

KUALA LUMPUR | MAY 2014



"I'm certain I speak for the entire legal profession when I say that the fee is reasonable and just."

The economics of fee scales

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Personal views of author. Does not represent opinion or position of any institutions to which he is affiliated.

Contents

- The economics of fee scales
 - Theory of why harmful
 - Evidence from studies
 - Theory of why beneficial
 - Interaction with other types of regulation
- The political economy of fee scales
 - Challenge of self-regulation
 - Protecting consumers / empowering consumers
- The need for evidence based regulation

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Fixed fee scales harm competition by reducing the ability to “win business”

- If fee-scale set at a cost-reflective level
 - Firms can not win business by reducing fees
 - Substantially reduces incentive to be more efficient
- If fee scale is set higher than costs
 - Equivalent to collusion
- Who sets the fees? Who says if it’s “too high”?

Fixed fee scales harm consumers by reducing price dispersion

- Some consumers want cheap services
 - Fee scales prevent them accessing cheap services
 - They are removed from the market
- Some consumers want premium services
 - Fee scales prevent firms from offering high-price premium services
 - Premium consumers' demands are not met

Fixed fee scales can harm business by mismatching capacity

- Fee levels that are “too high”
 - A large number of firms chasing a small number of profitable clients
 - Excess capacity, reduced profitability
- Fee levels that are “too low”
 - Firms not able to increase fees to manage demand
 - Directly reduces profits

Recommended fee scales are also likely to be harmful

- Behavioural economics → provides a “price anchor”
 - Consumers compare to the fee scale
 - Firms benchmark to the fee scale
 - Softens price competition

Economic evidence suggests even recommended fee scales are harmful

- Arnould and Fiedland (1977)
 - Lawyers in US districts with fee scales earn more
- Stephen (1993)
 - 60% of Scottish conveyancers charged at the fee-scale level
- Schinnick (2003)
 - Scale fees used as focal point in determining conveyancing fees.

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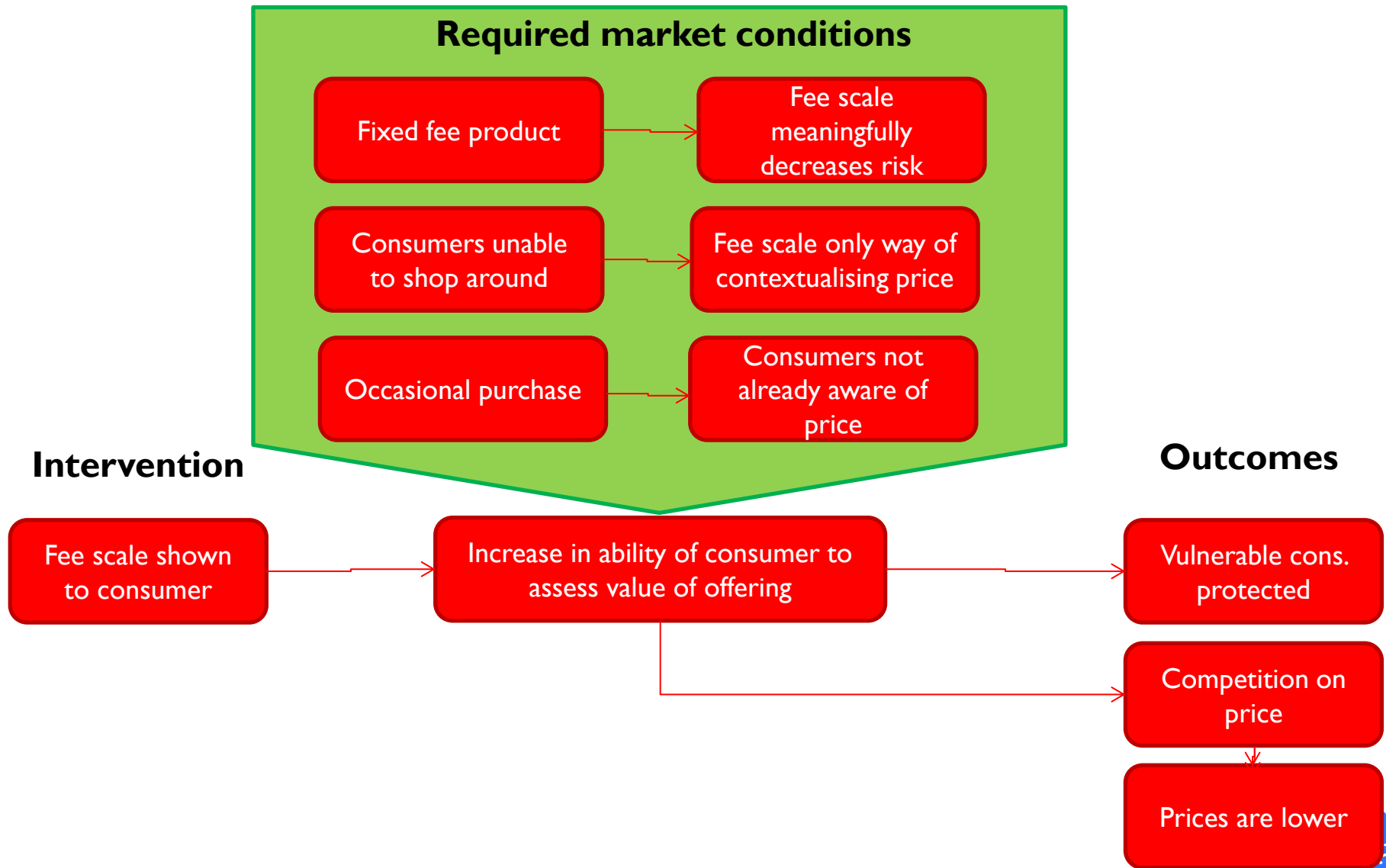
What does a recommended fee-scale do?

