THE CURRENT AND FUTURE STRUCTURE AND INTERNAL ORGANISATION OF THE LEGAL PROFESSION
- A NEW INSTITUTIONAL PERSPECTIVE

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ABSTRACT:

Economic analyses of legal partnerships are conspicuous by their absence. Recent theoretical developments within increasingly interconnected areas of law, economics and organisation facilitate more useful analysis of such issues. The resultant theoretical framework provides an ideal backdrop against which regulatory and related internal and external organisation issues concerning the legal profession in general, and law firms in particular, are discussed. Regulatory issues are discussed in the context of primary information collected during interviews with law firms.

Partnership is one of only two currently legitimate practice options for UK solicitors in private practice, the other being sole practice. Presently prohibited corporate and multi-disciplinary practice (MDP), are under current consideration in response to growing pressure to attenuate restrictive regulation. Current proposals for further deregulation threaten professional partnership as an institution.

Conventional wisdom argues partnership with joint and several liability is appropriate for legal service provision, where partners monitor each others' work quality and have an incentive to through cross-guaranteeing personal liabilities. Mutual monitoring, although important, is not the sole function of partnership, which performs a pivotal role in the wider professionalisation/ socialisation process of the lawyer, and in screening processes within firms. The comprehensive set of strengths and weaknesses of partnership and alternatives thereto are empirically assessed.

Certain partnership problems, particularly those of large multi-partner firms, would likely simply re-emerge within alternative practising arrangements. Large firms confront mutual monitoring difficulties, reluctant delegation of decision making authority and cumbersome decision making procedures. The current tendency of growth in partnership size places great strain on partnership and question its longer term viability. The survivability of traditional screening procedures and informal incentive-penalty-reward systems within large modern partnerships are assessed within this thesis. Permitting a wider set of organisational options may do little to ameliorate these and other problems.

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-oOo- THESIS CONTENTS -oOo-

-CHAPTER ONE-

Background and general issues in the current structure of the solicitor profession:

Introduction:

This thesis focuses on salient features of the current and future structure and internal organisation of the legal profession. The resulting economic analysis conducted examines these features using the prism of newer, primarily contractual based, theories of the firm. These theories combine to play a central role in providing building blocks which together constitute the analytical environment from within which actual behaviour of a sample of law firms has been empirically observed.

The thesis will commence by initially examining issues in the current structure and organisation of the solicitors profession and describing a methodology suitable for conducting an economic analysis thereof. The remainder of the thesis follows four major themes. Chapters Three, Four and Five present the broad theme of economic organisation of relationships between the firm and its clients. Chapter Three examines general literature of the economics of organisation, not specifically relating to law firms, Chapter Four outlines its specific relevance to the law firm, with Chapter Five presenting empirical observations relating to the client/ firm relationship.

Chapters Six and Seven share a eommon theme of investigating organisation of economic relationships between partners of the law firm. The internal organisation and ownership structure of partnership as a mechanism for dividing income between partners and binding partners together is examined in Chapter Six. Chapter Seven presents empirical observation of these issues for the sample firms.

Chapter Eight's theme is an examination of the organisation of economic relationships between partners and QAs of the law firm, focusing particularly on screening mechanisms, promotion tournaments and up-or-out rules employed in partnership. This chapter also examines empirical information collected to investigate these issues for sample firms.

Chapter Nine's theme is future oriented, looking towards the future of the legal profession and considering alternative practising modes given uncertain longer term survivability of partnership as a mode of governing economic relations across all dimensions discussed in preceding chapters.

By shifting through these themes the thesis broadly focuses on the current and future structure and internal organisation of the solicitor branch of the legal profession. The aim of the thesis is, firstly, to provide an economic rationale for the current structure and, secondly, to assess the likely effects

of any attempt to precipitate structural change. Analysis is conducted against a backdrop comprising newer organisational theories of the firm and current Government proposals for a complete overhaul of the solicitor branch of the legal profession.

As a precursor to examining how solicitors internally organise their firms, it is necessary to examine the background to the current structure of the legal profession and to establish the link between structure and its effect on the manner in which solicitors internally organise their firms. It will be demonstrated that the restrictions imposed on practising arrangements for solicitors are essentially determinative of the current structure and impinge to a large extent on the manner in which solicitors internally organise their firms.

It is intended this first chapter will initially serve as an introduction to the background underlying the current structure, highlighting the nature of the regulation problem in relation to the legal profession. Following this, some assessment of the Government's probable objectives in relation to legal services and regulation thereof, will be attempted.

The section following this will detail specific restrictions on law firm organisation which will be examined to expose finer details of the current structure and its intended consequences.

The final section will outline major features that characterise a profession in general and will also focus attention specifically on characteristic features of the legal profession. This section is aimed at revealing features of the profession of importance in determining how stringent regulation of its members should be and how successful self regulation can be expected to be.

Section One: Structure, Organisation and Regulation.....an overview.

1.1 The economic significance of structure and the importance of understanding its origins:

It is vital for any existing (or proposed) structure of an industry to be conducive to innovation, as it is this 'perennial gale of creative destruction' which is argued to be strongly determinative of the ability of an economy to achieve expansionary growth [1]. The structure of an industry has a marked effect on the prices, costs and quality of products/ services etc. of that industry. For this reason, proposals for substantial structural change must only be made when their proponents are as fully aware as possible of the likely effects such changes would have across these dimensions. In the absence of a comprehensive understanding, proposals will almost certainly be incorrectly based and consequences of their adoption, potentially unexpected.

The implementation of efficient and effective regulation, therefore, requires as a prerequisite as complete an understanding as possible of the background underpinning current structure, its origins, and the factors that precipitated the original regulatory framework. Additionally, an understanding of changes that have occurred within the external practising environment in the period between regulation and proposed re-regulation, is essential. Without this understanding, formulation and effective administration of policy aimed at precipitating regulatory change is likely to have unpredictable consequences. In terms of securing a specific desired outcome, attempting to change an unknown quantity may at best only have a random chance of success. In short, knowledge of the evolutionary process involved will always be incomplete but failure to increase this stock of knowledge heightens chances of ineffective policy making, encourages irrational policy formulation and induces ad-hoc policy application with, at best, unpredictable consequences.

1.2 A brief initial introduction to current structure of the UK's solicitors profession:

The legal profession in the UK consists of the twin long standing, yet independent, institutions of solicitors and barristers/ advocates. Whilst acknowledging that their respective structures and resultant practising arrangements of course impinge upon each other, this thesis focuses exclusively upon the solicitor branch of the profession.

The structure of the solicitor branch of the legal profession can be regarded as unusual in terms of industrial organisation as it embodies few organisational forms. The immediate reason for this is the existence of specific legislative and regulatory limitations on practising arrangements. The purpose of these limitations is to restrict the choice of organisational form from which solicitors may offer their services. An initial goal in relation to the practice of UK solicitors has thus been identified - the goal of fostering a restrictive structure that directly imposes specific constraints on solicitors practising in private practice.

1.3 Government policy towards solicitors in the U.K.:

The Government of the day will possess a set of objectives in relation to the profession and through a combination of its regulatory legislation and self-regulatory rules of the Law Societies, it anticipates these objectives will be fulfilled. There is an unfortunate tendency for the apparent success of a current regulatory environment to cause that framework to be viewed in some sense as optimal. In the case of the solicitor profession, while it is undoubtedly the case that the current regulatory framework may attain many (if not all) of the Government's objectives, increasing numbers subscribe to the view that current regulation is not sufficiently flexible to facilitate

evolution of practising arrangements capable of accommodating the swift and constant substantial change in the contemporary market for legal services.

In view of this substantial change, doubts have been growing as to how able and, therefore, how appropriate current structural arrangements are in dealing with current, and more importantly, further future developments in legal services. Recognising this, the government has recently acted as a catalyst to introduce sweeping regulatory change throughout the legal profession. The current Government's bent towards free market philosophy, so evident in many areas of its policy formulation, has had the unprecedented effect of challenging certain areas of the legal profession's traditional safe haven. In order that the legal profession may be more able to adjust to dynamic changes in the market for legal (and other related) services, the Government has diagnosed that the profession requires a much looser regulatory framework. The Government apparently subscribes to the view that if structure is subject to overly tight control, the Profession is likely to become increasingly unable to adjust to changing demand patterns in legal and related services.

1.4 The nature of the final product.....a need for regulation?:

The above discussion largely eschews the basic issue whether regulation of the Profession is actually necessary or desirable. This section aims to convince the reader that there are in fact sound reasons, based on protecting the consumer from information asymmetry, for insisting that the profession is subject to some form of Government regulation.

In any form of industrial economic analysis an important factor which must be identified is the nature of the final product and the market it serves. In the case of the solicitor branch of the legal profession, the final product is intangible and can be classified as a service. The legal profession, being a member of the service industry species, places an entirely different set of demands upon the organisational form of its service providers, than is the case for the producer of a conventional tangible product.

1.5 Protection of the consumer from information asymmetry:

The producer of a physical product or service will typically wish to convey certain information, primarily relating to price, quantity and quality, to its prospective consumers. Where a product is tangible, consumers are readily receptive to price, quantity and quality information and are able to easily assess the product's physically observable characteristics against comparable and competing products in the market. In the case of services, this type of information is less easily perceived and

evaluated the typical consumer. For the typical consumer of legal services, the major implication of this is that a significant, if not severe, deficiency of information regarding relative prices and quality of legal services of competing suppliers in the market has to be confronted. Due to this lack of information and knowledge of the consumer, the characteristics of the market for legal services require quite distinctive and careful treatment in economic theory and analysis.

It is demonstrated above that the nature of services require them to be treated differently in economic theory, but further complexity is introduced as a result of these services being legal services. In the UK, the right to justice, independent of financial means, is perceived as being one of the civil rights of each citizen. Legal services essentially exhibit similar characteristics to 'merit goods' - while it would be foolish to claim that the Government views their consumption to be desirable, they do view reasonable access to them as desirable, encouraging this via subsidy and/ or protective regulation.

1.6 The inevitable entrance of the Government's value judgements:

In the case of the legal profession, the government plays a front line role in social efficiency considerations. The Government's view as to what constitutes social efficiency is reflected in the manner in which it permits the legal profession to operate. In the UK, the final product of the legal profession has been deemed to be distributed on a "need" rather than a "willingness to pay" basis and the Government is, therefore, duty bound to uphold a right of access to legal services and ensure that the legal profession upholds its obligation to provide them.

It is a concern of many whether the existence of restrictive practices in the market for legal services results is necessary to control the practice of the profession and indeed whether they are detrimental, or conducive, to efficiency. The Government faces the problem of society viewing its notion of social efficiency in terms of how it chooses to regulate the profession. Past Government regulation has permitted legal services to become perceived as a right. It is too easy nowadays for Government regulation of legal services to be criticised since the system appears to fall short of upholding this right of access for every individual. How to obtain social efficiency, however defined, in the market for legal services constitutes a substantial policy-making problem for Government. One measure of the effectiveness of the structure of an industry is arguably how conducive it is to attaining social efficiency.

By its very nature, this area, like many areas of Government policy-making, will be contentious as value judgements will have to be made at the level of defining what constitutes social efficiency. Value judgements also enter at the level of assessing whether or not the current structure is conducive to, or detrimental to, social efficiency according to this definition. They again enter when alternative practising arrangements, and the likely respective effects of their introduction, are

discussed. While this is not a problem specific to research into the market for legal services but rather part of a wider problem economics as a social science must face, it is mentioned here as a reminder of the importance of recognising and making explicit the role of value judgements in economic analysis.

Where, as is the case in legal services, the final product/ service is viewed as the right of the individual, the definition of social efficiency will tend to have easy access, and an equitable distribution, high on its list of constituent elements. Increased social efficiency in legal services could clearly be achieved by in some way addressing the identified areas of unfulfilled need in legal services, if the above definition is accepted.

When it is contended that increased access can enhance efficiency, it must be remembered that this statement itself involves expression of a value judgement. Any efficiency comparisons will by their very nature, involve the offsetting of gains and losses in public and private welfare with subjective weighting attached to each.

The government is faced with the problem of balancing competing forces to the extent that;

1. It must allow the profession sufficient autonomy to operate effectively,

2. It must ensure the profession fulfils its obligation to provide legal services in order that consumers' rights are respected, and,

3. It must establish the correct balance between "laissez faire" and intervention to maintain trust and confidence in a market whose proper functioning is dependent upon such characteristics.

The basic problem is that although the individual assigns the government the duty to uphold a right to legal services, it is not the government itself who ultimately service this right. The legal profession act as agents of the government, creating a problem of infinite regress - Who regulates the regulators?

The profession, in defending its monopoly structure and anti-competitive practices, argue that its constant adherence to ethical and professional standards at all times, obviates any requirement for rigorous external regulation. If it is accepted that the profession does practice ethically at all times, then self-regulation appears to be a rational and effective mode of regulation.

The Government regulates the profession via its self-regulatory agent, The Law Society, and subsidises consumption of legal services through its Legal Aid scheme. As indicated before, the

Government does not view consumption of the service itself as desirable - only that the right of access is honoured and respected for every citizen irrespective of wealth. To this extent, it is perhaps better to view access to legal services rather than the legal service itself as the merit good. It would be an unwise government that either encouraged unnecessary consumption of legal services, or that did not offer reasonable access to legal redress to protect individual liberties. The regulatory regime chosen attempts to create a sensible balance between these essentially opposing forces.

1.7 Market failure and the resultant attempt by Government to ensure 'reasonable access':

The duty of determining what constitutes 'reasonable access to legal services' is incumbent on the Government due to market failure in providing a viable solution. Consequently, as is evident from the above discussion, any resultant regulation implicitly embodies the Government's value judgement regarding legal services. The entrance of value judgements is an endemic feature of policy making and analysis, and is indeed a prevalent characteristic of most economic enquiry. Resultant analytical discussion of these issues, however, remains uncompromised where the inherent nature of value judgements is acknowledged and other analytical limitations are similarly conceded.

A broad spectrum of unique and conflicting individual philosophies can be identified regarding the status of legal services ranging between the two extremes of them being viewed as a basic civil right or viewed as a privilege. The Government in its guise of regulator of the legal profession has the unenviable task of having to select a popular compromise of the myriad of diverse individual philosophies regarding the status of legal services, and impart this selection on the market. The compromise solution will be selected with reference to efficiency of regulation and equity and distribution of legal services. In essence, what the Government attempts is 'socially efficient' regulation of legal services, what ever the Government judges social efficiency to comprise of. Opinions ventured supporting or denouncing the success, or otherwise, of the chosen regulatory framework in creating a socially efficient market for legal services, will be similarly subjective.

1.8 The resultant restricted set of valid organisational forms:

The solicitor branch of the legal profession is basically restricted to two organisational modes. The first of these, the less common of the two, is the sole practitioner, with the second being the far more popular professional partnership. The striking feature of the legal profession, and to a lesser extent many other professions, is the conspicuous absence of corporate organisational forms. This is not merely a quirk of pure chance but rather the result of a desire for the practice modes of the legal profession to evolve solely in non-corporate forms. In terms of the structural analysis of the

legal profession being conducted here the, desire to restrict legitimate organisational choice in this manner is obviously of central importance and requires rationalisation.

A necessary precursor to providing a rationale for current structural arrangements involves outlining what the expected consequences of such a limitation are likely to be. The apparent desire to restrict choice of organisational form indicates that a "laissez faire" policy in relation to legal services would be likely to produce undesirable effects in terms of efficiency, equity and distribution (ie. market failure). This demonstrates the importance that must be assigned to scrutinising any policy proposals to alter structure, to ensure their foundations are set in sound economic logic. In this respect, it is imperative to determine whether any proposed structure would be likely to continue to fulfil the objectives in relation to legal services, outlined above.

1.9 Challenging the status-quo....why change the regulatory framework?:

In typical debate concerning regulatory change, it is often naively argued that the apparent success of the current regulatory framework is a good enough reason for retaining it and staving off any attempt to change it. This serves to illustrate a problem that exists throughout much of economics, that being the naive view that for a current state of affairs to be sustainable, it must be efficient or, at the extreme, optimal. This view is incorrectly based as it implicitly ignores the importance of unique historical events and the dynamic nature of economic exchange and relationships. In the case of regulation, the absence of constant adaptation to changes in the external practising environment will result in regulation becoming increasingly unable to meet the demands of modern practice. The regulatory framework will become increasingly less appropriate and less efficient becoming more of a hindrance than an aid to orderly practice. Efficient regulation requires a flexible and dynamic framework which can sequentially adapt to changes in the external practising environment.

In the specific context of legal services, current policy clearly impedes the operation of a free market. It should not be taken as read that the source of market failure that precipitated the initial regulatory framework still exists. If the source is no longer a problem then the current regulation could be regarded as inappropriate. If it still is a problem, then it may be the case that new regulation with an altered focus may be more appropriate than the old framework. A failure to recognise such change can easily lead to obsolete policy which can needlessly impede free commerce and can dull the propensity to be innovative in terms of new services and practice options. It is unquestionable that this is likely to be detrimental to efficiency.

It is often argued that what is required is a complete overhaul of the system of provision of legal services. Some argue that the market mechanism is far too imperfect to provide legal services and what is required is organised state provision. Proponents of this view have little confidence in either

the market or in self-regulation (combined with restrictions and regulations) to ensure the desired outcome [2]. When structural change is considered for an industry, more than a passing glance should be paid to the changes in distribution and equity that are likely to be caused by structural change. This should be reflected in considerations of social efficiency.

1.10 Major elements casting doubts on current structure and regulation:

The current structure of the legal profession can be regarded as being subject to major forces which in combination are threatening to undermine its current organisation. This casts doubts on its ability to adapt flexibly enough to current and future developments both within the legal profession itself, and in significant areas of related business. These primary forces of change are discussed below.

1. The Government is pressurising the profession to introduce freer competition, both within the legal profession, and between the different professions.

2. The recent revolution in financial service provision has resulted in many people extending their job descriptions and entering areas of work which were traditionally well defined between different service practitioners.

3. Increased harmonisation within Europe since 1992 and beyond has forcibly pushed different professions and service practitioners to take a more strategic and less myopic view of their position in the market-place for professional and related services.

From the perspective of the legal profession, increased competition, or at least the threat of it, has forced lawyers to adopt more business-like attitudes and to become more aware of the specific nature of the 'product' they are selling to consumers. Some perceive a strategic advantage possibly accruing from combining legal and other professional or ancillary services within one organisation [3]. For this to be realised, paired with the fact that in future more concrete ties with foreign firms will become possible or even essential, it will be necessary for substantial change to take place in the manner in which the legal profession is regulated at present [4].

The market-place has also been subject to substantial change in recent years principally due to the rapid growth in the absolute volume of legal services, which can be seen to at least partially be a consequence of the expansion of laws and the increasing complexity of both UK and EC legislation. Hence, a healthy market still exists for the supplier of legal services but firms are realising that in order to ensure survival within a tougher modern market-place, they have to be leaner and fitter and rise to the challenges of what has become an increasingly 'cut-throat' commercial environment.

In terms of how this will affect the consumer of legal services, it is likely that firms will have to emphasise differentiation of their product from competitors. The traditional tools for doing so involve use of the vehicles of advertising and promotion to gain strategic advantage in relation to price and/ or quality competition. Firms will also be forced to look beyond these methods to find new and novel ways to survive in the market-place. As a consequence of having to fight harder for clients, firms may be forced to compete by providing more information to prospective clients, thereby reducing the traditional information asymmetry that exists between client and firm. For this to be to the advantage of the consumer of legal services, the information must be perceived by the consumer as further facilitating the choice of law firm, or rendering service quality evaluation an easier task. Essentially this requires consumers of legal services to become more sophisticated; a transformation that firms typically perceive to be currently occurring across client types.

In any case, the market will expose both winners and losers, but increased competitive pressures could be expected to precipitate a more urgent shakeout of less efficient firms than would have been the case in a more sheltered market. One major reservation is that should increased competition precipitate such a shakeout, this may seriously compromise the Government's goal of reasonable access to legal services for every citizen. Another potential problem is that there may be a tendency for those firms which do survive to become larger and more interested in serving commerce than the private client, thereby increasing concentration and reducing geographical coverage in private client services. This would merely compound problems of access for individual private consumers.

The already apparent and deepening split that has developed in the solicitors profession, between private client firms and commercial client firms, is likely to become still more pronounced in future via increased specialisation. A major concern here is that commercial client work, if it continues on its current path, may become increasingly more profitable than private client work, leading to a general shift away from private client work by a significant number of firms.

As has become strikingly evident in recent years, fewer and fewer firms are likely to continue to offer Legal Aid services. This service, already under severe strain (and some would say impending collapse) will cease to protect the very people most in need of protection of their rights of access. The result may be that the legal profession, in order to survive commercially, may increasingly turn its back on private client work, and in particular Legal Aid work, to concentrate on commercial clients, who can more easily afford to protect their legal rights irrespective of cost.

The growing complexity of processing modern commercial transactions, partly fuelled by the internationalisation of firms, often requires teams of lawyers to work on problems for long periods of time. This requires either that firms are large enough to be able to tie up a team of lawyers for

such a period, or that commercial clients externalise these transactions to specialist 'boutique' commercial firms.

Any resultant regulation will require to cope with these and other newer trends in the provision of legal services as they develop in the near future. The impact of increased competition may justify more stringent regulation in respect of private clients, than for commercial clients, for aforementioned reasons. If law firms do continue to become larger, as has been the trend in recent years, this may cast doubts on the continuing viability of the partnership mode of organisation. Such doubts precipitate a requirement to examine corporate and other practice forms to evaluate their likely success or failure in overcoming potential problems of large scale partnership practice. This would naturally require an abandonment of the current regulatory regime and the ushering in of a more liberal regulatory framework in relation to firm organisation.

The above should leave the reader with at least a flavour for some of the pertinent issues surrounding the organisation and structure of the legal profession in the wider context of regulatory discussion. These recurring themes will all be explored at greater length and in finer detail in the main body of the thesis.

Section Two: Plausible Government objectives/ concerns in legal service provision.

2.1 The wider regulation problem - focusing issues:

As a necessary precursor to any serious attempt at evaluating the puzzle of the structure and organisation of the legal profession, the problem must initially be placed in the wider context of the objectives the Government apparently sets in respect of legal services. What follows, therefore, exposes the wider regulation problem before embarking on a more sharply focused discussion of the separate issues identified during this process.

2.2 What actually are the Government's policy objectives?:

It is inherently difficult and problematic to attempt to identify exactly what the Government's objectives are in relation to any of the multitude of areas in which it has a policy making role. Firstly, in the quest to identify the Government's objectives, the observer can incorrectly perceive what these actually are. Subsequent analysis will be flawed to the extent that the objectives perceived by the observer may not coincide with the Government's actual objectives.

Secondly, history has proved it unreliable to accept stated government objectives to be those actually embodied in policy it administers. In many areas stated Government objectives appear

completely incompatible with the actions taken to procure their fulfilment. In essence, what the government says, what it does, and what it says it does, are often far from consistent.

Consequently, perhaps the most useful and reliable method of examining Government objectives in relation to the provision of legal services, is to import to the analysis an idealised/ model set of government objectives and examine the implications of their procurement for the structure of the legal profession. It is anticipated this will expose a rationale for the current evolved structure and provide justification for the current legislatory and regulatory framework perceived necessary to control provision of legal services.

2.3 The importance of identifying underlying objectives:

Continuing the theme in section one of this chapter, it is recalled that it is important to attempt to identify the Government's underlying philosophy in relation to legal services. This will have an obvious and direct bearing on how they decide to organise their provision. This underlying philosophy is likely to exist somewhere in the middle ground between the two extremes of legal services being viewed as basic civil right or a privilege. The stronger the orientation of the Government towards a free market philosophy, endorsing increased market liberalisation, the more attenuated will be its perceived philosophy of viewing legal services as a basic civil right.

2.4 Legal services - basic civil right or privilege?:

Any distribution of legal services resulting from them being deemed a basic human right, will almost inevitably require some form of protection from an unbridled free market solution. In the absence of some form of market regulation, it would be extremely unlikely that the Government could ensure for each member of society, protection of this basic civil right the Government has itself invested in the individual. In creating this right, the Government essentially assumes some duty to ensure that persons have access to at least a minimum of legal services and benefits of a full and fair judicial system, irrespective of income and wealth.

Should the Government embody a less egalitarian philosophy, upon which to base distribution of legal services, it will impose limits on its duty to exert control over the market mechanism. The Government effectively delegates its responsibility to the market to ensure an efficient and equitable allocation, having confidence in the ability of the market mechanism to do so. While it is true that a free market philosophy in legal services would be likely to garner productive type efficiency goals, the resulting allocative solution may be politically and democratically unacceptable. In subjecting allocation of legal services to the full force of the market mechanism, producers could be expected to more closely adhere to behaviour in keeping with 'Neoclassical profit maximisation', wherein fair and equitable distribution of legal services would likely take a

back seat. In metaphorical terms, the invisible hand of the free market would pick the pockets of the less well off and redistribute in favour of the better off in society.

The UK the legal system has evolved with an underlying philosophy whereby reasonable access to legal services of at least a minimum level should be the right of each individual. It has also evolved such that the Government should perform some role as custodian of this right by ensuring that the individual is able to exercise this right. The Government seeks to ensure this right of access is protected, and in the past it has done so by guiding the legal profession with a "less than invisible hand" from time to time.

The strongest form of Government intervention would be characterised by some form of organised state provision of legal services - an idea which has support from those who advocate state provision of legal services along similar lines to provision of state medical care by the NHS. Within the current system, however, Government and State are invested with coercive power to arrest any abusive or unethical practice by members of the legal profession and, in essence, the profession is contractually bound to the State to provide legal services. The authority of lawyers to practice their skills and provide legal services to members of society ultimately derives from the State. While this contractual obligation is incapable of precise definition and is naturally limited, it nevertheless results in the legal profession, not only being directly accountable to its clients, but also ultimately to the State.

2.5 Self regulation.....Government control at arms length:

On grounds of efficiency and independence, the Government is likely to perceive advantages in permitting the legal profession as much practising freedom as it reasonably can. This will have the effect of initially creating and subsequently sustaining trust and confidence in the market. Creation and maintenance of trust is essential in the market for legal services as the profession's very existence (and to a great extent its operation) depends on the strong social institution of trust. In the absence of trust, problems of quality evaluation, ignorance and uncertainty, and information asymmetries, that typically face consumers of legal services, would be an even greater problem than they are where trust is a prevalent characteristic of such a market.

The degree of government intervention thought necessary to control the profession can be viewed;

1. As reflecting the degree of trust invested in the profession by Government.

2. As also reflecting the Government's confidence in its ability to effectively self-regulate and,

3. As indicative of the status of the profession as perceived by the Government.

By creating the above situation, the Government hopes trust and confidence will percolate down through society creating a general public that is trusting and confident of the legal profession and its abilities. The government, however, must seek to avoid giving the profession too much freedom since complete liberalisation may be incompatible with the concept of legal services as a basic individual right. As with the majority of Government policy, it is hoped that the public interest receives at least recognition, if not priority, in the list of government concerns.

As a self regulating monopoly, the legal profession has control over legal services and information. It controls the types of organisations from which lawyers are permitted to provide legal services, and the amount of information that can be made publicly available to the consumer of legal services. The consumer, therefore, suffers from an information deficiency over which the profession has some degree of control. The extent of this information problem will vary from client to client and will also be prevalent to differing degrees in both private and commercial client work. It may be, for example, that commercial clients suffer from lower levels of information deficiency than private clients - this would constitute a less powerful argument for a requirement for a similar degree of regulation for both commercial and private clients [5]. This issue will be discussed later.

The conferral of self regulatory status on the profession results in certain powers and duties being invested in the profession. Self regulation can be defended on grounds that malpractice must be identified and avoided, with unscrupulous practitioners being exposed and expelled. The expected benefit of self regulation is that the profession's members have a vested interest in maintaining the credibility of their own profession. Consequently, through property rights they have a strong incentive to monitor and control to avoid personal loss. The profession is also arguably the best qualified/ most knowledgable to determine what is right and what is wrong in relation to legal practice.

Self regulation, if effective, can be expected to be successful in protecting those consumers who are at greatest risk from unscrupulous professionals through low levels of sophistication. Stringent and widespread professional self-control, however, restricts flows of information and results in weakened competitive pressures which can in turn result in a tendency for over-priced services. Benham and Benham (1975) argue that the profession's desire to control information flows stems from a belief that removal of commercial stimuli (which has the undesirable consequence of limiting consumers' knowledge) reduces potential benefits of those members of the profession who deviate from expected practice standards [6]. Consequently, Benham and Benham (1975) argue granting information monopoly may be one of the least politically sensitive and controversial methods for constraining the behaviour of suppliers and consumers to achieve desired outcomes [7].

2.6 Potential abuse of monopoly power:

By granting the profession self-regulatory status, the government does unfortunately precipitate another set of problems. These problems basically stem from the fact that professions are essentially monopoly suppliers and, as with all monopolies, the fundamental concern is the natural tendency for sub-optimal output to occur at a price which exceeds marginal cost. This is naturally detrimental to efficiency and the likely scenario of the supplier auctioning output at inflated market prices clearly conflicts with interests of the general public and objectives of distribution and equity.

The Government, therefore, relies on the trust of the profession to rigorously exercise its characteristically strong moral and ethical qualities to restrain its own members from extracting monopoly profits and reducing service quality. While restrictions on competition and market entry act as protective institutions to facilitate the ease of operation of the legal profession and gain trust, they do conversely present the profession with an ideal forum from which to act to the detriment of public interest. A traditional criticism of weakened competitive forces (in its strongest form, a tendency towards monopoly) is that pressure to innovate and effect technical progress is dulled or distorted with corresponding X-efficiency losses [8].

From a socialist perspective, the simple existence of professionalism is criticised for obstructing free mobility of labour units and for, thereby, being conducive to further accentuation of social inequality [9].

2.7 Does competition exist at all in legal services?:

Since the market for legal services enjoys attenuated competitive pressures, price competition could be expected to play a far less significant role than in many other markets. The market is, therefore, characterised by competition based more on quality criteria rather than price. It is nevertheless the case that within certain segments of the overall market for legal services (particularly those where services are relatively standardised/ homogeneous, such as domestic conveyancing) atomistic price competition may remain a prevalent market characteristic.

In the absence of full competitive forces, the government is concerned that an environment is created wherein the legal profession strive to at least maintain, but better still increase, the quality of their services without unnecessary cost increases to the consumer. The government will also wish to ensure that consumers from all geographical areas have reasonable access and proximity to legal services by avoiding solicitors concentrating their activities only in main urban conurbations. While concentration of solicitors will be far higher in densely populated areas, the government will seek to create a fairly even concentration overall which minimises areas of unfulfilled need and allows all prospective consumers to access services.

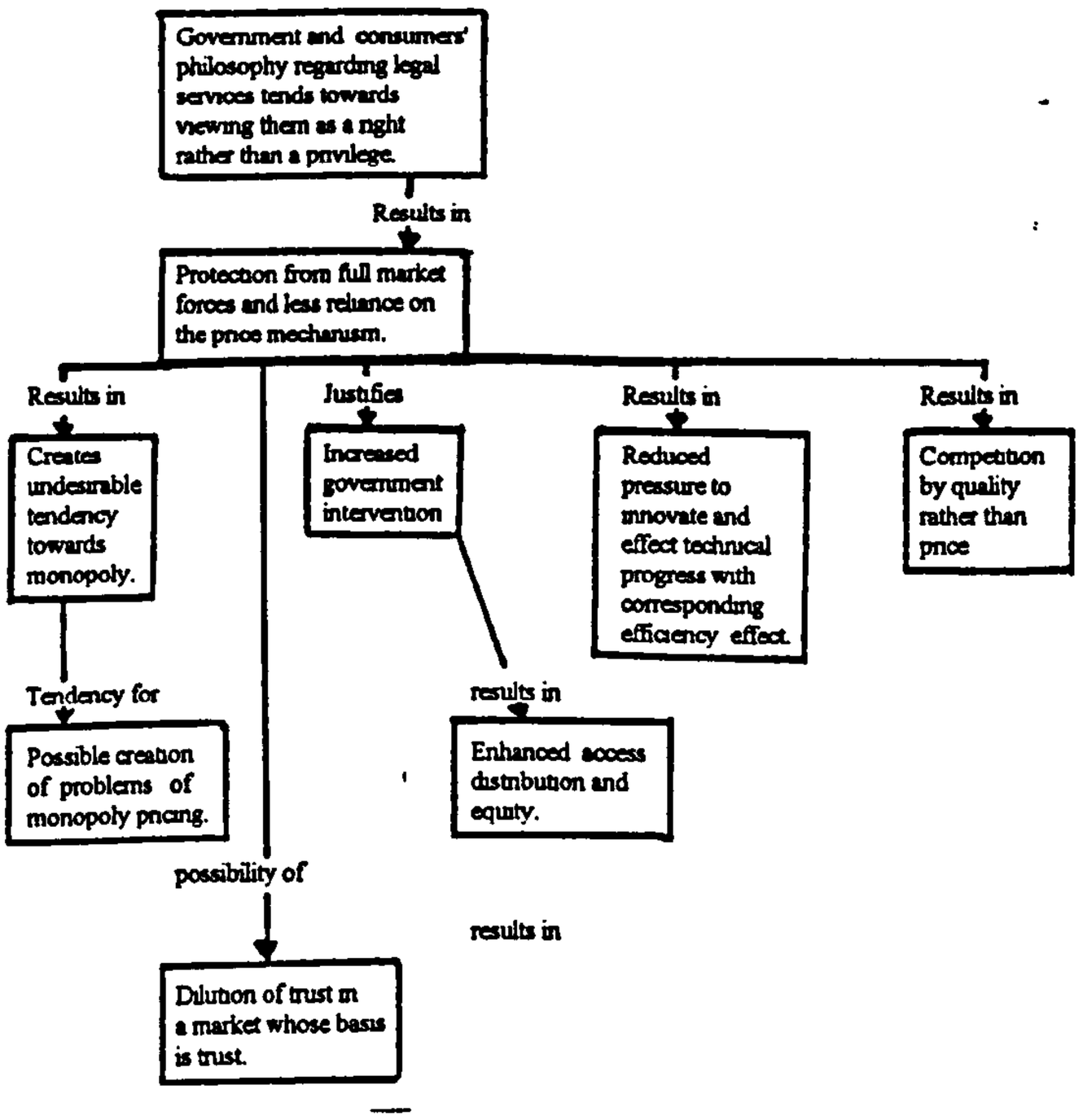
2.8 The problem of market failure:

Clearly, a legal profession operating in a completely unregulated free market would be extremely unlikely to meet the objectives of government discussed above. The legislatory and regulatory framework which has evolved can be regarded as a response to major elements of 'market failure' [10].

