

Research Specification: Understanding the economic rationale for legal services regulation

Purpose

The purpose of this research is to take a step back from the existing structure of regulation in legal services and consider the economic rationale for regulation of the legal services market and the legal services professions. In particular, the research should consider where regulation has welfare benefits (and/or its absence major welfare losses or threats) and why it may be rational for consumers of legal services, providers of legal services, regulators and the wider government and society to demand regulation of legal services. This research should set out clearly the intellectual case for regulation and where this case is strongest and where it is more problematic.

Background

The LSB has been set up to reform and modernise the legal services market in the interests of consumers, enhancing quality, ensuring value for money and improving access to justice across England and Wales. The LSB will achieve this pursuing its regulatory objectives¹ and providing regulatory oversight for the eight approved frontline regulators².

Existing regulation of legal services consists of a number of branches of the profession, some with reserved titles, other branches do not have reserved titles but are allowed to practice one or more of the six *reserved legal activities* set out in the Legal Services Act 2007:

- The exercise of a right of audience
- The conduct of litigation
- Reserved instrument activities
- Probate activities
- Notarial activities
- The administration of oaths.

Other reserved activities include immigration work (Immigration Act 1999) and claims management services (Compensation Act 2006). The reserved legal activities all have roots that are more than a hundred years old. They developed over time in a piecemeal way with little structured analysis as to their purpose or consistency between them. Key features of activities that are reserved are: they are exceptional or very irregular, often involuntary and for high personal civil or criminal stakes, often under time or other pressure. But there has been no attempt to develop an intellectual framework to analyse whether the right areas of legal services are regulated which prevents a reasoned analysis of the appropriateness of the existing reserved/non-reserved divide.

¹ http://www.opsi.gov.uk/acts/acts2007/ukpga_20070029_en_2#pt1

² The Law Society, General Council of the Bar, Council for Licensed Conveyancers, The Institute of Legal Executives, The Chartered Institute of Patent Attorneys, The Institute of Trade Mark Attorneys, Association of Law Costs Draftsmen, Master of the Faculties.

The current regulatory map is further complicated by the presence of the reserved titles for some (but not all) of the main branches of the legal profession. For example the titles 'solicitor' and 'barrister' are protected while others such as 'lawyer' and 'cost lawyer' are not. In effect any individual can set themselves up as a lawyer, but for example only an individual who pays their practicing fee to The Law Society can describe themselves as a solicitor.

While the reserved activities formally impose boundaries on the scope of regulation, in practice regulation reaches much further than these formal boundaries. For example, solicitors who make up the majority of the profession are subject to the regulatory rules for all activities, whether reserved or non-reserved. Three different factors interact with this rule to make most legal services subject to regulation (as the majority of legal services are provided by solicitors):

- For Solicitors and Barristers only members of the profession can own law firms, preventing an easy separation within a firm between regulated and unregulated activities involving solicitors and barristers (this may change - see Alternative Business Structures below)
- Solicitors have an extremely powerful professional brand that means for most consumers they are the first port of call for all legal advice
- A consumer, even a relatively informed one, may not necessarily know what legal services they need, so it may make sense for them to go to a firm that can carry out a variety of services, including reserved activities, when seeking legal advice.

The obvious argument for protection of title and/or service is consumer protection. Equally protections allow providers to restrict supply. For most consumers the impact is that the legal services they pay for are regulated beyond the intended reach of regulation set out in the various government acts

It is difficult to know precisely why competition between legal service providers has not led to more services being supplied outside of regulation. At present few consumers shop around between legal service providers. Most choose their legal service provider based on a recommendation, though acknowledge that they are unable to actually judge the quality of the service they receive³. In summary, consumers are not a strong pro-competitive force in the market leaving little competitive pressure on legal firms to adopt new business models.

Many legal services are supplied by individuals who are not part of the regulated profession, whether by para-legal firms, accountants, will-writers, insurers etc. But for the majority of individuals seeking formal legal advice they will turn to a regulated provider of legal services – whether the service they need is a reserved service or not. Potentially the introduction of Alternative Business Structures (removing restrictions on the ownership of legal firms) could lead to a significant change in the pattern of regulation over time. Equally changes in consumer demand and greater use of IT could change consumer demand for and supply of services facilitating major changes in the market and regulation.

