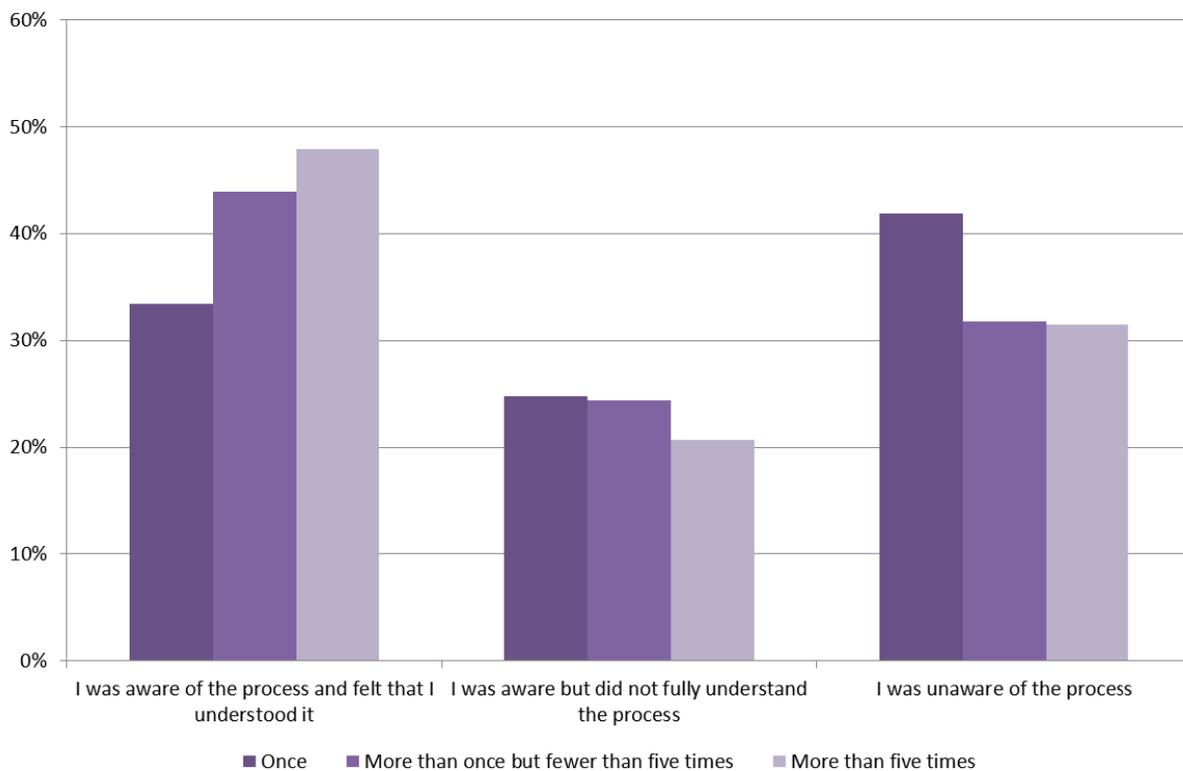
**Consumer awareness of complaints process prior to using legal professional based on experience of ever using legal professionals in England and Wales**

	Respondents who had used a legal professional in a personal capacity since 2007			
	All	Respondents who had ever personally used a legal professional in a personal or professional capacity		
		More than five times	More than once but fewer than five times	Once
Number in category	593*	36	191	366
I was aware of the process and felt that I understood it	38%	48%	44%	33%
I was aware but did not fully understand the process	24%	21%	24%	25%
I was unaware of the process	38%	31%	32%	42%

\* Excluding the two respondents who answered don't know

Source: Europe Economics' consumer survey

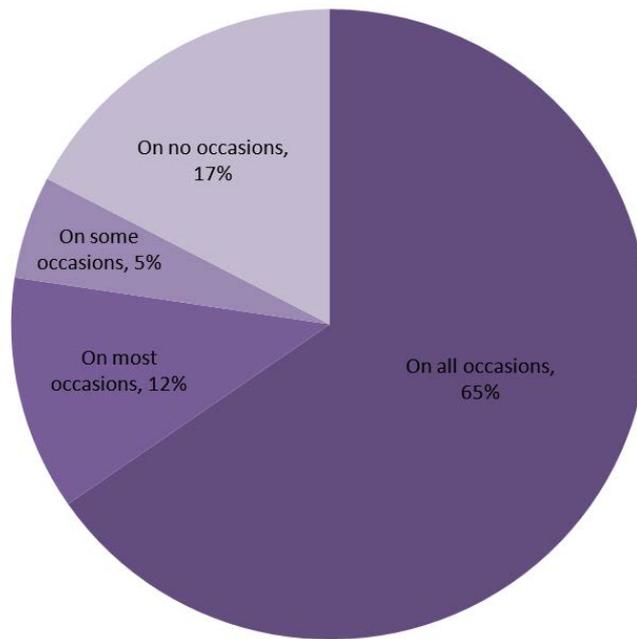
**Consumer awareness of complaints process prior to using legal professional based on experience of ever using legal professionals**



Note: Percentage of the 366/191/36 respondents who had used a legal professional in a personal capacity since 2007 and had used one once/more than once but fewer than five times/more than five times.

Source: Europe Economics' consumer survey

**Proportion of consumers in England and Wales that were made aware of complaints process by the provider of legal services**



Note: Percentage of the 223 respondents who were aware of the process for making a complaint before using the legal service(s) and felt that they understood it, excluding 29 respondents who could not remember

Source: Europe Economics' consumer survey

### List of documents referred to in the Law Society response

Document	Attachment
Barker, G, ANU Centre for Law and Economics, and Law and Economic Consulting Associates, <i>A theoretical framework for assessing the value of legal services</i> (October 2015 - for the Law Society). <b>As yet unpublished, but included in the submission.</b>	<b>A</b>
BDRC Continental, <i>Legal Services Benchmarking Report 2012</i> (for the Legal Services Board) <a href="https://research.legalservicesboard.org.uk/wp-content/media/2012-Individual-consumers-legal-needs-report.pdf">https://research.legalservicesboard.org.uk/wp-content/media/2012-Individual-consumers-legal-needs-report.pdf</a>	
CCBE paper, <i>Position on Regulatory and Representative Functions of Bars</i> (2005) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_reg1_1182254709.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_reg1_1182254709.pdf</a>	
CCBE/IBA, <i>Justice under siege: A report on the Rule of Law in Poland</i> (2007) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/11_2007_Nov06_Report1_1194344860.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/11_2007_Nov06_Report1_1194344860.pdf</a>	
CCBE paper, <i>Position on Non-Lawyer owned firms</i> (2005) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_non1_1182254612.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_non1_1182254612.pdf</a>	
CCBE paper, <i>Position on Multi-Disciplinary Partnerships</i> (2005) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_mdp1_1182254536.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/ccbe_position_on_mdp1_1182254536.pdf</a>	
CCBE paper, <i>Position on Legal Services Board's consultation on a regulatory regime for Alternative Business Structures</i> (2009) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/EN_CCBE_response_to_1_1253701378.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/EN_CCBE_response_to_1_1253701378.pdf</a>	
CCBE paper, <i>Position on the Solicitors Regulation Authority's consultation on new forms of practice and regulation for Alternative Business Structures</i> (2009) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/EN_CCBE_Response_to_1_1253696350.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/EN_CCBE_Response_to_1_1253696350.pdf</a>	
CCBE letter re <i>LSB consultation on Alternative Business Structures approaches to licensing</i> (2010) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/100125_CCBE_letter_t1_1264511673.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/100125_CCBE_letter_t1_1264511673.pdf</a>	
CCBE letter to the Taoiseach re the <i>Legal Services Regulation Bill 2011</i> (2012) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/110112_Letter_Ir_el1_1326374114.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/110112_Letter_Ir_el1_1326374114.pdf</a>	
CCBE/ABA letter to IMF re <i>radical reform of the legal profession</i> (2011) <a href="http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/CCBE_and_ABA_Letter_1_1325686329.pdf">http://www.ccbe.eu/fileadmin/user_upload/NTCdocument/CCBE_and_ABA_Letter_1_1325686329.pdf</a>	
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Regulatory data received by the Law Society from the SRA on a quarterly basis. Subject to a legal agreement with the SRA, we are unable to share	

## List of documents referred to in the Law Society response

Document	Attachment
<p>this dataset in full. Specific aggregate data can be supplied to the CMA on request, subject to confirmation from the SRA.</p>	
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The Law Society

## **CMA Legal Services Market Study: Theories of Harm**



# CMA Legal Services Market Study: Theories of Harm

## Specific Questions raised in the Statement of Scope

### 1. Introduction and executive summary

- 1.1. This submission supplements our first submission to the CMA in response to this Market Study. In this submission we give our views on each of the three theories of harm that the CMA is considering.
- 1.2. In section 2 below, in response to the first theory of harm (the ability of consumers to drive competition through informed purchasing decisions), we indicate the intensity of competition between solicitors firms; describe the wide choice of providers consumers have (regulated and unregulated); set out the criteria consumers take into account in selecting a provider and describe the information available to consumers concerning the costs and quality of legal advice; we set out the ways in which legal service providers seek to acquire customers and describe the role of intermediaries.
- 1.3. In section 3 below, on the second theory of harm (information failures), we describe the obligations on solicitors to provide detailed information to clients on a range of matters (including insurance and redress mechanisms) and contrast this with the lack of such obligations for unregulated providers; we set out the scope for consumer confusion and the distortion of the competitive process where providers offering the same service have materially different obligations.
- 1.4. In section 4 we respond to the third theory of harm (impact of regulation on competition). We set out our views on the scope of regulatory obligations for solicitors which are necessary for the protection of consumers and the public interest; we describe the dangers to consumers, the public interest and competition of unregulated providers offering such critical services without even minimal regulatory protections; we set out why solicitors (and other authorised professionals) should be subject to the same independently determined regulatory obligations (by independent regulators) as other legal service providers with professional bodies responsible for setting any higher standards for the holding of professional title; we indicate why the title „lawyer“ as well as „solicitor“ and „barrister should be protected; we explain that ABS have begun to make a mark on the market but it is too early to judge their long term impact.

### 2. Theme 1: The ability of consumers to drive effective competition through making informed purchasing decisions

- 2.1. As we described in our first submission to the CMA, the legal services market is competitive and highly fragmented with a wide variety of regulated and unregulated providers. Solicitors represent approximately 38-46% of all legal services providers and they compete fiercely among themselves as well as with legal executives, licensed conveyancers, notaries, specialist attorneys and the wider unregulated sector.<sup>1</sup> This

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<sup>1</sup> *The Future of Legal Services*, (TLS, January 2015).

view of the intensity of competition supported by recent independent assessments of the market, for example the IRN Research *UK Legal Services Market* report.<sup>2</sup>

2.2. Competition in consumer law practice, (including residential conveyancing, personal injury and medical negligence, family law, wills and probate, and employment law) is particularly strong and this is resulting in consolidation in some segments of the legal services market as larger firms merge to grow their market share. This is significant because high street solicitors and law firms serving mainly personal rather than corporate customers is the largest market segment in terms of the number of firms and these firms are facing the greatest pressure on revenue and profits. Annual growth in this segment is modest and there is pressure on margins for many firms. It has been suggested that smaller and medium sized consumer law firms will leave the market or be taken over by larger players.<sup>3</sup>

2.3. An April 2014 report by RBS observed:

*“One serious underlying structural challenge for the UK legal services market is that it suffers from over-capacity.....The size and shape of the supply side of the legal market continues to develop, and is characterised by ongoing growth in the number of market participants.”*

*“It is clear that the low growth evident in the market over recent years has forced firms to grow their businesses by capturing market share from competitors”.*

The report expected that legal sector consolidation would continue to drive firms’ growth in the medium term, which in our view is proving to be true.<sup>4</sup>

2.4. The following year’s assessment (published under the by NatWest brand) reached the same conclusion in relation to the competitive pressures on medium-sized firms as a result of the increasing amount of legal services work being taken on by large professional services firms:

*“Mid-tier firms are also suffering intense competition from the big-four accountants, which are quietly taking the more commoditised work away from them (see p16), while clients remain committed to fee reductions and fixed-pricing arrangements across the board. Differentiation and a clear brand identity have never been more important, as clients become much more selective about whom they instruct.”<sup>5</sup>*

2.5. A LexisNexis report on *The Age of the Client*, based on interviews with law firms and their clients, concluded:

*“The consumer culture of 24/7 availability will become even more entrenched, DIY internet-based solutions will spread to other areas of the law and competition from non-traditional sources will continue to*

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<sup>2</sup> *UK Legal Services Market Report 2015* available at:<http://www.irn-research.com/news/uk-legal-services-market-report-2015/>

<sup>3</sup> A number of the observations in this submission are based on the YouGov *Legal Services 2015* report. We have not been authorised by YouGov to quote directly from the report or to disclose all details but the report has influenced our views on the market as described in tis submission.

<sup>4</sup> RBS, *A perspective on the legal market*, April 2014, pp. 10 & 12.

<sup>5</sup> NatWest *A perspective eon the legal market report on legal services 2014-15*, p. 13.

*grow. Against this background of rapid and constant change, lawyers can't afford to become complacent. Only a culture of continuous innovation will ensure they can meet future challenges head-on.*"<sup>6</sup>

75% of respondents to the survey considered „attracting new clients“ as an important challenge for them.<sup>7</sup>

- 2.6. The Society's *Annual Firms Survey 2014-15* found competition for new business a key concern for solicitors when it asked a sample of 1000 firms whether a number of issues were a problem on a scale 1-5 (with 1=no problem to 5=very significant problem).<sup>8</sup> 21% of firms said that „competition for business“ was a significant problem for them (up from 15% in the 2013-14 Survey), with competition for business the (equal) third most common problem after (1st) changes in legal aid (23% of firms saying this was a significant problem), (2nd) costs of employing solicitors (22%), and (equal 3rd) complying with regulations on legal services provision (21%). Breaking down the results by sizes of solicitors' firms<sup>9</sup>, 20% of small firms; 24% of medium firms and 34% of large firms said that competition for business was a significant problem for them (in comparison to 14% of small firms; 19% of medium firms; and 35% of large firms in 2013-14). The increase in the percentage of firms considering that competition for business was a significant problem for them from the previous year's Survey suggests that competitive pressures on firms have been increasing. It should be noted that when asked to look at the longer term firms were most worried about competition (and government spending such as in legal aid).
- 2.7. While the absolute percentage for each category of problem was low (reflecting perhaps the diverse competitive pressures firms are under - each firm having a different view as to the relative significance of the challenges it faces) the high ranking of competition compared to other problems indicates that it is a material pressure.
- 2.8. The Society's Survey<sup>10</sup> asked those firms that identified competition for business as a significant problem, what the main source(s) of this competition were: 31% of firms identified local solicitor firms as the source; 35% regional and national solicitor firms; 22% networks of solicitors; 46% non-solicitor legal providers; 50% „volume“ legal services providers and 33% Alternative Business Structures (**ABS**). „Volume“ legal services providers were therefore a significantly higher source of competition and networks of solicitors a significantly lower source of competition. The question was not repeated in the 2014-15 survey, or the forthcoming 2015-16 survey.
- 2.9. To complement the recent studies that the Legal Services Board (**LSB**) and Legal Services Consumer Panel (**LSCP**) have commissioned, the CMA may wish to review YouGov's suite of legal services reports

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<sup>6</sup> LexisNexis, *The Age of the Client* (2015), p.12. Available here [http://businessoflaw.lexisnexis.co.uk/wp-content/uploads/sites/24/2015/04/LexisNexis\\_Bellwether2015\\_Age\\_of\\_the\\_Client.pdf](http://businessoflaw.lexisnexis.co.uk/wp-content/uploads/sites/24/2015/04/LexisNexis_Bellwether2015_Age_of_the_Client.pdf)

<sup>7</sup> *Ibid.*, p. 10.

<sup>8</sup> See <http://www.lawsociety.org.uk/support-services/research-trends/annual-firm-survey-2014-15-snapshots-from-the-results/>

<sup>9</sup> The sizes of solicitors firms are measured in terms of their number of partners. Small firms are defined as 1-4 partners, medium size firms as 5-25 partners, and large firms as 26+ partners. These sizebands do imply lower bands than the standard ONS/Eurostat bands, which is necessary in order to give sensible splits of solicitor firms by size. The approximate relationship between the solicitor firm sizebands (in terms of number of partners) and the ONS/Eurostat sizebands (in terms of total number of employees) is shown in the table below.

<sup>10</sup> See <http://www.lawsociety.org.uk/support-services/research-trends/firm-survey-2013-14/>

which indicate that competitive pressures are increasing as new entrants and business models become more significant.

- 2.10. The Legal Needs Survey that we are undertaking jointly with the LSB and the Legal Education Foundation (LEF) and which is planned to be published this spring is likely to prove relevant to many of the questions identified under this theme. The questionnaire is based on that used in LSB's 2012 Legal Needs Survey.

**What information do consumers use to judge the quality of legal services and/or legal services providers? What price information is made available to consumers? Do consumers find it easy or difficult to compare the quality and prices of legal services?**

- 2.11. Consumers have a wide choice of legal service provider. The 2014 report by RBS characterises the legal services market as *"currently a buyers" market, which means that clients are in a position to more readily dictate terms on price, service and ancillary support. The pressure on billing rates is set to continue, as is an increasing requirement for alternative fee arrangements, greater pricing transparency and more value.*<sup>11</sup> This is borne out by the findings of the LSCP tracker survey, that almost 70% of people who used legal services in the past two years felt they had a choice of provider, and 25% shopped around.<sup>12</sup>
- 2.12. The ways in which customers choose legal services providers vary depending on the complexity of their problem and the area of law involved. The YouGov *Legal Services 2015* report examined these methods in some detail.
- 2.13. As a general reflection of trends across consumer markets, the number of potential clients looking to internet search engines, consumer review websites and specialist online legal directories and using the Citizens Advice Bureau is undoubtedly increasing.
- 2.14. Research by LexisNexis found that consumers are more likely to search online to gather information to help them identify, validate and select a legal provider (individual or organisation) than to rely on a recommendation (see the table below).<sup>13</sup> This trend towards using online resources may lead to consumers shopping around even more for their legal services in the future.<sup>14</sup>

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<sup>11</sup> RBS, *A perspective on the legal market*, April 2014, p.24.

<sup>12</sup> [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Using\\_legal\\_services\\_000.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Using_legal_services_000.pdf)

<sup>13</sup> The Attorney Selection Research Study conducted by LexisNexis Martindale-Hubbell in February 2012 (Survey base: 4,000 consumers).

<sup>14</sup> YouGov *Legal Services 2015*, pp. 27-30. We subscribe to YouGov's legal channel reports and use of findings is restricted. Publications can be purchased from YouGov and we recommend this to the CMA if the CMA wishes to find further information on these findings.

**A Closer Look at Online Resources and Friends/Family Usage**

	Gather	Find	Validate	Select
<b>Online resources (net)</b>	65%	61%	53%	44%
Online search engines	39%*	35%	23%	20%
Online directories	31%	30%	21%	16%
Social media sites	26%	22%	16%	11%
Law firm websites	31%	35%	26%	21%
Legal blogs	29%	21%	17%	12%
Online legal advice forums	34%	22%	18%	13%
<b>Friends/Family advice/ recommendation (outside of social media sites)</b>	39%*	45%*	36%*	36%*

★ Indicates leader in category

Comparison of online resources and family/friends usage by those who sought an attorney in the past year, broken down by each stage of the search process.

