

Measuring change in the legal services market – The Oxera segmentation framework summary

1. Background

This short paper is designed to introduce and simplify the segmentation framework published by the LSB last September. This is to support the application of this framework to the legal services market.

The segmentation framework was developed by Oxera and published in the report [A framework to monitor the legal services sector](#). This should be read alongside the LSB's [evaluation framework](#), and [interim baseline report](#) which draw heavily on the Oxera framework. The segmentation framework represents a theoretical approach to legal services segmentation, but requires a degree of tailoring in order to be applied on a practical basis.

Recognising that this is new territory for the legal services market, the paper begins with a section on why segmentation will be beneficial. This is followed by a section explaining the segmentation model. This is designed to demonstrate the value of using elements of economics to understand what's happening in the legal services market, beyond the reported perspectives of the regulated professions. The final section makes recommendations on additional reading and sources of information.

2. Why bother with market segmentation?

We often talk about the legal services market, yet rarely is it defined. If it isn't defined it is impossible to understand how it changes over time. If we don't understand how it changes over time we cannot impartially assess the delivery of the [regulatory objectives](#). Parliament has given the LSB and each of the Approved Regulators a statutory duty to promote these objectives. A segmentation framework supports this in the following ways:

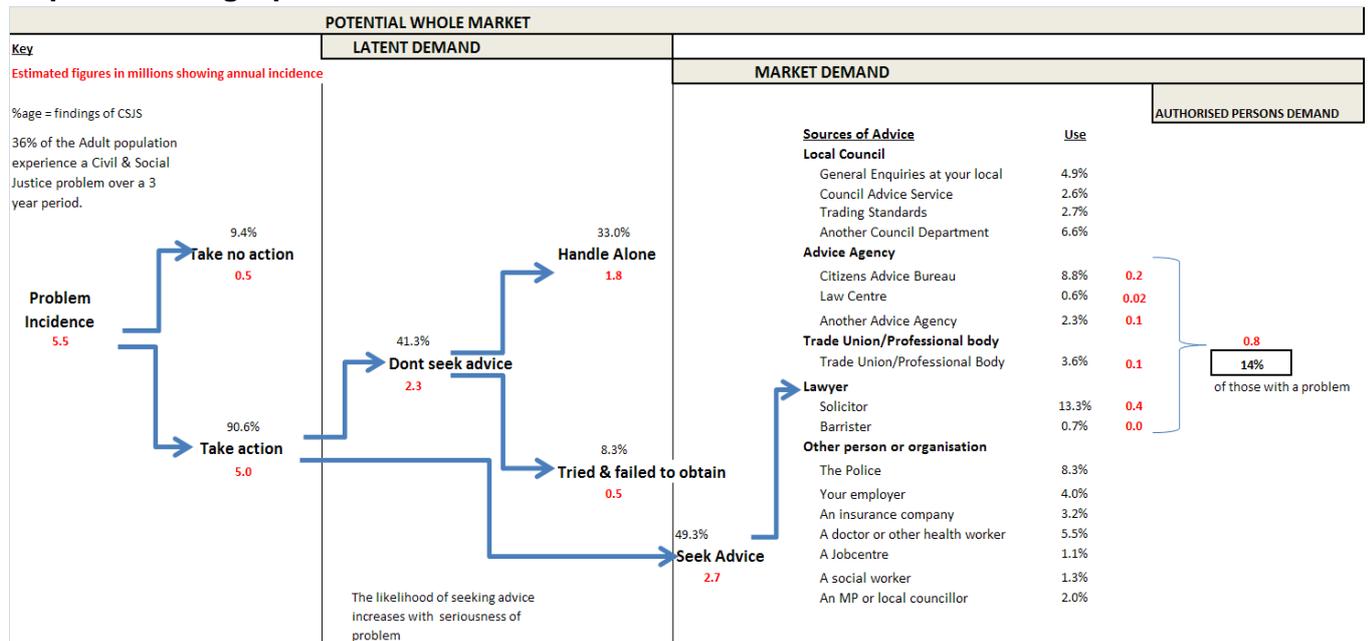
- **Economic definition of the legal services market:** By identifying the types of legal services and suppliers that consumers can switch between (i.e., demand-side substitution), and the circumstances in which suppliers are in competition with each other within a market (i.e. where either demand- or supply-side substitution occurs), legal service transactions can be grouped into different markets. Specifically:
 - **Demand side substitution-** Consumers have a number of alternative options available. Choices can be both consumer and issue specific, along the lines of whether to take legal action at all; whether to handle the problem alone or seek legal advice; and which legal service supplier to use. This is common terminology in legal need surveys for individuals, as is shown in Figure 1 below¹, and we would recognise the 'make or buy' decision in businesses and organisations. How changes in price change consumers' actions can be described as the elasticity of demand.
 - **Supply side substitution-** suppliers have a number of choices in the way they supply legal services. This can have two parts: First, suppliers can in

