

Liberalisation of Legal Services in Europe: Progress and Prospects

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The usual excuse for regulation is the failure of market provision. This paper examines legal services and suggests that in the case of provision of commercial legal services to corporate clients, true events of market failure, to support the case for regulation, and more particularly self-regulation, are hard to locate. It further argues that the market for legal services is heavily stratified with a commercial legal services market effectively operating quite separately to that of professional legal services for private clients. In consequence, it may be more effective and proportionate to adopt differentiated strategies of regulation. This might be achieved by shifting the focus of regulation away from the individual practitioner, as is historically the case, towards law firms as such. This simple step, it is suggested, could facilitate much greater liberalisation of the market for legal services. This proposal is explored with particular reference to freedom of services within the European single market and, as a backdrop to the paper, progress to date in facilitating cross border legal services in Europe is reviewed.

INTRODUCTION

Market liberalisation has greatly enhanced the free flow of goods and services across national borders. Such services include legal services, though the legal sector is not merely the subject of liberalisation but is an important actor in achieving and ensuring cross border economic activity. Globalisation of legal services reflects the desire of law firms to follow corporate clients as they pursue

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the economic advantages of global markets. Legal services have been key in creating the conditions for economic globalisation and not merely by supporting the commercial cross border activity of clients but also in creating the structures of the global markets through programmes of privatisation and foreign direct investment. In such areas experience of re-structuring the legal fabric of economic infrastructure was often gained in one country before that experience was re-utilised in another country. The ability of lawyers to provide services outside the jurisdiction in which they were originally located can be said to amount to a necessary pre-condition of wider economic globalisation.

The European Union has been built on the idea of market liberalisation to the point of creating a single market in goods and services straddling a large number of nation states. This paper examines the functioning of that European market with regard to the provision of legal services questioning the extent to which that market enables 'seamless'¹ multi-jurisdictional practice. 'Seamless' here reflects the desire of law firms represented in more than one jurisdiction to offer a level of service standards to clients that is indistinguishable by reference to location. Consequently the issue here is not whether cross-border legal practice is currently realisable within the EU; it clearly is. The issue is whether conditions exist to facilitate an efficient platform for multi-jurisdictional legal practice.

There is an existing and reasonably extensive literature emanating from Law and Bar Societies, the European Commission and academic and professional commentators, both lawyers and economists. This literature engages largely with three concerns, which this paper will mirror: (1) the historical and current position of the internal EU legal market in controlling the delivery of professional legal services and the generic barriers to cross border practice; (2) the private and public interests served by regulation and how these might most appropriately be safeguarded; and (3) because, as this suggests, few commentators would dispense entirely with regulation, the appropriate balance of regulatory activity. Following a review of this literature it is argued that

¹ The word seamless is one widely adopted by law firms themselves as may be indicated by using a search engine to find material on "seamless legal service" – as to why such a standard might be important to them see Le Goff P, 'Global Law: A Legal Phenomenon Emerging from the Process of Globalisation' (2007) 14(1) *Indiana Journal of Global Legal Studies* 119 – 145.

professional conduct rules do act as an inhibitor to the provision of legal services across borders, not least because of what is described below as 'double deontology' facing law firms with conflicting conduct rules in neighbouring jurisdictions.

Broadly, the paper suggests that many of the events of market failure that support the case for regulation, and more particularly self-regulation, of legal services look particularly weak when applied to the position of multinational commercial clients rather than other consumers of legal services. Moreover, because the market for legal services is heavily stratified so that the commercial legal services market is effectively a separate market, it may be more effective and proportionate to adopt differentiated strategies of regulation. The paper argues therefore the focus of regulation ought to be law firms rather than individual practitioners, as is historically the case, and that this simple step could prove a significant one in allowing greater liberalisation of the market for legal services.

PRESENT PROVISION FOR CROSS BORDER LEGAL SERVICES IN THE EUROPEAN SINGLE MARKET

Commentators on the current structure of the EU legal market largely view the regulatory system within the EU in positive light as it is viewed as highly liberalised.² This is said to follow from the 1998³ Establishment Directive⁴ and the 2005 Recognition of Qualifications Directive⁵ and from the lead of the

² For a comparative perspective see: Worth S.M., *The Transnational Practice of Law: Staggering Growth in spite of Economic and Regulatory Barriers to Entry*, (2003-04) 7 *Gonzaga Journal of International Law*: <http://www.gonzagajil.org/content/view/96/26/>

³ An earlier Legal Services Directive, 77/249/EC sought to facilitate cross-border legal services but somewhat narrowly defined and with a limited list of the types of lawyers to which it applied. A second Directive, 89/48/EC, allowing mutual recognition of professional qualifications, applied equally to lawyers but is now less significant in this sphere because of Directive 98/5/EC. These are explored below.

⁴ Directive 98/5/EC of the European Parliament and of the Council of 16 February 1998 to facilitate practice of the profession of lawyer on a permanent basis in a Member State other than that in which the qualification was obtained; hereafter the Establishment Directive.

⁵ See Directive 2005/36/EC of the European Parliament and of the Council on the recognition of professional qualifications replacing Council Directives 89/48/EEC and 92/51/EEC as well as Directive 1999/42/EC on the general system for the recognition of

European Court of Justice (ECJ) in pursuing a bold approach to the interpretation of Articles 44-47 of the EC Treaty. The Establishment Directive, which is explained fully below, has been described as '*an absolutely fundamental and revolutionary achievement in the realization of a single market for lawyers*'⁶ and it is said that '*a combination of legislation and case law has steadily expanded interstate legal practice rights, making the multistate practice of law a reality throughout the EU*'.⁷ Such comments reflect a broad commendation for the EU's attempts at liberalisation and for the progress made in comparison to other non-EU jurisdictions. However, the pace of regulatory change must be judged also against the highly dynamic shifts in cross border commerce. Assessed on this basis it is possible to argue that attempts to liberalise lag behind the ambitions of lawyers to follow corporate clients and provide cross border legal services.

Moreover, while forces of globalisation have driven a more liberalised legal market within Europe,⁸ one must be cautious with comparisons. As Vagts points out⁹ it is not unusual for lawyers in the USA to be admitted in two or more States, but on the whole this would not be taken as a sign of success when compared with the opening up of practice rights across the very different jurisdictions in the European market.¹⁰ In addition, there may be a difference in constructing the mechanisms of cross border practice and ensuring that

professional qualifications together with a host of Directives covering particular occupations.

⁶ Gromek-Broc, K., 'The Legal Profession in the European Union – A Comparative Analysis Of Four Member States' (2002) 24 *Liverpool Law Review* 109–130.

⁷ Quinn, J.P., 'The Right to Practice Law in the European Union: An American Perspective' 2004 [2004] 1 *Macquarie Business Law Journal* 113 -130.

⁸ See Thomas R.S., Schwab S.J. and Hansen R.G., "Megafirms" (2001) 80 *North Carolina Law Review* 115 at 151 who state that: "the driving force behind these international mergers (of law firms in Europe) is the increased demand by clients for legal services on a global basis".

⁹ Vagts D.F., "Professional Responsibility in Transborder Practice: Conflict and Resolution" (2000) 13(4) *Georgetown Journal of Legal Ethics*, 677 – 698.