2.15. The Society provides a Find A Solicitor (**FAS**) service online and on the phone – now linked to a „Lawyers For Your Business“ accreditation which has proved popular with consumers. The website receives 554,000 average visits each month (6.65 million visitors in the year) and the telephone service is also popular with 89.34% of callers either satisfied or very satisfied with the service they received.<sup>15</sup> This is proving a valuable resource for consumers with recent research commissioned by the Society finding that when consumers were asked about specific websites whose reviews would be trusted, the two top rated websites were the Law Society and the Solicitors Regulation Authority.<sup>16</sup> The Society’s accreditation system is a valuable resource to help support consumers’ decision-making process to identify, validate and select a law firm or solicitor with validated expertise. In the absence of a recommendation, accreditations serve as a quality mark to help short-circuit the decision making in the buying process. 14,952 individuals are accredited to one of our schemes (figures as at 18 January 2016). The Wills & Inheritance Quality (**WIQS**) accreditation is a good example. We market this to solicitors firms as a way to inform and gain client confidence, as follows: „*Demonstrate your firm’s excellence in delivering wills and inheritance advice through a best practice quality mark that prospective clients can trust*“ and „*Gaining WIQs accreditation can help you to win more business, increase client satisfaction and minimise the risk of claims*“.<sup>17</sup>

2.16. Alongside changing trends in the way in which consumers find a solicitor, there are discernible trends in how they make a choice. Recent research for the Society found that, among a number of criteria used to

<sup>15</sup> The Law Society, Find a Solicitor Google Analytics data, Jan - Dec 2015.

<sup>16</sup> Consumer use of ratings for solicitors/law firms, omnibus survey conducted by Bilendi for the Law Society, April 2015, Survey base: 2,009 UK adults aged 18 and above.

<sup>17</sup> *Promoting your Wills and Inheritance Quality Scheme Accreditation Practical guidance to help you market your accreditation* (TLS, 2014).

choose a solicitor, respondents rated as most important „understanding needs“ and „quality of client service“, while the least important were the location and size of the firm. „Keeping you informed“ and „explaining the process and options clearly“ were rated more highly than „value for money“ although the percentage differences were small.<sup>18</sup> YouGov’s research also reports on trends in the information consumers use to choose and judge legal services. While experience and reputation remain important criteria these have recently been overtaken by the cost of services. Costs are important both in terms of the absolute amount but also as the ability to be certain about likely costs. Consumers therefore show a strong and increasing preference for fixed fee and no-win-no-fee arrangements. Fixed fees have been prevalent in residential conveyancing and wills for many years.

- 2.17. Fixed-fee arrangements are more prevalent than hourly-billing in conveyancing, will-writing and immigration law.<sup>19</sup> YouGov, in its 2015 report, found that 58% of those using law firms and solicitors in the last three years paid for their legal advice on a fixed fee basis, with 49% charged the fee at the end of the legal matter that they were quoted initially. Only 12% of consumers were charged using an hourly rate model. No-win, no-fee arrangements accounted for a further 6%, and legal aid only 3%.<sup>20</sup> It is worth noting, that the scope of fixed fee agreements will be limited depending on the particular area of law and that, on some occasions, unbundled advice can cost more.
- 2.18. As well as offering more services on a fixed fee basis, solicitors are endeavouring to provide more transparency of fees to differentiate themselves from their competitors and help consumers make an informed decision. Many solicitors firms now give fixed fees on their websites and offer quotation services.<sup>21</sup> Research by the LSB into how costs are presented to wills and probate consumers found that 54% of consumer respondents were provided with an estimated cost before commissioning work and 26% of respondents were provided with a formal quote. Questioned about the end of the process, 62% said the final cost was about the same as they expected, 27% said it was either slightly or much more and 5% said it was slightly less or much less.<sup>22</sup>
- 2.19. While these trends to fixed fees and greater transparency makes price comparison easier, it is more difficult for consumers to compare the quality of the legal services they purchase. We agree with Richard Moorhead’s conclusion in a paper for the LSB that:

*„for the market to function effectively, signals about the relative quality of legal services have to be at least as meaningful as signals on price. If they are not, quality is likely to diminish significantly as a result of*

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<sup>18</sup> Consumer use of ratings for solicitors/law firms, omnibus survey conducted by Bilendi for the Law Society, April 2015. Survey base: 2,009 UK adults aged 18 and above.

<sup>19</sup> SRA Risk Outlook, page 10. Available at <https://www.sra.org.uk/risk/outlook/risk-outlook-2015-2016.page>

<sup>20</sup> YouGov *Legal Services 2015*, p.11.

<sup>21</sup> See for example: [http://www.tmsolicitors.co.uk/probate-solicitors-costs/?utm\\_term=%2Bprobate%20%2Bservices&utm\\_content=108363862408&utm\\_campaign=225232888&utm\\_source=google&utm\\_medium=cpc&mh\\_keyword=%2Bprobate%20%2Bservices&gclid=ClihxotPqcsCFRYW0wodMMch9w](http://www.tmsolicitors.co.uk/probate-solicitors-costs/?utm_term=%2Bprobate%20%2Bservices&utm_content=108363862408&utm_campaign=225232888&utm_source=google&utm_medium=cpc&mh_keyword=%2Bprobate%20%2Bservices&gclid=ClihxotPqcsCFRYW0wodMMch9w) and <http://www.probaters.com/our-services/?gclid=CPGAzpHPqcsCFQccGwodXikMiQ>.

<sup>22</sup> LSB, *The use of probate and estate administration services* (2012), pp. 45 & 48. Available at [http://www.legalservicesboard.org.uk/Projects/reviewing\\_the\\_scope\\_of\\_regulation/yougov\\_research.pdf](http://www.legalservicesboard.org.uk/Projects/reviewing_the_scope_of_regulation/yougov_research.pdf)

*competition. Ensuring that stronger signals of relative quality develop within legal services markets should be a central goal of service providers and regulators.*<sup>23</sup>

- 2.20. This is partly an inherent problem as many legal services are an “experience good” - a service where product characteristics are difficult to observe in advance, but where these characteristics can be ascertained upon consumption. In many instances legal services may be “post-experience goods” (or “credence” goods), with individual customers being uncertain as to the quality they have received even after purchasing the service.<sup>24</sup> An obvious example is will writing, where the purchaser will not necessarily ever know if the job was done well.<sup>25</sup> Any problems with conveyancing, legal contracts or advice may not emerge for many years after the initial advice or transaction.
- 2.21. In judging quality, consumers can face particular difficulties when seeking to differentiate between legal services provided by regulated as opposed to unregulated service providers. An important aspect of the quality of service offered is the level of consumer protection offered by the legal service provider which differs enormously between, on the one hand, solicitors (and other regulated providers) and unregulated providers (as explored in more detail in our response to the Theme 2 and Theme 3 questions below). Many consumers assume that unregulated providers offer the same level of protection as regulated providers, severely inhibiting their ability to make informed purchasing decisions.
- 2.22. Two research reports from 2013 looked into this issue. The LSB's Consumer Panel 2013 report on risk and the role of regulation was commissioned from Vanilla Research ('the Vanilla research') in response to the (then) government's concern that too much regulation was leading to a compensation culture.<sup>26</sup> The aim of the research was to gather information about consumer perceptions in order to inform a wider LSCP project which aimed to address the question of whether the financial protection arrangements in place in the legal services market were fit for purpose.
- 2.23. In summary, the Vanilla research found that:

*'Consumers have minimal knowledge of existing consumer protections. As might be expected, there is little actual knowledge about the various protections that are currently in place for legal services consumers. Nearly everyone assumes something is in place, but few can describe what this something is, other than some general references to "an Ombudsman". The assumption is a reasoned one in consumers' minds – being a solicitor is a "profession", with standards, and so they feel confident there is some kind of consumer protection in place'; and*

*'Although consumers generally took plenty of reassurance from the existing consumer protection schemes, a contradiction exists: the risks consumers are most worried about when dealing with legal*

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<sup>23</sup> *Understanding the economic rationale for legal services regulation – A collection of essays* (2011), LSB.

<sup>24</sup> See CMA Statement of Scope at 3.19.

<sup>25</sup> Of course, the purchaser may feel the service levels were high and the matters well explained, but they would be unlikely to know whether the will was drafted effectively.

<sup>26</sup> *Risk and the role of regulation* report for the Legal Services Consumer Panel by Vanilla Research, January 2013. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf)

*services are not thought to be covered by these current protections (for example inexorably rising costs), and two of the main risks that are covered (fraud and bankruptcy) are not something consumers consider'.*

- 2.24. In so far as unpredicted costs were a concern identified by Vanilla the market response has been a much greater use of fixed fees as described above.
- 2.25. The Vanilla research found that few consumers were happy at the thought of the existing levels of client financial protections being taken away: *'There is a view that legal services are different to other sectors (it's a profession, dealing with the law, and life-changing events), and that there should be sector-wide protections in place'.*
- 2.26. Consumers rejected the suggestion that they should take on risk themselves<sup>27</sup> and the research identified strong resistance among consumers to the idea of purchasing their own insurance as they had little confidence in their own abilities to make informed decisions about which policy was right for them. Additionally, there was a further complicating worry that consumers, if forced to purchase their own insurance for certain areas of legal advice, would not actually know what they were buying (in terms of risks they were insuring against, or the level of cover needed). In other areas, such as conveyancing, the decision making on such questions is led by the lenders who fund the transaction.
- 2.27. The LSCP's report *Financial protection arrangements* in June 2013 referred to previous studies which suggested that consumers of legal services generally lack the detailed knowledge needed to compare services accurately and access quality.<sup>28</sup> The LSCP report identified the risk that: *'...informed consumers will only use insured lawyers, while more vulnerable consumers will either not realise that mandatory protections are not in place or will choose lawyers without insurance solely on the basis of cost'.*
- 2.28. In light of this, the LSCP report recommended that the financial protections should remain mandatory and that consumers should not be asked to source their own insurance, mirroring the Vanilla research's findings on consumer's views.<sup>29</sup> The report states that:

*'Despite some challenges around access to data, at a high level, and on most occasions the financial protection regimes will deliver redress against each of the key risks that consumers face when buying legal services. They are designed to offer a comprehensive level of protection and assume that consumers should bear quite a low burden of risk – we consider this is entirely appropriate given the nature of legal services, consequences of the risks transpiring and the difficulty consumers face in preventing loss'.*

We have over the last two years provided extensive comment to the SRA on the existing solicitors' client financial protections in response to the SRA's desire to dilute these protections and our views are summarised in our responses to the Theme 2 questions below.

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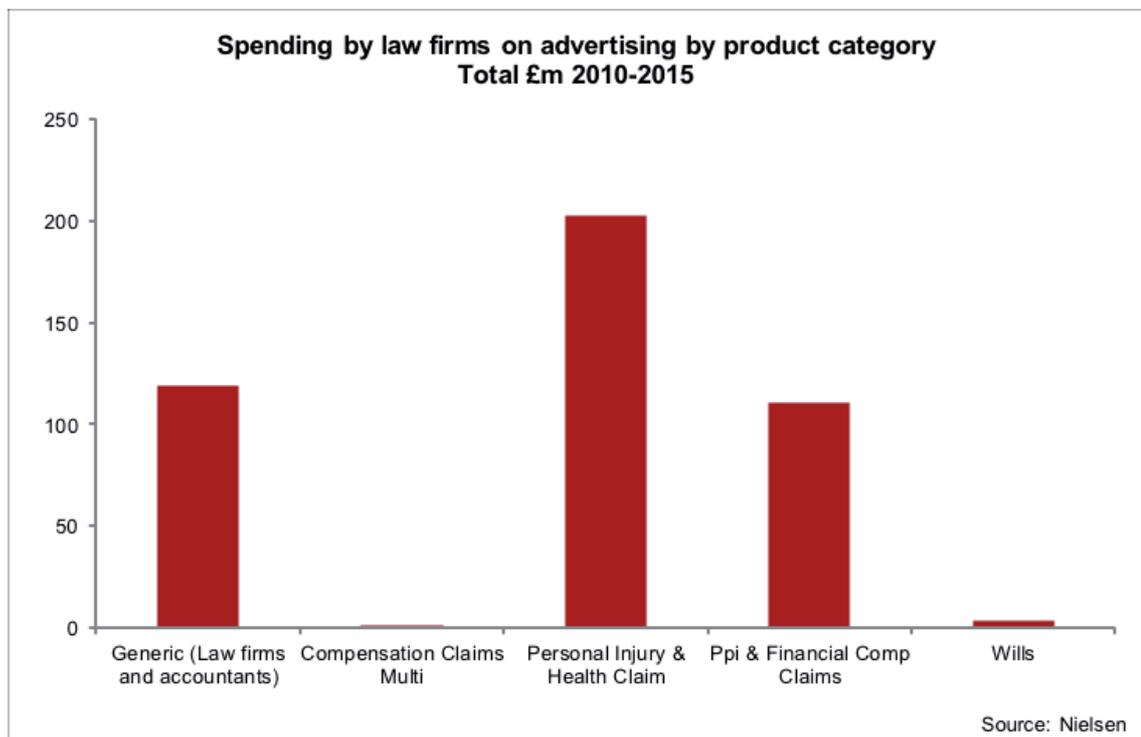
<sup>27</sup> A suggestions that is still found in the rationale for the SRA's recent proposals to change consumer protection levels by changing the minimum terms and conditions of solicitors' PII cover.

<sup>28</sup> <http://www.legalservicesconsumerpanel.org.uk/ourwork/Financial%20Protection/FPAs%202013%2006%2010%20final.pdf>

<sup>29</sup> <http://www.legalservicesconsumerpanel.org.uk/ourwork/Financial%20Protection/FPAs%202013%2006%2010%20final.pdf>

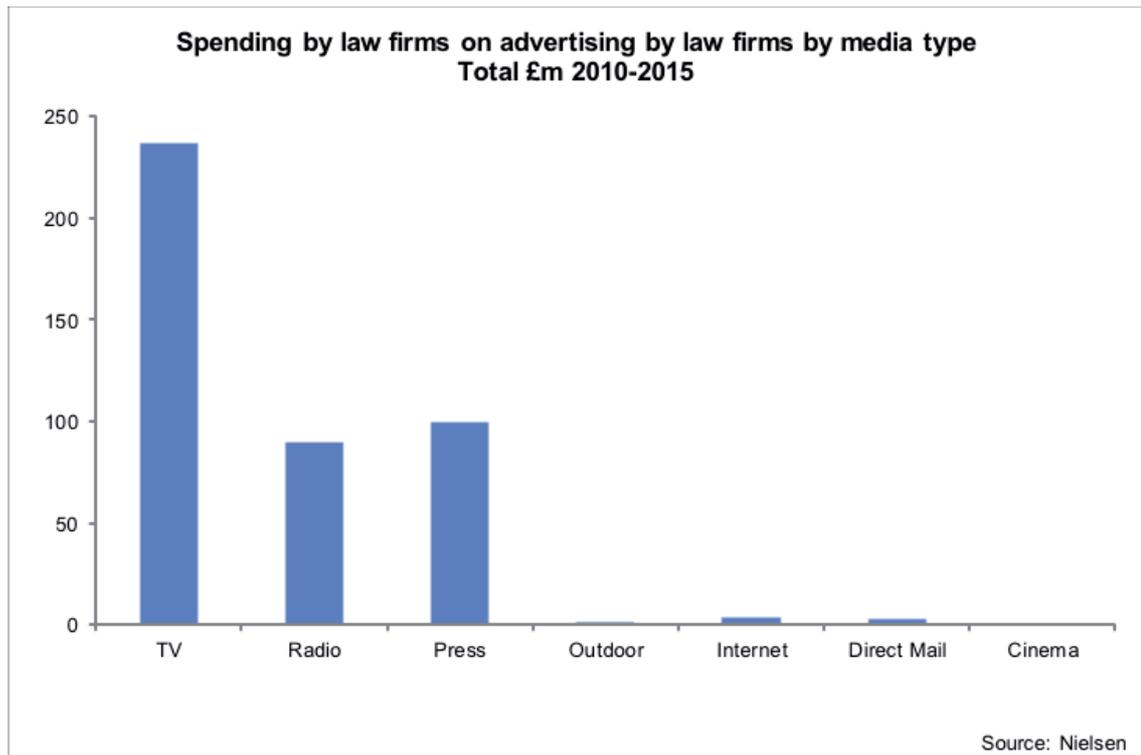
**How do providers of legal services compete with each other in seeking to win new business? Do they face any difficulties in winning new business?**

- 2.29. Solicitors (and other legal services providers) are responding to competitive pressures in a variety of ways in their attempts to win new business. This is most explicit in direct advertising campaigns. Two national law firms (Slater & Gordon and Irwin Mitchell) have embarked on major TV advertising campaigns in the last 18 months (and other firms have previously engaged in such campaigns), while claims management companies have been ubiquitous across all media channels.<sup>30</sup>
- 2.30. Research by Nielsen over the five years from 2010-2015 shows that the amount spent on advertising and the media channel used depends on the area of legal service.<sup>31</sup> The main areas of legal service advertised by law firms are personal injury and health claims followed by PPI and financial claims and then generic advertising. The main media used are TV, radio and press – again with some variation depending on the area of legal service, with will writing advertised mainly in the press. The graphs below shows the total amount spent by law firms on advertising by legal service and media channel:



<sup>30</sup> A survey of marketing professionals in the legal sector was carried out in association with The Lawyer by eConsultancy in 2015, providing information on digital marketing media and plans. We will provide this to the CMA separately.

<sup>31</sup> AC Nielsen.



2.31. Smaller firms lack the resources, expertise or money for high profile campaigns though they do benefit from Society campaigns advising consumers on the benefits of using a solicitor. In any event it would be wrong to consider direct advertising as the most significant method used by law firms to acquire customers. In common with other professional service providers, particularly those with a principally local client base, solicitors go about customer acquisition through networking, providing training opportunities and client publications and other ways of raising their profile among potential clients. For small firms in particular, word of mouth is key to their winning business and they explore ways to become better known in their local area or for their area(s) of expertise. This would involve activities such as client seminars on developing areas of law, placing articles in local newspapers, commenting on issues on local radio, attendance at networking events such as chamber of commerce and trade union events, corporate social responsibility work and the like. Participating in or sponsoring local and national business and legal awards can also be used to raise a firm's profile as shown in a recent example where a firm noted its award win from the Law Society's Excellence Awards 2016 on its website.<sup>32</sup> Some, but not all, of these activities would be captured in solicitors firms' marketing spend but much of it is unlikely to be formally recorded as a „cost“ to the firm or necessarily identified as a marketing activity. Nevertheless the principle reason for engaging in such activities is to build and retain the client base.