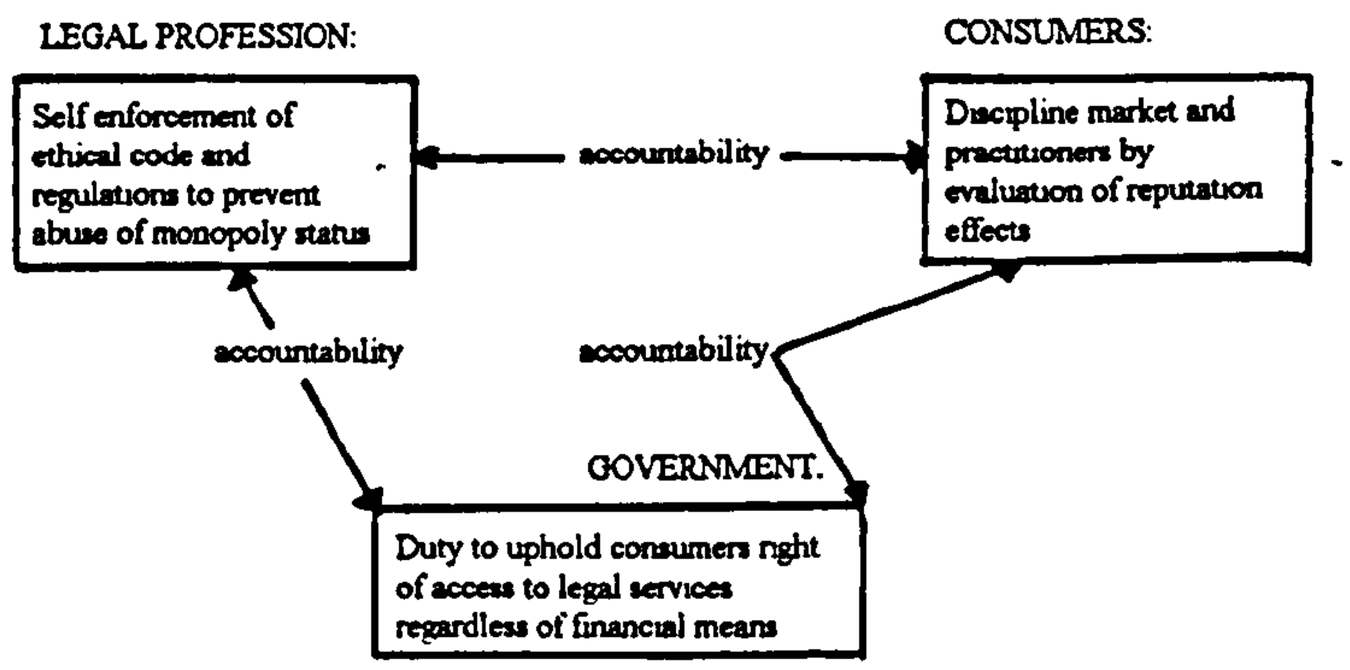
Regulation can be regarded as a set of rules or conditions that specifically seek to safeguard against problems which would likely arise under a free market situation. Current practising restrictions can therefore be viewed as an attempt to modify operation of the market mechanism with the aim that the combination of regulation and quality based competition will fulfil government objectives. Within the scenario of diluted competitive forces, while consumers clearly suffer from information deficiency, they do play a pivotal role in disciplining practitioners within the market. The consumers' disciplinary power is derived from the existence of reputation effects in the market. Through the process of non-price, primarily quality based competition, consumers evaluate respective quality and reputations, and in this manner consumers may exert as strong a disciplinary force upon the legal practitioner as does the organisation to which he belongs. The important point here is that, together, firm and market jointly constrain the behaviour of legal practitioners. In a similar vein, initial entry restrictions within professions can be regarded as positive attempts to preserve and enhance quality of both practitioners and their services within the market.

The diagram below essentially summarises the constantly interacting aspects of the provision of legal services as outlined above:

(Diagram 1)



(Diagram 2) below demonstrates the dual disciplinary mechanism that exists to constrain the practice of the legal profession:



The following table summarises plausible objectives and policies of the government as outlined and discussed above:

(TABLE 1)

OBJECTIVES	CONSEQUENCES & SOLUTIONS
To invest every individual in society with the right of access to legal services irrespective of financial means.	Close monitoring of the profession by Govt., protect right in conjunction with Legal Aid scheme. Emphasis on non-market solution.
To maintain the quality of these legal services.	Entry restrictions and reliance on reputation effects. Reliance on partnership mode with joint and several liability.
To maintain low prices to the consumer of legal services.	Govt. price subsidy via Legal Aid scheme and reliance on price competition.
To maintain fairness in distribution and equity.	Enhanced consumer access, avoidance of unhealthy market concentration and geographical imbalance.
To ensure efficient production and supply of legal services.	Atomistic competition and reliance on market/ price mechanism to produce efficiency.
To stimulate innovation and effect technical progression.	Increased competitive pressure.
To grant the legal profession sufficient freedom to operate effectively and preserve trust and confidence in the market.	Reliance on self-regulation, grant power to the Law Societies, minimum Govt. interference and involvement.
To avoid abuse of privileged monopoly status.	Increase Govt. influence/ control and promote increased competition between practitioners/ service suppliers.
To tie the legal profession to Govt. policy.	Consultation procedures between the Govt. and the profession to ensure congruence of goals.

2.9 The puzzle.....is a solution possible?:

Referring to TABLE 1. above, obvious substantial conflict exists between objectives and solutions. Consequently, it is impossible to simultaneously pursue all objectives - some well designed compromise is required. Some objectives point to the desirability of increasing competitive pressure, others point to a desire to protect from full market forces, some emphasise reliance on the full market forces/ price mechanism while others emphasise non-market, specific regulatory solutions. The exact role played by the Government in solving this puzzle is also a matter for protracted debate.

Upon recognition and realisation of the numerous and conflicting interest groups from the discussion and diagrams/ table above, it becomes apparent that the traditional Neoclassical view of the firm omits many of the interesting economic interactions which will be focused upon during this thesis. Viewing the firm as a nexus of contracts (specified and unspecified) internal and external to the firm appears more suited to a holistic analysis of the legal profession in the wider context of these issues [11]. This far more permissive view of the firm tolerates introduction of a far

wider set of economic actors, both in the interior and exterior of the firm, than is the case with conventional theory of the firm. This more holistic perspective will be explored at greater depth in later chapters, where the advantages of using such a view of the firm will become immediately apparent.

2.10 How far does the potential audience of parties to the firm extend?:

Issues such as, 'what is a firm' and, 'what are the limits to a firm' have become increasingly popular topics of discussion in theory of the firm in recent years. Perhaps the simplest answer to questions such as these is that the firm is exactly what the analyst wants it to be - there are no internal or external limits to the nexus of contracts/ treaties of the firm. Where the analyst wishes to impose a limit this can simply be made explicit by that person in analysing a particular economic problem. In adopting this view of the firm, the size, breadth and depth of the nexus of contracts of the firm is as wide or as narrow as the person conducting the analysis perceives necessary to conduct that particular analysis.

To place this in the specific context of the legal profession, the fact that the final product is a service which has evolved as a right of each individual, serves to reinforce the contractual duties binding upon this widened set of parties to the contract of the firm. The fact that consumers play an important and integral part in regulating and disciplining the profession through reputation effects, strongly indicates the requirement for them to secure a role in analysis as party to the overall nexus of contracts of the firm.

Continuing this theme, in the case of Multi-Disciplinary Practice (MDP) between lawyers and members from other professions (currently a focus in debate concerning the future of the legal profession) there would be a still wider set of parties to the nexus of contracts [12].

A current trend witnessed in legal partnerships (one which is likely to continue and perhaps become stronger in future) relates to increases in the size of productive teams. This, by introducing a larger set of agents within the firm, ushers in a whole new set of contractual problems/ difficulties. For instance, problems associated with monitoring a larger set of contractual agents of the firm will be augmented. This indicates the requirement to focus upon some of the most interesting and important problems of a contractual nature within the firm, namely a) the internal structure of the firm and b) in particular the income division bargain

between the primary agents (partners) of the firm. These issues will be examined in fine detail and at greater length elsewhere in this thesis.

Now that the background to the regulation problem has been sketched out and the role of government, consumers and self-regulation outlined, this chapter will next examine the specific legal restrictions presently incumbent upon legal practitioners in the UK. These combine to give structure to and largely determine current patterns of formal contractual relations between practitioners within legal partnerships and between firms.

Section Three: Legal restrictions on law firm organisation.

The resultant specific organisational constraints and regulations imposed on the practice of solicitors can be seen as an attempt by the Government to satisfy at least some of the objectives outlined in the previous section.

3.1 A short historical perspective:

Within the professions it has traditionally been the norm for individual practitioners either to set up practice on their own, or with colleagues from their own profession in a partnership form of organisation. This has been the historical norm for the vast majority of professions both within the UK. and abroad [13].. Practice in either of these forms signals to potential users of professional services that the practitioner is totally committed to any prospective client he should transact with, and that he backs any professional advice he provides with both the resources of the business entity to which he belongs, and his own personal assets. Hence, the more common of the two forms, the partnership, is more commonly used in professions where the code of conduct assumes that the practitioner, in holding himself out to clients as being a fit and proper professional, stands firmly behind any professional advice or service he willingly offers, without limit to his personal liability [14]. It is the rare or exceptional case in the UK., or in any member states of the EEC., for any professional regulatory body to permit practice in a corporate form or with limited liability [15]. These does, however, exist a minority of exceptions to this general rule, these notably including the following examples;

1. Some, but not all, of the States in the USA. permit corporate practice for lawyers and,

2. In the case of Chartered Surveyors in the UK., the Royal Institute of Chartered Surveyors (RICS) have recently lifted their prohibition regarding corporate practice with

limited liability and now permit such practising arrangements, subject to some qualifying restrictions.

It must be remarked at this juncture that, in recent years, the scope and nature of what is deemed to be an insurable risk paired with the comprehensive nature of cover available through ever expanding insurance markets is an important factor in considering this area. As a result, the issue that professional practitioners should assume unlimited liability for services they transact, may now form more of an arbitrary academic question than a public interest question, than was the case in earlier years. It appears not unreasonable to suggest that the best interests of clients may be better served by the provision of adequate and appropriate professional indemnity insurance. Consequently, it may be seen as more appropriate that the professional governing bodies assume a role of designing and prescribing more extensive indemnity insurance requirements for their respective members, and keep these under constant review, rather than engage in debate over what constitutes appropriate forms through which members may offer their services. This forms part of a wider discussion averted to in a later chapter.

Restrictions relating to the structure of the professions can be imposed in a variety of ways. The overall effects and consequences of their imposition, in relation to a diverse range of social and economic criteria, must be uniquely assessed with due recognition of the peculiarities of circumstance resulting from the unique environment from within which each profession operates. The issue of structural restrictions relating to the professions has been the focus of recent attention, most notably from both the Office of Fair Trading (OFT) and the Government via its White Paper proposals for major overhaul of the entire UK legal system [16].

This thesis focuses exclusively on the legal profession in the UK taking account, where necessary, of the different positions facing solicitors in England and Wales and in Scotland. What follows is an outline of the current position regarding solicitors in the UK and the restrictions on organisational form which govern their practice. This will highlight the combined effect of statutory legislation regarding the practice of solicitors, and the rules and regulations made by the Law Societies, which jointly act to limit the scope of the environment from which professional legal services may be rendered, by the legal profession, to the public.

Furthermore, this thesis is exclusively concerned with the solicitor side of the profession and will thereby exclude the other legal gender, Barristers and Advocates [17]. It is, however, interesting to note that in the process of compiling their 1986 report [18], the OFT consulted 130 professional

bodies and found that instances where only sole practice was permitted were rare, with Barristers being the only notable example.

A more indepth examination of the legal restrictions on law firm organisation is clearly required and follows below.

3.2 The source of specific organisational restrictions:

Restrictions relating to the practice of solicitors in England and Wales and in Scotland are the result of solicitors being a registered profession subject to :

1. The Solicitors Act 1974 and The Solicitors (Scotland) Act 1980 respectively and,

2. Rules made under these acts by The Law Society and The Law Society of Scotland.

Under these Acts, certain rights are conferred upon solicitors to carry out designated functions, these including conveyancing and applications for probate among others. As a prerequisite for lawful practice, the name of every solicitor must appear on a Roll of Solicitors and the solicitor must be in possession of a current practising certificate issued by the relevant Law Society. In England and Wales solicitors need not be members of the Law Society, although most actually are, but non-members are still subject to the Rules made and administered under The Acts by The Law Society [19]. In Scotland a solicitor must be a member of The Law Society of Scotland and is therefore, by virtue of his contract, automatically bound by all of the Societies rules in order to hold a practising certificate.

3.3 The primary restrictions relating to organisational form:

The primary restrictions relating to the organisational form through which solicitors may only offer their services, are as follows;

1. A prohibition on corporate practice and,

2. A prohibition on solicitors setting up partnerships with members from other professions. Limitations are also placed upon arrangements with members of other professions for the introduction of business and on other activities engaged in whilst in practice as a solicitor.

3.4 Specific challenges to these restrictions:

1. Corporate practice:

Radical alteration has occurred in respect of the first of these restrictions, namely the lifting of the prohibition relating to corporate practice for solicitors [20]. In keeping with arguments delivered by the legal profession to both The Benson and Hughes Commissions [21], solicitors will now be permitted to practice in corporate form, subject to rules ensuring the maintenance of certain criteria. These criteria encompass matters of competence, independence, insurance and compensation funds and accounting for funds held in trust for clients.

The ultimate effect of this legislation has been to make provision for the relevant Law Societies to design rules for the recognition and control of incorporated solicitors companies. Under the Acts, the Law Societies are empowered to design and administer rules that will control the practice and conduct of duly authorised corporations of solicitors.'These rules are in respect of the manner in which such firms will be permitted to carry out the functions that individual solicitors are currently authorised to undertake, by way of the Solicitors Acts.

Like other rules of the Law Societies, these rules will be subject to approval by the Master of The Rolls, in England and Wales, and by the Lord President of The Court of Session in Scotland. The rules regarding incorporation have now been set up in Scotland, and the Law Society of Scotland has produced a set of incorporated solicitors practice rules that outline requirements vis-a-vis corporate law firms in unlimited, limited and limited by guarantee forms. As yet in England and Wales, incorporation of solicitors firms is still prohibited.

The issue of the degree of and limit to liability for solicitors, consequent upon the lifting of the corporate practice restriction, has been a problematic area of debate, and indeed divided the opinions of the Benson and Hughes Commissions. The Benson Commission recommended against incorporated solicitors firms with limited liability with the Hughes Commission assuming the opposite polar stance. It is interesting to note that during debate of The Administration of Justice Bill in January 1985 The Law Society, as quoted by The Lord Chancellor, indicated the position it would take as regards the degree of liability. It was indicated at this time that The Law Society intended to prohibit corporate practice with limited liability unless it could be sure that proper and adequate consumer protection could be maintained.

It is evident that the Law Society has reconsidered the position it indicated back in January 1985 during debate but its position remains unclear with respect to England and Wales.

In Scotland, the rules that cover the incorporation of solicitors firms can be found in the Solicitors (Scotland) (Incorporated Practices) Practice Rules 1987 that came into operation as from 1st November 1987. These rules have been made under section 34(1A) of the Solicitors Scotland Act 1980, which was inserted by the Law Reform (Miscellaneous Provisions) (Scotland) Act 1985, and empowered the Council to make rules providing for the management and control of bodies corporate providing professional services, such as are provided by individuals and firms practising as solicitors. Under the Act, the membership of such bodies corporate must be restricted to solicitors holding practising certificates, their executors and other incorporated practices.

The Administration of Justice Act 1985, empowers the Council of the Law Society of England to make similar rules. During the parliamentary passage of this, Act the Lord Chancellor indicated that it was not intended that English solicitors should be permitted to practice in corporate forms with limited liability. In Scotland no similar statement was made by the Lord Advocate, although the Scottish Law Society did promise that if incorporation with limited liability was permitted, the interests of clients would not be prejudiced. The Scottish Law Society decided after long and careful deliberation that all forms of incorporation would be permitted (that is unlimited, limited by shares or limited by guarantee) for Scottish solicitors.

It is intended that the interests of clients will be preserved by the combined effect of the provisions relating to financial soundness (Rule 5(3)), contributions (Rule 5(4)) and indemnity insurance (Rule 10). Management and control provisions contained in three styles of Memoranda and Articles of Association, in tandem with these and the other rules, will ensure solicitor authority at all times in an incorporated practice.

2. Multi-Disciplinary Partnership (MDP):

The second of these practice restrictions, which essentially prohibits the formation of mixed professional practices, has also been the focus of intense debate in recent years [22]. The formation of MDPs between solicitors and members of other professions is restricted both by Statute, and by professional rules that jointly act to limit the ways in which solicitors can seek business and most significantly, prohibit fee sharing with non solicitors.

The Law Society Practice Rules, Rule 3 (practice rules 1936-1972, as amended), made under authority of The Solicitors Act s.31 and concurrent authority of the Master of The Rolls, provides that a solicitor shall not share, or agree to share, his professional fees with any person except another solicitor. This, in tandem with Rule 1, which relates to the obtaining of business, essentially precludes any lawful attempt at formation of an MDP.

In Scotland, the Law Society Practice Rules 2 and 3 (1964 rules), made by the Council currently under the authority of the Solicitors (Scotland)Act 1980 s.34, have a broadly similar effect and block the formation of MDPs. The rationale behind these restrictive prohibitions is to ensure that only properly trained and qualified legal practitioners initiate and conduct the delivery of legal services to the public [23].

The statutory restrictions are explicit as regards solicitors in Scotland and Northern Ireland by way of The Solicitors (Scotland) Act 1980 s.27 and The Solicitors Act (Northern Ireland) 1938 s.45, respectively.

The position is less well defined in England and Wales, however, as the prohibition appears only to apply to fees derived from contentious business [24]. This is the result of the combined effect of the Solicitors Act 1974 s.39 and the Partnership Act 1980 s.5. There are no statutory prohibitions on mixed partnerships in England and Wales, so far as non contentious business is concerned. The Law Society has, however, drawn attention to the Solicitors Act 1974 s.22 under which a possible offence could be committed should an MDP of solicitors and estate agents supply a conveyancing service.

The practice rules that prohibit fee sharing with non solicitors, act as an obstruction that is unparalleled in any of the other professions examined in a 1986 Office of Fair Trading report [25]. This, of course, excepts the restrictions placed upon barristers and advocates which prohibit any form of practice other than as a sole practitioner. The solicitors fee sharing prohibition inhibits members of the legal profession in a manner in which rules of other professions regulatory bodies do not.

3.5 Why are such restrictions important and are they a justifiable constraint?:

Entity restrictions, by which the members of a profession are restricted as to the form of organisation through which they can choose to deliver their services, are of important

consequence since they essentially prohibit and constrain the formation of otherwise legitimate forms of organisation.

Many of the concerns relating to abandonment of these restrictions are amongst those addressed by the Benson Commission in 1979, and by the Hughes Commission in 1980 [26]. The findings from these comprehensive reports, together with information from other sources, forms the basis of the 1986 Office of Fair Trading report [27], which has called in to question the current organisation of the legal profession and has augmented enquiry in this area to provide a more comprehensive overview of the problems with greater detail and clarity.

A recent challenge to current practice restrictions has been launched by The Secretary of State For Scotland in a Scottish Home and Health Department discussion paper entitled "The Practice of The Solicitor Profession in Scotland" [28]. This called for the introduction of MDP's, but The Law Society of Scotland was speedy in responding to this call by indicating that it was strongly against their introduction.

It is anticipated that the above will provide some indication of the source of the current practice restrictions and will concurrently highlight some of the major obstacles that stand in the way of regulatory and, therefore, structural change in the market for legal services in the UK.

3.6 The rationale behind imposing restrictions on organisational form:

Such restrictions can be viewed as an attempt to preserve the interests of the consumers of professional services. This is a recurring theme in arguments forwarded by the professional regulatory bodies in defence of their restrictions. Another central argument advanced is that which emphasises the need to ensure high standards of professional competence and integrity, and in many cases, to avoid conflicts between different interest groups. A further argument propounded to defend restrictions is that which recognises the need to preserve a practitioner's independence and freedom from external pressure.

With these propositions in mind, it is apparent that where corporate practice is permitted, the doctrine followed is one whereby the members of the profession choosing to practice in a corporate form, should remain subject to the conventional standards and disciplinary procedures of the appropriate regulatory body, as are partners in a partnership or sole practitioners. In

addition, the principle applied is to keep the company under professional control by way of a requirement for a majority of directors, or shareholders, to be professionally qualified.

In instances where mixed practices are permitted, the doctrine followed with regard to the conduct of practitioners, appears to be aimed at avoiding the use of one activity to unfairly attract business for another. This would appear to be in keeping with the general proposition often forwarded that restrictions on practitioners to compete with each other should be the minimum necessary to ensure an adequate degree of consumer protection. The strength of the concept of the personal fiduciary nature of the relationship between client and practitioner as a defence for restrictions would appear to vary, dependent upon;

1. The minimum size of practice required to serve the requirements of large corporate customers,

2. The frequency with which the client makes use of the professional service and,

3. The extent to which the practitioner is able to, and actually does, delegate work to the employees of the practice.

It is commonplace for the professional regulatory bodies either to recommend to, or to place compulsory requirements upon, members of their respective professions regarding PI insurance. It has been remarked by several of these bodies that the sharply rising cost of cover, paired with the difficulties in obtaining adequate cover through insurance markets, is a problem [29].

The National Consumer Council (NCC), the Scottish Consumer Council (SCC) and the Consumer Association (CA), bodies who share a common aim in representing the interests of consumers, are broadly in favour of relaxing restrictions. They are sceptical, it is fair to say, though in varying degrees, as to the validity and strength of the defence put forward by the professional bodies to justify their restrictions [30]. They are all in general agreement, however, over the need to arrange adequate consumer safeguards in the event of the emergence of innovative forms of mixed and corporate practice, should restrictions be liberalised. In stark to some of the professional bodies, such organisations do not envisage almost insurmountable practical difficulties in designing and devising such safeguards.

Bodies representing the interests of business consumers of professional services, on the whole accept the need to ensure safeguards, as noted above, and many did concede that there appeared

to be an ascendancy in interest in the provision of services via mixed service practices. Many of these bodies, however, thought that many business consumers (particularly smaller scale ones) may be relatively indifferent to innovative practice forms and would tend to be more concerned with the quality of the services rendered rather than the organisational mode through which they were rendered. The quality of service is a problem which deeply concerns business consumer representative bodies with many of them holding reservations that quality of service may fall without commensurate cost savings, and that choice may become limited.

A general conclusion can be arrived at here, and indeed echoes that arrived at by the Monopolies Commission as far back as 1970 [31], and that is that the removal of entity restrictions are, or at least could be, in the interests of the public provider their removal would not;

1. Endanger the personal fiduciary nature of the client practitioner relationship, where the nature of the professional's attention is essential or,

2. Lead to an over concentration of professional services in the form of local or specialised monopoly.

This Commission did, however, predict that these cases would be exceptional and of comparatively rare occurrence. The Commission also concluded that rules which prohibited mixed professional partnership were likely to be contrary to public interest, in the absence of any serious conflict of interest prejudiced against the client and in particular where there exists a recognised public demand for combined practice services, or where there is potential for cost economies and/ or increased efficiency of service and scope.

Bearing these issues in mind, it is patently obvious that any restrictions which act to impair the choice of organisational form for a profession, must be a compromise between a plethora of factors at constant variance. In the remainder of this thesis these and other themes will recur and be subjected to more rigorous analysis.

Section Four: The Socialisation of the Solicitor - Creation of a Professional Atmosphere.

4.1 Characteristics of a Profession:

A profession is a long standing institution that can be seen to engender certain characteristics that are thought to be desirable for the betterment of society as a whole [32]. In the case of legal

services, certain persons are given the legitimate authority by the Government, via the Law Societies, to carry out the functions of solicitor or barrister/ advocate [33]. The right to legal redress is recognised by the Government and through the Law Societies, practitioners are franchised with the right to carry out specific functions to service individuals' rights to legal redress [34].

The following characteristics are commonly found in professions and in particular describe the legal profession;

1. Practitioners are usually required to complete a specific University Degree typically followed by some form of "on the job" apprenticeship [35]. Competition for entrance places in these degree courses tends to be very high and consequently, entrance qualifications tend to be similarly high. This, essentially, acts as an educational filter with only the highest academic achievers gaining entry. The voluntary social conditioning process affects the individual from this point onwards where this academic school is typically a very intense and close-knit community. Peer pressure and pressure from mentors in combination tends to be strong and those who do not conform to established norms will find it difficult, if not impossible, to survive.

2. In addition to high entrance requirements, professions will limit absolute numbers of future practitioners which has the dual effect of maintaining a strong demand for their skills and preserving the exclusivity of the "professional club" [36]. The apprenticeship is a vital part of the institutionalisation of incoming practitioners as it is perceived as being essential that the skills of the mentors' generation are entrusted only to those who are perceived to be worthy of receiving such skills. The apprenticeship acts as a forum for the incoming professional to be subjected to a series of tests by the present generations of professionals. This period also encourages incoming professionals to compete by signalling their suitability and this should have the effect of generally enhancing the quality of this group of incoming professionals.

3. Those professionals in firms, or in practising arrangements with others, will not let anyone join their ranks and again there is a filtering process that enables existing members to assess the suitability of newer members of the profession to join firm or practice ranks. This has become institutionalised in the case of partnership as a pre-partnership period as a salaried member, during which the potential partner must demonstrate his/ her suitability for full partnership.

4. Professionals are often required to be members of a professional body or at least be subject to some disciplinary procedure to check against mal-practice. This is often combined with a self regulatory regime which is expected to operate efficiently as it relies on those best qualified to monitor and punish ie. similar professional practitioners [37].

5. Professions often place restrictive regulations upon their members in relation to their ability to compete with each other. This often manifests itself in terms of advertising restrictions which put paid to any attempt to signal a differentiated quality of service to consumers or attempts to poach customers from other practitioners. This exists in order that a feeling of professional omni-competence is instilled in consumers [38].

From the above, it is apparent that the profession tends to subject its incoming members to a series of rigorous filters and tests. Those who pass through these filters and tests are expected to be those who can be relied on to self-enforce incentives and self-monitor. This is, of course, bolstered by effective mutual monitoring. This could be expected to work effectively as they have a strong vested interest in preserving the value of the 'club' which they have strived to gain acceptance into. Consequently, self-enforcement/ monitoring and mutual/ peer group monitoring are expected to be all pervasive features of a profession.

In the case of the legal profession, two major screening processes can be identified;

1. Upon initial entry into the profession and,

2. Upon entry into the partnership's formal equity sharing agreement as a partner.

It is true to say that professionals tend to have a more extensive educational and training background, and are subjected to a more rigorous socialisation process than many other occupational groups. The result is the creation of a college of consistent knowledge, norms, attitudes and values. The individual is constantly thereby subject to high expectations and is expected to strive for professional autonomy, not only from competing organisations and society, but also in their work setting and organisation.

There is a potential for conflict to arise in respect of external constraint on the individual as it is likely to be the belief of the professional that only his peers are qualified to evaluate his performance. There is also potential for conflict in view of the fact that professionals are likely to argue that it is appropriate that they should be at complete liberty to exercise their personal

judgement in the absence of any organisational of client originated constraints or extra-professional restraint.

The characteristic client orientation of the professional should ensure that client needs take precedence over personal needs. This introduces the potential for further conflict, in this instance between the needs of the client, and needs of the organisation. This may promote a general resistance in the individual to organisational rules. In relation to the client, the professional enjoys systematic knowledge power over the client, and in a wider sense holds this advantage over ordinary members of society.

A profession is constructed and organised around a formal and well ordered body of knowledge [39]. The profession is invested with substantial power to make judgements and recommendations to the relatively 'ignorant' client. The legitimisation of the profession and its authority by society imparts vast power to the profession. Through manipulation of this power it can determine its educational and training requirements, set minimum standards and evaluate performance within the profession. A binding code of ethics is established which regulates behaviour between client and practitioner and also between fellow practitioners. This self enforced code reinforces development of a professional 'culture' consisting of membership and language/ symbolic norms etc.

Full time occupational involvement is expected of the professional. As a result of its training becoming highly formalised, the profession becomes affiliated with well respected and highly reputable further educational establishments. The formalisation of this training enables the duty of dissemination of the accepted required knowledge and skills to be invested only in bodies selected by the profession as being suitable to perform such a function. A professional association is established which legitimises the practice of only those individuals perceived as fit for the profession. The power of the professional is gained through membership of this association. A code of ethical practice formally states expected behavioural standards between the professional and his clients and also between fellow professionals. Professionals can be seen to possess knowledge power rather than positional power as is normally within the possession of bureaucrats.

Professionalisation is not constant over time and there is no formal consensus within the profession as to what constitutes professional behaviour in legal practice.

4.2 Attacking traditional professional conservatism.....increasing competition between professionals:

The profession has recently been subject to increasing pressure to induce greater competition [40]. In this respect the ability of the partnership form of organisation to cope with this increased competition has been questioned. This strikes at the heart of a long established traditional institution within the legal profession, the legal partnership [41].

Competition is a permanent feature of any commercial environment and the balance between commercial motives and ethical practice can be seen as constantly shifting. At present, there is a greater emphasis on commercial considerations and the role of increased competition in a freer market mechanism [42]. Some fear this may result in a dilution of ethical considerations. It has become apparent that as a result of recent increasing liberalisation in the market for legal services, lawyers have been forced to become more business like and commercially aware. It is a fear held, mainly by those who oppose further liberalisation, that lawyers may be forced still further to become more like businessmen to survive in the more competitive environment, and that this may cause the truly ethical solicitor to be drawn into more frequent situations of questionable ethical practice than was previously the case.

The legal profession could be criticised as servants of tradition, who are trapped in their conservatism and mystique and are programmed/ conditioned to maintain the status quo in which they flourish. By subscribing to this view the lawyer perceives that any element of reform or change, serves to diminish that which the lawyer has worked to acquire in terms of knowledge/ human capital. This threat tends to result in a natural inbuilt tendency for such a lawyer to resist and oppose any change in relation to legal services and practice. An unfortunate consequence of this can be that the profession can develop a very retrospective attitude which results in it being averse to moving into new and expanding fields of business with any great speed and causes it to be incapable of forward planning effectively. There is a general feeling that holding this type of attitude only serves to alienate the profession from consumers, Government and other professional groups etc. thereby leaving the profession in a weaker position than would have been the case if they had been party to negotiating practice and other related changes initially with a more accommodating and positive attitude.

From a Marxist perspective the legal profession is criticised as being characteristically insular, secretive etc. and that it deliberately attempts to create a forum from which it can exploit its self

made and self perpetuating monopoly. The profession is capable of sustaining this monopoly by the use of language alien to the man in the street and abusing its informational advantage [43].

Marxists would tend to view the lawyer as analogous to the "Putter Outer" in the early capitalist economies [44]. Here, the entrepreneur was characterised as deliberately and systematically, splitting up the production process so that the workers could only have the information to produce that part of the process that they were familiar with. They did not have the information, or the resources, to come together and start up the whole production process themselves.

As a result, the workers receive a disproportionately small return on the value added resulting from their input. In the case of legal services, they are separated from the final product by regulatory legislation that dictates that only qualified legal practitioners can conduct certain legal services.

Here, there exists an institutionalised form of legalised information monopoly over the worker due to a limited delegation authority. In this view of the law firm, the partners input can be seen as the entrepreneurial capital input, and the workers services as the labour input.

Lawyers may be more boundedly ethical than they used to be, or to be more cynical, selectively ethical, and may now pursue their own goals to a greater extent by viewing it as less questionable to exploit consumers than was previously the case. This could be the result of the profession attempting to shake off its previously retrospective nature as the old guard leave and younger members of the profession enter who are now forced, and more willing, to act in a more ruthless and commercially oriented manner.

From the perspective of this study this is of central importance as it is essential to attempt to discover whether the behavioural constraints thought necessary to constrain the behaviour of lawyers in the past and present, will be perceived to be sufficient for the future. Accepting that current constraints on individuals in the typical law firm are likely to be very liberal, it is tempting to suggest that they may not prove to be sufficient in the law firm of tomorrow when paired with the newer breed of lawyer entering the profession. It is anticipated that the empirical study may reveal that firms are having to place more formal constraints upon firm members than was previously the case.

4.3 The conflict between competition and cooperation:

Quite clearly, a profession places great emphasis on creating a reputation and installing safeguards to maintain, or even enhance, the reputation created. Attempts to instill attitudes extolling the virtues of cooperative rather than competitive behaviour and relationships between professionals, is a component of the process of socialising professionals [45].

The professions, therefore, have a tendency to be anticompetitive and their operation relies on trust and confidence. A reliance on reputation effects, results in consumers disciplining the practice of lawyers to a certain extent. This disciplinary effect could be as strong as the effect on the lawyer of belonging to a firm/ organisation. It could be argued that the organisational form is simply one part of a greater whole of.disciplinary procedures affecting the lawyer. The twin primary restrictions are fundamentally those of an anticompetitive nature, and those that are entry barriers. Consequently, professions have been characterised as 'cartels backed by licensure laws' [46].

It is argued that professions undesirably restrict the free flow of labour units and, as a result, accentuate social inequality [47]. In this respect, the public interest is at stake and that which is deemed to be in the public interest is often a central or prime consideration when proposing change within the professions. Notions of what is in the interest of the public could arguably be equated with what is deemed to be socially beneficial/ efficient [48].

4.4 Information advantage and control of quantity and quality of output by the profession:

In the context of legal services, it could be contended that informational problems are a major cause of market failure and are an obstacle to obtaining socially optimal production. A prime source of this informational problem is the difficulties that typically unsophisticated clients face in attempting to evaluate the quality of legal services [49].

It is viewed as a potential consequence of the information disadvantage that faces consumers of legal services, that lawyers may either supplier induce demand (SID) or restrict output with inflated prices [50]. Clearly these two forces oppose, but which ever may be the case, the problem is that the client potentially suffers at the mercy of the profession. It could be suggested that perhaps lawyers aim for income targets and work load/ leisure trade-offs, adjusting their activities to yield these. The profession, by restricting membership, can maintain the value of its members services as supply will be limited to available capacity, which is constantly kept in

check. In this manner, salaries and profit shares can be maintained at relatively high levels as there will at all times be at least a stable, if not strong, demand for legal services. The legal profession is consequently usually working towards the limits of its capacity and in this manner it is easier for the profession to justify the high rewards to its members. Lawyers do tend to require to work fairly long hours and again this reinforces the socialisation process, where only those that are willing to put in long hours will be accepted fully into the 'club' ie. offered equity sharing partnership.

The quality of lawyers' output can be regulated via either a market, or a non-market solution [51]. Ultimate coercive power rests in the hands of government protecting the consumer (and if necessary the producer) from the vagaries of market competition in this case. The fact that the government at the bottom line can change any aspect of the legal profession as it sees fit, within reason, may render the profession's abuse of its monopoly powers unattractive. The profession is, in essence, in contract with the State and consumers and as a result, is accountable to both. This view of three main interest groups is consistent with a nexus of contracts (both internal and external) view of the firm [52].

4.5 The effect of a recent change in Government policy towards the legal profession:

A recent example of a major shift in Government policy towards the profession is that of the change in rules regarding the provision of conveyancing services in England and Wales. It is interesting to note that, in anticipation of the cessation of solicitors monopoly of conveyancing in England on 1/5/87, average prices for conveyancing services fell in most geographical areas in England [53]. This can be rationalised in terms of the legal profession fearing that as licensed conveyancers would now be permitted to offer residential conveyancing services, they would flood the market and severely undercut solicitors firms. What has become evident is that, before the above policy change, solicitors must have typically enjoyed relatively large producer surpluses from practising conveyancing. In 1990, conveyancing fees were generally similar in nominal terms to what they were at the time of abolition of scale fees in 1984. In real terms they are substantially lower.

As it transpired, the large influx of non-lawyer competition, feared by the profession, did not materialise and only very peripheral competition was felt, primarily in the larger markets in the UK. (defined in terms of TTWAs) The fear the profession had may have been founded on the realisation that, because substantial monopoly rents were being appropriated from consumers of conveyancing services, this would result in non-lawyer competition perceiving a perfect market to

contest. The probable reason that non-lawyer competition chose not to contest the market were The likely reasons that not many actually did contest the market were twofold. Firstly, prices had fallen sharply causing the market to become less appealing as monopoly profits were being transferred back to consumers and, secondly, as lawyers increasingly felt increased competition, they turned to cost cutting exercises. Ironically, an effective cost cutting method was to make better use of low cost labour and employment of Licensed Conveyancers within law firms proved popular. Figures from the register obtained from the Council of Licensed Conveyancers demonstrate that actually very few licensed conveyancers practice as principals in their own firms [54].

4.6 Why attempt to further free the market in legal services?:

There is a general feeling that uncertainty surrounding quality, and the existence of relatively high search costs, act to impede competitive pressure in legal services. Consequently, price discrimination will tend to remain as a characteristic feature of such markets. Price discrimination thrives on weakened, or the complete absence of, intra-professional competition. These conditions apply when their are bans on advertising and formal tariffs for commissions, thus creating a situation conducive to the existence of price discrimination. In this context, the Government has lately relaxed the rules regarding advertising and also abolished scale fees, however, it is likely that price discrimination remains a feature of the market for legal services in the UK [55]. Additionally, it is the case that weakened competitive pressures can stifle innovation, where taken to its logical conclusion, this argument also posits that innovation could be better stimulated under other practising forms eg. corporate and MDP.

4.7 Are Professions desirable or even necessary.....how restrictive should regulation be?:

As far back as the time of Adam Smith, there have been challenges to the status of professions [56]. Adam Smith, in his Wealth of Nations, appeared to be a firm believer in the fact that occupational monopolies and restrictive practises were neither quality enhancing, nor indeed necessary. The current thinking of the present Government appears to echo these sentiments.

Adam Smith viewed consumers as the regulators of the market, replacing the requirement for the professions to be occupational monopolies in order to regulate and discipline the market. In subscribing to this view, Smith can be regarded as having unfailing confidence in the ability of reputation effects to discipline the market. Where Smith's advocated consumer based governance

of the market would be insufficient in preserving trust and confidence in the market, barriers to entry could be defended as performing a valid role in this respect.

