

**INCORPORATED LEGAL PRACTICES:  
DRAGGING THE REGULATION OF THE LEGAL  
PROFESSION INTO THE MODERN ERA <sup>i</sup>**

**John Briton**

**Legal Services Commissioner**

and

**Scott McLean**

**Principal Legal Officer and Practice Compliance Manager**

**Legal Services Commission Queensland**

**THIRD INTERNATIONAL  
LEGAL ETHICS CONFERENCE**

**Gold Coast Australia**

**13-16 July 2008**

Queensland's *Legal Profession Act 2007* (the Act) like its counterpart legislation in the other Australian states and territories allows law firms to structure themselves as companies and to trade as incorporated legal practices - and of course then creates the regulatory framework for the provision of legal services by (what the Act calls) incorporated legal practices. The new framework came into effect on 1 July 2007. It reflects the national model laws and is identical in all essential respects with the arrangements that have or soon will come into effect elsewhere throughout Australia.

The regulatory arrangements in relation to incorporated legal practices threaten to drag the regulation of the legal profession into the modern era by modelling new ways of monitoring and enforcing standards of conduct within the profession that we think should apply equally to all law firms, incorporated or otherwise. It's a form of regulation that includes but goes beyond the traditional complaints-based regimes that allow us as regulators to respond to alleged misconduct only on the part of individual lawyers. It recognises what ought be obvious - that the law is not only a profession but a business; that legal services are delivered by individual lawyers to be sure, but by individuals who sell their services for profit within commercial enterprises; and that law firms like other commercial enterprises have organisational and workplace cultures that shape the ethical conduct of the people who work for them, for better or worse.

It follows, it seems to us, that law firms should be capable of being held to account when the services they provide fall short of ethical expectation - not just the individual lawyers who work for them and not just incorporated law firms but all law firms.

## **THE LIMITATIONS OF COMPLAINTS-DRIVEN PROCESSES FOR ENFORCING PROFESSIONAL STANDARDS**

Traditional complaints-driven regimes for monitoring and enforcing standards of conduct have some significant limitations, not least the following:

### **a) complaints-driven processes focus exclusively on the conduct of individuals**

Traditional complaints-driven regimes for monitoring and enforcing standards of conduct confine our gaze as regulators solely to the conduct of individual lawyers. They ignore the reality that their conduct is a function in part at least of the workplace cultures of the law firms within which they work, as if that isn't true - or as if it's irrelevant even if it is. They

give us a means of identifying and dealing with the ‘bad eggs’ in the profession but leave incubator law firms off-limits.

How can this be? It’s obvious that “law firm policies and procedures, both formal and informal, create economic and social incentives for individual conduct” and that “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.”<sup>ii</sup>

Clearly it’s important that law firms have policies and procedures that explicitly promote compliance with ethical standards. It’s even more important, however, because policies and procedures can be as honoured in the breach as the observance, that law firms have an ethical workplace culture. There is good empirical evidence that an organization’s culture has a greater impact on its ethical performance than its organizational structure and policies and procedures<sup>iii</sup> and that “it’s not enough to have policies. It’s not enough to have procedures. It’s not enough to have good intentions. All of these can help. But to be successful, compliance must be an embedded part of [a] firm’s culture.”<sup>iv</sup>

The research findings to that effect make good intuitive sense. We all know of managers who boast about their open door but who never seem to notice how few of their employees ever come on in. We all know of organizations that boast best practice policies and procedures in relation to whistle blowing and workplace bullying, including obviously policies that prohibit retaliation against employees or clients who blow the whistle or complain, but where no one ever dares to blow the whistle or complain for fear of retaliation. And we all know about Enron and the triumph of form over substance that happened there.

It follows, if we’re serious about improving standards of conduct within the profession, that we should pay serious attention to scrutinising not only how individual lawyers conduct themselves and to their character and values and professional competence and skills but also to their workplace cultures and the ‘ethical infrastructures’ of the law firms that employ them. We should pay serious attention to their firm’s formal policies and procedures but recognise that their conduct will be shaped by other influences, too.

A firm’s policies and procedures describe its intentions, or in the worst case scenario only what its leaders say their intentions are, and may bear little if any resemblance to what actually happens in practice. And so we should also and just as importantly pay attention

to the myriad other factors that influence what actually happens – the unwritten rules and ways of doing things, the values, customs, practices, management behaviours and patterns of incentives and disincentives explicitly stated or otherwise that motivate and sustain the firm's lawyers to conduct themselves ethically or, alternatively, that leave them to their own ethical devices or worse, by actually encouraging them to conduct themselves unethically.<sup>v</sup>

It puzzles us that the traditional complaints-based approach to enforcing professional standards makes individual lawyers solely responsible for their conduct and absolves their law firms a priori. The laws that regulate the professional conduct of lawyers stand in stark contrast in this respect to the laws which regulate our workplace conduct more generally and that are intended to set a standard. The laws in this and every other state and federally in relation to sexual harassment, for example, make employers vicariously liable for the proven misconduct of their employees and agents unless they can prove they took all reasonable steps to prevent the conduct from occurring.

We can see no good reason why law firms shouldn't be similarly capable of being held to account for the unacceptable conduct of their employees, especially when there is reason to believe that a firm effectively condoned or tolerated such conduct, much less encouraged or expected it.

**b) complaints-driven processes are highly selective in their application**

Lawyers who do residential conveyances and family law or personal injuries or deceased estates work are many times more likely to find themselves subject to complaint than lawyers who do commercial litigation or banking or building and construction law. Similarly lawyers who work in sole practice or small law firms are many times more likely to find themselves subject to complaint than lawyers who work in medium sized and larger law firms – to the extent that lawyers who work in medium sized and larger law firms are only nominally subject to any statutory oversight and in reality are almost entirely self-regulated, whether by their own consciences and character or their law firm's systems and processes or both.<sup>vi</sup>

There are good public policy reasons why the individual clients of mainly modest means who use the services of small law firms for their family law matter or the purchase or sale of their family home or their claim to be compensated for a personal injury should have a

priority claim on our services and we should be unapologetic that they do. They are less well equipped to look after themselves when they believe their lawyer has given them less than a good or a fair deal than the wealthier, more sophisticated and typically corporate repeat clients who use the services of the larger law firms.

We shouldn't ignore the larger law firms even so, or other areas of law. We have a consumer protection role, to be sure, but we have an equally fundamental role to promote and enforce professional standards in the profession generally – and we can't assume for a moment that the complaints data is a measure somehow of the prevalence or distribution of misconduct within the profession. We can't take it to mean that lawyers who do commercial litigation work and the like or who work for medium-sized and larger law firms are more ethical or have higher standards of conduct than lawyers who do conveyances or work in sole practice or small law firms. There is no good reason to believe that.<sup>vii</sup>

Those are ultimately empirical questions of course and there has been precious little empirical research, certainly in Australia, but the evidence from the North American context is troubling.<sup>viii</sup> The indirect evidence - the evidence of the damage that can be done to workplace cultures and to individual professional standards by unreasonable pressure to meet unrealistic billings targets, for example, or by performance against billings targets becoming an 'all purpose' performance measure for promotion and other purposes - is positively sobering.<sup>ix</sup>

**c) complaints-driven processes focus exclusively on minimum standards**

Complaints-driven regimes confine our gaze equally to the very merest of minimum standards – the point at which conduct becomes 'unsatisfactory professional conduct' or worse and stands to attract a disciplinary sanction. Ethical lawyers set their sights higher than trying not to fall below or just treading the line. There is more to acting well than not acting badly. We can exhort as much as we like, but it would be nice as regulators to have some power to set our sights higher than the merest of minimum standards, and to set the profession's sights higher too.