2.32. The Law Society's Law Management Section's recent financial benchmarking survey found that the median spend on direct marketing (including staff costs) has remained stable at 2% of practice fee income in both 2015 and 2014 but for reasons explained above this is likely to understate customer acquisition

<sup>32</sup> See <http://www.lawsociety.org.uk/support-services/events-training/excellence-awards/> and <http://www.debenhamsottaway.co.uk/news/2016/02/a-great-start-to-2016-for-debenhams-ottaway>

activity.<sup>33</sup> Research by LexisNexis examined firms' marketing spend globally and found that: for smaller practices (1-20 lawyers), an overall marketing budget of less than \$155,000 was most prevalent; for medium sized practices (20-50 lawyers), the size of the marketing budget crept up more towards the \$775,000 mark while; for practices of 50-100 lawyers, marketing expenditure levels up to \$1.5 million were commonplace.<sup>34</sup> Solicitors increasingly recognise the importance of their marketing spend, with the LexisNexis *The Age of the Client* report finding that 57% of respondents have „planned or implemented increased spend on marketing“.<sup>35</sup>

- 2.33. Solicitors are also looking online for ways to engage with clients and potential clients. Recent research conducted by the Society found that email, website and social media are the top three channels that law firms are using to engage with customers. Content marketing (i.e. of a firms' expertise or legal issues), email marketing and data management/eCRM were cited as of being particularly important resources for solicitors. The report says: *“Asked specifically about client acquisition through digital marketing, content marketing predominates (67%). Content has always been important for client retention but is here shown as vital for acquisition. Content in turn impacts SEO [online search engines], also highlighted as an important activity for customer acquisition (59%)”*<sup>36</sup>.
- 2.34. Exploring firms' websites can give some insight into the types of customer acquisition activities undertaken by solicitors and examining the advice given to solicitors firms by marketing advisors and by the Society itself is also instructive. Marketing companies offer services to help solicitors to raise their profile, such as producing key facts and figures cards in their specialist areas.<sup>37</sup>
- 2.35. We have sought to help solicitors to explore these options, within the last few years producing such publications as „Marketing Legal Services“ (2011), „Law Firm Marketing Toolkit“ (2013), „Social Media in the Legal Sector Special Report (2013)“ and „Niche Marketing for the Legal Sector Special Report“ (2015). We also provide training for its members, with recent examples including „Survive and thrive - growing your law firm in a competitive market“ (2015), „Social media for lawyers“ (2015) and „Grow your small firm with LinkedIn“ (due to take place in March 2016). We seek to share our members' knowledge and experience on competitive strategies and activities through our website and community pages.<sup>38</sup> Our most recent project is Lawyers for Your Business (LFYB) – a scheme aimed at smaller firms and sole practitioners who would like help in generating new business enquiries from start-up, small and medium, size businesses which is due to launch soon. Business consumers can filter results to only display LFYB

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<sup>33</sup> Law Management Section, *Financial Benchmarking Survey*, p. 41.

<sup>34</sup> The Use of Websites in Law Firm Marketing, conducted by Purple Market Research for LexisNexis Martindale-Hubbell, July 2012. While this was a global study, its findings are still relevant to the UK as, within a survey base of 184 law firms, 60 were from firms in England and Wales)

<sup>35</sup>

[http://businessoflaw.lexisnexis.co.uk/wpcontent/uploads/sites/24/2015/04/LexisNexis\\_Bellwether2015\\_Age\\_of\\_the\\_Client.pdf](http://businessoflaw.lexisnexis.co.uk/wpcontent/uploads/sites/24/2015/04/LexisNexis_Bellwether2015_Age_of_the_Client.pdf)

<sup>36</sup> Consumer use of ratings for solicitors/law firms, omnibus survey conducted by Bilendi for the Law Society, April 2015. Survey base: 2,009 UK adults aged 18 and above

<sup>37</sup> See for example <http://www.bernersmarketing.co.uk/news/2016-employment-law-facts-figures-cards-now-available.html>

<sup>38</sup> See for instance <http://communities.lawsociety.org.uk/small-firms/features-and-interviews/practical-support-features/marketing-the-small-law-firm-five-things-i-learned-using-google-adwords/-pay-per-click-advertising-ppc/5052666.article>; <http://communities.lawsociety.org.uk/small-firms/features-and-interviews/interviews/marcus-hayes-my-niche-practice-firm/5053399.article>; and <http://communities.lawsociety.org.uk/small-firms/features-and-interviews/practical-support-features/small-firm-entrepreneurs/5051105.article>.

members or to find their nearest LFYB member by searching against specific areas of practice. Improved marketing will include paid search campaigns and extending work with third party referrers, for example Barclays Bank, who have already introduced LFYB as part of their business start-up package.<sup>39</sup>

**Do intermediaries (such as estate agents, insurers and accountants) play a role in helping consumers to choose legal services providers?**

- 2.36. Research has shown that many consumers return to a legal services provider they have used before (21% of those survey by the LSCP found their lawyer this way) but personal recommendation (14%) and referral by a company (13%) are also common routes.<sup>40</sup> The LSCP tracker also shows that that 70% of consumers felt that they had had a great deal or fair amount of choice overall. Those whose service was provided by insurers rated satisfaction with choice far lower at 42% (52% for those using trade unions).<sup>41</sup> The YouGov 2015 report has insights on referrals.<sup>42</sup>
- 2.37. In many cases, referrals from intermediaries will be based on their experience of dealing with that legal services provider. However, in some cases intermediaries require a fee to be paid by a lawyer to be introduced and referred work (a referral fee). For instance, it is frequently the case that an estate agent or a financial advisor will require to be paid a fee by the solicitor to recommend the legal service to clients. When the fee is paid varies with the transaction type: some fees may be paid for leads while others might only be paid where a transaction is completed. The payment of referral fees within the legal market has caused controversy and in the personal injury market such payments are now banned. In other areas of law referral fees are still permitted though there are conduct rules for solicitors regarding payment of such fee. Solicitors are required to ensure any such arrangement is in the best interest of their client; that the referrer has not used marketing tactics that would be banned under the SRA Code of Conduct; and that clients are made aware of any fee paid.<sup>43</sup>
- 2.38. In conveyancing, some solicitors firms make payments to estate agents for referrals within segments of the market. A market appraisal undertaken by the Society in 2013 indicated that fees ranged between £100 and £200, while an earlier investigation into referral fees by the LSB indicated that fees could be as high as £250 - £400.<sup>44</sup> The LSB investigation suggested that referral fees did not damage the quality of service provided by lawyers or the cost paid by consumers in either the personal injury or conveyancing market.
- 2.39. In the case of will writing, some banks and building societies offer these services to their clients or refer them to other providers. In these circumstances, we have concerns that consumers are not making an

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<sup>39</sup> See <http://www.lawsociety.org.uk/support-services/lfyb/>

<sup>40</sup> Legal Services Consumer Panel (2015), *Tracker Survey 2015* - data tables for recent users.

<sup>41</sup> Legal Services Consumer Panel (2015), *Tracker Survey 2015* - data tables for recent users. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Tracker\\_Users\\_15\\_000.xlsx](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Tracker_Users_15_000.xlsx) Q60

<sup>42</sup> YouGov *Legal Services 2015*, p.27.

<sup>43</sup> SRA Code of Conduct (version 15) <http://www.sra.org.uk/solicitors/handbook/code/part3/rule9/content.page>

<sup>44</sup> Legal Services Board (2010) *Cost benefit analysis of policy options related to referral fees in legal services* <https://research.legalservicesboard.org.uk/wp-content/media/2010-Investigation-into-referral-fees-report.pdf>

informed choice of will writer and may not be advised of the difference between a regulated and unregulated will writer.

**3. Theme 2: Whether information failures expose consumers to harm that is not being adequately addressed through existing regulation or redress mechanisms**

**Are current regulations effective in protecting consumers' interests?**

- 3.1. For the reserved activities ex-ante protection ensures that providers are properly trained and are subject to appropriate regulatory supervision and redress systems. In the case of solicitors these protections extend beyond the reserved activities to all of the authorised person's activities as a solicitor. Chapter 1 of the SRA Handbook<sup>45</sup> requires solicitors to achieve a number of client care outcomes including informing clients at the outset of the likely scope of the work and costs and of redress mechanisms. The YouGov 2015 report found in its December 2014 survey, that an overwhelming majority of clients felt that the information provided by their legal representative was clear and easy to understand (85% found information presented in consultations with their solicitors easy to understand and 80% found information in legal documents clear and easy to understand).<sup>46</sup> No such information obligations exist for the unregulated sector.
- 3.2. Such protections are necessary because legal services are experience or credence services and consumers will in many cases not be in a position to judge what may be involved in a legal service, the complexity of the service and the likely costs. They are therefore reliant on what the service provider tells them and on the fact that the service provider is properly trained and supervised. Absent these protections the consumer is at risk.
- 3.3. The asymmetry of information between provider and consumer does not just relate to the nature, extent and cost of the legal service but also to the levels of protection available to the consumer. Consumers may assume that all providers of legal services are regulated and that a similar level of protection exists in relation to all providers. An unregulated provider has no obligation to tell a consumer that it is not regulated.
- 3.4. The Legal Ombudsman has reported cases where consumers complain about a legal service they have received but because the provider is unregulated no redress is available:

*“These cases reveal a mismatch between consumer expectations of what constitutes a „legal service“ - which consumers clearly assume implies access to a proper system of regulation and redress - and the reality of the diverse market providing such services. This confusion is not helped by the habit many*

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<sup>45</sup> SRA Handbook, *Code of Conduct*, Chapter 1. Available at <https://www.sra.org.uk/solicitors/handbook/code/part2/content.page>. See in particular Outcomes 1.9, 1.10, 1.13, 1.14 & 1.16.

<sup>46</sup> YouGov *Legal Services 2015*, p.34.

*unregulated companies have of presenting themselves as though they were traditional law firms, with websites and advertising material branded with the panoply of wigs, gowns and quill pens.*<sup>47</sup>

- 3.5. There is a significant difference between consumer satisfaction levels when using a solicitor and using an unregulated provider. The YouGov 2015 report found that customer satisfaction was materially lower for those using other providers than those using law firms and solicitors.<sup>48</sup>
- 3.6. The existence of appropriate insurance cover is an important consumer protection. Claims against a legal service provider might not arise for many years (for example, when a will is executed or a property is sold). For this reason, solicitors' compulsory professional indemnity insurance (**PII**) is provided on a 'claims made' basis whereby the insurer currently providing cover assumes the risk for any claim that is made during the current insurance period. In contrast, unregulated providers simply do not have the same level of client protection arrangements in place (and in many cases no protection at all).
- 3.7. As set out in full in our first submission to the CMA, the compulsory PII Minimum Terms and Conditions provide redress to clients and protection for managers and partners and also solicitors and staff in the firm for negligent mistakes:
  - (a) The firm's PII policy will meet each and every claim up to £2m under the minimum terms and conditions (£3m for LLPs). There are very limited occasions when the PII will not be valid. Clients are protected even if there has been misrepresentation on the proposal and if there has been dishonesty (unless all partners are tainted with the fraud –see Compensation Fund);
  - (b) it is important to note that solicitors are not permitted to limit their liability to clients to less than the minimum sum insured;
  - (c) Top up cover is available and often purchased by firms which consider that their work involves higher risk, on negotiated terms;
  - (d) Where the insurance cover is insufficient, the firms' partners (and, possibly former partners) are liable for any losses;
  - (e) Run-off cover must be purchased on disclosure and is guaranteed by qualifying insurers for six years after the firm ceases to practise; and
  - (f) Claims which arise more than six years after closure are at present handled with by the Solicitors Indemnity Fund,(which has been in run off since 2000) but this arrangement will only last until 2020 unless the SRA decide it is willing to continue this consumer protection). Current SRA proposals are for the Fund to cease operations after 2020 and offer no cover beyond that year leaving firms that now close without automatic protection six years after their closure. SRA has also proposed

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<sup>47</sup> Legal Ombudsman, *Annual Report and Accounts* (2011), pp. 21-22. Available here <http://www.legalombudsman.org.uk/downloads/documents/publications/Annual-Report-2010-11.pdf>

<sup>48</sup> YouGov *Legal Services* 2015, pp. 12 & 37.

reducing the level of compulsory run off cover from six years to three, which we consider will create a significant gap in client protection.<sup>49</sup>

- 3.8. Solicitors are also required to contribute to a Compensation Fund which, in broad terms, is used to compensate clients for certain losses caused by uninsured solicitors or where funds have been misappropriated.<sup>50</sup>
- 3.9. These complementary client protections re-enforce the solicitors' profession covenant of trust with the public - the importance of which was highlighted by the *Wolstenholmes* case sentencing judge when he referred to the profession as: *'...a business in which members of the public are entitled to place absolute trust'*.<sup>51</sup> Client protections benefit solicitors and their staff as well as the public, as recognised by the House of Lords judgment in *Swain v The Law Society*.<sup>52</sup> The 2012 SRA annual report also recognised the advantages to consumers and to the economy of these high client protections:

*'Consumers of legal services in England and Wales are better protected than in comparable jurisdictions abroad. This certainly enhances the reputation and offering of solicitors, who will generally see it as a price worth paying'*.<sup>53</sup>

- 3.10. The LSB carried out qualitative research in 2015 which largely corroborates the SRA's 2012 statement.<sup>54</sup> The LSB's recognised that the current protections come at a high cost to the profession. It states that PII was perceived to be one of the highest cost areas of regulation: *'While 19% of entities nominated PII as their priority to keep, 8% identified it as their priority to remove.'* As the RBS report of April 2014 says: *'PII is a major law firm expense-irrespective of the size of the practice'*.<sup>55</sup>
- 3.11. Nevertheless, the report demonstrated that PII is valued by the profession, finding that: *"Of those that wanted to keep PII, 53% - or 10% of all respondents - felt it should be kept because that specific regulation helps them get work and reduces the costs they would otherwise face."* Indeed, *"the highest*

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<sup>49</sup> The Solicitors Indemnity Fund (SIF) was created in the late 1980s to act as the profession's own insurer, providing also run-off cover for perpetuity for solicitors and firms which ceased to trade, without any requirement on them to continue to pay contributions. In 2000, the profession voted to close the SIF and to move to the open market for its members' indemnity needs. The contributions collected, and investment income, were used by the SIF to fund the handling, defence and settlement of claims which still fell to be dealt with it. The two main categories were (A) claims made or intimated prior to 1 September 2000 and (B) 'run-off claims', made on or after 1 September 2000 in respect of principals who had retired before that date. In 2004 the Society decided to use part of the remaining SIF surplus to purchase additional run-off cover for solicitors who remained in practice after 1 September 2000. This reflected a concern at the time of the abolition of the SIF, which led to the Society at that time deciding that the profession would collectively make arrangements to fund run-off cover to the extent that that was not provided through the minimum terms and conditions. This led to the use of part of the SIF surplus to purchase post six-year run-off cover, commencing on 1 September 2007 and running to 30 September 2017. As a consequence of the 2007 act, the SRA is responsible for decisions relating to indemnity as a regulatory function and is therefore responsible for deciding whether the current SIF should be extended. One such extension was made to 2020. A further decision by the SRA - whether, subject to adequacy of remaining surpluses, to extend beyond 2020, is awaited.

<sup>50</sup> SRA Compensation Fund Rules 2011

<sup>51</sup> See <https://www.gov.uk/government/news/13m-shortfall-2500-dissatisfied-clients-former-members-of-legal-firm-wolstenholmes-get-combined-70-years-director-disqualifications>

<sup>52</sup> *Swain v The Law Society* [1983] 1 AC 598 (5:36).

<sup>53</sup> SRA, Annual Report (2012), Chairman's Foreword. Available at <http://www.sra.org.uk/sra/how-we-work/reports/moving-forward.page>

<sup>54</sup> LSB, *The regulated communities' views on the cost of regulation* (2015), p.6. Available at <https://research.legalservicesboard.org.uk/wp-content/media/Cost-of-Regulation-Survey-Report.pdf>

<sup>55</sup> RBS, *A perspective on the legal market*, April 2014, p. 15.

ranked area of regulation to keep was PII", with 18% of entities and 19% of individuals choosing this area. The comments suggested that it was an area to keep because of the protection it provides to those in business. As one entity respondent stated: "I'm human, therefore I'm fallible. It makes good economic sense and is good risk management to have an insurance policy in case something goes wrong..."<sup>56</sup>

**Are consumers aware of the existing redress mechanisms? Are they being pointed to redress mechanisms by providers when appropriate?**

- 3.12. Solicitors are obliged to make their clients aware of their complaints process and access to the Legal Ombudsman's service both at the start of a matter and at the end of any complaints handling procedure. Many solicitors choose to do so in their initial engagement letter. The LSCP consumer tracker data found that 44% of consumers said they would know how to go about making a complaint, with the majority (56%) saying they would go to the firm itself and the Legal Ombudsman the next most common response (19%).<sup>57</sup>
- 3.13. Despite the importance of appropriate redress mechanism for consumer protection, the regulation of client protection is applied inconsistently across the legal services market: the level of protection offered by solicitors is not available from other providers and certainly not from unregulated providers. The LSB has established that, in the case of will writing, many consumers are not adequately protected at the time a will is written or an estate is administered.<sup>58</sup> As explained further above at paragraph 3.4 and in our first submission to the CMA, consumers are not aware of this difference when they purchase legal services and do not therefore know that, in choosing an unregulated provider of legal services, they are exposing themselves to risk.
- 3.14. Statements by the Legal Ombudsman included in our first submission to the CMA describe this discrepancy: "*These cases reveal a mismatch between consumer expectations of what constitutes a 'legal service' - which consumers clearly assume implies access to a proper system of regulation and redress - and the reality of the diverse market providing such services. This confusion is not helped by the habit many unregulated companies have of presenting themselves as though they were traditional law firms, with websites and advertising material branded with the panoply of wigs, gowns and quill pens.*"<sup>59</sup> This can result in consumers raising complaints with the Legal Ombudsman only to be turned away as their legal service provider is unregulated.<sup>60</sup>
- 3.15. We consider that this is a fundamental issue, particularly as it is something of which customers are often unaware. In this context, the key considerations are: (i) whether redress mechanisms exist in relation to

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<sup>56</sup> LSB, *The regulated communities' views on the cost of regulation* (2015), p.53. Available at

<https://research.legalservicesboard.org.uk/wp-content/media/Cost-of-Regulation-Survey-Report.pdf>

<sup>57</sup> Legal Services Consumer Panel (2015), Tracker Survey 2015 - data tables for recent users. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Tracker\\_Users\\_15\\_000.xlsx](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Tracker_Users_15_000.xlsx)

<sup>58</sup> See

[http://www.legalservicesboard.org.uk/what\\_we\\_do/consultations/open/pdf/will\\_writing\\_consultation\\_document\\_27\\_sep\\_12.pdf](http://www.legalservicesboard.org.uk/what_we_do/consultations/open/pdf/will_writing_consultation_document_27_sep_12.pdf)

<sup>59</sup> Written evidence from the Legal Ombudsman to the Justice Committee, September 2011. Available at

<http://www.publications.parliament.uk/pa/cm201213/cmselect/cmjust/97/97we04.htm>

<sup>60</sup> See the case study on this scenario provided in the Legal Ombudsman 2010-2011 Annual Report available at <http://www.legalombudsman.org.uk/downloads/documents/publications/Annual-Report-2010-11.pdf>

the provision of that legal service; (ii) whether customers are able to find out what these mechanisms are; and (iii) whether the mechanisms are effective in addressing customers' complaints. Questions addressing these points were posed in the 2016 TLS/LSB /LEF Legal Needs Survey, the results of which

### **Are redress mechanisms effective in addressing consumers' complaints?**

- 3.16. There are detailed requirements set out in the SRA Code of Conduct on the systems solicitors should have in place to handle any client complaint. Complainants can use the Legal Ombudsman service; an alternative to negligence claims where the amount of the claim is below £50,000. Services complaints which include an element of negligence can be made to the Ombudsman and will be considered; there is no costs risk for the complainant. The Ombudsman has considerable powers to resolve service complaints including ordering compensation, reducing the bill and making a firm apologise. Its approach is non-technical so there is no requirement for a complainant to be represented. If the complainant is unhappy with the outcome they can reject the Ombudsman's decision and take the matter to Court, although the trend for now seems to be to direct individual and micro-enterprise claimants towards alternative dispute resolution as opposed to going to the courts.
- 3.17. A stakeholder survey commissioned by the Legal Ombudsman in 2013 stated that: *"The majority of stakeholders believe that the Legal Ombudsman is improving access to redress, demonstrating fairness, contributing to improvements and building consumer confidence."*<sup>61</sup>
- 3.18. Complaints about misconduct cannot be dealt with by the Ombudsman but will be referred to the regulator. While there is no specific consumer redress through this route disciplinary actions taken by the SRA are published and in serious cases solicitors may be referred to the Solicitors Disciplinary Tribunal.
- 3.19. Consumer confidence in complaining about a lawyer is similar to other service providers such as accountants and mobile phone companies and only slightly lower than banks<sup>62</sup>. Awareness of the Ombudsman Service amongst consumers in the LSCP survey was 59% (higher for recent users of legal services at 64%). This is lower than awareness of the Financial Ombudsman Service (FOS) (77%<sup>63</sup>). When the Legal Ombudsman asked clients about where they had heard about the Ombudsman, 23% stated that it was through their lawyer. A slightly higher percentage of complainants referring a complaint to the FOS had heard about them through a financial business (30%). This indicates that this is an area where lawyers could do better and we are working with solicitors to improve signposting through our updated practice notes and risk and compliance service.
- 3.20. The fact that consumers of unregulated legal services do not have redress to the Legal Ombudsman (or the other redress mechanisms provided by solicitors set out above) renders it difficult to compare the

