

**REGULATING LAW FIRM ETHICAL INFRASTRUCTURE:
AN EMPIRICAL ASSESSMENT OF THE POTENTIAL FOR MANAGEMENT-
BASED REGULATION OF LEGAL PRACTICES**

Christine Parker^{*}, Tahlia Gordon^{**} and Steve Mark^{***}

DRAFT

** Associate Professor and Reader, ARC Australian Research Fellow, Melbourne Law School, University of Melbourne, Victoria 3052, Australia. Email: c.parker@unimelb.edu.au*

*** Research Officer, Office of the Legal Services Commissioner, NSW*

**** Legal Services Commissioner, NSW*

This paper is based on an online research report published by the NSW Office of the Legal Services Commissioner: C. Parker, T. Gordon & S. Mark, *Research Report: Assessing the Impact of Management-Based Regulation on NSW Incorporated Legal Practices* (2008) available at [http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/vwFiles/Research_Report_ILPs.pdf/\\$file/Research_Report_ILPs.pdf](http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/vwFiles/Research_Report_ILPs.pdf/$file/Research_Report_ILPs.pdf) (visited 1 January 2009). We would like to acknowledge the hard work and expert assistance of Malcolm Anderson in preparing the statistical analyses reported here, and also the work of research assistant, Caitlin Hamilton in preparing the data for analysis. We would also like to acknowledge the very helpful comments and assistance of Esther Bedgood, Molly Hutcherson and Lynda Mustyn of the Office of the Legal Services Commissioner, and also the comments and advice of John Gray, Linda Haller, Gillian McAllister and Vic Marles. This research was made possible by funding from a Melbourne Law School School Faculty Small Grant to Dr Christine Parker, for which she is grateful. This research was conducted by Christine Parker in collaboration with the New South Wales Office of the Legal Services Commissioner. It was not a paid consultancy.

ABSTRACT

It has been suggested that law firms should pay attention to their own ethical infrastructure in order to make sure that their formal and informal management policies, procedures and controls support and encourage ethical decision-making by lawyers within the firm. Professor Ted Schneyer, and Professors Elizabeth Chambliss and David Wilkins have both suggested that the regulatory system for the legal profession should place requirements on law firms (not just individual lawyers) with the aim of encouraging or requiring firms to put in place ethical infrastructures.

The deregulation of law firm structure and investment in Australia and the UK for policy-makers and legal profession regulators to require law firms to implement an ethical infrastructure. New South Wales, Australia, was the first jurisdiction in the world to remove all restrictions on incorporated legal practices legislation. New South Wales requires incorporated legal practices to appoint a legal practitioner director responsible for ensuring that the firm delivers legal services in compliance with ethical and conduct obligations and to put in place ‘appropriate management systems’ to do so. This ‘management-based regulation’ approach to promoting ethical infrastructure is broadly consistent with that recommended by Chambliss and Wilkins.

This paper critically assesses the potential for this approach to improve the behaviour and ethical decision-making of lawyers as a matter of principle. The paper also presents results of an empirical assessment of the actual effects of this management-based regulation approach on complaints levels in New South Wales. We find that the process of self-assessment of the firm’s ethical infrastructure in itself leads to a large and statistically significant drop in complaints, but that the (self-assessed) level of implementation of ethical infrastructure does not make any difference. These results suggest that the management-based approach to regulation of law firm ethical infrastructure is promising.

INTRODUCTION

A number of scholars and commentators on legal ethics in the US have suggested that it is a major weakness of legal profession regulation and ethics that the focus continues to remain on individual lawyers alone. Many lawyers these days work in large firms that shape their behaviour, values, and capacity to act and think ethically: Therefore it is suggested that law firms and legal practice groups, as well as individual lawyers, should also be the subject of ethical and regulatory responsibilities. In particular, law firms and legal practices should be encouraged or required to ensure that they have in place internal systems and cultures that ensure compliance with professional conduct obligations and enhance individual lawyers' ethical awareness and behaviour.¹

Traditionally the regulation of the practice of law has focused almost exclusively on individual legal practitioners through character and educational and training standards for admission and the disciplinary process for failures to reach character and ethical standards. More recently, consumer dispute resolution processes have been added to disciplinary processes, but these still focus almost exclusively on disputes between individual practitioners and their clients.² In Australia recent moves to deregulate law firm structure and investment have prompted, for the first time, regulation of the management and behaviour of firms as firms.³ Australia is beginning to require legal practices to have appropriate management systems and cultures for the ethical provision of legal services in an attempt to avoid the risks of overly commercial, unethical conduct in legal practices that are no longer structured as partnerships. England and Wales are also introducing firm-based regulation with the deregulation of legal practice to allow alternative business structures, but the exact shape of this regulation is not yet known.⁴

¹ See below notes 6 and 7.

² C. Parker, 'Regulation of the ethics of Australian legal practice: Autonomy and responsiveness' (2002) 25 *University of New South Wales Law Journal* 676.

³ S. Fortney, 'Tales of two regimes for regulating limited liability law firms in the U.S. and Australia: client protection and risk management lessons' (2008) 11 *Legal Ethics* (forthcoming).

⁴ *Legal Services Act* UK (2007). See also J. Flood, 'Will there be fallout from Clementi? The global repercussions for the legal profession after the UK Legal Services Act 2007' (April 2008) Miami-Florida European Union Center Jean Monnet/Robert Schuman Paper Series, Vol. 8, No. 6; U. of

The Australian approach has been pioneered in the most populous state of Australia, New South Wales (NSW), the first place in the world to remove all restrictions on incorporation of legal practices. This paper evaluates the potential of the New South Wales approach to regulating ethical infrastructure in incorporated legal practices (ILPs).

The next section of the paper briefly sets out the arguments for why legal profession regulation should encourage law firm implementation of effective ethical infrastructure, and not just focus on individual practitioners. It goes on to describe the New South Wales model which includes legislation that requires ILPs to implement an ‘appropriate management system’ to ensure legal practice according to professional ethical and quality standards, and a compliance strategy in which firms must self-assess their own implementation of appropriate management systems with the guidance of the independent regulator and subject to possible review by the regulator. We label this ‘management-based regulation’ as it requires firms to implement an effective ethical infrastructure that achieves the goal of ethical delivery of legal services without prescribing in detail exactly how it should be done.⁵

The remainder of the paper critically assesses the potential of this approach to law firm regulation in principle, and then using empirical evidence of NSW firms’ self-assessments and complaints rates. First, we discuss the main arguments in principle as to why management-based regulation to achieve effective law firm ethical infrastructures might not work and argue that despite potential weaknesses, the NSW approach is promising. Second, we use quantitative data from the independent regulator of the NSW to test whether regulating ILPs in this way improves their ethical management and behaviour as

Westminster School of Law Research Paper No. 08-03. Available at SSRN:

<http://ssrn.com/abstract=1128398>, S. Mayson, *Law Firm Strategy: Competitive Advantage and Valuation* (2007); Ministry of Justice, *Alternative Business Structures Fact Sheet* (9 June 2008) available at <http://www.justice.gov.uk/docs/abs-fact-sheet.pdf>; Solicitors Regulatory Authority, *Legal Services Act: New Forms of Practice and Regulation* (November 2007). The existing and fairly detailed client care and management and supervision rules will likely apply to alternative business structures and their managers: see below n 19. The legislation also requires alternative business structures to have an approved Head of Legal Practice and Head of Finance and Administration, and fitness to own test will be applied to all external investors with more than 10% ownership stake.

⁵ C. Coglianese & D. Lazer, ‘Management-based regulation: prescribing private management to achieve public goals’ (2003) 37 *Law & Society Review* 691.

indicated by lower complaints rates. We find that the NSW approach to regulating the ethical management of law firms has a dramatic and positive impact. The final section discusses these findings and concludes.

REGULATING LAW FIRMS FOR ETHICAL INFRASTRUCTURE

The Call for Regulation to Promote Implementation of Effective Ethical Infrastructures in Law Firms

A number of commentators on ethics in the profession have argued that the legal profession and regulators of the legal profession have not traditionally done enough to make sure that law firms have in place internal management efforts to ensure ethical conduct. They argue that law firms should consciously put in place ‘ethical infrastructures’ – formal and informal management policies, procedures and controls, work team cultures, and habits of interaction and practice that support and encourage ethical behaviour – and that law firms should be regulated in a way that encourages them to do so.⁶ They argue that there have been cases where firm-level policies and procedures create economic and social incentives for unethical individual conduct, or at least where firm management systems and cultures do not do enough to make ethical conduct regular and systematic. Yet ethical regulation of the legal profession and most ethical commentary and discussion has focused solely on individual legal professionals, not the organisations (firms and practices) they work in and that shape their behaviour.

⁶ The term, “ethical infrastructure” was coined by T. Schneyer, ‘A tale of four systems: reflections on how law influences the “ethical infrastructure” of law firms’ (1998) 39 *South Texas Law Review* 245. See also T. Schneyer, ‘Professional discipline for law firms’ (1991) 77 *Cornell Law Review* 1; and further developed by E. Chambliss & D. Wilkins, ‘A new framework for law firm discipline’ (2003) 16 *Georgetown Journal of Legal Ethics* 335; and E. Chambliss and D. Wilkins, ‘Promoting effective ethical infrastructure in large law firms: a call for research and reporting’ (2002) 30 *Hofstra Law Review* 691. See also C. Parker, A. Evans, L. Haller, S. LeMire & R. Mortensen, ‘The ethical infrastructure of legal practice in larger law firms: values, policy and behaviour’ (2008) 31 *University of New South Wales Law Journal* 158; and M. Regan, *Eat What You Kill: The Fall of a Wall Street Lawyer* (2004) 358-361.