- Provides **information** to the consumer
- Reduces **incentive** for firms to undercut each other on price

Fee scales might protect vulnerable consumers and reduce search costs

- Knowledge of fee scale allows consumer to spot both bargains and fees that are “too high”
- This requires:
 - **Inability to shop around** → perhaps a pressured sale
 - **Consumer is informed of scale at point of decision** → can compare
 - **Fixed fee** → limited residual uncertainty

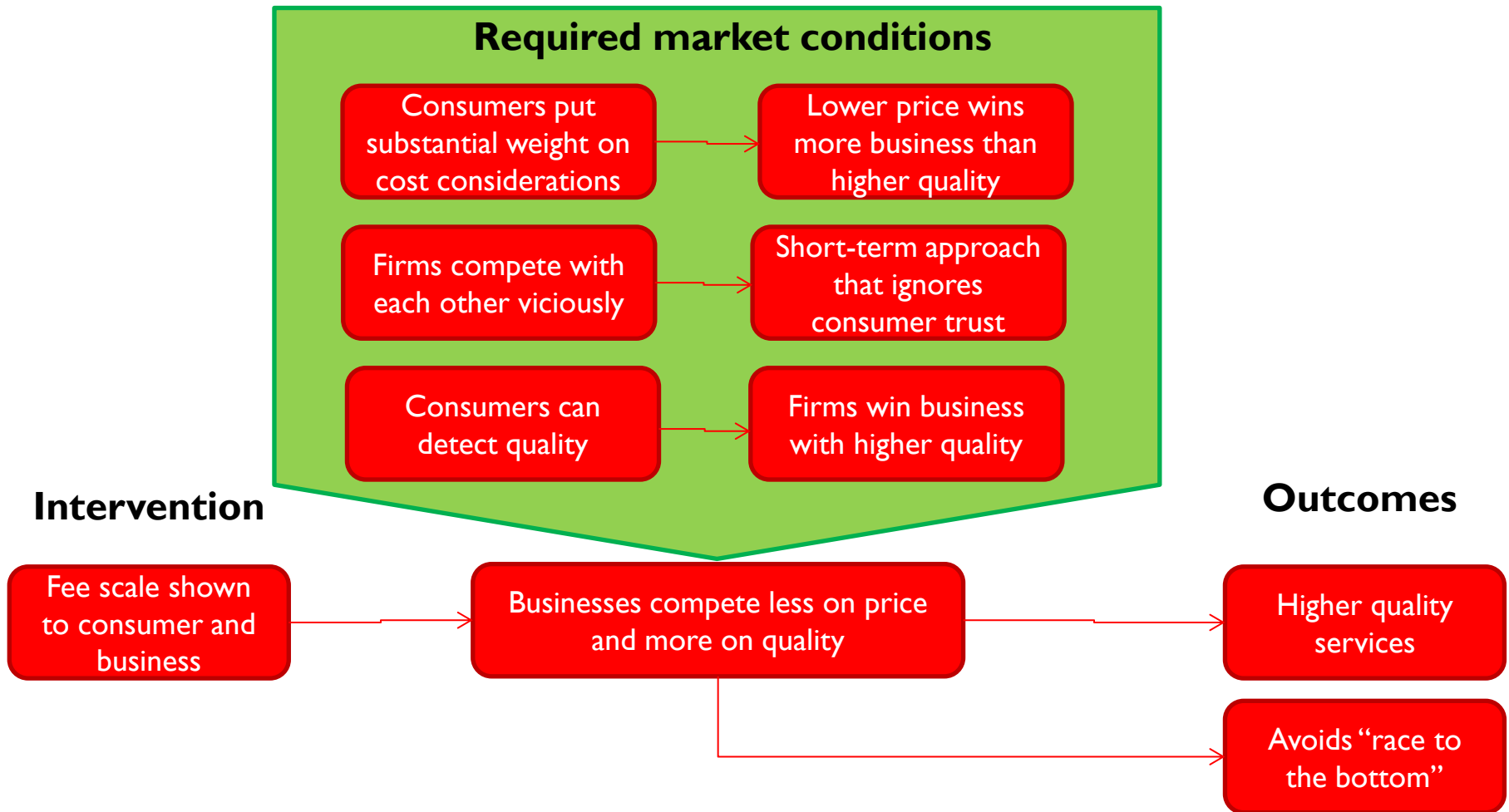
Intervention logic model for reason 1



Fee scales might prevent firms from competing “too hard”

- **Focussing competition on service**
 - Encourages firms to compete on service level, not on price. Prevents “**race to the bottom**”.
- For rationale to be credible, requires:
 - **Consumers can choose on quality** → firms compete on quality
 - **Consumer somehow focusses too much on cost** → would ignore quality if prices differed widely
 - **Consumer is informed of scale** → can compare
 - **Fixed fee** → limited residual cost uncertainty

Intervention logic model for reason 2



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Other types of regulation

- Information provision to help consumers choose
 - Price comparison services
 - Standardised pricing templates
 - Removing restrictions on advertising,
 - etc.

Other types of regulation

- Other ways to regulate fees
 - Ombudsmen services
 - After-the-event review

The logo features the word "LEGAL" in a pink, cursive script font, followed by "OMBUDSMAN" in a black, sans-serif, all-caps font. The entire logo is enclosed in a thin black rectangular border.

