

The Corporatisation of Law Firms - Conflicts of interests for Publicly Listed Law Firms

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Over the past few years the legal profession in New South Wales has undergone a formidable change in both size and structure. Traditionally, solicitors in NSW practiced as sole practitioners, or in partnership with other lawyers and this remained the dominant legal structure for many years. Since July 2001 however, there has been a notable move away from the traditional sole practitioner structure toward more innovative structures such as incorporated legal practices and multidisciplinary practices. The reason for this move is largely as a result of a growing perception that the traditional structure of law firms no longer meets the needs of many practitioners. Statistics from my office show a steady stream of NSW firms have been incorporating since 2001. At present the total number of ILPs in NSW as at 21 September 2007 is 749.

As the first jurisdiction in Australia and indeed the rest of the (common law) world to permit incorporation (including multidisciplinary practices) under the Corporations Law, incorporation created a number of unique regulatory challenges for my office. One of the biggest challenges as a regulator of legal practitioners is ensuring that the legal profession maintains its ethical responsibilities and duties in spite of possible conflicts that may arise. Our hope has been to achieve a balance between commercialism and professionalism, and provide consumer protection. Through the implementation of an education towards compliance strategy we have been able to successfully maintain this balance. In May this year however, the listing of a law firm, Slater & Gordon on the Australian Stock Exchange (ASX) added another dimension to the legal services market in Australia and raised additional uncharted pathways for my office to contemplate.

The public listing of Slater & Gordon raised the fundamental concern about the tension between a practitioner's duties owed under the *Legal Profession Act 2004 (NSW)* (LPA) and the requirements of a director, officer or employee under the *Corporations Act 2001 (Cth)* (Corporations Act). In stark contrast to the obligations under the LPA 2004, the Corporations Act advocates for the paramountcy of the rights and protection of shareholders. Accordingly, there is a latent tension between a solicitor director's duties to a company's shareholders and a solicitor's professional obligations. Professionalism speaks of ethically minded conduct and duties to the court all of which may be antithetical to business objectives.

While it may be the first law firm to list, Slater & Gordon will not be the last. Following Slater & Gordon's successful listing, Integrated Legal Holdings in Western Australia

listed on the ASX on 17 August this year. Other firms and consortiums have expressed a similar interest in listing and have had informal discussions with my office concerning the possibility. Interest in public listing is not however just limited to Australia. Both the United States and the United Kingdom have expressed an interest in the corporatisation of law firms, however not without significant controversy.

Incorporation in New South Wales

On 1 July 2001 the *Legal Profession (Incorporated Legal Practices) Act 2000* ("the 2000 Act") and the *Legal Profession (Incorporated Legal Practices) Regulation 2001* ("Regulations") came into force in New South Wales. The 2000 Act and Regulations enabled providers of legal services in NSW to incorporate by registering a company with the Australian Securities & Investment Commission (ASIC). Similar provisions are also included in the *Legal Profession Act 2004* (LPA 2004), which superseded the 1987 Act. Once registered with ASIC, the rules that govern the framework of an incorporated legal practice (ILP) are found not only in the company's constitution, the LPA 2004 but also in the Corporations Act.¹

Pursuant to Part 2.6 of the LPA 2004 a legal service provider is permitted to incorporate and provide legal services either alone or alongside other legal service providers who may, or may not be "legal practitioners." The primary structural requirement of an ILP is that at least one legal practitioner director must be appointed.² The legal practitioner director is generally responsible for the management of the legal services provided in NSW by the ILP. The legal practitioner director is defined as a director of an incorporated legal practice who is an Australian legal practitioner holding an unrestricted practicing certificate. Section 142(2) provides that it is an offence if an incorporated legal practice does not have any legal practitioner directors for a period exceeding seven days, and unless a legal practitioner director is appointed by the Law Society, the ILP must cease to provide legal services.