Prof Ted Schneyer has argued that law firms, not just individual legal practitioners, ought to be the subject of discipline.⁷ The primary purpose of this discipline should be to promote ethical infrastructures within firms because the quality and probity of a lawyer's work can depend crucially on the 'ethical infrastructure' or internal controls her workplace deploys'.⁸ Schneyer argues that,

Given the evidentiary problems of pinning professional misconduct on one or more members of a lawyering team, the reluctance to scapegoat some lawyers for sins potentially shared by others in their firm, and especially the importance of a firm's ethical infrastructure and the diffuse responsibility for creating and maintaining that infrastructure, a disciplinary regime that targets only individual lawyers in an era of large law firms is no longer sufficient. Sanctions against firms are needed as well.⁹

Similarly Professors Elizabeth Chambliss and David Wilkins argue that 'Because lawyers increasingly practice in large, multi-jurisdictional firms, professional regulation increasingly depends on structural controls *within* firms, such as conflicts avoidance systems, internal reporting procedures, billing guidelines and the like.'¹⁰ Chambliss and Wilkins' review of previously published empirical research indicated that most US law firms had inadequate internal structural controls.¹¹ But their own primary empirical research on the evolution of inhouse compliance specialists in US law firms (including law firm general counsel, loss prevention and risk management partners, and in-house ethics advisors) suggested that firms are beginning to develop internal controls to

⁷ Schneyer above n 6 (1991 and 1998). See also Note, 'Collective sanctions and large law firm discipline' (2005) 118 *Harvard Law Review* 2236; M. Regan, 'Risky business' (2006) 94 *The Georgetown Law Journal* 1957.

⁸ Schneyer, 'Tale of four systems' above n 6, 246.

⁹ Schneyer, 'Professional discipline for law firms?' above n 6, 11 & 12.

¹⁰ Chambliss & Wilkins, 'A new framework' above n 6, ?. See also E. Chambliss, 'MDPs: towards an institutional strategy for entity regulation' (2002) 4 *Legal Ethics* 45, 47-49.

¹¹ Chambliss & Wilkins, 'Promoting effective ethical infrastructure' above n 6, 697-699. See also S. Fortney 'Are law firm partners islands unto themselves? An empirical study of law firm peer review culture' (1996) 10 *Georgetown Journal of Legal Ethics* 271-316.

manage firm compliance with professional regulation.¹² On the basis of their interviews with ethics partners and in-house counsel in larger law firms, they suggested that all firms should be encouraged or legally required to appoint an inhouse ethics or compliance specialist who would promote an ethical infrastructure throughout the whole firm.¹³ They see this as an end in itself:

Policies and procedures that explicitly promote compliance with ethical standards make a statement about firm values to firm members and to the broader ethical community. Within the firm, such policies and procedures provide guidance for well-meaning lawyers and may help them resist informal pressure to lower their practice standards. [they cite some empirical evidence on this]... A firm's creation of specific types of ethical infrastructure also sends an important signal to the managers of similar firms, who may feel institutional pressure to follow suit.¹⁴

Unlike Schneyer, Chambliss and Wilkins do not necessarily see the introduction of discipline of law firms as crucial to promote the implementation of effective ethical infrastructures by law firms, at least in the first instance.

Schneyer, Chambliss and Wilkins frame their arguments for regulating law firm ethical infrastructure in terms of the particular challenges of ensuring ethical conduct inside larger law firms. But many client complaints about legal practitioners in small and medium sized firms also stem from failures of basic practice management procedures that could be addressed by appropriate practice-level ethical infrastructures. For example, the NSW Office of the Legal Services Commissioner (OLSC) (the independent complaints handler and regulator for the legal profession in that Australian state) receives frequent complaints about practitioners not actioning files, or returning telephone calls or facilitating file transfers. Implementing an effective management system which enables

¹² E. Chambliss & D. Wilkins, 'The emerging role of ethics advisors, general counsel, and other compliance specialists in large law firms' (2002) 44 *Arizona Law Review* 559; E. Chambliss, 'The professionalization of law firm in-house counsel' (2006) 84 *North Carolina Law Review* 1515. See also K. Kirkland, 'Ethical infrastructures and de facto ethical norms at work in large US law firms' (2008) 11(2) *Legal Ethics* forthcoming.

¹³ Chambliss & Wilkins, 'A new framework' above n 6.

¹⁴ *Ibid* at 343.

files to be easily located and organised in a way to ensure that tasks are prioritised can obviate these complaints. Similarly, many complaints concern lack of regular communication, and failing to have a good system for informing clients about how costs will be charged in a way that the practitioner is sure that clients understand - matters that can be improved and addressed via firm-level management systems.¹⁵

Regulation of both individual business people and whole firms is of course the standard approach in other areas of business regulation such as environmental, health and safety, discrimination and consumer protection. Regulation that requires business firms to put in place management systems and policies to ensure compliance with various policy goals and seek to inculcate an ethical and compliant culture are increasingly popular.¹⁶

Previous Attempts to Encourage or Require Ethical Infrastructure in Law Firms

Because of the prevalence of complaints like these about lawyers, regulators and legal professional associations in the UK and Australia have encouraged 'client care' and total quality management initiatives beginning in the 1980s and 1990s.¹⁷ Like the proposals that firms implement ethical infrastructures, these initiatives were aimed at firm-level management to ensure compliance with ethical conduct rules and consumer service standards, and sought to address the imbalance in traditional professional regulation that was aimed purely at individual legal practitioners. These were however directed at individual practitioners only – either in relation to their own relationships with clients or as supervisors of other lawyers. Empirical research soon after they were introduced, however, suggested that most of these were not very successful at changing firm

¹⁵ M. Seneviratne, 'Consumer complaints and the legal profession: making self-regulation work?' (2000) 7 *International Journal of the Legal Profession* 39; Avrom Sherr, *Client Care for Lawyers* (1999); C. Parker, 'Regulation of the ethics of Australian legal practice: Autonomy and responsiveness' (2002) 25 *University of New South Wales Law Journal* 676.

¹⁶ C. Coglianese & D. Lazer, 'Management-based regulation: prescribing private management to achieve public goals' (2003) 37 *Law & Society Review* 691; K. Krawiec, 'Cosmetic compliance and the failure of negotiated governance' (2003) 81 *Washington University Law Quarterly* 487; C. Parker, *The Open Corporation* (2002).

¹⁷ E. Greenebaum, 'Development of law firm training programs: coping with a turbulent environment' (1996) 3 *International Journal of the Legal Profession* 315, 320-1.

behaviour.¹⁸ The regulation of solicitors in England and Wales still includes quite detailed client care rules concerning communication, agreements about costs and management and supervision of law firms, but (until reforms take effect) they can still only be enforced against individual lawyers, not law firms.¹⁹ Negligent liability has also prompted some ‘private regulation’ of law firms by insurers seeking to improve law firm internal quality management by providing education, guidance and lower premiums for firms to adopt various risk management measures.²⁰ A number of total quality management systems for law firms have also been developed including Lexcel in the UK and a variation of ISO 9000 for law firms in Australia.²¹ Two jurisdictions in the US have introduced the possibility of discipline for firms consistent with Schneyer’s recommendations, but these provisions have not been widely used and have not spread to other jurisdictions as yet.²²

Deregulation of Law Firm Structure and Investment and Regulatory Requirements for Ethical Infrastructure

In both Australia and the UK, legislative reforms to the structure and regulation of the legal profession, specifically the removal of restrictions on ‘incorporated legal practices’ (ILPs) (as they are called in Australia) or ‘alternative business structures’ (as the same thing is called in England and Wales) have prompted policy-makers to introduce firm-based regulation for the legal profession, in addition to the more traditional controls on individual practitioners.

The full incorporation of law firms – under the ordinary company law and without any restrictions on who may own shares or what type of business can be carried on – is now

¹⁸ C. Parker, *Just Lawyers: Regulation and Access to Justice* (1999) 21-22, 153. See also S. Abraham, M. Spencer & E. Monk, ‘Total quality management: applicability to law firms’ (1998) 25 *International Journal of Quality and Reliability Management* 541. [Has there been subsequent research?]

¹⁹ *Solicitors’ Code of Conduct* (2007) Rules 2 and 5.

²⁰ Schneyer, ‘A tale of four systems’ above n 6, 272-275. [other references??]

²¹ References?

²² Transcript, ‘How should we regulate large law firms? Is a law firm disciplinary rule the answer?’ (2002) 16 *Georgetown Journal of Legal Ethics* 203.

allowed in six of Australia's eight states and territories, and will probably be allowed shortly in the other two.²³ Hundreds of legal practices in Australia have incorporated as ordinary companies (known as 'incorporated legal practices' or 'ILPs'), and two Australian law firms have even listed on the Australian Securities Exchange. The deregulation of law firm structure and investment has been decried by some as ethically dangerous.²⁴ But although there may no longer be rules restricting the formal structure of the business entity that carries on the practice of law, a new regulatory regime and associated compliance mechanisms were introduced to prevent ethical risks without restricting legal practice to the partnership structure. This new regime is a revolution in the regulation of legal practice because it focuses on improving the management and culture of the firm as a whole not just disciplining individual legal practitioners or resolving individual lawyer-client disputes.²⁵ Indeed, the approach taken is very similar to that independently proposed by Chambliss and Wilkins (in papers published after the NSW legislation was already in place but with no apparent awareness of the NSW system). It is likely that Australian policy-makers drew on the client care and total quality management for law firm initiatives in England and Wales and in Australia in the 1980s and 1990s in designing their innovative approach that essentially requires the newly allowed incorporated legal practices to put in place an ethical infrastructure and appoint a senior legal practitioner manager to be responsible for maintaining it.

²³ See C. Parker, 'Law firms incorporated: how incorporation could and should make firms more ethically responsible' (2004) 23 *University of Queensland Law Journal* 347; C.Parker, 'Peering over the ethical precipice: incorporation, listing and the ethical responsibilities of law firms,' forthcoming in Kieran Tranter et al (eds) *Re-Affirming Legal Ethics* (forthcoming). Available at <http://www.law.georgetown.edu/LegalProfession/Papers.html>.

²⁴ B. MacEwan, M. Regan & L. Ribstein, 'Law firms, ethics, and equity capital' (2008) 21 *Georgetown Journal of Legal Ethics* 61; S. Mark, 'The corporatisation of law firms – conflicts of interests for publicly listed law firms' Paper presented to Australian Lawyers Alliance National Conference 2007 (available at http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/pages/OLSC_speeches - visited 26 February 2008); Parker *ibid* (2004 and forthcoming).

