

INDEPENDENT REGULATOR OF LEGAL SERVICES POLICY OUTLINE

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INTRODUCTION

This proposal sets forth a system of regulation for legal service providers. The proposed system envisions a **non-profit, independent regulator** of legal service providers implementing a risk-based approach to regulation that seeks to advance the regulatory objective outlined below. This proposal is simply that—a proposal for which we hope to gather feedback and input from all sectors of the legal economy.

THE REGULATOR

CORE REGULATORY OBJECTIVE

To ensure consumers access to a well-developed, high-quality, innovative, and competitive market for legal services.¹

REGULATORY PRINCIPLES

1. Regulation should be risk-based (proportionate and responsive to actual risks of harm posed to consumers of legal services).
2. Regulation should be guided by a market-based approach.
3. Regulation should establish probabilistic thresholds for acceptable levels of harm.
4. Regulation should be empirically-driven.

KEY RISKS

The regulator's primary approach to achieving the core regulatory objective is through the identification and reduction of the major risks to consumers in the legal services market. We have identified five key risks:

¹ This system is designed specifically for the regulation of consumer facing legal services and targeted at the risks posed to the purchasers of legal services. Although we believe that ensuring the system protects the consumers' interests will serve the public interest, in particular strengthening the rule of law, the institutions of law, the administration of justice, and access to justice, it is not the primary objective. To the extent there are public policy goals not met by this system, it is our assumption that those goals should be addressed elsewhere in the system (*i.e.* the courts, the bar, other government regulators or legislation).

1. Consumer fails to exercise their legal rights because they did not know they possessed that right.
2. Consumer achieves a worse legal result than they would have had they used the next best alternative.
3. Consumer overpays for a legal service.
4. Consumer purchases a legal service not needed or not appropriate to their legal issue.
5. Consumer does not engage with the legal services market at all.

SOURCE OF REGULATORY AUTHORITY

1. The state courts may delegate regulatory power over legal service providers to the regulator.²
2. The state courts also may enact rules:
 - a. permitting legal entities duly licensed by the regulator to practice law in the state and ensuring that such entities will not be subject to unauthorized practice of law enforcement; and
 - b. permitting traditionally licensed lawyers to enter into business relationships of any form with duly licensed legal entities.
3. The state courts retain the duty to assess the performance of the regulator, including the continuing evaluation of the regulator's achievement of the core regulatory objective and whether further potential rule changes might be necessary to advance the regulatory objective and the public interest (*e.g.* changing rules about court appearances).

THE REGULATED MARKET

LEGAL SERVICE PROVIDERS

Those offering any service to the public that informs, advises, assists, advocates for or drafts documents for individuals and entities on the interests, rights, and obligations of such individuals and entities under the law (local, state, federal, and international).

RISK MATRIX

The regulator will develop a risk matrix around the key risks. The risk matrix should identify and assess risks in terms of their impact and probability on specific classes of consumers, thereby enabling the regulator to prioritize and categorize regulatory interventions. In this process, and in

² The delegation of authority by the state courts is limited, as we have noted, by the specific core regulatory objective. The state courts maintain the authority and duty to address issues of public interest and policy beyond consumer protection, including issues of access to justice.

light of the core regulatory objective and regulatory principles, the regulator should identify levels of tolerable risk for which hard regulatory intervention is not necessary. It should also identify those risks which are intolerable in light of the core regulatory objective and principles.

Ultimately, the regulatory matrix will be developed by the regulator through engagement with various market participants and other expert sources. The risk matrix is used by the regulator both in assessing the market as a whole (establishing status quo at the outset of the new system and continually to measure impact and assess progress market-wide) and as the framework for assessment of the risk posed by individual entities within the system during application, through monitoring, and to address enforcement). See the Risk Matrix Example at Appendix A.

THE REGULATORY PROCESS

APPLICATION FOR LICENSE

The licensing approach is guided by the following analysis:

1. What is the specific nature of the risk posed to the consumer by this business model/product/service?
2. How does the proposed business model/product/service fit into the risk matrix?
3. Can the applicant provide sufficient evidence on the risk?
4. What mechanisms might mitigate those risks and how? What are the costs and benefits of those mechanisms?

An application for licensure could have three parts.

PART ONE: APPLICANT INITIATES PROCESS

The applicant describes the business model/product/service offered. The explanation should be simple and short. The applicant should submit supplemental materials (visuals, etc.) as necessary.

PART TWO: RISK ASSESSMENT

Based on the description provided in Part One, supplemented as necessary with information requests to the applicant, the regulator initiates the risk assessment process.

With reference to the risk matrix, both the regulator and the applicant can identify the prioritized risk concerns and risk threshold requirements. The regulator shall indicate to the applicant which risks are prioritized for its particular proposal, which risk thresholds apply, and what types of quantitative or qualitative data the applicant must submit on these risks. The applicant should also

submit any information on mitigation of these risks and response to risk realization built into its model.