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<sup>61</sup> *Legal Ombudsman Stakeholder Survey* (March 2013), p. 2. Available at

<http://www.legalombudsman.org.uk/downloads/documents/publications/Legal-Ombudsman-Stakeholder-Survey-2013.pdf>

<sup>62</sup> Legal Services Consumer Panel (2014) *Tracker Briefing 2: Confidence and satisfaction*, p. 7. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/)

<sup>63</sup> Financial Ombudsman Services (2014) *Annual Review 2013/14* <http://www.financial-ombudsman.org.uk/publications/ar14/complained.html#a3>. The figure includes those who could name the Financial Ombudsman as well as those who may have heard of the service and definitely have heard of the service.

relative effectiveness of complaints handling between the regulated and unregulated sectors. The LSB has acknowledged this difficulty, and gives it as a reason for its forthcoming research project into unregulated providers.<sup>64</sup>

#### **4. Theme 3: Impact of regulations and the regulatory framework on competition**

- 4.1. A level of regulation is necessary for a well-functioning legal system. As we explained in our initial submission, regulation is required to protect the immediate consumers of legal services (that is those who purchase the service); to protect a wider group of consumers (who rely on the effectiveness of the legal system to underpin transactions, security of title and other rights and interests); and the wider public interest (for example in ensuring an efficient and fair system of dispute resolution). In seeking to balance the burden and cost imposed by regulation against the benefits it is important the CMA takes account of these wider externalities.
- 4.2. In order to provide a reserved activity a provider must be authorised by an approved regulator. For solicitors, non-reserved legal activities are also subject to regulation thus solicitors cannot offer those services without undergoing suitable education and training, complying with the SRA Handbook outcomes, contributing to the compensation fund, having PII cover in place and offering access to the Ombudsman. This means that there is a significant part of the market (all non-reserved activities) in which non-regulated providers compete with highly regulated providers. The latter will carry the costs of regulation and offer appropriate consumer protection (and contribute to wider externalities) the former will not. There is an element of free-riding by the unregulated sector in that, as explained above, many consumers believe that non-regulated providers are in fact regulated. Thus, non-regulated providers get some of the brand and reputational benefits from the regulatory system without paying for it and consumers are (unknown to them) unprotected.
- 4.3. The current regulatory regime therefore distorts competition, by imposing regulatory obligations selectively on certain legal service providers but not others, and giving misleading messages to consumers and the market.
- 4.4. This was explained in the 2009 Hunt Review of the Regulation of Legal Services:

*“This leads directly to the question of the extent of the regulatory “net”. I have been struck by the unanimity of view, across the profession and bodies representing consumers, in favour of giving serious consideration to extending legal regulation to other areas of activity where consumers currently enjoy no regulatory protection. I perceive a serious breach of both the public and the consumer interest in any area of activity that looks or “smells” like a reserved activity but is allowed to go unregulated. Most of our fellow*

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<sup>64</sup> See [http://www.legalservicesboard.org.uk/Projects/Unregulated\\_Legal\\_Services\\_Providers/index.htm](http://www.legalservicesboard.org.uk/Projects/Unregulated_Legal_Services_Providers/index.htm)

*citizens would surely be taken aback to learn that anyone can currently set himself or herself up as a will-writer and also that some aspects of probate activity can take place outside the regulatory "net".*<sup>65</sup>

- 4.5. The reserved activities relate to matters which require *ex-ante* regulation in the consumer and public interest. They are areas in which consumers find it hard to judge quality in advance of purchase (or sometimes after purchase) and in which there is a considerable public interest in ensuring that the relevant activity is conducted by a trained adviser who is subject to regulatory supervision and an effective compensation and complaints regime. We therefore believe that such activities should only be offered by properly authorised providers and see no basis for reducing the number of reserved activities.
- 4.6. Will writing is a "credence good", namely one whose quality cannot be ascertained by the consumer until some time after purchase, or indeed ever as the efficacy of the will may not be known until after the consumer's death. It is therefore essential for the protection of the client and the wider public interest in securing the proper administration of estates that will writers should be subject to appropriate training, insurance and redress obligations.
- 4.7. We believe that the broad scope of regulation of solicitors, as set out in the SRA Handbook, is correct in that it encompasses client and business conduct; accounting and client money requirements; authorisation and practice obligations (including education and training); client protection (including insurance and compensation and redress) and disciplinary matters. Although we would not necessarily agree with all the detail of current regulation in each of these areas or with the current regulatory structure (see below).
- 4.8. Because consumers are confused by a system that includes regulated and unregulated providers we believe that unregulated providers who offer legal advice outside of reserved activities should be subject to a minimum level of regulatory obligation to include at least access to the Ombudsman and indemnity insurance.
- 4.9. The SRA has recently changed the „separate business rule“ (**SBR**) which prohibited solicitors from owning or managing an unregulated legal services business, that is a solicitor could not separate reserved activities from non-reserved activities and operate the latter as if it were an unregulated provider. This distorted competition between solicitors firms and some ABS (such as accountancy firms) which were granted an exemption from the SBR by the SRA. The SBR now enables solicitors to own and manage a separate business though solicitors still cannot act as a solicitor in such a business<sup>66</sup>. The SRA has indicated that it will this year consult on further changes to allow solicitors to offer non-reserved activities in a separate business.<sup>67</sup>

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<sup>65</sup> *The Hunt Review of the Regulation of Legal Services* (2009), p.80. Available at [https://www.lsc.qld.gov.au/data/assets/pdf\\_file/0016/260035/The-Hunt-Review-of-the-Regulation-of-Legal-Services-NZ-Dec-2009.pdf](https://www.lsc.qld.gov.au/data/assets/pdf_file/0016/260035/The-Hunt-Review-of-the-Regulation-of-Legal-Services-NZ-Dec-2009.pdf)

<sup>66</sup> <http://www.sra.org.uk/solicitors/handbook/code/part5/rule12/content.page>

<sup>67</sup> <http://www.sra.org.uk/sra/policy/future/position-paper.page>

- 4.10. The SRA proposes to give non-regulated legal service providers who wish to offer some reserved activities the option to „opt-in“ to the regulatory regime. We consider this to be contrary to the public interest and liable to cause even more confusion to consumers. If certain activities require regulatory protection in the public interest it should not be left to the discretion of providers whether they offer that protection. Further, protection should be offered whether or not the provider also offers a reserved activity.
- 4.11. The role of the regulator is to regulate in the consumer and public interest. For reserved activities this may require the full gamut of *ex-ante* (authorisation and conduct standards), during the event (client money, insurance and compensation) and after the event (redress) regulation. For non-reserved activities the focus for all providers should be on after the event and (for some activities) during the event regulation. We see no basis for the regulator subjecting solicitors to a different burden to other providers in this regard.
- 4.12. We consider it important that solicitors abide by professional principles that can give an assurance of quality that come from holding the title of „solicitor“. It is for the professional bodies (The Law Society for solicitors, the Bar Council for barristers and other relevant bodies for other professionals) to set professional standards which may be the same as, or higher than, the minimum regulatory standards and would extend beyond reserved activities. This will also ensure that internationally the legal profession is seen to be independent.
- 4.13. Because of the scope for consumer confusion we consider that the title „lawyer“ should be protected in the same way as „solicitor“ and „barrister“ and reserved to professionals who have been authorised by a relevant professional body.
- 4.14. We consider that the multiplicity of regulators risks consumer confusion and there is no evidence that, as originally intended, having a number of frontline regulators has driven down costs. We believe that regulators of legal services should set the minimum regulatory rules and be responsible for independent regulatory enforcement against those minimum rules.
- 4.15. The hybrid approach that we describe, with the regulators setting the minimum standards required in consumer and public interest and the professional bodies dealing with professional principles associated with professional title, addresses the concern set out in our initial submission about independence of the profession from the state while ensuring that the consumer interest is protected by independent regulators. This would ensure that professional standards of entry are maintained and the international reputation of English and Welsh law and England and Wales as the jurisdiction of choice is protected.

**Do the current regulations create disproportionate barriers to entry and expansion into the legal services sector? What difficulties have new entrants faced?**

- 4.16. Most of the current regulations are necessary for the proper protection of consumers and wider interests. We are not aware of evidence to show linkage between lessening the cost of client protections and stimulating new entrants to the legal services market. Nor does the evidence suggest that reducing cost would lead to a greater number of consumers turning to a legal professional to resolve their legal problems.

- 4.17. Firms have to apply to be regulated via the SRA which assesses the suitability of the firm, for instance, whether they have systems in place to comply with SRA requirements and relevant experience. The SRA will also give some consideration to the viability of the business. This is not a matter all regulators would consider but is important because: (i) of the effect a sudden closure can have on clients; and (ii) over reliance on one client can make it difficult for a solicitor to maintain their independence.
- 4.18. Once regulated the firm will pay an annual fee based on number of lawyers and turnover.
- 4.19. There are barriers to exit for SRA regulated firms. Firms who have no successor have to purchase PII run off cover for the 6 years after they cease trading. This is to ensure that clients who wish to make a claim after a firms ceases will still be able to do so. They also need to make arrangements to repay all client monies and close their client bank accounts and store files. This is a particular difficulty for solicitors firms as they often store important client documents, such as wills, which cannot be destroyed for free. Where a firm is unable to organise the storage of files, for instance become it has become insolvent or been abandoned, the SRA will step in and store the files. The cost of intervening and sorting, archiving and storing files is borne by the profession.
- 4.20. Entry and exit rates over 2-3 years are around 10%, a little below average entry and exit rates across all UK businesses. This suggests that those wishing to enter the market are able to do so.<sup>68</sup> The Regulatory Policy Institute's 2013 report for the Society and the LSB regarding barriers to entry and exit highlighted that further barriers to entry, and particularly innovation, could be created by the SRA's focus on business models, finances and governance, concluding that: *"at a broad level, therefore, the market has shown itself capable of significant change" but that „regulation can be said to be impeding flexibility and innovation in business structures and business practices, in a number of ways”*.<sup>69</sup>

**Does the current regulatory framework impose disproportionate costs on legal services providers?**

- 4.21. As described above, a level of regulation is fundamentally necessary to a well-functioning legal system and proportionality should be considered in terms of consumer protection and the public interest as well as the burden placed on legal service providers. However, the regulatory framework for legal services – and so the costs imposed by this – are uneven. Unregulated providers bear far fewer costs than solicitors as they are not subject to the same regulation. For them, the regulatory framework is inadequate and they do not bear a proper share of the costs of regulating the system. For many solicitors, however, the costs of regulatory compliance are unnecessarily burdensome.
- 4.22. In 2015, the LSB conducted research with 16 solicitor firms on costs that they incurred solely to comply with legal services regulation (incremental costs). Those firms participating reported that the areas of regulation where incremental costs of regulation were highest were: PII, continuous professional

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<sup>68</sup> *Understanding barriers to entry, exit and merger, 2013*, Regulatory Policy Institute (George Yarrow and Chris Decker) for TLS and LSB.

<sup>69</sup> *Ibid.*

development (CPD) (the SRA last year reduced the formal CPD obligations on solicitors<sup>70</sup>) and information from the regulator. Other areas of regulatory costs identified included annual renewal and changes to regulation. On average, the entities reported that the total cost of regulation as a proportion of total practice costs was between 15% and 23%. Due to the small sample, the findings are qualitative and cannot be claimed to be necessarily representative of the cost of regulation felt by solicitors generally. For reliable data a significantly larger survey would have to be carried out.<sup>71</sup>

4.23. In recent years, following the Legal Services Act 2007, the regulatory costs and barriers relating to the management of risks by new firms have increased, with requirements for Compliance Officers for Legal Practice (COLP) and for Finance Administration (COFA) as well as the need to demonstrate risk management and sound business plans.

4.24. The detail of certain areas of regulation could be simplified in order to reduce waste. The impediments are more pronounced for small practices and non-traditional business models: some regulatory requirements involve a great deal of unnecessary duplication of effort, which raises costs in relation to start up merger and closure costs. As the Regulatory Policy Institute found,

*“A system that, in effect, leaves a large amount of work to be done by each of thousands of small businesses to work out what it is they have to do to comply with what appears to be a complex and not self-evidently coherent set of regulatory requirements, will tend to raise the costs of doing business. More significantly, it has the potential to divert non trivial amounts of the key resources of small practices (the time, attention and cognitive effort of the proprietors or partners) from other matters, such as the practice of law and the training of the next generation of lawyers”.*<sup>72</sup>

4.25. It has been suggested that premium levels might reduce if the compulsory PII Minimum Terms and Conditions were varied. But this would result in reduced protection for consumers. The LSB, in its decision not to grant the SRA's application for a reduction in minimum PII cover, stated that it *“did not consider that the argued countervailing benefits to this or the other objectives are sufficient or certain enough to justify an alternative decision”*. The LSB considered the SRA's reasoning, especially in relation to access to justice, and concluded that the evidence and analysis relied on by the SRA were insufficient to demonstrate a likely benefit.<sup>73</sup> Such a change could also result in an increase in premiums for solicitors who wished to continue to offer the current minimum conditions thus deterring them from doing so.

4.26. The contributions made by the profession to the Compensation Fund in 2015, as in the previous year, of £32 on a practising certificate and £548 on all entities that hold client money, appear good value for ensuring that consumers are protected from a practitioner's dishonesty, particularly when compared to the

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<sup>70</sup> <http://www.sra.org.uk/sra/news/press/sra-board-announces-new-approach-to-ensure-solicitors-remain-competent-page>

<sup>71</sup> Legal Services Board, *In-depth investigation into the costs of regulation in the market for legal services* (2015). Available at <https://research.legalservicesboard.org.uk/wp-content/media/in-depth-study-into-the-cost-of-regulation-version-2-for-publication.pdf> p24

<sup>72</sup> *Understanding barriers to entry, exit and merger*, 2013, Regulatory Policy Institute (George Yarrow and Chris Decker) for TLS and LSB, p. 3. Available at <file:///C:/Users/mmal/Downloads/RPI%20Report%20Summary%20and%20main%20conclusions%2010%20December%202013.pdf>

<sup>73</sup> *Ibid.*

cost of PII for cover against civil liability. The amount paid out by the Compensation Fund in respect of fraud is a tiny proportion compared to the huge amount held in solicitor client bank accounts at any given moment each day.

- 4.27. Some of the costs associated with regulation arise under a broader regulatory regime that is not specific to legal services, for example anti-money laundering legislation.<sup>74</sup> Other regulatory requirements, such as ensuring client confidentiality and conflict rules, reflect the common law. The 2015 Society Survey of solicitor firms' views of regulation attempted to quantify the overlap between SRA regulation and other regulation and legislation in a broad range of areas (for example equality and diversity, management, and confidentiality). The results show that, on average, approximately three-quarters of firms see at least some overlap (varying by area of compliance) and three in ten firms who see an overlap consider that SRA regulation reduces the "effort" of broader compliance.
- 4.28. Some costs that are presently mandatory under the regulatory regime would in any event be incurred by solicitors in the proper running of their business. An SRA survey indicated that 85% of firms reported that they would continue what they currently do to comply simply in order to run their firm well and look after clients' interests.<sup>75</sup> However, almost half of respondents thought that, given the size and nature of their business and their level of risk, the internal costs of compliance were excessive.
- 4.29. It should be noted that the benefits of legal services regulation, which generally do not accrue directly to legal services providers but to others in the economy, should be weighed against the costs to providers. Regulation generally benefits consumers of legal services and the economy in aggregate by promoting high quality legal work that supports the rule of law within the wider legal system. LSB's research in 2013 showed that consumers generally understood this, seeing the protections in place as striking a good balance and not wishing to see them removed.<sup>76</sup>

**What has been the impact of ABS entry on competition in the legal services sector, including on innovation, price and quality?**

**Are the rules governing ABSs unnecessarily restrictive such that they have hindered the entry and expansion of ABSs?**

**Have there been opportunities for more competition in particular legal service areas as a result of regulatory**

- 4.30. ABS are having some impact on competition in the legal services sector. This varies according to the area of legal work involved and the full impact is yet to be seen. Although more prominent in specific areas of practise, ABS constitute a small proportion of the wider legal services market: 451 SRA licensed ABS

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<sup>74</sup> Legal Services Board (2015) *The regulated communities' views on the cost of regulation*, p. 40. Available at <https://research.legalservicesboard.org.uk/wp-content/media/Cost-of-Regulation-Survey-Report.pdf>

<sup>75</sup> *Ibid* and SRA (2013) *Measuring the impact of Outcomes-focused Regulation (OFR) on firms* [www.sra.org.uk/impactofr/](http://www.sra.org.uk/impactofr/)

<sup>76</sup> *Risk and the role of regulation – Final report*, 2013, Vanilla research for the LSCP.

(January 2016) as against 10,306 solicitor firms (December 2015). About 5% of legal services are provided by ABS. Indeed, the 451 figure may not accurately represent the number of active ABS:

*'Based on the latest Law Society data extract, out of the 372 registered ABS, only 282 (approximately 75 per cent) appear to be operating as firms, which means that some 25 per cent of ABS registrations have been made, but either nothing has currently been done with them or they are operating as shell financing companies. (The SRA web site counts 405 registered ABS as at August 2015 – though again it is unlikely all of these are operational).'*<sup>77</sup>

- 4.31. Research conducted by the SRA in 2014 emphasised that it was too early to come to firm conclusions about the operation of ABS in the wider legal services market. The wide variety of ABS was cited as a barrier to drawing general conclusions: *"ABSs encompass a very wide range of different types of organisation, making it very difficult to draw generalisations about them as a distinct subset of the legal services sector. Some ABSs are very small firms, while others contain hundreds of partners and have turnovers in excess of £100 million."*<sup>78</sup>
- 4.32. ABS entrants include: (i) small law firms bringing in a partner who is not a lawyer (often relatives of lawyer-owners, managers or finance directors); (ii) traditional law firms wanting outside investors; (iii) in-house lawyers wishing to establish legal teams as ABS; and (iv) big external businesses. We understand that the largest group of ABS are medium and smaller general practice law firms, typically bringing in non-lawyer shareholders such as accountants, marketing directors, finance directors, or practice managers. Specialist practices make up the second largest group and some of the largest law firms and three of the top four accountancy firms in the UK have also established their own legal businesses.<sup>79</sup>
- 4.33. The first external entrants appeared to move into areas which are more commoditised such as personal injury and it is now estimated that almost 30% of the value of the personal injury market is accounted for by ABS.<sup>80</sup> There have been some high profile failures amongst this group. Recently, for instance, Saga Legal Services announced that it stopped taking on new business last year following the break-up of the Parabis Group (although it plans to take on new work in the future) only weeks after the AA withdrew from the market.<sup>81</sup> The Co-operative was also forced to make redundancies in its personal injury department and is now focussing more on its core family law practice.<sup>82</sup> It is noteworthy that the newest insurance company entering the market, LV, has chosen not to become an ABS and has instead partnered with a solicitors firm.
- 4.34. These failures may be explained by normal forces within a competitive market rather than ascribable to restrictive regulation. The Society's *Future Services* report predicts that by 2020 a growing number of new types of business model, often with a strong non-lawyer presence and with external investment, will exist

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<sup>77</sup> [The Future of Legal Services](#) (TLS, January 2015), p. 21.