As stated at the beginning of this paper OLSC statistics show a steady stream of NSW firms have been incorporating since 2001. Based on last years' Law Society figures, there were 4278 firms in New South Wales (including both traditionally structured firms and ILPs) as at December. Assuming little movement in this figure, we can estimate that ILPs now compose about 18% of all firms in NSW (up from 16% in January 2007). We understand that this figure is similar for other States that have now legislated to allow incorporated legal practices. At the time of writing these notes there are 43 multi-disciplinary practices in New South Wales, and the number appears to be decreasing.

Challenges of regulating an incorporated legal practice

The advent of incorporation has brought many practical and philosophical challenges for my office as the regulator of the legal profession in New South Wales. One of the main concerns my office had of incorporation was the added responsibilities imposed on legal practitioner directors of incorporated legal practices.

¹ The Corporations Act 2001 (Cth) was previously known as the "Corporations Law."

² Section 140(1) of the LPA 2004.

The principal legislation governing the legal profession in New South Wales is the *Legal Profession Act 2004 (NSW)* (the LPA) and the *Legal Profession Regulations 2005*. Section 143 of the LPA 2004 provides that Australian legal practitioners, who provide legal services on behalf of an incorporated legal practice in the capacity of an officer or employee of that practice, maintain the professional privileges of an Australian legal practitioner and must therefore comply with their usual professional obligations.

In addition to the normal duties owed by partners and employed solicitors the LPA 2004 and the Regulations provide for additional responsibilities for legal practitioner directors of ILPs. The additional responsibilities include:

- (i) A general responsibility on the solicitor director for management of the legal services provided by the incorporated legal practice - this responsibility probably does not extend beyond those general responsibilities that partners have to the general management of their partnership.
- (ii) The implementation and maintenance of "appropriate management systems" to enable the provision of legal services in accordance with the professional obligations of solicitors and the other obligations imposed by or under section 140(2) and (3) of the LPA 2004. Failure to implement and maintain "appropriate management systems" is declared to be professional misconduct.
- (iii) A responsibility to report to the Law Society any conduct of another director of the practice that has resulted in or is likely to result in a contravention of that person's professional obligations or other obligations imposed by or under the Act.³
- (iv) Report to the Law Society any professional misconduct of a solicitor employed by the practice.
- (v) An obligation to take all action reasonably available to deal with any professional misconduct or unsatisfactory professional conduct of a solicitor employed by the practice.⁴

While the Law Society provides general information to the potential ILP about the advantages and disadvantages of incorporation, this does not extend to any specific due diligence. The Law Society role extends only to ensuring that certain documentation (including a certificate of incorporation, a certificate of insurance and a company search which reveals the appointment of at least one solicitor director with an unrestricted practising certificate) is produced.

However, the OLSC has worked closely with the Law Society, LawCover, the provider of professional indemnity insurance in New South Wales, and the College of Law, the largest provider of continuing legal education in New South Wales, to develop an educative programme to assist legal practitioner directors to comply with their professional responsibilities.

The OLSC has, in practice, by agreement with the Law Society, assumed the role of auditing ILPs for compliance with the LPA and Regulations pursuant to sections

³ Section 140(4) of the LPA 2004.

⁴ Section 141 of the LPA 2004.

140(3) and 670 of the LPA. The test for compliance is found in part in s 140(3) of the LPA, which provides that a legal practitioner director must ensure that “appropriate management systems” are implemented and maintained by the ILP. Failure to do so is capable of being professional misconduct.

The LPA does not define “appropriate management systems.” Accordingly, the OLSC collaborated with the Law Society, the College of Law and LawCover to determine the objectives to be met to help ascertain whether an ILP has “appropriate management systems” in place. The approach formulated is an “education towards compliance” strategy in which ILPs must show that they have procedures in place which evidence compliance with what the OLSC considers to be the ten objectives of a sound legal practice.