**d) complaints-driven processes are almost entirely reactive**

Finally, complaints-driven regimes confine our gaze to the past - they are inherently reactive. Again as regulators we can exhort as much as we like but our powers in relation to complaints are confined to dealing with things only after the horse has bolted – only after some conduct has occurred and given rise to complaint or, in the case of ‘own motion’ investigations, which give us at least a measure of pro-active capacity, still only after some conduct has occurred that causes us to have reasonable suspicions. Imposing disciplinary sanctions for proven misconduct sends a message, of course, and hopefully has a deterrent effect, but it would be nice to be able to get in first and to do something constructive to prevent it.

Surely we can do better. The framework for regulating incorporated legal practices shows us how. It focuses on the future, not just the past; on doing the right thing, not just avoiding the wrong thing; on all incorporated law firms, not just a sub-set of firms; and it puts law firm culture at the very front and centre of the regulatory regime.

### **THE FRAMEWORK FOR REGULATING PROFESSIONAL STANDARDS IN INCORPORATED LEGAL PRACTICES**

Obviously we will regulate the provision of legal services by incorporated legal practices in part at least in exactly the same way we regulate the provision of legal services by any other law practice – by responding to complaints about or, if we suspect all is not as it should be, by initiating ‘own motion’ investigations into the conduct of the lawyers who work for them including their legal practitioner directors.

Notably however the Act requires incorporated legal practices to have at least one legal practitioner director and it imposes obligations on legal practitioner directors over and above their ordinary professional obligations as lawyers, not least:

- to “keep and implement appropriate management systems to enable the provision of legal services by the practice under the professional obligations of Australian legal practitioners and other obligations imposed under this Act”;
- to take “all reasonable action” to ensure that practitioners employed by the practice comply with their professional obligations, and to take “appropriate remedial action” in the event that they don’t including “all reasonable action... to deal with any

unsatisfactory professional conduct or professional misconduct of a legal practitioner employed by the practice”; and

- to ensure that the conduct of other, non-legal directors does not “adversely affect the provision of legal services by the practice.”<sup>x</sup>

Legal practitioner directors who fail to take “all reasonable steps” available to them to meet their obligations in this regard can be found guilty of unsatisfactory professional conduct or professional misconduct for that reason, and for that reason alone.

We will respond to complaints about and initiate own motion investigations in relation to the conduct of legal practitioner directors in relation to their additional obligations under that guise in exactly the same way we respond to complaints and initiate own motion investigations in relation to their professional obligations more generally.

Crucially, however - and this is the power that promises to drag the regulation of the profession into a new era - the Act empowers us to “conduct an audit [a compliance audit] of an incorporated legal practice about:

- the compliance of the practice, and of its officers and employees, with the requirements of [the Act] or a regulation, the legal profession rules or the administration rules so far as they apply to incorporated legal practices; and
- the management of the provision of legal services by the incorporated legal practice, including the supervision of the officers and employees providing the services”;

and it allows us to conduct an audit “whether or not a complaint has been made.”<sup>xi</sup>

The Act is silent about how we should go about conducting compliance audits other than requiring us to give the firms we audit a report of the audit.<sup>xii</sup> Notably however it gives us all the same and more powers in relation to compliance audits than we have in relation to complaints and investigation matters - powers to require reasonable help and cooperation in conducting an audit, to require the production of documents and information, to enter places including if needs be by warrant, to examine books, to seize evidence, to examine persons and to hold hearings.<sup>xiii</sup>

### **Appropriate management systems**

Incorporated legal practices are likely to have little in common if anything but for being incorporated - they will vary significantly in size; in the legal services they provide; in the business services they provide in addition to legal services, if any; in the composition of their boards, and so on. It might be tempting to conclude that appropriate management systems will have little in common either.

Of course it's true that a firm's management systems will only be 'appropriate' if they're appropriate to its own individual circumstances and are likely for that reason to be different from the management systems that are appropriate for other firms. But they will have to be appropriate in another sense, too, to count as appropriate management systems in this context and in a sense that gives the term 'appropriate management systems' a common defining characteristic whatever a firm's circumstances.

Management systems count as appropriate in this context only by reference to the purposes they're intended to achieve and, even more fundamentally, by the impacts and outcomes they do in fact achieve. We're regulators, not management consultants, and we're interested not in systems per se but in conduct – in how a firm's systems play themselves out in practice, and in certain aspects of practice at that.

A firm's management systems won't count as appropriate whatever their purposes if they're applied only sometimes and not others or are applied differently by different of its employees people at different times or because the people 'down the line' don't know about them or understand them or worse still just don't care. And they might be designed to achieve and might in fact achieve any number of worthy management purposes but they'll count as appropriate management systems not because they enable the firm to be more business like or profitable, for example, or to reduce its exposure to claims on its professional indemnity insurance, but because (and only because) they "enable the provision of legal services by the practice under the professional obligations of Australian legal practitioners."

We can assume that the systems that are appropriate to enable a firm to achieve those other worthy purposes will overlap with the systems that are appropriate to achieve this ethical purpose but no one should assume that the systems will be the same or co-extensive. That might be obvious but it's worth reminding ourselves that law firms like other business enterprises are likely to put more time and energy into keeping and implementing systems that

enable them to improve their financial performance than systems that enable them to improve their ethical performance.<sup>xiv</sup> They can't assume they're killing two birds with one stone, nor can they regard the ethical performance of their lawyer employees as a matter for them, as individual professionals, and not a corporate responsibility.

The word 'enable' in the definition of appropriate management systems is significant. It means that management systems count as appropriate in this context only if they support and encourage and guide a firm's employees to do the right thing and discourage and deter them from doing the wrong thing and, given that even the best systems might be less than completely successful in that regard, only if they maximise the likelihood any wrongdoing will be detected and dealt with, including with appropriate remedial action.<sup>xv</sup>

The duty of the legal practitioner directors of incorporated legal practices to keep and implement appropriate management systems is in effect a duty to ensure that the firm develops and maintains an ethical infrastructure.<sup>xvi</sup>

### **Compliance audits**

An audit is 'a review or examination of any aspect of the operations of [a] person or body'.<sup>xvii</sup> A compliance audit by that account is a review of a firm's ethical performance - of the firm's and its employees' compliance with their corporate and professional obligations and the appropriateness of its management systems in the sense that we've just described. Our audit power is a power to conduct ethics audits, in effect.

Compliance audits are different from audits that review other aspects of a firm's operations in the same way that the management systems that are appropriate to enable it to provide legal services under the professional obligations of Australian legal practitioners are different from the management systems that might be appropriate to enable it to achieve some other worthy management purposes. They are not the same as risk management audits that review a firm's exposure to claims on its professional indemnity insurance, for example, or commercially driven quality assurance audits that review primarily the efficiency and consistency of a firm's business processes.