LEGAL OMBUDSMAN



Financial
Ombudsman
Service

Other types of regulation

The image shows a screenshot of a website for legal services comparison. At the top left, the logo for 'local surveyors direct' is visible, with the tagline 'the price comparison site for legal services'. To the right of the logo is a search bar and navigation links: 'Member Login | Logout | Give Feedback | Join Us | Contact Us'. Below the search bar are social media icons for Twitter and Facebook, both labeled 'Follow us'. The main heading is 'Compare Legal Costs'. Below this is a navigation menu with links: 'How It Works', 'Consumers', 'Businesses', 'FAQs', and 'Legal Services'. A large banner for 'Accountant-quotes.co.uk' is featured, with the text 'FIXED COST QUOTES FOR' partially visible on the left. The banner includes a circular badge that says 'get up to 5 quotes'. Below the banner, there are three columns of text: 'Quick & easy' (Connect with local accountants in minutes. Fill out the form below), 'Secure' (Compare ratings on accountants. Your contact details are treated securely), and 'Free' (Get up to Free & no). At the bottom of the page is a horizontal menu with categories: Debt, Accident Compensation Claims, Property, Wills and Probate, Divorce and Family, Road Traffic Offences, Employment Claims, Disputes, and Business Law.

local surveyors direct
the price comparison site for legal services

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Your contact details are treated securely