The rewards to professionals can be viewed as reflecting the rank they have been given in society, which in itself is a reflection of the trust invested in them. Marxists ardently oppose this view, claiming that such barriers to entry act merely to promote social inequality and are an abuse of market power that they stimulate [57]. Opponents of this view typically argue that professions can be regarded as an important stabilising force in society, and who embody all the necessary features that combine to maintain a peaceful society [58].

4.8 Concern regarding professional ethics and quality of service:

A primary concern of the professions, and indeed of society, is whether ethical requirements are fulfilled under the prevailing structure of the professions, or indeed whether they will be under any proposed as a replacement. It can be argued that in any existing structure of a profession, it is likely that there will be a minority of practitioners whose practising techniques are less than ethical. This is an undesirable, yet unavoidable, quirk of human nature rather than a consequence of ineffective regulatory design. So long as such unscrupulous practitioners remain very much in the minority, then society has nothing to fear in this respect. It may be the case, however, that the more competitive the profession becomes, the greater is the risk that more may join the ranks of unethical practitioners, altering the traditional characteristics of the profession. Such a group, via expanded ranks, may be able to increasingly establish the practising norms for the whole profession by squeezing out more and more ethical practitioners who find profit margins dwindling and staff recruitment difficult [59].

A distribution of legal services based on a philosophy of right of access to legal services is useless should the opposite contracting party decide to fail to meet the obligation of the contract. The interest groups of suppliers, users and general society can be identified as parties to such a contract.

With protective regulation, market entry is limited and mobility and competition are constrained, resulting in a restriction of the workings of the market mechanism and a tendency for higher than normal prices. Regulation of the market can prevent would-be price cutters from increasing their market share.

Chapter One - Endnotes

1. This was in essence the process of competition and engine of economic innovation and development envisaged by Schumpeter. For a detailed explanation of this concept and it's development in a wider economic context see; Schumpeter, J.A., **Capitalism, Socialism and Democracy.** London: Unwin, 1952. and Schumpeter, J.A., **The Theory of Economic Development. An Inquiry into Profits, Capital, Credit, Interest and the Business Cycle.** New York: Oxford University Press, 1961.

2. This argument is proposed by those who believe that since the government has the duty to uphold the right of access to legal services, it would be better if they also directly fulfilled the right. This would remove one level of the agency problem and remove some of the monitoring problem. This would result in elimination of any possibility of the profession reneging on it's obligation to uphold the right of access to the individual consumer of legal services.

3. When considering the provision of combined services through inter disciplinary mixed professional practices it is necessary to establish either of the following:

1. An actual demand for combined services, or
2. Cost advantages of mediating services (even individual services) through such organisations due to economies of scope.

In the absence of either of these it would appear less rational to consider mixed practices as this would involve consideration of an option to which no apparent benefits accrue. The specific constraint on ability to practice in MDP form may, however, act as a constraint on innovative practice and development of new products in the absence of the above.

4. From a Scottish perspective, the combined effect of these forces could be such that they may seriously threaten the long term existence of a separate Scots Law entity.

5. It may be the case, however, that commercial clients may actually not be any more able than private ones to rationally chose a solicitor and may suffer from similar information deficiencies and difficulties in quality evaluation. This issue will be explored at greater length in a later section of the thesis to attempt to determine whether commercial clients are better equipped to perceive quality and evaluate price differentials in the market. There may be a greater potential for lawyers to induce demand in private transactions to a greater degree than with commercial transactions given the greater expected sophistication attending commercial clients.

6. See; Benham, L. & Benham, A., Regulating Through the Professions: A Perspective on Information Control. ***Journal of Law and Economics,*** Vol.XVIII(2), Oct. 1975.

7. ***Supra*** Note 6.

8. X-Efficiency is the term that describes the minimisation of cost which occurs under conditions of competition. Conventional wisdom states that it is a necessary corollary of profit maximisation behaviour that a firm achieves X-efficiency Under conditions of monopoly, or oligopoly for that matter, attenuated competitive pressures are protective of the firm thereby reducing the requirement to be X-Efficient. In the longer run, this will tend to be accompanied with a general upward shift in cost curves of firms in that market.

This upward shift in cost curves worsens the adverse effects of monopoly. X-Efficiency has been a major preoccupation of H. Leibenstein in recent years and his 1978 work entitled, **General X-Efficiency Theory and Economic Development**, provides a comprehensive guide to this issue.

9. These and other issues will be adverted to in a later section of this thesis. Although an indepth discussion of these issues is outwith the ambit of this thesis, such issues have been the focus of discussion by sociologists, many of whom see the professions as a sinister mechanism of social control. For a good summary and analysis of these sociological and socio-economic issues from various perspectives, see; Abel, R.A., **The Legal Profession in England and Wales: 1988.** See also; Dingwall, R. & Lewis, P., (eds) **The Sociology of the Professions.** Macmillan, 1983.

10. Market failure is simply any situation where the operation of the forces of the market mechanism fail to result in a desirable outcome in terms of pricing, output or allocation.

11. In searching for a 'Theory of the Firm' economics has in more recent times looked to other disciplines to provide theoretical inputs (eg. sociology, psychology, strategic management, organisational theory and law and others). It is upon recognising the value of this less narrowly focused approach that theory of the firm is becoming more useful as a framework for analysing organisations, particularly from a holistic perspective.

A common thread that runs through newer approaches to the firm, developed from this interdisciplinary approach, is the importance of contracts. This is true of the major contributions to theory of the firm from the literatures of property rights, agency cost and transactions cost theory and network theory. For an introduction to discussion of the collected major contributions in the area of the firm as a nexus of contracts, see; Ricketts, M., **The Economics of Business Enterprise. Wheatsheaf** Books, 1987. See also; Aoki, M., Gustafsson, B. & Williamson, O.E., **The Firm as a Nexus of Treaties.** Sage, 1990.

12. It appears to be the case that arguments against mixed professional practice are commonly concerned with potential problems of contractual specification and policing/ monitoring between this wider set of agents. Partisan interests of a more varied and complex nature than typically currently exist in the legal partnership, would be a probable effect of a mixed professional organisation. The issues surrounding MDPs will be further explored in later chapters.

13. Practice in corporate forms is unusual, though it is only forbidden by rule by a small number of professional bodies. Prohibition of corporate practice through limited liability companies is relatively common.

14. The personal assets of the practitioner are at risk should he be held liable beyond the extent of the assets of the business entity.

15. Recent relaxation of Rules governing form of practice organisation for accountants by the recognised bodies has not greatly induced corporate accounting practice, most probably due to the fact that such a corporation may not engage in company audit work. The professional accountants bodies rules against corporate practice with unlimited liability have now disappeared, so far as they are compatible with the law. Architects may now practice in limited and unlimited companies.

16. Restrictions on the kind of organisation through which members of the professions may offer their services - A report by the Director General of Fair Trading (Published August 1986).

A wider perspective was introduced in analysis of this area, via a 1985 OECD report whose findings, together with other others from a wide range of sources, were accounted for and summarised in the above OFT report.

Competition Policy and the Professions, a report by the Committee of Experts on Restrictive Business Practices, Organisation for Economic Cooperation and Development, Paris 1985 (24 85 01 1) ISBN. 92-64-12685-6.

A flavour of the recent and ongoing debate regarding the future of the legal profession and the Government's White Paper proposals for reform in legal services can be obtained from the following sources;

Review of Government Legal Services/ a Report by Sir Robert Andrew, London HMSO, 1989.

The Lord Chancellor's Department: Legal Services - A framework for the Future/ presented to parliament by the Lord High Chancellor by command of Her Royal Majesty, July 1989. London HMSO, 1989.

The Lord Chancellor's Department: The Work and Organisation of the Legal Profession, London HMSO, 1989. Cm 570.

17. The general effect of the relevant codes of practice which serve to regulate here, though differing in detail, is to effectively restrict permitted practice to that as a sole practitioner only. There are no statutory provisions here, but the codes of practice are a response to the recognition that the barrister's skills are of a very idiosyncratic and personal nature;

a) His duty to the Courts requires a complete independence and freedom from external pressure and,

b) Any potential for conflicts of interest must be minimised or avoided.

18. *Supra* Note 16.

19. These rules cover matters such as; accounts, PI insurance and compensation funds. Disciplinary procedures enforced for contravention of rules include; suspension or revocation of practising certificates, or the ultimate sanction, striking the solicitor from the Solicitors' Roll.

20. This is by way of legislation contained in the Administration of Justice Act 1985, governing England and Wales, and the Law Reform (Miscellaneous Provisions)(Scotland) Act 1985, covering Scotland.

21. The Benson Commission - The Royal Commission on Legal Services, Final Report Oct. 1979, CMND 7648.

See also; The Royal Commission on Legal Services. Legal Services and Lawyers - a Summary of the Report of the Royal Commission on Legal Services, London HMSO, 1979.

The Hughes Commission - The Royal Commission on Legal Services in Scotland, May 1980, CMND 7846.

22. The debate was largely instigated by a statement by the Solicitor General (Hansard, 17 Feb. 1984, Cols. 347 & 348) announcing the Government's plans to improve the house transfer system in England and Wales. This set in motion consultation which propagated the provisions of the Building Societies Bill.

23. The Law Society has engaged in extensive consultations with solicitors, but there has been no desire shown to lift the prohibition on fee sharing.

24. Contentious business includes matters such as crime, divorce and litigation.

25. *Supra* Note 16.

26. *Supra* Note 21.

27. *Supra* Note 16.

28. Scottish Home and Health Department: The Practice of the Solicitor Profession in Scotland: A Discussion Paper, Nov. 1987.

29. Invariably, professional bodies have rules and disciplinary procedures regarding a multitude of factors relating to their individual profession, but responses from these bodies show that the use of formal procedures to enforce restrictions on practice modes were rare. This could be attributable to the effectiveness of informal advice given by these bodies, coupled with a low propensity of practitioners to actually contravene practice restrictions.

30. The explanation provided here is that the balance of benefit to the consumer would be better served, and the example used to support this argument was in the domain of house transfer systems.

31. The Monopolies Commission: A report on the general effect on the public interest of certain restrictive practices, so far as they prevail in relation to the supply of professional services. Part 1 - The Report (Oct. 1970, CMND 4463), Part 2 - The Appendices (Oct. 1970, CMND 4463-I).

32. The concept of a Profession, and the socialisation process surrounding those who are members of a profession, has long been a preoccupation of sociologists and others from related disciplines who seek to explain socio-economic institutions and phenomena in society.

The following can be regarded as an obviously incomplete, yet hopefully representative, list of sociologically slanted writings, either in the general area of the professions, or in the more specific area of the legal profession;

Abel, R.A., **The Legal Profession in England and Wales**. 1988.

Dingwall, R. & Lewis, P. (eds), **The Sociology of the Professions**. Macmillan 1983.

Elliott, P., **The Sociology of the Professions**. Macmillan 1972.

Freidson, E., **Professional Powers - a Study of the Institutionalization of Formal Knowledge**. University of Chicago Press 1986.

" " (ed) **The Professions and their Prospects**. Sage 1973

Zander, M., **Lawyers and the Public Interest - a Study in Restrictive Practices**. Weidenfield and Nicolson 1968.

" " **Legal Services for the Community**. Temple Smith 1978.

33. The authority to carry out these functions is specifically derived from the legal profession being a registered profession. As such, the profession is invested with specific statutory power via Acts of Parliament that outline the practice of the legal profession. These powers are also affected by rules and regulations made by the respective Law Societies and the Council of the Bar/ Faculty of Advocates.

34. In Scotland, all solicitors must be members of the Law Society of Scotland in order to exercise this franchised right to practice. In England and Wales, however, solicitors need not be members of the Law Society but in any case are still subject to rules and regulations concerning private practice.

35. For a comprehensive examination of the socialisation aspects of entry into the profession see Zander, M. (1968), supra Note 32.

36. The desire of the profession to remain exclusive by restriction of membership numbers and enforcing rigorous selection in order to preserve quality may be disadvantageous in the respect that it does not guarantee safety in numbers.

37. For an excellent discussion of issues surrounding professional regulation see; Dingwall, R. & Fenn, P., A Respectable Profession? Sociological and Economic Perspectives on the Regulation of Professional Services. ***International Review of Law and Economics***, Vol 7. No.1, June 1983. See also; Shaked, A. & Sutton, J., The Self Regulating Profession. ***Review of Economic Studies***, April 1981, Vol.48(2), pp.217-234.

38. See the discussion of law firm advertising in Evans, W.G. & Trebilcock, M.J. (eds), **Lawyers and the Public Interest**, Toronto, Butterworth, 1987. Chapter 5. Trebilcock, M.J. Competitive Advertising. See also, Hudec, A.J & Trebilcock, M.J., Lawyer Advertising and the Supply of Information in the Market for Legal Services. ***University of Western Ontario Law Review***, Vol.20 No.1, 1982.

39. For a discussion on the relationship of formal, codified knowledge to power of individuals within society, and many other related issues see; Freidson, E. (1986), *supra* Note.32.

40. The profession has been subjected already to a fair degree of liberalisation in recent years via abolition of scale fees, abolition of the conveyancing monopoly (in England and Wales) and increasing liberalisation in advertising restrictions. Details concerning the proposals for increased liberalisation in the future can be obtained from the following sources;

> Review of Government Legal Services/ a report by Sir Robert Andrew, London HMSO, 1989.
> The Lord Chancellor's Department: Legal Services - A framework for the future/ presented to parliament by the Lord High Chancellor by order of Her Royal Majesty, July 1989, London HMSO, 1989. Cm 740.
>
> The Lord Chancellor's Department: The Work and Organisation of the Legal Profession, London HMSO, 1989. Cm 570.

41. An interesting parallel can be drawn from theory of the labour managed firm where it is argued that it is difficult for internally financed labour managed firms to survive in a capitalist competitive environment. See; Williamson, O.E. The Organisation of Work: A Comparative Institutional Assessment. ***Journal of Economic Behaviour and Organisation***, Vol.1, pp.5-18.

42. This change in emphasis towards increasing competition in many aspects of the practice of the legal profession is evident on inspection of the details of the current proposals. These details are to be obtained from the sources listed above, ***supra*** Note 40.

43. The analysis of the professions from a Marxist perspective is one of 3 main perspectives that Abel, R.A. identifies within his book **'The Legal Profession in England and Wales.'** (1988), ***supra*** Note 32, in which he attempts a comprehensive sociology of the professions. The three perspectives he identifies and utilises are; 1) Weberian, 2) Marxist and 3) Structural Functionalism with it's roots in Durkheim. An interesting discussion of the legal profession using an analytical framework synthesising all three of these perspectives is the preoccupation of Abel in a large part of his book.

44. See; Marglin, S., Knowledge and Power, in Stephen, F.H. (ed), **Firms, Organisation and Labour.** St. Martins Press, NY. pp 146-164.

45. The nature of the dichotomy between competition and cooperative behaviour amongst professionals in a regulatory context is examined in Freidson, E. (ed) (1973), ***supra*** Note 32. See in particular; Freidson, E., Professions and the Occupational Principle, pp.19-38; Daniels, A. Kaplan, How Free Should Professions Be?, pp.39-58, Ritzer, G., Professionalism and the Individual, pp.59-74.

46. See, Trebilcock, M.J. & Reiter, B J., Licensure in Law, in Evans, W.G. & Trebilcock, M.J., (1987), ***supra*** Note 38. See also; Rhode, D.L. & Hazard, G.C., **The Legal Profession: Responsibility and Regulation**, Foundation Press, 1985.

47. This is essentially a Marxist perspective of a potential impact of the practice of the profession. A development of this theme and themes base on alternative and complimentary perspectives is obtained above; Abel, R.A. (1988), ***supra*** Note 43.

48. For a full discussion of issues surrounding the public interest in legal services see; Evans, R.G. & Wolfson, A.D., CUI BONO - Who benefits from increased access to legal services? in Evans, R.G. & Trebilcock, M.J. (eds) (1987), *supra* Note 38. See also; Rhode, D.L. & Hazard, G.C. (1985), *supra* Note 46. See also; Slayton, P. & Trebilcock, M.J., **The Professions and Public Policy**, Toronto, Faculty of Law, University of Toronto, 1978. See also; Zander, M., (1978), *supra* Note 32..

49. Informational problems, primarily arising from deficiencies, and the resultant impact this has regarding consumers' choice and quality evaluation abilities, has received much attention in economics in relatively recent years. Notable examples are as follows; Stigler, G., The Economics of Information, ***Journal of Political Economy***, 1969, Vol.69, pp.213-225; Akerlof, G.A. The Market for Lemons - Quality, Uncertainty and the Market Mechanism, *QJE*, August 1970, pp 488-500; Demsetz, H., Information and Efficiency : Another Viewpoint, ***Journal of Law and Economics***, Vol.12, 1969, pp.1-22; Galatin, M. & Leitler, R.D., **Economics of Information**, Martinus Nijhoff, 1981; Hudec, A.J. & Trebilcock, M.J., (1982) *supra* Note 38.; Krouse, K.C., Brand Name as a Barrier to Entry: The RealLemon Case, ***Southern Economic Journal***, Vol.51(2), Oct. 1984, pp.495-502, Nelson, P., Information and Consumer Behaviour. ***Journal of Political Economy***, 1970, Vol.78, pp.311-329. Rogerson, W.P., Reputation and Product Quality. ***Bell Journal of Economics***, Autumn 1983, Vol.14(2), pp.508-516; Shapiro, C., Consumer Information, Product Quality and Seller Reputation. *QJE*, Vol.XCVIII, Nov.1983, pp.659-680.

50. Supplier induced demand has been viewed as being a potential problem in professional services, particularly in view of the fact that there is typically a wide gulf of information between the client and the firm. It has in particular, therefore, become a central feature of work done in the field of health economics. For further analysis of SID in various service type settings see; Anderson, R.K., House, D. & Ormiston, M.B., A Theory of Physician Behaviour with Supplier Induced Demand.; Evans, R.G., Supplier Induced Demand : Some Empirical Evidence and Implications. in Evans, W.G and Trebilcock, M.J. (eds) (1987) *supra* Note 38.; Perlman, M. (ed), **The Economics of Health and Medical Cases**. Macmillan, 1974; Reinhardt, V.E., The theory of Physician Induced Demand : Reflections after a Decade. ***Journal of Health Economics***, Vol.4, 1985, pp.187-193, (editorial).

51. *supra* Note 37.

52. See Chapter One-Section Three, for an explanation of the interest groups and parties to the nexus of contracts of the firm.

53. See; Paterson, A., Farmer, L., Stephen, F H. & Love, J.H., Competition and the Market for Legal Services. Journal of Law and Society, 1988, Vol 15, pp 361-373. See also; Love, J.H., Stephen, F.H., Gillanders, D.D. & Paterson, A.A., Spatial Aspects of Deregulation in the Market for Legal Services, 1991.

54. See, Love et al (1991), *supra* Note 53. at p.10.

55. See; Love, J.H., Stephen, F.H., Gillanders, D.D. & Paterson, A.A., Deregulation and Price Discrimination in the Conveyancing Market, 1991. See also; Love, J.H., Stephen, F.H., Gillanders, D.D. & Paterson, A.A., Testing for Price Discrimination in the market for Conveyancing Services, ***International Review of Law and Economics***, (forthcoming).

56. Smith, A., **The Wealth of Nations**, 1776.

57. ***supra*** Note 43.

58. This viewpoint appears not incompatible with that categorised by Abel (1988) ***supra*** Note 43. as being 'structural functionalist'. Social order was also a concern of Dingwall: Introduction (1983) in Dingwall, R. & Lewis, P. (eds), ***supra*** Note 32., who echoed this Durkheimian perspective, viewing the professions as a stabilising device in society.

59. In view of the strength of the characteristics of the profession, it is difficult to anticipate that this doomsday scenario for professionalism would become reality.

-Chapter Two -

The Economics of Legal Firms - Theoretical & Empirical Methodology and Description of Sample firms:

Introduction:

Prior to initially explaining the function of this chapter and proceeding into the chapter itself I feel the need to offer some justification for the methodology being situated at such an early point in the thesis. Accepting the fact that it is not possible to resolve the 'chicken and egg' dilemma confronting all who seek to perform empirical analysis in economics - that being uncertainty surrounding whether theory or methodology should be stated first since they both presuppose each others' existence - I have preferred here to state methodology first and later detail theory to be used. In doing so, this has also been usefully combined with an initial description of the sample firms under observation. Hence, the first two sections of Chapter Two outline the theoretical and empirical methodology underpinning the thesis. This is followed in section three by a description of the sample of firms being observed.

Section One: Methodology:

1.1 Why investigate the practice of law firms?:

It is now apparent from discussion in the preceding chapter of the practical issues surrounding the practice of law firms, that the law firm is itself an interesting and complex animal to subject to empirical investigation. Theoretical discussion in following chapters will simply reinforce the view that the law firm is a worthy subject for economic analysis.

The reasons for devoting much time to investigating the law firm are twofold. Firstly, the law firm provides an ideal organisational setting against which newer organisational theories can be discussed. Secondly, there is an increasing reliance on service providing industries (of which legal services is one), within the UK at present as the country moves ever closer to becoming a service based economy. The implication of this is that increasing numbers of organisations will be forced to deal with the particular problems associated with high levels of human capital input, information and knowledge in their organisation. This particular feature is apparent upon observing the manner in which professions are organised. Organisational culture is a central pivot of the incentive structure in place within the professional organisation [1].

1.2 Discussion of law firms within economic theory:

To date, specific studies of the law firm within economic literature have been confined to a few isolated attempts which have gone relatively unnoticed. These specific studies, and their

deficiencies, will be the focus of lengthy discussion in following chapters. Several relatively recent developments in general economic theory, particularly those associated with the New Institutional paradigm, appear to lend themselves to a more rigorous and complete exposure of the law firm as an economic organisation. These recent developments mark a distinct departure from mainstream Neoclassical micro theory and involve an interdisciplinary approach typified by the "Carnegie School".

These newer, more permissive frameworks most significantly involve introduction of behavioural postulates which introduce far more overt roles for the individual, through behavioural motivation and incentive creation within the organisation. A direct implication of this is that by emphasising the importance of contractual interaction between individuals, the existence of different organisational forms can be rationalised in terms of behavioural responses evoked by the incentive schemes embodied in the contractual structure of the organisation, and confronted by those individuals who are party to it.

The applicability of this type of analytical framework is more wide-ranging than Neoclassical theory of the firm since;

1. It actually gives the organisation a role to play and,

2. It takes greater account of the differing parties within the organisation and the fact that their objectives are seldom inter-consistent or consistent with that of the organisation to which they belong.

Greater realism is an important feature these newer theories impart on more conventional micro theory, through recognition of motivation and conflict. The implications of newer theories are more far reaching since within a traditional Neoclassical view;

1. Behavioural responses of the individual are singularly constrained to full rational utility maximisation,

2. The role of the organisation is absent where structure is taken as given and,

3. No account of incentive shaping hierarchical features is taken.

Hence, the expanded view of organisations aims to facilitate a richer and more satisfactory explanation of reasons why industries are organised as they are - something the traditional Structure-Conduct-Performance paradigm finds great difficulty in doing. From discussion of these newer theories, however, it will become apparent they too suffer from severe limitations arising

from the fact that they still tend to explicitly assume or implicitly infer maximising behaviour of the individual. This is not strictly consistent with the view of the economic actor as a boundedly rational being.

1.3 Understand the past before proposing change for the future:

To examine the implications of any proposed change to a currently existing structure it is necessary to, as fully as is possible, attempt to understand why the current structure has arisen. In the context of this study it is, therefore, necessary to understand why lawyers practice as they do currently. Once this rationale has been established, it will be possible to more correctly base any examination or forecast of the implications of any proposed change to current practising arrangements.

It is anticipated that a survey and integration of recent theoretical developments in organisational economics can provide a theoretical rationale for why solicitors practice as they do at present. It is too easy to state that the reason they practice as they do is because it is their only legal option - this misses the point completely. The theory being employed here will indicate sound reasons why it was thought necessary to restrict practising arrangements in the first instance.

It will be demonstrated theoretically that sole practitioner and partnership forms are rational responses to particular problems associated with legal practice. It will also be demonstrated that incorporation and mixed professional practice are also rational responses to particular (albeit different) institutional problems of legal practice in certain cases.

1.4 Bridging the gulf between theory and practice:

Too often in there appears a wide gulf between economic theory and practice, provoking popular criticism of unrealistic economic theory. Bridging this gap between theory and practice, however, often necessitates employing certain assumptions as to behavioural responses of the individuals in the economic system under scrutiny. Theory used within this thesis arguably employs behavioural assumptions which are more realistic than those of Neoclassical theory. To this extent at least, the 'reality gap' may be narrower than would be the case if traditional theory were being used.

Empirical testing of the newer theories' behavioural assumptions in this thesis will hopefully assist in some sense to reduce the width of this gulf by exposing similar instances of behaviour in theory and in practice. It will be interesting to see the extent to which behavioural responses of individuals in the real life law firm mimic those predicted by theory. At a simple level, observed behaviour will either corroborate or refute validity of behavioural assumptions of the theories employed.

1.5 The remaining testing problem:

In economics there remains an unfortunate and ever present burden associated with empirical testing. This problem can be characterised as not knowing whether theories are being accepted (rejected) because of factors which have been explicitly tested, or if the object under observation is operating 'as if' the theory was correct (incorrect). For example, a behavioural response predicted by theory can be examined empirically for a real life firm. If observed behaviour is consistent with predicted behaviour then arguably theory has been corroborated by empirical evidence.

However, this is problematic as some other reason may be validating that behavioural response. The observer is left with the explanation that observed behaviour is consistent with behaviour predicted by theory, ie. economic actors are behaving 'as if' theory is correct. In these circumstances the observer may easily be led to wrongly accept an incorrect but fortunately consistent explanation. In such circumstances it is advisable to seek other plausible explanations for observed behaviour to determine if they provide a more convincing explanation than that offered by the theory being tested. If this is consistently the case then it can be argued that the wrong theory is being tested. The filtering process for theory occurs when the observer chooses which theory he wishes to test - this choice being most likely based on which one is perceived to be most effective and efficient in its application to the situation under investigation.

Where observed behaviour is inconsistent with predicted behaviour it can be argued that theory has been refuted by empirical evidence. The remaining problem here that some other reason may be invalidating that behavioural response and this leaves the conclusion that observed behaviour is inconsistent with behaviour predicted by theory, ie. economic actors behave 'as if' the theory is incorrect. In this circumstance, theory may wrongly be rejected on grounds of an unfortunately inconsistent explanation (where the observation is actually correct). In these circumstances the observer will tend to search for logical explanations to rationalise why the theory appears to have been refuted. Subsequent testing of this theory should incorporate these new circumstances with a view to them becoming part of the testable theory should they become a common feature of similar empirical studies in future.

The behavioural assumptions employed in the New Institutional Economics are fairly realistic (excepting the assumption of maximising behaviour) so it could be expected that theoretical predictions not far removed from observed reality will be offered. Subjecting New Institutional theory to empirical testing is in its infancy at present, so empirical work conducted here has little to base its structure on. Given this, it may be over-optimistic to expect empirical work being conducted here to achieve much more than simply indicating whether observed behaviour is consistent or inconsistent with predicted behaviour.

1.6 Comparative Institutional Arrangements:

A New Institutional methodology also calls for a comparison between abilities of alternative institutional modes to constrain individual behaviour in such a manner so as to be compatible with the organisation's objective. This methodology appears ideally suited to an analysis seeking to compare and evaluate alternative practice modes for solicitors. Some attempt will be made to forecast the relative merits and disadvantages of each system of organisation in a systematic and informed manner.

1.7 The importance of contracts:

A strong thread which runs through many newer theoretical contributions in the area of organisations is their emphasis on;

1. Contracts,
2. Incentives,
3. Behaviour of the individual and,
4. The resultant interaction of these factors.

In the context of the law firm it is possible to integrate many of the concepts from these newer theories and expose the law firm as a nexus of contracts. These contracts (written and unwritten) largely specify the incentives within the structure of the firm which evoke resultant strategies and behavioural responses from the many parties to this nexus of contracts. The theoretical background will suggest what these incentives which confront those within the typical law firm can be expected to be and what resultant behavioural strategies/ responses could be expected from those individuals within the law firm.

1.8 Symbiosis of theory and empirical information:

The empirical research conducted will feed a comprehensive examination of the set of suggested theoretical incentives and behavioural responses for a sample of real world firms with a view to discovering whether the law firm in reality operates along lines indicated by theory. A symbiotic analysis will be established where theory and practice feed off each other and coexist.

After stating its conclusions this thesis will conclude by setting out an agenda for future research. It is my hope that the information I have unearthed concerning real world law firms through conducting the empirical study will facilitate the future development of a more comprehensive model of the law firm for researchers in this area. Additionally, it is hoped that more general issues

concerning application of newer theory of the firm will be revealed, simultaneously exposing its revealed strengths and weaknesses.

Theoretical discussion in the following chapters will suggest there to be many important relevant characteristics which cause law firms to be organised as they are. Empirical examination of the relative importance of these characteristics will be useful in explaining the current structure of law firms and will also assist in revealing what the likely effect would be of proposed changes to this structure [2].

1.9 Empirical methodology - The coverage of the empirical study:

A major difficulty confronted by this thesis is that, as such, there is no existing comprehensive model of the law firm which can be tested using the empirical information collected. The absence of such a model is perhaps fortunate, however, in the respect that most economic models tend to be fairly formal and specific in their predictions as a result of the typically restrictive assumptions they employ (for instance, that of fully rational maximisation).

In this respect the word 'test' can be challenged as inappropriately describing that which the paradigm of newer organisational theories of the firm seeks to achieve. Formal testable models can be criticised as unrealistic, but it is perhaps better to question their usefulness rather than realism in relation to explaining observed behaviour in the context of the real life firm.

The theoretical framework prefered for analysis to be conducted in this thesis has not merely been chosen at random. It has been selected due to characteristics it has evolved in the relatively short period since its initial development. The framework has evolved through a process of intuition, common sense, hypothesising, deduction, induction and also through the process of empirical corroboration and refutation. Unfortunately, the process of empirical testing in this area of research is in its infancy and very little work of this nature has preceded analysis conducted here within this thesis. The body of theory chosen to underpin the empirical study, nevertheless, is that which I have judged to be the best available at the time, given bounds to my own rationality.

Comparison of empirical reality with theoretical prediction will expose the strengths and weaknesses of the theory chosen, in terms of its power of predicting behaviour which is observed to be consistent (and inconsistent) with it.

1.10 The requirement to make value judgements to choose between theories:

Where a Popperian falsificationist approach is pursued, it is only possible to refute theories, thereby implying that it is never possible to prove their validity [3]. If observed reality coincides with

theoretical prediction, then it can only be claimed that the theory is consistent with reality, not that it has been conclusively proved. Reality may be consistent with other alternative or competing theories.

If observed reality is inconsistent with theoretical prediction then it may simply be the case that the chosen theory does not hold for the set of circumstances that have been observed [4]. That theory has been falsified by empirical observation. It subsequently falls to the researcher to attempt to explain the failure of the chosen theory, or suggest alternative theoretical explanations. This process sets the agenda for future research and to that extent, the refutation of theory must be accorded due respect as a valid and positive contribution to scientific research.

Unfortunately, within economics and many other sciences, greater emphasis is placed on positive rather than negative results, glossing over the fact that refutation of a theory is arguably just as strong a result as corroboration of a theory. This view can be rationalised since refutation is definite in its rejection of the theory in relation to the set of circumstances under observation at that time. Corroboration of the theory, however, provides the observer with no mechanism to choose between that particular theoretical explanation and other valid theoretical explanations of that set of circumstances at that time. The mechanism that operates to facilitate choice between competing valid theoretical explanations is driven by the value judgement of the researcher. In these circumstances the researcher must judge, pre-analysis, which theory/ set of theories, provides what he perceives would provide the best explanation from the set of consistent theoretical explanations [5].

In general, within empirical 'testing' in economics in general (and, therefore, within the specific area of industrial organisation) I would argue that analysis seeks to observe empirical situations and determine whether the observed patterns of behaviour are consistent with the body of theory that sets the agenda/ framework from within which the problem is examined. The process is inherently value judgement laden. A value judgement must be made firstly, as to what theoretical components will constitute the framework and secondly, which theory consequently provides the 'best' explanation where observed empirical reality coincides with theoretical prediction.

1.11 Empirical investigation procedure in economics:

I argue, therefore, that empirical research in this area should follow the procedure outlined below;

1. Initial identification of an interesting economic phenomena worthy of research.
2. Gathering of diverse theoretical inputs to provide a suitable analytical framework from within which the interesting economic phenomena can be examined.

3. Realisation of specific features suggested by the theoretical framework which should be the focus of analysis within the chosen area of research.
4. Design of an empirical study based on the theoretical framework to abstract information/ observations, relating to the theoretical focii of analysis, for the chosen sample.
5. Comparison of observed behaviour with behaviour predicted by the theoretical framework.
6. Evaluation of the theoretical framework chosen in terms of its ability to be consistent with observed facts.
7. Acceptance of the chosen theory as the best explanation of that which has been observed in those areas where empirical observation has coincided with theoretical prediction.
8. Rejection of the chosen theory as an explanation of what has been observed in those areas where empirical observation has been inconsistent with theoretical prediction.
9. Objective criticism of the chosen framework in terms of its ability and inability to cope with the foci of analysis in the chosen area of research.
10. Setting of an agenda for future research within chosen area of research embodying suggestions for areas of development for the theoretical framework used and possible theoretical avenues to explore for those areas where empirical observation refuted the chosen theoretical framework.

1.12 The measurement difficulty problem:

A major problem which is an endemic feature of empirical research in economics is that very often many of the relevant and most important 'variables' are incapable of being directly measured or observed. In terms of relationships examined from the perspective of newer organisational theory of the firm in this thesis, it is difficult to conceptualise how important factors such as opportunism, contractual atmosphere, bounded rationality and the like are to be meaningfully measured or observed.

To a greater or lesser extent, proxies or indicators can be developed and used to circumvent this problem. While these are naturally imperfect and wholly subjective, this must be contrasted with the less acceptable traditional method of coping with them in theory - assuming they do not exist. This solution circumvents any requirement to spend time designing analytical methods to cope with them. Omitting them because they are incapable of being measured, or lumping them together in some form of residual term simply to keep analysis tidy, undercuts the whole point of analysis. It is precisely these types of unquantifiable yet vitally important relationships/ variables economic theory seeks to explain. The real world is typically full of these types of immeasurable/ unquantifiable relationships. Consequently, to gloss over them is to act in a similar manner to the

often quoted drunk man who upon losing his wallet looks for it beneath the nearest lamp-post simply because it is brightest there.

These factors are in themselves general limitations of economic theory and not specifically of newer organisational theories of the firm. So long as these limitations of the theoretical framework are recognised and made explicit, analysis will be as good as it can be in the circumstances. Williamson (1985) has himself recognised limitations of the transactions cost paradigm which basically stem from it still being a fairly crude body of theory in early genesis [6].

These newer theories provide plenty indication as to the type of empirical information/ data should be collected and reasons why it should be collected, but fail to provide any guidance as to what should be specifically 'tested' and more importantly and fundamentally, what format testing should take. The framework does, however, appear to set the agenda for the collection of qualitative rather than quantitative information more in the mould of descriptive narrative. The framework, thereby, provides an ideal backdrop against which primary empirical data collected can be transformed into useful descriptive analysis of phenomena under investigation. Williamson (1985) appears to explicitly endorse a more descriptive/ case study approach, at least in the short-run, when utilising the transactions cost framework [7].

Section Two: Questionnaire Methodology:

2.1 Collection of information:

The information required for this empirical study was not available from traditional published sources and, therefore, reliance on published statistics was simply not an option. Consequently, a set of primary information required to be collected directly from firms themselves [8].

It was decided the most successful manner to gather reliable indepth information for the purposes of this study would likely be by interviewing senior partners of a sample of law firms. A postal questionnaire was deliberately avoided since these very typically suffer from poor response rates and a high incidence of unusable/ incomplete responses if returned. In any case, given the sensitive nature of some of the information being requested, it would be unlikely that this information would have been forthcoming using either this method or a telephone based interview survey.

It must be said, however, that initially on commencement of the work for this thesis, the insular reputation of the profession did little to inspire confidence, even in the preferred and selected interview method of information collection. Fortunately, levels of cooperation I received from the profession quickly disproved my initial doubts and the participation rate of firms was overall very encouraging.