<sup>78</sup> See <http://www.sra.org.uk/documents/SRA/research/abs-quantitative-research-may-2014.pdf> and <http://www.sra.org.uk/documents/SRA/research/abs-qualitative-research-may-2014.pdf>

<sup>79</sup> See YouGov *Legal Services 2015*, p. 65.

<sup>80</sup> *Ibid.*

<sup>81</sup> <http://www.lawgazette.co.uk/practice/saga-legal-admits-it-stopped-taking-new-work-last-year/5053373.fullarticle>

<sup>82</sup> <http://www.lawgazette.co.uk/practice/co-op-legal-heralds-turnaround-after-200k-half-year-profits/5050796.fullarticle>

and that 2020 should see ABS as a fully entrenched part of the profession and serious competition to smaller-medium Business to Consumer (**B2C**) firms<sup>83</sup> Indeed, some research contemplates the widespread financial failure of existing law firms as a result: the Association of Business Recovery Professionals, for instance, predicted in 2014 that 31% of all law firms were at risk of financial failure within the coming year.<sup>84</sup>

4.35. It is likely that the Business to Business (**B2B**) legal services market will also become more attractive for external investment through ABS because of:

- (a) increasing market size;
- (b) potential profit margins;
- (c) the fragmented nature of the market (the largest firm accounts for only 3% of the market);
- (d) increasing willingness of clients to disaggregate/unbundle legal services;
- (e) growing willingness of clients to substitute top law firms with lower-cost providers;
- (f) expanding opportunities to use technology and process re-engineering to increase efficiencies and standardisation of the delivery of legal services; and
- (g) top firms that appear to be willing to cede what they perceive as lower-margin work to other providers.

4.36. In their report *Innovation in UK legal service providers*, Roper, Love and Bourke suggest that the adoption of ABS status has a positive effect on innovation. All else being equal, ABS are 13-15% more likely to introduce new legal services and the authors infer „that the wider adoption of ABS status would be likely to increase the range of legal services on offer“.<sup>85</sup> This may be true if „introducing new services“ referred to new-to-the-market services rather than new-to-the-firm services but, whereas the report makes that distinction in some sections, this is not the case for the analysis of impacts of ABS. Furthermore, the underlying analysis did not identify causality from a firm becoming an ABS and the introduction of new, innovative, legal services. More generally, Roper et al found that innovation in the sector has not typically focused on lowering cost.

4.37. Some solicitors have envisaged significant problems arising in relation to conflicts of interest between firm senior management and shareholders. For retail markets, such conflicts might be in terms of which services a practice offers in order to return a decent profit – thus pushing some already vulnerable areas of law further out of reach for many. For business markets, conflicts between shareholders, firm and clients“ interests were potentially much more significant. The SRA considers that that there is no

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<sup>83</sup> *The Future of Legal Services* (TLS, January 2015), pp. 28 & 51.

<sup>84</sup> RBS, *A perspective on the legal market*, April 2014, p. 29.

<sup>85</sup> Roper, Love, Bourke, 2015, *Innovation in UK legal service providers*, SRA and LSB.

“additional risk” caused by the operation of a legal business through an ABS; a statement with which we agree.<sup>86</sup> Certainly the risk profile of an ABS will depend on a number of factors.

- 4.38. An example of ABS not entering a new market as had been expected is the Legal Services Commission’s (as it was) prediction in around 2001 that Community Legal Advice Centres (**CLACs**) and Community Legal Networks (**CLANs**) would be run by ABS (in collaboration with others) entering the market place. CLANs were intended to be networks of existing organisations. CLACS were new individual entities. Some of them were collaborations between existing advice organisations who, to a greater or lesser extent, maintained their separate identities. Two or three of them were set up by a solicitors’ firms in Sheffield in conjunction with A4E, but that focused on social welfare government contracts. By 2007, they were stalling, and by 2010 their presence was all but gone, finally being terminated in about 2012.

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<sup>86</sup> See the Society’s 2013 practice note available at <http://www.lawsociety.org.uk/support-services/advice/practice-notes/alternative-business-structures/>



The Law Society

## **CMA Legal Services Market Study: Theories of Harm**



# CMA Legal Services Market Study: Theories of Harm

## Specific Questions raised in the Statement of Scope

### 1. Introduction and executive summary

- 1.1. This submission supplements our first submission to the CMA in response to this Market Study. In this submission we give our views on each of the three theories of harm that the CMA is considering.
- 1.2. In section 2 below, in response to the first theory of harm (the ability of consumers to drive competition through informed purchasing decisions), we indicate the intensity of competition between solicitors firms; describe the wide choice of providers consumers have (regulated and unregulated); set out the criteria consumers take into account in selecting a provider and describe the information available to consumers concerning the costs and quality of legal advice; we set out the ways in which legal service providers seek to acquire customers and describe the role of intermediaries.
- 1.3. In section 3 below, on the second theory of harm (information failures), we describe the obligations on solicitors to provide detailed information to clients on a range of matters (including insurance and redress mechanisms) and contrast this with the lack of such obligations for unregulated providers; we set out the scope for consumer confusion and the distortion of the competitive process where providers offering the same service have materially different obligations.
- 1.4. In section 4 we respond to the third theory of harm (impact of regulation on competition). We set out our views on the scope of regulatory obligations for solicitors which are necessary for the protection of consumers and the public interest; we describe the dangers to consumers, the public interest and competition of unregulated providers offering such critical services without even minimal regulatory protections; we set out why solicitors (and other authorised professionals) should be subject to the same independently determined regulatory obligations (by independent regulators) as other legal service providers with professional bodies responsible for setting any higher standards for the holding of professional title; we indicate why the title „lawyer“ as well as „solicitor“ and „barrister should be protected; we explain that ABS have begun to make a mark on the market but it is too early to judge their long term impact.

### 2. Theme 1: The ability of consumers to drive effective competition through making informed purchasing decisions

- 2.1. As we described in our first submission to the CMA, the legal services market is competitive and highly fragmented with a wide variety of regulated and unregulated providers. Solicitors represent approximately 38-46% of all legal services providers and they compete fiercely among themselves as well as with legal executives, licensed conveyancers, notaries, specialist attorneys and the wider unregulated sector.<sup>1</sup> This

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<sup>1</sup> *The Future of Legal Services*, (TLS, January 2015).

view of the intensity of competition supported by recent independent assessments of the market, for example the IRN Research *UK Legal Services Market* report.<sup>2</sup>

2.2. Competition in consumer law practice, (including residential conveyancing, personal injury and medical negligence, family law, wills and probate, and employment law) is particularly strong and this is resulting in consolidation in some segments of the legal services market as larger firms merge to grow their market share. This is significant because high street solicitors and law firms serving mainly personal rather than corporate customers is the largest market segment in terms of the number of firms and these firms are facing the greatest pressure on revenue and profits. Annual growth in this segment is modest and there is pressure on margins for many firms. It has been suggested that smaller and medium sized consumer law firms will leave the market or be taken over by larger players.<sup>3</sup>

2.3. An April 2014 report by RBS observed:

*“One serious underlying structural challenge for the UK legal services market is that it suffers from over-capacity.....The size and shape of the supply side of the legal market continues to develop, and is characterised by ongoing growth in the number of market participants.”*

*“It is clear that the low growth evident in the market over recent years has forced firms to grow their businesses by capturing market share from competitors”.*

The report expected that legal sector consolidation would continue to drive firms’ growth in the medium term, which in our view is proving to be true.<sup>4</sup>

2.4. The following year’s assessment (published under the by NatWest brand) reached the same conclusion in relation to the competitive pressures on medium-sized firms as a result of the increasing amount of legal services work being taken on by large professional services firms:

*“Mid-tier firms are also suffering intense competition from the big-four accountants, which are quietly taking the more commoditised work away from them (see p16), while clients remain committed to fee reductions and fixed-pricing arrangements across the board. Differentiation and a clear brand identity have never been more important, as clients become much more selective about whom they instruct.”<sup>5</sup>*

2.5. A LexisNexis report on *The Age of the Client*, based on interviews with law firms and their clients, concluded:

*“The consumer culture of 24/7 availability will become even more entrenched, DIY internet-based solutions will spread to other areas of the law and competition from non-traditional sources will continue to*

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<sup>2</sup> *UK Legal Services Market Report 2015* available at:<http://www.irn-research.com/news/uk-legal-services-market-report-2015/>

<sup>3</sup> A number of the observations in this submission are based on the YouGov *Legal Services 2015* report. We have not been authorised by YouGov to quote directly from the report or to disclose all details but the report has influenced our views on the market as described in tis submission.

<sup>4</sup> RBS, *A perspective on the legal market*, April 2014, pp. 10 & 12.

<sup>5</sup> NatWest *A perspective eon the legal market report on legal services 2014-15*, p. 13.

*grow. Against this background of rapid and constant change, lawyers can't afford to become complacent. Only a culture of continuous innovation will ensure they can meet future challenges head-on.*"<sup>6</sup>

75% of respondents to the survey considered „attracting new clients“ as an important challenge for them.<sup>7</sup>

- 2.6. The Society's *Annual Firms Survey 2014-15* found competition for new business a key concern for solicitors when it asked a sample of 1000 firms whether a number of issues were a problem on a scale 1-5 (with 1=no problem to 5=very significant problem).<sup>8</sup> 21% of firms said that „competition for business“ was a significant problem for them (up from 15% in the 2013-14 Survey), with competition for business the (equal) third most common problem after (1st) changes in legal aid (23% of firms saying this was a significant problem), (2nd) costs of employing solicitors (22%), and (equal 3rd) complying with regulations on legal services provision (21%). Breaking down the results by sizes of solicitors' firms<sup>9</sup>, 20% of small firms; 24% of medium firms and 34% of large firms said that competition for business was a significant problem for them (in comparison to 14% of small firms; 19% of medium firms; and 35% of large firms in 2013-14). The increase in the percentage of firms considering that competition for business was a significant problem for them from the previous year's Survey suggests that competitive pressures on firms have been increasing. It should be noted that when asked to look at the longer term firms were most worried about competition (and government spending such as in legal aid).
- 2.7. While the absolute percentage for each category of problem was low (reflecting perhaps the diverse competitive pressures firms are under - each firm having a different view as to the relative significance of the challenges it faces) the high ranking of competition compared to other problems indicates that it is a material pressure.
- 2.8. The Society's Survey<sup>10</sup> asked those firms that identified competition for business as a significant problem, what the main source(s) of this competition were: 31% of firms identified local solicitor firms as the source; 35% regional and national solicitor firms; 22% networks of solicitors; 46% non-solicitor legal providers; 50% „volume“ legal services providers and 33% Alternative Business Structures (**ABS**). „Volume“ legal services providers were therefore a significantly higher source of competition and networks of solicitors a significantly lower source of competition. The question was not repeated in the 2014-15 survey, or the forthcoming 2015-16 survey.
- 2.9. To complement the recent studies that the Legal Services Board (**LSB**) and Legal Services Consumer Panel (**LSCP**) have commissioned, the CMA may wish to review YouGov's suite of legal services reports

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<sup>6</sup> LexisNexis, *The Age of the Client* (2015), p.12. Available here [http://businessoflaw.lexisnexis.co.uk/wp-content/uploads/sites/24/2015/04/LexisNexis\\_Bellwether2015\\_Age\\_of\\_the\\_Client.pdf](http://businessoflaw.lexisnexis.co.uk/wp-content/uploads/sites/24/2015/04/LexisNexis_Bellwether2015_Age_of_the_Client.pdf)

<sup>7</sup> *Ibid.*, p. 10.

<sup>8</sup> See <http://www.lawsociety.org.uk/support-services/research-trends/annual-firm-survey-2014-15-snapshots-from-the-results/>

<sup>9</sup> The sizes of solicitors firms are measured in terms of their number of partners. Small firms are defined as 1-4 partners, medium size firms as 5-25 partners, and large firms as 26+ partners. These sizebands do imply lower bands than the standard ONS/Eurostat bands, which is necessary in order to give sensible splits of solicitor firms by size. The approximate relationship between the solicitor firm sizebands (in terms of number of partners) and the ONS/Eurostat sizebands (in terms of total number of employees) is shown in the table below.

<sup>10</sup> See <http://www.lawsociety.org.uk/support-services/research-trends/firm-survey-2013-14/>

which indicate that competitive pressures are increasing as new entrants and business models become more significant.

- 2.10. The Legal Needs Survey that we are undertaking jointly with the LSB and the Legal Education Foundation (LEF) and which is planned to be published this spring is likely to prove relevant to many of the questions identified under this theme. The questionnaire is based on that used in LSB's 2012 Legal Needs Survey.

**What information do consumers use to judge the quality of legal services and/or legal services providers? What price information is made available to consumers? Do consumers find it easy or difficult to compare the quality and prices of legal services?**

- 2.11. Consumers have a wide choice of legal service provider. The 2014 report by RBS characterises the legal services market as *"currently a buyers" market, which means that clients are in a position to more readily dictate terms on price, service and ancillary support. The pressure on billing rates is set to continue, as is an increasing requirement for alternative fee arrangements, greater pricing transparency and more value.*<sup>11</sup> This is borne out by the findings of the LSCP tracker survey, that almost 70% of people who used legal services in the past two years felt they had a choice of provider, and 25% shopped around.<sup>12</sup>
- 2.12. The ways in which customers choose legal services providers vary depending on the complexity of their problem and the area of law involved. The YouGov *Legal Services 2015* report examined these methods in some detail.
- 2.13. As a general reflection of trends across consumer markets, the number of potential clients looking to internet search engines, consumer review websites and specialist online legal directories and using the Citizens Advice Bureau is undoubtedly increasing.
- 2.14. Research by LexisNexis found that consumers are more likely to search online to gather information to help them identify, validate and select a legal provider (individual or organisation) than to rely on a recommendation (see the table below).<sup>13</sup> This trend towards using online resources may lead to consumers shopping around even more for their legal services in the future.<sup>14</sup>

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<sup>11</sup> RBS, *A perspective on the legal market*, April 2014, p.24.

<sup>12</sup> [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Using\\_legal\\_services\\_000.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Using_legal_services_000.pdf)

<sup>13</sup> The Attorney Selection Research Study conducted by LexisNexis Martindale-Hubbell in February 2012 (Survey base: 4,000 consumers).

<sup>14</sup> YouGov *Legal Services 2015*, pp. 27-30. We subscribe to YouGov's legal channel reports and use of findings is restricted. Publications can be purchased from YouGov and we recommend this to the CMA if the CMA wishes to find further information on these findings.

**A Closer Look at Online Resources and Friends/Family Usage**

	Gather	Find	Validate	Select
<b>Online resources (net)</b>	65%	61%	53%	44%
Online search engines	39%*	35%	23%	20%
Online directories	31%	30%	21%	16%
Social media sites	26%	22%	16%	11%
Law firm websites	31%	35%	26%	21%
Legal blogs	29%	21%	17%	12%
Online legal advice forums	34%	22%	18%	13%
<b>Friends/Family advice/ recommendation (outside of social media sites)</b>	39%*	45%*	36%*	36%*

★ Indicates leader in category

Comparison of online resources and family/friends usage by those who sought an attorney in the past year, broken down by each stage of the search process.

2.15. The Society provides a Find A Solicitor (**FAS**) service online and on the phone – now linked to a „Lawyers For Your Business“ accreditation which has proved popular with consumers. The website receives 554,000 average visits each month (6.65 million visitors in the year) and the telephone service is also popular with 89.34% of callers either satisfied or very satisfied with the service they received.<sup>15</sup> This is proving a valuable resource for consumers with recent research commissioned by the Society finding that when consumers were asked about specific websites whose reviews would be trusted, the two top rated websites were the Law Society and the Solicitors Regulation Authority.<sup>16</sup> The Society’s accreditation system is a valuable resource to help support consumers’ decision-making process to identify, validate and select a law firm or solicitor with validated expertise. In the absence of a recommendation, accreditations serve as a quality mark to help short-circuit the decision making in the buying process. 14,952 individuals are accredited to one of our schemes (figures as at 18 January 2016). The Wills & Inheritance Quality (**WIQS**) accreditation is a good example. We market this to solicitors firms as a way to inform and gain client confidence, as follows: „*Demonstrate your firm’s excellence in delivering wills and inheritance advice through a best practice quality mark that prospective clients can trust*“ and „*Gaining WIQs accreditation can help you to win more business, increase client satisfaction and minimise the risk of claims*“.<sup>17</sup>

2.16. Alongside changing trends in the way in which consumers find a solicitor, there are discernible trends in how they make a choice. Recent research for the Society found that, among a number of criteria used to

<sup>15</sup> The Law Society, Find a Solicitor Google Analytics data, Jan - Dec 2015.

<sup>16</sup> Consumer use of ratings for solicitors/law firms, omnibus survey conducted by Bilendi for the Law Society, April 2015, Survey base: 2,009 UK adults aged 18 and above.

<sup>17</sup> *Promoting your Wills and Inheritance Quality Scheme Accreditation Practical guidance to help you market your accreditation* (TLS, 2014).

choose a solicitor, respondents rated as most important „understanding needs“ and „quality of client service“, while the least important were the location and size of the firm. „Keeping you informed“ and „explaining the process and options clearly“ were rated more highly than „value for money“ although the percentage differences were small.<sup>18</sup> YouGov’s research also reports on trends in the information consumers use to choose and judge legal services. While experience and reputation remain important criteria these have recently been overtaken by the cost of services. Costs are important both in terms of the absolute amount but also as the ability to be certain about likely costs. Consumers therefore show a strong and increasing preference for fixed fee and no-win-no-fee arrangements. Fixed fees have been prevalent in residential conveyancing and wills for many years.

- 2.17. Fixed-fee arrangements are more prevalent than hourly-billing in conveyancing, will-writing and immigration law.<sup>19</sup> YouGov, in its 2015 report, found that 58% of those using law firms and solicitors in the last three years paid for their legal advice on a fixed fee basis, with 49% charged the fee at the end of the legal matter that they were quoted initially. Only 12% of consumers were charged using an hourly rate model. No-win, no-fee arrangements accounted for a further 6%, and legal aid only 3%.<sup>20</sup> It is worth noting, that the scope of fixed fee agreements will be limited depending on the particular area of law and that, on some occasions, unbundled advice can cost more.
- 2.18. As well as offering more services on a fixed fee basis, solicitors are endeavouring to provide more transparency of fees to differentiate themselves from their competitors and help consumers make an informed decision. Many solicitors firms now give fixed fees on their websites and offer quotation services.<sup>21</sup> Research by the LSB into how costs are presented to wills and probate consumers found that 54% of consumer respondents were provided with an estimated cost before commissioning work and 26% of respondents were provided with a formal quote. Questioned about the end of the process, 62% said the final cost was about the same as they expected, 27% said it was either slightly or much more and 5% said it was slightly less or much less.<sup>22</sup>
- 2.19. While these trends to fixed fees and greater transparency makes price comparison easier, it is more difficult for consumers to compare the quality of the legal services they purchase. We agree with Richard Moorhead’s conclusion in a paper for the LSB that:

*„for the market to function effectively, signals about the relative quality of legal services have to be at least as meaningful as signals on price. If they are not, quality is likely to diminish significantly as a result of*

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<sup>18</sup> Consumer use of ratings for solicitors/law firms, omnibus survey conducted by Bilendi for the Law Society, April 2015. Survey base: 2,009 UK adults aged 18 and above.

<sup>19</sup> SRA Risk Outlook, page 10. Available at <https://www.sra.org.uk/risk/outlook/risk-outlook-2015-2016.page>

<sup>20</sup> YouGov *Legal Services 2015*, p.11.