Free
Get up to Free & no

Debt Accident Compensation Claims Property Wills and Probate Divorce and Family Road Traffic Offences Employment Claims Disputes Business Law

Other types of regulation

- Quality controls to prevent a “race to the bottom”
 - Continued professional assessment
 - Robust independent complaints and redress processes
 - Public record of complaints / success rates / service comparisons

Other types of regulation



Health A-Z

GP Dr U K

Telephone: 011
Address: Fosse
LE3 0QD
Website: Webs

Overview Service

Ratings ⓘ

2.5 Stars

 **Anonymous** gave Dr U K Roy a rating of 1 stars

Rude Doctor

New to Leicester I signed up to this doctor as it was close by to where I live.

About 6 months later I needed to make an appointment with the Doctor. I managed to get the last appointment of the day so this may be why they were so rude (but still inexcusable). It took me a week to build up the courage to see them as I was very nervous. When I saw them however, they said that I looked (!) perfectly healthy and that I was wasting their time! They refused to even look at me or refer me to somebody else. I questioned them several times but they kept saying I was "young and healthy looking". I was mortified and angry. I soon went to a different practice who actually helped me.

On the plus side, the receptionist was very friendly and helpful.

Visited in September 2013. Posted on 19 January 2014

[Report as unsuitable](#)

Other types of regulation

- Quantity regulation interacts with fee scales
 - Ensuring quality by restricting supply is inefficient and raises prices
 - Fee scales may be set so that current supply matches demand, but if supply is liberalised than fee scales will lead to substantial inefficiencies

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The challenges of self-regulation

- Problem with professional bodies
 - **Advocate** for the profession vs.
 - **Regulator** of the profession in consumer interests



Reasonable people differ on how much we should protect consumers

Continuum of opinion

“Hard nosed”

- Standard consumer and competition laws
 - No collusion
 - Fair advertising
 - Contract law
- Consumer can litigate if don't like it

“Soft heart”

- Active consumer protection
 - Protection against exploitative behaviour
 - Specialised ombudsmen, etc.)
- Soften competition
 - Regulation of entry,
 - Fees

I think it is unrealistic to be too “hard nosed”



"I'm certain I speak for the entire legal profession when I say that the fee is reasonable and just."

Drawing by Leo Cullum; © 1995
The New Yorker Magazine, Inc.