2.2 Providers of sample information:

The port of entry to the sample firms was chosen to be their senior or managing partners, who it was felt would be most likely to have the broadest knowledge of the firm's operations. These persons were initially contacted in writing to seek their cooperation in an indepth interview. After this initial contact and replies to this request had been received (or a reasonable time had lapsed without response), they were contacted by telephone either to arrange an interview or to attempt to encourage them to cooperate in interview.

By far the majority of persons contacted agreed to an interview without further pressure and all participants provided most, if not all, of the information requested. Rare omissions from the information requested tended to be due to either of the two following reasons - firstly, the person did not have the knowledge/ information to answer and/ or could not access it easily, or secondly, the person was unwilling to divulge it for research purposes.

2.3 The structured questionnaire - provision of a consistent interview framework:

To preserve consistency between respondents and create structure to interviews, a questionnaire was derived from the theory examined which concentrated on those issues which appeared to be theoretically and empirically most interesting in the context of legal practice.

(i) The structure of the actual questionnaire:

The questionnaire developed comprises seven sections, each of which contained several questions on a particular area of legal practice/ law firm organisation:

Section One - The Firm
Section Two - The Client/ Firm Relation
Section Three - Inside the Firm
Section Four - Allocation of Clients
Section Five - Internal Promotion and Firm Growth
Section Six - The Sharing Bargain
Section Seven - The Future of the Profession

Each sample firm was asked all questions from all sections and responses were noted against a set of possible answers pre-formulated at the time of initially designing the questionnaire [9]. The formulated answers to each of the questions formed a set of responses which were not mutually

exclusive, thereby introducing the possibility of a firm's response to a question to be marked against one or more of the pre-formulated answers.

(ii) The coding procedure of respondents' information:

The questionnaire was pre-coded in anticipation of entering the respondents' data on the VAX mainframe. The final dataset collected was fairly substantial (33 firms X 418 maximum observations) and it was managed and analyzed using the SPSSx statistical package on mainframe. This basic dataset was mostly in binary form, ie. respondents coded 1 (Yes) against those responses they mentioned, and 0 (No) against those they did not. The missing values were; 7 (fail to ask), 8 (don't know) and 9 (won't say).

Consequently, it is possible for firms to exist for which certain of the responses should be 1, but due to the fact they favoured to mentioned other of the formulated responses, or forgot to mention that particular response, the code 0 was be entered against that particular response. Consequently, where this has occurred, aggregations across firms for a particular response within a question will tend to, if anything, underestimate the strength of truly positive responses to any given question.

Each possible response to a question possesses a variable name, so for any question there will be either one variable name (or a set of variable names) the values of which, in combination, describe that firm's response to the question.

2.4 The basic aims of this empirical study:

Empirical research conducted here faces a dual task:

1. Attempting to answer why law firms are organised as they are at present to provide a rationale for the current structure.

2. Based on answers derived above, providing evaluation of what the likely effects (if any) would be should any proposed structural change be implemented.

It is answers to precisely the above questions, and other less significant ones, which this specific study aims to provide. Various sections of the thesis reviewed each of the sections of the formal questionnaire and stated suggested 'hypotheses' the empirical study set out to test. Much of the data collected can be regarded as wholly descriptive, but that in itself should be regarded as extremely useful, given the lack of understanding that exists concerning how law firms organise their activities.

(I) Provision of a rationale for the current structure:

It is hoped that empirical research designed to facilitate abstraction of the above information will go some way towards fostering an understanding of why the current organisation of law firms has evolved as it has. Building upon these foundations, it is far easier to predict consequences of proposals aimed at altering the current organisational structure - any forecast will have a firm and rational basis.

(II) Justification of the theoretical method chosen:

It is hoped empirical results derived from the questionnaire based interviews will reinforce the merits of employing a comparative institutional methodology, through concentrating on more recent developments in organisational economic theory. Here an attempt was made to compare the behaviour observed empirically with the behavioural postulates employed in these approaches to reveal consistencies and inconsistencies.

(III) Evaluation of alternative practice options:

The study also attempts to explicitly address the pertinent issues of the proposed changes to practising arrangements. To this end, the study collects the views of various members of the legal profession in relation to the proposals. These respondents were practising in different areas of law and in different scales of, and types of, organisation - thereby exposing areas where those involved perceive advantageous possibilities and problematic consequences.

The aim is that greater light will be shed on the potential for new and novel forms of practising arrangements. The exposure of potentially problematic areas will create an ideal forum from which solutions can be suggested/ discussed and problems hopefully surmounted.

It is likely that certain types of legal work will be more amenable to certain types of practice mode - a factor which proposals fail to discuss in any detail. This study has been conducted in a manner such that the goal of transactions cost literature of assigning transactions to governance structures in a discriminating manner, is furthered. Certain types of law firm may, therefore, welcome the proposals, as they view present arrangements as far too restrictive for the area of work in which they specialise. Others may perceive no advantages in alternative practising arrangements.

(IV) Descriptive analysis and hypothesis testing:

In analysing the empirical results in following chapters, specific hypotheses suggested by the theoretical framework used will be tested so far as this is possible, and a descriptive discourse on

the practising arrangements and experience of the sample firms will be presented. The uniqueness of each firm precludes very formal testing of the expected relationships and what can be expected are generalisations across firms that either offer support to, or refute, the predictions/ expectations of the theory employed.

The following section of this chapter and latter chapters will systematically analyze the information obtained from the sample firms, in each of the areas explored by the questionnaire, and in doing so, it is anticipated that two major analyses will be simultaneously developed;

1. A purely descriptive explanation of the firms interviewed and,
2. Comparison of empirical reality against theoretically derived hypotheses to check applicability and consistency of the chosen theoretical framework.

The tables within these sections and following chapters are primarily summaries of the responses to each of the questions asked in the questionnaire. They indicate the total number of positive responses for each of the variables within each question and also additionally group firms together into cells (where possible) by shared responses across variables in each question. This should provide some indication of the popularity of particular combinations of responses to questions and also facilitate identification of patterns of responses across sample firms.

At all times, due to the diversity or characteristics of sample firms, there has been a conscious attempt to avoid forcing firms into categories merely for the sake of 'tidying' analysis. This tidying process would simply lose many of the salient features of firms and gloss over the diversity of their characteristics. It is precisely this diversity which was one of the major catalysts in provoking analysis of legal partnerships in the first instance.

Section Three: Description of the Sample Firms.

This section will describe the sample of firms interviewed using qualitative primary information derived from Section One of the Questionnaire - The Firm:

3.1 Abstraction of important differences between firms:

It is probable that the law firm in reality and in theory will be two quite distinct animals. The firm can in reality can and does assume many unique forms depending on a multitude of diverse factors. The empirical study will reveal many of these major differences and hopefully reasons for their existence. At its simplest level the empirical study must be designed to accommodate two main differences between law firms. These are firstly, absolute size and secondly, type of firm. Within these groupings, the problems each type of firm faces are very different in nature.

Quite clearly different scales of firm are presented with different problems, as are firms who deal with small private clients and those who deal mainly with corporate commercial work. The two characteristics of size and type could be expected to be related in some instances as certain corporate work may require a minimum scale of operations implying a larger organisational scale. Private client work is more amenable to being served by firms of varying scales as private client work is far less scale dependent.

The information requested in the first section of the questionnaire is primarily simple details relating to the firm such as; location of the main office, number of offices/ branches and numbers employed in different categories of the firm's labour. It is intended that this information will provide some indication of the scale of the firm in terms of its physical/ geographical spread and size of labour inputs.

Firms are requested to reveal the relative proportions of commercial work and private client work which they process and also how they would categorise the firm on a private-commercial work continuum. This information is requested with a view to being able to identify two main distinct types of firm ie. commercial firms and private firms. It is expected that hybrid/ mixed type firms will be common, but it is anticipated that most firms will attempt to lean towards one end of the client spectrum.

(I) Specialisation and fragmentation of firms' offices:

The organisation of the firms offices, where applicable, is also investigated in terms of how specialised and fragmented the firm is. The tendency to fragment the firm into smaller specialist departments and/ or offices could be expected to be more common the larger the firm is, given the problems which such a move could help overcome will be more pertinent in larger firms.

(II) The importance of the number of partners of the firm:

The most meaningful measure of law firm size is undoubtedly the number of partners, whereby the following categories will be used within the respondent firms: 1, 2, 3, 4-6, 7-9, 10-14, 15-19, 20-29, 30 or more. It is the intention within the study to investigate any relationship that may exist between firm size and firm type. In assessing the theory examined, it could be hypothesised that commercial client oriented firms will tend to be larger as they will tend to have to utilise larger pools of resources and devote teams of lawyers to this type of work. The premise that commercial practice may be more sensitive to minimum scale requirements will be tested so far as it is possible.

(III) Standardisation in legal services:

It could be expected that the larger a firm is, the greater may be its use of standard procedures etc. to facilitate exploitation of economies of scale. This will be investigated with a view to unearthing areas of legal work where economies of scale (and scope) may exist. There is an unavoidable problem here of determining the direction of causation. The firm may have become large because it introduced and now uses standard procedures etc. and can process many transactions, or it may have introduced standard procedures to cope with the number of clients it serves as a result of its large scale of operation. In any case, the use of standard procedures may be driven more by work type than by firm size.

The degree to which services are capable of, or incapable of, being standardised could be expected to be a significant determinant of whether economies of scale are available or not. This issue, though undoubtedly important, will not be directly addressed in this thesis. The issue of economies of scope may be more applicable to exposure of the potential benefits of mixed professional practice and identification of services that may be amenable to such a practice mode on that criteria.

(IV) The firm's method of growth:

Respondents are finally requested to provide an outline of how the firm has evolved in order to help explain how it has reached its present form and achieved its current scale of operations.

Overall, the information gathered in this section is largely basic and descriptive information which will provide a description of the sample firms. A number of intuitive hypotheses (detailed below) will, however, be examined and verified or rejected in light of empirical information collected.

3.2 Basic hypotheses to be tested:

Hypothesis 1: Larger firms will tend to specialise to a greater degree in commercial rather than private client business which will be the specialism of small/ medium size firms.

Hypothesis 2: Larger firms will tend to have greater degrees of specialisation and fragmentation within their offices than small/ medium firms whose specialisation will tend to be between offices.

Hypothesis 3: Larger firms can be expected to employ a higher gearing (ie. ratio of qualified assistants to partners) than small/ medium firms.

Hypothesis 4: Larger firms will be more likely to have foreign offices and affiliated offices abroad than small/ medium sized firms.

Hypothesis 5: Larger firms can be expected to have used bolt-ons and headhunting to a greater degree than small/ medium sized firms.

3.3 Description of sample firms using information from questionnaire section one:

A total of 33 firms were interviewed for the purposes of the empirical study. The study has a natural bias towards larger (>30 partner) firms since larger firms were expected to be a more interesting group. The search for large UK law firms results in the sample of firms of this scale all being drawn from London (firms of this scale outside London are very rare). Financial constraints on the research conducted also constrained the geographical dispersion of the sample.

(I) Partnership size:

In this study, the most meaningful measure of scale of the law firm was taken to be number of partners of the firm. Within the scale groups previously outlined sample firms comprised the following;

(TABLE 2.1)

Firm size	Number in sample
1 partner	0
2 partners	1
3 partners	0
4-6 partners	2
7-9 partners	1
10-14 partners	2
15-19 partners	6
20-29 partners	5
30 or more partners	16

The sample firms were assigned geographical identities in terms of the location of their main office, which was generally where the interview took place. The following describes the geographical characteristics of the sample;

(II) Location and number of offices/ branches:

The sample firms fall into the following locations;

(TABLE 2.2)

Location	Frequency	Percent	Cumulative %
Glasgow	11	33.3	33.3
Edinburgh	2	6.1	39.4
Nottingham	2	6.1	45.5
Blackpool	1	3.0	48.5
Greenock	1	3.0	51.5
London	15	45.5	97.0
USA *	1	3.0	100.0
	33	100.0	

* Interviewed in London

The number of offices/ branches of the sample firms were as follows;

(TABLE 2.3)

Number of offices/ branches	Frequency	Percent	Cumulative %
1	6	18.2	18.2
2	12	36.4	54.5
3	3	9.1	63.6
4	2	6.1	69.7
5	4	12.1	81.8
6	3	9.1	90.9
7	1	3.0	93.9
8	1	3.0	97.0
50	1	3.0	100.0
	33	100.0	

(III) Labour inputs within partnerships:

The sample is initially best viewed as comprising of two sub-samples. These are firstly, large firms of greater than 30 partners and, secondly, the remainder of the sample which are small to medium size firms. The following table shows the size of the firms, firstly, in terms of partners, secondly, in terms of numbers of Qualified Assistants (QAs) and, finally, in terms of employees that are combined with partners in each of the sample firms.

(TABLE 2.4)

Firm Number	Partners	Qual. Assts.	Employees
Firm 1	16	6	102
Firm 2	18	20	105
Firm 3	16	17	125
Firm 4	30	45	246
Firm 5	8	7	45
Firm 6	13	6	63
Firm 7	18	13	158
Firm 8	4	2	16
Firm 9	25	28	175
Firm 10	16	3	84
Firm 11	6	5	30
Firm 12	17	20	125
Firm 13	2	2	12
Firm 14	27	Missing	200
Firm 15	20	12	145
Firm 16	20	12	140
Firm 17	10	2	35
Firm 18	66	121	580
Firm 19	38	70	Missing
Firm 20	54	58	406
Firm 21	57	125	360
Firm 22	47	60	320
Firm 23	96	180	815
Firm 24	114	336	1150
Firm 25	29	21	145
Firm 26	49	80	320
Firm 27	48	50	340
Firm 28	70	95	350
Firm 29	500	Missing	Missing
Firm 30	43	105	445
Firm 31	36	82	271
Firm 32	97	300	1250
Firm 33	90	254	875
Mean (Cases)	51.52 (33)	68.94 (31)	304.29 (31)

(IV) Partnership Gearing:

In relation to testing Hypothesis 3. in this section, namely that which states that larger firms can be expected to employ a higher gearing (ie. ratio of qualified assistants to partners) than small firms, the following table is constructed. Partnership gearing is calculated by dividing the number of QAs by the number of partners for each firm.

GEARING = QA / PTR

From the table below, a simple analysis of variance (ANOVA) was conducted for the two groups of firms (large firms and small firms). Groups were created by selecting firms with greater or fewer than 30 partners and assigning a value for dummy variable BIGFIRM of 1 or 0 respectively.

Variable: GEARING by BIGFIRM - Analysis of variance.

SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	11.6248	11.6248	43.3761	0.0000
Within groups	29	7.7720	0.2680		(Sig.5%)
TOTAL	30	19.3967			

(TABLE 2.5)

Firm Number	Gearing	Firm Number	Gearing	Firm Number	Gearing
Firm 1	0.38	Firm 12	1.18	Firm 23	1.88
Firm 2	1.11	Firm 13	1.00	Firm 24	2.95
Firm 3	1.06	Firm 14	(No Data)	Firm 25	0.72
Firm 4	1.50	Firm 15	0.60	Firm 26	1.63
Firm 5	0.88	Firm 16	0.60	Firm 27	1.04
Firm 6	0.46	Firm 17	0.20	Firm 28	1.36
Firm 7	0.72	Firm 18	1.83	Firm 29	(No Data)
Firm 8	0.50	Firm 19	1.84	Firm 30	2.44
Firm 9	1.12	Firm 20	1.07	Firm 31	2.28
Firm 10	0.19	Firm 21	2.19	Firm 32	3.09
Firm 11	0.83	Firm 22	1.28	Firm 33	2.82
				Mean (Cases)	1.31 (31)

The sample of large firms (for which BIGFIRM=1), have a statistically significant higher gearing than small/ medium firms (for which BIGFIRM=0). This result implicitly rejects the null hypothesis that gearing will be similar for the two firm groups, thereby confirming that large firms have a statistically significantly higher gearing than small/ medium sized ones in this sample, as claimed by Hypothesis 3.

(V) The proportions of private and commercial business:

Hypothesis 1. in this section states that larger firms will tend to specialise to a greater degree in commercial rather than private client business. In terms of proportions of business transacted for commercial or private clients, the two groups of firms are significantly different from each other. The analysis of variance (ANOVA) below confirms this to be the case.

GROUP	PROP COMMERCIAL BUSINESS			PROP PRIVATE BUSINESS		
	Mean	Std Dev	Cases	Mean	Std Dev	Cases
BIGFIRM=0	47.9412	29.2115	17	52.0588	29.2115	17
BIGFIRM=1	93.4000	6.5444	15	6.6000	6.5444	15
ENTIRE POPULATION	69.2500	31.4796	32	30.7500	31.4796	32

Variable: PROPCOMM by BIGFIRM - Analysis of variance.

SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	16467.4588	16467.4588	34.6622	0.0000
Within groups	30	14252.5412	475.0847		(Sig.5%)
TOTAL	30	30720.0000			

The variable PROPPRIV is obviously the mirror image of PROPCOMM and is not reported since the analysis of variance would be identical to that of PROPCOMM. The above result confirms the hypothesis that larger firms will specialise to a greater degree in commercial rather than private client business.

The following table demonstrates in greater detail the degree of specialisation that occurs within the sample firms.

(VI) Description of sample firms by type of work in which firm specialises:

(TABLE 2.6)

Firm No.	FULL PRIV	FULL COMM	SPEC COMM	SPEC PRIV	TIED COMM	COMM NICH	PRIV NICH	MOST PRIV	MOST COMM
2,4,6,7,14,15,16,17, 19,28,29 (11 firms=33.3%)	Yes	Yes	No	No	No	No	No	No	No
22,23,24,26,27 (5 Firms=15.2%)	No	Yes	No	No	No	No	No	No	No
3,9,12,18 (4 Firms=12.1%)	No	Yes	No	No	No	No	No	Yes	No
1,13 (2 Firms=6.1%)	No	No	No	No	No	No	No	Yes	Yes
31,32 (2 Firms=6.1%)	No	Yes	No	No	No	Yes	No	No	No
20,33 (2 Firms=6.1%)	No	Yes	No	No	Yes	No	No	No	No
5,10 (2 Firms=6.1%)	Yes	No	No	No	No	No	No	No	Yes
21 (1 Firm=3.0%)	No	No	No	No	No	No	No	No	Yes
8 (1 Firm=3.0%)	No	No	No	No	No	No	Yes	No	No
11 (1 Firm=3.0%)	No	No	No	No	No	Yes	Yes	No	No
30 (1 Firm=3.0%)	No	Yes	No	No	Yes	Yes	No	No	No
25 (1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	Yes	No	No
TOTAL FIRMS	14	26	0	0	3	5	3	6	5
%age FIRMS	42.2	78.8	100	100	9.1	15.2	9.1	18.2	15.2

Description of variables:
FULLPRIV-Full private client service
FULLCOMM-Full commercial client service
SPECCOMM-Specialist commercial client service
SPECPRIV-Specialist private client service
TIEDCOMM-Any private client work is tied to commercial clients
COMMNICH-Commercial niche service
PRIVNICH-Private niche service
MOSTPRIV-Most types of private client work undertaken
MOSTCOMM-Most types of commercial work undertaken

The striking feature here is the diversity of responses from the firms interviewed regarding what type of firm they perceived themselves as being. No firms indicated either that they were specialist private or specialist commercial firms.

A total of 26 firms indicated that they they offered a full range of commercial services and 14 indicated that they offered a full range of private client services. Of these firms, 12 firms indicated that they offered a full service to both private and commercial firms. 5 of the firms described themselves as not offering either a full private or commercial service.

5 of the full service commercial firms attempted no private client work, and 4 indicated that they would attempt most types of private client but do not offer the full range of private client services.

2 firms said that they would attempt most forms of either commercial or private work but would not describe themselves as offering a full range of services to either of these client types.

Of the full service commercial firms, 2 indicated that they would only do private client work for commercial clients, mostly as a PR exercise. Another 2 of the full service commercial firms indicated that they also specialised in particular niche areas of commercial work.

2 full service private client firms in the sample revealed that they would also attempt most types of commercial work. The remaining firms uniquely categorised themselves. One indicated that it would attempt most, but not all, types of commercial work. Another perceived itself as practising in a niche area of private client work and on no accounts did it offer a full service. One of the remaining firms viewed itself as concentrating in niche areas of both private and commercial client work. Another of the full service firms indicated that within this full service it specialised in niche areas of commercial work and additionally any private client work was done only for its commercial clients. The final firm saw itself as offering a full service to both private and commercial clients but specialising in niche areas in each category.

(VII) Description of sample firms by organisational structure:

The following table exposes the differences between the organisational structures across firms in the study;

(TABLE 2.7)

Firm No.	ONE SPEC	NO DEPTS	VERT HORI	GENO FFIC	SPEC OFFI	FOR OFF	AFF OFF	UKG ROUP	HEAD OFF	PUP PET	LOC INT
2,4,9,12,15,16,22 (7 Firms=21.4%)	No	No	No	Yes	No	No	No	No	No	No	No
23,24,25,26,30,32 (6 Firms=18.2%)	No	No	Yes	Yes	No	Yes	Yes	No	No	No	No
18,19,31 (3 Firms=9.1%)	No	No	No	Yes	No	Yes	Yes	No	No	No	No
1,7 (2 Firms=6.1%)	No	No	No	Yes	No	No	No	No	Yes	No	No
3,8 (2 Firms=6.1%)	No	No	No	Yes	No	No	No	No	No	Yes	No
5 (1 Firm=3.0%)	No	No	No	No	Yes	No	No	No	No	No	No
12 (1 Firm=3.0%)	No	No	No	Yes	No	No	No	Yes	No	No	No
27 (1 Firm=3.0%)	No	No	No	Yes	No	Yes	No	No	No	No	No
28 (1 Firm=3.0%)	No	No	Yes	Yes	No	No	No	No	No	No	No
20 (1 Firm=3.0%)	No	No	Yes	Yes	No	Yes	No	No	No	No	No
29 (1 Firm=3.0%)	No	No	Yes	Yes	No	Yes	Yes	No	No	No	Yes
33 (1 Firm=3.0%)	No	No	Yes	Yes	No	Yes	Yes	Yes	No	Yes	No
6,13 (2 Firms=6.1%)	No	Yes	No	No	No	No	No	No	No	No	No
11,14,17 (3 Firms=9.1%)	Yes	No	No	No	No	Yes	No	No	No	No	No
21 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No	No	No	No	No
TOTAL FIRMS	4	2	11	26	1	13	11	2	2	3	1
%age FIRMS	12.2	6.1	33.3	78.8	3.0	39.4	33.3	6.1	6.1	6.1	3.0

Description of variables:
ONESPEC-One office with specialised departments
NODEPTS-One office with no specialised departments
VERTHORI-Specialised vertical departments and horizontal teams
GENOFFIC-More than one office with no specialised functions
SPECOFFI-More than one office with specialised functions
FOROFF-Offices overseas
AFFOFF-Affiliated offices overseas
UKGROUP-UK legal groupings/ joint ventures
HEADOFF-Difficult work referred to head office
PUPPET-Puppet offices to gather business/ hold meetings
LOCINT-Full local & international partnership

26 respondents were firms that had more than one office but these offices were not functionally specialised between each other. Only 1 firm had more than one office, each with its own specialised function, this being its only revealed characteristic. The remaining 6 firms were all one office

firms, 4 of whom were split into specialist departments and 2 of whom had no departmental specialisation within the firm.

(VIII) Firms with multiple general function offices - further breakdown:

Of the 26 firms with more than one general function office, 7 firms disclosed this as the only feature of their firm. 6 further disclosed that they also had foreign and affiliated offices abroad, and that their general function offices were internally split into specialist vertical departments with fluid associations of lawyers between these departments who constituted horizontal teams. 3 of 26 firms indicated that they had foreign and affiliated offices abroad. Another 2 firms indicated that they had a head office to which difficult work could be referred from general function satellite offices. 2 firms indicated the existence of puppet offices which were used to gather business or hold meetings in.

The remaining firms all fell into unique classifications. One firm also participated in UK grouping arrangements of lawyers/ joint ventures with other law firms[10]. Another indicated that it had foreign offices abroad but no foreign affiliations with other law firms abroad. One firm indicated that it also had specialist vertical departments and horizontal teams, with another revealing this combined characteristic plus the existence of foreign offices. The next firm indicated the three characteristics of the last firm plus the existence of affiliated offices abroad and also that it could be described as a full international partnership. The final firm revealed the existence of specialist vertical departments and horizontal teams[11], foreign and affiliated offices abroad, participation in UK legal groupings/ joint ventures and also puppet offices.

(IX) One office firms - further breakdown:

3 of the 6 single office firms revealed that they had specialist departments and also had foreign offices abroad. 2 firms had only one office and this office was not split functionally into specialist departments. The final one office firm was characterised by the existence of specialist vertical departments and horizontal teams.

It is apparent from the TABLE 2.7 and from the preceding one, TABLE 2.6, that the law firm is typically a very complex organisation. The diversity of methods used to specialise within and between offices, expand abroad with foreign offices and affiliated offices, and at home via UK groupings/ joint ventures, is an indication of the difficult task faced by theory in any attempt to analyze behavioural characteristics of the 'typical' law firm.

(X) Degree of specialisation and fragmentation:

Hypothesis 2. proposes that larger firms will tend to have greater degrees of specialisation and fragmentation within their offices than smaller firms whose specialisation will tend to be between offices. This hypothesis is, by initial inspection, not as easy to test as those tested previously.

A oneway analysis of variance was conducted on each of the variables ONESPEC through to LOCINT to see if there was any statistically significant difference between the responses to these variables for the two groups BIGFIRM=1 and BIGFIRM=0.

The following variables had significantly different means for the two groups;

Variable: VERTHORI by BIGFIRM - Analysis of variance.

SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	2.6422	2.6422	17.4598	0.0002
Within groups	31	4.6912	0.1513		(Sig.5%)
TOTAL	32	7.3333			

This indicates that large firms are more likely to have specialised vertical departments with horizontal teams than small/ medium firms. Of the firms sampled 10 out of 16 large firms and only 1 out of 17 small/ medium firms indicated that they were arranged in this manner. This lends support to Hypothesis 2.

Variable: GENOFFIC by BIGFIRM - Analysis of variance.

SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	0.6953	0.6953	4.4720	0.0426
Within groups	31	4.8199	0.1555		(Sig.5%)
TOTAL	32	5.5152			

The result here confirms that large firms are more likely to have more than one office with no functional specialisation between them, than small/ medium firms. 11 of the 17 small/ medium firms disclosed this characteristic whereas 15 of the 16 large firms did so. This is indicative of greater functional specialisation between offices for small/ medium firms than for large firms. This result is supportive of Hypothesis 2.

We now turn to Hypothesis 4 which predicts that larger firms will be more likely to have foreign offices and affiliated offices abroad than small/ medium sized firms. The following analyses of variance were conducted;

Variable: FOROFF by BIGFIRM - Analysis of variance.					
SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	3.9376	3.9376	30.9720	0.0000
Within groups	31	3.9412	0.1271		(Sig.5%)
TOTAL	32	7.8788			

The result above is indicative of the tendency that large firms are more likely to have foreign offices than small/ medium sized ones. 12 of the 16 large firms had foreign offices whereas only 1 of the 17 small/ medium sized firms did. This offers support to Hypothesis 4 under examination here.

Variable: AFFOFF by BIGFIRM - Analysis of variance.					
SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	2.6422	2.6422	17.4598	0.0002
Within groups	31	4.6912	0.1513		(Sig.5%)
TOTAL	32	7.3333			

In the above analysis of variance it is indicated that large firms are more likely to have affiliated offices abroad than small/ medium firms. 10 of the 16 large firms had them whereas only 1 of the 17 small/ medium sized firms did. This is again supportive of hypothesis 4

(XI) Description of sample firms by modes of partnership growth:

The following information was derived from section one of the questionnaire. It relates to the manner in which the firms in the sample have grown to date;

(TABLE 2.8)

Firm No.	ORGANIC	MERGERS	NEWFIRM	TAKEOVER	BOLTS	HEADHUNT	AGENCIES
2,4,5,6,7,11,14, 15,16,17,20,27,33 (13 Firms=39.4%)	Yes	Yes	No	No	No	No	No
3,8,9,12,13,19, 21,22,24,30,31,32 (12 Firms=36.4%)	Yes	No	No	No	No	No	No
23,28 (2 Firms=6.1%)	Yes	Yes	No	No	Yes	No	No
10 (1 Firm=3.0%)	No	Yes	No	No	No	No	No
18 (1 Firm=3.0%)	Yes	No	No	No	No	Yes	No
25 (1 Firm=3.0%)	Yes	No	No	No	Yes	No	No
1 (1 Firm=3.0%)	Yes	No	No	Yes	No	No	No
26 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	Yes	Yes
29 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	No
TOTAL FIRMS	32	17	1	2	5	3	1
%age FIRMS	97.0	51.5	3.0	6.1	15.2	9.1	3.0

Description of variables:
ORGANIC-Organic growth
MERGERS-Mergers
NEWFIRM-New firm
TAKEOVER-Takeovers
BOLTS-Bolt on teams/ firms etc
HEADHUNT-Partners and staff headhunted
AGENCIES-Agencies contacting firm to place candidates

From TABLE 2.8, it is apparent that all but one of the firms interviewed has been subject to historical growth. The one firm that bucked this trend paradoxically has experienced an ever increasing client base, but its partner numbers have steadily declined. Mergers have proved to be fairly common, occurring in 17 of the 33 firms in the sample. Bolt-ons, headhunting and takeovers in that order were the next most popular growth methods occurring in 5, 3, and 2 of the 33 firms respectively. In only one firm had agencies successfully contacted the firm and placed new partners within that firm. One of the sample firms, albeit one of the larger firms, was also set up fairly recently and was thus a relatively new firm.

With reference to Hypothesis 5, which states that larger firms can be expected to have used bolt-ons and headhunting to a greater degree than small/ medium sized firms the appropriate analyses of variance were conducted. The variables ORGANIC to AGENCIES were subjected to oneway analyses of variance for the two groups BIGFIRM=0 and BIGFIRM=1.

Only one of the variables showed a statistically significant difference between the two groups. The variable in question was HEADHUNT and the results are shown below;

HEADHUNT by BIGFIRM - Analysis of variance.

SOURCE	D.F.	SUM OF SQUARES	MEAN SQUARES	F RATIO	F PROB
Between groups	1	0.2898	0.2898	3.6853	0.0641
Within groups	31	2.4375	0.0786		(Sig.10%)
TOTAL	32	2.7273			

Headhunting occurred in 3 of the 16 large firms and none of the 17 small/ medium firms and the above result is supportive of Hypothesis 5. The analysis of variance of BOLTS demonstrated no significant difference between bolt-on activity of small/ medium and larger firms. This was the case even though it was the case that 4 of the 5 instances of bolt-on activity occurred in large firms. This result casts doubts on the validity of the claims of hypothesis 5.

In summary, evidence supports the headhunting claim of the hypothesis but rejects the bolt-ons prediction. It must be said that the numbers of positive responses out of the relatively small sample of 33 firms makes the ANOVA analysis particularly sensitive. Thus although the ANOVA results are mixed, intuitively the Hypothesis is confirmed by initial inspection of responses of the firms two groups of firms in relation to headhunting and bolt-on activity.

(XII) Standardisation in legal services - use of standard documentation and procedures:

The following table summarises firms' responses to the question of their uses of standard documents, routines and precedents in legal transactions;

(TABLE 2.9)

Firm No.	STD DOC	ALLT RANS	SOME TRAN	NET WORK	FLOWS	DEP WORK	NOT STD	SPEC WORK	INC STD	FUT STD
10 (1 Firm=3.0%)	No	No	No	No	No	No	No	No	No	Yes
13 (1 Firm=3.0%)	No	No	No	No	No	No	Yes	Yes	No	No
1,17,26 (3 Firms=9.1%)	Yes	Yes	No	No	No	No	No	No	No	No
5,6,21 (3 Firms=9.1%)	Yes	Yes	No	No	No	Yes	No	No	No	No
24,28,33 (3 Firms=9.1%)	Yes	Yes	No	Yes	Yes	Yes	No	No	No	No
23 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	No	No	No	No	No
29 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	No	No	Yes	Yes
3,4,8,9,11,12 (6 Firms=18.2%)	Yes	No	Yes	No	No	No	No	No	No	No
2,14,18,19,22,30 (6 Firms=18.2%)	Yes	No	Yes	No	No	Yes	No	No	No	No
7,16,27 (3 Firms=9.1%)	Yes	No	Yes	No	No	Yes	No	No	Yes	No
15 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No	No	Yes	No
31 (1 Firm=3.0%)	Yes	No	Yes	No	No	Yes	No	No	No	Yes
25 (1 Firm=3.0%)	Yes	No	Yes	No	No	Yes	No	No	Yes	Yes
32 (1 Firm=3.0%)	Yes	No	Yes	No	No	Yes	No	Yes	No	No
20 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	Yes	No	No	Yes	Yes
TOTAL FIRMS	31	11	20	6	5	20	1	2	7	5
%age FIRMS	93.9	33.3	60.6	18.2	15.2	60.6	3.0	6 1	21.2	15.

Description of variables:
STDDOC-Standard documentation used
ALLTRANS-Standard documentation used in all transactions
SOMETRAN-Standard documentation used in some transactions
NETWORK-Computerised document networking system used
FLOWS-Flowcharting type procedures in operation
DEPWORK-Use of standard documentation depends on type of work
NOTSTD-Cannot use standardised documentation at all
SPECWORK-Work is too specialised to use standard documentation
INCSTD-Standardisation is increasing at present
FUTSTD-Need to introduce greater standardisation in future

As was anticipated, the utilisation of standard documents and procedures is now relatively widespread if the responses of sample firms can be extrapolated to apply to the wider population of law firms. In fact, in only 2 firms was there no use of standard documentation. In one of these firms it was conceded that more effort would have to be made to do this and the firm admitted that there was a genuine need to introduce this in future. In the other firm, the work they did was alleged to be too specialised to use standard documentation effectively, thereby precluding the use of standard documentation within that firm.

Standard documentation was therefore used in 31 of the 33 firms, with 11 firms indicating that they could use it in all transactions, to a greater or lesser extent, and 20 firms indicating that standard documentation could only be a feature of some transactions.

(XIII) Firms who use standard documentation in all transactions - further breakdown:

Of the 11 firms in this category, 3 firms revealed no further information and 3 indicated that the extent to which they could utilise standard documentation in any transaction was dependent on work type. 3 firms also indicated that work type had a similar bearing on the extent to which standard documentation could be used as an input but also revealed that they additionally utilised flowcharting procedures/ systems to attempt to increase speed and efficiency of transactions by

procedural sequencing. 1 firm added to the characteristics revealed by this last firm the fact that they utilised a computerised document networking system. The final firm used a similar document networking system, again used flowcharting procedures but indicated that the extent to which they could use standard documentation was work type dependent. Additionally, this firm noted that standardisation was on the increase at present within the firm and also intimated that there was a need to increase standardisation in future.

(XIV) Firms who use standard documentation in some transactions - further breakdown:

6 of these 20 firms revealed no further information regarding their use or otherwise of standard documentation. Another 6 firms said their ability to either include (or exclude) the usage of standard documentation was dependent on work type. 3 firms also revealed this information but indicated that they were increasing their usage of standard documentation at present.

Another firm revealed only that they were increasing use of standard documentation at present. 1 firm disclosed that their ability to use (or otherwise) standard documentation was dependent on transaction type and also that there was a need to increase standardisation in future. One other firm also revealed this exact information but also noted that their use of standard documentation was increasing at present. Another firm indicated that its use or non-use of standard documentation was dependent on transaction type and often work was too specialised to permit usage of standard documentation. The final firm also noted that its ability to use or not use standard documentation was dependent on work type, indicated that it used a document networking system and that standardisation was increasing at present and finally that there was a need to introduce greater standardisation in future.

It can be concluded from this that firms generally do perceive a need to standardise those elements of amenable transactions that are capable of being standardised. The fact that firms are attempting to currently increase levels of standardisation and recognise the requirement to introduce greater levels in the future is strongly indicative of the advantages, and the necessity, of doing so. Those firms who use document networking and procedure flowcharting can be looked upon as the forward thinkers, however, such systems are costly both in time and money to set up and operationalise effectively. This may require a sufficient scale in order to justify such standardisation and benefit from its introduction. The fact that the firms in which these schemes have been have introduced are all large, lends support to this view.

Chapter Two - Endnotes

1. See; Chapter One for an indepth discussion of these strong cultural aspects and influences in the context of law firm organisation.