The ten objectives or “ten commandments” as they have become known, are as follows:

1. Competent work practices to avoid negligence
2. Effective, timely and courteous communication
3. Timely delivery, review and follow up of legal services to avoid instances of delay
4. Acceptable processes for liens and file transfers
5. Shared understanding and appropriate documentation from commencement through to termination of retainer covering costs disclosure, billing practices and termination of retainer
6. Timely identification and resolution of the many different incarnations of conflicts of interest including when acting for both parties to a transaction 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 which includes minimising the likelihood of loss or destruction of correspondence and documents through appropriate document retention, filing, archiving etc and providing for compliance with requirements as regards registers of files, safe custody, financial interests
8. Undertakings to be given with authority, monitoring of compliance and timely compliance with notices, orders, rulings, directions or other requirements of regulatory authorities such as the OLSC, Law Society, courts or costs assessors
9. Supervision of the practice and staff
10. Avoiding failure to account and breaches of s61 of the Act in relation to trust accounts.

To enable legal practitioner directors to assess their management systems, a standard “self-assessment” document has been developed and is sent to all legal practitioner directors as part of the impending ILP review programme. The self-assessment document contains concepts to consider when addressing each of the ten objectives and then examples of what an ILP *may* do to evidence compliance with each of the objectives. For example, under the objective of maintaining “competent work practices to avoid negligence,” a concept to consider is that, “fee earners practise only in areas where they have appropriate competence and expertise.” The self-assessment document then suggests that an example of a procedure that will evidence compliance is that there is “a written statement setting out the types of matters in which the practice will accept instructions and that

instructions will not be accepted in any other types of matters.” The self-assessment document also contains a column within which the legal practitioner director can rate the ILP’s compliance with each of the ten objectives as either “Compliant,” “Non-Compliant” or “Partially Compliant.”

A second major concern my office had of incorporation was the perceived conflict of economic versus ethical issues. In a corporate structure, directors have an overriding duty to the company and its shareholders. This is an unfamiliar concept for lawyers because in a partnership, a partner’s overriding duty is to the court. This dilemma was effectively overcome in 2001 in the drafting of the legislation permitting incorporation, which explicitly provided pursuant to section 47S that where there was an inconsistency between the *Corporations Act 2001 (Cth)* and the *Legal Profession Act 1987 (LPA 1987)*, the LPA 1987 prevails to the extent of the inconsistency.

The *Legal Profession Act 2004* attempted to incorporate the same concept by providing in section 163 that Corporations Act displacement provisions are to be established by the *Legal Profession Regulation 2005 (NSW)* (2005 Regulation). The 2005 Regulation has not however established any displacement provisions to date. This is a continuing concern for my office as a number of firms move toward listing. Specifically we are concerned of a possible tension between a practitioner’s duties owed under the LPA 2004 and the requirements of a director or officer under sections 181-184 of the Corporations Act.

Section 181 of the Corporations Act provides for example that a director or an officer must exercise their powers and discharge their duties “in good faith in the best interests of the corporation” and “for a proper purpose.” Section 182 provides that a director, officer or employee must not improperly use their position to “gain an advantage for themselves or someone else” or “cause detriment to the corporation.” Without any displacement provisions, a practitioner’s duty to the court, which must be paramount, may cause a detriment to the corporation which will breach section 182 of the Corporations Act. An example of this inconsistency could be as basic as settling major litigation in accordance with the lawyer’s duty to the court and the client but thereby causing a detriment to the corporation because of the diminution in fees earned.

The public listing of law firms

Since 2001 when the ILP amendments to the LPA 1987 came into effect, law firms were, for the first time in Australian legal history given the opportunity to list on the ASX. In March 2004, Noyce Legal, a Sydney based law firm, listed its banking and finance division of its practice on the ASX. Noyce Legal did not however list the whole firm but incorporated the division which specialised in residential mortgage processing, into National Lending Services Ltd and sold all of its shares to listed consumer finance website Infochoice.