It's not hard to imagine a firm getting a pass mark or better on audits of those kinds but 'failing' an ethics audit. Imagine for example a firm that improves the consistency and efficiency of its time-recording system for human resource management purposes but then

applies the data it collects for those purposes to counting billable time. The firm stands to bill its clients for all manner of activities that can't properly be billed to them unless it's got systems in place to exclude the time spent on those activities from the calculation - activities such as 'diary reviews', 'file retrieval' and 'collating', for example.

So: how should we go about doing compliance audits? We envisage conducting two types of audit - internal or self-assessment audits that we will expect incorporated legal practices to undertake themselves, through their legal practitioner directors, and external audits that we undertake, looking in from the outside.

We note before proceeding that we have agreed with our counterpart regulators in New South Wales and Victoria to adopt the 'education towards compliance' approach that has been pioneered over recent years in New South Wales.<sup>xviii</sup> We want to exercise our audit powers in such a way as to encourage the highest possible level of voluntary compliance. We want to engage legal practitioner directors with problem-solving how they might best develop and continually improve their management systems and processes and workplace cultures to better support and sustain high standards of conduct, and in such a way as to engage them in a continuing conversation with us about their progress in that regard.

Of course it is possible that compliance audits will throw up evidence of misconduct of one kind or another in which case we will deal with it, and no doubt in some circumstances we'll use our audit powers specifically to go looking for it, but that's not their primary purpose. Their primary purpose is to encourage and to 'up the ante' on legal practitioner directors to keep and implement appropriate management systems and to continually improve them.

**a) self assessment audits**

We have adopted the self-assessment audit process that has been used for some time now in New South Wales. We will require the legal practitioner directors of every incorporated legal practice to audit their practice's management systems and supervisory arrangements soon after the corporation has given the required notice of its intention to commence legal practice. We will require them to complete a pro forma self-assessment audit form - a form they will be able to complete on-line in the not too distant future - which asks them to assess how effectively their systems meet 'the ten objectives of a sound legal practice':

- competent work practices to avoid negligence

- effective, timely and courteous communication
- timely delivery, review and follow up of legal services to avoid delay
- acceptable processes for liens and file transfers
- shared understandings and appropriate documentation covering cost disclosure, billing practices and termination of retainer
- timely identification and resolution of conflicts of interests
- appropriate records management
- authorising and monitoring compliance with undertakings
- effective supervision of the practice and its staff, and
- compliance with trust account regulations and accounting procedures.

We want and we hope and expect that legal practitioner directors will engage positively with the exercise and candidly identify any aspects of their practice's management systems that might require or benefit from improvement. We will require them to return the completed self-assessment form to us within a designated period and we will evaluate the information and engage in a conversation with them about what further steps they might take, if any, to fix any perceived weaknesses.

We will then work with them or refer them to their professional body or other advisors to get whatever assistance and support they might require to develop an action plan to achieve that goal and we will ask them in due course to report their progress. We will ask them in any event to conduct periodic 'maintenance audits' to bring us up to date with any changes they initiate themselves, outside that cycle.

The initial self-assessment audits, in other words, are 'gap analyses' or 'risk assessments' or 'management reviews' that are designed to be a baseline for future improvements to the practice's management systems and supervisory arrangements and reports on future improvements, and the subsequent or 'maintenance' self assessment audits become those progress reports.

The self-assessment form is readily accessible on the Commission's website. It is an only slightly revised version of the form that has been used in New South Wales for some years now but it does include an entirely new section which requires legal practitioner directors to provide us with information about their practice including information about its non-legal directors and their occupations, its shareholders and their relationship to the

law practice, the number of lawyers it employs, its gross fee income and the services it provides other than legal services, if any.

We will use that information to check whether the corporation is complying with its obligations in relation to disqualified persons, for example, but also and more fundamentally to complement our existing complaints data to help enable us develop risk indicators and over time increasingly sophisticated evidence based risk analyses which will allow us to identify the incorporated legal practices most likely to be at ethical risk. We want to develop a capacity to target our regulatory resource to where it is most needed and to do that in an educated way.

## **b) external audits**

Clearly we will need to develop and conduct a program of audits ourselves so that we can know whether the self-assessment audits legal practitioner directors undertake at our request are giving us a fair and reasonable and for that matter an honest appraisal of the actual state of play. We can't simply take their word for it.

What might an effective program of external audits look like? It's a good question - there is no established practice as yet, unlike with self-assessment audits. Let's start by going back to basics. What do we want to achieve? What are the underlying principles? What are the strategic imperatives? How will we measure our success?

No doubt there are others but it seems to us that our audit program will have to satisfy at least four fundamental criteria, all of them obvious at one level and all of them worthy of close attention but which fit together only uneasily at best:

- firstly, our audit program should be and be seen by incorporated legal practices and all our other stakeholders to be credible and robust, and sufficiently credible and robust to justify public confidence in the provision of legal services by incorporated legal practices and that we're on the job, as it were.

That suggests, if we turn our minds to performance indicators, that we should have regard both to the frequency of our audit interactions with incorporated legal practices and their quality. We will need to in due course to set ourselves more specific targets than these but we will have to do better in relation to frequency,

surely, than getting around to auditing incorporated legal practices only once every few years or so. We shouldn't be in their face, if we can use that expression, but we should be visible and have a presence.

We say that not least because there is substantial evidence in relation to companies generally, if not law firms, that they tend to implement compliance management programs 'only to the extent necessary to ensure that they look legitimate, or to the extent that they are forced to do so [or] feel compelled... by pressure from regulators or elsewhere.'<sup>xix</sup>

Similarly we will have to be able to say in relation to quality, surely, that our audit program adds value in ways we can point to and defend – that it makes a difference and a difference for the better.

- secondly, our program of external audits should be fully consistent with and complement the 'education towards compliance' thrust of the initial self assessment audits. It should value-add by encouraging legal practitioner directors to stay engaged or to re-engage with efforts to continually improve their management systems and supervisory arrangements and to further their conversation with us as regulators about their progress in that regard.
- thirdly, we should allow for the fact that we will inevitably have limited resources to conduct and evaluate audits and to prepare the required reports. New South Wales has allowed law firms to incorporate since 2001 and has more than 800 incorporated legal practices now, or about 20% of all its law firms, and the number is steadily growing. There are already more than 100 incorporated legal practices in Queensland after only a year, or almost 10% of all Queensland law firms and the number is steadily growing here, too.<sup>xx</sup> The same is true of Victoria.

It is likely on current trends that there will be more incorporated than unincorporated law firms within only a few years. We one person dedicated to the audit function currently, with a largely developmental role to date, and we do not expect to secure a commensurate increase in our staff numbers or to be able to redeploy staff who are currently dealing with complaints. Complaints are not going to go away.

- fourthly, we should allow equally or the fact that incorporated legal practices will have resource constraints also – and we should not add unnecessarily to their regulatory burden in any event. We should design an auditing program that allows the compliance costs to incorporated legal practices to be proportionate to the potential significance of the information we are seeking to obtain<sup>xxi</sup> and we can expect resistance if we don't, rightfully so.