2. It must be noted that any structure of law firms has implications for conduct and performance. Hence, structural change would therefore tend to imply another set of conduct and performance responses, which is likely to precipitate a feedback-loop of further structural change. Whilst I do not view the application of traditional static structure-conduct-performance analysis to industrial organisation as the best way of examining dynamic problems of this type, I do concede the usefulness of attempting to understand the relationship between the three elements in the industry under observation.

3. For a good explanation of Popperian Falsificationism and other methodological viewpoints see; ?

4. This does not preclude it from explaining a similar set of circumstances in the future, in the past or from explaining other sets of circumstances.

5. To this extent the individual suffers from bounded rationality in not being equipped to perceive the entire set of theoretical explanations which are likely to provide predictions consistent with observed empirical behaviour.

6. See; Williamson, O.E., **The Economic Institutions of Capitalism**. Free Press, (1985), Chapter 15, pp385-408.

7. See; Williamson (1985), *supra* Note 6., at p.391, where he states; 'as between breadth—more observations—and depth—fewer but more relevant data—the needs of transactions cost economics, at least in the near term, are apt to be better served by the latter.'

8. There is often a concern surrounding the quality of such data, particularly by individuals who believe such information to be inferior to published sources. It is, however, true to say that it is not until the surface is scratched for many of these published sources, that it becomes apparent that the collection methods are no different and certainly no better than a well designed primary source enquiry. Published data is not always necessarily consistent through time and can have certain limitations that are often simply ignored or overlooked. Any good piece of empirical research should recognise and be conscious of the limitations of the data being collected regardless of its origin.

9. It must be admitted that due to bounds to my own rationality, it was not possible to foresee all possible eventualities and formulate a complete set of possible answers. I feel, nevertheless, I successfully provided a comprehensive enough set of possible given that in no instances did a firm provide a useful answer that lay outwith this set of anticipated answers.

10. UK groupings/ joint ventures are associations of lawyers in a network that agree to cooperate usually across a wider geographical area for joint benefit.

11. Vertical departments are departments designated by legal speciality and vertical teams are fluid teams comprising of members from these departments who work on specific client problems. The firm can assemble these component teams easily and customise their membership to solve client specific legal problems.

-Chapter Three-

Economics of organisational forms - literature of relevance in understanding organisational relationships between lawyers and clients:

Introduction:

This chapter will outline the areas of theory and literature which will be used to provide the backdrop to examining the client/ firm relationship. This relationship (contract) is the cornerstone of the manner in which the legal profession is structured and organised at the level of the individual firm (hierarchy), and at the broader level of the overall profession (market). It is recalled that Chapter One described the background to the profession, outlining its characteristic features and highlighting, in particular, the central importance of the client/ firm relationship. In examining this client/ firm relationship further the critical focus is the severe information asymmetry in favour of the law firm. It is precisely how theory attempts to deal with information asymmetry such as this which the current chapter will focus upon.

In focusing upon this information asymmetry between client and firm, it is immediately apparent that the relationship and interaction between market (client) and hierarchy (firm) requires examination. This chapter will firstly examine how traditional Neoclassical theory attempts to cope with an explanation of interaction between firm and market organisation. In view of its inability to do so satisfactorily, more recent developments in theory of organisation will subsequently be examined to assess their success in doing so. While addressing some of the deficiencies of Neoclassical theory it will become apparent that they remain far from being able to cope with explaining many aspects of economic behaviour in firms and markets.

Section One: Critique of Neoclassical Theory of Industrial Organisation.

1.1 The Explanatory power of Neoclassical Theory.

Neoclassical theory of the firm is devoid of much explanatory power due to a paradoxical amnesia on the part of its founders to actually give the firm a role to play. Neoclassical theory is in essence a theory of markets which examines the implications of different production and output decisions on the given market structure. In this context, the structure is given pre-analysis and the firm has no role beyond that of an interface between product and factor markets. Its only other role is as a hanger upon which analytical concepts such as isoquants and cost curves are placed as pedagogic devices. This body of theory has little or nothing to say about customers/ clients who are, in essence, faceless and relatively unimportant individually of even collectively. When Neoclassical theory talks of markets, they are not seen as a bodies of customers/ clients but rather as forms of industrial structure eg. monopolistic, oligopolistic, monopoly etc.

Traditional theory of the firm is also devoid of hierarchical features of organisations which are increasingly becoming the focus of newer strains of micro economic analysis. As a result, such theory is becoming increasingly recognised as ill equipped to cope with many of the features of current industrial structure. The response has been the introduction of new theoretical perspectives into the Neoclassical paradigm [1]. These newer perspectives are best viewed as complementary to, rather than as replacing, existing micro theory. They are an attempt to address the paradox that Neoclassical theory of the firm assigns the firm no role, is actually more a theory of markets, and makes no explicit link between firm and market whatsoever.

Economic theory in this respect can be observed to have turned full circle since the earlier period when economists began to doubt the usefulness of wholly descriptive studies of industrial organisation [2]. The ascending view at that time was to favour more theoretical input and abstraction and shift from indepth empiricism, typical of studies carried out by many of the economic/ industrial historians of the time. An unfortunate consequence of this shift was the attenuation of much of the explanatory power and realism of micro economic theory. Recently, it has become increasingly apparent that these self-imposed limitations have been compromising economic analyses of industrial organisation and consequently, a more permissive methodology has gained wider acceptance. This has had the effect of facilitating a more descriptive approach incorporating greater realism through interdisciplinary analysis [3].

The anticipation here is that economic theory, through emphasis on a more holistic approach, will be better equipped to deal with the increasing number of anomalies thrown up by an increasingly useless body of Neoclassical theory.

1.2 Supplementing Neoclassical Theory - the role of newer Theories of Organisation:

Traditional economic concepts such as specialisation/ division of labour, economies of scale and scope, elasticity of demand, the nature of an industry's product (service) and the Structure-Conduct-Performance paradigm are by no means redundant in contemporary economic theory of organisation. It would be sheer folly to suggest that such cornerstones of micro-economics could be rejected wholesale. Recent developments, however, have undoubtedly injected greater realism into theory of organisation/ the firm [newer theories are more theories of 'organisation' than of 'the firm' as such since they discuss hierarchical and market organisation and recognise the existence of a link between them]. This increased realism has been accomplished primarily through the introduction of elements of human behaviour and rationality, particularly in the context of decision making processes of individual economic actors. One of the most fundamental manifestations of this altered focus on the individual within economic systems has resulted in an alternative role for 'Economic Man'. More specifically, 'Economic Man's' capacity to be at all times fully rational, clearly

has a place in simple economic analysis but it is difficult to argue that he has a role to play beyond this pedagogic one when observing and attempting to explain more complex areas of economic behaviour [4].

The act of reducing analysis to that which assumes complete certainty of behaviour for any given set of circumstances can be challenged as inappropriate for a social science that seeks to explain capricious human behaviour. Progress in micro theory in this direction has been made by challenging the assumptions of Neoclassical theory in order to achieve greater realism and usefulness. This challenge has involved attempting to incorporate notions of uncertainty and other behavioural and organisational features previously alien to theory in the Neoclassical tradition and more at home within other social sciences.

The upshot of this compromise and inclusion of other worthy academic disciplines has been that the individual and institution, and firm and market, now have pivotal interacting roles to play in theoretical analysis, mirroring their importance in the real economy. This switch in emphasis has been effected with a view to reducing the wide, and often criticised, gulf between theory and practice in economics.

1.3 Exit economic man...enter contractual man:

Within these newer economic theories of industrial organisation, economic man is displaced in favour of contractual man, propelling the theme of greater realism and explanatory power. Within much of this recently developed theory relating to the organisation of firms and markets, there is a continued emphasis on the importance of contracts. This parallels a greater recognition of the importance of, and increased reliance upon, contractual relations within the real economy and business environment. The analytical framework which examines contractual relationships between interacting individuals and firms has evolved from a synthesis of the ideas contained primarily in the literatures of Property Rights, Agency Costs and Transactions Costs [5]. These arguably more relevant and useful perspectives are best viewed as performing a role complimentary to existing micro theory whereby they foster an enhanced understanding of economic behaviour, relationships and organisation.

The nature of contractual relations that bind individual economic agents together is, therefore, a primary focus and preoccupation of newer economic theories of organisation. The fundamental concept of choice in economics requires that the individual forms arrangements and even agreements (whether formal or informal) with others. The expectation of the individual is that such activities will yield gains from trade through specialisation. At the extremes such contracts can take place within the firm, in which case the focus is on the interior of the firm, or across markets, in which case the focus shifts to the exterior of the firm and the market. Many forms of exchange, however, occur in the middle ground between

market and hierarchy.

Chapter One introduced the concept of information deficiency and asymmetry - a concept which will be discussed at length in following chapters. The nature, extent and consequences of information deficiencies within economic relationships is vitally important. Information (or lack of it) as a valuable commodity plays a centre stage role not only in real economic activity but also within the newer theories of organisation. Unfortunately, economic theory has largely developed to the present day in such a manner that it finds difficulty in coping with and conceptualising information and knowledge (even where it is the case that the economic problem attempting to be theorised is information/ knowledge based). It is essentially information, or a lack of it, that is determinative of transactions costs and, therefore, how economic relationships are organised.

Regardless of how difficult it is to cope with information and knowledge in economic theory, it is, nevertheless, a crucial element that should be included within any economic analysis. To a great extent, it partially determines the potential costs and benefits of agents entering contracts with others. Information and knowledge is not costless to obtain and is a source of potential power over others, where its use and abuse performs a major role in economic activity. Information and knowledge, to a large extent essentially is economic activity. In the absence of a full set of the necessary information, which will typically be the norm in almost every situation, the individual faces potentially high search costs to discover all relevant information - an activity that is far from costless.

In the absence of formation of costless agreements, and in situations where new opportunities are revealed continuously, the firm can be regarded as a device to reduce the costs of achieving coordinated effort whilst sourcing, utilising and managing information and knowledge. The firm acts as a mechanism that specifies contracts, setting out and allocating bargains in order that individual specialisations can be made compatible and operationalized in a manner in which cooperative gains will be the result. Specialisation naturally implies that knowledge and information will be fragmented across individuals within the firm. This demonstrates the requirement for, and importance of, the existence of the firm as a means of efficiently and effectively integrating and coordinating knowledge and information whilst simultaneously economising on the bounded rationality of its members.

The role assigned to the entrepreneurial firm in conventional Neoclassical microeconomics is one of a coordinator of factors of production. The motivation for the entrepreneur is assumed to be residual or profit maximisation. The resultant analysis typically predicts changes in the parameters of the stylised model under the profit maximising assumption, but in reality, the modern corporation is fundamentally different and considerably more complex in operation.

1.4 Problems with Neoclassical analysis of the firm:

The central assumption of profit maximisation is challenged to the extent that those in control of the operational decisions of the real world firm, ie. the managers, can choose to pursue other, perhaps more self-oriented goals. Such managerial discretion is assumed away in Neoclassical economics. One of the major critics of rational maximisation based behaviour, as posited in Neoclassical theory, is Herbert Simon who, throughout his seminal works, views humans as being satisficing rather than maximising beings. He bases this premise on his belief that individuals do not possess sufficient information processing abilities or levels of rationality which would permit them to process all necessary information in order to purposefully make maximising decisions [6].

Firms within the real life economy are seldom, if ever, perceived or observed to base many of their decisions on relative assessments of marginal costs and benefits, even if these could be identified and measured. Amongst many others, Machlup (1967) and Penrose (1959) have championed a defence of the Neoclassical model, where Machlup's assertion is that different models are applicable to different phenomena [7]. Hence, Neoclassical theory can be viewed as a theory of competitive markets. It is, therefore, assigned no role in observing how firms grow and is thus an interface between factor and product markets - essentially no more than a collection of isoquants and cost curves. Penrose (1959), on the other hand, chooses to view the firm simply as an administrative unit and a collection of productive resources [8].

As many of the proponents of newer theories of the firm perceive it, Neoclassical theory of the firm is devoid of interesting and important hierarchical characteristics. It is these typically difficult to theorise characteristics that constitute the fabric of the complex modern firm and institute many of the difficulties experienced within the real life organisation. As a result, the 'black box' theory of the firm paradoxically assigns the firm no role to play and chooses to neglect to investigate the contents of the interior of the 'black box'.

Many of the pre-war economists studied in a descriptive rather than theoretical format, the complexity of the organisation of industry. Though comprehensive and useful, these studies are criticised by Coase (1972) as devoid of a theory of what determined the observed structure of industry [9]. Neoclassical theory claims to have a theory of structure but it is in fact essentially a price theory where structure is taken as 'a given' and the pricing, output and welfare implications of this structure are assessed.

1.5 The dual importance of firm and market:

In arguably his most famous and commonly cited work, Coase (1937) introduced the premise that firms existed due to attendant costs in using the market mechanism. In this respect,

Coase can be perceived to be one of the father figures in development of the contemporary theory of transactions costs economics [10]. While this perceptive view of Coase did not appear to gain wide acceptance within economic circles for many years, this may have been due to the fact that many economists overlooked the central message Coase was attempting to transmit, namely that markets and firms could be regarded as alternatives. Loasby (1976) argues that this oversight essentially occurred due to the ascendancy of the popularity of the Neoclassical paradigm at the same time [11]. Consequently, many economists viewed the paper through Neoclassical eyes as a simple maximisation problem, whereby transactions were internalised at the margin up until the marginal cost of the last transaction equalled the marginal benefit derived from its internalisation. Consequently, Coases' profound insight remained hitherto undeveloped until Oliver Williamson noted the relevance of Coase's work to a study of market failure and vertical integration he was engaged in at the time [12].

A forceful objection to the Structure-Conduct-Performance paradigm is that an ignorance of the reasons why current structure has arisen results in the application of any structure changing policy to an unknown quantity. This is precisely the deficiency that Coase eluded to in relation to historically based descriptive analyses and which Neoclassical theory purported could be explained from within its framework. Within Neoclassical theory, however, no rational base from which to predict an efficiency outcome is provided. There is also an inherent tendency for those of the Neoclassical tradition to view that which exists as optimal or that an optimal solution can be obtained in theory for every problem. This is a naturally a naively held view as single-exit determinism is not compatible with capricious human behaviour. The default, therefore, tends to be that there exists only one solution for managing many economic problems. This again is over simplistic since, for instance, there are many solutions to the problems of managing the economic problem of opportunism of economic agents within firms and in markets, depending on the specifics of the situation in question.

1.6 What is 'a firm' ?:

Coase (1937) views the firm as a 'desirable' collection of vague long term contracts, but provides no explicit reason for why he should believe them to be desirable [13]. Coase does not overtly state that he shares the view of Knight (1921) who views the firm as a means of reducing risk and uncertainty, [14] although implicitly these two views are not inconsistent if we make the realistic assumption that it is desirable to reduce risk and uncertainty and this is the purpose of such a collection of long term contracts.

Machlup's (1967) defence of Neoclassical treatment of the firm, on reflection of the Marginalist controversy, views the firm as a mere mental, analytical construct of pedagogic value and of use in evaluation of the real world firm [15].

Hence, economists have long since searched for an answer to the question of what constitutes 'a firm', and many have provided their own specific answers to the question. While, from a lay-man's viewpoint, this question may appear too simple to ask let alone answer, this fundamental question even today continues to preoccupy and grab the attention of many working in the field of organisational/ industrial economics. This continual search, thankfully, has benefitted recently from increased input from related academic disciplines which have encouraged more fruitful analysis and discussion of many of those aspects of the firm which were previously outwith the ambit of discussion in Neoclassical orthodoxy.

In relation to the specific questions to be addressed within this thesis, namely what constitutes a law firm and why has it evolved as is observed, diverse theoretical inputs will be synthesised to provide plausible answers. To be sure, there are important aspects of specialisation and likely economies of scale in certain aspects of the business of the legal profession, but its organisation owes as much, if not more, to a multitude of other factors. The empirical study conducted within this thesis aims to expose areas in which significant specialisation benefits and economies of scale can be captured by the law firm, but also aims to disclose other benefits of legal practice in groups within partnership. To observe these features, it is necessary to examine the productive process of lawyers and the firms to which they belong. In this context, it is necessary to examine the law firm and evaluate many dimensions of its behaviour in relation to the highly regulated legal services market. To facilitate this it is necessary to step outwith the Neoclassical paradigm and take a more complex and holistic view of the organisation.

The following section, therefore, represents a brief and by no means complete voyage through some recent major and important theoretical developments in the area of industrial organisation. These developments are to be viewed as a supplement to Neoclassical theory and will be utilised within this thesis to constitute the theoretical framework from which the legal profession in general and law firms in particular will be analyzed.

Section Two: More recent developments in Economic Theory of Organisation.

Introduction:

It was revealed in Chapter One that the market for legal services is highly regulated as a consequence of notable and fundamental elements of market failure. Above, it became apparent that since Neoclassical theory is essentially a price theory which concentrates on abstract analysis of perfect and imperfect markets, it would be irrational to attempt an analysis of the legal profession in general, and of law firms in particular, based on Neoclassical underpinnings. The importance of the governance role assigned to the interior of the law firm within the market for legal services, provides strong indication of the necessity of

understanding, in-depth, the interior of the law firm and its evolved organisational governance of the information asymmetry laden client/ firm relationship.

2.1 Critique of the importance of Property Rights and Incentives:

Property Rights theory, associated most closely with the work of Furubotn and Pejovich (1972), Alchian and Demsetz (1972) and Becker (1977), involves making some crucial changes to the theory of production and exchange of the Neoclassical tradition [16]. Within this theory, individual economic actors are assumed to play important positive roles thereby switching traditional focus away from the organisation and towards the individual. Utility maximisation is a core behavioural assumption applied to individuals within the bounds of the organisation, wherein more than one pattern of property rights can exist and profit maximisation is not deterministic.

The property rights approach facilitates a detailed analysis of economic behaviour and its inter-relationship with institutional arrangements, by observing the consequences of different property right assignations on the penalty/ reward system of the organisation. Property rights theory permits analysis of the system of property rights and incentives embedded within the contractual composition of organisations of differing forms.

In sharp contrast to the frictionless, zero transactions cost world of Neoclassical orthodoxy, transactions costs are now assumed to exist and perform an important function within the firm. The firm is characterised as a system of property rights within which formal and informal contracts specify the system of property rights and determine the resultant distribution of costs and benefits of engaging in individual and joint economic activity within the firm.

Furubotn and Pejovich (1972) propose two major advantages of the property rights approach over the standard Neoclassical approach [17];

1. Externalities can be explained to be a direct consequence of incompletely and imprecisely defined property rights.

2. Non-profit maximising behaviour can now be viewed as a rational choice and is furthermore argued to be a consequence of an attenuation of fully and privately held property rights.

Methodologically the property rights approach can still be regarded as embodying firmly Neoclassical roots, even accepting its explicit rejection of a strict profit maximising objective. The theory is concerned with utility maximisation, under which constraints on such behaviour

are more fully and precisely defined.

The basic thesis of the approach is that any attenuation of fully and privately held property rights results in behaviour that is inconsistent with wealth maximisation. Such non-profit maximising behaviour is an anomaly which greatly puzzles Neoclassical orthodoxy. The property rights approach attempts to inject greater realism into existing micro theory as a complementary facet by recognising motivational forces of the individual. It can, by no means, be viewed as superseding existing Neoclassical theory.

Behavioural problems act to constrain the pursuit of utility maximisation by individuals in a similar way that profit maximisation is constrained in Neoclassical theory. The link between these deviations from maximising behaviour is provided by recognition of the concept of limitations on the capacity of humans to be at all times fully rational and possess the ability to perceive and process all available information. This bounded rationality concept, of course, owes its development to Herbert Simon who ideas have become cornerstones of much of contemporary organisational theory [18].

An unfortunate and significant deficiency of the property rights approach is its apparent inability to provide an explanation for the persistence of certain observed forms of attenuations of property rights (in the absence of any legal enforcement) if they are perceived as being inefficient. Such inefficiency is a viewed as a consequence of non-maximising behaviour. Fortunately the endurance of 'apparently inefficient' systems of property rights is capable of explanation, albeit outwith the domain of property rights theory. Refuge in this direction is sought within the domain of agency cost and transactions cost theory. Nevertheless, the property rights approach significantly highlights the importance of taking account of behaviour of individuals within the firm, the importance and significance of the explicit and implicit contracts existing between them, and the importance of the system of property rights and incentives which is firmly embedded within the contractual framework of the firm. Furthermore, this accentuates the requirement for analysis of the firm to accommodate and address these types of issues and move beyond traditional Neoclassical orthodoxy.

2.2 Critique of the Development of Agency Theory from Property Rights Theory:

The Agency Cost literature, associated most closely with Fama (1980), Fama and Jensen (1983) and Jensen and Meckling (1976), builds upon the profound insights drawn from the literature of property rights [19]. Agency theory can be championed as the last bastion of Neoclassical economics to the extent that it performs a synthesis of the property rights literature with modern finance theory, wherein it appeals to the efficient capital market to constrain non-maximising behaviour.

Agency cost theory proposes to demonstrate that certain attenuations of property rights are efficient, where agency costs can be regarded as the optimal costs of the divorce of ownership from control. The behavioural implications of systems of property rights, specified in the contracts existing between the owners and controllers of the firm, are examined in the case of differing organisational forms.

Within the agency theory literature, the capital market is assumed to operate on the basis of rational expectations with unbiased estimation on the part of its constituent actors. This precludes systematic valuation errors being made in discounting or appreciating the capital market valuation of firms. The market is expected to discount/ appreciate the value of the firm in accordance with the behaviour of the persons within the firm to whom decision making authority has been delegated.

The principal within the agency relationship is assumed to have a vested interest in monitoring the behaviour of those agents with whom he contracts. This activity, while deemed to be necessary, is not without its cost in time and resources. Agency theorists argue that this monitoring activity is necessary in order to create a situation where the agents incentives are broadly aligned with those of the organisation.

The rational agent is also presumed to perceive it to be in his own interests to incur bonding costs to guarantee his performance to the principal. It is argued that this demonstrates to the principal that, even though he may stand to gain, the agent will not act in an opportunistic manner against the interests of the principal. The anticipation is that both agent and principal will yield positive benefits where the combined activities are directed towards maximisation of joint gains.

The agency cost perspective envisages the firm to comprise a nexus of formal and informal contracts which are both internal and external to the firm. In assuming this perspective, the concept of the firm becomes more encompassing than in restrictive Neoclassical theory. Alchian and Demsetz (1972) argue that firms exist due to a desire by individuals to create and utilise teams to achieve economic benefits [20]. This theme is shared by agency theory although where Alchian and Demsetz stress 'metering problems' of team production, agency theorists prefer to use the terminology of monitoring/ agency problems, although they describe essentially the same problem.

Fama and Jensen (1983) argue that all organisations have an 'agency problem' to solve and that this revolves around three main functions of the firm [21]:

1. Decision management - the initiation and implementation of decisions which affect

resource allocation.

2. Decision control - the ratification of proposals and monitoring of implemented decisions.

3. Residual risk bearing - those agents who bear the risk of variations in stochastic flows of net residual income of the firm.

Different organisational forms can be regarded as reflecting differing combinations of these functions, invested in one or more agents of the firm. Fama and Jensen (1983) further propose that, it is the incidence of residual risk bearing that is determinative of organisational form [22]. The resulting organisational form is itself viewed as the evolved response to control agency problems between the above three interacting functions.

Agency theory appeals to the functioning of the market for corporate control and the capital market to control agency problems associated with misalignment of incentives and non-maximising behaviour. It is through this markets process that the performance of managers is punished or rewarded accordingly. Poor performance of managers resulting and reflected in decreased profits leaves the firm susceptible to takeover, where the firm's share price (capital market valuation) will be discounted by the market. A takeover could potentially result in management teams being sacked or demoted, thereby personally punishing poor management. Poor managerial performance will also result in the value of such managers' services being discounted by the market, reducing their personal rewards.

In the context of the law firm, the external capital market is absent since the partnership is internally financed by those who act as combined principal/ agents. It is these individuals who themselves act in combination as an internal capital market as they have control of the major functions of the firm. This is achieved by the partnership decision and screening function whereby acceptance or non-acceptance to partnership can be used to punish or reward QAs within the firm [23].

In the case where the law firm became incorporated then it would be likely that the above situation would persist. The most likely scenario for incorporation would be where the partners became the combined director/ shareholders of the newly incorporated firm. Hence, the functions of the firm would be combined within the same set of agents as was perviously the case.

The partners of a law firm can be regarded as the 'ultimate' in shareholders. Unlike in the capitalist corporation, where a divorce of ownership from control exists, ownership and control functions are invested in the same set of agents. As such, the firm's lawyers, who have made considerable investments in personal and collective (firm) human capital assets, are in a position to more directly receive the benefits of such investments. The traditional monitoring

problem between owners and controllers is superseded by one of a quite different type. In the case of partnership, the monitoring/ agency problem is a combination of self monitoring and mutual monitoring.

Hence, in applying the concepts of agency theory to the partnership form of organisation, analysis must acknowledge the combined effect of the external capital market and the market for corporate control being absent. Fama and Jensen would argue that, because the external capital market is absent, and the primary agents of the firm are decision managers and controllers, they will necessarily also assume the role of residual claimants. The lack of the aforementioned 'market based' disciplinary mechanisms, introducing great scope for the existence of severe agency problems, can be viewed as the crux of the problem the partnership is forced to solve in designing the framework which structures its internal relationships.

The conferral of residual claimant status (strengthening property rights) on authority bearing agents can have the paradoxical dual and opposing effect of;

1. Altering (reducing) the shirking inclination of these agents and,
2. Enhancing potential rewards to these agents from indulging in deviant behaviour.

Hence, conferring residual claimant status on agents could be expected to have the following combined effect. It could be expected that this would reduce their propensity to shirk, due to lessened attenuation of their property rights, but conversely enhance the value of shirking since such behaviour will now have a stronger and more direct benefit to the shirker.

In the context of the law firm, the partners are the sole residual risk bearers of the organisation [24]. This implies that they bear the personal risk of the difference between stochastic flows of income and the expenditure of the firm. Fama and Jensen (1983) argue that it is the incidence of this residual risk bearing function that is instrumental in determining organisational form [25].

2.3 Critique of the Framework of Transactions Cost Theory:

The transactions cost framework has firm foundations in the earlier work of Coase [26], Commons [27] and Simon [28]. In transactions cost economics, the unit of analysis is the transaction rather than the firm or the individual, even though its founder and main advocate Oliver Williamson curiously neglects to define exactly what he views as constituting 'a transaction' in his analysis. His writing draws heavily on post-war market failure literature, associated primarily with Kenneth Arrow, and exploits an permissive inter-disciplinary methodology associated with The Carnegie-Mellon School [29].

Williamson draws heavily on Simon's concept of 'Bounded Rationality' which forms an important cornerstone of much of his transactions cost analysis. This concept describes the situation whereby, in relation to the vast amount of information that exists, the capacity of the individual to perceive, process and comprehend this information is severely limited [30].

As has been described above, Neoclassical theory tends to focus almost exclusively on the market, and in doing so assumes away most important aspects of the role of the firm. The majority of problems/ difficulties typically faced by the firm are encountered in the period prior to trading with each other across markets. Consequently, Neoclassical theory is ill equipped to cope with many pre-market problems. Such theory is compromised in its ability to rationalise reliance on non-market solutions in situations that are anything other than an ad-hoc addition to the Neoclassical paradigm.

Transactions Cost Economics, like Agency Cost Theory, is also perhaps best viewed as complementary to, rather than as a replacement for, the existing neoclassical approach. In economics there is a requirement to consider how the firm dynamically changes over time, and to avoid simple static analysis. In terms of transactions, it may be the case that transactions previously governed by a certain mode require governing by some other mode in the future.

(I) Assessing Comparative Contractual Efficiency:

Williamson (1985) argues that the efficiency of different forms of governance can be compared within the comparative capability of his transactions cost framework [31]. Within the transactions cost framework, comparison of the advantages of one form of governance structure over another are based solely on aggregate transactions cost differentials. A major drawback of this is that such comparisons tend to implicitly ignore the distributional effects on agents under different governance arrangements. This distributional effect is largely ignored by Williamson throughout his work and can be regarded as a major failing of his otherwise comprehensive framework. In addition, because the cost comparisons will tend to be in relation to costs that are difficult to quantify, transactions cost comparisons will tend to be qualitative rather than quantitative. This is slightly at odds with the manner in which Williamson stresses the quasi-mathematical nature of the objective of his analysis, namely the constrained minimisation of transactions costs.

In accordance with agency theory, the importance of contracts is stressed and Williamson introduces "contractual man" as a replacement for his economic cousin. In Neoclassical analysis the paradigm transaction is 'sharp in-sharp out' by performance, ie. non-complex and instantly completed. In reality very few contracts are subject to complete certainty with fully

presentiated future contingencies. Williamson, therefore, concentrates on multi-dimensional aspects of contracting transactions and introduces a synthesis of the contractual analysis of Macneil (1981) [32], and the behavioural assumptions of Simon [33], in order to construct the transaction cost framework.

(II) Characteristics of Human Rationality:

Within this framework, he argues that the resultant combinations of characteristics of transactions and behaviour require particular discriminatory mediation. A point that Williamson unfortunately neglects to stress is that rationality varies over time for the same individual (inter-temporal variation), and also between individuals at any one point in time (inter-personal variation) as does the degree of opportunism. This is perhaps inadvertently subsumed within his concept of 'contractual atmosphere' but Williamson does not expand this concept sufficiently to make it a more useful part of his analysis. In essence, the bounds of an individual's rationality are constantly changing as a reaction to internal and external stimuli and can be regarded as constantly changing with respect to that of others. Williamson's work fails to expand sufficiently on the variability of bounded rationality and its consequence for decision making and the nature of organisational theory. A more explicit discussion of contractual atmosphere by Williamson would have given his framework greater depth and perhaps addressed some of these deficiencies.

Network theorists and Neo-institutionalists are critical of Williamson's work for not being as interdisciplinary as he claims it to be and for being firmly Neoclassical in its acceptance of the assumption that the most efficient form of institutional arrangement will survive [34]. For example, Simon's notion of bounded rationality is applied across the board and treated as given without an indepth discussion of many of its specific implications for the individual and organisation.

(III) Other Transactions Cost Assumptions:

Much of Williamson's work focuses firmly on the economics of idiosyncrasies, asset specificity or small numbers, as it is these situations that facilitate opportunistic behaviour with the greatest ease. Individuals are also assumed to have a behavioural characteristic of opportunism whereby they act at all times with 'self-interest and guile'. This major assumption is one which does not rest well with sociologists, and casual empiricism often suggests that social/ cultural exchange can occur where significant elements of mutual trust and reciprocity characterise economic relationships. Williamson tends to subsume these 'unwieldy to formalise' elements of exchange behaviour within his notion of 'Contractual Atmosphere'. Unfortunately, as indicated previously this is a seldom discussed, yet vitally important, part of his analysis in view of the fact that it sets the environment from within

which certain types of contractual/ exchange behaviour may be constrained or encouraged.

It is a valid criticism of Williamson's work, and perhaps a conscious omission on his part, that he fails to discuss the social efficiency effects of his analysis. This is perhaps due to the fact that he views efficient contractual relations as connoting some form of productive efficiency. He does not develop how he envisages contractual efficiency translating to social efficiency. It is also curious how, if it is accepted that individuals are boundedly rational, such individuals could identify, quantify and make a relative assessment of the transactions costs surrounding various modes of governing contractual relations.

Williamson argues that his 'organisational failures framework' can be applied to many sets of circumstances, so long as the problems are of a contractual nature. He views this approach as yielding the primary advantage of removing the need to attach ad-hoc assumptions to existing Neoclassical theory. In using the analytical framework of Neoclassical economics it is often the case that such assumptions are necessary in order that theory can explain that which it could not in its pre-altered state.

Williamson, throughout his analysis, constantly refers to transactions cost minimisation. As a consequence, his theory thereby remains firmly entrenched in methodology of a Neoclassical tradition. Goldberg, on the other hand, conducts a similar analysis to that of Williamson but prefers to emphasise 'contractual difficulties' rather than seek to solve an optimisation problem [35].

Williamson's insistence to transactions cost minimise implicitly affirms the widely held Neoclassical belief that there must be an optimal and determinate solution to every problem and that single-exit determinism is theoretically applicable. One major inconsistency within Williamson's framework is the fact that one the one hand he utilises the concept of bounded rationality, which implies satisficing rather than maximising behaviour, and yet on the other hand he talks of transactions cost minimisation. Minimisation and maximisation are only possible behavioural characteristics where it is possible for individuals to be fully (not boundedly) rational and perceive and process all available information correctly.

(IV) The self-proclaimed advantages of Williamson's Transactions Cost Framework:

While being far from perfect, this New Institutional approach does, nevertheless, recognise and remedy some of the important omissions of standard Neoclassical microeconomics. Williamson (1985) argues that its advantages are as follows [36]:

1. More micro analytic.
2. More self conscious of its behavioural assumptions.

3. Introduces and develops the economic significance of asset specificity.
4. Regards the firm as a governance structure rather than a production function.
5. Relies on a more comparative institutional analysis.

Transactions costs can be seen as the economic counterpart to friction in the physical sciences. In conventional economics, transactions costs are assumed away rather like friction is in simplistic scientific analysis. While scientists soon recognised the need to incorporate friction in scientific analysis, many economists are less welcoming in introducing non-zero transactions costs, most probably as it messes up their otherwise tidy analysis. The assumption of zero transactions costs is perhaps better defended as being analytically convenient, rather than criticised as being unrealistic.

While Williamson proclaims the efficiency advantages of discriminantly assigning particular transactions to particular governance structures, it is not made explicit in his work who actually performs the discriminatory assignment of transactions to governance modes. As a result of his assumption of opportunism, individuals who perform this function are consequently likely to bias the chosen modes to appropriate more value from contracts and transactions towards themselves. This is likely to be particularly true given the opportunism assumption paired with the fact that often it is the case that certain individuals are passive within relationships/ organisations. The result is hardly likely to be conducive to truly efficient governance of contractual relations.

Williamson's analysis tends to focus on one particular exchange relationship/ contract, ceteris paribus. It is, however, the case that all transactions/ contracts/ exchanges will be more or less interdependent, implying that changing the institutional form of one of the relationships, will affect to a greater or lesser extent, all others. Hence, Williamson's failure to recognise the dynamic systems nature of these underlying relationships implies that by attempting to increase contractual efficiency in one area (reducing transactions costs), any benefits may be far outweighed by introduction of greater contractual inefficiencies (increased transactions costs) elsewhere in the system. Williamson's analysis overlooks this potential problem and offers no comment on this probable situation.

2.4 Creating an analytical framework by synthesis of elements of these theories:

From the preceding critiques of the newer property rights, agency costs and transactions costs approaches to organisation, it is apparent that while these newer theories do offer significant insights in industrial organisation beyond those of Neoclassical orthodoxy, they are, nevertheless, far from perfect. They are perhaps best viewed as a good point of origin/ departure rather than a theoretical terminus. They are strongly indicative and informative of the types of issues theory should address, and should be capable of addressing satisfactorily.

An examination of these theories' inherent failings points to directions in which theorists should strive to develop them further to improve their collective ability to explain modern industrial organisation.

(I) The importance of individual behaviour in organisation.

It has been demonstrated through the series of critiques above that the importance of ownership is crucial in terms of incentive creation, manipulation of incentives, and influencing individual behaviour. This can be traced back to the input of the property rights approach. The importance of the alignment of incentives to avoid conflict in behaviour of individuals is also apparent, and this notion derives directly from agency theory. The importance of the specification of implicit and explicit contracts to influence behaviour in various directions is stressed by all of these theories, which share a view of the firm as a collection of such contracts.

(II) The importance of satisficing behaviour and bounds to human rationality:

The economic agents interacting within any economic system cannot simultaneously maximise their maximands (or even all simultaneously engage in successful satisficing behaviour) except in the restrictive and highly improbable situation where their objectives are exactly aligned inter-personally. At best there can be joint benefits from cooperation and exchange. The organisation has to solve the problem of how to organise its interior and exterior to manage formal and informal exchange between its constituent economic actors and achieve non-zero sum gain within the overall system. In terms of Neoclassical theory an interesting anomaly is posed here. Utility maximisation and profit maximisation would appear to be assumptions which cannot coexist in the absence of behaviour by agents of the firm gaining utility exclusively from the maximisation of firm profits. This is strictly irrational behaviour which would conflict with the standard Neoclassical assumption of full rationality of economic man.

Buchanan (1975) saw economics as a science of contract rather than choice, where the maximiser is replaced by an arbitrator in order to align incentives and organise conflicting aims in a compromise [37]. In the light of this view of economics, it is difficult to see how optimisation can occur for many economic problems given constraints and the existence of conflicting agents. This view is consistent with that of Simon and his exposition of human rationality and consequent decision making capabilities.