Three years later, on 21 May 2007 incorporated legal practice, Slater & Gordon made legal and corporate history when it became the first law firm in the world to list its whole firm on the Australian Stock Exchange. The firm has more than 95 million shares on offer and another 12 million non-voting shares. Shares in the firm, issued at \$1, closed at \$1.40, on volume of 8.2 million on the first day of trading.

Following Slater & Gordon's listing, Integrated Legal Holdings (IHL), a Western Australian based law firm listed on the ASX on 17 August this year. IHL offered lawyers and non-lawyers an opportunity to invest in their firm via an Initial Public Offer (IPO) offering of 24 million shares at 50 cents each. Unlike Slater & Gordon, IHL's initial listing was not spectacular. At the close of trade on the first day of listing, a day after the ASX suffered its biggest loss in seven years, IHL shares fell to just 38c, losing about a quarter of the value in one day.⁵ Interestingly this has not prevented continuing interest in listing by other law firms, as IHL has appeared to recover some lost share price.

IHL's model is considerably different to Slater & Gordon's. IHL was formed to own and operate a number of firms under one business structure, the Integrated Legal Group. IHL plans to either purchase a law firm and merge that law firm into an existing IHL firm or acquire a firm, which continues to operate under its own business name. IHL's involvement in the latter will extend to its CFO working with each practice acquired on budget and budget performance. To this end IHL initially acquired the legal practices of two firms – Talbot Oliver and Brett Davies Lawyers. In addition to purchasing law firms, IHL is also acquiring shares in a legal information company, Law Central Co Pty Ltd. Of the opportunity to invest in IHL, Brett Davies, IHL's spokesperson, said:

“we believe that there are better ways of operating a law firm than the old partnership model...Traditionally, the ultimate aim of joining a law firm was obtaining a partnership. This meant that you spent a long time in one firm to eventually build up to that position. But eventually you retire with little value for your partnership interest. However, this structure is beginning to break down due to the X and Y generation's perspective. Often they do not want that long term tenure or the joint financial liability with other partners. So, our business plan is transforming the structure of law firms to make them more appealing and therefore fast track growth.”⁶

According to Davies there are five reasons why law firm equity partners would consider joining IHL:

1. “making a partner's interest liquid and providing ongoing passive income through potential dividends;
2. allowing equity partners to continue managing their practices but with employee share schemes to increase staff retention and hiring – rather than the traditional offer of partnerships which is less appealing to the X and Y generation;
3. facilitating growth of their practices through “tuck in” opportunities where the purchased law firms are merged into a willing existing IHL law firm;
4. enabling Integrated law firms to refer work to other Integrated practices; and
5. providing group economies of scale.”⁷

⁵ S. Moran, “New listing rocked by turbulence”, The Australian, 24 August 2007, available at <http://www.theaustralian.news.com.au/story/0,25197,22296937-17044,00.html>

⁶ “IHL – Sharing lawyers' profits”, Cover Story, The Australian Investor, 9 July 2007 available at <http://australianinvestor.com.au/magazine>

⁷ Integrated Legal Holdings Limited, Integrated Legal Holdings IPO closes early and oversubscribed”, 20 July 2007 available at <http://www.ilh.com.au/MediaCentre.asp>

Since publicly announcing a possible float, IHL has received over 89 requests from other law firms and associated businesses for information, and IHL is acting on these enquiries.⁸ IHL's latest acquisition occurred on 19 September this year when they acquired legal practice Peter Marks Succession Lawyers for \$125,000, to be incorporated into subsidiary Talbot Olivier. The move represents the company's first acquisition since its debut on the ASX last month.⁹

With the advent of Slater & Gordon's and IHL's listings, interest in the public listing of law firms is growing. Here in Australia a number of firms, both mid-size and larger have touted the idea of listing. Similar levels of interest are also being evidenced overseas particularly in the United Kingdom where new legislation soon to be enacted will allow lawyers to set up alternative business structures, with external, non-lawyer investors, go into business with other professionals in multidisciplinary "one-stop shops"; and float their shares on the stock market. The legislation will also make it possible for the partners of law firms to benefit financially from the goodwill wrapped up in their businesses (see below).