It is difficult to see how we could possibly meet all four criteria at once if we conceive a program of external audits to require us to conduct regular and comprehensive reviews of every aspect of every incorporated legal practice's compliance with its obligations under the Act and of its management systems and supervisory arrangements – we don't and won't ever have the resources we need to do that.

We can take some comfort however in the fact that our responsibility as auditors is not to certify or 'sign off' much less guarantee that incorporated legal practices and their legal practitioner directors are complying with their obligations. That is their job. Ours is a more modest job - to run a credible and defensible program of audits to check that they're doing theirs, as constructively and helpfully as we can but at the same time and without dwelling on it so as to expose them to a real risk they'll be found out if they're not.

It follows, putting all this together, that we envisage ourselves conducting comprehensive external audits only occasionally, and only of those incorporated legal practices we believe are most likely to fall short of expectation - and even then only of those particular aspects of a firm's systems we believe are most likely to fall short of expectation. We will need to rapidly acquire the data and the skills and the analytical capacity necessary to make evidence based risk assessments of those kinds.

How then within our limited capacity can we best add value? No doubt there are others, but it seems to us that our audit program will have to satisfy at least the following secondary criteria, in addition to the four fundamental criteria we've identified already:

- we should direct our energies as auditors not to reviewing policy and procedure manuals and the like and checking them against the best practice characteristics of documents of that kind but to trying to find out how they're perceived down the line and whether they're followed through. We should be collecting evidence about their impacts and outcomes and what's actually happening in practice.<sup>xxii</sup>

And of course in our case, given our particular niche in the quality assurance market, we should be collecting evidence about the ethical impacts and outcomes of law firms' management systems down the line, not their impacts and outcomes more generally. We should be collecting evidence about the way a firm actually delivers legal services and whether it delivers them "under the professional obligations of Australian legal practitioners."

- we should assume at every stage of the audit process that "there will be problems, things that have been missed, things that can be improved and things that should be changed because internal or external circumstances have changed" - we should adopt the working hypothesis that we will find problems that can be corrected and so lead to improvements and we should go looking for them, and we should assume we've missed something if we don't find them.<sup>xxiii</sup>

This does not imply that we should be mistrustful or suspicious much less aggressive or adversarial in the way we go about our work. We're describing a methodological approach, not a pre-emptive finding - we're saying no more than that we'll have a good platform to discuss possible improvements to a firm's ethical infrastructure if we go looking for problems and find them and a good reason to be confident all is well if we go looking to no avail.

Certainly we'll be better placed to add value in this way than the legal practitioner directors of the firms we audit. Insiders will have more invested in their management systems than we will as dispassionate outsiders and they'll be less inclined to go looking for anomalies or otherwise to find fault. Indeed they may find it difficult to 'see' a problem even when they're looking right at it.<sup>xxiv</sup> That is human nature, and so the role falls to us.

- we should in any event but we've flagged already that we'll have no option but to target our scarce regulatory resource to where is most needed. It follows that we'll have to develop a capacity to make informed and evidence-based risk-assessments. That will be a two-pronged exercise. We should try to identify not only the law firms that are the least likely to deliver legal services 'under the professional obligations of Australian legal practitioners' but also the aspects of

legal practice most likely to be problematic in this regard - billing practices, perhaps, or supervision.

We need to be mindful, however, of a potential downside to an overemphasis on risk assessment. We need to maintain a credible presence even among those firms we assess to be least at risk. We might get our risk assessments wrong, for one thing and let's be honest: we might get good at it but risk-assessment will always be an art not a science and will always require guesswork - increasingly educated guesswork, we hope, but guesswork nonetheless. Nor do we want to encourage legal practitioner directors in low risk firms to drop the ball by too often directing our attention elsewhere. We should have a presence with them as well.

- we will have to have full regard for the fact that incorporated legal practices might have little in common but for being incorporated and design our auditing strategies accordingly, so that 'no one size fits all'. So we should identify not just the aspects of legal practice most likely to be problematic in law firms but the aspects of legal practice most likely to be problematic within different categories of law firms - billing practices within large commercial law firms, perhaps, or supervision practices within high-volume residential conveyancing firms - and tailor make our audits to suit.

Finally, we shouldn't forget in this context the principles we should try to apply in all aspects of our work and that apply equally to the exercise of our audit power – hence:

- we should go about our business as auditors as openly and transparently as we reasonably can. We should, for example, publish materials that alert incorporated legal practices, the profession at large and the broader community to the practices we believe are most likely to be problematic and accordingly to attract our attention. And of course we'll very likely want to direct our attention to different practices from one year to the next and so we should say so in advance and say why. We should never forget that our aim is not to catch law firms out, but to identify potential problems and help resolve them by driving continual improvements.

Similarly, we should routinely publish de-identified and aggregated data that describes what our audit program is telling us not only about the problems we are

encountering but how the best law firms are resolving them. We will be well placed to and we should take the opportunity to help law firms develop more effective ethical infrastructures “by increasing the visibility of law firm policies and procedures and by promoting best practice within law firms.”<sup>xxv</sup>

- equally, we should go about our business as collaboratively as we reasonably can. We should design our auditing program and strategies in active consultation with our counterpart regulators in the other states and territories certainly but also with the professional bodies, the professional indemnity insurers, other quality assurance auditors, law firms and their legal practitioner directors, the law schools, legal academics and others.

We should ‘road test’ our audits and certainly we should dovetail what we do with what other stakeholders might be doing and avoid any duplication - some firms already audit their organizational performance, for example, and some professional indemnity insurers already audit law firms in ways that potentially overlap with what we might want to do. Similarly we should pick the brains of the legal academics and wherever we can offer them something in return. Our program will be all the more relevant and practical for it, and better targeted and better accepted.

- finally and obviously, we should make the best possible use of the available technologies, to get the best possible mileage from our scarce resources and to minimize the compliance costs for the firms we are auditing.

## **WHAT AN EFFECTIVE PROGRAM OF EXTERNAL AUDITS MIGHT LOOK LIKE**

We’ve said we will expect incorporated legal practices to complete self-assessment audits shortly after they commence engaging in legal practice. We’ve said that we want to conduct a complementary program of external audits and we’ve described a set of guiding principles we think should inform us in developing such a program. Those principles tell us we should have a visible presence with all the firms potentially subject to audit, not just those of them we assess to be ‘at risk’; that we should keep their compliance costs proportionate to the potential significance of the information we are seeking to obtain; that we should direct our limited resources to “the measurement of impacts within small, specific and well defined problem

areas”; and that we should design “creative-tailor made solutions [that] procure compliance while recognising the need to retain enforcement as the ultimate threat.”<sup>xxvi</sup>

We envisage conducting a wide variety of external audits of different kinds and different levels of intensity depending on the circumstances of the law firms subject to audit. We will separate them into two kinds for performance reporting and broader descriptive purposes – web-based surveys and on-site reviews.<sup>xxvii</sup>

#### **a) web-based surveys**

We envisage developing a varied and ever-expanding suite of short, sharp web-based surveys which test discrete aspects of a law firm’s ethical infrastructure. We’re confident that web-based surveys can tell us a great deal.<sup>xxviii</sup>

We envisage requiring all firms potentially subject to audit to complete web-based surveys at regular intervals, not just the firms we assess to be most ‘at risk’ - just how regular is a nice question we’ll have to answer in consultation with law firms having regard to the compliance costs. We envisage making risk assessments even so, and informing our approach accordingly, by designing and directing the surveys to the particular aspects of practice we believe to be most problematic, either for all law firms or particular kinds of law firms.