²⁵ S. Mark & G. Cowdroy, 'Incorporated legal practices – a new era in the provision of legal services', (2004) 22 *Penn State International Law Review* 4; J. Briton & S. McLean, 'Incorporated legal practices: dragging the regulation of the legal profession into the modern era' (2008) 11(2) *Legal Ethics* forthcoming.

The most populous state in Australia, New South Wales (NSW), was the first state to allow full incorporation in 2001. Consequently it was New South Wales legislators that initiated this regime and the NSW Office of the Legal Services Commissioner ('OLSC'), the independent regulator of the legal profession in NSW, that first had to work out how to implement it. This paper focuses on the regime they developed. This NSW model is now being adopted throughout Australia.

The New South Wales Model for Regulation of Ethical Infrastructure for Incorporated Legal Practices

Legal work within incorporated legal practices must still be carried out by qualified and certified legal practitioners, and all the traditional professional conduct and duty of care obligations continue to apply to each legal practitioner employed by the firm, including obligations to have a practising certificate and to have mandatory professional liability insurance.²⁶ In addition to these traditional requirements for *individual* legal practitioners, new requirements that focus on management responsibilities and systems for the ethics and quality of legal practice are placed on the *firm*.²⁷ Consistent with the recommendations of Chambliss and Wilkins, this new regime requires ILPs to implement an effective ethical infrastructure and appoint a senior lawyer/manager who must be responsible for the maintenance of this effective ethical infrastructure. This is done by two inter-linked requirements:

- All ILPs must have at least one director who is a legal practitioner (a 'legal practitioner director') who is generally responsible for the management of the legal services provided by ILPs, and for the implementation and maintenance of 'appropriate management systems'.²⁸ They also have an obligation to prevent or remedy any professional misconduct or unsatisfactory professional conduct of a legal

²⁶ Section 143 of the *Legal Profession Act 2004* (NSW) ('LPA').

²⁷ Section 140 LPA. Once incorporated, the company is also of course obliged to abide by its constitution and the *Corporations Act 2001* (Cth), and is regulated by the Australian Securities and Investments Commission.

²⁸ Section 140(1) of the LPA. It is an offence if an incorporated legal practice does not have any legal practitioner directors for a period exceeding seven days, and the practice may be forced into administration if that is the case: Section 142(1) LPA.

practitioner employed by the practice.²⁹ They can be held personally responsible in professional disciplinary action for failures in relation to any of these responsibilities on their own part or for any breaches on the part of officers or employees of the ILP unless they can establish that they took all reasonable steps to prevent the misconduct.³⁰

- All ILPs must have ‘appropriate management systems’ in place to enable the provision of legal services by the practice in accordance with professional obligations and so that the carrying out of these obligations is not affected by other non-lawyer officers or employees of the practice.³¹ It is the legal practitioner director/s responsibility to ensure that appropriate management systems are implemented and maintained.³²

In this paper our focus is on the requirement for ILPs to implement ‘appropriate management systems’.³³ The OLSC has by agreement with the Law Society of New South Wales taken on the role of regulating ILPs for compliance with the appropriate management systems requirement,³⁴ which it does by requiring self-assessments by the firms themselves and conducting ‘performance reviews’.³⁵

²⁹ Section 141 LPA. This includes reporting to the Law Society any conduct of another director of the practice that contravenes that person’s professional obligations or other obligations imposed by or under the Act, as well as any professional misconduct of a legal practitioner employed by the practice: section 140(4) LPA.

³⁰ Section 141(1A) LPA.

³¹ Section 140(2) LPA.

³² Failure to implement and maintain “appropriate management systems” is professional misconduct on the part of the legal practitioner director: section 140(5) LPA.

³³ See also J. Gray, G. McAllister & M. Adams, ‘Qui bono? How will changes in business models for law firms affect organization, governance and regulation of legal services? Report of a pilot study,’ paper presented to Challenging Institutions Workshop, University of New South Wales 19-20 June 2008.

³⁴ Mark & Cowdroy above n 25, 671.

³⁵ Under section 670 LPA either the OLSC or the Law Society of NSW Council can audit or review legal practices including incorporated legal practices. The OLSC has, in practice, by agreement with the Law Society, assumed the role of auditing or reviewing ILPs for compliance.

The nature and coverage of the ‘appropriate management systems’ are not defined in the LPA. Therefore the OLSC has collaborated with the Law Society of NSW, the College of Law (a provider of practical legal training for the legal profession) and LawCover (a legal profession insurer) to define ten key areas or objectives that should be addressed by ‘appropriate management systems’ (shown in Table 1). The ten objectives are intended to help ILPs work out how to systematise professional ethical conduct, rather than prescribing detailed management systems from above.

The OLSC also formulated an ‘education towards compliance’ strategy in which ILPs must self-assess whether they have procedures in place which evidence compliance with the ten objectives of appropriate management systems, and report this back to the OLSC. The OLSC send legal practitioner directors of each new ILP a standard self-assessment document, based on the ten objectives, to enable them to assess their management systems when they commence operation.³⁶ The form requires ILPs to assess themselves as to how well they have achieved each of these ten objectives throughout the firm on a five point scale from ‘non compliant’ to ‘fully compliant plus’ (see Table 2) – and send the filled in form back to the OLSC.

ILPs are given three months initially to self-assess themselves and return the filled in form. Those that rate themselves as ‘compliant’ or more with all ten areas receive an acknowledgement letter from the OLSC. If an ILP rates itself as only ‘partially compliant’ or ‘non-compliant’ in any area then they receive a follow up letter asking them to, ‘Please advise as to what action you intend to take and when you expect this to occur so that a “C” (compliant) rating can be achieved as soon as possible.’ The OLSC also provides some guidance on how compliance can be achieved. The ILP is given a date one month later by which they are expected to reply with evidence of what they have done to comply.

In most cases this process of self-assessment and response by the OLSC results in a dialogue between the OLSC and the ILP – sometimes conducted in letters and sometimes in phonecalls and face to face meetings – about what management systems

are appropriate for that particular ILP. The OLSC will often make suggestions about what they think is appropriate and explain why they expect certain procedures and processes to be important. The ILP in turn might explain why they think some things are not necessary for their practice either because of the size or the nature of the practice. Ultimately it is the legal practitioner director/s' responsibility to decide what management systems are appropriate for their own practice.

In the (very rare cases) where there is no response to the self-assessment process, or the response is inadequate or raises questions about whether appropriate management systems have been established and maintained, the OLSC conducts a practice review of the ILP and its appropriate management systems, and may also initiate a complaint against the ILP which could lead on to further investigation and professional discipline. A practice review may also occur where there is a referral from a Law Society trusts account inspector. The OLSC can also issue a 'section 660 notice' requiring the production of documents and information and cooperation with its investigation.³⁷

The OLSC may conduct a practice review whether or not a complaint has been made about the ILP's provision of legal services. But in some cases repeated complaints about practitioners in a particular ILP have prompted a practice review where the complaints raise issues about whether appropriate management systems are in place. The OLSC practice review generally seeks to guide the legal practice towards the ultimate objective of better practice management and compliance with the LPA.³⁸ But if the practice review uncovers breaches, then the OLSC can take disciplinary action. The results of any practice review may be taken into account in any disciplinary proceedings against a legal practitioner director or other persons, and in decisions about the grant, renewal, amendment, cancellation or suspension of a practising certificate.

³⁷ Section 660 LPA.

³⁸ See above n 35.

TABLE 1: TEN OBJECTIVES OF 'APPROPRIATE MANAGEMENT SYSTEMS' FOR ILPS³⁹

AREA TO BE ADDRESSED	OBJECTIVE OF APPROPRIATE MANAGEMENT SYSTEMS IN EACH AREA
1. Negligence	Competent work practices
2. Communication	Effective, timely and courteous communication
3. Delay	Timely review, delivery and follow up of legal services
4. Liens/File Transfers	Timely resolution of document/file transfers
5. Cost Disclosure/Billing Practices/Termination of Retainer	Shared understanding and appropriate documentation on commencement and termination of retainer along with appropriate billing practices during the retainer
6. Conflict of Interests	Timely identification and resolution of the many different incarnations of "conflict of interest", including when acting for both parties or acting against previous clients as well as potential conflicts which may arise in relationships with debt collectors and mercantile agencies, or conducting another business, referral fees and commissions etc
7. Records Management	Minimising the likelihood of loss or destruction of correspondence and documents through appropriate document retention, filing, archiving etc and providing for compliance with requirements regarding registers of files, safe custody, financial interests
8. Undertakings	Undertakings to be given, monitoring of compliance and timely compliance with notices, orders, rulings, directions or other requirements of regulatory authorities such as the OLSC, courts, costs assessors
9. Supervision of Practice and Staff	Compliance with statutory obligations covering licence and practising certificate conditions, employment of persons and providing; quality assurance of work outputs and performance of legal, paralegal and non-legal staff involved in the delivery of legal services
10. Trust Account Regulations	Avoiding failure to account and breaches of s61 of the Act in relation to trust accounts.

³⁹ Available at NSW OLSC website:

http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/pages/OLSC_tenobjectives (accessed on 17 July 2008).

TABLE 2: RATINGS USED IN SELF-ASSESSMENT OF APPROPRIATE MANAGEMENT SYSTEMS

SELF-ASSESSMENT RATING	CODE	NUMERICAL RANKING (for statistical analyses)	EXPLANATION
Non-Compliant	NC	1	The Objective has not been addressed.
Partially Compliant	PC	2	The Objective has been addressed but management systems are not fully functional.
Compliant	C	3	Management systems exist for the Objective and are fully functional.
Fully Compliant	FC	4	Management systems exist for the Objective and are fully functional and regularly assessed for effectiveness.
Fully Compliant Plus	FC Plus	5	The Objective has been addressed, all management systems are documented and all are fully functional and all are assessed regularly for effectiveness plus improvements are made when needed.

