NATIONAL LEGAL PROFESSIONAL REFORM

RESPONSE TO TASKFORCE DISCUSSION PAPER ON BUSINESS STRUCTURES "LAW PRACTICES"

This response to the Taskforce's 25 November 2009 paper on *Business Structures - "law practices"* has been approved by the following members of the Consultative Group:-

Tony Abbott - Lawyer, Law Society of South Australia

Barbara Bradshaw - CEO, Law Society of NT

Joe Catanzariti - President, Law Society of NSW

Harold Cottee - General Manager, Professional Standards, LIV

Noela L'Estrange - CEO, Queensland Law Society

Martyn Hagan - CEO, Law Society of Tasmania

Philip Selth - Executive Director, NSW Bar Association

Dudley Stow - Immediate Past President, Law Society of Western Australia

Context

1. In terms of the size of the profession, the legal profession is already the most heavily regulated profession if not industry in Australia. Further, the level of regulation goes considerably beyond the level of regulation anywhere else in the world.
2. The data shows the vast majority of lawyers in Australia practice in small firms. The degree to which they operate as Incorporated Legal Practices (ILPs) varies substantially between states.
3. The general statements in the introduction section of the discussion paper indicate that there is an ongoing issue with the extent to which business structures are being used by lawyers to limit the extent of their professional responsibilities and liabilities. As with many of the papers produced for comment, there is no evidence of this. It also does not appear to be an issue of substance in the Annual Reports of the various legal regulatory bodies. Whilst lack of evidence may be related to the speed of this reform process, it is not a good basis of making legislative and regulatory change. Some clear view of the need for reform, and the issues to be addressed is part of sensible and meaningful consultation.

What needs to be regulated?

4. Whilst there is now the ability to use a variety of business structures to conduct a law practice, the most consistent standard for the hierarchy of obligations of lawyers can be found quickly and non-controversially, in the Australian Solicitors' Conduct Rules and in the Australian Barristers' Conduct Rules. These documents clearly set out the professional obligations of an Australian legal practitioner. If these Rules are accepted and referenced as part of the regulatory regime, which has been proposed by the Task Force, then for consistency and clarity, they should not be re-stated or summarized in the legislation.

5. It should also be noted that very few of the ILPs in Australia are publicly listed. Even if that position alters, the Conduct Rules ought still to be the reference point for the statement of legal practice professional obligations.

Barristers

6. The Bar in Australia operates as independent sole practitioners. The definitions and the proposals in this paper do not recognize that fact, which is written about business structures that only relate to solicitors. The definitions in the Draft Bill must exclude barristers from the definition of a "law practice".

Lack of Regulatory Funding Information, Statistical or other Information

7. This paper exhibits the same flaw as its predecessors in that it is difficult to validate the proposals in the absence of first, any relevant statistical or other information and secondly, the financial costing associated with either current or prospective regulatory activities.

8. We agree with the proposal that the legal professional obligations should apply to all practice principals. We therefore propose that Principle 2 should read:

   "***Each law practice, regardless of business structure***, must have at least one Principal who has an unrestricted practising certificate (i.e a "legal practitioner director" or a "legal practitioner partner").

9. The drafting of Principle 3 requires review. Deeming provisions may be a breach of some States' Fundamental Legislative Principles (see, eg the Queensland Legislative Standards Act 1992).

10. Principles 7 and 8 introduce unnecessary regulatory and cost burdens (**emphasis added**):

Principle 7: If the Board considers it necessary to do so, the Board may conduct an **audit** of the compliance of a law practice with the National Law or the National Rules, and the management of the provision of legal services by the law practice.

Principle 8: If the Board considers it necessary to do so, the Board may require a law practice to:

-ensure that an **appropriate management system** is implemented and maintained to enable the provision of legal services by the law practice in accordance with the National Law, National Rules and the professional obligations of legal practitioners within the law practice; and

-provide **periodic reports** on its compliance with the appropriate management system.

11. The Task Force "...proposes a new system that applies consistent standards to law practices of all kinds, while seeking to ensure that legal service providers cannot hide behind the corporate veil"[1].

12. We are concerned that the Board appears to be given the responsibility for operational matters. This does not accord with our understanding of how the proposed model of the Board and a National Legal Services Commissioner would work in practice. The NLSC would be responsible, through the appropriate State and Territory Regulatory Authorities, for the compliance operations of the regulatory system. If the Board's responsibility is standard setting and oversight of the system, it should receive appropriate reports on compliance from the NLSC, rather than undertaking these activities itself. It should remain at arm's length from the compliance and regulatory work. We would be particularly concerned at the potential for the need for additional resources and associated costs, if the Board was to be practically involved in regulatory activities, in addition to the NLSC.