³http://www.legalservicesboard.org.uk/what_we_do/Research/Publications/pdf/lspb_summary_of_yougov_research.pdf

The presence of areas of reserved activities and titles causes such challenges of regulatory boundaries in many sectors, including law. Some practitioners in areas of law such as will-writing would like greater regulation, while cost lawyers would like regulatory protection of title, although it is not clear whether the LSB could achieve this, even if it were minded, in any way other than be an extension of the scope of reserved activities. Understanding whether the current regulatory map matches actual regulatory need and where more or less regulation would be appropriate is an important area of policy interest for the LSB.

Aims and Objectives

The LSB would like to develop a proportionate approach to the regulation of legal services, ensuring that regulatory burdens are appropriate and unnecessary costs for consumers and providers of legal advice are minimised. We would like the author to take a step back from the existing regulatory framework – ignoring the current reserved activities and titles and consider instead the economic rationale for any regulation of the sector. The analysis should draw together argument and assessment of the likely externalities and market failures present in the legal services market and from this conclude where regulation is most likely to be required and where it is not.

The report should not attempt to evaluate the empirical evidence for the presence of externalities or market failures in any detail nor should it consider the alternative models for the regulation of legal services, or detail of particular regulatory instruments in depth. Later work from the LSB will look at consumers' desired outcomes and effectiveness of potential interventions. This study should focus primarily on providing a theoretical basis for analysis of the use of regulation in legal services.

We would hope that the report produced could mirror the type of analysis undertaken in the set-up phase of the Financial Services Authority in 1999 to provide a framework for the development of regulation within that sector⁴. In particular, the report should take a wide look at the provision of legal services, highlighting broadly the areas presenting concerns of market failures and noting particular areas of law where these concerns might arise.

Issues and scope

The challenge in looking at any market as broad as legal services is trying to draw meaningful conclusions without limiting their applicability to a small subset of the market. The report should draw together the analysis by concentrating on the key externalities and market failures, considering where features of legal services make these more likely to arise, why and in what form. It is likely to require primarily an activity based approach to the analysis with the more usual professions or service based approaches taking a lesser role. The author will need to draw together disparate types of law into common features and challenges for consumers. We would expect the author to agree the exact segmentation to be used with the LSB.

The research should also consider whether the types of externality or market failure vary by the type of legal services provider or client.

We expect the author to draw evidence for this report largely on existing academic studies – whether economic looking at market failure literature or from socio-economic studies of legal

⁴ <http://www.fsa.gov.uk/pubs/occpapers/OP01.pdf>

services. These should be pulled together into a framework for the analysis of regulation in legal services.

Tender Evaluation Criteria

All projects commissioned by the LSB are subject to our standard terms of contract. Tenders will be evaluated on best value for money and will be assessed on the basis of:

1. Overall cost. Please include appropriate breakdowns
2. The extent to which tenders are clearly written and meet the specified objectives, present a sound methodology, identifying any potential problems, and proposing suitable solutions
3. Address outputs and ensure these are in line with requirements and the required timing of the project
4. Proposed team composition, expertise and management and the organisation's diversity policy
5. How diversity issues would be addressed in the research.

Deliverables

Output

The output for this research should be an executive summary together with a report. The report should be suitable for publication, although any decision to publish will remain with the LSB. It is essential that the report and underlying research is sufficiently robust so that the LSB can use this in discussions with external stakeholders and can underpin the work of the LSB.

We would also like an interim short paper for discussion at a LSB Board Away Day on 7 September drawing together the key themes emerging from the study. The author may be asked to present the interim report at this session.

The LSB will retain ownership of the report.

Project plan

Tenders should include a project plan and time schedule for the work that identifies the main task and key milestones that will be used to monitor progress. The plan should be accompanied by a resource profile, giving a breakdown of the resources in person days allocated to each task.

Duration

The research should commence in July 2010. Tenders should set out dates for completing key milestones such as information gathering, analysis, synthesis and report writing. An initial interim short report must be submitted to the LSB by 30 August 2010, with the draft final report completed by the end of September 2010. A final agreed report should be completed by end October 2010.

Legal Services Board Contact Details

Tenders with any queries about the research specification should contact:

Policy team: Chris Handford 020 7271 0074

Research: Alex Roy 020 7271 0060

Tenders must be submitted by 5pm on Thursday 22 July 2010