The UK *Legal Services Bill* is currently before the House of Lords and is expected to receive Royal Assent later this year. Next year could thus see the first UK firm to publicly list. This being so, moves toward flotations are being seriously considered by a number of middle-sized UK law firms. According to a survey conducted this year for *The Lawyer UK 100 Annual Report 2007*, about 30% of firms in the United Kingdom indicated that there were in favour of UK firms being free to attract external investment. A significant proportion of firms further indicated that they were either neutral to the idea or left the question blank which indicates that the eventual number in favour could possibly be higher than 30 per cent.¹⁰ The support of the new reform has led several UK firms to engage in conversations with investment houses and private equity banks about the prospects of external investment. John Young, Senior Partner at Lovells stated he 'ticked the box' in favour for the flexibility and freedom the new reform offers:

"Every other professional group has these freedoms...Why are lawyers so different or so in need of protection that they don't?"¹¹

U.S. firms with London operations and international offices are following the Legal Services Bill with much interest. New York legal consultant Bruce MacEwen said that if U.K. firms begin going public, U.S. firms may push for similar changes within two to three years.¹²

⁸ S. Moran, "New listing rocked by turbulence", *The Australian*, 24 August 2007, available at <http://www.theaustralian.news.com.au/story/0,25197,22296937-17044,00.html>

⁹ Edited announcement, "Integrated Legal acquires Peter Marks for \$125,000", *WA Business News*, 19 September 2007 available at <http://www.wabusinessnews.com.au/en-story/1/56863/Integrated-Legal-acquires-Peter-Marks-for-125K>

¹⁰ M. Byrne, "LG weighs up flotation as firms open eyes to Legal Services Bill opportunities", *The Lawyer.com*, 25 June 2007, available at <http://www.thelawyer.com>

¹¹ *Id.*

¹² L. Fortado, Slater & Gordon lifts Curtain on Global Law Firms Going Public, *Bloomberg.com*, 12 June 2007 available at <http://www.bloomberg.com/apps/news?pid=20601109&sid=aa5QVuS4JCbk&refer=news>

Challenges regulating a publicly listed law firm

As I have briefly discussed above the challenges brought about by permitting law firms to incorporate, challenges which have become all the more apparent by the listing of Slater & Gordon and IHL on the ASX.

Duty to the Court

In Australia a legal practitioner's primary duty is owed to the court. No other profession shares this duty. This poses a problem for a listed corporation whose primary duty is to its shareholders.

Realising the possibility of this conflict between the duties owed to the company and shareholders and the duties owed to the court and to clients the OLSC worked together with Slater & Gordon prior to listing to ensure that Slater & Gordon's prospectus, constituent documents and shareholder agreements dealt with the issue. As a result, the Slater and Gordon prospectus states:

The constitution states that where an inconsistency or conflict arises between the duties of the company (and the duties of the lawyers employed by the company), the company's duty to the court will prevail over all the duties and the company's duty to its clients will prevail over the duty to shareholders.

The primacy of a lawyer's duties to the court, as stated in the prospectus, is also reflected in Slater & Gordon's constituent documents and shareholder agreements.

Duty of Confidentiality

A fundamental duty owed by a lawyer to the client is the duty to maintain confidentiality. A lawyer's client is entitled to expect that all information received by the lawyer in relation to the client will be treated as confidential. Such a duty does not however attach to a business relationship. A duty of confidentiality may be part of a business relationship if included in the contract between the parties, but it is not implied into that relationship, as it is in the case of professionals and their clients. Shareholders therefore have no reciprocal commitment to maintain client confidentiality.

Slater & Gordon's prospectus covers this dilemma by explicitly stating that the lawyer has a primary duty to the client.