The second part of the risk assessment is a self-assessment in which the applicant will be expected to identify any risks to consumers not covered under part one. These may be risks specific to the type of technology proposed (the blockchain presents different concerns from a document completion tool for example), the business model, the area of law, or the consumer population targeted.

To gain a license, the applicant must, for each listed risk, show whether or how its proposed business model/product/service might trigger such risk, what processes and procedures the applicant has in place to mitigate such risk, how it might redress any harm, and any other showings required by the regulator.

The regulator shall develop a mechanism for sealed risk disclosures, to the extent any necessary disclosures around technology or other risk mitigation processes should not be public.

PART THREE: FEES

The applicant will submit licensing fees both at the outset of the licensing process and annually in order to maintain an active license. The fee regime will be developed to scale with nationwide revenues of the applicant.

REGULATOR RESPONSE: RISK PROFILE

The regulator will then use the application and its own research into such technical, economic, or ethical issues as necessary to develop an overall risk profile of the proposed business model/product/service. A risk profile is not a list of potential risks with little or no differentiation between them. The risk profile should assess the identified risks both in relation to each other (which are the most likely (common), which present the greatest financial risk, *etc.*) and in relation to the market for legal services overall. It may be that the risk profile is essentially the scoring of the applicant in the context of the risk matrix.

The risk profile should seek to make clear, to the applicant, the regulator, and the public, how this model/product/service compares to other similar services on certain key points. The risk profile will also guide the regulator in its regulatory approach going forward, *i.e.* how frequent to audit, what kind of ongoing monitoring or reporting, what kinds of enforcement tools need to be considered and which are not necessary.

It is important to be clear in this assessment that the risk profile is not being created as against a standard of “perfect legal service by a lawyer,” but rather is a tool to show the relative risk of this offering in context of the myriad other possible offerings on the market and as against the risks

imposed if a person does not have access to help at all. Such an assessment should be as empirically driven as possible.

The risk profile shall also to illuminate how different types of legal services inherently present different potential risks to the consumer. Obviously, the risks of poor legal help (whether lawyer or otherwise) in criminal case or “crisis point” civil case (eviction, child custody, *etc.*) are more significant, immediate, and difficult to remedy than the risks of poor legal help in a will drafting. We should not assume that the public knows or understands this in every case.

REGULATOR RESPONSE: DETERMINATION ON LICENSURE

After creation of the risk profile, the regulator shall make a determination on licensure. If, based on the risk profile, the regulator finds that significant risks have been identified but it is not clear how the applicant shall address and mitigate those risks, the regulator shall impose probationary requirements on the applicant targeted at those risks.

MONITORING AND DATA COLLECTION

Monitoring and collection of data enable continual improvement of the regulatory system toward the core objective. Through gathering of data and continual interaction with the regulated entities, the regulator is better able to understand risks in the market and identify trends. The regulator is also able to observe, measure, and adjust any regulatory initiatives to drive progress toward the core objective. Monitoring is not the regulator simply checking the box on a list of requirements.

The regulator could establish the requirement that regulated entities periodically and routinely provide standard harm data sets tied to the risk reduction objectives. The regulator should have the flexibility to reduce or eliminate specific reporting requirements if the data consistently shows no harm impacts on consumers. The regulator could have the authority to conduct unannounced testing or evaluation of a regulated entities’ performance through, for example, anonymous testing of software tools or services.

The regulated entities will have an affirmative duty themselves to monitor for and disclose any unforeseen impacts on consumers.

Data should also be used both for issuing regular market reports and for issuing guidance to the public and regulated entities.

ENFORCEMENT

Enforcement is necessary when the activities of licensed entities are harming consumers. The regulator takes action when evidence of consumer harm exceeds the risk thresholds identified in the risk matrix.

Evidence of harm or non-compliance can come before the regulator in a variety of ways, including:

1. Regulator finds evidence of consumer harm through the course of its monitoring, auditing, or testing of regulated entities;
2. Regulator finds evidence of consumer harm through its monitoring of the legal services market;
3. Consumer complaints; and
4. Whistleblower reports.

The regulator will develop a process for enforcement intake (complaints and funneling of information from all possible sources), investigation, and redress.

If the regulator makes a finding of consumer harm that exceeds the applicable threshold, then penalties are triggered. The penalty system should be clear, simple, and essentially automatic. If a legal service provider is unable to meet the risk threshold over a certain probationary period, then their license is suspended. To be reinstated, the legal service provider needs to provide data showing mitigation efforts and how the threshold is met. Evidence of harm at certain identified points beyond the threshold trigger monetary or other penalties, including possible revocation of license.

There should be a process for appeal of enforcement decisions, both within the regulator and to the state supreme court. The regulator should make regular reports on enforcement data and actions to the supreme court.

OTHER DUTIES

The regulator may have other duties that advance the core objective, including reporting duties to the state supreme court and the public. The reports would include the overall state of the market, risks across the market, prioritized risk areas, and specific market sectors (by consumer, by area of law, etc.). The regulator may also have the authority to develop initiatives including public information and education campaigns.