¹⁰ Since the early 1990s by virtue of Directive 1989/48, any lawyer qualified in the EU could seek to re-establish in any other EU country, in line with Article 52 of the Treaty and principles of freedom of establishment, and to re-qualify as a local lawyer assisted by the system of mutual recognition of diplomas. However, linguistic barriers and differences in the underpinning legal system may make this more problematic than (say) between states in the USA.

professional rules in Member States also facilitate the liberalising goals of such mechanisms.¹¹

There are terminological difficulties in discussing the provision of legal services across Member States of the European Union. Although we are talking generally of the liberalisation of legal services, freedom of services in EU law denotes a somewhat limited right, which contrasts with the right of establishment. Whereas freedom of services concerns the right to offer services across national boundaries, this falls short of the establishment of a firm in another Member State in order to undertake work there. Service provision therefore implies distance or temporary provision falling short of permanent establishment. The situation is further confused because, while in most cases the freedoms of services or establishment are likely to be pursued by firms seeking to exploit business opportunity, licensing of legal services invariably attaches to the individual practitioner. Therefore the issue is the extent to which recognition is afforded to lawyers seeking to provide legal services outside their home jurisdiction or, in the terms employed in EU law, whether the lawyers' existing qualifications can be accorded recognition without a requirement to entirely re-qualify in a second jurisdiction. It is the assumption that any such recognition by one state would be accorded reciprocity by other states – hence the term of 'mutual recognition'. The development of a concept of mutual recognition followed initial attempts to facilitate freedom of services but pre-dated wider establishment rights. Indeed the chronological order of European Directives, beginning with provision of legal services, then mutual recognition and finally rights to establish, reflects the widening of cross border rights from limited provision through services to better recognition of legal qualifications and reaching as far as the right to establish. We can explore these measures in turn.

The Services Directive¹², dating back to the mid 1970s, followed an important ruling of the European Court of Justice that (what is now) Article 43 of the EC Treaty on non discrimination on grounds of nationality had direct effect and

¹¹ Gromek-Broc acknowledges in her article that there are further reforms that could be undertaken to extend cross border practice in the EU; however she suggests that the remaining challenges lie within the ambit of nation states, rather than at EU level.

¹² Council Directive 77/249/EEC of 22 March 1977 to facilitate the effective exercise by lawyers of freedom to provide services, hereafter the Services Directive. not to be confused with Directive 2006/123/EC of 12 December 2006 on services in the internal market, which is referred to below.

could apply to the advantage of a Dutch national prohibited from practising as an advocate in the Belgian courts on the grounds that he did not have Belgian nationality.¹³ The Directive contrasts services with establishment, the two being mutually exclusive for the purposes of the Directive. It also contrasts legal representation before the courts or public tribunals with other types of legal services. Both are covered by the Directive but the former are subject to Host State rules of professional conduct, whereas the latter remain subject to the applicable conduct rules of the Home State but "without prejudice to respect for the rules, whatever their source, which govern the profession in the host Member State."¹⁴

By subjecting lawyers providing cross border services to both Home and Host State controls the Directive raises the spectre of what has become known as 'double deontology'. As liberalisation of professional services continues apace, problems of double deontology assume much larger proportions as divisions arising out of the degree of professional restriction become more marked. This is well illustrated by the following passage from the Parliamentary Joint Committee on the UK Legal Services Bill considering the introduction of business structures for law firms which might include non-lawyers:

'We were particularly concerned by the written evidence we received from the Bundesrechtsanwaltskammer (the German Federal Bar which is set up in statute as the self-regulatory body of the German legal profession). They told us of "certain obstacles which Alternative Business Structures would encounter in Germany". They told us that ABS firms which had shareholders from outside the profession and whose management would not necessarily be in the hands of a majority of lawyers would be "inconsistent with the requirements of German law". They are of the opinion that "German *Rechtsanwälte* as well as solicitors and barristers established in Germany would infringe German professional rules if they became a member of such type of an ABS.'

The disbarment of law firm partners qualified in Germany on account of the structure lawfully adopted by their partners qualified in England seems the most extreme consequence of double deontology. Most examples will be more prosaic. However, in Kantian ethics, no universal deontology exists so that it is perfectly possible for deontological rules, about what is considered good or bad, to vary –

¹³ *Jean Reyners v State of Belgium* Case 2/74 [1974] ECR 631.

¹⁴ See Article 4 of the Services Directive.

in our case from State to State.¹⁵ Double deontology implies a simultaneous obligation to two sets of rules, both intending an ethical outcome, which might even conflict with each other. In areas such as conflicts of interest, client confidentiality and legal privilege it is perfectly plausible that the line between the private (client facing) and public (court based) duties of the lawyer have been drawn at different points. Indeed these differences may be expected to some degree in European legal systems that reflect both common law-based, adversarial and Roman law, inquisitorial traditions.¹⁶

There is a mechanism for the resolution of problems of double deontology in Article 7 of the Services Directive. It begins with the right of the Host State to demand proof of a lawyer's credentials. In the event of non-compliance with a professional conduct rule within the Host State, the competent authority of that State is able to determine in accordance with its own rules and procedures the regulatory consequences. However, the Directive allows that in order to do so that authority may obtain 'appropriate professional information' concerning the lawyer providing services and should notify the competent authority of the lawyer's Home State of any decision taken. This is a procedure that has 'rarely, if ever, been used'.¹⁷ One can speculate on why this may be so. Doubtless lawyers have been careful to reconcile competing professional demands and have strong internal control systems¹⁸ but professional bodies also may have had no great relish for seeking to reconcile the irreconcilable.

The Mutual Recognition of Diplomas Directive¹⁹ sought to facilitate the transfer of a legal practitioner from one Member State to another without the need for the

¹⁵ Nagel M.T., 'Double Deontology and the CCBE: Harmonizing the Double Trouble in Europe' (2007) 6 *Washington University Global Studies Law Review* 455 – 481.

¹⁶ Ibid at p.461; see also Hellwig H-J 'The Legal Profession in Europe: Achievements, Challenges and Chances' (2003) 4(3) *German Law Journal* 263 – 276.

¹⁷ Goldsmith J, Cross Border Practice in the EU, Paper given at ABA International Law and Practice Section Conference on *Regulation of Cross-Border Legal Practice* held in Brussels, October 17, 2003, and available at:

<http://www.abanet.org/intlaw/hubs/programs/Fall0311.01-11.04.pdf>

¹⁸ Etherington L and Lee R (2007) 'Ethical Codes and Cultural Context: Ensuring Legal Ethics in the Global Law Firm' 14(1) *Indiana Journal of Global Legal Studies* 95 – 118.

¹⁹ Council Directive 89/48/EEC of 21 December 1988 on a general system for the recognition of higher-education diplomas awarded on completion of professional education and training of at least three years' duration, hereafter the Mutual Recognition of Diplomas Directive; Directive 2005/36/EC has now consolidated, into a single text, this and two other Directives on the general system for the recognition of professional qualifications, together with a host of other sectoral Directives. However these do not

lawyer to completely re-qualify in that second Member State.²⁰ The primary mechanism to achieve this was an aptitude test restricted to the testing of only the features which could be said to be different to those of the lawyer's Home State or otherwise unique. This carries an implicit assumption that notwithstanding different backgrounds and length of education, the operating standards of legal practitioners in the European market are broadly similar. While this might seem doubtful, the experience in England and Wales suggests otherwise. It does seem to be the case that there have been no great difficulties in assimilating foreign lawyers into the English profession, which has historically run a Qualified Lawyers Transfer Test (QLTT) which is liberal in its administration and extends far beyond European jurisdictions in welcoming lawyers into the English Legal System.²¹ The QLTT remains as a route of transfer but is less commonly used by lawyers in Member States of the EU because of the more liberal approach of the Establishment Directive²².

Adopted in 1998 and taking effect in most Member States by 2000, the Establishment Directive facilitates the movement of lawyers by allowing them to practise law "on a permanent basis in a Member State other than that in which the qualification was obtained." This right to practise requires no more than registration in the Host State. Directive 1998/5 enables a lawyer qualified within one EU Member State to practise in another Member State as a registered foreign lawyer, a term that indicates the need for registration with the competent authorities of the Host Member State.²³ The authorization given is to practise under the professional title of the home-country; however, after an uninterrupted period of three years in the Host State the lawyer can seek admission in that State without the requirement to prove aptitude through any

include services and establishment directives applicable to lawyers since they concern the recognition not of professional qualifications but of the authorisation to practise.

²⁰ It may be that a Member State would in any case be obligated to take into account a lawyer's knowledge and experience and evaluate this as against national requirements for entry in order to fulfil obligations on free movement in accordance with the Treaty: *Irene Vlassopoulou v Ministerium für Justiz Bundes-und Europaan-gelegenheiten Baden Wurttemberg* (C-340/89) [1991] ECR 2357.