But what happens if Slater & Gordon are running an action against a particular individual who is very well-resourced, and that individual buys a substantial number of shares in Slater & Gordon and then demands that the action against him cease? Slater & Gordon's prospectus has attempted to address this situation by clearly stating that one of the risks of investing in the company is that it may be required to act against the interests of the shareholders.

Similarly, what happens if Slater & Gordon is obliged to disclose that they are appearing for a client but that client doesn't want Slater & Gordon to disclose the representation?

Under the Corporation's Law, a corporation is obliged to continually disclose its business and dealings. Section 674 of the *Corporations Act 2001* makes it a legal requirement for listed disclosing entities to abide by the ASX Listing Rule 3.1 on continuous disclosure.¹³ The ASX defines continuous disclosure as the "timely advising of information to keep the market informed of events and developments as they occur". The obligation of continuous disclosure is further reinforced in Principle 5 from the ASX Corporate Governance Council *Principles of Good Corporate Governance and Best Practice Recommendations* which supports timely and balanced disclosure.¹⁴ A failure to comply with the continuous disclosure requirements is an offence under s674 of the *Corporations Act* and can create a civil or criminal liability.

The obligation of continuous disclosure is based on the principle that all investors should have equal and timely access to information about a company. Pursuant to this obligation a corporation is required to notify the ASX if the corporation has information that is not generally available the information is information that a reasonable person would expect, if it were generally available, to have a material effect on the price or value of enhanced disclosure (ED) securities of the entity. The ASX requires that a corporation disclose the following information:

- "Information relating to the making of a takeover bid;
- Certain information relating to share buyback offers;
- Changes to the company's capital structure;
- Information relating to options;
- Certain information when shares in a no liability company are forfeited;
- Information relating to meetings – dates, resolutions and outcomes announcements given to investors;
- Change of contact details of the principal office or share registry;
- Other changes of substantial shareholders to the share register;
- Changes to the chair, directors, responsible entity, management company or auditors;
- Documents sent to security holders;
- Notice of directors' interests;
- Information memoranda, product disclosure statements;
- If the entity's securities are subject to ownership limits, then certain information relevant to the ownership limit must be disclosed; and
- Financial information and yearly and half yearly accounts."¹⁵

The ASX may also ask a company to clarify its position if the market appears to be moving as a result of media speculation. The obligation of continuous disclosure could thus be a problem for a corporation whose client does not wish for the corporation to disclose representation. Juxtaposed to this obligation is a lawyers duty to maintain confidentiality.

¹³ ASX Listing Rules, Chapter 3, Continuous Disclosure, available at <http://www.asx.com.au/ListingRules/chapters/Chapter03.pdf> ; ASX Guidance Note 8: Listing Rule 3.1 <http://www.asx.com.au/ListingRules/guidance/GuidanceNote8.pdf>

¹⁴ See Australian Institute of Company Directors, "Continuous Disclosure Requirements", 2 February 2006 available at <http://www.companydirectors.com.au/Policy/FAQ/>

¹⁵ Id

Once again, careful drafting of the corporations prospectus, constituent documents and shareholder agreements which explicitly stipulates that the lawyer has a primary duty to the client will hopefully address most, if not all of these problems.

In addition to the above conflicts there are other challenges that public listing has brought. The listing of law firms, for example, also raises the issue as to whether law firms actually have any goodwill. Ascertaining the true worth of a law firm is very challenging. Slater & Gordon managed to convince prospective investors that they indeed have goodwill due to their significant market standing (branding) but it is doubtful that there are many law firms that would be able to demonstrate such standing in Australia.

Slater & Gordon are a niche national firm that has built up a powerful reputation and profile in the Australian legal market. They enjoy a strong position in the personal injuries and class action litigation market in Australia. Furthermore Slater & Gordon's prospectus states that they are one of the most recognisable names in Australia and that a study commissioned in 2004 found that general public awareness of the Slater & Gordon name was 60% nationally and 83% in Melbourne.¹⁶ There are very few firms in Australia that have built up such a powerful brand.