<sup>21</sup> See for example: [http://www.tmsolicitors.co.uk/probate-solicitors-costs/?utm\\_term=%2Bprobate%20%2Bservices&utm\\_content=108363862408&utm\\_campaign=225232888&utm\\_source=google&utm\\_medium=cpc&mh\\_keyword=%2Bprobate%20%2Bservices&gclid=ClihxotPgcsCFRYW0wodMMch9w](http://www.tmsolicitors.co.uk/probate-solicitors-costs/?utm_term=%2Bprobate%20%2Bservices&utm_content=108363862408&utm_campaign=225232888&utm_source=google&utm_medium=cpc&mh_keyword=%2Bprobate%20%2Bservices&gclid=ClihxotPgcsCFRYW0wodMMch9w) and <http://www.probaters.com/our-services/?gclid=CPGAzpHPgcsCFQccGwodXIkMiQ>.

<sup>22</sup> LSB, *The use of probate and estate administration services* (2012), pp. 45 & 48. Available at [http://www.legalservicesboard.org.uk/Projects/reviewing\\_the\\_scope\\_of\\_regulation/yougov\\_research.pdf](http://www.legalservicesboard.org.uk/Projects/reviewing_the_scope_of_regulation/yougov_research.pdf)

*competition. Ensuring that stronger signals of relative quality develop within legal services markets should be a central goal of service providers and regulators.*<sup>23</sup>

- 2.20. This is partly an inherent problem as many legal services are an “experience good” - a service where product characteristics are difficult to observe in advance, but where these characteristics can be ascertained upon consumption. In many instances legal services may be “post-experience goods” (or “credence” goods), with individual customers being uncertain as to the quality they have received even after purchasing the service.<sup>24</sup> An obvious example is will writing, where the purchaser will not necessarily ever know if the job was done well.<sup>25</sup> Any problems with conveyancing, legal contracts or advice may not emerge for many years after the initial advice or transaction.
- 2.21. In judging quality, consumers can face particular difficulties when seeking to differentiate between legal services provided by regulated as opposed to unregulated service providers. An important aspect of the quality of service offered is the level of consumer protection offered by the legal service provider which differs enormously between, on the one hand, solicitors (and other regulated providers) and unregulated providers (as explored in more detail in our response to the Theme 2 and Theme 3 questions below). Many consumers assume that unregulated providers offer the same level of protection as regulated providers, severely inhibiting their ability to make informed purchasing decisions.
- 2.22. Two research reports from 2013 looked into this issue. The LSB's Consumer Panel 2013 report on risk and the role of regulation was commissioned from Vanilla Research ('the Vanilla research') in response to the (then) government's concern that too much regulation was leading to a compensation culture.<sup>26</sup> The aim of the research was to gather information about consumer perceptions in order to inform a wider LSCP project which aimed to address the question of whether the financial protection arrangements in place in the legal services market were fit for purpose.
- 2.23. In summary, the Vanilla research found that:

*'Consumers have minimal knowledge of existing consumer protections. As might be expected, there is little actual knowledge about the various protections that are currently in place for legal services consumers. Nearly everyone assumes something is in place, but few can describe what this something is, other than some general references to "an Ombudsman". The assumption is a reasoned one in consumers' minds – being a solicitor is a "profession", with standards, and so they feel confident there is some kind of consumer protection in place'; and*

*'Although consumers generally took plenty of reassurance from the existing consumer protection schemes, a contradiction exists: the risks consumers are most worried about when dealing with legal*

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<sup>23</sup> *Understanding the economic rationale for legal services regulation – A collection of essays* (2011), LSB.

<sup>24</sup> See CMA Statement of Scope at 3.19.

<sup>25</sup> Of course, the purchaser may feel the service levels were high and the matters well explained, but they would be unlikely to know whether the will was drafted effectively.

<sup>26</sup> *Risk and the role of regulation* report for the Legal Services Consumer Panel by Vanilla Research, January 2013. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf)

*services are not thought to be covered by these current protections (for example inexorably rising costs), and two of the main risks that are covered (fraud and bankruptcy) are not something consumers consider'.*

- 2.24. In so far as unpredicted costs were a concern identified by Vanilla the market response has been a much greater use of fixed fees as described above.
- 2.25. The Vanilla research found that few consumers were happy at the thought of the existing levels of client financial protections being taken away: *'There is a view that legal services are different to other sectors (it's a profession, dealing with the law, and life-changing events), and that there should be sector-wide protections in place'.*
- 2.26. Consumers rejected the suggestion that they should take on risk themselves<sup>27</sup> and the research identified strong resistance among consumers to the idea of purchasing their own insurance as they had little confidence in their own abilities to make informed decisions about which policy was right for them. Additionally, there was a further complicating worry that consumers, if forced to purchase their own insurance for certain areas of legal advice, would not actually know what they were buying (in terms of risks they were insuring against, or the level of cover needed). In other areas, such as conveyancing, the decision making on such questions is led by the lenders who fund the transaction.
- 2.27. The LSCP's report *Financial protection arrangements* in June 2013 referred to previous studies which suggested that consumers of legal services generally lack the detailed knowledge needed to compare services accurately and access quality.<sup>28</sup> The LSCP report identified the risk that: *'...informed consumers will only use insured lawyers, while more vulnerable consumers will either not realise that mandatory protections are not in place or will choose lawyers without insurance solely on the basis of cost'.*
- 2.28. In light of this, the LSCP report recommended that the financial protections should remain mandatory and that consumers should not be asked to source their own insurance, mirroring the Vanilla research's findings on consumer's views.<sup>29</sup> The report states that:

*'Despite some challenges around access to data, at a high level, and on most occasions the financial protection regimes will deliver redress against each of the key risks that consumers face when buying legal services. They are designed to offer a comprehensive level of protection and assume that consumers should bear quite a low burden of risk – we consider this is entirely appropriate given the nature of legal services, consequences of the risks transpiring and the difficulty consumers face in preventing loss'.*

We have over the last two years provided extensive comment to the SRA on the existing solicitors' client financial protections in response to the SRA's desire to dilute these protections and our views are summarised in our responses to the Theme 2 questions below.

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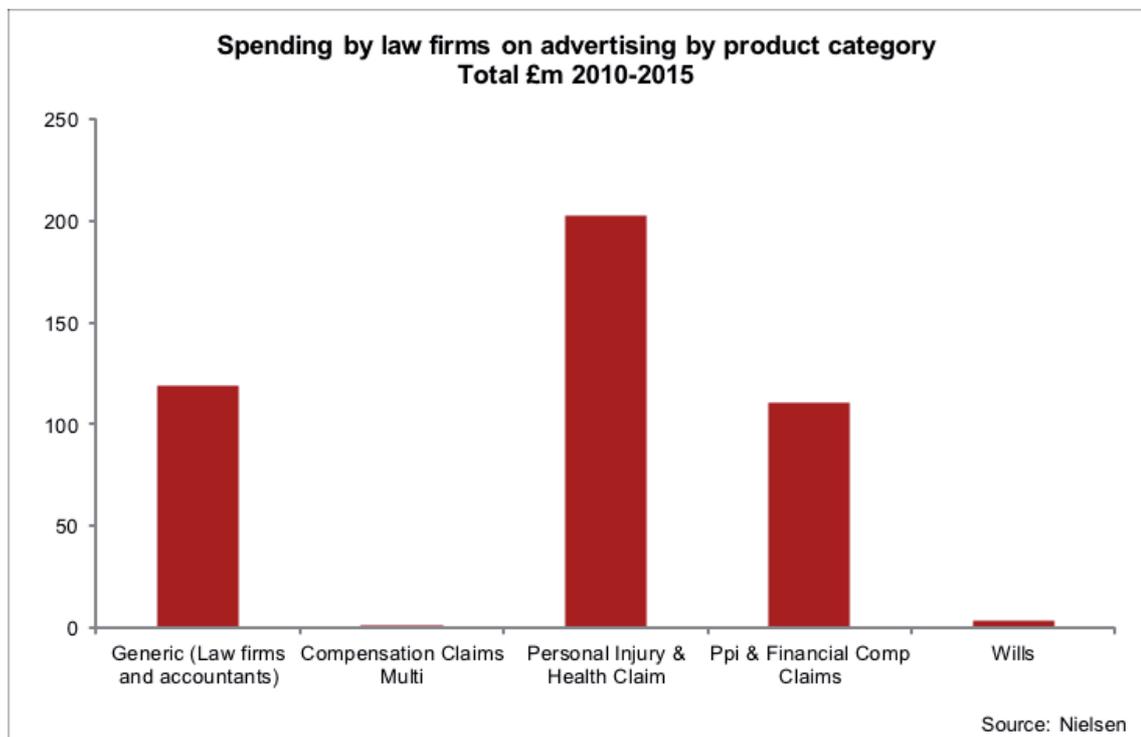
<sup>27</sup> A suggestions that is still found in the rationale for the SRA's recent proposals to change consumer protection levels by changing the minimum terms and conditions of solicitors' PII cover.

<sup>28</sup> <http://www.legalservicesconsumerpanel.org.uk/ourwork/Financial%20Protection/FPAs%202013%2006%2010%20final.pdf>

<sup>29</sup> <http://www.legalservicesconsumerpanel.org.uk/ourwork/Financial%20Protection/FPAs%202013%2006%2010%20final.pdf>

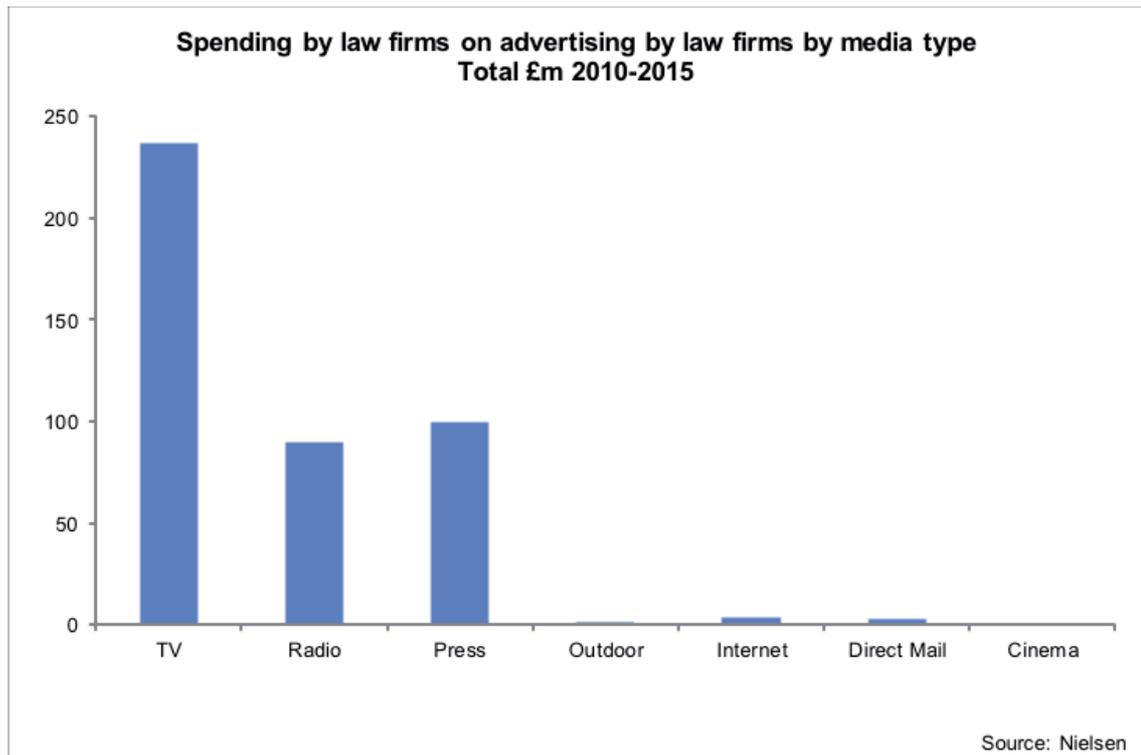
**How do providers of legal services compete with each other in seeking to win new business? Do they face any difficulties in winning new business?**

- 2.29. Solicitors (and other legal services providers) are responding to competitive pressures in a variety of ways in their attempts to win new business. This is most explicit in direct advertising campaigns. Two national law firms (Slater & Gordon and Irwin Mitchell) have embarked on major TV advertising campaigns in the last 18 months (and other firms have previously engaged in such campaigns), while claims management companies have been ubiquitous across all media channels.<sup>30</sup>
- 2.30. Research by Nielsen over the five years from 2010-2015 shows that the amount spent on advertising and the media channel used depends on the area of legal service.<sup>31</sup> The main areas of legal service advertised by law firms are personal injury and health claims followed by PPI and financial claims and then generic advertising. The main media used are TV, radio and press – again with some variation depending on the area of legal service, with will writing advertised mainly in the press. The graphs below shows the total amount spent by law firms on advertising by legal service and media channel:



<sup>30</sup> A survey of marketing professionals in the legal sector was carried out in association with The Lawyer by eConsultancy in 2015, providing information on digital marketing media and plans. We will provide this to the CMA separately.

<sup>31</sup> AC Nielsen.



2.31. Smaller firms lack the resources, expertise or money for high profile campaigns though they do benefit from Society campaigns advising consumers on the benefits of using a solicitor. In any event it would be wrong to consider direct advertising as the most significant method used by law firms to acquire customers. In common with other professional service providers, particularly those with a principally local client base, solicitors go about customer acquisition through networking, providing training opportunities and client publications and other ways of raising their profile among potential clients. For small firms in particular, word of mouth is key to their winning business and they explore ways to become better known in their local area or for their area(s) of expertise. This would involve activities such as client seminars on developing areas of law, placing articles in local newspapers, commenting on issues on local radio, attendance at networking events such as chamber of commerce and trade union events, corporate social responsibility work and the like. Participating in or sponsoring local and national business and legal awards can also be used to raise a firm's profile as shown in a recent example where a firm noted its award win from the Law Society's Excellence Awards 2016 on its website.<sup>32</sup> Some, but not all, of these activities would be captured in solicitors firms' marketing spend but much of it is unlikely to be formally recorded as a „cost" to the firm or necessarily identified as a marketing activity. Nevertheless the principle reason for engaging in such activities is to build and retain the client base.

2.32. The Law Society's Law Management Section's recent financial benchmarking survey found that the median spend on direct marketing (including staff costs) has remained stable at 2% of practice fee income in both 2015 and 2014 but for reasons explained above this is likely to understate customer acquisition

<sup>32</sup> See <http://www.lawsociety.org.uk/support-services/events-training/excellence-awards/> and <http://www.debenhamsottaway.co.uk/news/2016/02/a-great-start-to-2016-for-debenhams-ottaway>

activity.<sup>33</sup> Research by LexisNexis examined firms' marketing spend globally and found that: for smaller practices (1-20 lawyers), an overall marketing budget of less than \$155,000 was most prevalent; for medium sized practices (20-50 lawyers), the size of the marketing budget crept up more towards the \$775,000 mark while; for practices of 50-100 lawyers, marketing expenditure levels up to \$1.5 million were commonplace.<sup>34</sup> Solicitors increasingly recognise the importance of their marketing spend, with the LexisNexis *The Age of the Client* report finding that 57% of respondents have „planned or implemented increased spend on marketing“.<sup>35</sup>

- 2.33. Solicitors are also looking online for ways to engage with clients and potential clients. Recent research conducted by the Society found that email, website and social media are the top three channels that law firms are using to engage with customers. Content marketing (i.e. of a firms' expertise or legal issues), email marketing and data management/eCRM were cited as of being particularly important resources for solicitors. The report says: *“Asked specifically about client acquisition through digital marketing, content marketing predominates (67%). Content has always been important for client retention but is here shown as vital for acquisition. Content in turn impacts SEO [online search engines], also highlighted as an important activity for customer acquisition (59%)”*<sup>36</sup>.
- 2.34. Exploring firms' websites can give some insight into the types of customer acquisition activities undertaken by solicitors and examining the advice given to solicitors firms by marketing advisors and by the Society itself is also instructive. Marketing companies offer services to help solicitors to raise their profile, such as producing key facts and figures cards in their specialist areas.<sup>37</sup>
- 2.35. We have sought to help solicitors to explore these options, within the last few years producing such publications as „Marketing Legal Services“ (2011), „Law Firm Marketing Toolkit“ (2013), „Social Media in the Legal Sector Special Report (2013)“ and „Niche Marketing for the Legal Sector Special Report“ (2015). We also provide training for its members, with recent examples including „Survive and thrive - growing your law firm in a competitive market“ (2015), „Social media for lawyers“ (2015) and „Grow your small firm with LinkedIn“ (due to take place in March 2016). We seek to share our members' knowledge and experience on competitive strategies and activities through our website and community pages.<sup>38</sup> Our most recent project is Lawyers for Your Business (LFYB) – a scheme aimed at smaller firms and sole practitioners who would like help in generating new business enquiries from start-up, small and medium, size businesses which is due to launch soon. Business consumers can filter results to only display LFYB

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<sup>33</sup> Law Management Section, *Financial Benchmarking Survey*, p. 41.

<sup>34</sup> The Use of Websites in Law Firm Marketing, conducted by Purple Market Research for LexisNexis Martindale-Hubbell, July 2012. While this was a global study, its findings are still relevant to the UK as, within a survey base of 184 law firms, 60 were from firms in England and Wales)

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[http://businessoflaw.lexisnexis.co.uk/wpcontent/uploads/sites/24/2015/04/LexisNexis\\_Bellwether2015\\_Age\\_of\\_the\\_Client.pdf](http://businessoflaw.lexisnexis.co.uk/wpcontent/uploads/sites/24/2015/04/LexisNexis_Bellwether2015_Age_of_the_Client.pdf)

<sup>36</sup> Consumer use of ratings for solicitors/law firms, omnibus survey conducted by Bilendi for the Law Society, April 2015. Survey base: 2,009 UK adults aged 18 and above

<sup>37</sup> See for example <http://www.bernersmarketing.co.uk/news/2016-employment-law-facts-figures-cards-now-available.html>

<sup>38</sup> See for instance <http://communities.lawsociety.org.uk/small-firms/features-and-interviews/practical-support-features/marketing-the-small-law-firm-five-things-i-learned-using-google-adwords/-pay-per-click-advertising-ppc/5052666.article>; <http://communities.lawsociety.org.uk/small-firms/features-and-interviews/interviews/marcus-hayes-my-niche-practice-firm/5053399.article>; and <http://communities.lawsociety.org.uk/small-firms/features-and-interviews/practical-support-features/small-firm-entrepreneurs/5051105.article>.

members or to find their nearest LFYB member by searching against specific areas of practice. Improved marketing will include paid search campaigns and extending work with third party referrers, for example Barclays Bank, who have already introduced LFYB as part of their business start-up package.<sup>39</sup>

**Do intermediaries (such as estate agents, insurers and accountants) play a role in helping consumers to choose legal services providers?**

- 2.36. Research has shown that many consumers return to a legal services provider they have used before (21% of those survey by the LSCP found their lawyer this way) but personal recommendation (14%) and referral by a company (13%) are also common routes.<sup>40</sup> The LSCP tracker also shows that that 70% of consumers felt that they had had a great deal or fair amount of choice overall. Those whose service was provided by insurers rated satisfaction with choice far lower at 42% (52% for those using trade unions).<sup>41</sup> The YouGov 2015 report has insights on referrals.<sup>42</sup>
- 2.37. In many cases, referrals from intermediaries will be based on their experience of dealing with that legal services provider. However, in some cases intermediaries require a fee to be paid by a lawyer to be introduced and referred work (a referral fee). For instance, it is frequently the case that an estate agent or a financial advisor will require to be paid a fee by the solicitor to recommend the legal service to clients. When the fee is paid varies with the transaction type: some fees may be paid for leads while others might only be paid where a transaction is completed. The payment of referral fees within the legal market has caused controversy and in the personal injury market such payments are now banned. In other areas of law referral fees are still permitted though there are conduct rules for solicitors regarding payment of such fee. Solicitors are required to ensure any such arrangement is in the best interest of their client; that the referrer has not used marketing tactics that would be banned under the SRA Code of Conduct; and that clients are made aware of any fee paid.<sup>43</sup>
- 2.38. In conveyancing, some solicitors firms make payments to estate agents for referrals within segments of the market. A market appraisal undertaken by the Society in 2013 indicated that fees ranged between £100 and £200, while an earlier investigation into referral fees by the LSB indicated that fees could be as high as £250 - £400.<sup>44</sup> The LSB investigation suggested that referral fees did not damage the quality of service provided by lawyers or the cost paid by consumers in either the personal injury or conveyancing market.
- 2.39. In the case of will writing, some banks and building societies offer these services to their clients or refer them to other providers. In these circumstances, we have concerns that consumers are not making an

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<sup>39</sup> See <http://www.lawsociety.org.uk/support-services/lfyb/>

<sup>40</sup> Legal Services Consumer Panel (2015), *Tracker Survey 2015* - data tables for recent users.