²¹ In the years 1995 to 2005 16% of solicitors admitted in England and Wales had first qualified in some other jurisdiction – see Solicitors Regulation Authority, Requirements for Lawyers Qualifying as Solicitors in England and Wales (SRA, 2008).

²² *Supra* n.4.

²³ A process that may vary in length and complexity depending upon the member state in question – see Guermontprez Y., 'Conquering the Continent' (2003) *The Trainee* (May) 28 – 29.

form of test.²⁴ This does depend on the lawyer in question providing legal services involving the law of the Host State.²⁵ It follows that registered lawyers must be permitted to practise in the manner of other host country lawyers in order to be able to gain admission rights and fall under the disciplinary mechanisms of the host regulator. Equally if, as is likely, the lawyers wish only to advise only on their own Home State law in order to serve clients based in the Host State, then admission will not be a possibility without undertaking the required test of aptitude. In general terms, however, registration provides a simple mechanism for re-qualification and hence establishment.

The Establishment Directive offered the opportunity to re-visit the problem of double deontology some 20 years after grappling with this issue in the Services Directive. Again, a Host State formulation is favoured since Article 6 says that whatever the practice rules of the Home State a registered foreign lawyer:

“shall be subject to the same rules of professional conduct as lawyers practising under the relevant professional title of the host Member State in respect of all the activities he pursues in its territory.”

In the event of a foreign lawyer offending those Host State rules:

“the rules of procedure, penalties and remedies provided for in the host Member State shall apply.”

As law firms have lawyers working alongside each other on the same or similar transactions but subject to different codes, an increasingly large number of dual qualified lawyers face confusion as to which code might be appropriate to follow, knowing that there may be disciplinary consequences attaching to a wrong choice.²⁶ Precisely which code will apply will depend upon the circumstances in which legal services are offered. Important questions here include: whether the legal services are actually of a cross border nature (rather than e.g. the provision of domestic law advice to an overseas' client); whether the work is

²⁴ Article 10 of the Directive.

²⁵ Though this may include EC law.

²⁶ A good example is that of fees in litigation with conditional fees supported in England and Wales and levied in the event of success, as are 'honoraire' premiums for success in France and 'palmario' for successful representation in Italy whereas other jurisdictions would frown upon success fees – see Maurer V., Thomas R.E., and DeBooth P.A., 'Attorney Fee Arrangements: The US and Western European Perspectives' (1998) 19 *Northwestern Journal of International Law and Business* 272-329.

contentious or non contentious; whether it constitutes the temporary provision of services outside the Home State; or whether the lawyer is more permanently established in the jurisdiction in question. This also means that the professional status of the lawyer undertaking the work is crucial. Finally note the vulnerability of the lawyer here, particularly perhaps under the Establishment Directive under which problems of double jeopardy²⁷ may arise. Whatever action the Host State authority applies during disciplinary procedures, the Home State authority has the right to audit those procedures and take independent action. If this results in revocation of the lawyer's home licence, then this will effectively put an end to any right to practise in the Host State, irrespective of the outcome of disciplinary proceedings there. In spite of such difficulties, the opportunities to practise law across borders have been vigorously pursued and the following section examines the patterns of such activity.

THE EXTENT OF CROSS BORDER LEGAL PRACTICE

Before attempting to assess the extent to which these cross border possibilities have been exploited in the market for legal services, it is worth dwelling on why a law firm might wish to be represented in more than one jurisdiction. One reason might be that the firm is in any case offering services that are only loosely connected to a single jurisdiction. A good example of such global legal services might be work supporting the capital markets where representation in chosen financial centres is beneficial to the law firm even though the content of the legal work is unrelated to the law of the jurisdiction in which the financial centre is located. This contrasts with work undertaken to support cross border trade. Here the law firm may wish to be represented in a State in which its client undertakes a high level of business. In such an instance, there is more chance of the firm needing to engage with local law, though even this is not certain as contracts may have choice of law clauses and the law firm's brief may be limited to certain types of legal work. It may well be possible to offer this type of service without directly locating in another jurisdiction through partnering with local law firms. Although some firms have maintained this type of approach, this is hardly

²⁷ Lonbay J 'Legal Ethics and Professional Responsibility in a Global Context' (2005) 4 *Washington University Global Studies Law Review* 609 - 616

the dominant model.²⁸ Rather it is one which law firms tend to pursue at early stages of international work since it requires relatively little capital outlay, but once a clear market for cross border services is established, the firm begins to contemplate the possibility of opening up foreign offices.

Silver has tried to capture patterns of global growth in her analysis of four ideal types of internationalization: domestic; international; multinational; and transnational.²⁹ In this typification, purely domestic law firms may become international, perhaps as a facet of size through simple steps such as advising foreign clients on the domestic law which they practise. This might even include the opening of an office outside of the jurisdiction to provide advice based upon the knowledge of their domestic law. This international step can lead to the next category, multi-national status, perhaps by the simple process of opening offices in yet more jurisdictions. However, as the network grows so too do the managerial tasks of training and co-ordinating the lawyers in the many offices. An alternative model is that of the transnational law firm which Silver defines as multiple nationally based groups of lawyers specializing in their own national law systems. This is famously the Baker and McKenzie model. Because these models are ideal types, there will be variants of them and the models may be adapted to suit the work types, with some of the larger firms manifesting both multinational and transnational traits.

Silver's analysis may depict a history which itself has changed alongside greater globalisation to the point at which the distinctions are less meaningful than before. The fact is that lawyers serving multinational corporations will find that they have invested strongly in global brands. Their activity is now international in its character. Such corporations will wish to work to a global template with as little change as necessary in order to be compliant with local law. Even where work is domestic, rather than international per se, such as a property transaction to establish a presence in a particular State, the corporate client will want to standardise the transaction in so far as it is possible to do so. The best

²⁸ But Slaughter and May in the English market have historically pursued this approach with great success – see Chambers M and Rose C, 'Slaughter and May's International Strategy' (November/December 1997) *Commercial Lawyer* 20.

²⁹ Silver, C., 'Regulatory Mismatch in the International Market for Legal Services' (2003) 23 *Northwestern Journal of International Law and Business* 487-550

means of accessing this standardised legal product may be a chosen law firm with a presence in the major markets.

In an important paper,³⁰ the economist Frank Stephen has explored the significance of opportunities for trans-border legal services' provision in the production of yet greater market liberalisation. Like all great insights the one offered in the paper is somewhat obvious on reflection. Markets which remain relatively closed are likely to offer greater rents and prove attractive to those able to exploit rights to cross border practice. There will be costs attaching to establishment in these markets but those both best placed and with the greatest incentive to enter will be firms from relatively open markets. As the prices in the closed market will be higher, it is likely that the cost base will be higher also while shielded from competition. But firms from more competitive markets have already learnt to innovate to drive down the unit cost of legal services through process re-engineering.³¹ Firms from the more closed jurisdictions will have little incentive to exploit cross border rights to enter the more open jurisdictions and face yet greater competition. However, the shift of firms from more open to more closed jurisdictions will increase "efficiency and social welfare in an inefficient jurisdiction even if the practice rules and fees in the inefficient jurisdiction remain unchanged."³²

Stephen's paper also considers the likely mode of service provision from one jurisdiction to the other. Provision of the type envisaged by the Services Directive, namely the cross border export of the home based service is thought unlikely to fully penetrate the opportunities of the relatively closed market. In order to exploit the advantages of process re-engineering in which the firm has invested it will wish to actually enter the market. This it could do by way of foreign direct investment in, say, an office in the target jurisdiction, but merger with an existing firm is thought to be the most credible form of entry since it guarantees access to both the market knowledge and reputation available to the

³⁰ Stephen F.H., 'The European Single Market and the Regulation of the Legal Profession: An Economic Analysis' (2002) 23 *Managerial and decision Economics* 115 – 125.

³¹ Stephen uses the term 'technology' while making it clear that he is concerned nonetheless with human capital; the idea of process re-engineering perhaps better captures how legal services can be commodified under forces of competition to realise efficiency gains.