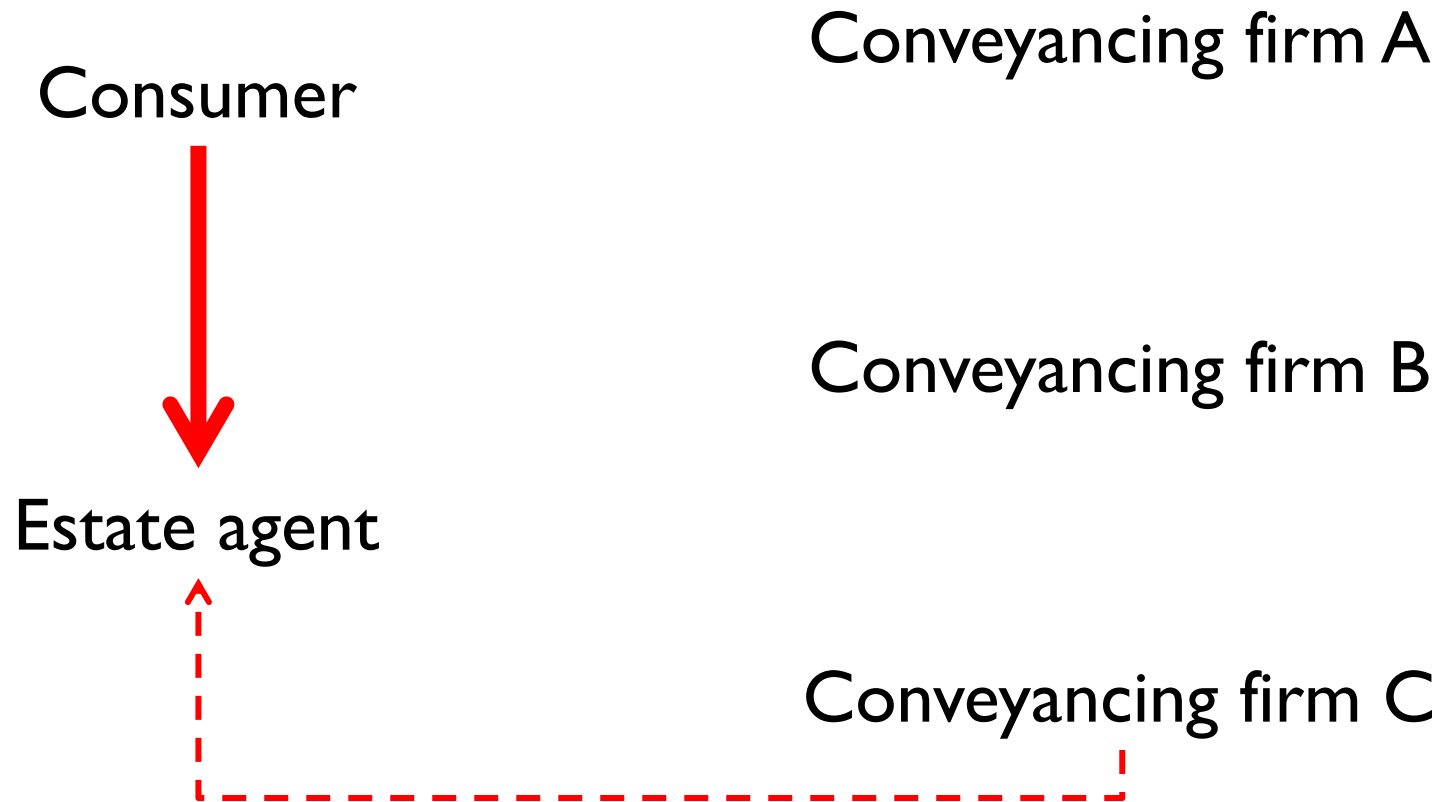
There has to be a middle ground

- Expect too much:
 - **Market failure** → Economically inefficient
 - Dereliction in government **duty of care?**
- Expect too little:
 - Consumers don't learn