We envisage the web-based surveys having the following characteristics:

- they will be designed specifically to maximize the value of the information they elicit at the same time as minimizing the compliance costs. We will design them so they take no more than and preferably less than 30 minutes to complete. We want them to be equally resource-friendly from our point of view also – and so will use software that can automatically calculate the key results.
- they will be directed not just to a firm’s legal practitioner director(s) but to all its employees, or in large firms at least significant samples of the different levels and classifications of their employees – directors, senior lawyers, junior lawyers, paralegals and other non-legal staff. We want the employees to give us, and the firm, a window on how the firm’s policies and procedures and systems are

perceived and understood and implemented ‘down the line’ by the different levels and classifications of their people.

- they will encourage respondents to be frank, by guaranteeing their anonymity. We note that there is evidence that respondents answer on-line surveys more honestly than face to face surveys.<sup>xxix</sup>
- they will have an educational value, if we get the questions right, by prompting each individual respondent to reflect on the significance of the questions and the implications of their answers both for them as individuals and their firm.
- they will add value from the firm’s point of view also, by ‘taking its pulse’. The respondents’ answers and in particular the patterns of answers across the different levels and classifications of the firm’s employees will be a handy indicator of which of its management systems if any might need improvement. So too, when a firm has more than one office, will the patterns of answers across the different offices. That will be a handy indicator of the consistency of the firm’s ethical culture across its various locations.
- they will add value from our point of view, too, as a risk indicator. The answers and the patterns of answers across the different levels and classifications of a firm’s employees might be positively encouraging or they might be anomalous, by suggesting that the firm’s systems are not always reflected in what actually happens ‘down the line’ and stand to be improved by clarification or further training and the like. Equally they might hint at deep-seated problems that warrant a closer look by means of a comprehensive on-site review.

Certainly the information we obtain in this way will add powerfully to the risk information we will already have at our disposal, including the firm’s complaints history and its legal practitioner director’s self-assessment of the appropriateness of its systems and supervisory arrangements.<sup>xxx</sup>

- they have potential to add further value again, if as we envisage we publish the aggregated and de-identified results. That will enable law firms to compare their performance with the performance of their law firm peers - and serve the public interest, too, by exposing aspects of law firm culture to public scrutiny.

Despite our reassurances, some law firms will very likely be uneasy about the compliance costs to their business if we require all or at least representative samples of the different levels and classifications of their employees to complete the surveys. We don't believe the audit process will impose an unreasonable financial burden but in any event we hope to convince law firms that the process will value-add in the ways we've described and, if it does, that the cost will be more than outweighed by the benefits.<sup>xxxii</sup> We note that the compliance costs equation takes on a whole new complexion if the costs are subtracted not from the time fee earners would otherwise dedicate to billable work but from the time they've got set aside already for professional development and other non-billable activities.

Similarly some law firms are likely to be uneasy with the notion that we will require their employees or at least representative samples of their employees to complete the surveys on-line and in that way to communicate with us as regulators directly and anonymously, and not through their legal practitioner director(s) as intermediaries.

Their unease will be understandable but misplaced. The law firms' and their legal practitioner directors' interests and the public interest will all be well served if the audit methodology causes employees to engage with ethical issues and to respond honestly to the questions whether their responses suggest all is well with the firms' management systems and supervisory arrangements or otherwise. The point of the exercise, remember, is not to go looking for disciplinary breaches but 'to encourage the highest possible level of voluntary compliance [and] to engage legal practitioner directors with problem solving how they might best develop and continually improve their management systems and processes and workplaces cultures to better support and sustain high standards of conduct...'. It's all to the better if involving a firm's employees and encouraging them to be candid by guaranteeing their anonymity maximises the likelihood we and in due course the firm can identify anomalies and in that way lead to improvements.

Furthermore the audit process like the process for investigating complaints is entirely confidential - the Act prohibits us and rightly so from disclosing any information we obtain in this way except in very limited circumstances, none of which will ordinarily apply.<sup>xxxii</sup>

Of course it's possible that some employees will take advantage of the anonymity the process affords them to blow the whistle on some of their firm's practices or a colleague or supervisor, honestly or perhaps even maliciously. Maybe, but the worst that can happen on either score is that we would initiate more detailed inquiries to test what we've been told and that's a process that leads nowhere in the absence of evidence. We might of course find such evidence - to support the need for systems improvements or perhaps to warrant filing disciplinary charges - but those would be good outcomes in the public interest, both of them. And of course the exercise would remain entirely confidential unless and until we file any disciplinary charges - and that will be only very rarely, in our estimation.

What matters most at the end of the day is that the surveys are practical and relevant and well designed from a technical point of view, and that they do in fact value add in the ways we've described - and to that end we envisage road-testing prospective surveys with selected law firms and other relevant stakeholders before proceeding.

We are particularly keen to explore potential collaborations with legal academics with research interests in the area - collaborations in which they lend us their expertise to help develop survey instruments which we can administer as audits and that will serve both our purposes. We've noted already the dearth of empirical research about ethical conduct within law firms and we're struck by the fact that the web-based surveys we have in mind are in effect just that - a form of empirical research.

Our interest as regulators will rest at least in the first instance with what the survey results tell us about particular law firms subject to audit and we are (as we've noted already) rightly and strictly prohibited from disclosing that information to anyone outside the firm. Legal academics will be interested however in the aggregated and de-identified results and there is nothing to prevent us disclosing that information and indeed we should, to inform the public and promote informed discussion. The data stands to be a rich source of information about law firm culture - to provide snapshots of the ethical performance of potentially large numbers of law firms, about 1500 incorporated legal practices down the eastern seaboard of Australia on the current count if our counterparts in New South Wales and Victoria join us in the exercise.

We hope and expect in the medium term to survey not only incorporated but traditionally structured law firms, too, whether by voluntary agreement - because we persuade them

that it's the worthwhile exercise we believe it to be - or by legislative amendments to extend our powers. That will enable us to measure the differences between incorporated and unincorporated firms, the impacts of their different business structures and the effectiveness of the different regulatory regimes.

We have developed three web-based surveys at the time of writing and they are all readily accessible on the Commission's website.

- an audit of practice culture, or *workplace culture check*: we developed this survey before we even began thinking through how we would go about auditing incorporated legal practices, simply to give law firms a means of testing the health of their ethical culture by exploring some probably unspoken and unexamined dimensions of their organisational life.