³² Stephen (op.cit. n 30) at p. 118

firm in the target jurisdiction and the process efficiencies generated by the would-be market entrant. The overall effect of the transfer of more efficient working structures is said to be pressure for the liberalisation of both fees and practices in the less efficient jurisdiction over time. In this way the opening up of markets begets yet more market openness.

Although Stephen's paper has no empirical base as such, he does claim that this type of analysis helps explain the strong interest of English law firms in the German market.³³ Clearly the opportunities offered by the liberalising mechanisms discussed above have led to an increasingly cosmopolitan European market for legal services. Stephen's analysis does not really account for the lesser degree of activity in markets like Germany of law firms from say Scandinavia which is generally taken to exhibit a high degree of liberalisation in the legal services sector. An analysis of the highly liberalised legal services markets in Denmark, Finland and Sweden shows a preference for a model of association with other foreign firms rather than establishment abroad. This is true for the top ten Danish firms³⁴ none of which has overseas' offices. In Finland the top 4 firms have over 70 fee earners whose capacity to complete cross border commercial transactions is described as 'outstanding'.³⁵ The market in Finland is widely regarded as being saturated and as a result its largest firms have looked at opportunities abroad though the modest size of most practices in Finland obviously acts as a restraint. Sweden has a strong legal services market with a large international presence and domestic firms of considerable fee earner strength – the top 2 both having over 260 fee earners. Yet, as with the Danish firms, there is not much expansion overseas directly, the larger firms preferring to join networks or affiliations.

This short review of the Scandinavian market³⁶ tends to suggest that it is not only the extent of market liberalisation that drives overseas expansion but that

³³ Though clearly Frankfurt may have an independent lure as a financial centre.

³⁴ Each of which has at least 50 fee-earners and with the top four much larger than that.

³⁵ Legal 500, 'Finland Country Overview' available at <http://www.legal500.com/books/lfe> last accessed 19 May 2009.

³⁶ Although Scandinavia has been covered here there are fascinating other examples of international expansion. Wolf Theiss which has offices in Albania, Bosnia & Herzegovina, Croatia, Romania, Serbia, Slovenia and the Slovak Republic was named 'Austrian Law Firm of the Year' and 'Czech Republic Law Firm of the Year' by the International Financial Law Review in 2008.

relative size and in turn available resources may play a part. There are also factors that might favour Anglo/US driven expansion such as the English language, the strength of the London/New York markets and the choice of common law to govern commercial contracting. Even so we can observe two significant developments in Scandinavia. The first is that where, as in Finland, the market is highly competitive, firms do begin to branch out beyond their borders. The second is that the majority of larger firms are developing international strategies, albeit that these are in the form of networks and associations that mirror the early developments of UK and other Northern European firms as they began first to explore opportunities overseas. This tends to suggest that the strategy is not so different but the timeframe is slightly altered. If this is so then one would expect to see the type of embryonic exploitation of establishment rights already pursued by Finland spreading more widely within Scandinavia on the back of the degree of market liberalisation already apparent in the region.³⁷

PUBLIC AND PRIVATE INTEREST IN REGULATION

In a European market for legal services already depicted as liberalised, however, a plethora of practice rules at Member State level remain. Indeed a Commission study of 2003 concludes that:

'entry barriers, price fixing or recommended prices, prohibition of advertising and rigorous definition of form of business add up to quite a restricted regulatory environment of the profession in most new Member States'.³⁸

Since all of these types of restrictions can be found to a greater or lesser degree in the Single Market, the obvious question to ask is how well do such rules serve the public interest or is it more the case that they are driven by and accommodate private interests in that even control of entry into the profession is simply 'the first line of defence' in a pattern of regulation that aims to 'protect

³⁷ For some support for this view see: Nelson L, 'Independent Streak' (May 2009) *Commercial Lawyer* 30

³⁸ European Commission (DG Competition) *Stocktaking Exercise on Regulation of Professional Services* COMP/D3/MK/D (2004) at para. 41.

against market forces'?³⁹ It is possible to make some assessment of private and public interest by reviewing the rationality of regulation.

It is commonly accepted that the rationale for regulating services that might otherwise be subject to market competition is some failure of the market.⁴⁰ Here, given the specialised, knowledge-base of legal services, it is argued that information asymmetry between legal provider and consumer would prevail if their provision went unregulated. As the free flow of reliable information is a condition for the functioning of an efficient market in services, the danger is a lowering of quality standards as consumers are prepared to pay less for services if they are unsure of the quality, and providers produce lesser quality services in response to the promise of lower rents. There is not a total failure of information here. The consumer may be able to assess the success (or otherwise) of the intervention but unable to judge accurately either the quality or quantity of the services taken to reach that outcome especially if service providers act opportunistically as a result; hence the label 'credence goods' to this type of service.⁴¹ Infrequent and private client consumers of legal services may be particularly exposed to such opportunistic behaviour and may be "required to hold the provider of the service in a position of trust."⁴² The presence, in such a market, of poor quality service providers which nonetheless attract business may deter better quality providers and drive down the overall quality of legal services.⁴³ The argument is that a regulator may be better placed than the consumer to determine and regulate the quality of provision, reducing search costs and restoring confidence in the market.⁴⁴

A very closely related problem to that of information asymmetry is a species of moral hazard relating to supplier induced demand. Here the argument is that

³⁹ Abel R "English Lawyers between Market and State: The Politics of Professionalism", Oxford University Press, (2003) at 96.

⁴⁰ Anthony Ogus, *Regulation: Legal Form and Economic Theory* (Hart, 2004) chapter 3.

⁴¹ M Darby and E Karni "Free competition and the Optimal Amount of Fraud" (1973) 16 *Journal of Law and Economics* 67 - 88

⁴² F Stephen, J Love and A Paterson "Deregulation of Conveyancing Markets in England and Wales" (1994) 15(4) *Fiscal Studies* 102-18 at 103

⁴³ This phenomenon is often referred to as a 'lemons market' following a famous essay: Akerlof G 'The market for "lemons": Quality Uncertainty and the Market Mechanism' (1970) 84 *Quarterly Journal of Economics* 488 - 500.

⁴⁴ For a review of this argument see Dingwall R and Fenn P 'A Respectable Profession?' Sociological and Economic Perspectives on the Regulation of Professional Services' (1987) 7 *International Journal of Law and Economics* 51.

even if the consumer adequately assesses the quality of the legal services on offer, it may be challenging indeed to determine the quantity of legal services needed. Garoupa has suggested that these problems may abound when, as is often the case in legal services the agency function (that which isolates the problem and devises a remedy) and the service function (the delivery of that remedy) are in the same hands.⁴⁵ How is the consumer to effectively determine the level of resource needed to effect the remedy except by following the advice offered by the legal services' provider?⁴⁶

Another event of market failure could be said to be the presence of externalities. External costs and benefits may attach to the delivery of legal services. As externalities may be both positive and negative it is possible that the effective provision of good legal advice to (say) an employer may have considerable social beneficial impacts, for example to employees of that client. Arguably this makes the 'market' price paid for the service too low from a social perspective.⁴⁷ Externalities may also arise as specialist knowledge reaches the public domain as transactional documents are shared or legal argument is heard in court allowing the potential of other people to simply free ride on the work of others without reference to market payments. These external benefits might begin to make a case for restrictions on who can enter the market for legal services, but it is generally negative externalities such as the social damage of bad advice or faulty transactions that drives regulation.⁴⁸

In addressing these negative externalities, it becomes apparent that there is a level at which legal services begin to exhibit a hybrid nature in that, though they comprise a private good, they exhibit a large element of public significance – even in the commercial law area where private interest might seem at its highest. The resolution of a purely private dispute may set a binding precedent

⁴⁵ Garoupa N, 'Regulation of Professions in Portugal: A Case Study in Rent Seeking' (2004) Banco de Portugal Conference Proceedings on *Portuguese Economic Development in the European Union*.

⁴⁶ This is a problem that bedevils legal aid provision – see Bevan G, 'Has There Been Supplier-induced Demand for Legal Aid?' (1996) 5 *Civil Justice Quarterly* 98; Cape E and Moorhead R, *Demand Induced Supply? Identifying Cost Drivers in Criminal Defence Work* (2005) Legal Services Commission, London.