MANAGEMENT-BASED REGULATION OF LAW FIRMS: CRITICAL ASSESSMENT

Regulatory theorists have labelled this type of approach ‘management-based regulation’ because it requires firms to engage in their own planning and internal management processes with the objective of achieving defined public goals, in this case the ethical, high quality delivery of legal services.⁴⁰ This can be distinguished from more traditional legal approaches to business regulation in which certain behaviours (eg misleading and deceptive conduct, discrimination or fraud) or performance standards (eg levels of pollutant emissions) are defined and firms sanctioned if they are not met. Nor is it the more prescriptive process-oriented regulation that would prescribe exact management systems or technologies that firms should put in place and sanction them if they fail to do so. There are several practical and theoretical reasons why this management-based approach may not be effective at ensuring high standards of ethical conduct and quality of service as applied to NSW ILPs.

⁴⁰ Coglianese & Lazer above n 16, 692 & 694. (Coglianese & Lazer cite E. Bardach & R. Kagan, *Going by the Book: The Problem of Regulatory Unreasonableness* (1982) at 224 as originating the term ‘management-based regulation’).

Appropriate Management Systems Too Managerialist

One objection is that management-based regulation is a type of managerialism that is inappropriate to the profession of law. On this view the profession of law relies on highly individual judgments made in specific circumstances about specific cases. Each individual legal professional needs to have a high degree of autonomy to make these individual judgments. It is therefore not appropriate for a regulator to attempt to require all legal practices to 'manage' the provision of legal services through a set of templates. It is also inappropriate within a law firm for the top management of the firm to micro-manage individual legal professionals, or for the firm to prescribe standardised ways of running each case. Managerialism of this type is seen as an assault on professional autonomy and self-regulation that will ultimately result in lower ethical standards and less high quality professional services. For example, the UK Legal Aid accreditation scheme for law firms, which regulates the management of cases in very detailed ways is regarded by many as too prescriptive and controlling.⁴¹

The very advantage of management-based regulation, however, is that it should be very flexible and give a great deal of discretion to each individual firm to plan and implement in its own way to fulfill important publicly defined values (the ethical practice of law) within the context of its own practice and clients. This is why the NSW OLSC purposely chose not to impose a more detailed and prescriptive management system standard on ILPs such as ISO 9000 quality systems management or other more specific management system standards that have been developed for law firms specifically (such as Lexcel in the UK).

Coglianesse and Lazer suggest that management-based regulation is the best method of regulation where the type of services being regulated are highly individualised and contextual, and the precise outcomes (the application of ethical values) being sought cannot easily be measured by external regulators.⁴² Legal services are indeed highly contextual and individual depending on the area of law, the client and the nature of the

⁴¹ H. Sommerlad, 'The implementation of quality initiatives and the New Public Management in the legal aid sector in England and Wales: bureaucratisation, stratification and surveillance' (1999) 6 *International Journal of the Legal Profession* 311; H. Sommerlad, 'Managerialism and the legal profession: a new professional paradigm' (1995) 2 *International Journal of the Legal Profession* 159.

⁴² Coglianesse & Lazer above n 16 at 705.

problem. There are few, if any, general ways in which regulators can objectively measure whether lawyers have engaged in ethical behaviour unlike, say, environmental regulation where one might measure emissions or health and safety regulation where one can measure injuries. This means that individual firms and practitioners need to be trusted to a certain extent to regulate their own ethics. But one thing regulators can do is require firms to at least plan and implement controls to make sure that they are regulating their own ethics – and then test the extent to which they have done so. This is what management-based regulation does.

In practice the way the OLSC (or any other regulator) implements a supposedly flexible management-based regulatory approach may be too rigid and ‘managerialist’. Or law firm management might interpret its requirements too rigidly or choose to impose rigid requirements on its own employees. We would not expect management-based regulation to be as effective in those circumstances.

On the other hand, it is not true that the profession of law requires no management at all. Managerialism for its own sake is of course useless. But good management is not. Good management is generally considered fundamental to legal compliance and ethical conduct in any industry or organization (although there is more to ethical conduct than management). The historical tradition of legal practices operating as small partnerships means that many legal practices are still relatively new to the need for management planning and implementation to achieve their business goals and ethical standards.⁴³ Clients of all but the largest law firms have not generally had sufficient market power or knowledge of the law to encourage law firms to put appropriate management practices in place to ensure ethical, high quality services. This does not mean that individual lawyers have not been sufficiently motivated to be ethical. It does mean that the market for legal services has been organised such that law firms as firms have not necessarily felt the pressure to manage themselves in such a way as to ensure ethical, quality services. Management-based regulation can be particularly useful in industries, like law, that have not historically had sufficient incentives to engage in planning and implementation to make sure they meet public values.⁴⁴

⁴³ S. Mayson, ‘Your capital: building sustainable capital: a capital idea’ in L. Empson (ed), *Managing the Modern Law Firm* (2007) 141.

⁴⁴ Coglianesse & Lazer above n 16 at 710-711.

ILPs Too Small for Appropriate Management Systems

The vast majority of unincorporated legal practices in Australia are still small practices with a single principal⁴⁵ practitioner (with or without employee lawyers) – and the vast majority of the 631 legal practices in NSW that have incorporated and gone through the self-assessment process are too (see Tables 3 and 4).⁴⁶ A high proportion of ILPs are effectively sole practitioners who may not be expected to need complex management systems. It could therefore be argued that we would not expect to see a management-based approach to regulation making much difference to professional behaviour and complaints for these small practices. Many practitioners in fact made this point in the self-assessment documents they sent back to the OLSC.

The OLSC (like most other legal profession complaints handlers in Australia, the UK and US), however, receives disproportionately more complaints relating to practitioners in small to medium-sized practices than larger ones.⁴⁷ Many of these complaints relate to precisely the sort of things that appropriate management systems are supposed to address – particularly setting and keeping to expectations about communication from lawyer to client, timing for different steps of each matter (and avoiding delay) and costs. This suggests that even very small practices need to prioritise effective practice management to make sure that lawyers deliver services, communicate with clients, and explain costs information to a high quality regularly and systematically. While commentators like Schneyer and Chambliss and Wilkins have focused on the need for regulation to ensure effective ethical infrastructure in larger firms to ensure a consistent ethical culture among diverse work groups, there is also an argument that even smaller firms should be thought of and regulated as businesses or firms in addition to any

⁴⁵ ‘Principal’ includes a partner, solicitor director or other legal practitioner responsible for the running of a legal practice.

⁴⁶ In 2002 about 70% of Australian solicitors’ firms had single principals/proprietors: Australian Bureau of Statistics (‘ABS’), *8667.0 Legal Practices Australia 2001-2* (2003), 21.

⁴⁷ See B. Arnold & F. Kay, ‘Social capital, violations of trust and the vulnerability of isolates: the social organization of law practice and professional self-regulation’ (1995) 23 *International Journal of the Sociology of Law* 321, 339; L. Haller, ‘Solicitors’ disciplinary hearings in Queensland 1930-2000: A statistical analysis’ (2001) 13 *Bond Law Review* 1, 16.

regulation of individual professionals. The management of even smaller firms can make a big difference to practitioners' ability to comply with professional conduct rules and ethics.

Moreover, the management-based regulation adopted by the OLSC does not require all firms to put in place exactly the same procedures and systems no matter the nature and size of the practice. There is considerable flexibility, and the OLSC has been quite willing to accept that certain requirements are not applicable for some practices. Indeed the OLSC has been very clear that its intention is to encourage ILPs to build up ethical behaviours and systems that suit their own practices rather than imposing complex management structures on practices regardless of what actually makes sense for them. We would therefore expect that going through a self-assessment process and putting in place appropriate management processes should assist even very small practices to meet the objectives of ethical, quality legal service delivery better.

TABLE 3: PROPORTION OF NSW SELF-ASSESSED ILPs BY SIZE (NUMBER OF LEGAL PRACTITIONER DIRECTORS) 2008⁴⁸

Number of Principals (Legal Practitioner Directors) ⁴⁹	Number of Self-Assessed ILPs	Number of Self-Assessed ILPs of that Size as Proportion of All Self-Assessed ILPs of All Sizes	Total Number of NSW Legal Practices with that Number of Principals ⁵⁰	Number of Self-Assessed ILPs as Proportion of All Legal Practices in NSW of Same Size
1	482	76%	3684	16%
2	94	15%	398	24%
3-5	42	7%	172	33%
6-10	6	1%	53	11%
11-20	0	0	3	-
21+	1	<1%	23	4%
Total	631	100%	4341	15%

⁴⁸ Based on information about ILPs at 1 March 2008 and total practices at 1 May 2007 supplied by Law Society of NSW.

⁴⁹ Counted as number of solicitors holding principal practising certificate. Six self-assessed ILPs are recorded as having 0 principals by Law Society of NSW data.

⁵⁰ Non-incorporated legal practices will not have 'legal practitioner directors' since only companies have directors. Non-incorporated practices will have 'partners' or a 'principal' instead. The term 'principal' includes partners, legal practitioner directors or anyone with a principal practising certificate able to be responsible for a legal practice (whether incorporated or not).

TABLE 4: SELF-ASSESSED ILPs BY SIZE (NUMBER OF LEGAL PRACTITIONER DIRECTORS AND TOTAL NUMBER OF LEGAL PRACTITIONERS) 2008

Total Number of Practitioners in ILP	1	2	3-5	6-10	11-20	21+	Total
ILPs with 1 Director (Percentage of all 631 self-assessed ILPs)	236 (37%)	133 (21%)	99 (16%)	18 (3%)	0	1 (<1%)	481 (76%)
ILPs with 2 Directors (Percentage of all 631 self-assessed ILPs)	-	27 (4%)	50 (8%)	15 (2%)	2 (<1%)	0	94 (20%)
All Self-Assessed ILPs (Percentage)	237 (38%)	157 (25%)	159 (25%)	55 (9%)	16 (3%)	7 (1%)	631 (100%)

Meaningless Box-Ticking

Management-based regulation might be too flexible and therefore easily become a purely symbolic, hypocritical, box-ticking exercise for the firms involved. Cynics would argue that some firms will fill in the self-assessment forms to indicate that they comply without even thinking about it; or without there being sufficient evidence of management systems being implemented effectively; or that they will put in place very minimal changes to please the OLSA that in fact make no difference to everyday behaviours. To the extent that firms do implement appropriate management systems and take them seriously, those systems might still make no difference to ethical behaviour if they are not supported by commitment to ethical values by lawyers throughout each firm. In particular these management systems might fail to support or encourage the development of individual lawyers' awareness of their own ethical values and ethical judgment as to how to apply them in practice.⁵¹

Despite the potential lack of substance of the management-based approach to regulating ILPs, there are a number of reasons why we might expect it to be influential.