(IV) The importance of inter-dependency and a systems view of organisation:

Neoclassical economics assigns no role to asset specificity. In many economic problems, the

existence of asset specificity is an important feature and this is a theme constantly stressed by Williamson throughout his work. Neoclassical economic theory is ill equipped to deal with the problems of asset specificity and as a result cannot explain 'locking in' and interdependency in many important economic relationships and organisation [38]. Firms within markets are very much inter-dependent and not independent of each other and this is another aspect which contemporary theory of organisation requires to deal with.

Thus, some of these important elements have been partially addressed by some of the newer theories. To date, however, they remain underdeveloped and theory must develop to address and accommodate, in particular;

1. Inter-temporal and inter-personal variability in individuals' information processing and, hence, decision making capabilities,
2. Recognition of the interdependency and systems nature of much of economic activity and organisation, and,
3. Dynamic and evolutionary processes that constantly alter the efficiency and effectiveness of current solutions, require constant selection and adaptation, and force the requirement to perceive desirable future directions and implement strategies to steer towards them.

2.5 Strategic Individual Behaviour in Organisations and Networks:

One significant problem theory of organisation requires to address is that firms are collections of individuals each of whom have their own personal objectives which coexist alongside those of the firm (some of which will be consistent and others inconsistent with that of the firm). Further complexity is introduced into this objective system on recognising that within this interacting system of personal and firm objectives, individuals' objectives will not be entirely inter-consistent. Furthermore, groups of individuals within the firm (eg. constituting a department/ division) will also have objectives either consistent or inconsistent with those of the firm, other sub-groups of the firm, other individuals within and outwith the group, and the like. It is clear that in understanding the firm as a collection of these agitated individual molecules, theory of the firm faces an formidable and unenviable task.

(I) Uncertainty, risk and human decision making:

It is, however, not the case that individuals behave in a random manner - only a purposeful and capricious one. If humans behaved in a completely random fashion, it would be impossible and a complete waste of time to observe and theorise their behaviour. Hence, for a given set of circumstances it is possible to narrow down from all perceived possible

behavioural responses, those which are more likely to occur. Faced with problems of uncertainty, economists have attempted to conceptualise theoretically, how individuals behave within organisations.

One school of thought would argue that assessments of probability of occurrence of different behavioural responses can be used. This technique, popular in areas such as game theory and certain theories that attempt to explain risk, suffers from the severe limitation that in order to attach probability to the set of possible outcomes, all possible outcomes must be known in advance [39]. In the area of human behaviour it is unlikely, especially if it is accepted that individuals are boundedly rational, that all possibilities can be foreseen. Hence, the assignment of probabilities to examine behavioural responses has its problems.

Individuals do, however, when faced with the choice of behaving in alternative ways (for instance when decision making) require to formulate strategies in response to situations they perceive themselves to be in within the organisation. As we know from above, analytically, Neoclassical economics sets single exit determinism as the default so that behaviour is known in advance with complete certainty. In the typical case where behavioural alternatives exist and an undefinable and indeterminable range of outcomes could occur (given various combinations of strategies that can interact within the organisational setting), single exit determinism can be regarded as being analytically very restrictive. The concepts of opportunism and the existence of differing degrees of rationality are pivotal within this view. It should be noted here that the use of probabilistic models with multiple defined exit solutions are also restrictive to the extent that, by specifying all possible outcomes in advance, they too assume away uncertainty [40].

In this context, Williamson's transactions cost analysis would be analytically far stronger if he accommodated variability in bounded rationality and opportunism, combined with an expanded and more explicit notion of his concept of contractual atmosphere.

The organisation is essentially a resultant of continuously revised strategies and behavioural responses adopted by all who are party to the inter-dependent network of contracts of the firm. Utilising such a view of the organisation effectively captures the dynamic qualities of intra and inter-firm relations, where the network is part of a wider system of other networks which itself is subject to constant change. Differing individual behavioural responses can be understood as rational in terms of the levels of rationality, perception and interpretation attending particular individuals and resultant strategies adopted by them in relation to these characteristics.

Strategic behavioural responses adopted by an individual in relation to internal and external stimuli can be viewed as reflecting many of that individual's revealed characteristics such as;

risk aversion, utility preferences, degree of opportunism, goals etc. This view highlights the heterogeneity of, and constantly changing dynamic properties of, individuals within any organisational system. In this context, individuals cannot simply be viewed as two dimensional beings who exhibit constant and predictable behavioural traits independent of time or circumstance.

The implication of the above is that in order to understand modern, complex systems of organisation, what is required is a more descriptive analysis which stresses even more strongly the role of individual behaviour within organisations than do newer organisational theories, even accepting their more permissive methodology.

To this end, it is necessary to go beyond Williamson's inclusion of opportunism to a situation where the degrees of opportunism are more explicitly viewed as a characteristic that varies between persons, time and circumstances. The analytical focus and unit of analysis to this extent will require to switch from emphasising the importance of transactions to emphasize, through decomposing the organisation into a system of individuals, the principle components of the firm (ie. its individual constituent members).

(II) The importance of the non-consistency of opportunism and human rationality:

Williamson's safety net for his assumption of the constant and ever present opportunism characteristic is his implicit reliance on readers of his theory to apply the concept of contractual atmosphere as they see fit to vary the degree of opportunism. This is unsatisfactory since in many circumstances only ad-hoc adjustment of the theory will facilitate an explanation of the economic problem under scrutiny.

In certain circumstances contractual atmosphere exclusively provides an explanation for observed governance, and the explanation becomes more user driven than founded in the main body of his theory. This is particularly true when observing patterns of contractual and exchange relationships characterised by complexity/ uncertainty, which appear to have little or no formal governance, rely purely on reciprocity and trust, and which would otherwise appear to be potentially hazardous from the point of view of opportunism. The transactions cost framework, by assuming the existence of opportunism as a default, copes far less adequately with situations of cooperation and trust. An alternative framework which embodied variability in opportunism and human rationality, along lines to that which is discussed above, would go some distance in dealing more satisfactorily with situations of cooperation and trust between individuals and firms.

2.6 A Comparison between Transactions Cost Theory and Network Theory:

Network theory purports to address some of the deficiencies of newer theory of organisation highlighted above by viewing the organisation as a relational network. Hereby, network theory attempts to integrate concepts drawn from nexus of contracts approaches to the organisation, with notions of strategic behaviour. This approach can help make more explicit some of the notions left to the imagination within Williamson's concept of 'contractual atmosphere'. Within a network theory view of organisation, trust is the implicit default characteristic for individuals, thus providing an ideal contrast to the opportunism assumption of the transactions cost framework. Trust can be regarded as a very future-oriented concept although it is firmly rooted in past interactions and present behaviour, whereas opportunism is entirely a present based concept which discounts the value of both future and past interactions.

Different degrees of, and opportunities for, opportunistic behaviour can be viewed as evoking different rationally evaluated strategies. In terms of the transactions cost framework its attraction lies in its ability to explain the existence and persistence of different forms of contractual governance and/ or evolved institutional forms, for different sets of circumstances. However, in relation to its ability to explain more complex strategic behaviour it is in general weak due to its preoccupation with conditions necessary for stable equilibrium and single-exit deterministic solutions (behaviour is assumed to at all times be directed towards opportunism, and governance towards protecting transactions from its inevitable consequences).

For a broader and more informative analysis of the multiple behavioural and related governance possibilities which face the firm, transactions cost economics must make way for network theory which highlights the wider set of possible opportunities and responses which confront the future oriented firm, in any set of circumstances.

(I) Dealing with incompatible individual behaviour in the Transactions Costs framework - contractual efficiency implications:

Within any system of organisation, it has been previously argued that individuals can, and often do, pursue goals which are incompatible and conflicting with the overall goal of the organisation. Individuals often interact with other individuals and sub-groups of the overall organisation in such a way that the individual behavioural responses appear to make little reference to overall objectives of the organisation. Williamson overlooks, or at least fails to discuss this distributional problem among agents, particularly with reference to his policy of discriminately assigning particular governance structures to particular transactions. It may be useful here to think of individuals possessing their own behavioural strategies where modes of

governance pursued by the firm to govern specific transactions can be viewed as problems of strategy coordination. The coordination/ implementation problem is characterised by a requirement to formulate and manage strategies aimed at implementing, desired modes of governance, paired with a need to respond to and control strategies aimed at counteracting their implementation.

Any resulting implementation is, therefore, likely to be far more adequately informed of reasons why certain individuals are for, or against, certain modes of governing transactions. This should address at least some of the distributional concerns, highlighted by but largely ignored within the transactions cost framework. To facilitate this the features of the incentive structure of the firm require to be made far more explicit and identifiable, and be more consciously and carefully designed to avoid sub-goal pursuit.

It would be entirely rational when the mode used to governing a particular transaction changed for potential losers to behave to defend their position by attempting to minimise its impact and for potential gainers to attempt to maximise its impact. The actual redistributive outcome precipitated by change in governance will be some compromise with the losers not losing as much as they anticipated and the winners not gaining as much as they anticipated. This outcome is likely to differ from that which would have been likely to occur where the bargaining process to change governance structures had been based, as Williamson seems to indicate it would be, on pure contractual efficiency grounds.

Williamson's concept of efficiency appears to correlate most closely with productive efficiency, with an apparent complete neglect of distributional efficiency effects. In the absence of an independent neutral third party who makes and implements the decision regarding which transactions to assign to which governance modes, it will almost inevitably be the case that any decision will favour the party making the decision. This problem, however, even presupposes that boundedly rational agents responsible for assigning governance modes to transactions can make rational comparative transactional efficiency comparisons. This is highly unlikely, and in this respect, it is arguable that the efficiency argument proposed by Williamson, for assigning particular governance structures to particular transaction types, become almost irrelevant - the decision is likely to be based not on efficiency grounds but on biased subjective comparisons. At best such a decision process would become inherently biased.

Instead of being based on objective efficiency criteria, the decision to assign governance modes to transactions will rather tend to be based on which mode of governance appropriates the greatest distribution of money and psychic wealth towards those who take the decision. The implication of this for the organisation is that the decision process will tend to be assigned to those who are at the top levels of the hierarchy. The firm will, consequently, have

a natural tendency to evolve in a manner in which the organisation suits those who have control over the decision making authority in the firm. This highlights the problem in simply assuming that certain observed patterns of evolved contractual relations are efficient.

(II) Opportunism.....cause or effect ?:

Williamson's discriminatory assignment of governance structures to transaction types implicitly assumes that the party responsible for doing so is completely impartial and indifferent to the resultant redistributional effects any new governance mode. It is precisely because of the decision making/ hierarchical bias discussed above that opportunism is likely to be a feature of behaviour of the decision making authority in such situations. Williamson may have taken on board the opportunism assumption within his framework simply because of the natural existence of this bias (which tends to exist as an inherent feature of the modern corporation) rather than because it is an ever present and intrinsic feature of individuals.

In terms of establishing a direction of causation, rather than evolving to cope with and protect against opportunism, modes of governance many may have evolved to facilitate the institutionalization of opportunism. In this sense opportunism is not a characteristic feature of the individual per se, but rather a trait which is picked up from the way in which the firm is organised. The winners will systematically tend to be those individuals within the firm who have the authority to take decisions and perpetuate their position through opportunism.

(III) Trust vs. Opportunism:

While Williamson focuses on potential situations arising from opportunistic behaviour (which is viewed as an omnipresent potential hazard in many situations involving human interaction), Network theory prefers to stress trust and benefits from cooperation. Consequently, it is far less a conflict management approach than Transactions Cost Theory. As a result of trust, network theory stresses the role to be played by organisation in the transactional middle ground between market and hierarchy (which Williamson says very little about throughout his work). Network theory argues that in this middle ground area, may adequate solutions to the management of opportunism/ development of trust when contracting may be found. It is claimed by Network Theorists that network organisation fits somewhere in between market and hierarchy [41].

(IV) Reconciling Bounded Rationality and Boundless Information:

In the process of selecting strategic behavioural responses, the individual must overcome a number of problems. These problems basically all stem from the fundamental problem of the individual suffering from bounds to his rationality. Through time, as the individual processes

more bits of information and gains knowledge his behaviour will change to reflect the wider information set in his domain. This information set and domain will be different for each individual within the firm due to differences in perception levels and interpretive flexibility in processing and assessment. Hence, some elements of misinformation and irrelevant information will be incorporated in the manner in which individuals choose to behave within an organisation.

The strategic use to which an individual will be able to put information will depend on numerous factors including the following:

1. The extent of the information and knowledge in the individual's domain,
2. The privacy of that information in relation to others,
3. The extent to which the individual can utilise his rationality, perception and decision making capacity,
4. The extent to which that person can issue signals which may lead to incorrect strategy formulation on the part of others (eg. 'bluffing' and 'chicken' techniques).

The individual's resultant ability to deal with complexity, perceive strategies and react to them, will be a strong determinant of his success or otherwise within the organisation.

In summary, mainstream attempts to introduce strategic behaviour to analyses of the organisation have tended to concentrate on situations of complete certainty, complete information sets and fully rational behaviour on the part of individuals. As a result the behaviour of the individual is characterised in a broadly similar manner to Neoclassical theory by assuming maximising rather than satisficing behaviour of agents. To this extent, bar the introduction of the concept of strategic behaviour via game theory, mainstream attempts lend very little to theory of the firm in terms of explaining many economic problems resulting from behavioural interaction of individuals within and between firms.

Network theory stresses the importance of both competitive and cooperative relationships [42]. Its framework further recognises that the ability of the firm to create and sustain cooperative agreements can be determinative of its ability to survive within its external (selection) competitive environment.

(V) Between Markets and Hierarchies - Networks and Relational Inter-dependence:

Thorelli (1986) [43] views networks as existing somewhere between markets and hierarchies, which provides an interesting contrast to the view of Coase (1937) [44] who viewed the market as an alternative to the firm. These views of organisation, while differing, are broadly consistent to the extent that they focus on different aspects of the same problem.

The network view stresses that, as a precursor to understanding the firm, one must first refer to its relationships with many other firms. As such, the firm must be situated within the wider context of its relations with others in the market-place. In essence, a nexus of contracts view, consistent with theoretical perspectives discussed earlier in this chapter, is applied. In the case of network theory, the major difference is that the boundaries of the firm and its organisation are explicitly recognised as being wider still.

Consequently, networks are envisaged to constitute sets of complex arrays of relationships between firms. The pivotal role of contractual and informal arrangements/ agreements is to facilitate preservation of these relations and the consistency of the network. Within network analysis, the role of the firm in relation to competitiveness is to secure a position within the network (ie. manipulate it using trust) rather than attack an established system (opportunism against other firms).

This attempt at securing a position within a network is not without attendant costs. This implies that to penetrate and subsequently survive within a network the firm must expend time and resources. The general outcome is expected to be the sustained health of all firms in the network, through mutual recognition of the desirability and advantages of inter-dependency of network member firms.

For the individual firm this implies that a prime motivation of the firm is to attempt to secure the best position it can within the network without upsetting the rest of the system. In this sense, aggressive penetration aimed at knocking out some of the existing network members is short sighted opportunism. Network positioning requires good quality information concerning the network and a well reasoned strategy on the part of the positioning firm. Within network theory the importance of strategies is clearly evident and this can be regarded as a prime motivation for Jarillo (1988) to entitle his article 'Strategic Networks' [45].

Within any network, firms are only limitedly interdependent since complete mutual dependency, in the absence of excessive transaction/ agency costs, may rationally justify, or at least suggest, a move towards vertical/ horizontal integration. An important point should be made at this juncture, namely that transactions costs can be perceived to significantly affect entry to, positioning and re-positioning within, and exit from established networks.

Relationships developed within the network are vital to the competitive position of network firms both with respect to competitiveness of individual firms within the network, and in respect to other firms outwith the network. The existence of a strategic network requires the inclusion of the "hub-firm" concept. The 'hub-firm' is the firm that instigates initial formation of the network and plays a coordinating role by takes positive steps to protect its existence.

The role of the hub firm is to preserve the network by taking positive actions to ensure that constituent firms continue to perceive congruence of goals in order that non-zero sum benefits accrue through cooperation. The role of the hub-firm thus closely parallels that of the head office in Williamson's analysis of the M-Form organisation [46].

In terms of applying network theory to the law firm in particular, the sharing bargain can be understood in the context of network theory. A correctly designed partnership sharing bargain within the law firm, can parallel the role of the hub firm where it has similar goals in its attempt to secure pursuit of congruence of goals with a resultant non-zero sum benefits between partners. In this case, network organisation is envisaged on a more micro level within the firm, as opposed to existing between firms at a more aggregate level.

Within his transactions costs analysis, Williamson's discussion of modes of transacting between market and hierarchy is almost non-existent compared to his lavish analysis of these two polar transactional modes. His interpretation of middle ground relationships involving mutual orientation/ reciprocity is that bilateral governance will effectively manage such transactions. He implicitly views this informal reciprocal relationship as a characteristically unstable form of institutionalised transaction. Adopting this view, network organisation, which very much mirrors this type of transactional mode, would be characterised as an unstable mode of governing transactions. Network theorists are quick, however, to emphasise that network relationships are characteristically stable, not unstable. .

Opportunism can be regarded as the behavioural antithesis of trust and it is lack of trust (or potential for opportunism) that can be viewed as being largely determinative of transactions costs. It could be thereby implied that network organisation and exchange may possess an inherent tendency to be more transactions cost efficient than many other institutionalised modes of governing transactions. The stability of the network, resulting from the trust which forms its foundations is likely to subsequently feed back to the network reinforcing trust and stability in a self-fortifying manner. It could be expected that fewer resources are consumed in respect of attempting to safeguard against opportunism in the case of network exchange as this thrives on trust and cooperation.

It is necessary, however, to outline the factors which could be actually create the stability and trust alleged to be inherent within network organisation. Firstly, in order that a form of organisation initially evolves - thereafter becoming self-sustaining - the twin characteristics of effectiveness and efficiency are likely to require to be addressed. In this respect, the organisation can be perceived to be 'effective' if it achieves that which it was established to achieve. It is 'efficient' if it does so whilst, at the same time, offering inducements to its constituent members beyond the level of their inputs to the firm, thereby making it attractive to stay rather than exit the organisation.. These two basic conditions, effectiveness and

efficiency, are the basic conditions necessary for the existence of network (and any other) organisation.

(VI) How are effectiveness and efficiency fulfilled by organisation?:

To answer this question it is necessary to focus on the mechanisms through which conditions of effectiveness and efficiency are fulfilled within an organisation. The incentive structure of the firm comes under close scrutiny in this respect, whereby a well designed incentive structure should be aimed at creating an atmosphere of trust, mutual cooperation and reciprocity. These conditions can be regarded to be desirable elements of behaviour which counteract expansion in transactional difficulties/ costs associated with collective pursuit of economic aims.

To achieve this desirable 'contractual atmosphere', to borrow Williamson's phrase, individuals must acknowledge the mutual interest that exists within exchange relations and the value of their continuance over and above short sighted opportunism. This mutual understanding need not be made explicit and should be perceived by all relevant parties in exchange through release and receipt of appropriate signals/ information. The careful screening and choice of individuals who are likely to have similar values is likely to create identity and similar motivations that are conducive to the emergence of trust, within the organisation. This informal signalling and implicit exchange of trust can be regarded as a much diluted and less formal variant of monitoring and bonding activities, emphasised in theory of agency relationships.

There is a strong link here with a central posit of game theory which states that cooperative relations are likely to be more conducive to non-zero sum games and competitive ones to zero sum games. The implication is that, within the network, cooperation is of the essence in order that the firms within the network are poised to compete from a strong position with firms outwith that network [47].

Network theory places great emphasis on long term relationships in view of the fact that such relationships are more conducive to the development of trust. At the commencement of a relationship, the emphasis placed by each party on the desire for the relationship to become long term sends out mutual signals of the resultant non-viability of opportunism. As the relationship develops, the longevity of the relationship signals its value to those that are party to it. To that extent opportunism, which would cause the relationship to cease, would be less likely [48].

In the context of multi-disciplinary practice (MDP), the existing situation, whereby professions view each other as a threat, could be converted into a situation whereby a

network could be established. Cooperation, inter alia, would ensure competitive strength against those outwith the network. Here, the strategy would be to create a supportive network based on trust between professional sub-units of the network, to exploit the non-zero sum game advantages of cooperation. To a certain extent, these informal professional networks already exist whereby banks and building societies, solicitors, estate agents, financial consultants, accountants etc. all currently feed each other with clients and business, relying on reputation and trust based network incentives for stability and reciprocity of exchange.

Networks are viewed as exhibiting the twin (opposing) characteristics of stability and dynamism. They are stable irrespective of their constituents, yet are subject to constant change as firms enter, position, reposition and exit [49]. Bonds are developed between firms within the network in terms of information, knowledge, contracts, technology, human characteristics, social norms etc. with the resultant network process being characteristically dynamic as firms relative positions and powers change.

In network theory, the realistic assumption is made that the individual firm does not have complete command over all resources necessary for its survival. This recognition of the inability to survive individually emphasizes the requirement for firms to cooperate with each other and underscores the interdependency/ systems nature of industrial organisation. Some firms may actually be subject to quasi control by one or more of firms within a network. Firms must be aware of interdependency which exists and behave at all times in a manner which is consistent with the continuance of the interdependency. The mechanism for problem solving is through the use of 'voice' rather than 'exit' options as this should be more conducive to longer term survival [50].

The result will be the adaptation of relationships in a sequential manner as contingencies arise and this should reinforce bonds between firms through increasing inter-dependencies. The goal is the creation and sustainment of a mutual orientation in the network.

Network theory, to a certain extent, addresses one of the major criticisms levelled at Williamson's transactions cost framework, namely acceptance of the Neoclassical assumption of survival of the most efficient organisational form. Network theory envisages the organisational problem as being a constantly shifting dynamic issue, thereby rejecting any notion of static optimality in organisational form. Organisations are, thereby, perceived to be typically the result of a mix of conscious design, evolution and self-selective/ accidental development, whereby it is unlikely that the form of organisation that exists at any given time will be optimal in any sense.

Network theory also goes further than Williamson's behavioural assumption of individuals being characteristically opportunistic. It is argued that it is unlikely that individuals will be

subject to a constant characteristic of opportunism and that they may actually be just as (or even more) likely to exhibit trust as a behavioural trait. The implication, here, is that analysis must not adapt either of these characteristics as exclusive behavioural norms but rather view behavioural possibilities/ scenarios along a continuum between the two extremes of trust and opportunism. Williamson's work does not stress the importance of the consequences of such behavioural possibilities/ variations.

Arguably, the main failing of the transactions cost framework is its emphasis on conditions necessary for stable equilibrium. Consequently, the deterministic implications derived from its framework compromise its ability to analyze strategic motivations of the firm and its individual constituents. It is this deficiency which network theory may be able to partially address.

Network theory is perhaps most usefully seen as an enrichment of Williamson's characteristic of "contractual atmosphere" where network exchange can be viewed to facilitate the creation and sustainment of trust. This would at least partially obviate a major cause of transactions costs, namely lack of trust, or as Williamson prefers to succinctly label it, 'opportunism'. Network mode of exchange/ organisation can be viewed as a device that can economise on transaction costs and the bounded rationality of individuals therein. The bounds to individuals' rationality are exhausted far more quickly under conditions of opportunism than trust.

The is no explicit definition within network theory as to what constitutes a network. In this respect, network theory suffers from a similar problem to transactions cost theory, wherein Williamson neglects to provide a precise definition regarding what constitutes a transaction. To this extent both theoretical perspectives can be criticised for suffering definitional imprecision. From surveying the relatively small literature on network organisation, it can be argued that network organisation essentially describes structures of relationships (contractual and implicit) between individuals/ firms which are self-sustaining as a consequence of the high levels of implicit trust that characterise the atmosphere surrounding them.

An interesting parallel can be drawn at this juncture between networks and cartels. Both can be perceived as having similar goals of insulating its members from the forces of competition. They do, however, have differing levels of success in this direction to the extent that networks are characteristically stable whereas cartels are typically not due to, for instance, quota cheating [51]. By drawing this comparison it appears that networks must possess some intrinsic feature that prevents individuals cheating on the rest of the network. Networks must possess some feature that promotes stability and self-sustainment. It is most likely that this stabilising factor is its incentive structure. In network organisation the risk and penalty of being discovered acting in an opportunistic manner far outweighs any short term gain that may

accrue from doing so. The penalty would be exclusion from any future participation in the network.

Networks could thus be likely to evolve and survive as successful governance modes in situations where any dissenting participant would be subjected to substantial personal loss consequent on trust breaching behaviour being discovered. The professional partnership, and indeed the legal profession as a whole, is clearly a strong example of this, where trust is a crucial firm and market characteristic. At the market level, those practising the law have been subjected to the continual socialisation and rigorous selection procedures of the profession. At the firm level, there is a firm specific socialisation process and rigorous selection procedure for initial entry to the firm, and more importantly, entry to profit sharing partnership [52].

In legal partnerships it is often the case that partners are observed to engage in altruistic behaviour in respect of their fellow partners. The transactions cost framework finds difficulty in explaining altruistic behaviour between actors within exchange relationships as it appears irrational and inviting of opportunism. This behaviour is viewed as puzzling as a direct consequence of the behavioural assumption that individuals are basically opportunistic. Against this assumption, altruistic behaviour is perceived as being irrational.

In the case of network exchange, it is precisely this type of altruistic behaviour which must be present in order for the network to come evolve in the first instance and thereafter become self-sustaining. In assessing the applicability of either a transactions cost or a network approach to analysing the organisation, a crucial factor appears to be the nature of the expected behaviour of the individuals within the organisation under scrutiny. The extent of the expected altruism/ trust or opportunism will shed light on the level of expected transactional difficulties. Hence, the behavioural assumptions most closely expected to apply to those within the organisation under analysis, will become apparent, indicating which of the theoretical approaches would be likely to be most applicable. This will additionally indicate the extent to which formal behavioural constraints could be expected to exist within the organisation to cope with potential transactions cost enhancing problems of opportunism.

It could be implied from the above that due to high levels of trust and potential avoidance of the requirement to have in place costly (transactions cost reducing) behavioural constraints, network exchange is a relatively cost-effective governance mode in appropriate circumstances. It is, however, necessary to attempt to identify, and as thoroughly as possible quantify, the costs of using networks as a governance mode. These costs will most significantly include initial costs of setting up the network, selection/ positioning/ repositioning costs, and costs of running the network (including screening, monitoring and bonding costs). The distribution of these potentially significant costs between network members is also of central importance.

Network organisation can clearly exist as a replacement for, or as complement to, market exchange. In such organisation, however, there requires to be some controlling function of the network and in its absence the network would be likely to operate far less effectively and efficiently. The 'hub firm' could perform the function of overall monitor of the network. It is not clear, however, whether the hub firm would require to perform this function in order for the network to come about in the first instance, or whether this function would simply necessarily evolve to ensure that the network was efficient and effective. In the case of the legal profession this 'hub-firm' role is played by the relevant Law Societies, in the case of the medical profession by the BMA, and by the Royal Pharmaceutical Society in the case of Pharmacists [53]. These monitoring (hub-firm) institutions exist for the communal benefit of network members and also the consuming public. They may, however, perform wholly self-interested roles in the maintenance and furtherance of network interests. In the absence of a legalised or legitimised overall monitor function to preside impartially over relatively rare instances of intra-network conflict, it could be expected less likely that network exchange and organisation would occur and survive.

An interesting question is posed on comparison of network and market organisation. If it accepted that the advantages of network organisation proposed by disciples of network theory actually exist, why is market organisation the more popular evolved governance mechanism? It can be construed by observing relative popularity that market organisation appears to outperform network organisation in many sets of circumstances. It is likely, therefore, that in order for networks to evolve in the first instance and then become sustainable, a set of particular conditions require to be satisfied. It is imperative, therefore, that network theorists explicitly identify these conditions and, in addressing organisational issues, reveal the precise nature of the types of problems the existence of network organisation seeks to address, and what determines their survival and stability.

2.7 Characteristics of Network Organisation:

From the literature it can be inferred that the overall aim of network organisation is to foster and encourage supportive cooperation between individuals and firms. In order that this occurs, members goals and strategies must be seen to be broadly consistent with the overall network strategy in order to avoid being ostracized. In this respect, the distinction between loose and tight network relations must be investigated. The 'tightness' of a network will be dependent on the quantity, quality and the type of interactions in the network paired with the relationship between power/ influence and trust existing between members [54].

In any network it is necessary to uncover the flows of information, authority and payments in order that network members' strategies can be interpreted. The primary focus of the strategy

of a network, and of members strategies within networks, is power. Power can be regarded as the ability to influence the decisions and actions of others. In a multi-firm network, the power of a firm will be determined by its relative position within the network, and this will have consequences for the strategies it can formulate and implement.

Network members may provide certain services to other network members and members may access benefits that are not available to those outwith the network. An example of such benefits could be information/ knowledge, which can be a substantial source of power for firms over those firms external to the network. This provides network members with an individual advantage over non-members and also provides the overall network with a first mover advantage over competitors/ other networks.

Certain forms of behaviour are to be recognised as unviable within networks (eg. plagiarism in academia). The threat of exclusion from participation in all future benefits of the network acts as a severe constraint on the viability of such behaviour. The harsh penalty of exclusion should avert such behaviour from network members. A paradox of behaviour is apparent here since, in order for the opportunism to be of benefit to the wrongdoer, it is likely that it would have to be repeated. This repetition, however, would increase the chance of being discovered and penalised. Only blatant opportunistic behaviour is likely to be of worthwhile immediate gain, but this will almost certainly be discovered immediately and is, therefore, not viable. Exclusion from the network is the price to pay here, and this could result in a loss of human capital and/ or the value of any bonding effect of capital input to the firm.

The combination of high entry and exit costs can be seen as a bonding mechanism/ incentive to remain in the network. With low entry and exit costs it could be expected that networks would be eroded away fairly quickly and indeed these may be a necessary, yet insufficient, condition for the existence of a network.

Networks are most valuably viewed as being multi-layered/ multi-dimensional in the respect that they can operate at the level of the individual firm and also, for example, in the case of legal services, at the level of the profession. There is, in essence, an overall network which contains sub-networks in a nested system.

Networks are likely to be able to cope more adequately than markets, or traditional hierarchies, with externalities such as those commonly associated with training and R&D expenditure. The high incidence of externalities that attend such activities often result in, for example, joint venture agreements/ strategic alliances as a method of attempting to suppress at least some of the externalities and gain required complementarity in skills, human capital, knowledge etc. To this extent, networks may partially mitigate problems of under-investment in activities such as R&D and training, traditionally viewed as pertaining to other

organisational modes.

In a typical market based transaction, faceless buyers and sellers meet and exchange contracts with immediate settlement. In a network, however, no immediate payment need be received - in fact no payment may be necessary or identifiable in relation to specific transactions. There must, however, be an expectation of gain from share in the present value of many future benefits and transactions.

Thorelli (1986) very loosely views a network as consisting of two or more organisations involved in long term relationships [55]. Within such relationships, payments and benefits are generally often unspecified and the transaction is characterised and surrounded by reciprocity, high degrees of inclusion and self discipline, recognition of common values/ beliefs and importance of social/ behavioural norms.

The repetition of contracts is viewed to be of crucial importance as a concept within the newer literatures concerning contracts (eg. transaction and agency cost theory). Their notion of repetition, however, does not go far enough and the recognition of two types of repetition would appear to be required. In this direction, a distinction between 'horizontal' and 'vertical' repetition of contacts is important. 'Horizontal' refers to the repetition of a number of similar contracts commencing in the current period and taking place over a period of time in the future with the same contracting party. 'Vertical' refers to repetition of a number of different contracts in the present period with the same contracting party.

A network is in no sense a static system since its internal interdependencies change over time. Resources are consumed in networks, firstly, in order that the network can survive and attain its reason for existence and, secondly, to overcome intra-network friction and conflict and attain cooperation [56].

The position of the firm within a network is important and Thorelli (1986) [57] argues that this depends on the following factors;

1. The domain of the firm, which Thorelli (1968) [58] identifies as being defined by five dimensions;

(i) product (or service) offered in the environment,
(ii) clientele served,
(iii) functions performed (modes of operating),
(iv) territory,
(v) time.

2. The position of the firm in the network, which is closely related to the relative power/ influence it has in relation to others in the network. Power is manifested by a differential advantage (short term perceived/ long term real) in one or more of the following areas;

(i) economic base,
(ii) technology,
(iii) expertise,
(iv) trust,
(v) legitimacy.

Trust is the central feature of network theory, where it can perform the important role of superseding formal contractual relationships. In many instances it can supplement formal contractual exchange to promote increased contractual efficiency. Strategic utilisation by a firm of its power/ influence is very important. An important feature here is the interdependence of firms and their actions. The inclusion of the concept of interdependency can be seen to the antithesis of conventional treatment of the atomistic firm within Neoclassical theory of competitive markets.

Thorelli (1986) views the dynamics of network theory emanating from the dynamic process he envisages occurring in network organisation [59]. This process is characterised by a four stage process of entry, positioning, re-positioning and exit. Transactions costs can be viewed as affecting the ease with which the stages in this process can occur.

When a new member enters a network he has to gain position, and this is a function of his power and influence. This requires that existing members reposition themselves in the network. Their repositioning strategy will be dependent on their reactions to the perceived power and trustworthiness of the new member.

Networks will tend to fail when a buyer becomes his own supplier. Over time, in the absence of active and effective network management, Thorelli (1986) argues that it would be likely that networks would be subject to natural wastage and tend to disintegrate under the impact of entropy [60].

It could be the case that firms may view networks as viable alternative solutions to many strategic problems, including several that have been discussed in Williamson's transactions cost framework where various relational exchange solutions have been suggested.

With reference to network stability, the difference between constructive competition and destructive competition is important. For example, in oligopoly there is usually either tacit or

overt collusion and this can be argued to be constructive competition. The same may be true in network theory where there may be significant degrees of competition between network members, but also strong elements of cooperation.

Network theory can be seen as useful in analysing many areas of industrial organisation where even newer theories such as the those of transactions or agency cost provide inadequate insight [61]. It also concentrates on the importance of individual behaviour and the importance of behavioural norms, trust, social expectations and less visible (yet vitally important) aspects of exchange between firms and individuals. Network theory also stresses the dual importance of competition and cooperation as interacting and concurrent states that exist within and between firms, inside and outside networks and markets. Network theory further highlights the importance of efficient cooperative agreements as it results in non-zero sum benefits for the participant firms.

2.8 How can these theories aid understanding of organisation of the legal profession?:

Within an examination of the practice of the law firm, it is advantageous to employ a nexus of contracts view and one which recognises the importance of individual behaviour within the firm. This is justifiable in terms of the importance of the elements of market failure in legal services, and the expectations of the current structure of the legal profession in addressing such market failure problems. The introduction of all important contracting parties in this expanded view of the firm, permits a more comprehensive examination of the complete set of organisational (interior) and market (exterior) problems. It is only then that an understanding of law firm practice may be forthcoming.

In conceptualising this nexus of contracts view of the firm, it is necessary to draw together notions drawn from property rights theory, agency theory and the transactions cost approach together with notions of directions in which analysis should be going to overcome some of their current deficiencies. In this light, Network Theory and its attempts at circumventing some of the criticisms of mainly Transactions Cost Theory, is a useful addition to the body of theory required to explain organisation. Although these profess to be differing views of the organisation, they do all reach broadly similar conclusions, excepting Network Theory. This is hardly surprising given that they all employ similar initial behavioural assumptions and merely emphasise the requirement to focus on different aspects of similar problems. The strongest thread running through the approaches is the recognition of the importance of contracts and the existence of principal - agent relationships with their attendant difficulties.

Within the study of the law firm, an examination of the nature and causes of potential opportunism in two major areas is required. These areas are;

1. The exterior of the firm - the market for legal services, where the regulation of the market can be seen as a response to constrain opportunism and elements of market failure.

2. The interior of the firm - within the firm itself, where the firm is viewed as a set of contracts drawn up to constrain opportunism.

More specifically, the primary concern of this thesis, in its quest to explore the interior of the firm, is the nature of the income sharing bargain between partners. The firm and market elements are of course not unrelated since market and hierarchy are at least partially determinative of each other in both directions of causation. The interior and exterior of the firm are co-determined and co-exist and at the extreme (such as in the 'make-or-buy' decision) they are coexisting and alternative methods of governing transactions. Where opportunism is absent, or it would appear the potential for opportunism is great relative to the mechanisms in place to constrain it, Network Theory and its behavioural assumption of trust rather than opportunism will aid understanding of the organisation of law firms.