The survey had its origins in research findings to the effect that organisations have a stronger ethical culture if their staff respond affirmatively to questions like the following but are vulnerable if they respond negatively: do employees feel a sense of responsibility and accountability for their actions?; do they freely raise issues and concerns with their supervisors without fear of retaliation?; do managers model the behaviour they demand of their employees; do managers communicate the importance of integrity when making difficult decisions? They're good questions, and we wanted to encourage law firms to ask them. We road-tested an earlier version of the survey with three large and two mid-size firms who gave us encouraging feedback and it dawned on us that it would serve as a form of compliance audit also.

- an audit of *billing practices in medium to large law firms*: we designed this survey having regard to the issues we encounter daily in our complaints driven work. We 'road-tested' an earlier version with one of the large national law firms and were greatly encouraged by the firm's response - the managing partner of its Brisbane office told us "the survey was a useful reminder of the issues that arise in best billing practice. It has prompted us to review our own management systems to see how effectively they deliver best billing practice and given us some very good ideas as to how to improve our systems."<sup>xxxiii</sup>

The survey draws with her kind permission on the survey Susan Saab Fortney administered as part of the empirical research to which we referred earlier.<sup>xxxiv</sup>

The overlap between her research interests and our interests as regulators encourages us to believe we'll be able to develop mutually advantageous collaborations with legal academics in designing effective web-based surveys.

- an audit of *complaints management systems* in law firms: no law firm's management system will count as fully appropriate in the absence of an effective system for dealing with complaints, whether by clients, other law firms, internal whistle blowers or anyone else. We note that about three-quarters of the complaints that come to us as statutory regulators could have been avoided if only law firms subject to complaint had kept and implemented complaints-management systems that encouraged and allowed disgruntled clients and others to have their concerns dealt with in-house.

We have several further surveys in various stages of development including surveys about supervision practices and duties to the courts and third parties.

#### **b) on-site reviews**

On site reviews by their very nature will be a more resource intensive exercise both from our point of view and point of view of the law firms subject to review, and it follows that we envisage conducting reviews of this more intensive kind significantly less frequently than web based surveys and only on an 'as needs' basis - on the basis of a risk assessment that tells us that a firm or some aspects of its practice are or are highly likely to be non-compliant.

We envisage on-site reviews comprising tailor-made combinations of some or all the following kinds of activities:

- further web based surveys of the kinds we have already described;
- traditional desk-top policy and procedure reviews;
- detailed analyses of the firms' complaints history, including detailed analyses of the investigation files held by the Commission;
- interviews with legal practitioner directors, supervisors and managers;
- interviews with and / or focus groups of individual employees 'down the line';

- interviews with and / or focus groups of clients, including but not only clients who have lodged complaints with the Commission;
- interviews with third parties including, for example, practitioners from other law firms that have regular dealings with the law firm subject to audit;
- reviews of selected or randomly selected client files<sup>xxxv</sup> and bills, in-house complaints registers and the like;
- client satisfaction surveys; and
- mystery or ‘shadow’ shopping - having real or pretend consumers deal with the firm and behave exactly as a genuine client might behave and asking them to report their experience<sup>xxxvi</sup> - and similarly mystery complaints.

## IN CONCLUSION

We will conclude what we have to say by returning to where we began – by arguing that as regulators we should be able to hold all law firms to account in the ways we’ve described and not only those of them who opt to incorporate and to do business as companies.

Ted Schneyer argued more than fifteen years ago now that not only individual lawyers but law firms should be capable of being held to account when the services they provide fall short of appropriate professional standards. He argued that “a disciplinary regime that targets only individual lawyers in an era of larger law firms is no longer sufficient. Sanctions against firms are needed as well.” He continued “the chief reason to allow disciplinary authorities to proceed directly against law firms is prophylaxis – the promotion of firm practices that prevent wrongdoing by individual lawyers” and he noted, for example, that “disciplinary agencies could... require firms to report periodically on the measures they have taken... and proceed against firms whose reports reveal clear inadequacies.”<sup>xxxvii</sup>

More recently Chambliss and Wilkins have argued that Schneyer “deserves great credit for initiating the conversation on law firm discipline” but that the time has come “to reconsider the regulatory framework he proposed.” They argue that “the design and monitoring of structural controls within law firms should be recognised - and regulated - as a specialised duty of management” rather than of law firms per se. They argue that “all law firms [should] be required to designate at least one partner [to be] the firm’s compliance specialist” and that compliance specialists should be personally liable for ensuring their firms maintain the appropriate structural controls.<sup>xxxviii</sup>

That is pretty much the framework that the Act creates here in relation to incorporated legal practices. It requires them to have at least one legal practitioner director and makes legal practitioner directors personally responsible on pain of disciplinary sanction for implementing 'appropriate management systems' and taking 'all reasonable action' to ensure that lawyers who work for the firm comply with their professional obligations and 'appropriate remedial action' if they don't.

We can see no good reason why sole practitioners and partners within traditionally structured law firms shouldn't be under exactly the same obligations. Indeed it's hard to imagine anyone trying seriously to argue that they have any lesser obligations as it is, albeit obligations set out in codes of conduct and not in statute.<sup>xxxix</sup>

The objection is more likely to be to the 'regulatory burden' - to the prospect of becoming subject to compliance audits. But the traditional complaints-driven processes for enforcing professional standards have significant limitations, for all the reasons we identified earlier, and the auditing processes we've described have significant benefits.

Furthermore we can see no 'in principle' reason why traditionally structured law practices should be subject to any less rigorous regulatory supervision than incorporated legal practices. Lawyers have always sold legal services for profit within a business enterprise, whatever its structure, and have always had to balance their commercial obligations to their business enterprise with their professional obligations to their clients and to the courts. There is no particular reason to think that lawyers who practice in incorporated legal practices will find it harder to balance their responsibilities than lawyers who practice within a traditional partnership arrangement.

More fundamentally, however, we've designed the auditing program that we've described in the pare deliberately and as a matter of principle so as not to add any significant additional regulatory burden to law firms unless there is some demonstrable risk-related reason in all the circumstances that justifies it and to remain consistent even then with the Administrative Review Council's best practice principles - precisely so as to ensure that the compliance costs remain proportionate to the potential significance of the information we're seeking to obtain.<sup>xi</sup>

---

<sup>i</sup> An edited version of this paper will appear in the journal *Legal Ethics*, Volume 11, No.2, 2009

---

<sup>ii</sup> Elizabeth Chambliss and David B Wilkins, *A New Framework for Law Firm Discipline*, 16 Georgia Journal of Legal Ethics, 2002-2003, at pp 338 and 343.

<sup>iii</sup> See, for example, Linda Klebe Trevino, Gary R Weaver, David G Gibson and Barbara Ley Toffler, *Managing Ethics and Legal Compliance: What Works and What Hurts*, California Management Review, Volume 41, Issue 2, January 1999. Their research shows that a company's compliance with its ethical obligations is determined less by the specific characteristics of its formal policies and procedures than by its employees' perception that the company and its leaders 'do as they say' by demonstrating ethical leadership, or their perception that the company and its leaders are motivated by self-interest and demand unquestioning obedience. It shows that companies and their leaders demonstrate ethical leadership among other things by openly discussing ethical issues that arise in the course of doing business, by treating their employees fairly, by rewarding ethical conduct and by showing concern for external stakeholders.