The appropriate management systems requirement and self-assessment requirement is intended to raise consciousness about the requirements of good management in legal practice precisely at a point where firms are undergoing significant structural and

⁵¹ Parker et al, above n 6.

management change anyway because they are incorporating.⁵² This is a point at which we can expect that firms are in a position to substantively change their practice, rather than just tick boxes, and the OLSC's ten objectives might therefore have the greatest potential of influence.

In fact, many firms have been willing to assess themselves as non-compliant or partially compliant on various of the 10 objectives rather than just ticking the 'compliant' box (see Table 5). It is true that in some cases an ILP has simply ticked the boxes without providing any further comment. But in a surprisingly large number of cases, ILPs have in fact filled in significant detail about their processes and systems. An earlier study conducted for the OLSC in 2006 found that, of the ILPs studied, 63% of them had returned their self-assessment forms with substantial comment on them, not just a mere rating.⁵³ Many have also engaged in substantial dialogue with the OLSC and made substantial changes to their management systems as a result of the self-assessment process. Indeed, in the correspondence about their self-assessments on the OLSC files, a number of legal practitioner directors have commented on how useful they found the process as part of their overall exercise of restructuring and rethinking their practice with incorporation. The study quoted above found that 56% of the ILPs studies were prompted to make changes to their management systems as a result of the self-assessment process as indicated by correspondence back and forth with the OLSC.⁵⁴ This suggests that the self-assessment process is being taken seriously, that it is having an impact on implementation of appropriate management systems and lessening complaints.

On the one hand, we might hope that firms can be relied on to fill out the self-assessments honestly and reliably using the guidance provided by the OLSC and that their self-assessment ratings might therefore form a basis for drawing conclusions about how well managed they actually are. In that case we would expect to see firms with higher ratings having less complaints than those with lower ratings.

⁵² Gray et al, above n 33.

⁵³ S. Miller & M. Ward, *Complaints and Self-Assessment Data Analysis in Relation to Incorporated Legal Practices* (Office of the Legal Services Commissioner and Centre for Applied Philosophy and Public Ethics, July 2006) available at <http://www.cappe.edu.au/docs/reports/consultancy/OLSC.pdf> (visited 26 June 2008).

⁵⁴ Ibid.

On the other hand, since we are relying on *self*-assessments of *appropriate* management systems, there is a lot of variation and subjective judgment necessarily involved in the assessment exercise. What is an appropriate management system for one firm of one size practising in one area of law may not be considered necessary or appropriate for another quite different firm. It is therefore inherently difficult to come up with a single scale for measuring management systems that can be adequately and reliably used to compare very different firms with different practices. Moreover the fact that these are *self*-assessments means that there is, by definition, a different person rating each firm, namely the legal practitioner director of that firm. That person will not really know how their own firm compares with other firms, and therefore how it should be rated to give reliable ratings for comparing firms. Therefore we should not really expect these ratings to be reliable and comparable.

It does not necessarily matter from a regulatory point of view if the actual self-assessment ratings (ie the levels) are not reliable and comparable. The main regulatory purpose is to get the firms to go through the process for themselves as a learning exercise to improve their own systems. Nevertheless it would be helpful to know if the actual (self-assessed) ratings on the five point scale do predict differences in actual management and behaviour as indicated by complaints rates, and we do test this below.

Lack of Regulatory Monitoring and Enforcement

A further argument against the likely effectiveness of the OLSC's management-based approach to regulating ILPs is the fact that it relies primarily on *self*-assessments. Insufficient external monitoring and enforcement of appropriate management systems and their impact on ethical behaviour might mean that the whole regime will make little difference to conduct: The good firms will continue to be good - and those that are bad will be able to get away with mismanagement and, potentially, misconduct.

The requirements that ILPs self-assess and manage themselves to meet the ten objectives are, however, just one set of compliance strategies that sit within the context of a whole regulatory system that includes strong independent regulatory oversight of individual ethical conduct and consumer disputes: The OLSC is also the complaints-handling and disciplinary prosecution body for all legal practitioners, and therefore does not have to rely on self-assessments alone to find out about and address potential problems of service and ethics in ILPs and all other legal practices. The OLSC also conducts practice

reviews of incorporated legal practices that either receive a lot of complaints or whose self-assessments are inadequate. In most cases the practice review will be a next step in helping ILPs achieve compliance.

The OLSC's investigation and audit powers mean that legal practitioner directors should be well aware that filling out a self-assessment carelessly or falsely could be found out, and could even result in disciplinary action – since the legal practitioner director must formally sign off on the self-assessment. In particular, the fact that there must be a legal practitioner director with an unrestricted practising certificate who takes responsibility for the management systems and ethical conduct generally in the ILP gives the ILP a powerful incentive to manage its practice ethically, as ILPs are not allowed to continue legal practice for more than seven days without a legal practitioner director with a valid practising certificate.

Despite the apparent 'softness' of the OLSC's education towards compliance approach, we can hypothesise that legal practitioner directors would generally be well aware of the implications for their own ability to practise if there are problems, and therefore have a high incentive to make sure management systems work properly.

Finally, the self-assessment form has been designed to give ILPs a number of 'face-saving' options to admit less than full compliance. There is the option of 'partial compliance' and three different levels of compliance from mere 'compliance' to 'fully compliant plus'. This gives firms the opportunity to rate themselves lower down the scale without rating themselves as 'non-compliant'. In fact many of them have been willing to honestly rate themselves as non or partially compliant (see Table 5). But it is probably unreasonable to expect that the way hundreds of different firms decide to place themselves on a five point scale of compliance with a flexible standard to be consistent and reliable.

MANAGEMENT-BASED REGULATION OF LAW FIRMS: EMPIRICAL ASSESSMENT

Introduction and Hypotheses

We have argued above that, in principle, management-based regulation to encourage the implementation of an effective ethical infrastructure in law firms shows some potential. In this section we report empirical research that evaluates whether the OLSC's management-based regulation of ILP has any impact in practice or not.

We expect incorporated law firms that have gone through the NSW self-assessment process to be better managed, meet their ethical conduct obligations better, and prompt less client and other complaints to the OLSC than before they went through the self-assessment process. This is because (a) we expect their self-assessment and appropriate management systems to prompt more ethical conduct, more effective communication with clients, and less disputes with clients in the first place; and (b) we expect their appropriate management systems to give them the capacity to identify, address and resolve client dissatisfaction and complaints internally before a complaint needs to be made to the OLSC.

For the same reasons, we also expect ILPs that have gone through the self-assessment process to be better managed and engage in more ethical conduct than those firms that are not incorporated at all, and therefore have not been required to go through the self-assessment process.

Finally, if ILPs' self-assessment ratings are reliable, we would expect those ILPs that have rated themselves more highly on their appropriate management systems to be better managed, engage in more ethical conduct, and have less client complaints than those who rate themselves more lowly.

We hypothesise that firms who have gone through this self-assessment process should have less complaints than they did before. We also hypothesise that they should have less complaints than firms that have never incorporated and never gone through the self-assessment process.

This is because the self-assessment process should guide ILPs to improve their management systems and ethical behaviour in ways appropriate to their own contexts. This should in turn improve their provision of legal services and help them to handle any

client complaints or dissatisfaction before it escalates to clients complaining to the OLSC.

Explanation of Strategy for Testing Hypotheses

We test our hypotheses that the OLSC's management-based regulation approach leads to better management and more ethical behaviour in incorporated legal practices that have been through the self-assessment process. We do this by:

- comparing complaints rates for ILPs before and after they have been through the process of self-assessment;
- testing whether those ILPs that self-assess themselves as having greater implementation of appropriate management systems have less complaints as a result;
- comparing complaints rates for ILPs before and after they have been through the self-assessment process with the complaints rates of legal practices that have never incorporated, and therefore have not gone through the self-assessment process.

We use rates of complaint as an indicator of good management and ethical behaviour in legal practices in order to test whether the OLSC's management-based regulation approach actually makes any difference. It is not a perfect solution to use complaints as an indicator of good management and ethical behaviour in a law firm for two reasons:

On the one hand, complaints made to the OLSC may include unfounded complaints or disputed facts that do not in fact indicate poor behaviour by lawyers.

On the other hand, there may be cases of poor behaviour that are not the subject of complaint because clients and other potential complainants lack the knowledge or capacity to complain. We might expect complaints rates to be under-inclusive of complaints from the very poorest and least educated clients who may not have the knowledge and capacity to complain. In particular, we also expect the complaints made to the OLSC to be under-represent unethical behaviour by lawyers that breaches lawyers' duty to the court and the justice system. This is because this type of misconduct is often hidden, and where it is known it is often only known to the client in whose interests it

occurs. Most complaints to the OLSC are from clients, but clients are unlikely to complain about conduct that is in their own interests.

On the whole, however, we expect the number of complaints to reflect how well each law firm is managed, and how well its lawyers behave in relation to important dimensions that the appropriate management systems are supposed to improve. The appropriate management systems requirements were designed explicitly to prevent the sort of conduct that clients do complain about. Therefore we should expect to see effective implementation of appropriate management systems leading to less complaints. Even in relation to supposedly ‘unfounded’ complaints, we would expect firms with good management systems to have fewer minor or apparently unfounded complaints by clients to the OLSC precisely because they should have better communication and internal complaints systems in place that would resolve those issue early on and avoid those complaints being made to the external regulator in the first place.