¹ Civil Justice in England and Wales - Report of the 2006-9 English and Welsh Civil and Social Justice Survey, Legal Services Research Centre, 2011

some instances switch between providing different legal services; while in other circumstances practical differences or real barriers can prevent suppliers from changing the services they offer. Often this switching in supply occurs as some types of services are more profitable than others, differences in profitability will be eroded over time as more suppliers move to the more profitable areas of work. Second, where there are few options available to the supplier, individual consumers may be able to drive a harder bargain with the supplier, reducing the cost of the service they pay. Areas of law where this may be relevant include criminal work and public law children cases. The relationship that explains how suppliers change their behaviour in response to changes in price is described as the elasticity of supply

Economic market definition, in contrast to a profession based definition, exposes the fact that different parts of the legal profession can compete with each other within the legal services market, enhancing our collective understanding of the legal services market beyond professional boundaries. For example, 2 out of every 5 individuals advising clients in solicitors firms, are not solicitors. More integrated working between professions and other legal advisers is a likely impact of the Legal Services Act 2007 reforms, the most obvious example being Legal Disciplinary Practices.

Figure 1. Demand side substitution in practice - Civil and Social Justice Survey and responses to legal problems



- Targeting of regulatory protection for consumers:** Different types of consumers are exposed to different types of risks (often described as market failures) when interacting with legal services. Examples of specific market failures include:
 - Asymmetric information** - the consumer may be less able than the supplier to judge the quality of the services provided. This can limit their ability to evaluate whether the service offers is right for their needs, at a fair price and at a sufficient level of quality.

- **Imperfect information** - often there is a more general uncertainty about the type of service required. This arises since for many legal services the full benefits take time to materialise and therefore depend on currently unknown events.
- **Consumer switching and search costs** - it may be costly for a consumer to gather the required information to choose effectively between different legal services and providers such that when infrequent purchases are expected choice is not well informed. Once a provider is chosen it may be costly to change provider mid service.

Put simply, an individual purchasing a one off legal service can be considered to be in a very different situation when compared to a larger business that has an in house solicitor and purchases legal services on an ongoing basis. Therefore regulatory protection should be adapted accordingly.

- **Assessing impacts of specific elements of regulation:** The point of the segmentation framework is to both allow the regulatory community to assess the impacts of regulatory reform, and target regulation to ensure that it is proportionate. The process of market segmentation identifies what information is desired and where gaps lie. Over time as evidence is gathered and different segments better understood, the segmentation model will provide a collective knowledge base, enabling objective assessment of different elements of regulation.
- **Consistent data collection and terminology:** To monitor changes in the legal services sector, it is crucial that the way in which data is collected and analysed remains consistent over time. Otherwise, it would become difficult to determine whether observed changes in the data reflect real market developments, or simply adjustments to the data reporting and/or analysis methodology. At present, there is no industry standard segmentation, and none of the prevailing segmentations identified in our Regulatory Information Review has remained stable over time. Annex 1 of the Oxera report maps existing classification systems to the Oxera segmentation framework.