 - **Limited market** → Economically inefficient
 - Undermine scope for **agency?**

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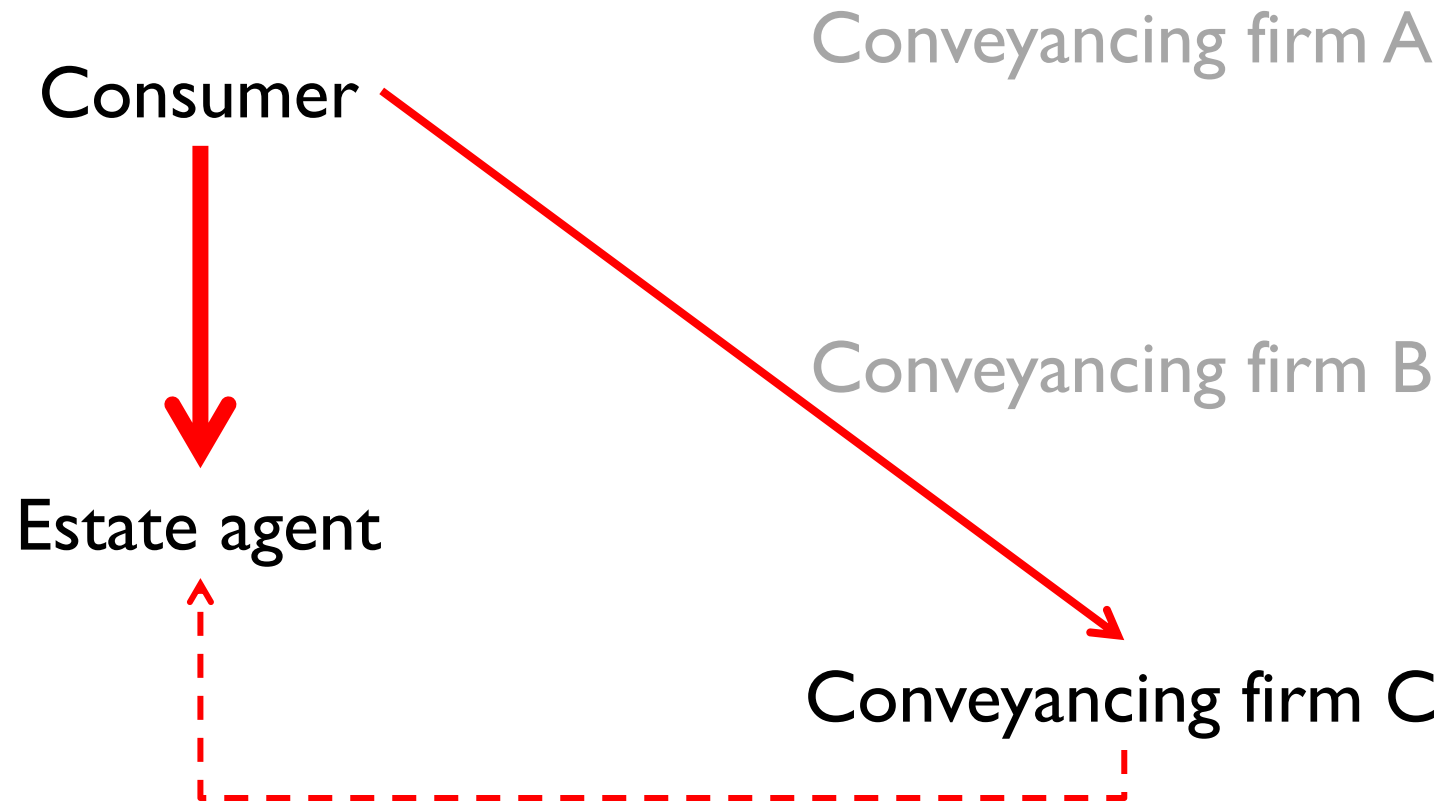
Case study: UK conveyancing market