Moreover, although the OLSC is primarily a reactive complaints receiving body, it is quite proactive about fulfilling its obligation to receive, record and attempt to resolve all grievances and dissatisfaction with legal practitioners. The OLSC is very proactive in educating the community as a whole and agencies that deal with socially disadvantaged groups in particular about the OLSC’s services and the fact that complaints can and should be made about lawyers to the OLSC where there are any problems. Therefore we can be reasonably confident that the OLSC does receive a large proportion of the expressions of dissatisfaction that clients have about their lawyers. We therefore expect complaints numbers to be a reasonably reliable indicator of firm management and behaviour.

Ideally a researcher might prefer to be able to test the effectiveness of management-based regulation by using data directly testing conduct and management in law firms. For example, if the OLSC engaged in inspections and visits of law firms, or surveyed members of law firms or clients regularly, data from these sources could be used to test the reliability of self-assessments and whether the requirement to self-assess was making any difference. But this sort of data simply is not available for a large range of law firms because the OLSC does not do this at this stage. It would cost too much for researchers to do it independently, as well as potentially raising difficult confidentiality issues. Therefore using complaints to test the effectiveness of the OLSC’s management-based regulation approach is the best method available at the moment.

For calculating rates of complaints per practitioner per year for each ILP to test the effectiveness of the OLSC's regulatory regime we use *all complaints made to the OLSC* and do not differentiate between consumer complaints and disciplinary investigations, or between complaints that led to disciplinary action and those that did not.⁵⁵

This is because once we look at the way the OLSC distinguishes between consumer complaints and disciplinary investigations, or focus on those cases in which disciplinary action is taken, too many exercises of discretion by staff of the OLSC enter the equation. These other factors make it more difficult to identify for sure the influence of appropriate management systems. In some cases for example the OLSC may have decided not to take formal action precisely because good appropriate management systems are in place. In other cases insufficient evidence of wrongdoing might have been found for a prosecution even though there is a reasonable likelihood that misconduct did indeed take place. In other cases investigators may have taken the view that there was indeed misconduct, but the sanction applied may have been private disciplinary action (a private reprimand) which was not recorded on the OLSC's database. It is a better test of the effectiveness of the appropriate management systems requirement to look at complaints globally than to start distinguishing between these different categories.

The Legal Services Commissioner only has power to receive and resolve or investigate complaints about individual legal practitioners, not ILPs as such – as there are no consumer or disciplinary remedies available against a whole practice. Therefore to calculate complaints made in relation to ILPs *after* their incorporation and self-assessment, we identified all complaints made against any individuals who were practising in that ILP at the time the complaint was made. We recorded all alternative names of each ILP that we could identify from OLSC records and webpages in order to make sure our matching of complaints to ILPs was as thorough as possible. Complaints are calculated as at February 2008. There is of course a time lag between the conduct complained about and the lodging of complaint, but the data did not allow the recording

⁵⁵ All complaints about legal practitioners must be made to the OLSC. The OLSC classifies complaints into those that concern consumer disputes and those that concern disciplinary matters. The same complaints can raise both sorts of issues. The OLSC can attempt to resolve consumer disputes. Those that concern potential disciplinary matters can be referred to the Law Society or Bar Council for investigation or investigated by the OLSC, with a decision then made about whether to pursue disciplinary action.

of the date of the alleged misconduct. Therefore these data will be overinclusive in the sense that they will include complaints of conduct as about ILPs which were not in fact ILPs at the time of the conduct complained about.

To calculate complaints made *before* ILPs incorporated, we used data that the OLSC collects about every ILP and its legal practitioner directors before they send out the self-assessment package to the ILP. The OLSC obtains these data from the same complaints database as mentioned above. This OLSC check identifies all complaints made against any individuals practising in the firm if the firm was in existence before it incorporated, and also any complaints made about the practice between when it was incorporated and when it was asked to self-assess. The OLSC also checks for complaints against any of the legal practitioner directors of the ILP individually (including when they were practising in other firms).

Background Descriptive Information About ILPs' Self-Assessments of Implementation of Appropriate Management Systems

Incorporation has been allowed in New South Wales since 2001, and there has been a steady and increasing stream of firms incorporating year by year. Some go out of business each year (around a fifth of the number incorporating each year) and others change name or change hands. Almost 20% of the firms in NSW are now ILPs - 790⁵⁶ out of the approximately 4341⁵⁷ (as of 1 March 2008).

This report focuses on those ILPs that are currently still in business and have been through the OLSC's self-assessment process. At the time our data were collected there were 631 ILPs in that category.⁵⁸ (Most of the remainder are still in the process of self-assessing themselves and having the OLSC check their self-assessments, or there is some

⁵⁶ Figure at 1 March 2008, from Law Society of NSW updated to 30 June 2008 via OLSC files and web searches of Law Society of New South Wales online 'search a lawyer' facility.

⁵⁷ Figure at 2 May 2007, obtained from Law Society of NSW.

⁵⁸ The OLSC has on file 620 self-assessments plus documentation from 11 ILPs who were not required to fill in a self-assessment form because they provided evidence that they have been accredited to a quality management standard for legal practices. Two ILPs provided both evidence of a quality management accreditation and a filled out self-assessment and are included in the 620.

other factor that has delayed or prevented the self-assessment process (eg ILPs based interstate).

In Table 5 we show a summary of the self-assessed ratings the ILPs gave themselves for each of the 10 objectives in their initial self-assessment. The self-assessment form required them to rate themselves for each objective on a 5 point scale from ‘non-compliant’ to ‘fully compliant plus’ (see Table 2) – shown as 1 through 5 respectively in Table 5.

Statistical tests showed that self-assessment ratings for all 10 objectives were highly correlated with one another – meaning that whatever rating an ILP gives itself on one objective, it is likely to give itself the same rating on all the other objectives as well.⁵⁹ This could suggest that ILPs simply tick the boxes giving themselves the same sort of rating on everything without thinking about it very much. On the other hand, it is not necessarily surprising that most firms would have roughly similar management system implementation across a range of different areas. At any rate, the fact that self-assessment ratings for all 10 objectives are highly correlated means that it makes sense to average the scores for each ILP to give a total self-assessment rating for all ten objectives, rather than differentiating between ratings for all 10 objectives individually. The total mean rating on this basis is 34 (out of a potential total of 50) with a standard deviation of 6.1.⁶⁰

Trust accounts is the area in which ILPs assess themselves to have the highest compliance levels (60% rated themselves as more than compliant), probably because there has been very heavy regulation and monitoring of trust accounts compliance for legal practitioners for so long. *Communication* and *supervision of practice and staff*, on the other hand, are the two

⁵⁹ The statistical tests used are principal components analysis (PCA); reliability analysis; and tests of correlation. The mean correlation is 0.55 and the minimum is 0.39. Both of these are high, and all correlations are in the same direction. The standardised Cronbach’s alpha is 0.9248, which is very high (but note that with 10 items in the scale, it is likely to be higher). (Cronbach’s Alpha measures how reliably a set of items (for example, questions in a survey) measures a single uni-dimensional latent variable. An index with a Cronbach’s Alpha score of 0.70 or higher is considered a strong index.)

⁶⁰ Scores have been averaged so that missing ratings for a particular objective (usually occurring because that objective was seen as irrelevant for the ILP) are disregarded and the other ratings are applied pro rata to give a score out of 50.

areas in which the largest number of ILPs initially assess themselves as non-compliant or only partially compliant. Communication is a common problem that is featured in almost every complaint the OLSC receives. In relation to supervision of practice and staff, some of the comments on the self-assessment forms suggested that many practices, especially smaller ones, had never thought about systematising staff induction and training. The next two areas most likely to be rated as non-compliant or partially compliant are *conflicts of interest* (14% rated themselves as non or partially compliant) and *undertakings* (13%). The lower ratings in these areas were probably because the self-assessment form suggests that particular formal, written procedures should be present in these areas.

TABLE 5: SUMMARY OF SELF-ASSESSMENT RATINGS OF CURRENT NSW ILPS (JUNE 2008)⁶¹

OBJECTIVE	SELF-ASSESSED RATING (Percentage of total ILPs self-assessing themselves on each objective)						MEAN RATING (Standard deviation in brackets)
	1	2	3	4	5	Total number of ILPs self-assessing	
Negligence	-	11%	47%	35%	7%	619	3.4 (.77)
Communication	1%	17%	46%	30%	7%	620	3.3 (.84)
Delay	<1%	8%	43%	40%	9%	618	3.5 (.78)
Liens and File Transfers	<1%	9%	52%	33%	6%	614	3.4 (.74)
Costs Disclosure	1%	10%	46%	36%	7%	618	3.4 (.79)
Conflicts of Interest	2%	12%	50%	32%	5%	619	3.3 (.79)
Records Management	1%	9%	48%	33%	9%	620	3.4 (.81)
Undertakings	2%	11%	49%	33%	5%	606	3.3 (.81)
Supervision of Practice	2%	16%	48%	28%	6%	611	3.2 (.85)
Trust Account	<1%	3%	37%	44%	16%	571	3.7 (.78)

⁶¹ Data from all ILPs with filled in self-assessments as at June 2008 based on OLSC files.

Percentages are shown as percentages of those rating themselves for each of ten objectives. See Table 2 for explanations of five ratings.

Do ILPs Have Lower Complaints Rates After Self-Assessment than Before?

A score was calculated for complaints per year per practitioner for each ILP for before self-assessment and also for after incorporation and self-assessment.

The date from which we expect to see a change in complaints is the *date of each ILPs' initial self-assessment*⁶² rather than the date of incorporation because it is self-assessment that should prompt changes to practice management, not incorporation by itself, if it is the OLSC's management-based approach to regulation that is making a difference.

The *before* rate is based on the OLSC's check of each practice at the time they ask it to self-assess. It includes complaints related to the practice before it incorporated (if it was in existence), between when it incorporated and when it was asked to self-assess, and also complaints against the individual legal practitioner directors of the ILP even when practising at other firms before the ILP came into existence. The *after* rate includes all complaints related to the ILP using all names that the ILP used for trading that were apparent from OLSC files and the firm's webpage.