3. What does the segmentation framework look like?

To provide a practical approach to market segmentation, the framework uses easily observable characteristics, in order to capture what might cause the legal service market to function in a different way. These are:

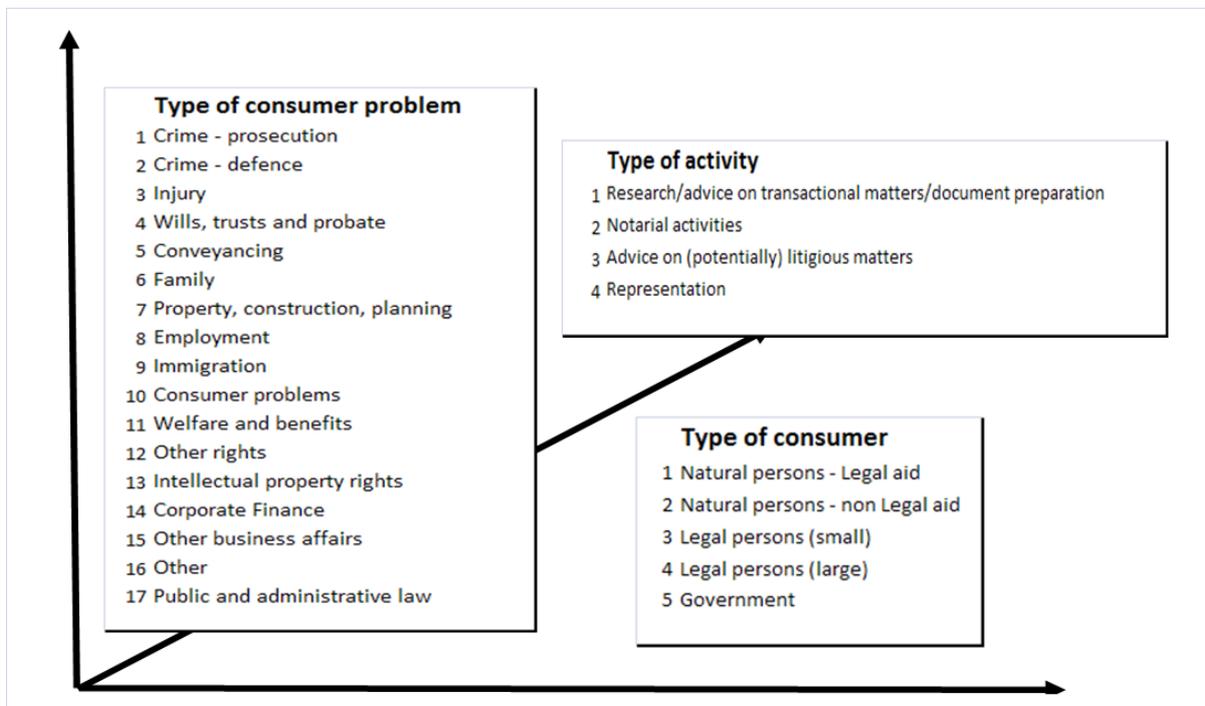
- a. **Type of consumer**— consumer-specific characteristics may alter the supplier - consumer relationship, and different consumers may require advice on different issues, even within a particular area of law.
- b. **Type of consumer problem**—there is a multitude of problems on which legal advice might be sought. Since consumers cannot alter the nature of these problems, there is limited substitutability between suppliers or services. Without the ability to switch between suppliers or services, differences in market outcomes can persist, since consumers cannot switch to the service with the characteristics they prefer. Thus, providers of different services do not need to compete. For example, advice in relation to a divorce proceeding is not a substitute for property conveyancing services. Therefore, the ideal market segmentation would split between each possible type of consumer problem on which legal advice might be sought.