See also Christine Parker, Adrian Evans, Linda Haller, Suzanne Le Mire and Reid Mortensen, *The Ethical Infrastructure of Legal Practice In Larger law Firms: Values, Policy and Behaviour* which has been accepted for publication in the University of New South Wales Law Journal during 2008 (and which we will refer to as Parker et al 2008), especially p.8, the references in footnotes 17-21, and p. 33.

<sup>iv</sup> Lori A Richards, Director, Office of Compliance Inspection and Examinations, US Securities and Exchange Commission, *The Culture of Compliance*, Spring Compliance Conference: National Regulatory Services, Tuscon, Arizona, April 23, 2003.

<sup>v</sup> Parker et al 2008 discuss and develop the concept of ethical infrastructure in some detail. They say 'the term 'ethical infrastructure' was originally coined in the United States to refer to policies and structures that support compliance with professional conduct rules' and they refer to the work of Ted Schneyer (see below) and Chambliss and Wilkins (above). They go on to say they use "a broader conception of ethical infrastructure that is concerned with positively promoting individual and corporate behaviours, structures and cultures that support the ethical values that lie behind the rules... The ethical infrastructure of a firm should not be seen merely as the formal ethics policies explicitly enunciated by management. All management policies, priorities and initiatives – formal and informal, and explicitly stated or implicitly assumed – can undermine or support ethical practice within a firm... The most important aspects of ethical infrastructure are less tangible than management systems for ensuring compliance with ethical rules. They have much more to do with the way the culture of the law firm connects with and empowers individual lawyers to express their own ethics and values in their

---

work, especially by feeling free to raise ethical issues with colleagues and supervisors - and have those queries taken seriously, discussed, and, where necessary, acted on” - see pp.3-4, 4-5 and 33.

<sup>vi</sup> The Commission publishes detailed complaints data by way of appendix to its annual reports which can be accessed at [www.lsc.qld.gov.au](http://www.lsc.qld.gov.au) . About half the complaints the Commission deals with are about the conduct of lawyers in family law matters (about 20%), residential conveyances (about 20%) and personal injury matters (about 10%). We know that 60% of all the complaints we dealt with in the 2006-07 reporting year were about sole practitioners; 84% were about lawyers who worked for firms with five or fewer partners (including sole practitioner firms); and only 3% were about lawyers who work in firms with 10 or more partners – yet only 30% of Queensland lawyers are sole practitioners; only 55% work in firms with five or fewer partners (including sole practitioner firms); and almost 30% work in firms with 10 or more partners.

<sup>vii</sup> It is likely that the typically wealthy and corporate clients who use the services of the larger law firms are not only better equipped to look after their own interests when they believe they’ve been dealt with less than appropriately but that they do, by using or threatening to use their economic leverage by taking their business elsewhere. They are also less inclined than the ordinary folk who use the services of small law firms to complain to statutory regulators. It might also be that lawyers in larger law firms typically work in teams and accordingly that it’s hard to attribute responsibility for some perceived shortcoming to any particular member of the team.

No doubt some people will argue that the complaints data simply reflect a reality in which lawyers in medium sized and larger law firms are less likely to act unethically than their small firm peers. They might argue, for example, that lawyers in larger law firms have more and better opportunities to seek advice and guidance from their peers and supervisors and generally to discuss ethical issues, and that their firms have economies of scale that allow them to better support them to act ethically through in-house training programs and the like. They might also argue that there will be more people to notice misconduct in larger firms, too, and hence that lawyers who do the wrong thing are less likely to be able to hide what they’re doing or otherwise to get away with it.

No doubt this is all true of the best firms. The problem however is that team environments are a double-edged sword. They can just as easily discourage ethical conduct – they can make it less likely that individual team members will take personal responsibility for the actions of the team, make team

---

members unwilling to rock the boat by questioning whether some team decision or strategy or course of action is ethical, and diminish the team members' capacity even to 'see' ethical issues that might be staring them in the face. See Parker et al 2008 generally but especially at pp. 5-8.

<sup>viii</sup> See Elizabeth Chambliss and David B Wilkins, *Promoting Effective Ethical Infrastructure in Large Law Firms: A Call for Research and Reporting*, 30 Hofstra Law review 691, 2001-2002 especially pp.698-699.

<sup>ix</sup> See Parker et al 2008 and also Christine Parker, *Peering Over the Ethical Precipice: Incorporation, Listing and the Ethical Responsibilities of Law Firms*, a paper first presented as the J. Donald Mawhinney Lecture in Professional Ethics at the University of British Columbia Law School on 12 February 2008, in particular the discussion above footnotes 38 and 40 and the references cited in those footnotes. Dr Parker presented a later version of the same paper at The Future of the Global Law Firm Symposium held at the Center for the Study of the Legal Profession, Georgetown Law Center, 17-18 April 2008.

See also Chambliss and Wilkins, 2002-03, above, at pp.342-343; Susan Saab Fortney, *Soul for Sale: An Empirical Study of Associate Satisfaction, Law Firm Culture and the Effects of Billable Hours Requirements*, UMKC Law Review, Vol 68, 2000-2001; and Lisa G Lerman, *A Double Standard for Lawyer Dishonesty: Billing Fraud Versus Misappropriation*, 34 Hofstra Law Review, 847, 2005-2006. More generally, see Patrick J Schiltz, *On Being a Happy, Healthy and Ethical Member of an Unhappy, Unhealthy and Unethical Profession*, 52, Vanderbilt Law Review 871, 1999 and the other articles Chambliss and Wilkins (2002-03, above) cite at p.242, note 10. Numerous articles to similar effect appear regularly in legal journalism such as *Lawyers Weekly*.

<sup>x</sup> See the *Legal Profession Act 2007* (Qld) Part 2.7, especially sections 117-129, 132 and 143, and also section 574. Note that legal practitioner directors, employees of incorporated legal practices, the corporation itself and in certain circumstances other people are liable for disciplinary and / or criminal sanction for a range of 'misconduct' that goes well beyond the additional duties of legal practitioner directors that we specifically mention in the main body of the text.

<sup>xi</sup> section 130

<sup>xii</sup> section 130(3)

<sup>xiii</sup> sections 131 and 540-581

---

<sup>xiv</sup> Chambliss and Wilkins 2001-2002 (above), p.705, especially footnote 93. Susan Saab Fortney has told us in a private communication that the findings from her studies of law firm peer review tend to support this conclusion. We note that Kimberly Kirkland reported in a paper she gave at this same conference that the large law firms she had studied typically had well developed policies and procedures for identifying and dealing with conflicts of interest but no formal policies and procedures for identifying and dealing with other ethical risks less likely to hurt the bottom line - becoming too close to clients, for example, or failing to honour duties to third parties, the administration of justice and the public.

We note also by way of personal observation that we have attended more than a few seminars and workshops that have been directed to helping law firms improve their management systems where we've been struck by the fact that the conversation was directed exclusively to the impact on the financial bottom-line and was totally silent about the impact on the ethical bottom-line.

<sup>xv</sup> This is the effect of sections 117(3), 117(4), 118(2) and 118(3) of the Act taken together.