We calculate the score by counting the complaints pro rata *per practitioner* because we would expect firms with more practitioners to have more opportunities to attract more complaints. Similarly, we pro rata the complaints *per year* because the more time the more opportunities for complaints to be made.

Before self-assessment, the mean rate of complaints for each ILP per practitioner per year is 0.301 (standard deviation: 0.51). *After self-assessment*, the mean rate of complaints per practitioner per year is 0.098 (standard deviation: 0.227). *Therefore on average the complaints rate for self-assessed ILPs drops by a full two thirds after they have completed their initial self-assessment.*

⁶² Complaints that occurred in the same three month period as the date of self-assessment are not counted as it is not clear whether they would have related to events and conduct that occurred before, after, or simultaneous with the self-assessment process, and so it is difficult to argue a causative relationship with the self-assessment process.

An appropriate statistical test was used to test whether this difference was statistically significant, or whether it could have occurred by chance. We found that this drop in complaints was statistically significant at the highest level.⁶³

Note also that this drop in complaints is not just the artefact of any overall drop in complaints against legal practitioners over a particular time period. The overall number of complaints received by the OLSC each year between 2000 and 2007 has hovered between 2600 and 2900 with the rate going up and down each year.⁶⁴ But we compared rates of complaints for ILPs before and after self-assessment regardless of the year in which the self-assessment occurred. Therefore this finding reflects a trend that occurs regardless of whether overall complaints against practitioners go up or down in a particular year.

Do ILPs Have Lower Complaints Rates than Non-incorporated Legal Practices?

To further test whether it is the self-assessment process that makes this difference or something else, we compare the complaints rates in ILPs with complaints in non-incorporated legal practices (that had not been required to self-assess) over the same period. Ideally we would have been able to conduct an experiment in which we randomly assigned ILPs to a group that is not required to go through self-assessment and one that

⁶³ The Paired T-Test which compares the difference in means from two matched groups: $p=0.0000$; $t\text{-value} = 9.69$; $n=630$. We also calculated these statistics a number of different ways to be sure of our results. All versions of the test showed a significant drop in complaints after self-assessment. Even using a more conservative test in which we compare only complaints between 2001 (when incorporation was first allowed) and 2008 for all self-assessed ILPs and only those complaints that clearly relate to the same firm, not those that relate to individual legal practitioner directors who may have been practising in other firms previously, the complaints rate (ie number of complaints per practitioner per year) drops from 0.169 to 0.098, that is, it almost halves: Full statistics available in the research report published by the OLSC: C. Parker, T. Gordon & S. Mark, *Research Report: Assessing the Impact of Management-Based Regulation on NSW Incorporated Legal Practices* (2008) available at [http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/vwFiles/Research_Report_ILPs.pdf/\\$file/Research_Report_ILPs.pdf](http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/vwFiles/Research_Report_ILPs.pdf/$file/Research_Report_ILPs.pdf) (visited 1 January 2009).

⁶⁴ Total numbers of complaints are reported in the OLSC's Annual Report each year, available on the OLSC webpage: <http://www.lawlink.nsw.gov.au/olsc>.

is, and then compare the results between the two groups to see if self-assessment makes a difference. In the absence of a comparable group of incorporated legal practices that did not experience the OLSC's management-based regulation, the best test available is to compare ILPs' complaints rates with non-incorporated practices acting as the control group. This also allows us to check whether ILPs overall have an unusual complaints rates – either higher or lower – to begin with that might contribute to the apparent drop in complaints after self-assessment. For example, perhaps ILPs are a self-selecting sample of those firms that have managed themselves better anyway from the beginning and therefore have fewer complaints.

We were not able to obtain sufficient data to be able to calculate complaints rates for all non-incorporated NSW law firms per practitioner per year.⁶⁵ However we were given sufficient data to be able to calculate complaints rates between 2001 (when incorporation was first allowed) and 2008 for every non-incorporated firm in NSW that had two or more principals in 2008 - a total of 354 firms. We compared complaints rates per practitioner per year for these 354 non-incorporated firms with that of the 143 ILPs with two or more directors.

The mean rate of complaints per practitioner per year for 2001 to 2008 for the 354 *non-incorporated law firms* is 0.222 (standard deviation: 0.213).

The mean rate of complaints per practitioner per year *before self-assessment* from 2001 only⁶⁶ for the 143 *incorporated law firms* is 0.148 (standard deviation: 0.209).

The mean rate of complaints per practitioner per year *after self-assessment* for the 143 *incorporated law firms* is 0.078 (standard deviation: 0.160).

Appropriate statistical tests were used to test whether the difference between the complaints rates for non-incorporated firms compared with ILPs before self-assessment and non-incorporated firms compared with ILPs after self-assessment was statistically

⁶⁵ Relevant data about firm names and size had to be obtained from the Law Society of New South Wales who considered it unreasonable to provide us with data from all firms.

⁶⁶ In order to be comparable with the complaints rates for non-incorporated firms, we have calculated this figure this time for data from 2001 only for the practice only not including checks of the individual directors. Therefore this figure underestimates complaints slightly.

significant.⁶⁷ We find that before self-assessment ILPs have a slightly lower rate of complaints than non-incorporated law firms that is statistically significant.⁶⁸ After self-assessment, ILPs have a complaints rate about one third that of non-incorporated law firms and this is statistically significant at the highest level.

These findings support the conclusion that the OLSC's self-assessment process makes a big difference to complaints rates. There is some evidence that ILPs as a group might be slightly better managed and have lower complaints than non-incorporated firms even before self-assessment, but even so, going through self-assessment makes an additional big difference to complaints rates.

Does the Higher Implementation of Appropriate Management Systems (Self-Assessed) Lead to Lower Complaints?

Finally we test whether the actual ratings that the firms give themselves in their self-assessments reliably reflect a real difference in their management systems and ethical behaviour. We use the statistical technical technique of regression analysis to do this. This allows us to test the extent to which a number of factors all explain variation in complaints rates at the same time and holding constant the effect of each of the other variables. This means that in addition to testing for the impact of rating levels on complaints we at the same time include a number of other factors as controls in our tests:

⁶⁷ Independent samples t-tests were used to test the significance of difference between each pair of results. In each case the independent samples t-test shows unequal variance and $p=0.000$. ANOVA (analysis of variance) tests comparing all three means (with separate tests using the two different measures of complaints before self-assessment) showed the same result – that there is a statistically significant difference between the means: $p= 0.000$.

⁶⁸ But note that a less inclusive way of calculating the number of complaints for ILPs before self-assessment was used here to be fully comparable with the way the same score was calculated for non-incorporated law firms. Using the more inclusive calculation used previously to compare complaints before and after self-assessment, the rate for ILPs is still lower but the difference is on the borderline of statistical significance. The complaints rate is 0.205 (standard deviation: 0.223) and the independent samples t-test shows equal variance and $p= 0.420$.

It is well known that small and medium sized practices generally receive more complaints than larger practices. By controlling for *size* in our regression tests we can test whether this is because larger firms have better management systems or because of some other reason to do with size. We use total number of practitioners as our measure of size.

We control for *location* (city, suburban or rural) because it has been suggested that legal practitioners in rural and outer suburban areas have less support and are therefore more likely to engage in unprofessional conduct, and that, in general, suburban legal practitioners are most likely to be complained about. Again, including this as a variable in our test allows us to test whether this is because of differences in management systems or some other independent reason. Because this is a variable that forms into three groups, we have to hold one of these groups constant in the regression analysis (city) and test the impact of the other two (suburban and rural).

We also control for the *change in complaints rate before or after self-assessment* since we already know that going through the self-assessment process in itself lowers complaints rates. Regression analysis allows us to test whether the effect of merely going through the process of self-assessment disappears once we take into account the self-assessed level of implementation.⁶⁹

⁶⁹ We looked at the time periods in which complaints were (or were not) recorded, careful to calculate the complaints rate as complaints per practitioner per year. The regression was run on all time periods for each firm (as the dependent variable), so both periods before incorporation and after were included. We then created a ‘dummy variable’ measuring whether the time period was after incorporation or not, and controlled for this by including scores from a selection of the self-assessment implementation criteria.

First, *we test whether the mean self-assessed implementation rate for all ten objectives as a whole makes a difference to complaints rates, taking into account all three control factors above.* Since, as we saw above, the ILPS' self-assessed rating for all ten objectives are highly correlated with one another, it makes statistical sense to add them all together into a single total mean of self-assessed level of implementation of appropriate management systems.

The results are shown in Table 6. We find that the total mean score for implementation of appropriate management systems as self-assessed makes no significant difference to complaints rates. The size (measured by number of practitioners) of a practice does make a difference to rates of complaints – with larger ILPs receiving less complaints per year per practitioner than smaller ILPs. (Table 6 shows a significant and negative association between size and complaints rates.)⁷⁰ Even taking into account all those effects, the fact that an ILP had been through the self-assessment process was a significant predictor of rate of complaints afterwards and more significant than anything else. (Table 6 shows a significant and negative association between complaints and the time period after self-assessment.)

⁷⁰ There was also some indication that suburban and rural ILPs receive more complaints per practitioner per year than city ILPs when we conducted the regression using complaints only from 2001 to 2008. The other results remained the same. Full statistics available in online research report above n 63.

TABLE 6: EXPLAINING VARIATION IN COMPLAINTS RATE BY SELF-ASSESSED LEVEL OF IMPLEMENTATION OF APPROPRIATE MANAGEMENT SYSTEMS, FACT OF SELF-ASSESSMENT AND OTHER FACTORS

EXPLANATORY VARIABLES	COMPLAINTS RATE
Change in complaints rate after self-assessment	-.25*** (-8.87)
Size (total number of practitioners)	-.07* (-2.46)
Suburban location	.05 (1.60)
Rural location	.06 (1.71)
(Constant – City)	(3.63)
Level of total self-assessment score	.02 (.59)
MODEL STATISTICS	
N=	631
Adjusted R ²	0.07
F-Value of full model	17.98***

Note: ***=p<0.005; **=p<0.01; *=p<0.05 (two-tailed). Cell entries are standardized regression coefficients with the absolute value of t-statistics in parentheses.