- c. **Type of legal activity**—the type of legal service provided can be seen as an additional relevant distinction since this limits the extent to which suppliers can supply different legal services. For example, the market for basic advice will function differently to the market for advocacy, due to the regulatory barrier controlling who can provide advocacy services at higher courts.

While information on the type of supplier is important – termed supply side segmentation – no single supply side segmentation captures the range of different groups of suppliers competing in each market.

These three segmentation dimensions are shown in figure 2 below. These represent Level 1 segmentation. Each dimension has a two more levels to allow for further sub segmentation where necessary. These sub-segments are designed to be used only where a specific policy need arises, due to the cost of acquiring data. For example any regulation to make advice a reserved activity will only affect the unreserved sector. These sub segments are explained below.

Figure 2. The segmentation dimensions



The framework identifies five different types of consumer groups, on the basis of risks of market failure. These are labelled from a legal perspective. These are shown in the Figure 3 below:

Figure 3. The type of consumer

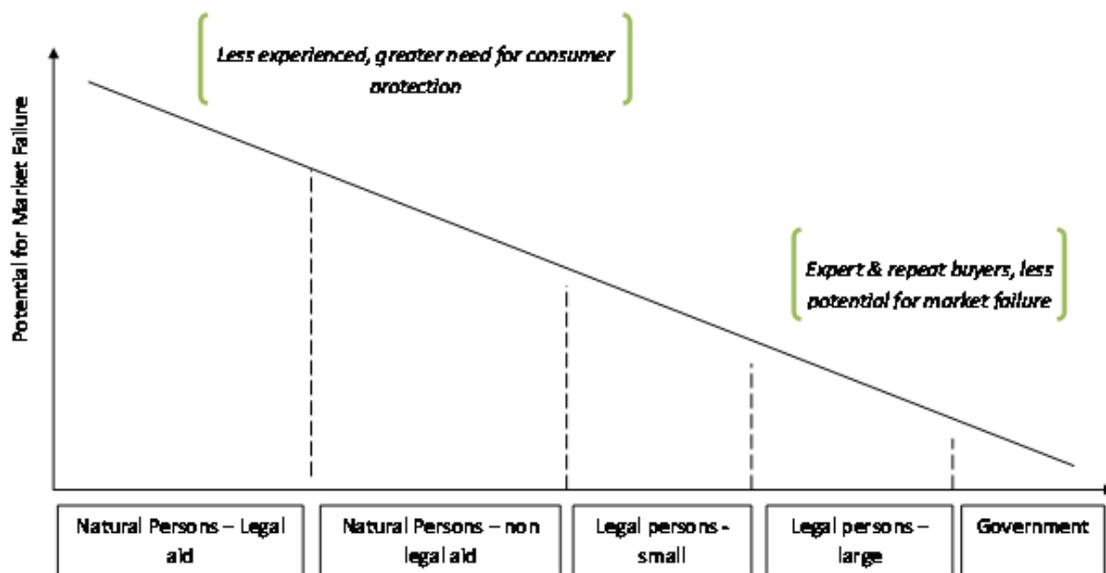
Type of consumer – Level 1	Translates to:	Group definition	Levels 2 & 3
Natural persons - Legal aid	Legal aid consumers	Individuals funded by legal aid, or accessing free at point of delivery legal services	Socio-demographic stats on consumers
Natural	Private	Individual buying legal services for	

persons - non Legal aid Legal persons (small) – less sophisticated Legal persons (large) – more sophisticated	consumers	themselves	
	SMEs and charities	An organisation with less than 250 employees, and no in-house legal team.	Type of organisation by for profit or not for profit, and size measured by number of employees and turnover.
	Large business and government	An organisation with 250 or more employees, or an In house legal team. Where the buyer is a government body, but the issue is also encountered by other private organisations, the appropriate classification of consumer type is legal persons (eg, the government purchasing legal advice in relation to employment contracts).	
Government	Government sole purchaser	Only applicable where the government body is the sole purchaser—eg, for advice in relation to rule-making. This is relevant within areas of public law, crime and issues regarding welfare, benefits and civil liberties.	Type of government – central, local, quasi.