⁴⁷ Rubalcaba, L., *Services in European Policies* (2007) Bruges European Economic Policy Briefings Paper 16.

⁴⁸ For a recent example of this see the consultation document proposing the much tougher regulation of immigration advisers: UK Border Agency, *Oversight of the Immigration Advice Sector* (May, 2009).

that offers important commercial certainty for others in the future. There exists a broad public interest in ensuring that commercial contracts are performed to acceptable standards and appropriately enforced. As more frequent users of legal services, commercial clients may be especially concerned that legal certainty can be guaranteed, that the administration of justice functions as it should and that democratic values can be promoted through the legal system.⁴⁹ In all of this, lawyers play a key role as is commonly reflected in professional codes which, as indicated earlier,⁵⁰ might emphasise a primary duty to the court in advance of that to the client.

These events of market failure provide the rationale for regulation of the legal profession in its various forms including: qualification; licensing; mandatory professional indemnity insurance; subscription to an ethical code etc. The extent to which such regulatory fabric is actually justified in the public interest is a matter of considerable debate if, as Abel has suggested,⁵¹ such professional admission and conduct rules may provide protectionist shelter from competitive forces. Abel has put the case that lawyers have sought out opportunity to assert significant control over the market for their services as this best serves their interest in preserving traditional, social and economic advantage.⁵² It is a consequence of Abel's argument that attempts to open up legal services to competition may be met by even greater attempts to assert professional control.⁵³ Abel in his later work commented that one of the major forces in curtailing the extent of the professional monopoly in recent times has been the stratification of the professional reflected in the gap between the large and the small firms.⁵⁴ This point, of obvious significance for this paper, is explored further below.

⁴⁹ This is so notwithstanding the reluctance of such clients to resort to litigation as the relational contract theorists point out – see for example Macauley S, 'An Empirical View of Contract' (1985) *Wisconsin Law Review* ` 465–482.

⁵⁰ See text at n16, supra.

⁵¹ Op cit. n 39.

⁵² Abel R., "England and Wales: A comparison of the Professional Projects of Barristers and Solicitors in Abel R. and Lewis P.S.C., (eds) *Lawyers in Society: The Common Law World* (1988).

⁵³ R. Lee *Firm Views: Work of and Work in the Largest Law Firms* (1999) Law Society (Research Paper No 35).

⁵⁴ Op cit. n 39.

The weight given to the public interest factors above will largely determine the extent of regulation. Few would advocate a complete free for all in the market for legal services but some would argue that there remain rules that serve self rather than public interest. In the following section we illustrate this by reference to the ongoing debate concerning competition in professional services in Europe.

DEBATING LEVELS OF REGULATION

As indicated above, and demonstrated by the market liberalisation measures to date, the European Commission occupies a key position as a driver for change in this area. In its 2004 report on Competition in Professional Services⁵⁵ the Commission addressed 5 key professional services including the legal sector. The report concluded that deregulation was necessary throughout the EU legal world in certain key categories of regulation including: price fixing (both fixed and recommended prices); advertising; entry restrictions; and business structure restrictions. Although the Report found that price fixing was a relatively minor scale problem within the EU market for legal services, advertising restrictions were said to increase fees with little (or at least an unknown) increase in the quality of services provided.

As for entry requirements and business structure, the Commission cited a US Federal Trade Commission review of studies⁵⁶ into licensing restrictions which found evidence for both quality improvements and quality shortfalls, but which largely concluded that quality was 'unaffected' by licensing and even that licensing may have a negative effect on quality'.⁵⁷ The problem with this type of review is that it is rather undiscerning as to the nature of the licensing restrictions under consideration and whether these related to access, continuing education within or participation in the profession.⁵⁸ Moreover it is unlikely that all studies reviewed would hold relevance for the legal profession. Nonetheless

⁵⁵ European Commission *Competition in Professional Services* COM(2004) 83 final.

⁵⁶ Cox C. and Foster S., "The Costs and Benefits of Occupational Regulation" Bureau of Economics Staff Report to the Federal Trade Commission, 1990, p. 26-27.

⁵⁷ European Commission Report (op. cit. n.21) at para. 50 and see Moorhead R, Sherr A and Paterson A 'Contesting Professionalism: Legal Aid and Non lawyers in England and Wales', (2003) 37 (4) *Law and Society Review*, 765-808.

⁵⁸ Moorhead R, *Lawyer Specialisation - Managing the Professional Paradox* (2008) Working Paper No 5, Cardiff Law School.

examples of deregulation in Australia, the UK and the Netherlands suggested lower consumer costs as a result.⁵⁹ In Australia, the removal of barristers' monopoly right of access to the courts resulted in a 12% reduction in costs; in the UK the extension of conveyancing work to non-legal providers resulted in 'lower prices' and in Holland the abolition in entry requirements for estate agents led to lower prices for estate transactions. The value of such costs' reduction, however, would need to be set alongside any commensurate increase in social costs if hybrid public goods were at stake.

The weighing of costs and benefits as part of a formal impact assessment is now a common feature of regulatory initiatives. Stephen⁶⁰ has argued that professional services should be *prima facie* subject to general competition law so that regulators should have to justify interventionist measures. This is premised on the arguments employed by the European Commission's in their review suggesting that qualification requirements lessen competition and heighten the fees chargeable by service providers to the detriment of consumers. Francisco Marcos⁶¹ advances similar arguments in his paper reviewing the debate in Spain concerning the provision of legal services by non-legal entities; in this case, auditors. Marcos is sceptical of public good arguments depicting lawyers as guardians of justice imbued with a 'peculiar essence or ethical standards that preserve the legal services out of a market' concluding that: 'Lawyers are not different to other professionals... nothing should insulate them from the competition of other professionals'.

Set against these types of argument is the Council of Bars and Law Societies of Europe's (CCBE) submission in response to the Commission's Communication on Professional Services.⁶² It attacks the Commission's depiction of business interests as the 'main user' of legal services, which it argues shapes the tone of

⁵⁹ All examples give here are taken from the Commission study at n.38, *supra*.

⁶⁰ Stephen F.H., 'The Market Failure Justification for the Regulation of Professional Service Markets and the Characteristics of Consumers' (2004) *Proceedings of the EU Competition Law and Policy Workshop* European University Institute, Florence.

⁶¹ Marcos F., 'The Storm over Our Heads: The Rendering of Legal Services by Audit Firms in Spain' (2000) 7(1) *International Journal of the Legal Profession* 7 - 38

⁶² Council of Bars and Law Societies of Europe, 'CCBE Responses to the Questions of the European Commission on the Future of the Internal Market', 14th July 2008 available at: http://www.ccbe.org/fileadmin/user_upload/NTCdocument/ccbe_responses_inter1_1182_240992.pdf

the paper when considering issues of public interest. The CCBE argues that there are numerically stronger groups comprised *inter alia* of: persons accused of crime and victims; families and children going through divorce; persons making wills; applicants for immigration; people with employment issues; accident victims etc. The CCBE accepts business as the main user of legal services in terms of value in the legal system but expresses 'regret that in current discussions concerning regulation of the legal profession the non-economic aspects are often downplayed or put aside'.

Close to this view would be that of the Chief Justice of New South Wales, The Honourable James Spigelman AC⁶³ who, from a jurisdiction with long established multi-disciplinary practices and liberalised legal representation rules, seeks perhaps to restore some balance. He argues that law is something more than a mere business given the significant public interests at stake but that decision-makers are increasingly mindful of narrow economic considerations to the exclusion of other factors. Spigelman urges regulators to quantify the positive effect of anti-market failure mechanisms such as quality guarantees and indemnity insurance. He draws an analogy with the UK competition regime which has moved (too far) away from public interest justifications for anti-competitive regulation under the UK Fair Trading Act 1973 towards purely economic ones under the Competition Act 1998, itself modelled on EC Treaty principles.