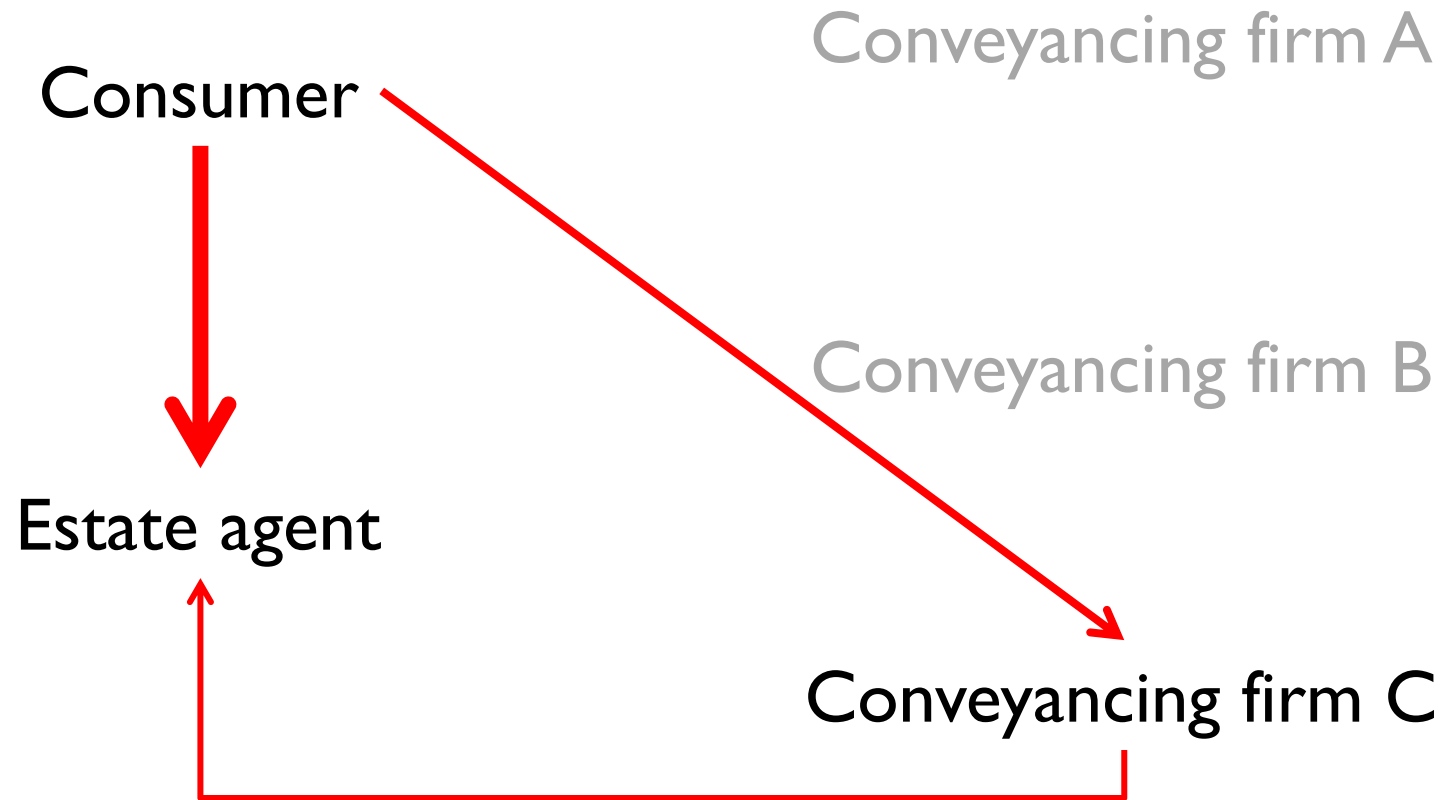
Case study: UK conveyancing market



Case study: UK conveyancing market



Case study: UK conveyancing market



Case study: UK conveyancing market

- Concerns
 - Consumer trust in estate agent being abused
 - Consumer pays too much for conveyancing
 - Consumer gets a low quality service
- → Law Society of UK wants them to be banned
- → Dedicated conveyancing regulator does not

Case study: UK conveyancing market

- Research
 - Those who choose a conveyancing firm through a referral arrangement:
 - → Pay less
 - → Receive a higher quality of service
- Why?

Case study: UK conveyancing market

- Large efficient firms expand their business through the payment of referral fees
 - Economics of scale → lower costs
 - Importance of brand → higher quality
- But, some concerns in rogue cases
 - New transparency guidelines brought in

Case study: UK conveyancing market

- Note: a different approach taken in personal injury cases
 - Had created an excessive market in “claims management companies” trying to find “injuries”
 - Led to inflated legal costs, particularly in relation to state-funded legal-aid
 - Banned in 2013

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Right Touch regulation

- **Identify** the problem
- Adopt a **proportionate response** – minimum intervention required
- Be **consistent in your levels** of intervention
- Be **transparent** in deliberation and conclusion

Identify the problem

- What is the consumer harm?
 - High prices?
 - Low quality?
 - High variability in prices / quality?
 - Vulnerable consumers harmed in particular?
- What is causing this harm?
 - Information problems?
 - Lack of ex-post redress options?
 - Insufficient regulation?
- **Get hard evidence**

Adopt a proportionate response

- What is the *least invasive* way to try and correct the problem?
- What will be the positive effects of the proposed response?
- What will be the negative effects?
 - On the market now?
 - On how it might develop in the future?
- Get **hard evidence**

Be consistent in your levels of intervention

- High entry barriers to “protect quality” without other measures?
- Fee scales to “protect the vulnerable” without other measures?

Be transparent in deliberation and conclusion

- Consult on regulation, from a zero base
 - Clear in reasoning
 - Supported by evidence

- Explain conclusions
 - Clear in reasoning
 - Supported by evidence
 - Detailed evaluation and monitoring plan

Conclusion: the regulatory map

	Market supporting regulation	Market changing regulation
Price	Require consistent pricing	Fee scales Setting fees Ex-post ombudsman review
Quality	Collation and publication of satisfaction and complaint statistics	Entry accreditation On-going accreditation Ex-post ombudsman review
Competition		Limiting advertising Limiting competition

The fee scale challenge

1. Appropriate consumer-focussed regulatory system
 2. Evidence of a problem
 3. Theory of how fee scales will solve it
 4. Alternative less harmful approaches tried first
 5. Transparent system monitoring impact
- **THEN** probably OK to try a fee scale