The test in Table 6 looks at total implementation of all ten objectives treated as one. However it may be that there are some aspects of appropriate management systems that are more important on their own in making a difference to complaints than others. In particular we expect that implementation of appropriate management systems relating to the objectives of delay, communication and costs should be most relevant to improving complaints rates because these raise most clearly the sorts of things that clients most often complain about to the OLSC.

Therefore, second, we conduct the same test using the same extra controls as above, but this time instead of looking at the effect of the overall total self-assessment score for level of implementation of appropriate management systems, *we test for the explanatory power of self-assessed level of implementation of appropriate management systems in relation to delay, costs and communication individually*. We measure implementation of these three aspects of appropriate management systems via the scores each ILP gave themselves on each of these three objectives and also by separate ‘dummy’ variables measuring whether the ILP gave themselves an under-compliant score (non or partially compliant) or over compliant score on each of the variables (fully compliant or fully compliant plus). Thus mid range

ratings were excluded from the analysis. We use these controls to isolate the effect of under or over compliance given that many ILPs rated themselves as simply compliant in the middle of the scale.

The results are shown in Table 7. We find self-assessed level of implementation of appropriate management systems related to the objectives of delay and communication makes no difference to complaints rates.⁷¹ There is some indication that implementation of systems related to costs makes a significant difference to complaints rates. Having gone through the self-assessment process is still always the most significant predictor of lower complaints rates even when we take into account all of these other factors.

Overall we have not been able to identify any effect of the actual level of self-assessment rating on rate of complaints. Rather our results strongly indicate that the mere fact of going through the self-assessment process makes a difference to ILPs' performance on complaints, regardless of the actual ratings they give themselves.

⁷¹ It makes no difference whether implementation is measured via the ILP's self-assessed score for implementation or by the dummy variables measuring under and over-compliance. It also makes no difference whether we test for the influence of these variables for delay, costs and communication individually in separate regressions or all together in one regression. In each case delay and communication make no difference. The results for the various alternative regressions are available from the first author upon request.

TABLE 7: EXPLAINING VARIATION IN COMPLAINTS RATE BY SELF-ASSESSED UNDER AND OVER COMPLIANCE IN RELATION TO COMMUNICATION, DELAY AND COSTS, FACT OF SELF-ASSESSMENT AND OTHER FACTORS

EXPLANATORY VARIABLES	COMPLAINTS RATE
Change in complaints rate after self-assessment	-.24*** (-8.75)
Size (total number of practitioners)	-.07* (-2.43)
Suburban location	.06 (1.69)
Rural location	.06 (1.80)
(Constant – City)	(9.77)
Communication – Under compliant	-.02 (-.54)
Communication – Over compliant	-.02 (-.40)
Delay – Under compliant	-.02 (-.56)
Delay – Over compliant	-.07 (-1.6)
Costs – Under compliant	.01 (.33)
Costs – Over compliant	2.18* (.03)
MODEL STATISTICS	
N=	631
Adjusted R ²	0.06
F-Value of full model	9.32***

Note: ***=p<0.005; **=p<0.01; *=p<0.05 (two-tailed). Cell entries are standardized regression coefficients with the absolute value of t-statistics in parentheses.

DISCUSSION AND CONCLUSION

The NSW management-based approach of regulating ILPs to ensure the delivery of high quality, ethical legal services in ways that suit their own practices is a ‘natural experiment’ in regulating the ethical infrastructure of legal practice. It is the first time regulators of the legal profession have sought to systematically and proactively ensure appropriate management and ethical standards for whole firms as well as individual practitioners.

We have shown that in principle there are good reasons to suppose that this management-based approach, similar to that proposed by Chambliss and Wilkins, is appropriate for the legal profession. It has the virtues of requiring legal practices to pay attention to management structures and systems to enable and ensure ethical behaviour, but at the same time being extremely flexible in allowing legal practices to build systems that support ethical behaviours from the ground up in their own ways. It does not require legal practices to put any particular and prescriptive management systems or structures in place.

We have also shown that there is compelling empirical evidence that the combination of the Australian legislation requiring ILPs to implement appropriate management systems and the NSW OLSC’s self-assessment regime for encouraging firms to actually put this into practice makes a big difference to how well these firms are managed and to lawyer behaviour as judged by complaints rates. On average the complaint rate for each ILP *after* self-assessment was one third the complaint rate *before* self-assessment. This is a huge drop in complaints, which is statistically significant at the highest level. We also find that ILPs that have gone through the self-assessment process have significantly less complaints afterwards than firms that have never incorporated – again, about a third the number of complaints. However, we find little evidence that different levels of self-assessed implementation of appropriate management systems makes a difference to complaints, suggesting that ILPs’ self-assessed levels of implementation of ethical infrastructure are not particularly reliable. The fact that an ILP has been through the self-assessment process is the most significant predictor of rate of complaints that we could identify. It appears to be the learning and changes prompted by self-assessment that makes a difference, not the (self-assessed) level of implementation of management systems.

This suggests that the OLSC's processes for educating ILPs about appropriate management systems or 'ethical infrastructure' for their firms, and ILPs' own internal process of assessing themselves and seeking to implement and maintain appropriate management systems, have a very good impact. This is very promising for the possibility that this type of approach – even at a voluntary and educative level – may be very useful for all firms, not just incorporated firms, and possibly for firms in other jurisdictions. Indeed there was some suggestion at the time that these requirements were introduced for NSW incorporated legal practices that they should be applied to all legal practices, not just those that are incorporated,⁷² and at least one other Australian regulator of a state legal profession is considering applying these requirements to all firms.⁷³ In England and Wales firm-based requirements will apply to all firms, not just alternative business structures, although it is unclear at present how similar the English approach will be to the NSW one. Would transferring this approach to other, non-incorporated, law firms, or in other jurisdictions outside NSW, obtain the same results in driving down complaints as were achieved in NSW?

It may be that the management of many legal practices has been quite poor in the past – especially bearing in mind that most ILPs are quite small practices that may not have had any reason to seriously think about their management practices before incorporating. Even though the ten objectives that form the basis of the self-assessment are reasonably basic, many firms and practitioners may not have consciously and systematically thought them through beforehand. The OLSC's self-assessment process may well be guiding, encouraging and requiring many practitioners to do this for the very first time – and thereby achieving significant results on complaints.

This would confirm the idea that where there is an industry that has historically had little pressure to worry about good management, management-based regulation might be quite effective, at least early on, in driving dramatic changes. It would indicate that expanding the program to other law firms in NSW might be very useful. It would also be very useful in other jurisdictions where there is evidence from complaints that standards of management in many firms could be improved. However, at some stage the overall standard of management practices in law firms might improve significantly – and then

⁷² G. Dwyer, 'The business of ethics' (2003) *Law Society Journal* 38 at 38.

⁷³ J. Briton & S. McLean, above n 25.

the OLSC would need to tweak their regulatory strategy to keep challenging firms to improve further in specific areas where improvements can still be made, or to pull back from an essentially educational task that has been completed.

One possibility is that the mere fact that ILPs have taken advantage of the opportunity to incorporate might indicate that ILPs are managed by lawyers who have decided to think more carefully and strategically about how to continuously improve their legal practices than other lawyers. Indeed for a pre-existing firm the process of incorporation is itself a disruption in the way it is managed. The incorporation process is likely to involve obtaining external advice on accounting, governance and management from accountants, the Law Society, the OLSC itself and, in some cases, management consultants. It will also involve many internal conversations and changes in the way the firm operates. So we might expect most firms that incorporate to go through a process of management change and improvement that would inherently lead to lower complaints rates than other legal practices. This would suggest that it might not be so easy to prompt the same dramatic improvement in other firms' ethical management and behaviour if they have not already chosen for themselves to make the changes associated with incorporation.

On the other hand we see such a dramatic change in complaints rates in relation to the date of self-assessment (which might have occurred some time after incorporation) that it is reasonable to conclude that a big change occurs because of the self-assessment requirement itself. It may be that firms that take the step of incorporation are ripe for that change. They may have already been very willing to revisit and improve their management systems. But nevertheless the evidence indicates that the way the OLSC steps in and guides them in this process through its self-assessment guidance document and phone and letter communications with firms going through incorporation self-assessment significantly improves the outcome. A regulator might have to work harder – more publicity and more external practice reviews – to show it is serious about effective ethical infrastructures to capture the attention of firms that are not already going through the change process of incorporation and to prompt dramatic change. But the evidence reported here suggests that it may well be worth it.

Another factor that was probably key to the success of the NSW system and may not be easily repeatable elsewhere is the fact that it was implemented by a completely independent regulator who has a reputation for being effective and trustworthy in the

way it carries out its task enjoys an excellent relationship with legal professional associations, consumers and other stakeholders. This means the regulator was able to develop and implement this new regulatory strategy in a consultative way and to quickly obtain the trust of most firms involved that it was a useful and appropriate process. In jurisdictions with larger professions or where there is more of a history of tension between the regulator (whether an independent regulator or a self-regulator) and segments of the process, this type of largely educative, capacity-building approach might be very difficult to pursue successfully without major change to the overall environment of regulation.

Finally, one area that deserves further, more specific attention is legal practitioners' ethical duties to the court and the law in the litigation and alternative dispute resolution context. Our tests of the impact of the OLSC's management-based regulation approach are based primarily on client complaints. Complaints rates tell us mostly about client satisfaction. They are less informative about other ethical issues that are of less concern to clients, especially where lawyers breach their duty to the court and the law to a client's benefit. Further investigation is necessary to see whether implementation of appropriate management systems addresses the (probably) less frequent but potentially most complex and difficult ethical problems of lawyers breaching their duty to the court and the law in the interests of clients for example by misleading the court in litigation or the other side in alternative dispute resolution. This is one area where it might be useful for the OLSC to develop some more specific guidance for legal practices who do lots of litigation and dispute resolution work about what they might do to ensure high ethical standards.⁷⁴

⁷⁴ See Briton & McLean, above n 25.