Olesen and Nielsen of *Copenhagen Economics* in their impressive study for the Danish Ministry of Justice⁶⁴ mediate nicely between the arguments above. The study was carried out notwithstanding that Denmark was at the time considered the third most liberal legal regime in Europe. According to the report, while there is a case for some liberalisation, if this reduces the requirements for legally qualified advisers it could affect the quality of legal services. In particular, the problem will affect primarily private clients and small enterprises because larger business clients have better opportunities for assessing the quality of the

⁶³ The Honourable JJ Spigelman AC, *Are Lawyers Lemons? Competition Principles and Professional Regulation* (2002) Sydney: St James Ethics Centre.

⁶⁴ Henrik Ballebye Olesen and Claus Kastberg Nielsen, 'The Legal Profession Competition and liberalisation' January 2006 available at: http://www.copenhageneconomics.com/Admin/Public/DWSDownload.aspx?File=%2FFiles%2FFiler%2FPublikationer%2FThe_legal_profession.pdf

lawyer's work and are in less need for protection.⁶⁵ A most interesting finding was that:

'Price is not a very important factor in the choice of lawyer because it is far more important to obtain good advice than to obtain cheap advice. This is true for both private clients and business clients.'⁶⁶

It follows from this that cost should not be the primary arbiter of consumer benefit as high quality is primarily what consumers seek. Moreover, the study found that lawyers are in fact engaged in serious competition both with other lawyers, non-lawyers such as accountants and foreign lawyers. Indeed the most significant barriers to new law firms establishing was not state regulation but the long-term investment in establishing a client base. This was said to be because reputation is of central importance and proof of such reputation takes time. A final point, and one referred to by the CCBE, was that contrary to the Commission view, qualification requirements do not lower competition in the market to a detrimental level but are crucial in ensuring the quality of advice consumers receive, though in the case of legal aid clients, at least, Moorhead *et al* have thrown doubt on this view.⁶⁷

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Part of the above debate centres on the effect upon competition of a regulatory monopoly held by Bar and Law Societies in policing practising lawyers. In addition to any ability to control entry and cap numbers to protect existing practice rights, it is said that the lack of democratic accountability attaching to self-regulation undermines any justification of anti-competitive measures. Van den Bergh,⁶⁸ on the other hand, considers such arguments but concludes that self-regulation is to be favoured as the profession itself retains the best knowledge of how a good lawyer should be operating. He suggests that the state

⁶⁵ It should be noted that Hadfield argues that the willingness of corporate clients to pay the necessary price for success means that legal resources are skewed towards the business segment of the profession, and towards efficiency and away from individual justice goals – see Hadfield G. K. 'The Price of Law: How the Market for Lawyers Distorts the Justice System', (2000): 98 *Michigan Law Review* 953-1006.

⁶⁶ This accords with the finding that sector specific expertise remains the single most important factor for clients when they select a law firm, followed by 'previous experience of using that law firm' see the *FTSE Client Satisfaction Report* (2008) Legal Week Intelligence.

⁶⁷ See Moorhead R *et al* 'Contesting Professionalism' at n.57

⁶⁸ Van den Bergh, R., 'Towards Efficient Self-Regulation in Markets for Professional Services' 2004 (2004) *Proceedings of the EU Competition Law and Policy Workshop* European University Institute, Florence.

is not in a good position to consider regulatory supervision as it has long proved ill-equipped in defining public interest goods.

Van den Bergh offers as an example of the success of competitive self-regulation the opening up of higher court advocacy rights to solicitors in England and Wales, with the consequence that higher court advocates were regulated either by the Law Society or the Bar Standards Board. Yet the apparent success of this competitive regulation does not really stand scrutiny. Solicitor-advocates in the higher courts are a distinct minority. This might suggest that greater consumer choice, allowing consumers to choose between a barrister and a solicitor-advocate, might have little meaning to clients unaware of differing regulatory standards of training or admission. But it might suggest that informed clients do recognise the greater level of training and experience as advocates vested in the Bar.⁶⁹ The injection of competition might be more real if (for example) the four Inns of Court competed against each other.⁷⁰ Yet the effect of this might actually be adverse to consumer interests as standards might take a race to the bottom in attracting Bar members.

Nonetheless it is clear that self regulation has the capacity to create barriers not just in areas such as admission but in terms of other restrictions on matters such as advertising or business structures. Operating at state level these can pose a barrier to cross border practice. Terry and Silver⁷¹ explore the differing response to the competition debate in Northern Ireland, the Netherlands, England and Wales and Poland. The Polish have taken the view that much of its legal regulation is unconstitutional and are creating a new system to govern lawyer admission and training. The Dutch had a public consultation which proposed to allow alternative business structures within the legal market. The

⁶⁹ The comparative competence of solicitor advocates has been an issue of recent controversy in England and Wales - see Baksi C, 'Law Society Complains Over Judge's Remarks on Solicitor Advocates' *Law Society's Gazette* 30 April 2009 - accessed online: <http://www.lawgazette.co.uk/news/law-society-complains-over-judge-s-remarks-solicitor-advocates>

⁷⁰ Antony Ogus has suggested this type of solution: Ogus A 'Rethinking Self-regulation' (2005)15 *Oxford Journal of Legal Studies*, 97-108. It might be argued that this is the *de facto* position in Europe, except that there is not complete freedom of movement and the spatial localised nature of certain services means that the model does not transfer easily to cross-border legal services.

⁷¹ Terry, L.S., Silver, C et al, 'Transnational Legal Practice' 2008 available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1265120

UK Legal Services Act 2007 adopts the most revolutionary elements of the Clementi report⁷² and expands upon them, allowing alternative business structures and legal disciplinary partnerships whereas Northern Ireland decided to keep ownership of law firms strictly to lawyers. This disparate response to the competition debate leads to inevitable difficulties for law firms seeking to penetrate non home markets. Firms entering Spain from jurisdictions in which legal services are restricted solely to lawyers will face increased levels of competition from non law firm providers of legal services. At the same time Italy may prove an impossible market for multi-disciplinary practices because of continuing Italian restrictions of business structure.

What is demonstrated here is that if there are events of market failure of the type considered above, it is still necessary to reflect on the type of intervention invoked to address the market failure problem and to make some assessment of the efficacy of the intervention when ranked against the seeming inadequacies of the market. In the case of legal services perhaps the most common form of intervention has been professional self regulation. Usually this springs from an argument that if the market failure is essentially one of information asymmetry, then those best placed to gauge the quality of provision are lawyers themselves. But as we have sought to illustrate above, the regulatory intervention can easily be subverted as such self regulation begins to encompass matters such as advertising restrictions or set/scale fees which are at best tangentially related to the problem of market failure that gave rise to the mandate for regulation. Moreover, the form of regulation, through professional bodies semi-detached from other public agencies, makes standardisation of professional rules problematic and helps produce the bewildering array of professional rules that undermines attempts at regulatory harmony in the interests of better competition. In short we might conclude that whatever the market weaknesses in relation to legal services provision, the remedy may be worse than the disease.

MARKET FAILURE AND COMMERCIAL LEGAL SERVICES

⁷² David Clementi, Report of the Review of the Regulatory Framework for Legal Services in England and Wales (2004) (DCA; London).

All of this assumes that we find the market failure analysis compelling. Some commentators at least would assert that the case is not so strong as to allow the effective capture of the system by those supposedly subject to control.⁷³ Here I wish to pursue a gentler line of argument that, whatever the general strength of arguments relating to market failure, they weaken considerably when one considers the case of commercial legal services at a multinational level. Beginning with arguments about information asymmetry, these are difficult to sustain for a number of reasons. One would be that the whole ethos of globalisation of legal services concerns law firms moving to be alongside the markets in which their clients are active. Such firms are already employed by these clients. Not only are the clients regular, repeat players in the legal services sector, but their choices are very often informed by in-house counsel no doubt recruited from the very sorts of firm which the client now engages. Information asymmetries attach most strongly to infrequent players and research⁷⁴ has suggested that reliance on trust alone is generally associated with lower levels of client impact. The more frequent consumers of business advice place greater reliance on formal contractual provisions with their service providers and are in a much better position to assess comparative service standards by experimenting with the different firms.⁷⁵

If market information is needed, it is readily available in the form of law firm guides, internet based information, specialist legal press, and increasingly transparent financial information about the firm, its profitability and its client base. Further information can be solicited in a number of forms, through tendering, beauty parades, panel competition, or simply a phone call. It is possible for the multinational corporate client base to actually generate competition between would-be providers. There is little reason for adverse selection and the search costs involved are happily borne in a market in which, as stated earlier, the quality of legal advice is far more important than its price.