When collecting information from barristers, this dimension refers to the end-consumer rather than the solicitor who may be contracting directly with the barrister on behalf of a diverse range of clients. How the work has been acquired, perhaps via solicitor referral or direct contact from the end-consumer via public access rights, is a key indicator to monitor overtime.

It is assumed that consumers’ frequency of use of legal services is key to understanding levels of confidence and empowerment. Consumers can be segmented on this basis, as set out in Figure 4 below.

Figure 4. Consumers of legal services segmented by experience



The assumption is that because the private consumer – the natural person - use legal services less frequently than other groups, having greater search costs and switching costs, they are therefore less empowered at present. This is supported by a range of research findings showing for private consumers *‘there was a poor understanding of what is involved in the provision of legal services, and the expertise required. This meant that participants found it difficult to make any valid comparison between two alternative services providers, as a) they did not know what skills/experience to look for in a legal services provider and b) they did not know how to go about finding out what their skills and experience were.’*² This is further supported by the prevalence of personal recommendations in individual consumer’s choice of provider. Put succinctly: *“The episodic nature of law-related problems is a key factor. Although law-related issues are commonplace they occur periodically, often around key life events that are separated in time. As a result most people, most of the time, don’t feel they need to think about the law. Instead they wait until a problem occurs and then try to acquire the knowledge needed to deal with it”*³

With regard to the type of consumer problem, the segmentation framework identifies 17 different types at Level 1. Each Level 1 category is broken-down Level 2 and Level 3 sub segments. Level 2 sub segmentation is down on the basis of whether the problem is contentious or not. By its very nature criminal law is contentious – proving or defending the guilt of an individual or a company. In other areas of law where there are a range of contentious and non contentious aspects, suppliers may specialise in either contentious or non-contentious issues such as property and planning, and some suppliers provide advice on non-contentious matters only.

For Level 3, each of the level 1 categories of consumer problem is broken down into different sub segments. One of the key challenges in developing the framework was to come up with a range of problem categories that allowed existing classifications, such as those used by the Law Society, or the Civil & Social Justice survey, to be mapped across. The Oxera report provides this mapping in Annex 1. These are summarised in Figure 5 below.

Because different types of consumers have different types of legal problem and different types of solution, the third segmentation dimension relates to the type of legal activity. This is set out in Figure 6 below, and relates to the framework set out in the Legal Services Act 2007 (LSA). Regulatory barriers drive specialism by supplier in some form – historically true for barristers and claims management companies for example. In other incidence this might be driven by the type of business model the firm adopts for example providing only basic advice across a wide range of services to avoid employing any authorised persons.

In addition, different types of legal activity are purchased in a different way, which can have a significant effect on the market. In particular, the majority of advocacy for individuals is often chosen by the solicitor, who acts as the consumers agent.

² Consumers attitudes to the purchase of legal services, GfK, Solicitors Regulation Authority 2010 <http://www.sra.org.uk/sra/how-we-work/consumer-research/consumer-research.page>