<sup>41</sup> Legal Services Consumer Panel (2015), *Tracker Survey 2015* - data tables for recent users. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Tracker\\_Users\\_15\\_000.xlsx](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Tracker_Users_15_000.xlsx) Q60

<sup>42</sup> YouGov *Legal Services 2015*, p.27.

<sup>43</sup> SRA Code of Conduct (version 15) <http://www.sra.org.uk/solicitors/handbook/code/part3/rule9/content.page>

<sup>44</sup> Legal Services Board (2010) *Cost benefit analysis of policy options related to referral fees in legal services* <https://research.legalservicesboard.org.uk/wp-content/media/2010-Investigation-into-referral-fees-report.pdf>

informed choice of will writer and may not be advised of the difference between a regulated and unregulated will writer.

**3. Theme 2: Whether information failures expose consumers to harm that is not being adequately addressed through existing regulation or redress mechanisms**

**Are current regulations effective in protecting consumers' interests?**

- 3.1. For the reserved activities ex-ante protection ensures that providers are properly trained and are subject to appropriate regulatory supervision and redress systems. In the case of solicitors these protections extend beyond the reserved activities to all of the authorised person's activities as a solicitor. Chapter 1 of the SRA Handbook<sup>45</sup> requires solicitors to achieve a number of client care outcomes including informing clients at the outset of the likely scope of the work and costs and of redress mechanisms. The YouGov 2015 report found in its December 2014 survey, that an overwhelming majority of clients felt that the information provided by their legal representative was clear and easy to understand (85% found information presented in consultations with their solicitors easy to understand and 80% found information in legal documents clear and easy to understand).<sup>46</sup> No such information obligations exist for the unregulated sector.
- 3.2. Such protections are necessary because legal services are experience or credence services and consumers will in many cases not be in a position to judge what may be involved in a legal service, the complexity of the service and the likely costs. They are therefore reliant on what the service provider tells them and on the fact that the service provider is properly trained and supervised. Absent these protections the consumer is at risk.
- 3.3. The asymmetry of information between provider and consumer does not just relate to the nature, extent and cost of the legal service but also to the levels of protection available to the consumer. Consumers may assume that all providers of legal services are regulated and that a similar level of protection exists in relation to all providers. An unregulated provider has no obligation to tell a consumer that it is not regulated.
- 3.4. The Legal Ombudsman has reported cases where consumers complain about a legal service they have received but because the provider is unregulated no redress is available:

*“These cases reveal a mismatch between consumer expectations of what constitutes a „legal service“ - which consumers clearly assume implies access to a proper system of regulation and redress - and the reality of the diverse market providing such services. This confusion is not helped by the habit many*

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<sup>45</sup> SRA Handbook, *Code of Conduct*, Chapter 1. Available at <https://www.sra.org.uk/solicitors/handbook/code/part2/content.page>. See in particular Outcomes 1.9. 1.10. 1.13, 1.14 & 1.16.

<sup>46</sup> YouGov *Legal Services 2015*, p.34.

*unregulated companies have of presenting themselves as though they were traditional law firms, with websites and advertising material branded with the panoply of wigs, gowns and quill pens.*<sup>47</sup>

- 3.5. There is a significant difference between consumer satisfaction levels when using a solicitor and using an unregulated provider. The YouGov 2015 report found that customer satisfaction was materially lower for those using other providers than those using law firms and solicitors.<sup>48</sup>
- 3.6. The existence of appropriate insurance cover is an important consumer protection. Claims against a legal service provider might not arise for many years (for example, when a will is executed or a property is sold). For this reason, solicitors' compulsory professional indemnity insurance (**PII**) is provided on a 'claims made' basis whereby the insurer currently providing cover assumes the risk for any claim that is made during the current insurance period. In contrast, unregulated providers simply do not have the same level of client protection arrangements in place (and in many cases no protection at all).
- 3.7. As set out in full in our first submission to the CMA, the compulsory PII Minimum Terms and Conditions provide redress to clients and protection for managers and partners and also solicitors and staff in the firm for negligent mistakes:
  - (a) The firm's PII policy will meet each and every claim up to £2m under the minimum terms and conditions (£3m for LLPs). There are very limited occasions when the PII will not be valid. Clients are protected even if there has been misrepresentation on the proposal and if there has been dishonesty (unless all partners are tainted with the fraud –see Compensation Fund);
  - (b) it is important to note that solicitors are not permitted to limit their liability to clients to less than the minimum sum insured;
  - (c) Top up cover is available and often purchased by firms which consider that their work involves higher risk, on negotiated terms;
  - (d) Where the insurance cover is insufficient, the firms' partners (and, possibly former partners) are liable for any losses;
  - (e) Run-off cover must be purchased on disclosure and is guaranteed by qualifying insurers for six years after the firm ceases to practise; and
  - (f) Claims which arise more than six years after closure are at present handled with by the Solicitors Indemnity Fund,(which has been in run off since 2000) but this arrangement will only last until 2020 unless the SRA decide it is willing to continue this consumer protection). Current SRA proposals are for the Fund to cease operations after 2020 and offer no cover beyond that year leaving firms that now close without automatic protection six years after their closure. SRA has also proposed

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<sup>47</sup> Legal Ombudsman, *Annual Report and Accounts* (2011), pp. 21-22. Available here <http://www.legalombudsman.org.uk/downloads/documents/publications/Annual-Report-2010-11.pdf>

<sup>48</sup> YouGov *Legal Services* 2015, pp. 12 & 37.

reducing the level of compulsory run off cover from six years to three, which we consider will create a significant gap in client protection.<sup>49</sup>

- 3.8. Solicitors are also required to contribute to a Compensation Fund which, in broad terms, is used to compensate clients for certain losses caused by uninsured solicitors or where funds have been misappropriated.<sup>50</sup>
- 3.9. These complementary client protections re-enforce the solicitors' profession covenant of trust with the public - the importance of which was highlighted by the *Wolstenholmes* case sentencing judge when he referred to the profession as: *'...a business in which members of the public are entitled to place absolute trust'*.<sup>51</sup> Client protections benefit solicitors and their staff as well as the public, as recognised by the House of Lords judgment in *Swain v The Law Society*.<sup>52</sup> The 2012 SRA annual report also recognised the advantages to consumers and to the economy of these high client protections:

*'Consumers of legal services in England and Wales are better protected than in comparable jurisdictions abroad. This certainly enhances the reputation and offering of solicitors, who will generally see it as a price worth paying'*.<sup>53</sup>

- 3.10. The LSB carried out qualitative research in 2015 which largely corroborates the SRA's 2012 statement.<sup>54</sup> The LSB's recognised that the current protections come at a high cost to the profession. It states that PII was perceived to be one of the highest cost areas of regulation: *'While 19% of entities nominated PII as their priority to keep, 8% identified it as their priority to remove.'* As the RBS report of April 2014 says: *'PII is a major law firm expense-irrespective of the size of the practice'*.<sup>55</sup>
- 3.11. Nevertheless, the report demonstrated that PII is valued by the profession, finding that: *"Of those that wanted to keep PII, 53% - or 10% of all respondents - felt it should be kept because that specific regulation helps them get work and reduces the costs they would otherwise face."* Indeed, *"the highest*

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<sup>49</sup> The Solicitors Indemnity Fund (SIF) was created in the late 1980s to act as the profession's own insurer, providing also run-off cover for perpetuity for solicitors and firms which ceased to trade, without any requirement on them to continue to pay contributions. In 2000, the profession voted to close the SIF and to move to the open market for its members' indemnity needs. The contributions collected, and investment income, were used by the SIF to fund the handling, defence and settlement of claims which still fell to be dealt with it. The two main categories were (A) claims made or intimated prior to 1 September 2000 and (B) 'run-off claims', made on or after 1 September 2000 in respect of principals who had retired before that date. In 2004 the Society decided to use part of the remaining SIF surplus to purchase additional run-off cover for solicitors who remained in practice after 1 September 2000. This reflected a concern at the time of the abolition of the SIF, which led to the Society at that time deciding that the profession would collectively make arrangements to fund run-off cover to the extent that that was not provided through the minimum terms and conditions. This led to the use of part of the SIF surplus to purchase post six-year run-off cover, commencing on 1 September 2007 and running to 30 September 2017. As a consequence of the 2007 act, the SRA is responsible for decisions relating to indemnity as a regulatory function and is therefore responsible for deciding whether the current SIF should be extended. One such extension was made to 2020. A further decision by the SRA - whether, subject to adequacy of remaining surpluses, to extend beyond 2020, is awaited.

<sup>50</sup> SRA Compensation Fund Rules 2011

<sup>51</sup> See <https://www.gov.uk/government/news/13m-shortfall-2500-dissatisfied-clients-former-members-of-legal-firm-wolstenholmes-get-combined-70-years-director-disqualifications>

<sup>52</sup> *Swain v The Law Society* [1983] 1 AC 598 (5:36).

<sup>53</sup> SRA, Annual Report (2012), Chairman's Foreword. Available at <http://www.sra.org.uk/sra/how-we-work/reports/moving-forward.page>

<sup>54</sup> LSB, *The regulated communities' views on the cost of regulation* (2015), p.6. Available at <https://research.legalservicesboard.org.uk/wp-content/media/Cost-of-Regulation-Survey-Report.pdf>

<sup>55</sup> RBS, *A perspective on the legal market*, April 2014, p. 15.

ranked area of regulation to keep was PII", with 18% of entities and 19% of individuals choosing this area. The comments suggested that it was an area to keep because of the protection it provides to those in business. As one entity respondent stated: "I'm human, therefore I'm fallible. It makes good economic sense and is good risk management to have an insurance policy in case something goes wrong..."<sup>56</sup>

**Are consumers aware of the existing redress mechanisms? Are they being pointed to redress mechanisms by providers when appropriate?**

- 3.12. Solicitors are obliged to make their clients aware of their complaints process and access to the Legal Ombudsman's service both at the start of a matter and at the end of any complaints handling procedure. Many solicitors choose to do so in their initial engagement letter. The LSCP consumer tracker data found that 44% of consumers said they would know how to go about making a complaint, with the majority (56%) saying they would go to the firm itself and the Legal Ombudsman the next most common response (19%).<sup>57</sup>
- 3.13. Despite the importance of appropriate redress mechanism for consumer protection, the regulation of client protection is applied inconsistently across the legal services market: the level of protection offered by solicitors is not available from other providers and certainly not from unregulated providers. The LSB has established that, in the case of will writing, many consumers are not adequately protected at the time a will is written or an estate is administered.<sup>58</sup> As explained further above at paragraph 3.4 and in our first submission to the CMA, consumers are not aware of this difference when they purchase legal services and do not therefore know that, in choosing an unregulated provider of legal services, they are exposing themselves to risk.
- 3.14. Statements by the Legal Ombudsman included in our first submission to the CMA describe this discrepancy: "*These cases reveal a mismatch between consumer expectations of what constitutes a 'legal service' - which consumers clearly assume implies access to a proper system of regulation and redress - and the reality of the diverse market providing such services. This confusion is not helped by the habit many unregulated companies have of presenting themselves as though they were traditional law firms, with websites and advertising material branded with the panoply of wigs, gowns and quill pens.*"<sup>59</sup> This can result in consumers raising complaints with the Legal Ombudsman only to be turned away as their legal service provider is unregulated.<sup>60</sup>
- 3.15. We consider that this is a fundamental issue, particularly as it is something of which customers are often unaware. In this context, the key considerations are: (i) whether redress mechanisms exist in relation to

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<sup>56</sup> LSB, *The regulated communities' views on the cost of regulation* (2015), p.53. Available at

<https://research.legalservicesboard.org.uk/wp-content/media/Cost-of-Regulation-Survey-Report.pdf>

<sup>57</sup> Legal Services Consumer Panel (2015), Tracker Survey 2015 - data tables for recent users. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/documents/Tracker\\_Users\\_15\\_000.xlsx](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Tracker_Users_15_000.xlsx)

<sup>58</sup> See

[http://www.legalservicesboard.org.uk/what\\_we\\_do/consultations/open/pdf/will\\_writing\\_consultation\\_document\\_27\\_sep\\_12.pdf](http://www.legalservicesboard.org.uk/what_we_do/consultations/open/pdf/will_writing_consultation_document_27_sep_12.pdf)

<sup>59</sup> Written evidence from the Legal Ombudsman to the Justice Committee, September 2011. Available at

<http://www.publications.parliament.uk/pa/cm201213/cmselect/cmjust/97/97we04.htm>

<sup>60</sup> See the case study on this scenario provided in the Legal Ombudsman 2010-2011 Annual Report available at <http://www.legalombudsman.org.uk/downloads/documents/publications/Annual-Report-2010-11.pdf>

the provision of that legal service; (ii) whether customers are able to find out what these mechanisms are; and (iii) whether the mechanisms are effective in addressing customers' complaints. Questions addressing these points were posed in the 2016 TLS/LSB /LEF Legal Needs Survey, the results of which

### **Are redress mechanisms effective in addressing consumers' complaints?**

- 3.16. There are detailed requirements set out in the SRA Code of Conduct on the systems solicitors should have in place to handle any client complaint. Complainants can use the Legal Ombudsman service; an alternative to negligence claims where the amount of the claim is below £50,000. Services complaints which include an element of negligence can be made to the Ombudsman and will be considered; there is no costs risk for the complainant. The Ombudsman has considerable powers to resolve service complaints including ordering compensation, reducing the bill and making a firm apologise. Its approach is non-technical so there is no requirement for a complainant to be represented. If the complainant is unhappy with the outcome they can reject the Ombudsman's decision and take the matter to Court, although the trend for now seems to be to direct individual and micro-enterprise claimants towards alternative dispute resolution as opposed to going to the courts.
- 3.17. A stakeholder survey commissioned by the Legal Ombudsman in 2013 stated that: *"The majority of stakeholders believe that the Legal Ombudsman is improving access to redress, demonstrating fairness, contributing to improvements and building consumer confidence."*<sup>61</sup>
- 3.18. Complaints about misconduct cannot be dealt with by the Ombudsman but will be referred to the regulator. While there is no specific consumer redress through this route disciplinary actions taken by the SRA are published and in serious cases solicitors may be referred to the Solicitors Disciplinary Tribunal.
- 3.19. Consumer confidence in complaining about a lawyer is similar to other service providers such as accountants and mobile phone companies and only slightly lower than banks<sup>62</sup>. Awareness of the Ombudsman Service amongst consumers in the LSCP survey was 59% (higher for recent users of legal services at 64%). This is lower than awareness of the Financial Ombudsman Service (FOS) (77%<sup>63</sup>). When the Legal Ombudsman asked clients about where they had heard about the Ombudsman, 23% stated that it was through their lawyer. A slightly higher percentage of complainants referring a complaint to the FOS had heard about them through a financial business (30%). This indicates that this is an area where lawyers could do better and we are working with solicitors to improve signposting through our updated practice notes and risk and compliance service.
- 3.20. The fact that consumers of unregulated legal services do not have redress to the Legal Ombudsman (or the other redress mechanisms provided by solicitors set out above) renders it difficult to compare the

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<sup>61</sup> *Legal Ombudsman Stakeholder Survey* (March 2013), p. 2. Available at

<http://www.legalombudsman.org.uk/downloads/documents/publications/Legal-Ombudsman-Stakeholder-Survey-2013.pdf>

<sup>62</sup> Legal Services Consumer Panel (2014) *Tracker Briefing 2: Confidence and satisfaction*, p. 7. Available at [http://www.legalservicesconsumerpanel.org.uk/publications/research\\_and\\_reports/](http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/)

<sup>63</sup> Financial Ombudsman Services (2014) *Annual Review 2013/14* <http://www.financial-ombudsman.org.uk/publications/ar14/complained.html#a3>. The figure includes those who could name the Financial Ombudsman as well as those who may have heard of the service and definitely have heard of the service.

relative effectiveness of complaints handling between the regulated and unregulated sectors. The LSB has acknowledged this difficulty, and gives it as a reason for its forthcoming research project into unregulated providers.<sup>64</sup>

#### **4. Theme 3: Impact of regulations and the regulatory framework on competition**

- 4.1. A level of regulation is necessary for a well-functioning legal system. As we explained in our initial submission, regulation is required to protect the immediate consumers of legal services (that is those who purchase the service); to protect a wider group of consumers (who rely on the effectiveness of the legal system to underpin transactions, security of title and other rights and interests); and the wider public interest (for example in ensuring an efficient and fair system of dispute resolution). In seeking to balance the burden and cost imposed by regulation against the benefits it is important the CMA takes account of these wider externalities.
- 4.2. In order to provide a reserved activity a provider must be authorised by an approved regulator. For solicitors, non-reserved legal activities are also subject to regulation thus solicitors cannot offer those services without undergoing suitable education and training, complying with the SRA Handbook outcomes, contributing to the compensation fund, having PII cover in place and offering access to the Ombudsman. This means that there is a significant part of the market (all non-reserved activities) in which non-regulated providers compete with highly regulated providers. The latter will carry the costs of regulation and offer appropriate consumer protection (and contribute to wider externalities) the former will not. There is an element of free-riding by the unregulated sector in that, as explained above, many consumers believe that non-regulated providers are in fact regulated. Thus, non-regulated providers get some of the brand and reputational benefits from the regulatory system without paying for it and consumers are (unknown to them) unprotected.
- 4.3. The current regulatory regime therefore distorts competition, by imposing regulatory obligations selectively on certain legal service providers but not others, and giving misleading messages to consumers and the market.
- 4.4. This was explained in the 2009 Hunt Review of the Regulation of Legal Services:

*“This leads directly to the question of the extent of the regulatory “net”. I have been struck by the unanimity of view, across the profession and bodies representing consumers, in favour of giving serious consideration to extending legal regulation to other areas of activity where consumers currently enjoy no regulatory protection. I perceive a serious breach of both the public and the consumer interest in any area of activity that looks or “smells” like a reserved activity but is allowed to go unregulated. Most of our fellow*

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<sup>64</sup> See [http://www.legalservicesboard.org.uk/Projects/Unregulated\\_Legal\\_Services\\_Providers/index.htm](http://www.legalservicesboard.org.uk/Projects/Unregulated_Legal_Services_Providers/index.htm)

*citizens would surely be taken aback to learn that anyone can currently set himself or herself up as a will-writer and also that some aspects of probate activity can take place outside the regulatory "net".*<sup>65</sup>