Within the interior of the firm, the partnership sharing bargain can be viewed as a focal point for the interaction of partners strategies and behaviour to the extent that it is this incentive structure which essentially creates the signals/ incentives that evoke and shape partner strategies. Analysis of this mainstay of partnership organisation will be greatly enhanced using the various complementary strands of theory outlined in this chapter.

Endnotes - Chapter Three

1. These newer perspectives can be viewed as consisting most significantly of the theories of Property Rights, Agency Costs and Transactions Costs, and Network Theory To a lesser extent, the managerial and behavioural theories of the firm mark a departure from the Neoclassical theories, but can be regarded as less significant in their contribution to the discussion within this thesis.

An area where Neoclassical Theory is not particularly useful is in making a strong distinction between the firm and the market. For example, the make-or-buy decision is far more usefully discussed in the context of these newer theories See: Williamson, O.E., The Vertical Integration of Production Market Failure Considerations, American Economic Review, Vol.61, 1971, pp.112-123, Williamson, O.E., **Markets and Hierarchies: Analysis and Antitrust Implications.** New York: Free Press, 1975; Williamson, O.E., Transactions Cost Economics: The Governance of Contractual Relations, ***Journal of Law and Economics***, Vol 22 (Oct), 1979, pp 233-261; Williamson, O.E., **The Economic Institutions of Capitalism**, New York. Free Press, 1985; Grossman, S. & Hart, O., The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration, ***Journal of Political Economy***, Vol 94 (Aug), 1986, pp. 691-719 all observing the 'make or buy' decision from a transactions cost perspective. See also; Marschak, J. & Radner, R., **The Theory of Teams**. New Haven, CT. Yale University Press, 1972 for communication benefits of team organisation perspective of the 'make or buy' decision and Alchian, A. & Demsetz, H., Production, Information Costs, and Economic Organisation, ***American Economic Review***, Vol.62, 1972, pp.777-795 for technological non-separability benefits of team production view of the 'make or buy' decision. See also: Aoki, M., **The Cooperative Game**

Theory of The Firm. London: Oxford University Press, 1984 for a co-operative games perspective of the 'make or buy' decision and Jensen, M. & Meckling, W., Theory of the Firm: Managerial Behaviour, Agency Costs and Capital Structure, ***Journal of Financial Economics***, Vol.3 (Oct), 1976, pp.305-360 and Fama, E., Agency Problems and the Theory of the Firm, ***Journal of Political Economy***, Vol.88, 1980, pp.288-307 for nexus of contracts view of the 'make or buy' decision.

In Neoclassical orthodoxy, the firm being viewed as a production function negates the requirement to decide between allocating activities to the market or the firm. Dyadic contract based approaches employ a comparative analysis where the activity under scrutiny is assessed under differing contractual governing methods to examine the comparative efficacy of these contractual modes. As a result, transactions are assigned to governing modes in a discriminatory manner. The transactions cost framework employs the reasoning whereby market contracting is to be used unless it is the case that circumstances surrounding the transaction dictate that a more complex and specialised contractual governance is required. Market governance is questionable when there are high degrees of uncertainty and high levels of asset specificity and a less market oriented governance may be required to provide additional signals and incentives beyond those of the price mechanism.

2. These descriptive studies included major works such as the following; Robertson, D.H., **The Control of Industry**. rev.ed., London; Nisbet & Co., 1928.; Robinson, E.A.G., **The Structure of Competitive Industry**. London; Nisbet & Co., 1931; Marshall, A., **Industry and Trade**. London, 1919 (3rd edition 1920, reprinted 1927).

In his 1972 work 'Industrial Organisation: A Proposal for Research' in V.Fuchs, **Policy Issues and Research Opportunities in Industrial Organisation**. New York, at p.62, Coase described these studies as being 'characterised by an interest in how industry was organised in all it's richness and complexity'.

Coase, in this same work, did, however, indicate that these works did lack a theory of what actually determined the structure of industry. In the period after the publication of the descriptive studies eluded to above, economists attempted to become much more abstract and theoretical and modern theory of the firm was born. This theory of the firm is really a theory of price determination which is incapable of identifying determinants of industrial structure.

3. The inter-disciplinarity introduced by theory of the firm in more recent times has been accomplished by sensible recognition that related academic disciplines can enrich existing economic theory. This has involved theoretical input from the areas of sociology, psychology, behavioural science, administrative and management science amongst others. To a large extent, however, many economists have been slow to recognise the value of these interactions perhaps as they view them as a severe compromise to their independent scientific discipline of pure economic theory. The more fruitful contemporary theories of the firm do, however, perceive a value in cross border interaction and I view this as the way forward for theory of the firm.

4. In particular the pioneering work of Herbert Simon in the area of the process of human rationality can be seen to be of vital importance to this altered focus within theory of the firm. His concept of bounded rationality is developed primarily within his following works; **Models of Man**, John Wiley & Sons, New York, 1957; **Administrative Behaviour: A study of Decision Making Processes in Administrative Organisation.** 3rd edition, New York Free Press, New York, 1976, Rationality as a process and as a product of thought, ***American Economic Review***, Papers and Proceedings, 1978, p.1., Rational decision making in business organisations, ***American Economic Review***, Vol.69, 1979, p 493.

5. The seminal works in each of these areas are often regarded as being as follows;

Property Rights Theory: Alchian, A. and Demsetz, H., Production, Information and Economic Organisation, ***American Economic Review***, Vol. 62, December 1972; Becker, L.C., **Property Rights.** Routledge and Keegan Paul, 1977. Furubotn, E. and Pejovich, S., Property Rights and Economic Theory: A Survey of Recent Literature, ***Journal of Economic Literature***, Vol X, No 4, December 1972, p 1137; Furubotn, E. and Pejovich, S. (eds), **The Economics of Property Rights**, Ballinger, 1974; De Alessi, L., The Economics of Property Rights: A Review of the Evidence, ***Research in Law and Economics***, Vol.2, 1983, pp 1-48; Goldberg, V.P., Public Choice - Property Rights, in Samuels, W.J. (ed), **The Methodology of Economic Thought.** Transaction Books, 1980, pp 402-426; Schmid, A.A., The Economics of Property Rights: A Review Article, in Samuels, W.J. (ed), **The Methodology of Economic Thought.** Transactions Books, 1980, pp.433-442; Nutzinger, H., Property Rights: A New Paradigm in Social Science, ***Economic Analysis and Workers Management***, Vol.XXVI, 1982.

Agency (Cost) Theory: Jensen, M C. and Meckling, W H., Theory of the Firm, Managerial Behaviour, Agency Cost and Ownership Structure, ***Journal of Financial Economics***, Vol. 3, 1976, pp 301-360; Fama, E., Agency Problems and Theory of the Firm, ***Journal of Political Economy***, Vol.88, 1980, pp.288-307; Fama, E. and Jensen, M C., Separation of Ownership From Control, ***Journal of Law and Economics***, Vol.XXVI, 1983a, pp.301-326; Fama, E. and Jensen, M.C., Agency Problems and Residual Claims, ***Journal of Law and Economics***, Vol.XXVI, 1983b, pp.327-352.

Transactions Cost Theory: Williamson, O E., **Markets and Hierarchies: Analysis and Anti-Trust Implications.** Free Press, 1975; Williamson, O.E., **The Economic Institutions of Capitalism.** Free Press, 1985, Chapters 1-3, 7 & 8; Williamson, O E., Transactions Cost Economics: The Governance of Contractual Relations, ***Journal of Law and Economics***, Vol. 29, 1979, pp.549-571.

6. *Supra* Note 4.

7. See, Machlup, F., Theories of the Firm: Marginalist, Behavioural, Managerial, ***American Economic Review***, Vol.62, 1967, p.1. and Penrose, E.T., **The Theory of the Growth of the Firm**, Basil Blackwell, Oxford, 1959.

8. *Supra* Note 7.

9. *Supra* Note 2.

10. See; Coase, R.H., The Nature of The Firm, ***Economica***, Vol.IV, November 1937.

This work of Coase and, to a lesser extent, that of Commons, J.R., **Institutional Economics: It's Place in Political Economy**, New York, 1934, are accepted as providing the profound insights for and foundations to Williamson's transactions cost framework.

11. See; Loasby, B.J., **Choice, Complexity and Ignorance** Cambridge University Press, Cambridge, 1976.

12. It was this recognition by Williamson that acted as the catalyst to development of the transactions cost framework, which made it's first appearance in his 1975 work, *supra* note 5, and has been subject to subsequent refinement throughout his later works.

13. *supra* Note 10.

14. Knight, F.H., **Risk, Uncertainty and Profit.** Houghton Mifflin, Boston, 1921.

15. *supra* Note 7

16. *supra* Note 5.

17. *supra* Note 5.

18. *supra* Note 4.

19. *supra* Note 5.

20. *supra* Note 5.

21. *supra* Note 5.

22. *supra* Note 5.

23. The partnership decision employs rigorous selection mechanisms in order that the value of the human capital of the firm may be maximised. Poor performance of these partner agents of the firm will result in the market (other firms and clients) discounting the reputation/ human capital value of the firm.

24. The incidence of residual risk bearing can be altered when the organisational mode changes, as would most probably be the case in situations where alternative practising arrangements for lawyers were permitted. Such arrangements (currently under discussion in the UK) would have the effect of markedly changing the levels of hierarchy within the firm and the relationships existing between different levels therein.

25. *supra* Note 5.

26. *supra* Note 10.

27. *supra* Note 10.

28. *supra* Note 4.

29. See, for example, Arrow, K.J., **Limits of Organisation**. New York, 1974. for an example of the influence of his work on that of Williamson.

The analytical inter-disciplinarity favoured by Williamson is evident from his work from his use of the insights of Simon, whose analysis is firmly situated within a Carnegie School methodology with strong influences from the likes of Chester Barnard.

30. See; Simon, H.A., **Models of Man.** John Wiley & Sons, Inc., N.Y., 1957.

The most popular and commonly cited description of the principle of bounded rationality is found on p.198 of this work. I quote, 'The capacity of the human mind for formulating and solving complex problems is very small when compared with the size of the problems whose solution is required for objectively rational behaviour in the real world - or even a reasonable approximation to such objective rationality'.

31. *supra* Note 5.

32. See; Macneil, I.R., Economic analysis of contractual relations, Chapter 3 in Burrows, P. and Veljanovski, C.G., (eds), **The Economic Approach to Law.** Butterworth, 1981.

33. *supra* Note 4.

34. See; Dugger, W M., The Transactions Cost Analysis of Oliver E. Williamson: A New Synthesis?, ***Journal of Economic Issues***, Vol.XVII(1), 1983, pp.95-114, for a 'neo-institutionalist (not new institutionalist) critique of Williamson's work. Neo-institutionalists firmly reject the encroachment of Neoclassical maximisation into the newer theories of the firm.

For an introduction to the important works in the area of Network Theory see; Johanson, J. and Mattsson, L-G, Interorganisational Relations in Industrial Systems: A Network Approach Compared with the Transactions Cost Approach, ***International Studies of Management and Organisation***, Vol.XVII, No 1, pp.34-48; Mattsson, L-G, Management of Strategic Change in a 'Markets-as-Networks' Perspective, Chapter 7 in Pettigrew, A. (ed), **The Management of Strategic Change.** Blackwell, 1987; Jarillo, J.C., On Strategic Networks, ***Strategic Management Journal***, Vol.9, 1988, pp.31-41; Thorelli, H.B., Networks: Between Markets and Hierarchies, ***Strategic Management Journal***, Vol.7, 1986, pp.37-51.

35. See; Goldberg, V.P., Towards an Expanded Theory of Contract, ***Journal of Economic Issues***, Vol.10, No.1, March 1976; Production Functions, Transactions Costs and New Institutionalism, in Feiwel, G. (ed), **Issues in Contemporary Microeconomics and Welfare.** Macmillan, 1985. See also; Goldberg, V.C., A Relational Exchange Perspective on the Employment Relationship, in Stephen, F.H (ed), **Firms, Organisation and Labour: Approaches to the Economics of Work Organisation.** Macmillan, 1984, pp.127-145.

36. *supra* Note 5.

37. See; Buchanan, J.M., **The Limits of Liberty: Between Anarchy and Leviathan.** University of Chicago Press, 1975.

38. An example of this is the domain of contestability theory, where there are zero sunk costs and the market has no barriers to entry, facilitating ease of entry for other

firms. Zero sunk costs implies that asset specificity plays no role, and that hit and run entry is viable. Where asset specificity does exist, the situation is likely to be very different in terms of behaviour and responses of individuals and firms. The comparative static responses will thus be different between Neoclassical analysis (which ignores asset specificity) and, for instance, transactions cost analysis which does recognise the importance of asset specificity.

39. If this was not the case then the probability distribution would not sum to unity. Unforeseen, yet possible, outcomes would require to be assigned some non-zero probability.

40. It is worth noting at this juncture that, throughout his work, Herbert Simon rejects the use of probability in behavioural theory and expresses a similar dislike of the use of game theory concepts.

41. See; Thorelli (1986) *supra* Note 34.

42. See; Note 34 for an introduction to some of the notable works in this area of theory.

43. *supra* Note 34.

44. *supra* Note 10.

45. *supra* Note 34.

46. See; Williamson (1985) *supra* Note 5.

47. This does not, however, preclude the existence of competition between firms within the network and this is in fact held to be a characteristic feature of network organisation. The network therefore consists of a nexus of simultaneously competitive and cooperative relationships.

48. Agency theorists take a similar line here by arguing that long term contracts are easier to enforce than spot contracts. By emphasising the long run, a contract can be converted from a situation of zero sum game to non-zero sum game, where the parties become more interdependent. This can be brought about by enhancing alignment of incentives through monitoring and bonding activities.

49. An interesting parallel can be drawn here with the law firm partnership. The partnership is a network exchange between lawyers for human capital that is stable, yet

is subject to frequent changes to its membership as existing partners leave the firm or die, new partners join and existing ones are repositioned within the partnership *sharing bargain.*

50. See; Hirschman, A.O., **Exit, Voice and Loyalty**. Harvard University Press, Cambridge, MA, 1970. The continuance of relationships in the face of problems is ensured when the problem is resolved by negotiation (voice) rather than by walking away from the relationship (exit), which naturally implies that any future benefits from that relationship are lost at the point of termination.

51. In the situation of a cartel, there is the likely problem of opportunism by one or more of the parties to the 'agreement' ie. the classic free rider problem. This is where it is perceived by a member of the cartel that if he should cheat on the cartel's agreement, he could appropriate a bigger than agreed slice of the pie and this would go unnoticed by the others. The likelihood of this occurring in cartel arrangements is high as trust between cartel members is poor and consequently cartel operations tend to be short lived and inherently unstable.

52. In this respect the concept of a clan/ club and a network are broadly consistent. See; Ouchi, W.G., Markets, Bureaucracies and Clans, *Administrative Science Quarterly*, Vol.22, 1980, pp.129-141, for an enlightening analysis of the importance of shared/ common values for individuals and the effect this has for intra-firm authority relationships.

Clans are characterised by two major features;

1. High levels of performance ambiguity and,
2. Low levels of opportunism.

Socialisation is an important characteristic that facilitates the above and this is brought about by high levels of inclusion which may require or display a high degree of discipline (immersion of *individual into whole-utopianism*) and teamwork.

Normative requirements for clans are:

1. Reciprocity
2. Legitimate authority
3. Common values and beliefs.

There is a strong possibility of a requirement for an "apprenticeship period" to be served before progress is made in the clan. This system is likely to perform a function that reduces the scope for opportunistic behaviour and instills communality of beliefs by a mentor/ protege relationship.

Traditions can be seen as *implicit, rather than explicit,* rules governing behaviour. These 'rules' are usually combined with a fairly fluid and unspecified penal system. This renders specific rule bending strategies unviable.

In the context of clan relationships, networks can be seen as broadly similar as they are a stable pattern of contracts, mainly informal and unwritten, that exist between persons at an individual level, or between aggregations of individuals at the firm level.

53. At the level of the individual law firm, viewed as a more micro level network, the collective body of partners perform the hub role. In larger firms, a partnership committee/ board may perform the hub role.

54. Although founded very much in the past, it should be remembered that trust is a very future orientated concept, whereas opportunism is typically present orientated.

55. *supra* Note 34. See also; Von Hippel, E., Cooperation Between Rivals· Informal Know-how Trading, ***Research Policy Journal***, Vol.16, 1987, pp.291-302, and Ouchi, W G. (1980) *supra* Note 52., for discussion in this area.

56. In this regard, it would be interesting to undertake a comparative study of the relative efficiencies of different types of transaction mediation in terms of resources used to stabilise different forms of organisation. This would, naturally, be problematic to the extent that it would be difficult to identify and quantify these resources and any comparative assessment would subsequently become qualitative rather than quantitative. Cooperative agreements could be expected to be less wasteful than competitive ones but they may not be as efficient in other directions. The resources consumed in stabilising the governance mode can be regarded as transactions costs.

57. See; Thorelli (1986), *supra* Note 34.

58. See; Thorelli, H.B , Organisational Theory· an Ecological View, Academy of Management Proceedings, December 1967, 1968, pp 66-84.

59. See, Thorelli (1986), *supra* Note 34.

60. See; Thorelli (1986), *supra* Note 34.

61. Network theory could be useful in examining franchise operations and indeed any situation where there is use of hostages to support exchange. Similarly, it may provide a good basis for analysing cartel operations and collusion. In the area of international ties/ joint ventures/ collaborative agreements or arrangements and the like, it may also provide a useful analytical framework. It may aid rigorous evaluation of situations and provide novel solutions to certain situations that are contrary to the public interest. Network theory may indicate solutions to problems that are more usually solved through Vertical Integration or Diversification (ie. network organisation could be used as an instrument to reach new clients and/ or countries). Network organisation could provide stimulus to economic growth where stability is ensured through effective network management. They could be used by firms to retain control of their core competencies/ differential advantages in certain fields of activity and hence, permit firms to become more in control of their future and strategies. Network theory copes much better than most, if not all, of the newer theories in terms of capturing dynamics of firm organisation and the concepts of strategy formulation.

-Chapter Four-

Important issues relating to organisational relationships between lawyers and clients:

Introduction:

Previous chapters of this thesis have made it apparent that a major problem arising in the operation and organisation of the legal profession is the imbalance of power which exists between the profession and those members of society who consume its services. This asymmetry in power vastly favours the profession and is a prime motivation in regulating the profession in order that attempts to abuse this power are pre-empted. At a more micro level this imbalance of power is mirrored in the typical client/ lawyer relationship. This chapter seeks to disclose the true nature of this relationship and discuss some of the implications and problems of supplying professional legal services to consumers in the presence of extreme information asymmetry.

Section One: The Nature of Legal Business and the Lawyer/ Client Relationship.

1.1 The nature of legal business.....creation of an agency relationship:

The nature of legal business is such-that for the vast majority of consumers it could be expected that they will fairly infrequently require the services of a lawyer. Consequently, after initial contact has been made with a lawyer, the client will typically regard the chosen lawyer as being his/ her lawyer. When the requirement to use a lawyer in future should arise, a client will tend to return to the initial lawyer, and this will hold true even where the period between initial contact and any subsequent requirement for legal services is a lengthy (even many years).

The legal services market has certain characteristics which determine the dispersion of information pertaining to legal services in that market. The typical legal service is most usually characterised by a high degree of specialisation and complexity (at least from the clients point of view). The immediate result is that a wedge of ignorance is driven between client and practitioner. In transactions cost terms, Williamson would describe this as asymmetric information being impacted in the lawyer within the client/ lawyer relationship [1]. The significant consequence of this extreme information asymmetry is that a fiduciary relationship, characterised by a high degree of trust between client and lawyer, is created.

The client/ lawyer relationship is therefore essentially an agency relationship where the principal (the client) hires the lawyer (his agent) for the purposes of resolving some specific legal difficulty or problem [2]. Under this agency relationship, the agent agrees to act at all times in the best interests of the principal. In order for an agency relationship to be interesting, it is alleged by Ricketts (1987), that two important features are required to hold.

Firstly, a conflict of interests between agent and principal must exist and, secondly, an asymmetry in information available to the principal and agent must exist [3].

It is immediately obvious that if no conflict of interest characterises the agency relationship, the existence of asymmetric information between the two contracting parties ceases to be a problem. The lawyer would perceive no incentive/ advantage in recommending a course of action that did anything other than accord completely with the interests of the client. Similarly, if there is a situation of symmetric information between client and lawyer, the potential conflict of interest ceases to be significant, as the client would have the ability to immediately detect instances of opportunism against him by the lawyer.

Within the client/ lawyer relationship it is characteristically the case that a significant level of information asymmetry and potential for conflict of interest are both present. The problem for the client (the weak party) is one of aligning the incentives facing the lawyer with his own so that by maximising his own personal payoff, the lawyer simultaneously maximises the clients payoff [4].

The typical agency relationship observed to exist between client and lawyer can be rationalised in terms of it being to the benefit of both parties to first establish and subsequently maintain a long term relationship/ contract [5]. In such a relational contract, the individual contracts parties enter from time to time are important, but past transactions and the stream of potential future ones are also important in determining the value of the relationship. Behavioural influences in this type of contract structure are of central importance, where the value of the relationship to the two parties is identifiable. Social ties exist between the parties and the relationship is cloaked in trust and characterised by mutual solidarity between the parties [6].

1.2 Exploring the information asymmetry between client and lawyer:

The market for legal services is, therefore, characterised by information asymmetry between buyer and seller - the service provider possesses much information regarding the product for sale and the customer possesses zero, or at best very little, regarding the final product [7]. As a result, the consumer of legal services faces search difficulties, as the information required to make a rational choice between solicitors is difficult to come by, and costly to obtain.

(I) The problem of initial selection - determination of quality pre-purchase:

Initially, the individual consumer faces a significant problem of information deficiency which severely compromises his ability to make a rational choice between competing law firms in the market. The traditional market signal, often relied on by the consumer when making such

a choice in relation to many other purchases, that being price, is typically absent in the case of most legal services. Even where consumers do receive price signals, these are not particularly useful signals for the consumer, as consumers typically do not have the experience of repeat purchase to establish how much they feel they should be paying for the service required [8].

In terms of the client's ability to evaluate quality ex-ante consumption, the quality of the legal service required is largely undetectable, except perhaps where the client has a unusually high degree of sophistication. For the majority of consumers, quality evaluation ex-post consumption may not even be viable. A consequence of infrequent usage of legal services by the vast majority of consumers, is that learning by experience is not applicable in selection of providers of legal services. Consumer awareness/ perception of quality is not subject to a learning process through repeat consumption.

Clients in established relationships could be expected to be typically relatively passive with a low degree of participation in contracts. As a result, they are unlikely to learn significant skills which would better enable them to evaluate the quality of the services they were receiving post-purchase. Consequently, clients in existing relationships may enjoy little or no sophistication advantage, when compared with individuals in the market attempting to evaluate reputation effects and choose a 'good' lawyer pre-purchase.

(II) The problem of assessing contractual performance - determination of quality post-purchase:

Related to the above problem of determining quality pre-purchase, is the additional post-purchase information deficiency which confronts the typical consumer of legal services. This is characterised by an inability of the typical client to recognise and evaluate the quality of the services provided, even after they have been rendered by the firm.

If it is accepted that the information asymmetry described above does exist, and that quality evaluation is likely to be a problem, both in the pre and post-purchase stages for the typical consumer, then the scenario for the client appears to be bleak. The client appears a prime target for opportunism by the firm.

As a consequence of the absence of a meaningful price signal in the market for legal services, competition between solicitors could perhaps be expected to be based on quality rather than price (remembering that it is not possible for consumers to evaluate relative prices of legal services as they are too heterogeneous to compare) [9]. Even in the case where firms competed by service quality, the consumer would still face difficulties, however, since;

1. It would be difficult for firms to demonstrate their products were of differentiable quality, since consumers do not tend to be repeat purchasers of legal services and,

2. Quality competition does not solve the consumers' problem since quality information in both pre and post-purchase states is incapable of being rationally assessed [10].

The absence of price as a signal, paired with the inability of the consumer to evaluate quality both pre and post-purchase, results in the consumer relying to a greater extent on his individual perception of quality and evaluation of reputation. A reliance on factors other than price results in a quicker exhaustion of the individual's bounds of rationality [11].

The nature and source of the information asymmetry and deficiencies that typically exist in the client/ lawyer relationship have been outlined, and the implication of this for the supply of professional legal services disclosed. Attention now turns to the instances of opportunism the agent could attempt to inflict upon the 'ignorant' principal, given the conditions surrounding the relationship [12].

1.3 Potential for agent opportunism against the principal:

For the possibility of opportunism to arise, it is obviously necessary that the principal and agent are actually in contract with each other. The balance of power in this contract naturally swings in favour of the lawyer, apparently leaving the client an easy target for opportunism. The lawyer, in essence, has powerful control over the client relationship due to information impactedness described above. This results in the client being in a weak position to rationally challenge the lawyer's diagnosis of what any transaction involves, or which path it should subsequently follow. The client finds himself in the vulnerable position of not knowing whether work the solicitor claims needs to be done actually is actually required, or whether it is simply an attempt to garner additional fees. This vulnerability resulting from information deficiency on the part of the client, induces high levels of uncertainty in the client.

Legal services are complex by their very nature, and this creates potential for the lawyer to act in an opportunistic manner against the client[13]. The extent of this potential is, however, conditional to some extent on the degree of sophistication which attends the client. Commercial clients could perhaps be expected to be typically more sophisticated than private individuals and, therefore, less easy targets for opportunistic behaviour by the law firm. In certain cases, however, the potential to act opportunistically may not differ greatly between client types (where sophistication levels are broadly similar), but the chances of, and more significantly the consequences of, being caught, could differ greatly [14].

There are basically two closely related and possibly coexisting main ways in which the lawyer can opportunistically act against the client. Firstly, the firm can act opportunistically in terms of the quantity of work which it claims is required and, secondly, the firm can act opportunistically in terms of the quality of the work provided. These constitute quantity/ price adjustments and quality adjustments, respectively, within the implicit contractual specification between principal and agent.

It would be relatively easy for the solicitor to determine at an early stage after initial contact with a client, whether that client would be an ideal subject for inducing additional fees. The lawyer could construct a stream of future transactions around this by peddling the language of the law and coercing the experience and reality of the client to fit particular legal definitions, thereby creating a perceived need in the client and, hence, work for the lawyer [15].

The foundation of the client/ lawyer relationship, is based on the individual placing his trust in the lawyer as a truthful and economic translator of legal problems into plain English. In this role, sociologists view the professions as a major mechanism of social control [16].

It is not unreasonable to suggest that clients most usually announce their needs in simple terms to the solicitor and set a basic objective to be attained by the lawyer. This requires that the individual actually knows what it is he wants, and afterwards that he can ascertain he has obtained it. This may be patently unrealistic for many classes of consumer. Hence, so long as the solicitor achieves the 'objective' set down by the consumer, within that individuals time and cost constraints, the solicitor is relatively free to choose the means by which he reaches that end. To that extent, abuse of the client's ignorance of untranslated law is potentially possible and may go largely undetected by the client [17].

The lawyer can act opportunistically against the client by initially informing the client that the work involved is much more complicated than it actually is. In such a situation the information deficiency attending the client can render him an easy target for the lawyer to cloak the work unnecessarily in legalistic language and hereby justify a prolonged duration of work with correspondingly higher fees. This scenario may be easy for the solicitor to precipitate by virtue of the fact that, although the relationship is relational and long term, many transactions are typically one-off unrepeated transactions for the client [18]. Overall, however, high levels of mutual trust and respect are likely to characterise the relationship between client and firm, with few instances of opportunistic behaviour against clients by firms.

Accepting the typical information asymmetry that attends that client/ lawyer relationship, it is also apparent that it is potentially possible for solicitors to provide clients with low quality services and charge unjustifiably high fees without the client knowing of this opportunistic

behaviour.

It is apparent that there are vast difficulties in evaluation of the quality of legal services for different classes of consumers in the ex-ante consumption stage and also often in the ex-post consumption stage [19].

The perception of quality of legal services by the consumer is a real problem for consumers. It is possible for the lawyer to advise clients what it is reasonable for them to expect in terms of service and results, thereby forming the consumer's perceptions or expectations regarding quality. In this scenario, it is quite possible for the law firm to consistently set goals which will please the consumer but at the same time cause the firm no great hardship in achieving [20].

The firm could ask consumers if they were satisfied with the services they have received post-completion of the service. This non-independent test would simply judge the service quality on criteria that have been set by the lawyer himself. This activity could itself be perceived as being demonstrative of good quality service. Additionally, by virtue of the fact that legal services are an experience good, individual perceptions as to what constitutes quality could be expected to vary widely across consumers. The upshot of all of this is that it is possible for the law firm to sustain production of services that are not consistently of a uniform quality without being penalised by the market for low quality. So long as the firm does not exploit any consumer to such an extent that consumer becomes aware that he has been exploited, the firm's reputation will not be discounted either by that consumer, or subsequently by other potential customers.

In situations where services are provided and the consumer of those services relies on expert advice because of his typically low level of knowledge regarding those services, there is a potential problem of Supplier Induced Demand (SID) [21]. This is the formal term to describe the situation discussed above where consumers can be talked into demanding services that they perhaps does not actually require. This problem arises due to consumer reliance on professional judgement in the face of being disadvantaged enormously in determining whether the correct advice is being given. As a result, the trusting consumer is at the mercy of the practitioner who can talk the consumer into perceiving a need for something that is not required.

This concept has obvious applicability in legal services, given the information asymmetry existing between lawyer and client. Determining the extent of this problem (assuming it is likely to exist to some extent in legal services) is outwith the ambit of this study but worth mentioning nevertheless. It may be the case that any SID problem that does exist could be expected to become greater with MDP where cross-selling services would be an imperative, or where competitive pressures are increased through greater liberalisation.

Legal services are viewed in the UK as a basic right and public policy is directed at protecting this right, especially for those who are at greatest potential risk from abuse by unscrupulous professionals. A prime example of a potential abuse by providers of legal services would be attempting to supplier induce demand (SID). This could be expected to be more of a potential problem with less sophisticated clients. The legal profession provides the ideal setting for SID to occur since it operates in an environment of self-regulation and has almost a free hand to monopoly price services via self-regulatory enforcement. It is evident from this and from the general discussion of potential opportunism by the agent against the principal above, that the consumer of legal services would appear to be in a potentially risky situation in respect of being vulnerable to opportunism.

1.4 Constraints on the agent acting opportunistically against the principal - Counteracting institutions to opportunism:

In the analysis above, the main focus of attention has been on the potential problems of opportunism by the lawyer agent against the client principal. From the previous chapter it will be recalled that in many of the newer theories of the firm there is a tendency to examine situations where the focus is on potential problems of opportunism that could arise as a consequence of the manner in which the matter being observed is organised. As a result, analysis tends to focus on ways in which opportunism can be safeguarded against, reduced or eliminated. This often overlooks the fact that in many situations, there is imbalance in power between contracting parties, exposing potential for opportunism, and yet there is little opportunistic behaviour between the parties. The importance of trust in such contractual exchanges is vital, and attention will now be diverted in this chapter to an examination of the trust surrounding the client/ solicitor relationship.

(I) The role of the Law Societies as a trust device:

The existence of the respective Law Societies should encourage a feeling of identity, colleague loyalty and shared values in the lawyer. The desire for such an institution to exist is founded primarily on the premise that some signal of formal omni-competence will be the device that will best generate public trust [22]. The importance of the existence of this trust cannot be over-emphasised, both in the wider context of the functioning of the profession in society, and in the narrower context of the lawyer/ client relationship.

The trust creating autonomy granted to the legal profession by the State, and the public as consumers, is borne out of true regard for the Profession's expertise and expected altruism [23]. Since the nature of the final output of the legal profession is an intangible service, the role of professional discretion recognised as being vast and legitimised. Decisions made by lawyers

are made on the basis of their collected professional knowledge [in theory no matter which lawyer one chose to consult, a similar (if not identical) legal opinion would be offered]. The resultant power of the lawyer could be used to very substantial effect in self-interested directions, but at all times it is expected that the interests of clients he chooses to represent are the over-arching concern of the lawyer [24].

(II) Mutual monitoring and self-regulation as a trust device:

As a result of the nature of professional services, it is contended that it is exclusively only other lawyers within that profession who possess the judgement and ability to apportion to other members, labels of incompetence. It is self evident that the ordinary man in the street cannot possibly be sufficiently informed to make judgements that abstract matters of incompetence from situations that are essentially quirks of the inevitable workings of the judicial system [25]. In view of this, self-regulation appears to be a rational organisational mechanism.

Within any system of self-regulation there is an inbuilt tendency for bias to enter as a consequence of vested interest and goals of self-preservation. The Law Societies, and other members of the profession, have a vested interest in attempting to cloak embarrassing acts of incompetence by its members, since (if exposed) these could seriously undermine the creditability of the profession. On the other hand, the legal profession may paradoxically wish to expose all acts of professional incompetence to demonstrate to the general public that high standards are enforced and that self-regulation can be relied upon to operate effectively and arrest mal-practice. In this way the profession would attempt to enhance consumer confidence by signalling that incompetent practitioners will be exposed and excluded.

It is argued, not surprisingly most often by the legal profession itself, that its complete autonomy is an essential requirement in order that its members can carry out their legal functions properly. In this sense, monopoly power is, therefore, a necessary and inevitable consequence of this autonomy, with self-regulation ensuring freedom from the shackles of Government influence. Strong ethical and moral standards are anticipated to serve to self-constrain any abuse of this extensive social privilege. These issues essentially form part of the wider problem of determining the most efficient and effective manner in which to socially control expertise within the economy [26].

(III) Professional socialisation and relational contracting as a trust device:

It could be expected that the professions would, by virtue of their monopoly position and the fact that they play a major role in stabilising society, have almost unlimited bargaining power. It is, however, the case that the professions are entrusted and expected to limit the use

of their power, where stringent professional ethics/ morals in combination with rigorous selection and training procedures essentially render abuse of this power an unviable option. In this context, the professions are in relationships with society characterised by features found in relational contracting arrangements [27]. The nature and extent of the socialisation process of those within the legal profession has been discussed at great length earlier in this thesis and therefore requires no further discussion here. It is, however, worth stressing in the context of the current section the reliance placed in this process to successfully create high levels of trust and an atmosphere in which opportunism is generally accepted to be an unacceptable behavioural trait.

It will be recalled from earlier discussion that the control of experts in society is broadly achieved by a combination of three main elements; (i) Consumers, (ii) Third party organisations (including Government) and, (iii) Self-regulation.

It is anticipated that these elements in combination will ensure that consumers are provided with quality legal services, and will not be subjected to abuse of monopoly power by those who supply these services [28]. In this sense the information asymmetry, creating the potential for opportunism, should not become a problem - it should not be irrational for the client to assume that the lawyer will act in his best interests. This should, thereby remove the conflict of interests problem and thus remove one interesting and crucial dimension of the principal/ agent problem [29].

The practice rules of the respective Law Societies can be regarded as an attempt to encourage practitioners to maintain some specified degree of legal competence. They may, however, do more to encourage practitioners to minimise deviance from legal competence than they do to encourage practitioners to strive for higher levels of legal competence. This could point towards a general desire by lawyers to seek to maintain a minimum acceptable standard of service throughout the profession, rather than strive to continually enhance quality in legal services. This scenario, however, would be at odds with the self-respect and quest for professional excellence traits which should have been invested in members of the profession throughout the continual and ongoing socialisation process of the profession. The socialisation process is more consistent with the scenario where practitioners continually strive to create and sustain and enhance reputation.

In long term relationships of trust, therefore, it could be expected that opportunism on the part of the lawyer would be avoided through a desire to maximise the possibility of the relationship continuing. This behaviour would also be more likely to create referrals from satisfied existing clients [30].

It is thus evidently in the interests of the law firm to attempt to maximise its reputation, in the

eyes of its existing and prospective clients, by attempting to maximise its service quality [31]. By doing so, it is anticipated that relational contracts will be established and sustained, with others developing as a result of referrals from other satisfied clients already in established relational contracts. Although the typical client/ lawyer relationship is characterised as a relational contract, the frequency of contact between the parties can be expected to vary quite widely within that relation. Private individuals are perhaps less likely to consult lawyers as often as commercial firms but when they do, it likely that they will consult the lawyer with whom they have already established a contractual relationship.