³ Legal Capability, Martin Jones, Plenet 2010

Figure 5. The type of consumer problem

Level 1	Level 2	Level 3
Crime—prosecution	Contentious	Range of criminal offences
Crime—defence	Contentious	
Injury	Contentious	Road traffic accidents, Injury at work, Clinical negligence
Wills, trusts and probate	Contentious	Contested probate
	Non-contentious	Wills, Trusts, Probate & estate administration
Conveyancing	Non-contentious	Commercial, residential
Family	Contentious	Children (eg, care proceedings), Matrimonial
	Non-contentious	Children (eg, adoption)
Property, construction and planning	Contentious	Landlord & tenant problems, Repossession, Squatters, Boundaries & rights of way, Planning
	Non-contentious	Landlord and tenant Other reasons for drawing up contracts, Property finance, Property leasing ,Planning applications
Employment (excluding injury at work)	Contentious	Pensions, Unfair dismissal, Redundancy
	Non-contentious	Pensions Establishing and maintaining contracts
Immigration and nationality	Contentious	Immigration and asylum
	Non-contentious	National insurance details, visa applications
Consumer problems	Contentious	Sale of goods and services, Hire purchase etc
Welfare and benefits	Contentious	Community care, Education, Benefits, Mental health
	Non-contentious	Applications for benefits
Civil liberties	Contentious	Human rights, Actions against the police, Discrimination (excluding employment), Other rights including specialist areas such as rights to life
Intellectual property rights	Contentious	Patents, Trademarks, Copyright, Confidentiality, IT
	Non-contentious	
Corporate taxation	Contentious	Indirect taxation, Property taxation, International taxation
	Non-contentious	
Corporate structuring and finance	Non-contentious	Mergers and acquisitions, Joint ventures, Public takeovers, Privatisations, Issuance of securities, Corporate insolvency
Other business affairs	Contentious	Infringement of contracts, Competition, Environmental
	Non-contentious	Procurement, Licensing, Business registration

Other Other public and administrative law	Contentious	Libel and defamation, Compensation arising from fraud, Debt management (debtor), Debt collection
	Non-contentious	judicial review, public inquiries
	Contentious	

Figure 6. The type of activity

Level 1	Level 2	Description
Research, advice on transactional matters and document preparation	Unreserved	Unreserved transactional legal services
	Reserved	Reserved activities as defined by the LSA
Notarial activities	Reserved	Notarial activities as defined by the LSA
Advice on (potentially) litigious matters and work required to prepare such advice	Unreserved	legal advice for a party to proceedings or for a person who is contemplating taking proceedings
	Reserved	Reserved activity of litigation as defined in the LSA
Representation (in person)	Unreserved	Representation in lower courts, arbitration, and mediation
	Reserved	reserved activity of advocacy as defined in the LSA

Putting these elements together, Figure 7 below provides a pictorial representation of the segmentation framework in its entirety at Level 1. The shaded areas are the segments where there is no consumer demand for services. This might be because of the nature of funding – for example legal aid doesn't fund conveyancing or notarial activities – or the nature of the law itself – for example family law does not apply to large businesses.

These three characteristics form the basis of data collection and market insight. A law firm is grouped for analysis with other law firms providing the same services for the same types of client; they can then be differentiated in such a group by more traditional data – numbers employed, turnover, etc. The market is defined by the features of competition within the market rather than simply the traditional legal structure of a legal firm.

The challenge is to understand the legal service market without imposing large information collection burdens - a cost for businesses that may be passed onto consumers. That means maximising the value of each existing information exchange and of the wide range of publically available information.

To be clear, neither the segmentation framework nor the LSB advocate the wholesale collection of information solely for market evaluation purposes. However, the LSB continues to push all of the regulatory community to be more evidenced based. The need to use evidence to inform design of regulatory arrangements, risk profiling of all aspects of market, and targeted supervision means that regulators are developing an evidence base to support the delivery of our shared regulatory objectives. It is a central part of Outcomes Focused Regulation. Further by better sharing and more publication of information, combined with

greater competition, the expectation is that the collective knowledge base will enhance overtime.

Figure 7. Segmentation framework – Level 1 perspective

Type of Consumer	Legal aid consumers			Private consumers			SMEs and charities			Large busines & Government			Government sole purchaser			
	Research	Notarial activities	Advice	Representation	Research	Notarial activities	Advice	Representation	Research	Notarial activities	Advice	Representation	Research	Notarial activities	Advice	Representation
Type of Activity																
Type of consumer problem																
Crime - prosecution																
Crime - defence																
Injury																
Wills, trusts and probate																
Conveyancing																
Family																
Property, construction, planning																
Employment																
Immigration																
Consumer problems																
Welfare and benefits																
Other rights & civil liberties																
Intellectual property rights																
Corporate Finance																
Other business affairs																
Other																
Public & admin. law																