⁷³ Hadfield, *op cit.* at n 63; McChesney, F., 'Rent Extraction and Rent creation in the Economic Theory of Regulation' (1987) 26 *Journal of Legal Studies* 101-118.

⁷⁴ Bennett R.J. and Robson P.J., "The role of trust and contract in the supply of business advice" (2004) 28(4) *Cambridge Journal of Economics* 471 - 488

⁷⁵ Almost two-thirds (62%) of FTSE companies have panels in place, but relatively few commit themselves to using only their panel firms and the role of procurement professionals in FTSE companies doubled in two years prior to 2008 – see *FTSE Client Satisfaction Report, supra n.66.*

All of this reflects the reality of the power relationship between the law firm and its commercial client which reduces considerably the information asymmetries that provide the main basis for regulation. The reality is management by the client of its legal services provision, often again by in-house counsel. If the argument for self regulation is that information asymmetries are best cured by legal professionals, then this is the solution in which corporate clients have invested heavily. The extent of monitoring and controls to eliminate over-provision of legal services is enormous and ranges from more simple fixed fee arrangements to real time supervision of spending through client access to the lawyers' own systems. Indeed the concern might not be so much that the client is manipulated by the lawyer but that the opposite is the case as lawyers seek to become increasingly 'flexible and adaptive' to accommodate the different demands of the clients.⁷⁶

As for those events of market failure that concern questions of public goods and of potential externalities, these too play out very differently when the market is that for multinational commercial legal services. While costs may attach to poor quality advice, rather than the social costs attaching to (say) a poorly handled child custody case or to uncompensated losses for accident victims, the costs of poor commercial advice will be internalised into the wider operating costs of the commercial client. This in part encourages vigilance on the part of these clients in selecting law firm representation. While there are unquestionably considerable issues of public interest in ensuring private client services such as effective criminal court representation, the prominence of that public interest is less obvious once we are dealing with law firms dispensing commercial services. Indeed, in this market even the private interests will look different. For example, it is likely that core technical competence will be taken as a given and that law firms actually compete on the basis of expertise, higher service standards and other values not necessarily so crucial for non-repeat players, such as loyalty or commercial confidentiality.

⁷⁶ Sida Liu 'Client Influence and the Contingency of Professionalism: The Work of Elite Corporate Lawyers in China' (2006) 40 *Law and Society Review* 751-782.

It was suggested earlier that there could also be positive externalities in the form of benefits accruing from advancing legal knowledge, settling the limits of the law to provide certainty for the commercial world and through innovative transactions which are quickly taken up within the market. While it is true that the presence of such externalities might mean that law firms fail to extract an appropriate level of reward from such services, it is not at all clear that we would wish to intervene through regulation to provide more extensive monopoly rights or to fix minimum fee levels.⁷⁷ In general terms the mere fact of something less than a perfect market does not mandate regulatory intervention. Throughout, the question is one in which it is necessary to balance the need for protection against the dilution of competition, which will follow from regulation. So we may be more inclined to intervene to protect private consumers and less inclined to intervene to protect law firms.⁷⁸

Put another way, all events of market failure ordinarily invoked as reasons for intervention in the provision of legal services, look surprisingly weak when applied to multinational commercial legal services. Yet the curiosity is that despite all of the evidence of increasing stratification of the legal profession, it has taken considerable time for any appreciation of the distinction between private client and corporate client lawyers to emerge when considering matters of regulation.⁷⁹ Stephen has suggested that this issue of market segmentation is hardly addressed at all in discussions on regulation even though market failure arising out of information asymmetry is 'likely to arise only in those markets where consumers are infrequent purchasers.'⁸⁰ Although Stephen seems to accept the general case for certification based on education and training,

⁷⁷ Arruñada B, 'Managing Competition in Professional Services and the Burden of Inertia' (2005) *Universitat Pompeu Fabra Working Paper* 827 argues that where such solutions are adopted they outlast their usefulness and are difficult to displace.

⁷⁸ Marty Lipton of Wachtell Lipton Rosen & Katz is said to have invented the 'Warrant Dividend Plan' (the so called poison pill) in late 1982 but its use in 1984 by Household Corporation resulted in heated litigation that went to the Supreme Court in Delaware in 1985. Once its legality was upheld, its use became pervasive and any advantage to Lipton was lost: see Appleton S 'Poison Pills, Thrills and Heavyweights' *Global Counsel* 3000 (May 2002).

⁷⁹ This looks set to change judging by early indications from the Hunt Review of Legal Regulation – see Hunt D, *Initial Response to Evidence* 5 May 2009.

⁸⁰ Stephen F 'The Market Failure Justification for the Regulation of Professional Service Markets and the Characteristics of Consumers', Ninth EU Competition Law and Policy Workshop: *The Relationship between Competition Law and (Liberal) Professions*, European University Institute, Florence, 11-12 June 2004.

thereafter he argues that the presumption of ordinary competition should apply with any derogation justified in the particular market place. If that was taken here to be the market for commercial legal services to multinational corporate clients, it might be difficult indeed to demonstrate how the types of market restriction still found across Europe, on issues such as advertising or form of business organisation, could be warranted.

The above discussion paints a picture in which major corporate clients turn increasingly to large commercial law firms which are themselves both sizeable enterprises with a multi-national presence. In looking for what we described earlier as a seamless level of service whatever the geographical point of provision, the corporate client is not looking to the provision of advice by a single lawyer, however close relationships between clients and law firm partners may be.⁸¹ In practice the type of transactional work demanded by the client will involve teams of lawyers (and paralegals, for whom certification requirements are irrelevant) often from different offices and in part the client is relying on the internal management capacity of the firm in its recruiting and training of lawyers to deliver the standard of service that it desires. This commercial reality contrasts starkly with much that is built into the professional standards' model, where the focus of regulatory attention in terms of qualification and conduct is historically the individual lawyer.⁸² This begs the question of whether more might not be achieved by both shifting the regulatory effort to the law firm and placing greater reliance on those mechanisms that are already part of the market relationship between lawyer and client whereby the firm shoulders greater responsibility for those lawyers within its organisation. It is argued in the following section that such a model may offer the key to yet greater market liberalisation.

FROM HOST TO HOME STATE CONTROL

⁸¹ And research suggests this is still a significant factor in the relationship between firm and client – see Uzzi B and Lancaster R, "Embeddedness and Price Formation in Corporate Law Markets." (2004) 69(3) *American Sociological Review*, 319-344.

⁸² Though this model is changing post Clementi through the use of a designated Head of Legal Practice ("HoLP") who is approved by the licensing authority as a fit and proper person as part of an Alternative Business Structure for legal services' provision – see the Legal Services Act 2007.

As stated earlier in the paper the problems of double deontology deepen with ever greater disparities in the extent of market liberalisation in the provision of legal services. This is a particular issue for jurisdictions like England and Wales and New South Wales⁸³ which have made provision for forms of law firm structure involving persons other than lawyers. Perhaps in recognition of this reality two recent reports in England and Wales have opened up the possibility of the law firm itself as the focus of legal regulation rather than the individual practitioner. In a review of the regulation of law firms, Lord Hunt was 'attracted' to a system in which large firms self-certify their compliance with regulatory requirements through a designated head of regulatory affairs, at board level or equivalent.⁸⁴ This would then be subject to periodic audit by a regulator, though Hunt was agnostic regarding earlier recommendations⁸⁵ that there should be a separate regulatory structure for the larger firms. Logically, however, a self certification system for larger firms would seem to imply their separation out for regulatory purposes. The focus on regulating firms which in turn regulate their members offers an important route to resolving barriers to cross border practice. Professional services regulation is often directed at individuals – doctors, dentists, etc – and if we consider legal services in this way, then Home State control of an individual operating many miles distant is no easy matter. Yet lawyers operating outside of the jurisdiction in which they qualified are usually practising within large commercial firms. If the firm becomes the focal point of regulation, the Home State control becomes a possibility replacing earlier notions of Host State control. Under a system of audited self certification, the firm becomes the most immediate point of supervision and regulation of the conduct of the individual lawyer.