<sup>xvi</sup> "the legislative provisions that... require incorporated legal practices to have an appropriate management systems [are] in effect a requirement that incorporated legal practices consciously implement an ethical infrastructure as part of their new business structure" - Parker at al, 2008, at p.21.

<sup>xvii</sup> Australian National Audit Office, *General Guidance on the Conduct of Performance Audits*, July 2003, p.1.

<sup>xviii</sup> See Steven Mark and Georgina Cowdroy, *Incorporated Legal Practices – A New Era in the Provision of Legal Services in the State of New South Wales*, Penn State International Law Review, Volume 2, Number 4, Spring 2004 at p.671; and Steven Mark and Molly Hutcherson, *New Structures for Legal Practices and the Challenges They Bring for Regulators*, published on the website of the Office of the Legal Services Commission New South Wales (<http://www.lawlink.nsw.gov.au/olsc>)

<sup>xix</sup> Christine Parker and Vibeke Lehman Neilsen, *Do Businesses Take Compliance Systems Seriously? An Empirical Study of the Implementation of Trade Practices Compliance Systems in Australia*, Melbourne Law Review, Vol 30, 2006, at pp. 443, 444, 474 and 482-483.

<sup>xx</sup> We will include detailed descriptive data about incorporated legal practices in the Commission's annual report.

---

<sup>xxi</sup> This principle echoes one of the best practice principles (principle 19) enunciated in the draft report of the Administrative Review Council published earlier this year under the title *Government Agency Coercive Information-Gathering Powers*.

<sup>xxii</sup> We have drawn heavily on Dr Christine Parker's work in getting our thinking to where it is not least her empirical study several years ago now of the compliance audit programs conducted by the Australian Competition and Consumer Commission (ACCC) and the Australian Securities and Investments Commission (ASIC) under the title *Regulator Required Corporate Compliance Program Audits*, Law and Policy, Volume 25, No. 3, July 2003. She describes 'a tendency for [the] audit methodology to focus on management systems at the expense of forensic investigation of harm done or likely to be done to consumers and investors'. She noted that most of the audits she studied 'relied primarily on documentation of the system and discussions with senior management, [that] there is no inspection, let alone testing of the processes in action, [that] most of these desk audits are really only capable of providing a view about the intended *design* of the compliance program p[and that] the methodologies were not rigorous enough to discover how compliance programs are actually *implemented* [or] what *outcomes* they are achieving.' We note that we understand both the ACCC and ASIC have since responded to Dr Parker's criticisms and adjusted their methodologies accordingly.

<sup>xxiii</sup> Parker, 2003.

<sup>xxiv</sup> Parker et al 2008 discuss at pp.9-11 how cultural factors can impact a person's capacity to 'see' ethical issues.

<sup>xxv</sup> Chambliss and Wilkins 2001-02 at pp.694 and 716.

<sup>xxvi</sup> Australian Law Reform Commission Discussion Paper 65: *Securing Compliance – Civil and Administrative Penalties in Australian Federal Regulation*, paragraphs 4.100-4.103 at pp.137-138.

<sup>xxvii</sup> We will need in due course to come up with an operational definition, probably a function of the total time it takes for a firm to complete the audit and the size of the firm - perhaps the total hours divided by the number of employees.

<sup>xxviii</sup> Trevino et al 1999. See also, the Ethics Resource Centre at <http://www.ethics.org/research/surveys-and-benchmarking.asp>

<sup>xxix</sup> Peter Comley, *Online Survey Techniques: Current Issues and Future Trends*, Interactive Marketing, Vol 4, No 2, October/ December 2002, pages 156-169 at page 160

---

<sup>xxx</sup> We have noted already that we shouldn't over-interpret the complaints data by taking it to be a measure somehow of the incidence of misconduct among lawyers and law firms - see note vii above. The problem with relying too heavily on self assessment audits undertaken by legal practitioner directors is the likelihood that the legal practitioner directors of the firms most at risk are the most likely to overstate their firm's compliance.

<sup>xxxi</sup> Say, for example, that a law firm has 100 employees, that we require 50 of them to complete the survey and that their charge out rate on average is \$300 per hour. The total cost to the firm, if the survey takes 30 minutes to complete and that time is conceived as time that would otherwise be put to billing clients, is \$7,500. The cost on these same assumptions to a firm that has 10 employees who undertake the audit is \$1,500. Those are not significant compliance costs for firms of their respective sizes – and are readily outweighed by the benefits and pale into insignificance compared to the dollar costs and the price one could put on the reputational damage consequent upon even a one-off instance of employee misconduct.

<sup>xxxii</sup> section 705

<sup>xxxiii</sup> The comment was made in private correspondence.

<sup>xxxiv</sup> Fortney, *Soul for Sale*, above

<sup>xxxv</sup> This would almost certainly require a legislative amendment in Queensland to allow us to require a legal practitioner director to produce the client files notwithstanding any duty of confidentiality the firm owes its clients (and requiring us of course not to disclose the information we obtain or to use it for any purposes other than discharging our regulatory responsibilities under the Act).

<sup>xxxvi</sup> This is a familiar strategy in the context of testing the quality of customer service provided by retailers, for example, but it can and has also been used to test the quality of professional advice including legal advice. ASIC have used mystery shoppers to test the quality of financial planning and superannuation advice (for example, see ASIC Report 18, *Survey on the quality of financial planning advice*, February 2003 and Report 69, *Shadow shopping survey on superannuation advice*, April 2006) and researchers in the UK have used mystery shoppers to test how lawyers respond to clients who approach them for advice in areas of work outside their areas of specialist expertise (for example, see Richard Moorhead and Avrom Sherr, *An anatomy of access : evaluating entry, initial advice and signposting using model clients*, 2003, <http://www.lsrc.org.uk/publications/modelclientpaper.pdf>)

---

<sup>xxxvii</sup> Ted Schneyer, *Professional Discipline for Law Firms?* 77 Cornell Law Review 2, 1991-1992, pp.11, 14 and 31.

<sup>xxxviii</sup> Chambliss and Wilkins, 2001-2002, p.336.

<sup>xxxix</sup> The obligation on legal practitioner directors to “keep and implement appropriate management systems to enable the provision of legal services... under the professional obligations of Australian legal practitioners” is more explicit than but hardly a radical extension of the current requirement of law firm partners under Rule 37 of the Legal Profession (Solicitors) Rules 2007. The rule says “a principal is responsible for exercising reasonable supervision over solicitors and all other employees in their provision of legal services by the law practice.” The Riley’s Solicitors Manual notes that “the duty on partners to supervise their staff goes beyond direct supervision [and] includes having appropriate systems and procedures in place which prevent, detect and deter misconduct by employees.” Rule 37 has its counterpart in Rule 5 of the Solicitors Regulation Authority Code of Conduct for England and Wales and in the American Bar Association’s Rule 5.1. These existing rules read very similarly at the end of the day to the obligations of legal practitioner directors.

<sup>xl</sup> We are referring to the best practice principles enunciated in the draft report of the Administrative Review Council headed *Government Agency Coercive Information Gathering Powers*, in particular best practice principles 2 and 19 which require agencies to have ‘reasonable grounds’ before using coercive information powers and to exercise their powers so that the compliance costs are ‘proportionate to the potential significance of the information sought’.