Legal Services Market Study: Response from Cambridge Economic Policy Associates and Suzanne Rab

Introduction

The CMA's Statement of Scope invited responses from interested parties on its proposed market study into the supply of legal services in England and Wales.

Cambridge Economic Policy Associates is an economic and financial policy consulting business; as well as focusing on traditional regulated industries such as energy and transport, we are also now active in financial regulation, where many of the issues (for example, the power conferred on incumbents through the control of 'rule-books') mirror those in legal services.

Suzanne Rab is an independent barrister at Serle Court Chambers specialising in competition law and regulation and who has wide experience of advising businesses and regulators on professional services regulation.

We are making this response from our joint multi-disciplinary perspectives, combining economics, policy and law. Our interests in making this response are with a view to informing the CMA's understanding and assessment of the relevant market and the impact of regulation and the regulatory framework on competition. The views expressed here are those of Cambridge Economic Policy Associates and the personal views of Suzanne Rab and do not necessarily represent those of our clients or any other affiliated organisation.

The themes suggested for investigation

We consider that the summary of recent developments in 2.12 provides a good summary of the main issues of interest to a competition authority such as the CMA. However, we are concerned that the themes suggested for investigation in Section 3 may not adequately capture these issues.

One reason for this could be the focus in Section 3 on information issues. While asymmetries of information are one feature of legal services markets, other characteristics also need to be looked at.

So, for example Theme 1 currently focuses on 'informed purchasing decisions'. We think it would be better to have a wider focus on 'unmet needs and quality of service issues', which directly picks up the first two issues highlighted in 2.12. Work on this theme would then focus on exploring how widespread these issues were, and whether specific features of current market, institutional and regulatory arrangements hindered the development of a market solution. This could involve:

- Understanding which categories of consumer have unmet needs, and for which services

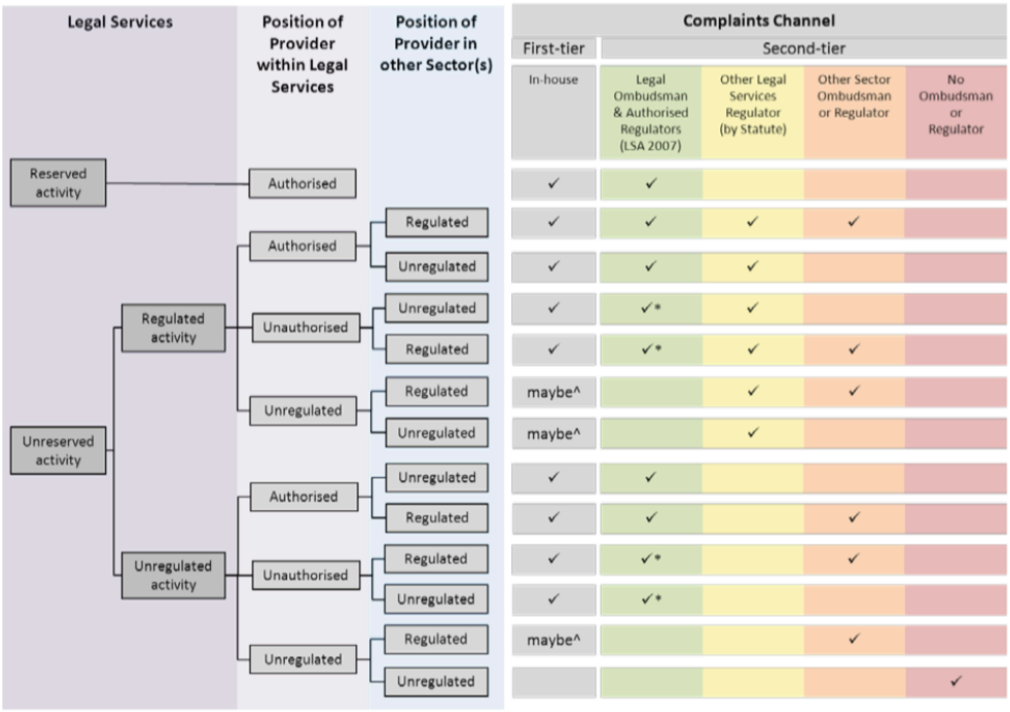
- Whether the needs are unmet because consumers do not seek out a legal service provider for those needs; whether there are barriers to them identifying a suitable provider; or whether a suitable provider exists at all
- If there are no suitable providers, is this because the service required could not be supplied at a reasonable profit? If so, are regulatory compliance costs an important barrier to profitable provision?
- Identifying indicative volumes and values for such services
- Consumers' perceptions and experience of quality and how these act as drivers of choice, including the role of professional titles, marketing, personal experience and referrals in influencing purchasing decisions
- Identifying how the potential barriers to provision could be removed.

Such barriers could have arisen from unintended consequences of the current regulatory arrangements, which may involve high compliance costs that are disproportionate to the risks of consumer detriment – a subject that we return to below.

Similarly we think it right that Theme 2 should focus on issues of effective consumer redress, but we are not convinced that this is simply a result of 'a lack of information or a lack of confidence on the part of consumers' (3.25). As the Report for the OFT on Regulatory Restrictions in the Legal Profession shows[1], the complexity of the regulatory structures for legal services makes it costly and difficult for a consumer to determine how to obtain redress. To illustrate the point, we show below one of the diagrams from the report that maps complaints channel by service type (note the 'maybe' references in particular):

[1] See - http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.oft.gov.uk/shared_oft/reports/professional_bodies/OFT1460.pdf ; and note the comment on p.70: 'Jurisdictional overlaps between redress mechanisms and the existence of unregulated individuals/activities can 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.'