Listing also raises concerns about its use as an exit strategy for partners/legal practitioner directors. Listing on the stock market is a great way for partners and legal practitioner directors of an incorporated legal practice to make money if they decide to leave the practice. Once all the money has been made in listing and the directors have left it is doubtful that there would be any value left for subsequent directors/shareholders.

The Slater & Gordon Prospectus attempts to placate some of these concerns by having staged processes by which the founding directors are required to stay for between three to six years to get the full economic value of their shareholding.

Another issue is the concern created by the income splitting provisions or the sharing of fees between lawyers and non-lawyers in incorporated practices in Australia and the UK. Income splitting, as known in the US, will now be available for incorporated law firms not just where those firms are multi-disciplinary but where administrative and other non-legal staff are able to purchase shares in an incorporated legal practice, which is purely a legal practice. This will produce difficulties in the US (where this practice is unacceptable) in how they characterise Australian (and soon UK) lawyers who wish to practice in America, even pro hac vice.

Corporatisation and Legal Ethics

One of the greatest concerns I had when incorporation was first permitted in 2001 was that firms would embrace corporatisation and focus more on profit than professionalism. I feared that law firms would adopt unethical business practices and the possibility of equity ownership through listing would enhance incentives for the legal profession to behave in ways that would undermine their professional obligations set out in the Act, Rules and the Regulations. My fear was not

¹⁶ Slater & Gordon Prospectus at p.10

uncommon. Similar concerns have been expressed about the possibility of incorporation thwarting the legal professions ethical obligations and responsibilities. In relation to the listing of law firms Professor Milton Regan from the United States, has for example commented:

“One concern about “practising to the share price” therefore is that lawyers may identify too closely with clients interests and will be less willing to place limits on their pursuit. That is, the problem may be precisely that the market will be too effective in aligning lawyers with clients, since that’s the path to profitability and a high share price. Playing the role of steward of the legal system may not be financially rewarding, and may in fact be financially counterproductive, in a competitive market for legal services. Lawyers may have little incentive to attend to the quality of the public good that they produce in every representation; after all, no one will be compensating them on behalf of society as a whole.

...what would be the impact of such reforms on lawyers’ ability and willingness both to place clients’ interests above financial self-interest, and to ensure that client conduct does not undermine the social capital embodied in the legal system? Expressed even more pointedly: would the existence of a share price, either shadow or actual, have any effects significantly different from the financial incentives that lawyers and law firms already face?”¹⁷

Apparently however my fears about law firms adopting unethical practices appear to be largely unwarranted.

According to the results of a study conducted by my office in conjunction with the Centre for Applied Philosophy and Public Ethics last year, complaints about ILPs have not increased in spite of their changed business practices. The study, our first major analysis of ILPs in NSW looked at the practices of a sample of 200 ILPs, which had both returned self-assessment forms and been the subject of consumer complaint. The study sought to analyse the type, size, geographic location and areas of practice of ILPs generally, and then to specifically examine whether there was a discernable link between the self-assessment process, and the likelihood of complaint.

The research revealed a correlation between very high levels of stated compliance with the ten commandments, and low levels of complaint. Those ILPs who rated themselves as being non compliant or partially compliant with three or more of the ten commandments had 45% more complaints per solicitor than those ILPs which rated themselves as compliant (or better) in respect of all of the ten commandments.

Most encouragingly from our perspective, the research revealed that 63% of ILPs were prompted to make substantive systems changes as a result of engaging in the self-assessment process. This process is therefore more than a ‘tick a box exercise’ – the research shows that the majority of legal practitioners engage in the process seriously and diligently. The imposition of a management methodology upon the delivery of legal services has enabled ILPs to provide a quality service efficiently and cost effectively, without compromising their professional responsibilities.