- 4.5. The reserved activities relate to matters which require *ex-ante* regulation in the consumer and public interest. They are areas in which consumers find it hard to judge quality in advance of purchase (or sometimes after purchase) and in which there is a considerable public interest in ensuring that the relevant activity is conducted by a trained adviser who is subject to regulatory supervision and an effective compensation and complaints regime. We therefore believe that such activities should only be offered by properly authorised providers and see no basis for reducing the number of reserved activities.
- 4.6. Will writing is a "credence good", namely one whose quality cannot be ascertained by the consumer until some time after purchase, or indeed ever as the efficacy of the will may not be known until after the consumer's death. It is therefore essential for the protection of the client and the wider public interest in securing the proper administration of estates that will writers should be subject to appropriate training, insurance and redress obligations.
- 4.7. We believe that the broad scope of regulation of solicitors, as set out in the SRA Handbook, is correct in that it encompasses client and business conduct; accounting and client money requirements; authorisation and practice obligations (including education and training); client protection (including insurance and compensation and redress) and disciplinary matters. Although we would not necessarily agree with all the detail of current regulation in each of these areas or with the current regulatory structure (see below).
- 4.8. Because consumers are confused by a system that includes regulated and unregulated providers we believe that unregulated providers who offer legal advice outside of reserved activities should be subject to a minimum level of regulatory obligation to include at least access to the Ombudsman and indemnity insurance.
- 4.9. The SRA has recently changed the „separate business rule“ (**SBR**) which prohibited solicitors from owning or managing an unregulated legal services business, that is a solicitor could not separate reserved activities from non-reserved activities and operate the latter as if it were an unregulated provider. This distorted competition between solicitors firms and some ABS (such as accountancy firms) which were granted an exemption from the SBR by the SRA. The SBR now enables solicitors to own and manage a separate business though solicitors still cannot act as a solicitor in such a business<sup>66</sup>. The SRA has indicated that it will this year consult on further changes to allow solicitors to offer non-reserved activities in a separate business.<sup>67</sup>

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<sup>65</sup> *The Hunt Review of the Regulation of Legal Services* (2009), p.80. Available at [https://www.lsc.qld.gov.au/data/assets/pdf\\_file/0016/260035/The-Hunt-Review-of-the-Regulation-of-Legal-Services-NZ-Dec-2009.pdf](https://www.lsc.qld.gov.au/data/assets/pdf_file/0016/260035/The-Hunt-Review-of-the-Regulation-of-Legal-Services-NZ-Dec-2009.pdf)

<sup>66</sup> <http://www.sra.org.uk/solicitors/handbook/code/part5/rule12/content.page>

<sup>67</sup> <http://www.sra.org.uk/sra/policy/future/position-paper.page>

- 4.10. The SRA proposes to give non-regulated legal service providers who wish to offer some reserved activities the option to „opt-in“ to the regulatory regime. We consider this to be contrary to the public interest and liable to cause even more confusion to consumers. If certain activities require regulatory protection in the public interest it should not be left to the discretion of providers whether they offer that protection. Further, protection should be offered whether or not the provider also offers a reserved activity.
- 4.11. The role of the regulator is to regulate in the consumer and public interest. For reserved activities this may require the full gamut of *ex-ante* (authorisation and conduct standards), during the event (client money, insurance and compensation) and after the event (redress) regulation. For non-reserved activities the focus for all providers should be on after the event and (for some activities) during the event regulation. We see no basis for the regulator subjecting solicitors to a different burden to other providers in this regard.
- 4.12. We consider it important that solicitors abide by professional principles that can give an assurance of quality that come from holding the title of „solicitor“. It is for the professional bodies (The Law Society for solicitors, the Bar Council for barristers and other relevant bodies for other professionals) to set professional standards which may be the same as, or higher than, the minimum regulatory standards and would extend beyond reserved activities. This will also ensure that internationally the legal profession is seen to be independent.
- 4.13. Because of the scope for consumer confusion we consider that the title „lawyer“ should be protected in the same way as „solicitor“ and „barrister“ and reserved to professionals who have been authorised by a relevant professional body.
- 4.14. We consider that the multiplicity of regulators risks consumer confusion and there is no evidence that, as originally intended, having a number of frontline regulators has driven down costs. We believe that regulators of legal services should set the minimum regulatory rules and be responsible for independent regulatory enforcement against those minimum rules.
- 4.15. The hybrid approach that we describe, with the regulators setting the minimum standards required in consumer and public interest and the professional bodies dealing with professional principles associated with professional title, addresses the concern set out in our initial submission about independence of the profession from the state while ensuring that the consumer interest is protected by independent regulators. This would ensure that professional standards of entry are maintained and the international reputation of English and Welsh law and England and Wales as the jurisdiction of choice is protected.

**Do the current regulations create disproportionate barriers to entry and expansion into the legal services sector? What difficulties have new entrants faced?**

- 4.16. Most of the current regulations are necessary for the proper protection of consumers and wider interests. We are not aware of evidence to show linkage between lessening the cost of client protections and stimulating new entrants to the legal services market. Nor does the evidence suggest that reducing cost would lead to a greater number of consumers turning to a legal professional to resolve their legal problems.

- 4.17. Firms have to apply to be regulated via the SRA which assesses the suitability of the firm, for instance, whether they have systems in place to comply with SRA requirements and relevant experience. The SRA will also give some consideration to the viability of the business. This is not a matter all regulators would consider but is important because: (i) of the effect a sudden closure can have on clients; and (ii) over reliance on one client can make it difficult for a solicitor to maintain their independence.
- 4.18. Once regulated the firm will pay an annual fee based on number of lawyers and turnover.
- 4.19. There are barriers to exit for SRA regulated firms. Firms who have no successor have to purchase PII run off cover for the 6 years after they cease trading. This is to ensure that clients who wish to make a claim after a firms ceases will still be able to do so. They also need to make arrangements to repay all client monies and close their client bank accounts and store files. This is a particular difficulty for solicitors firms as they often store important client documents, such as wills, which cannot be destroyed for free. Where a firm is unable to organise the storage of files, for instance become it has become insolvent or been abandoned, the SRA will step in and store the files. The cost of intervening and sorting, archiving and storing files is borne by the profession.
- 4.20. Entry and exit rates over 2-3 years are around 10%, a little below average entry and exit rates across all UK businesses. This suggests that those wishing to enter the market are able to do so.<sup>68</sup> The Regulatory Policy Institute's 2013 report for the Society and the LSB regarding barriers to entry and exit highlighted that further barriers to entry, and particularly innovation, could be created by the SRA's focus on business models, finances and governance, concluding that: *"at a broad level, therefore, the market has shown itself capable of significant change" but that „regulation can be said to be impeding flexibility and innovation in business structures and business practices, in a number of ways”*.<sup>69</sup>

**Does the current regulatory framework impose disproportionate costs on legal services providers?**

- 4.21. As described above, a level of regulation is fundamentally necessary to a well-functioning legal system and proportionality should be considered in terms of consumer protection and the public interest as well as the burden placed on legal service providers. However, the regulatory framework for legal services – and so the costs imposed by this – are uneven. Unregulated providers bear far fewer costs than solicitors as they are not subject to the same regulation. For them, the regulatory framework is inadequate and they do not bear a proper share of the costs of regulating the system. For many solicitors, however, the costs of regulatory compliance are unnecessarily burdensome.
- 4.22. In 2015, the LSB conducted research with 16 solicitor firms on costs that they incurred solely to comply with legal services regulation (incremental costs). Those firms participating reported that the areas of regulation where incremental costs of regulation were highest were: PII, continuous professional

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<sup>68</sup> *Understanding barriers to entry, exit and merger, 2013*, Regulatory Policy Institute (George Yarrow and Chris Decker) for TLS and LSB.

<sup>69</sup> *Ibid.*

development (CPD) (the SRA last year reduced the formal CPD obligations on solicitors<sup>70</sup>) and information from the regulator. Other areas of regulatory costs identified included annual renewal and changes to regulation. On average, the entities reported that the total cost of regulation as a proportion of total practice costs was between 15% and 23%. Due to the small sample, the findings are qualitative and cannot be claimed to be necessarily representative of the cost of regulation felt by solicitors generally. For reliable data a significantly larger survey would have to be carried out.<sup>71</sup>

4.23. In recent years, following the Legal Services Act 2007, the regulatory costs and barriers relating to the management of risks by new firms have increased, with requirements for Compliance Officers for Legal Practice (COLP) and for Finance Administration (COFA) as well as the need to demonstrate risk management and sound business plans.

4.24. The detail of certain areas of regulation could be simplified in order to reduce waste. The impediments are more pronounced for small practices and non-traditional business models: some regulatory requirements involve a great deal of unnecessary duplication of effort, which raises costs in relation to start up merger and closure costs. As the Regulatory Policy Institute found,

*“A system that, in effect, leaves a large amount of work to be done by each of thousands of small businesses to work out what it is they have to do to comply with what appears to be a complex and not self-evidently coherent set of regulatory requirements, will tend to raise the costs of doing business. More significantly, it has the potential to divert non trivial amounts of the key resources of small practices (the time, attention and cognitive effort of the proprietors or partners) from other matters, such as the practice of law and the training of the next generation of lawyers”.*<sup>72</sup>

4.25. It has been suggested that premium levels might reduce if the compulsory PII Minimum Terms and Conditions were varied. But this would result in reduced protection for consumers. The LSB, in its decision not to grant the SRA's application for a reduction in minimum PII cover, stated that it *“did not consider that the argued countervailing benefits to this or the other objectives are sufficient or certain enough to justify an alternative decision”*. The LSB considered the SRA's reasoning, especially in relation to access to justice, and concluded that the evidence and analysis relied on by the SRA were insufficient to demonstrate a likely benefit.<sup>73</sup> Such a change could also result in an increase in premiums for solicitors who wished to continue to offer the current minimum conditions thus deterring them from doing so.

4.26. The contributions made by the profession to the Compensation Fund in 2015, as in the previous year, of £32 on a practising certificate and £548 on all entities that hold client money, appear good value for ensuring that consumers are protected from a practitioner's dishonesty, particularly when compared to the

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<sup>70</sup> <http://www.sra.org.uk/sra/news/press/sra-board-announces-new-approach-to-ensure-solicitors-remain-competent-page>

<sup>71</sup> Legal Services Board, *In-depth investigation into the costs of regulation in the market for legal services* (2015). Available at <https://research.legalservicesboard.org.uk/wp-content/media/In-depth-study-into-the-cost-of-regulation-version-2-for-publication.pdf> p24

<sup>72</sup> *Understanding barriers to entry, exit and merger*, 2013, Regulatory Policy Institute (George Yarrow and Chris Decker) for TLS and LSB, p. 3. Available at <file:///C:/Users/mmal/Downloads/RPI%20Report%20Summary%20and%20main%20conclusions%2010%20December%202013.pdf>

<sup>73</sup> *Ibid.*

cost of PII for cover against civil liability. The amount paid out by the Compensation Fund in respect of fraud is a tiny proportion compared to the huge amount held in solicitor client bank accounts at any given moment each day.

- 4.27. Some of the costs associated with regulation arise under a broader regulatory regime that is not specific to legal services, for example anti-money laundering legislation.<sup>74</sup> Other regulatory requirements, such as ensuring client confidentiality and conflict rules, reflect the common law. The 2015 Society Survey of solicitor firms' views of regulation attempted to quantify the overlap between SRA regulation and other regulation and legislation in a broad range of areas (for example equality and diversity, management, and confidentiality). The results show that, on average, approximately three-quarters of firms see at least some overlap (varying by area of compliance) and three in ten firms who see an overlap consider that SRA regulation reduces the "effort" of broader compliance.
- 4.28. Some costs that are presently mandatory under the regulatory regime would in any event be incurred by solicitors in the proper running of their business. An SRA survey indicated that 85% of firms reported that they would continue what they currently do to comply simply in order to run their firm well and look after clients' interests.<sup>75</sup> However, almost half of respondents thought that, given the size and nature of their business and their level of risk, the internal costs of compliance were excessive.
- 4.29. It should be noted that the benefits of legal services regulation, which generally do not accrue directly to legal services providers but to others in the economy, should be weighed against the costs to providers. Regulation generally benefits consumers of legal services and the economy in aggregate by promoting high quality legal work that supports the rule of law within the wider legal system. LSB's research in 2013 showed that consumers generally understood this, seeing the protections in place as striking a good balance and not wishing to see them removed.<sup>76</sup>

**What has been the impact of ABS entry on competition in the legal services sector, including on innovation, price and quality?**

**Are the rules governing ABSs unnecessarily restrictive such that they have hindered the entry and expansion of ABSs?**

**Have there been opportunities for more competition in particular legal service areas as a result of regulatory**

- 4.30. ABS are having some impact on competition in the legal services sector. This varies according to the area of legal work involved and the full impact is yet to be seen. Although more prominent in specific areas of practise, ABS constitute a small proportion of the wider legal services market: 451 SRA licensed ABS

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<sup>74</sup> Legal Services Board (2015) *The regulated communities' views on the cost of regulation*, p. 40. Available at <https://research.legalservicesboard.org.uk/wp-content/media/Cost-of-Regulation-Survey-Report.pdf>

<sup>75</sup> *Ibid* and SRA (2013) *Measuring the impact of Outcomes-focused Regulation (OFR) on firms* [www.sra.org.uk/impactofr/](http://www.sra.org.uk/impactofr/)

<sup>76</sup> *Risk and the role of regulation – Final report*, 2013, Vanilla research for the LSCP.

(January 2016) as against 10,306 solicitor firms (December 2015). About 5% of legal services are provided by ABS. Indeed, the 451 figure may not accurately represent the number of active ABS:

*'Based on the latest Law Society data extract, out of the 372 registered ABS, only 282 (approximately 75 per cent) appear to be operating as firms, which means that some 25 per cent of ABS registrations have been made, but either nothing has currently been done with them or they are operating as shell financing companies. (The SRA web site counts 405 registered ABS as at August 2015 – though again it is unlikely all of these are operational).'*<sup>77</sup>

- 4.31. Research conducted by the SRA in 2014 emphasised that it was too early to come to firm conclusions about the operation of ABS in the wider legal services market. The wide variety of ABS was cited as a barrier to drawing general conclusions: *"ABSs encompass a very wide range of different types of organisation, making it very difficult to draw generalisations about them as a distinct subset of the legal services sector. Some ABSs are very small firms, while others contain hundreds of partners and have turnovers in excess of £100 million."*<sup>78</sup>
- 4.32. ABS entrants include: (i) small law firms bringing in a partner who is not a lawyer (often relatives of lawyer-owners, managers or finance directors); (ii) traditional law firms wanting outside investors; (iii) in-house lawyers wishing to establish legal teams as ABS; and (iv) big external businesses. We understand that the largest group of ABS are medium and smaller general practice law firms, typically bringing in non-lawyer shareholders such as accountants, marketing directors, finance directors, or practice managers. Specialist practices make up the second largest group and some of the largest law firms and three of the top four accountancy firms in the UK have also established their own legal businesses.<sup>79</sup>
- 4.33. The first external entrants appeared to move into areas which are more commoditised such as personal injury and it is now estimated that almost 30% of the value of the personal injury market is accounted for by ABS.<sup>80</sup> There have been some high profile failures amongst this group. Recently, for instance, Saga Legal Services announced that it stopped taking on new business last year following the break-up of the Parabis Group (although it plans to take on new work in the future) only weeks after the AA withdrew from the market.<sup>81</sup> The Co-operative was also forced to make redundancies in its personal injury department and is now focussing more on its core family law practice.<sup>82</sup> It is noteworthy that the newest insurance company entering the market, LV, has chosen not to become an ABS and has instead partnered with a solicitors firm.
- 4.34. These failures may be explained by normal forces within a competitive market rather than ascribable to restrictive regulation. The Society's *Future Services* report predicts that by 2020 a growing number of new types of business model, often with a strong non-lawyer presence and with external investment, will exist

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<sup>77</sup> [The Future of Legal Services](#) (TLS, January 2015), p. 21.

<sup>78</sup> See <http://www.sra.org.uk/documents/SRA/research/abs-quantitative-research-may-2014.pdf> and <http://www.sra.org.uk/documents/SRA/research/abs-qualitative-research-may-2014.pdf>

<sup>79</sup> See YouGov *Legal Services 2015*, p. 65.

<sup>80</sup> *Ibid.*

<sup>81</sup> <http://www.lawgazette.co.uk/practice/saga-legal-admits-it-stopped-taking-new-work-last-year/5053373.fullarticle>

<sup>82</sup> <http://www.lawgazette.co.uk/practice/co-op-legal-heralds-turnaround-after-200k-half-year-profits/5050796.fullarticle>

and that 2020 should see ABS as a fully entrenched part of the profession and serious competition to smaller-medium Business to Consumer (**B2C**) firms<sup>83</sup> Indeed, some research contemplates the widespread financial failure of existing law firms as a result: the Association of Business Recovery Professionals, for instance, predicted in 2014 that 31% of all law firms were at risk of financial failure within the coming year.<sup>84</sup>

4.35. It is likely that the Business to Business (**B2B**) legal services market will also become more attractive for external investment through ABS because of:

- (a) increasing market size;
- (b) potential profit margins;
- (c) the fragmented nature of the market (the largest firm accounts for only 3% of the market);
- (d) increasing willingness of clients to disaggregate/unbundle legal services;
- (e) growing willingness of clients to substitute top law firms with lower-cost providers;
- (f) expanding opportunities to use technology and process re-engineering to increase efficiencies and standardisation of the delivery of legal services; and
- (g) top firms that appear to be willing to cede what they perceive as lower-margin work to other providers.

4.36. In their report *Innovation in UK legal service providers*, Roper, Love and Bourke suggest that the adoption of ABS status has a positive effect on innovation. All else being equal, ABS are 13-15% more likely to introduce new legal services and the authors infer „that the wider adoption of ABS status would be likely to increase the range of legal services on offer“.<sup>85</sup> This may be true if „introducing new services“ referred to new-to-the-market services rather than new-to-the-firm services but, whereas the report makes that distinction in some sections, this is not the case for the analysis of impacts of ABS. Furthermore, the underlying analysis did not identify causality from a firm becoming an ABS and the introduction of new, innovative, legal services. More generally, Roper et al found that innovation in the sector has not typically focused on lowering cost.

4.37. Some solicitors have envisaged significant problems arising in relation to conflicts of interest between firm senior management and shareholders. For retail markets, such conflicts might be in terms of which services a practice offers in order to return a decent profit – thus pushing some already vulnerable areas of law further out of reach for many. For business markets, conflicts between shareholders, firm and clients“ interests were potentially much more significant. The SRA considers that that there is no

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<sup>83</sup> *The Future of Legal Services* (TLS, January 2015), pp. 28 & 51.

<sup>84</sup> RBS, *A perspective on the legal market*, April 2014, p. 29.

<sup>85</sup> Roper, Love, Bourke, 2015, *Innovation in UK legal service providers*, SRA and LSB.

“additional risk” caused by the operation of a legal business through an ABS; a statement with which we agree.<sup>86</sup> Certainly the risk profile of an ABS will depend on a number of factors.

- 4.38. An example of ABS not entering a new market as had been expected is the Legal Services Commission’s (as it was) prediction in around 2001 that Community Legal Advice Centres (**CLACs**) and Community Legal Networks (**CLANs**) would be run by ABS (in collaboration with others) entering the market place. CLANs were intended to be networks of existing organisations. CLACS were new individual entities. Some of them were collaborations between existing advice organisations who, to a greater or lesser extent, maintained their separate identities. Two or three of them were set up by a solicitors’ firms in Sheffield in conjunction with A4E, but that focused on social welfare government contracts. By 2007, they were stalling, and by 2010 their presence was all but gone, finally being terminated in about 2012.

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<sup>86</sup> See the Society’s 2013 practice note available at <http://www.lawsociety.org.uk/support-services/advice/practice-notes/alternative-business-structures/>