Figure 3.3: Complaints channels mapping by service type



If the CMA's work confirms that the complexity of customer redress is indeed an important issue, there are various potential remedies that could be examined.

One approach would be to harmonise redress within one central organisation with common rules on jurisdiction, time limits, procedures and powers. This would be a long term and ambitious project, but its feasibility and associated costs and benefits merit consideration. An alternative, shorter term approach to reduce this complexity is to request one organisation, such as the Legal Ombudsman, to provide a 'post box' service.[2] These alternatives (one radical, one evolutionary and incremental) illustrate a theme we return to below – the need to consider the best approach to improving legal services regulation.

We appreciate that redress is an area that has been examined in other contexts. However, if the market is to evolve in the way that Clementi envisaged it is important that the consumer has confidence in the market and the quality of services provided. It would seem therefore that the issue of redress – where by definition the consumer is not satisfied with the service they have received – is an all-pervasive issue for the CMA's study.

Evolution of the regulatory framework

Both Theme 2 and Theme 3 touch on the impact of regulations and the regulatory framework. Again, however, the focus is on barriers to entry and disproportionate costs. We think a better emphasis would be on how the regulatory structure should evolve to improve its effectiveness and reduce the

[2] Some initial work has already been done on this option in the report detailed above.

costs it imposes – in short, to ask whether there are are not 'more effective ways of doing things.'[3]

As the CMA notes, views on how to achieve this differ. At one extreme, the Legal Services Board (LSB) envisages a radical approach:

> 'the real goal of reduced, but more effective, regulation could be most securely built on a new paradigm, rather than within the existing framework or through incremental changes to it.'[4]

By contrast, the Regulatory Policy Institute: warns against the dangers of 'tearing up' the existing rule books and starting again:

> 'Change can be difficult to manage, and can be a burden to organisations. Regulatory change is no different in this respect, and one of the most consistent findings of Regulatory Policy Institute work over the years, across all sectors of the economy and including multiple projects for the Cabinet Office and BIS, is that it is most often change in regulations, rather than the overall level of regulation, that, on close analysis, tends to be what imposes the largest regulatory burdens, particularly on small firms.'[5]

These are quite different views, and we think it would aid the evolution of effective competition in legal services if this study, or a subsequent market investigation, examined the scale of the economic detriment caused by any inappropriate regulation and came to a view as to whether such detriment was best dealt with through a radical re-writing of the rules or a more evolutionary approach. If the latter is confirmed as the more appropriate course, a market investigation could also indicate which areas would give the most 'bang per buck' in terms of reducing economic detriment. And it is of course possible that radical change is needed in some areas, whereas a more evolutionary approach would work better elsewhere.

Some of the areas that we consider could benefit from this 'cost-benefit' approach would include:

- The distinction between "reserved" and "non-reserved" legal services. While it may ultimately be a matter for government to determine which services need to be regulated in the sense that a provider may not engage in them without authorisation, useful work could be done by the CMA in examining the continuing relevance of the distinction in the current market context and its impact on the effective functioning of the legal services market.

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[3] See 'Understanding the economic rationale for legal services regulation' by Chris Decker and George Yarrow, available at www.legalservicesboard.org.uk

[4] LSB (September 2013) A blueprint for reforming legal services provision – p11.

[5] See the RPI's response to the MoJ's review of legal services regulation – available at http://www.rpieurope.org/Publications/2013/RPI_response_to_MoJ_review_legal_services_regulation_GY.pdf

- The scope of the regulatory net where once a provider is engaged in a reserved activity they are also regulated for all other activities they carry out, even if unreserved. This has the consequence that a provider that is regulated by one approved regulator such as the SRA for, say, probate activities is regulated by the SRA for other (unreserved) activities such as employment law advice or will writing. Yet a provider that is not subject to regulation for a reserved activity would not be regulated for the provision of such unreserved activities.
- The role of the LSB itself as an oversight regulator which approves changes to regulation proposed by the frontline regulators to the extent that they meet the relevant regulatory objectives including promoting competition, yet is limited in terms of the changes that it can itself drive. This may limit the scope for deregulatory measures.

The CMA seems the body best equipped to undertake such a review. While we note that H M Treasury is intending to launch a consultation on removing barriers to entry for alternative business structures and on making legal service regulators independent from their representative bodies, the CMA's scope can be much wider, and the outcomes should be less subject to political lobbying.

Case studies

The CMA intends to carry out a limited number of case studies to examine certain themes and issues (will writing and probate services to individual consumers; employment law services to individuals and small businesses and commercial law services).

On the level of methodology, it was not clear to us whether such case studies would involve consumer or provider surveys and how they would relate to any existing studies conducted by the LSB or other regulators.

We note that these studies largely relate to unreserved activities. If the distinction between reserved and unreserved activities is to be examined thoroughly a useful area of inquiry could be in relation to the conduct of litigation to the extent this is not captured within employment/commercial law services.

As to the scope of the case study on commercial law, such a study could usefully include intellectual property services as well as trading issues as proposed. Such services are important to small businesses, particularly start-ups who want to protect their IPR. IP services are also an area where there is a range of providers including solicitors, patent attorneys, trade mark attorneys and unregulated.

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