The LSB's [interim baseline report](#) is an example of analysis using elements of the segmentation framework and a wide range of pre existing publically available information to understand the legal services market over the past five years. Annex 2 of the [Oxera report](#) provides a list of indicators metrics and data sources to consider when applying this framework. These are grouped into 4 areas, with a range of indicators applicable to each

In terms of developing our understanding of the legal services market, being able to baseline and monitor change at Level 1 is considered to be the most realistic aim, given the level of knowledge gaps in this sector. However in assessing the impact of regulatory changes it is recognised that individual pieces of research may provide insight into individual market sub-segments. We will seek to build a complete market picture over the coming years in conjunction with Approved Regulators and other stakeholders.

4. Applying the segmentation model – Example of Conveyancing

The LSB has started to utilise the Oxera segmentation model in its work. One published example is in the Immigration discussion paper⁴, published in March of this year. This section provides an example application to another consumer problem type – Conveyancing. In this example we look at how the market is functioning using the appropriate indicators set out in Annex 2 of the Oxera report.

The starting point is to isolate the relevant segments for the areas under consideration, and using Figures 3,5, and 6 above, we can see that the relevant segment for conveyancing is made up of the following sub segments:

Figure 8. Segmentation framework – conveyancing

The type of consumer problem	Conveyancing:	Residential	Commercial
	The type of consumer	Private consumers	- SMEs and charities - Large business and government
	The type of activity	Research, advice on transactional matters and document preparation.	Research, advice on transactional matters and document preparation.

The Oxera framework provides three elements to Market Functioning Indicators. These are:

- A. **Elasticity of Supply** - The rate at which supply changes in response to changes in prices
- B. **Elasticity of Demand** - The rate at which demand changes in response to changes in prices

⁴ See pages 21-24 Regulation of immigration advice and services – a discussion document for consultation: March 2012

http://www.legalservicesboard.org.uk/what_we_do/consultations/open/pdf/20120301_immigration_discussi_on_doc_1_1_final.pdf

- C. **Consumer understanding** - influenced by the level of information available in the market, and therefore providers' customer acquisition techniques (direct advertising compared to referrals for example).

In relation to each element Annex 2 puts forward a arrange of indicators – areas to consider when looking at how the market is working. A summary analysis of these indicators is set out below, based on published information and forthcoming LSB research into individual consumers⁵.

A. Elasticity of Supply

Regulation is a barrier to providing conveyancing services.

As a reserved activity only authorised persons can conduct these activities, regulated by the SRA, the CLC and the Master of the Faculties. For farm businesses only, Fellows of the Central Association of Agricultural Valuers, or a Member or Fellow of the Royal Institution of Chartered Surveyors can undertake conveyancing transactions.

Each regulator has its own set of required qualifications. For solicitors this requires a degree, a legal practice course, and a two year training contract, reflecting solicitors ability to offer a wide range of services. For licensed conveyancers this requires passing a series of examinations then supervised practical training of 1,200 hours over a 12 month period.

It is believed that the dominant customer acquisition channels in this area are referral via an estate agent or via mortgage lender, personal recommendation, and price comparison sites. How open these are to new entrants is unclear. Research in 2010 found that 81% of estate agents reported that they had a panel of solicitors/conveyancers to whom they referred customers, and that membership of these panels was largely stable. This research found that 42% of estate agents observed an increase in the use of national conveyancers while only 26% observed a decline in the use of national conveyancers

In terms of regulatory costs individual registration costs for the three approved regulators were very similar in 2011: SRA £328 - CLC £400 - MoF £380. Regulators costs are seen as low in the context of estimated price of conveyancing transactions of between £500-£1000. However voluntary accreditation schemes add to operating costs. For example the Law Society Conveyancing Quality Scheme cost between £420-£2,340 to join depending on firm size, with 1,400 member firms as at May 2012. These schemes can provide access to mortgage lender panels.