¹⁷ M.Regan, B.MacEwen & L.Ribstein, “Law Firms, Ethics and Equity Capital: A Conversation”, 21 Geo J. Legal Ethics (forthcoming Dec.2007) at p. 12.

Noting the benefits of the self-assessment process and the likelihood that an increasing number of firms will incorporate over the next few years, the OLSC has been working toward establishing an effective system to monitor compliance with the self-assessment programme. To this end the OLSC has worked closely with the Information Technology Services (ISB) at the Attorney General's Department to design and develop a web-based Portal for assessing compliance amongst ILPs.

One of our main objectives of the Portal is that it can be used by those other States and Territories in Australia that have permitted practices to incorporate so that a practice that operates in more than one jurisdiction will only have one system to comply with. Other objectives of the Portal are to:

- Enable the electronic submission of administrative and regulatory information by ILPs to the OLSC;
- Track the life cycle of an ILP by collating and indexing data in a searchable database;
- Allow the viewing, completion and submission of the self-assessment form and any supporting documentation online by an ILP;
- Automate the self-assessment process including validation of information submitted by ILPs;
- Enable the generation of standard and customised correspondence;
- Automate the tracking of the annual self-assessment process;
- Provide standard and customised reports for the OLSC and online distribution to other approved external parties such as ILPs, ASIC and the Law Society;
- Provide tracking of the assessment process electronically, including generating email alerts in the self-assessment process to improve monitoring of the process by both Legal Practitioner Directors and OLSC staff;
- Provide profiling to assist in the identification of suitable targets for information dissemination or audit by the OLSC;
- Enable the statistical analysis of ILP data using OLAP tools.
- Provide customisations of and alternate paths through the self-assessment and display different types of information that is relevant to ILP profiles;
- Enable electronic distribution of regulatory and educational information by the OLSC to ILPs and other interested parties via a web based portal; and
- Facilitate the adoption of good business practices and appropriate management systems through analysis of data submitted by ILPs.

At present we are working with ISB in the systems requirement analysis phase of the project. We anticipate that the construction phase will be completed in mid 2008. Following user acceptance testing and the successful completion of a pilot programme, the system should be available to all ILPs by late 2008.

Profit vs Ethics

In my view the research reveals that the oft-made distinction between ethics and profit is an illusory one. Many lawyers tell me that they feel they must choose between acting ethically and practising profitably. If legal practitioners abandon ethical standards, there will no longer be any point of differentiation between the legal profession and anyone else providing the same or similar services. Ethics are essential to the legal profession's very survival in an increasingly competitive market. Moreover, if the profession, with the supporting structures my Office provides in the form of "appropriate management systems" as based on the "ten commandments", does in fact achieve the ultimate goal of cultural change, then the issue falls away. If

all lawyers behave ethically, then there is no one for a client seeking unethical advice or services to approach.

My scepticism about how the incorporation of legal practices would play out in New South Wales has been overborne by the benefits, which sound management principles can bring to legal practice. Law can, and should, be regarded as both a profession and a business and in ILPs we witness the overt merger of the two roles. The perceived clash between duty to shareholder and duty to client has not, at this stage, given rise to the problems that such a duality might be expected to present. In fact, it seems to me that the commercial pressure brought to bear upon practitioners in a traditionally structured firm by large corporate clients to provide potentially ethically bankrupt advice in fact exceeds the pressure exerted by shareholders in search of the almighty dollar upon solicitor directors.

I say this because, with the introduction of "appropriate management systems", we have a codification of certain ethical and business principles. There will always be ethical and unethical people. What is now explicit is that "appropriate management systems" provide the framework for ethical behaviour, and they can also be enforced. In this way, it is clear that a solicitor director's duty to shareholders to return profit is in fact contingent upon the lawyer's professional duties to his or her client. Put another way, in an ILP, "appropriate management systems" (and the ethical and legislative responsibilities they encompass) can be seen as a derivative director's duty, much like occupational health and safety requirements and environmental responsibilities have come to be regarded in companies at large.