Among the matters to be policed within the firm is that only lawyers qualified to act within a jurisdiction will pursue reserved areas of work, including the right to appear in court, thus providing assurance that the working of the legal system will not be threatened by the influx of lawyers from a different tradition.⁸⁶ Of

⁸³ Lamb A and Littrich J *Lawyers in Australia* (2007, Federation Press) at 109 *et seq.*

⁸⁴ See Hunt, *supra* at n 79.

⁸⁵ Smedley N, *Review of the Regulation of Corporate Legal Work* (2009) (SRA, London).

⁸⁶ A point not pursued further here is the extent to which non reserved areas of work should be the subject of regulation – if at all.

course it might be ideal if procedural and other conduct rules were harmonised, but, as experience through the CCBE has shown, this may prove a long process. The CCBE attempts dating back to the 1980s to articulate and harmonise core ethical rules⁸⁷ seek to eliminate issues of double deontology to the advantage of law firms wishing to offer cross border services. In the absence of such a solution, however, regulation of the firm rather than that of the lawyer opens up better regulatory options less likely to hinder cross border activity than traditional models of Host State control.

A rule of Home State control, not uncommon in the financial services' market, would allow the Home State regulator to notify the Host State of the intention of a law firm to locate within the Host jurisdiction. While the two jurisdictions would co-operate and the ordinary background (criminal and civil) law would apply to a provider operating in the Host State, the Home State authority would remain the point of regulatory control. Once the firm is made the point of regulatory control it can give notice to its Home regulator of any intention to operate elsewhere in the Single Market. Lawyers within the firm then operate under that Home State control thereby avoiding many problems of double deontology.

If the public interests of the Host State are to be respected, then the practice rights of lawyers within the incoming firm would have to be curtailed. Its licence would be limited and would not include, for example, rights of audience in the Host State's courts. However, it is believed that large law firms would accept this restriction for two reasons. First, for many law firms court representation is not a service that it is seeking to offer to clients. This may be because the services actually offered are truly global services such as capital markets' work with little contentious content. Moreover, even where disputes do arise, the chosen forum for resolution by the commercial clients may well be private arbitration. Secondly, as we have seen, the chosen path of entry to many markets is by law firm merger, often following an earlier period of loose alliance. So the firm may be entering a market in which there are other lawyers on hand, qualified in the jurisdiction, to undertake reserved work not available to incoming lawyers from

⁸⁷ Conseil des Barreaux de l'Union Européenne, *Code of Conduct for Lawyers in the European Union* (1988 as amended 1998 and 2002) CCBE, Brussels.

its Home jurisdiction. As this suggests if local lawyers are available in the firm, then they would remain free to undertake reserved work and when doing so would revert to Host State control. It would be the task of the law firm to police this regulatory line and its lawyers would face disciplinary action in the Home State in the event that it was breached – for example by lawyers undertaking unlicensed court work.

Individual lawyers, not falling within the law firm umbrella authorisation, would still be entitled to move around the market by the existing processes of re-qualification either by examination or registration. But lawyers in large commercial law firms⁸⁸ could fall and would remain within Home State control, even if based elsewhere in the single market. Ultimately, lawyers would remain under the control of the jurisdiction in which they qualified, since the ultimate sanction, disbarment, might need to be exercised by the relevant competent authority. Regulatory co-operation across Member States would be necessary. Nonetheless, this model of passport rights for the large law firm would have advantages. It would offer a quick and easy route to other markets at the law firm level and thereby advance liberalisation of this sector. It would offer choice to many law firms by eliminating problems of double deontology as Home State lawyers working under passport rights would follow Home professional conduct requirements. However, for firms with lawyers also qualified in the Host State, it might well be open to the firm to make strategic choices about how to deploy its human resources in order to overcome regulatory restrictions in areas such as conflicts of interest.⁸⁹ This form of regulatory arbitrage is only regrettable if the rules themselves are defensible, but as argued in the previous section, these rules do little to actually protect already powerful corporate clients or to otherwise correct information deficits.

Ultimately if a model based on passport rights began to operate, it might be that the more liberal jurisdictions begin to attract lawyers on the back of their

⁸⁸ It is accepted that the parameters of the large firm would need to be fixed in a manner not open to abuse, but this is a task that in any case is thrown up by the Hunt Review.

⁸⁹ Lawyers would need to remain conscious of the differing views taken by their commercial clients on the extent to which conflicts of interest might be tolerated: see Griffiths-Baker J., *Serving Two Masters: Conflicts of Interest in the Modern Law Firm* (2002) Hart, Oxford.

elimination of unnecessary regulatory restrictions and the growth of opportunity offered by exploitation of passport rights. Under this model, we might grow closer to Ogus' model of regulatory agencies in competition against each other.⁹⁰ The advantage of a passport model is that it offers little opportunity for a Host State to seek to exploit professional conduct rules in a protectionist manner and close the borders to other legal service providers. In the longer term the experience of lawyers, under another model of control offering commercial legal services without untoward consequences, ought to drive a real and much-needed debate as to the extent of regulatory controls at the various layers of the heavily segmented legal services market. It should be borne in mind that regulatory failure might prove highly detrimental not merely to the particular law firm in question but to the confidence placed in the Home regulator of the jurisdiction in question.

This type of arrangement moves the market closer to the ethos of the 2006 Services Directive⁹¹ in facilitating the establishment of a business in another Member State. Placing the law firm as the object of regulatory focus allows for administrative simplification. It helps produce a horizontal approach, now an accepted method of promoting the cross-border provision of services. Regulation based in the country of origin, should provide a high level of protection of consumers as home regulators are conscious of the need to promote confidence in the services provided if they are to be successful across borders. This can be backed by obligations of mutual assistance and cooperation between national authorities, though the nature of those authorities is beginning to change as certain Member States loosen the ties of bar or law societies. As this trend continues, it may prove fascinating to see whether professional or independent scrutiny proves more attractive to consumers of legal services and also, ultimately, where the truly global law firms, which are likely to have a choice of lead regulator, place their faith.

⁹⁰ Ogus, op. cit n. 70.

⁹¹ Directive 2006/123/EC of 12 December 2006 on services in the internal market

CONCLUSION

This paper has traced the development of cross border legal services in Europe under the influence of a raft of legal measures to facilitate the liberalisation of legal services. It has suggested, however, that if the momentum is to continue, there is further room for mechanisms to facilitate cross border legal practice at least in the field of commercial legal services. This is a field that is easily identifiable as a segment of an increasingly stratified market for legal services and it is one in which the case for regulatory intervention on account of market failure is at its weakest. Accepting that these services are delivered by larger law firms, these, rather than the individual practitioner, would become the focus of regulation. This might in turn allow a process of Home State control with passport rights into a Host State on notification. The quid pro quo would be that the licence of these firms to practise through foreign lawyers would be limited to specified areas of transactional, non contentious law, at least until the point that through merger or local hiring the complement of staff was developed to include local lawyers.

Dating back to the Lisbon European Council Agenda of March 2000 the EU have set the target on becoming the most competitive and dynamic knowledge-based economy in the world by 2010.⁹² Cross border legal services have already contributed significant capacity towards this objective and by driving forward competitiveness not only in the legal services sector but in the European economy as a whole. Competitive service standards within law and high quality legal advice are crucial inputs into business and as such generate marked spillovers for the general economic good. Effective and professional legal advice benefits the general consumer of business goods and services and allows the efficient functioning of the Single European Market. Economic growth in the Single Market has been enhanced by the ability of law firms to follow and support the global activities of their clients. Against this background, it is imperative to search for mechanisms that will allow ease of access throughout Europe for both consumers and providers of commercial legal services.

⁹² European Commission *Report on Competition in Professional Services* COM (2004) 83 final at para. 8.