The number of firms withdrawing from or starting to provide conveyancing services overtime is not known, but the number of business providing these services appears to broadly static overall. For notaries, the Society of Notaries estimated that a maximum of 28 out of 845 (3%) notaries undertook some conveyancing in 2011. For CLC entities, as at mid 2011 the number had increased to 217 from a low of 185 in 2009. For SRA entities, in 2010 5,640 firms reported turnover in conveyancing, 4% of these just in commercial conveyancing and 15% just in residential. 25% of these firms reported having referral arrangements.

Research in 2007 found that approximately 95% of the whole market for conveyancing - residential and commercial - is accounted for by solicitors, with licensed conveyancers

⁵ Legal Services Benchmarking for individual consumers, BDRC Continental, LSB. To be published July 2012

accounting for the remaining 5%. Overall using Land Registry data, in 2010/11, 25% of conveyancing registrations were undertaken by 2.5% (208) organisations, compared to 2006/07, 25% of conveyancing registrations were undertaken by 3.5% (314) organisations. The average number of conveyances per organisation was 149 in 2006/07 compared to 84 in 2010/11.

While CLC entities and notaries can offer probate and notarial services, they can also offer other non reserved legal services. To what extent this occurs is unknown. For SRA entities, 2010 regulatory information shows a wide range of other legal services being provided by the same entities – 97% of these firms derive up to 49% of their income from other categories of law. It is not know how this has changed over time.

B. Elasticity of Demand

The focus here is on individual consumers in relation to residential property transaction. This is because of the lack of information in relation to other types of consumers.

Research into individual consumers experience of legal needs shows that conveyancing represents 11% of all legal needs. Over two thirds of these were actual transactions of buying and selling a house.

For buying or selling a house research shows that 68% individual consumers use a solicitor compared to 14% using licensed conveyancers. For remortgaging these figures are 62% and 12 % respectively.

In nearly 30% of cases the chosen provider was recommended by a friend or relative or they had been used before. In remortgaging cases 22% were contacted by the provider (presumably through the mortgage company) – this proactive approach only happened in 8% of conveyancing transactions.

Prices vary by the type of conveyancing transaction. The average fee charged for a remortgage was just under £800 and for a buying or selling it was nearly £1200. Solicitors fees are on average more expensive than licensed conveyancer (£1,300 versus £785). Consumers reported using a licensed conveyancer to keep costs down, and the cost of the service was a major factor for 52% of consumers when considering a provider. The same research suggests that 15% of consumers tried to negotiate the price of the conveyancing and approximately three quarters cases were successful in reducing fees

As a whole, this suggests a relatively high degree of shopping around by consumers in conveyancing, and active decision making around which provider to choose in a significant proportion of all cases.

Research into individual consumers shows that 17% of consumers who bought or sold a house or remortgaged in the past 3 years also purchased other legal services. These other services included tax advice, will writing, and other types of legal services.

C. Consumer Understanding

Closely linked to considerations of elasticity of demand, levels of consumer understanding are mixed. Research shows that a small minority of consumers actually

understand the differences between a licensed conveyancer and a solicitor, but where they do decision are made on the basis of price with consumers seeing licensed conveyancers as cheaper. In these incidences prices are not linked to quality.

A proportion of consumers handle the conveyancing transaction themselves. Research shows that remortgaging is less likely to involve using legal services providers, with a higher proportion of consumers using a financial adviser and non legal service providers, or undertaking the work themselves.

This information is designed to highlight regulatory risk, providing the context against which issues such as increasing rates of mortgage fraud can be considered. How the market is currently functioning might highlight areas of consumer detriment and result into different regulatory response in the conveyancing segment, compared to other segments. By understanding the market regulation can be better targeted at the relevant risks.

5. Further information

This short paper is designed to provide an introduction to this framework. Further information can be found in the research publications section of the LSB website.

For further information please contact the Research project manager, Robert Cross (robert.cross@legalservicesboard.org.uk).