13. The reason for the current regulatory obligations imposed upon ILPs and MDPs under the Model Bill was to extend to the corporation, in its capacity as a separate legal entity, the "professional obligations" that already applied to Australian Legal Practitioners. The ILP was required to address these obligations in part by having in place "appropriate management systems", which in turn were designed to balance the potential limitation on liability of the principals in a corporation. There is no demonstrated need to extend this requirement to partnerships, which do not enjoy the potential limitation on liability, and which have limitations on the persons who may be partners.

[1] Under the heading "Introduction"

14.Under the Model Bill, to ensure that an ILP or MDP was complying with its professional obligations including having "appropriate management systems", the regulator was provided with the power to conduct compliance audits. In New South Wales and Queensland this power vests with their respective Legal Services Commissioners.

15.Principles 7 and 8 would result in the introduction of regulatory mechanisms applicable to all law practices, namely the "audit" and "appropriate management system" regime that had originally been introduced to address the perceived ILP and MDP regulatory gap.

16.The allusion to the "success" of this approach[2] in respect to ILPs and the assertion that "...there has been a concerted call for it to be used to assist all law practices", are based on limited research in Australia, and would not appear to support the proposed extension of substantially intrusive powers to regulators across Australia.

17.The reach, scale and overlapping nature of this proposal is highlighted by the definition of "law practice" under section 1.2.1 of the Model Bill, which is to be adopted "with some additions to the definition"[3] by the new legislation:

(a) An Australian legal practitioner who is a sole practitioner; or,

(b) a law firm[4]; or,

(c) a multi-disciplinary partnership; or,

(d) an incorporated legal practice.

18.To impose the additional obligations set out in Principles 7 and 8 upon the many thousands of non incorporated law practices whose participants are required to observe their professional and other conduct obligations anyway is clearly unwarranted.

19.We do not agree that the Board – or even the National Legal Services Commissioner – should be auditing the "management of the provision of legal services by a law practice". This has the potential to interfere at a micro level in the running of a business, and is fraught with difficulty, as the size and experience of practices are widely variable. Additionally, in some states, the regulatory personnel would not have the skills to make any form of useful contribution to an audit of management practices in any law firm, let alone a sophisticated law firm. This would apparently mean recruitment of more staff and more expense; or alternatively, an incompetent use of the proposed power.

20.This proposal is also seriously at odds with the expressed desire to reduce compliance costs and a clear instance where its regulatory burden, impact and cost must be assessed and taken into account

[2] Paragraph 3 on page 5 under the heading "Guidelines"
[3] Paragraph 1 page 6
[4] meaning partnerships

before any decision is made. One of the clear pieces of evidence which is not used anywhere in this, or other discussion papers is the actual number of complaints received by the current regulatory authorities. As a percentage of the number of firms in practice, or by reference to the number of PC holders, the complaints lodged is below 5%. This percentage reduces dramatically if one applies the equation to the number of files or transactions under management by each PC holder. This is not a system in which the profession is riding roughshod over the needs of clients or the public in a way which demonstrates any need for an increase in regulatory and compliance requirements.

21. Australian law firms are predominantly small businesses, and should not be subject to compliance requirements which make running that business too difficult. There are significant access to justice issues if small businesses in remote, rural and regional parts of Australia close their doors.

22. We recognise that risk management, improved practice management and a sound understanding of applied ethics will support improved practice. However, we consider that this ought to be the primary work of the profession, through its membership services organisations. Indeed, the requirement of compulsory Professional Development in areas such as Ethics, Risk Management and Practice Management are now consistently applied across all jurisdictions, and made available through the professional organisations, who have established – and in many cases, quite sophisticated - processes for the design, development and delivery of this learning. Some PI insurers are also very active in the area of practice risk management, including, in some jurisdictions, undertaking extensive risk management workshops in practices across the State. This reflects in the potential for lower PI premia, and again, ought to be treated as a business consideration, rather than a regulatory one.

23. Whilst the regulator would be welcome to assist the profession in "getting the message" across, and giving the profession information about the trends of complaints lodged, we do not agree that the Regulator should be empowered to conduct audits of practitioners on the basis of preventative intervention, including audits of "the management of the provision of legal services by a law practice".

Conflicts of interest

24. We agree that the prohibition outlined in S2.7.4(3) should be retained, and extend to all practices. There is also a view that certain activities should be specifically prohibited. We would support the continuity of prohibition of managed investment schemes, and consider that mortgage financing should also be specifically prohibited.

Offences

25. Logically, offence (3) should extend to all law practices. However, from a practical perspective, it was considered necessary in the context of ILPs and MDPs to prevent interference by other directors/partners in the legal practitioner director's/ partner's discharge of their professional obligations. We consider it unlikely that such interference would occur in a legal partnership, but would not object to it being an offence.

Pro bono

26. We agree that the Model Bill provision relating to pro bono be retained.