The concepts of information asymmetry and reputation effects are closely related. If the consumer is willing to place trust in reputation, then information impactedness in the opposite contracting party will not act as a disincentive to the consumer to transact [32]. It has been argued above that the nature of the legal service is such that it is an "experience good", in so far as that pre-purchase it is impossible to determine the quality of the product by inspection. The reliance, therefore, of the consumer on reputation effects reduces would be high search costs to the consumer [33]. A perfect market characterised by competition based on quality and reputation is likely to present low search costs to the consumer if he is endowed with an ability to perceive quality/ good reputation.

The potential inability of the consumer to rationally perceive and evaluate reputation is but one of the imperfections of the market in question here. The producer has the ability to attempt to signal high quality levels through higher than normal prices (as a reputation premium). The consumer may then perceive high price as equating with high degrees of quality throughout the market. Some instances of high price are just as likely to reflect monopoly profits and a normal (or even low) standards of quality [34].

It could be expected that in the longer run, in a market where consumers could effectively perceive and evaluate reputation, those systematically charging fees above the value of their reputation would be discovered and consumers would discount the value of such firms reputations. The extent to which this effect would discipline the market is uncertain and is conditional on the ability of consumers to perceive and evaluate reputation effectively and efficiently. It is true to say nevertheless that the producer of high quality services has a higher opportunity cost of ruining his reputation and hence, faces a stronger incentive to maintain quality.

Now that a discussion of information deficiency has been presented above, attention will now turn to sources of information that are available to clients and potential consumers of legal services. What follows, therefore, is a discussion of how reliable these sources are, and whether they actually constitute useful information to the extent that they facilitate consumers' decisions concerning legal services.

1.5 Sources of information consumers typically rely upon in markets for legal services:

It has been demonstrated above that the consumer of legal services typically faces two major information problems in relation to legal services. Firstly, there is a lack of information upon which to base any decision regarding which law firm to employ for the required service. Secondly, there is the problem of evaluation of the quality of service provided.

Where economic agents face a deficiency of information regarding the set of future contingencies they will face, decisions must still be made regardless of the deficiency. This is essentially a situation where economic agents can be regarded as 'Boundedly Rational' where it is not possible for such agents to make hyper-rational decisions at all times[35].

These legal service characteristics combine to render the typical consumer of legal services deficient of information, thereby increasing uncertainty and exhausting quickly the bounds of that economic agent's rationality. There are, however, several sources of information available to the consumer of legal services. Hudec and Trebilcock (1982) identify seven main information sources available to the consumer of legal services [36];

(I) Sources of client information in legal services:

1. Personal experiences gained from general knowledge or previous personal consumption of legal services.
2. Recommendations/ referrals from family and friends etc.
3. Contacts with lawyers in a social context.
4. Initial consultations with a lawyer for prospective business.
5. Recommendations from external agencies eg. legal aid etc.
6. Yellow Pages/ phone book.
7. Public legal education and Law Society/ institutional advertising.

These sources of information to the consumer are subject to varying degrees of evaluation bias and accuracy. They can, however, play a considerable role in shaping the consumer preferences and perceptions regarding quality and expected quality of service.

The success of lawyer advertising could be expected to be determined by the extent to which consumers would relate choices they made to this source of information in relation to other sources. This rests, of course, on the nature of the client's decision making process and perceptions of information received. Information concerning lawyers can be expected to be subject to varying degrees of bias. Depending on client perceptions, such information could range from being completely impartial/ disinterested to being entirely self-benefitting,

depending on information type.

The consumers choice decision in legal services is consequently likely to be based on a number of factors relating to personal knowledge, reputation and advertising. Rarely will such a decision be based purely on advertising as the sole source of product and price information.

For informed decision making to occur, the client must have a degree of personal knowledge which requires familiarity with the services being provided by a number of lawyers. Due to high time and monetary search costs of obtaining such an information set, this is not available to the client. The result is a general low level of client sophistication and a characteristic deficiency of personal knowledge at the moment of decision making.

A greater emphasis is, therefore, likely to be placed on reputation effects since the consumer will expect reasonably accurate and reliable information to be given to him by family, friends and personal associates. This has the effect of, to a large extent, avoiding search costs by the consumer if he can rely on such 'second hand' information and trust its reliability.

This type of information does suffer from some inherent faults;

1. Individual perceptions, evaluations, opinions etc. are likely to be different and perhaps even conflicting/ contradictory between individuals.
2. There is also the problem that the experience of one individual may have been unrepresentative of the true general underlying quality of the firm's services. A good reference may be given without proper cause and based on an unrepresentative 'exception' rather 'the rule'.
3. The person offering the information is often unable to ascertain the quality of the service post consumption. This is in relation to;
    a) other work done by that firm of similar type,
    b) work done by that firm in other fields and,
    c) similar work done by other competing firms.

It is rational for the client to attempt to verify and confirm reputation if this is possible, in order to increase the completeness and reliability of the opinions of the advisors. The only practical way of doing this is either by personal consumption, or by increasing the sample of advisors. Increasing the sample of advisors involves the individual consuming resources through costly search activities and entering multiple non-costless transactions. Both of these options also remain subject to problems of the typical consumer's inability to rationally evaluate legal service quality either pre or post-consumption.

Where there is deficient access to legal services for a class of consumer, there will be still

fewer sources of reputation information. Verification and confirmation of reputation information, although perhaps an even more necessary requirement in such a situation, will be very difficult or even impossible.

It is true to say that lawyers may get a fair proportion of their business through social intercourse and networking, for instance, at the golf course etc. This suggests that the clients choice process is heavily influenced by inter-business networks, where the client does not really make his own choice at the end of the day in any event. The nature of such relationships are very difficult (or impossible) to handle in terms of conventional economic theory. It will be recalled from the previous chapter that even more modern theory of organisations (excepting perhaps Network Theory) offers little in addition in understanding these types of relationships [37].

The bottom line of the information deficiency problem is that only other lawyers are really sophisticated enough in relation to legal services to be able to rationally evaluate real quality of legal services. Due to low degrees of consumer sophistication and lack of knowledge of how to choose a "good" lawyer, paradoxically the best person to choose a good lawyer may perhaps be another lawyer.

Increases in firm size could be construed as demonstrating reputation reward by consumers and as a result, consumers could be fooled into equating size with reputation. In the case of law firms, the Law Society is essentially the quality signal that the consumer can rely on. The Law Society basically franchises out its reputation to firms to create professional omni-competence. At its most simple level, it could be expected that all the consumer has to do is to make sure the law firm is licensed by the Law Society to practice. Given this is a requirement for lawful practice, the firm is always likely to be franchised with Law Society practising authority. In theory, if the firm is a Law Society licensed firm, then it can be trusted by the consumer, and no matter which firm the consumer goes to he should receive legal services of a sufficient, if not uniform, quality. This perfect ideal situation is unlikely to fully exist, however, and in reality there will be a wide dispersion of price and quality in legal services, further complicated by the fact that consumer perceptions are far from being systematically correct or completely rationally based.

One of the problems the profession, consumers and Government must face is how to provide consumers with additional and more useful information - this may have the desired effect of reducing the information asymmetry. It could be argued that educating people with a basic understanding of the operations of the legal system could achieve more in the direction of addressing areas of unmet need in legal services than could any reorganisation. This would take the guise of some form of education/ public information service which would enhance consumer awareness of what the functions of the legal profession are, and how can they best

be utilised by the consumer.

1.6 Typical objectives of the consumer of legal services:

The consumer of legal services is likely to seek low cost, high quality and quickly executed legal services. Relative ease of access, low search costs and a desire to become immersed in a long term personal 'family lawyer' type of client/ lawyer relationship are likely to be desirable features the relationship between himself and the lawyer [38].

In many instances the consumer may actually be relatively ignorant of who actually supplies the service or from which form of organisation the service is rendered. This lack of knowledge may also be coupled with relative indifference as to who supplies the service, or from which organisational form the service is rendered [39].

The consumer's perception of quality in legal services is an important factor, as firms must attempt to satisfy which ever aspects of the service consumer perceive as indicating quality. These perceptions can actually bear little or no resemblance to what the lawyer would regard as quality in legal services. Quality perception and its relation to actual quality in legal services is very important in this respect. The law firm need only appeal to perceived quality, even if this is not consistent with real quality. In this analysis, the bottom line is that what constitutes quality is simply a subjective individual perception and is, therefore, impossible to - measure or identify with any great precision.

Section Two: Advertising in the context of the law firm.

Introduction:

It is useful to examine the role of advertising in legal services in view of the information deficiency which has been the focus of the earlier sections of this chapter[40]. Advertising is expected to play an informational role, conveying both price and non-price information to consumers of a product or service. In this respect, the potential role played by advertising in legal services in terms of reducing information asymmetry is of central importance. This role of advertising will be the focus of this section, where it is intended that a simple discussion of some of the issues relating to advertising in its information providing role will be discussed. In doing so, discussion will largely eschew many of the regulatory issues and mention only briefly many associated advantages and disadvantages of legal service advertising [41].

As a precursor to discussing law firm advertising it is advantageous to identify two main types of law firm transaction;

1. Those capable of being standardised and,
2. Those incapable of being standardised.

The existence of complexity in legal work need not necessarily require individualised services, as complex services can be subject to routinised processes and have large component elements of standardisation. The risk of contingent circumstances that could adversely affect the client in the transaction may be more strongly determinative of the degree to which standardisation can be introduced in transactions or not.

2.1 The role of price advertising in legal services:

It is anticipated that the introduction of price advertising in legal services would have the effect of stimulating increased price based competition, thus leading to lower prices to the consumer. As a result, abolition of bans on price advertising by solicitors could be expected to redistribute income from solicitors to consumers via lower prices and lower profits. Any statement of the desirability of such a redistribution naturally involves a value judgement as to the relative deservingness of each side and thus subjective determination of whether this is a benefit or cost of the introduction of price advertising. This aside, it is almost certain that unrestricted price advertising will enhance economic welfare of many consumers, firstly, since the market for legal services will function more efficiently by guaranteeing wider access to legal services for many previously extra-marginal consumers and, secondly, by way of firms improving their productive efficiency and innovativeness [42].

(I) Advantages of price advertising in legal services:

Trebilcock (1987) identifies two potential benefits of price advertising in legal services [43]. These benefits are alleged to be improved consumer access [44] and innovation in production [45]. The firm, however, is faced with the problem that there are few elements of standardisation in legal services. It is very difficult, therefore, to price advertise meaningfully since consumers will be unable to compare like with like [46]. Individual client demands are also characteristically inconsistent and, therefore, restriction of productive processes via standardisation is often not appropriate or even possible. For many consumers, while being an important factor, price may not be the single most important factor in selecting a lawyer.

Price advertising may have a likelihood of success in reducing prices where services are such that they are amenable to some form of standardisation. This has evidently been the case for conveyancing services in England and Wales in recent years [47]. It is anticipated that the empirical study will indicate those services areas (if any) in which standardisation can, or does, take place.

Price advertising can be regarded largely as an unattractive concept to the legal profession since, due to the fact that quantity demanded of most legal services is most likely relatively price elastic, price reductions are unlikely to generate levels of additional demand and revenue necessary to offset the cost of advertising and the effect of price reductions on revenue.

(II) Criticisms of price advertising in legal services:

Trebilcock (1987) also identifies and evaluates seven criticisms of price advertising in relation to legal services. These are the dead-weight social cost argument [48], potential problems of artificial product differentiation [49], potential problems of unhealthy market concentration [50], potential for supplier induced demand (SID) [51], inappropriateness of price advertising [52], deterioration of quality of service [53] and, undermining ability of the lawyer to cross-subsidise clients using supernormal profits [54].

Upon consideration of the above arguments in support of, and against price advertising, the most conclusion to be drawn is that it is apparent price advertising does not reduce the consumers' information problem to any significant degree. Price advertising of services does not ameliorate the information problem since the heterogeneity of services often precludes standardisation and hence, consumers cannot rationally compare services on price criteria alone.

Price advertising is therefore not a rational proposition in non-standardised services in terms of providing information to clients. The effect of price advertising, however, in standardised services will be examined below.

(III) Price advertising and standardisation of services:

Price advertising is a characteristic feature of, for instance, conveyancing markets where considerable elements of standardisation can be introduced with a degree of success into client services [55]. With standardised services, price advertising may have the effect of enhancing creation of a larger client base as it has the potential to furnish consumers with a threshold of information that may otherwise be deficient [56]. Information on relative prices is useful for clients to the extent that the total value of the contract will be known in advance thereby reducing uncertainty of the client. It is also likely that the consumer's perception will more readily view one lawyer as likely to produce similar quality services to another.

The anticipated outcome of price advertising with standardised services is thus expected to be enhanced consumer benefits through reduced prices. Law firms, as a consequence of price competition, would likely find their margins squeezed, necessitating an increase in sales volume. Price advertising may generate a higher volume of business for the price competitive

law firm. The law firm, when faced with this overall scenario, is likely to wish to reduce costs by introducing greater elements of standardisation, which again is likely to require a higher volume of sales to be cost effective, and thereby require price advertising to stimulate volume [57]. A 'catch 22' or 'chicken-and-egg' problem confronts firms in the market attempting to strategically manage their market share in the market characterised by price promotional competition. What is uncertain, however, is whether the quality of increased volume, lower price services would be likely to be of a lower quality standard than lower volume/ higher price services [58].

Although enhanced price competition is likely to reduce costs to consumers of standardised services, their information problem is not ameliorated and cost-cutting by services suppliers may result in quality problems and higher levels of opportunism against the interests of clients.

For non-standardisable services, there is little or no incentive to price advertise as high levels of risk and uncertainty attend the consumer's transaction, and a longer choice/ search period could reasonably be expected. Hence, price advertising would be unable to communicate that information which would be necessary to influence the consumer's choice in such circumstances. For such services the client will place great emphasis and a high level of reliance on reputation information.

Price may be only a minor consideration (or at the extreme not a consideration at all) in the purchase decision of the consumer. Many consumers are observed to freely enter contracts for legal services with no idea of the likely approximate cost of doing so. The role of non-price advertising in conveying quality information to consumers, will be examined next.

2.2 Non-price advertising in legal services:

In respect of non-price advertising of legal services by solicitors in the UK., a series of relatively recent liberalisations in practice rules of the respective Law Societies has resulted in rules evolving to permit almost any form of self-promotion so long as this is 'professional' (that is, in good taste and not of a character such as may reasonably be regarded as likely to bring the profession into disrepute).

Institutional advertising by the Law Societies, attempts to promote solicitors to the general public as a group, by attempting to help consumers identify a need for legal services in general. This, however, does not help the consumer's quest for information in relation to selecting a lawyer in particular in the case where the consumer does, thereafter, identify a need for legal services of one type or another [59].

With non-price advertising, the producer by issuing a short self-made message, attempts to capture a potentially wider client audience with the intention of reducing client search costs by reducing information problems. By issuing such information it is anticipated that this will facilitate clients to partially dispense with requirements to have repeated, personal, broad based experience of legal services to make an informed and rational choices.

An important consequence of restrictions imposed on law firm advertising is that firms are constrained to revealing only partial information. This information is typically issued impersonally to all consumers in the market, and is in no way targeted at specific individuals. Consequently, this information may be perceived by consumers as impersonal and not worth noticing. This type of information is characteristically not entirely disinterested as its primary function is undeniably to sell clients and prospective clients legal services. Consequently, consumers may attempt to seek verification of advertised information using other available sources of information or personal experience, in an attempt to identify and sterilise any bias that exists.

It is uncertain whether advertising does significantly benefit law firms in terms of them increasing the volume of their business. It is true to say that many firms who engage in advertising are uncertain of its effect (if any), but it is the case that when one or a few firms in any market advertise, other firms may feel compelled to in case they are strategically disadvantaged if they do not [60].

Should advertising, or any other reason for that matter, increase the level of quantity demanded (ceteris paribus) then some form of service standardisation in the production process may be desirable. This is likely to require some initial expenditure to research and develop routinised procedures and standardised services and then, subsequently, implement them.

In the absence of changes in advertising policy of the individual firm and of other competing firms in the market, demand for that firm's services could be expected to be relatively stable. Consequently, lawyers may exhibit a natural tendency to wish to avoid advertising and introducing standardised services as this would result in high initial set up costs associated with "mass production", so far as this is possible with legal services.

Where lawyers are specifically banned from advertising, legal services will be promoted through personal knowledge and reputation effects. Here, the law firm benefits from bearing none of the direct costs of providing consumers with such information, since it will be revealed as part of the course of their normal business[61].

Advertising expenditure does involve a certain degree of risk and uncertainty to the firm as its likely effects on consumer behaviour (especially in the area of legal services) are unpredictable and uncertain. The law firm could very easily engage in high levels expenditure for no justifiable reason, with no positive gains, or gains incommensurate with that level of expenditure. If the law firm is perceived as a reputedly bad firm by consumers, then advertising could have the paradoxical effect of reinforcing its bad name and reputation among a wider audience.

Advertising expenditure is undertaken to create greater familiarity with a certain firm and hopefully establish a 'brand name'. When a brand name is created, it is anticipated that any consumers will retain any information they hear and will associate it with that firm. They may also more readily discount any information they receive that does not confirm their evaluation of the reputation of the firm. It is also anticipated that increased latent demand will enhance consumer access to reputational information [62].

In the case where the real cost of the legal service to the client is increased due to advertising (where the consumer pays via higher real prices) then the issue then facing the consumer is whether the small amount of extra useful information (if any) derived from advertising is worth paying for in terms of higher prices [63].

Licensure in the legal profession essentially creates similar quality signals for consumers as those that are produced by the creation of brand names through advertising. Here each licensee (qualified lawyer) is franchised with the name of the Law Society as an assurance of quality to the consumer [64]. It is claimed by Trebilcock (1987) that licensure in the legal profession, whereby inputs are prescribed for the training and qualification of professionals, assumes that required training inputs correlate highly with desired service outputs [65]. He further argues that this assumption becomes increasingly tenuous as one approaches the situation, that typically exists with lawyers today, where a fairly narrowly circumscribed set of acceptable training inputs coexists with a widely varied range of desired service outputs. Consequently, licensing requirements, by themselves are argued to be weak guarantors of specialised professional competence [66].

Advertising is likely at best to merely complement information obtained by clients form other sources and, given its fairly limited maximum informational powers, it appears to play an essentially insignificant role in reducing information asymmetry between client and law firm [67].

Trebilcock (1987) assesses the sophistication of the differing types of clients on the demand side of legal services, and argues that certain private clients face the most significant deficiency of market information regarding comparative prices and qualities of differing law

firms and lawyers[68]. As a consequence, it is apparent that this client sector may receive greatest potential benefit from any potential informative value of advertising in legal services. Trebilcock (1987) argues the case for permissive liberalisation in law firm advertising restrictions, concurrently discounting the arguments against doing so [69].

In the market process of matching clients to law firms, it is claimed by Trebilcock (1987) that fairly extensive functional specialisation of law firms is evidence that the market mechanism in legal services is operating more effectively than it has done before, and better than many critics of the profession would care to admit [70].

Hence, advertising is likely to merely compliment information garnered from personal and traditional reputational sources. Client choice in less sophisticated sectors could perhaps be facilitated by lawyers disclosing information such as, for instance, educational qualifications, professional affiliations, representative clients (with permission and if not contrary to regulations), references and publications etc. This type of information could only be permitted within an advertising regime that has been subject to liberalisation [71].

2.3 Liberalisation in advertising rules in legal services:

The liberalisation of advertising rules could be expected to have a pronounced effect on the practice of solicitors by strengthening competitive pressures. Advertising creates a new dimension to the market for legal services in terms of its intended effect of furnishing consumers with greater information in order that they can make a more informed choice [72].

In an unliberated advertising regime, there is a characteristic tendency for restricted information flows in the professions via strict advertising bans or stringent regulation. The consumer of such services confronts problems in gathering information pre-purchase [73].

(I) Disinterested informational advertising:

Any restrictions remaining within a liberalised advertising regime are an attempt essentially to restrict advertising so that it performs a purely informational and disinterested role. It thereby tends to avoid advertising that implies or indicates (or attempts to) the superiority of the quality of one firm's services as against another. This goes against the grain of professional omni-competence signalled via the Law Societies in the guise of licensure. Impartial or wholly self-benefiting advertising is avoided and contrary to advertising regulations.

This reveals a strange anomaly in legal service advertising - legal restraints permit only strict information signalling type advertising, but the majority of consumers are unable to evaluate

such information. Consequently, there is no underlying rationale for the lawyer to advertise on the basis of information signalling, given the costs and benefits.

It is, therefore, unclear how such advertising is capable of providing consumers with the information that is required to rationally select lawyers. Such advertising is unable to signal product differentiation since lawyers are prohibited from advertising that they are better than each other. Many consumers may attempt to find some identifiable proxy for a quality signal, for example, firm size. Firm size could be used as a proxy on the basis that the firm would not have undergone an expansion if they had not satisfied an ever increasing client base.

It is the case, however, that the largest firms are commercial firms rather than private client firms. Their size may simply enable them to command a higher price for its services. They are, therefore, in the enviable position of being a large firm (thus perceived as a high quality firm) which is, thereby, able to charge a quality premium [74].

(II) Conclusion regarding using advertising to ameliorate information deficiency in legal services:

In conclusion, it is apparent from the discussion in this section that lawyer advertising does very little in the direction of providing consumers with useful information to rationally select a solicitor in the market. At best, advertising may perform the function of enhancing reputation information derived from other sources. Advertising may tend, however, to be less important in the consumer's choice decision than other sources, for example, referrals from friends and family and the like. The total effect of legal service advertising is dependent essentially on the extent to which consumers utilise that information as against other information they can utilise. The informative value of advertising in legal services is consequently uncertain.

Hudec and Trebilcock (1982) perceive the advantage of advertising over other sources of information as being that it can reach potential clients at an early stage in their decision making process [75]. They also argue that it does, however, have serious limitations as it cannot disseminate important information to clients such as the skill/ expertise in relation to the client's specific legal problem [76].

In relation to price advertising, advertising can convey flat fees charged for routine standardised services, but obviously cannot similarly quote fees for more complex transactions [77].

Advertising can in no way be regarded as remedy for deficient information of consumers and potential consumers of legal services, but it can play an important part in supplementing and

reinforcing traditional sources of consumer information in legal services and through plugging gaps in vital informal information networks [78].

Section Three: Creating Brand Name Capital in the Law Firm - its Significance and Consequences.

Introduction:

The previous section discussed the role of advertising in enhancing consumer's information regarding legal services. This section will examine the over-riding importance assigned to reputation of the firm, continuing the underlying theme of much of this chapter. The concept of a brand name and its consequences will become a central focus, wherein a critique of the effectiveness of partnership as a vehicle for organising and exploiting brand name capital will be presented.

3.1 The brand name concept:

A brand name exists in the situation where consumers of a product/ service systematically choose one firm's output in preference to that of competing firms. The consumer's reasons for doing so may be due to real aspects of product/ service differentiation, or due to perceived differences which do not really exist. In any case, it is imperative that the firm continually attempts to maintain the attractiveness of their brand against others, and this requires continual innovation and dynamism. Competing brands are characterised as having have low cross-price elasticity, thereby indicating the absence of close substitutability.

In discussion of the brand name concept, the related concept of franchising is a natural partner in discussion [79]. In the case where the firm has effectively created a brand name for its services through reputation, this can act as an effective quality signal to prospective consumers of its services. The brand name may supersede the effect of Law Society licensure, as the prime quality signal perceived by consumers [80]. It may be the case that advertising is aimed at promoting the brand name which has been created, but at all times reputable service must remain a feature of the firm's activities and form the actual substance behind any promotional advertising. In this respect, there may exist economies of scale in advertising in large brand name firms.

With an established brand name, the firm can effectively convey service quality information to the user of legal services. This reputation information is a valuable information source to the information deficient client.

3.2 Economies of scale in legal services:

It appears true that in only a few legal service types, amenable to standardisation and 'mass production' techniques, so far as these apply to such services, will economies of scale be a significant feature of service provision for law firms. In this case, the puzzle remains as to why law firms grow to scales which are likely to far exceed exhaustion of economies of scale. It can be argued that group practice may act as an effective quality assurance mechanism to clients, thereby offering at least a partial solution to this puzzle [81].

In the case of medical group practice, a similar agency relationship characterised by uncertainty and information asymmetry between patient and doctor exists to that which exists between client and solicitor in legal services. Getzen (1984) challenges the strict applicability of the traditional economies of scale argument to medical group practice [82]. This argument is viewed as deficient by Getzen since, while he concedes that scale related cost savings can and do occur in certain cases, he argues that the economies of scale argument relies on differences in transactions costs which render some organisational modes more costly than others [83].

In Neoclassical orthodoxy, production costs are assumed to determine economies of scale, where transactions costs are assumed to be zero and complete certainty is assumed. The combined existence of zero transactions costs and complete certainty is obviously the complete antithesis of the paradigm law firm transaction. This transaction is characterised by a non-trivial degree of uncertainty and extreme information asymmetry in exchange between client and professional practitioner. This casts doubts on the validity of the traditional Neoclassical explanation of optimum scale being determined by production cost savings, in the case of legal service provision.

Legal practice is very human capital intensive and the quality of output could be expected, therefore, to be subject to a moderate degree of variability. Costs of obtaining service quality information is far greater for consumers than for producers due to information impactedness. Consequently, Getzen (1984) argues, firstly, that such a transaction is apt to be governed in a relationship termed a 'brand name contract' and, secondly, that where reputations are so formed, clients are willing to pay a premium for services of that quality brand name [84].

3.3 Benefactors of the creation of a brand name:

Getzen (1984) argues that should a firm create a reputation, a premium reflecting quality may be included in that firm's service price in an attempt to signal quality levels over and above those of other firms. This creates an incentive for the firm to attempt to supply services of the quality it perceives to be expected in the market by consumers [85].

The consumer purchase decision is likely to be based on reputation of brand names and the producer of legal services could be expected to be penalised for quality reduction through loss of expected future earnings caused by reputation diminutions. In this case the consumers of legal services should benefit from the strong incentive that suppliers of services are provided with to continue to supply good quality legal services [86]. The basic thesis here is that brand name premia act as guarantees which have the effect of creating an incentive for the firm to fulfil the implicit contract between client and firm, by providing services of the quality expected by the client. These quality expectations have been formed by the brand name [87].

Consumers benefit from practitioners practising in conjunction within groups since internal mutual consulting and monitoring between individuals within the firm can at least partially replace costly search activity by individual consumers. The reputation of the firm and its constituent practitioners can be effectively conveyed and the firm's brand name can be effectively created at lower costs via group practice [88].

Consumers are not exclusively the benefactors of this brand name process. The lawyer, as well as the firm to which he belongs, will retain some of the value of the brand name capital. Similarly, reputation diminutions, if they are perceived by present and prospective clients of the firm, will result in the reputation value of that firm being discounted by these clients in the market. The lawyer practising within this firm will suffer reputation losses to the extent that he will be tarred with the same brush as the firm. The value of the firm's brand name is only an asset to the lawyer, however, if he remains within that firm [89].

When lawyers enter the firm, the established lawyers within the firm possess the brand name capital of the firm. The focus then becomes the transfer mechanism to transfer reputation of the firm and brand name down through to these new lawyers. The problem here is that these new lawyers may not have many (or any) clients. It would be in the interests of the existing lawyers to transfer some of their clients to the new lawyers in order that reputation and brand name capital also becomes associated with these new lawyers in the eyes of clients. The new lawyers benefit because they have an instant tranche of clients which would otherwise have taken them years to build up. Getzen (1984) views the fact that existing members receive a disproportionately large share of joint practice income, as compensating them for transferring brand name and reputation down to new members via client transfer [90].

The lawyers' human capital investments within the firm create a collective asset, which can be viewed as 'brand name capital'. The sum of the values of the individual human capital assets, is less than the value of the brand name capital of the firm, due to human capital synergy [91].

Getzen (1984) argues that partners are viewed by consumers (to a degree) as a single entity/

firm, thereby perceiving that quality will be the same regardless of which individual is seen within the firm. The firm thereby creates at a micro level a similar effect regarding professional omni-competence, as does licensure at the more macro level of the profession as a whole [92].

It is argued by Getzen (1984) that it is crucial for an asymmetry of information costs to exist, as it must be cheaper for existing members of the law firm to identify and enforce quality of service of its partners, than for consumers to do so. It is only if this condition is met, that the firm can economise on information costs. This should indeed be the case since only a lawyer is suitably endowed to rationally and effectively judge the quality of other lawyers [93].

3.4 The two period reputation problem and brand name capital:

Getzen (1984) reveals the two period problem that brand name capital creates for the practice;

1. The first period problem - the need to build a reputation from nothing.
2. The last period problem - the proximity of retirement for one or more of the partners can induce slack and low effort intensity in their attempts to maintain quality [94].

Getzen (1984) proposes that perpetual identity, separate from those individual constituent members, may ameliorate the first period problem. In essence, the identity of the firm is independent of the identities of its constituent members [95]. It is further argued that the existence of a separate identity of the firm reduces problems of consumers attempting to make comparisons of quality and contribution of firm members inter alia.

Where failures of quality are perceived by consumers it is argued that such comparison by the consumer will be irrelevant, and the failure to provide quality service will be attributable to the firm rather than one or more of its individual members [96]. In this respect, the last period problem no longer confronts the firm and its members.

The high cost of consumers obtaining information is a contributory factor in determining the inelastic nature of the demand that faces the firm for its services. Substantial information costs cause the price and marginal costs of the services to diverge, reducing cross-price elasticity [97]. It will be recalled that it was precisely this lack of cross-price elasticity (substitutability) which defined brand name loyalty [98].

This characteristically inelastic demand confronting law firms results in the firm valuing consumers' current and future business very highly, and should result in the firm attempting

to protect its brand name/ reputation with high quality output. As a consequence of the consumer perceiving services of uniform quality being offered by all constituent members of the firm, practising together in a group practice results in partners becoming better substitutes for each other, since their cross-price elasticity is increased [99]. Consequently, problems of firm member turnover, allocation of clients between firm members and client perceptions of relative quality and contributions of firm members are significantly ameliorated by group practice.

Getzen (1984) views the law firm/ partnership as a contract for the transaction of a brand name which can be exchanged by firm members as a capital asset. He also argues that incentives are created for firm members to internally transfer clients between each other and to maintain quality in order that the value of the firm is maximised. It is further argued that informational economies of scale are realised through the partial substitution of firm members mutual monitoring for evaluation by clients (which is costly for clients but relatively costless for the firm) [100].

The existence of the group practice will signal to clients the enforcement of uniformity in quality of service across practitioners and consequently, clients can use observations on quality of any one firm member and extrapolate this to apply across all firm members. Getzen argues that this permits the client to amass a greater body of experience and/ or number of observations, thereby reducing costs of search and quality prediction to clients [101].

It is true to say that some aspects of the multi-dimensional nature of the quality of services produced by a firm are less costly for clients to monitor as against fellow firm members. Examples of such an aspect of quality would be 'approachability', ability to communicate with particular clients and make them feel at ease, and the like. Nevertheless, group practice does provide significant advantages in the face of information difficulties and given the desire to create brand name capital to reduce them [102].

3.5 Law firms and reputation franchising:

Where a law firm creates a brand name it is possible for that firm to franchise shares of this brand name via some form of franchising process. As a consequence of consumers attaching a high quality evaluation to such firms, other firms may desire to share in a portion of this brand name. This could be brought about by franchised firms practising under the well known and respected firm's name, through a franchising/ licensing arrangement. This would operate on the basis of the firm's name, rather than membership of the Law Society, that signalling quality to the consumer [103].

It is clear that both franchiser and franchisees have potential gains from mutual association.

The granting of franchises by the franchiser/ brand name firm would allow that firm to become relatively large, via franchised outlets, gaining larger market shares and wider market coverage. Concurrently, this would permit the franchiser to maintain quality and, if properly designed and policed, may ameliorate many scale related problems inherent in large partnership practice.

The franchisees' potential advantages stem from their ability to market the branded service, in return for the payment of a fee to the franchiser. To be granted a franchise certain conditions stipulated by the franchiser regarding service provision would require to be fulfilled. The firm possessing the brand name could invite willing prospective franchisees to submit sealed bids/ tenders for franchises. The brand name firm would naturally wish to screen the bidding firms to ensure they were worthy of being awarded a franchise and posed no threat to the franchiser by practising under its brand name.

Monitoring activities on the part of the franchiser, combined with bonding activities of each franchisee, could ensure mutual practising benefits with reduced transactions costs. The franchised firms' behaviour could be expected to be regulated partially by threat/ penalty of losing the franchise (ie. a valuable share in brand name capital). The franchiser would also be able to spread risks inherent in human capital effectively and retain (relatively risk free) a wide portfolio of specialised 'compartmentalised' functions within the overall franchised partnership.

The issue of incentives to regulate the behaviour of both franchiser and franchisees, is of central importance to the franchise operation in ensuring its survival and efficient operation. Again, the principal/ agent relationship provides the framework in which incentives of such a franchise operation can be analyzed [104]. The basic 'rule' of the agency relationship is to attempt to align incentives of the agent and the principal, to maximise joint gains, whilst simultaneously minimising resources consumed by both parties via monitoring and bonding activities. As within partnership itself, issues of mutual incentives, quality assurance and monitoring and bonding activities are all of central importance within franchise operations.

It is now evident that within the UK some of the large chains of law firms practice with a head office and a branch network of 'quasi'-franchise type outlets. Firms are also increasingly observed entering into associations/ groupings of firms with other UK and foreign firms. For instance, often a group of non-London law firms become associated with a large London based firm, franchising that firm's name/ reputation [105].

Ultimately, at a more micro level, partners of the law firm may be viewed as franchisees of the firm to which they belong, since they benefit individually from shares in the brand name capital of the firm by partaking in a share of its collective reputation. A particular partnership

team is likely to have a high coalition value in terms of brand name capital, and if each partner recognises this, they are likely to be constrained from engaging in morally hazardous behaviour which may jeopardise it. At best, it may act as a strong mechanism to prevent partners from leaving the firm, where the specific constraint would be the potentially high opportunity cost of leaving a firm with high coalition specific success and an established brand name [106].

It is, therefore, apparent that the concept of a brand name in legal services may ameliorate, at least partially, the information difficulties of consumers and potential consumers of legal services. It has also been established that professionals jointly practising in a group offers advantages both to producers (partners) and consumers (clients) of legal services and provides an effective vehicle for the creation of brand name capital. This highlights the view of partnership as a relatively effective method of organising and exploiting brand name capital to the dual benefit of clients and partners. Alternative views and facets of partnership will be presented elsewhere later in this thesis.

Chapter Four - Endnotes

1. Information impactedness is essentially identical to information asymmetry, but the former is the preferred description for such a phenomenon, coined by Williamson in his transactions cost framework. See; Williamson, O.E., **Markets and Hierarchies.** New York. The Free Press, 1975. and also; Williamson O.E., **The Economic Institutions of Capitalism: Firms, Markets and Relational Contracting.** New York, The Free Press, 1985;

In the case of legal services clients enter into contracts with the firm individually, without coordination/ collusion and hence, the outcome of these contracts could be expected to be solely dependant on the efforts of the law firm. The performance of the typically passive client is usually irrelevant, leaving full responsibility for performance resting on the law firm.

Clients may be able, at best, to perform some monitoring function and thus are capable of creating some informational economies of scale. A client can perceive quality by evaluating information obtained on one partner to attempt to estimate the quality of service he expects to receive. Hence, a consumer who views all lawyers of that firm as being of uniform quality will have lower search costs.

Many services eg. leases, divorce, conveyancing, wills etc. are perhaps capable of some form of standardisation. Such services may resultantly be of a more uniform quality within a given law firm where standardisation has occurred, and also between law firms where standardisation is a feature. The empirical study will hopefully expose where standardisation can be used and thus identify services where it is easier for clients to evaluate quality.

2. Agency theory is the theoretical framework within economic theory of the firm that seeks to explain the issues surrounding such relationships. Agency theory is primarily concerned with finding organisational resolution to the problem of typically misaligned incentives of principals and agents. The focus, therefore, is the incentive structure/ mechanism that has evolved, or that it is necessary to evolve, between the two parties of conflicting interests

The seminal contributions in the area of agency cost theory are commonly accepted as being; Jensen, M C. & Meckling, W H., Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. ***Journal of Financial Economics***, Vol.3, 1976, pp. 305-360, and; Fama, E., Agency Problems and the Theory of the Firm, ***American Economic Review***, Vol.76, 1980, pp 971-983.

3. See, Ricketts, M., **The Economics of Business Enterprise: New Approaches to the Firm** Wheatsheaf, 1987 p.40

In the case of the client/ lawyer relationship the potential conflict of interest that could occur is that the lawyer will spend as little time as possible attending to the clients problem. The client, however, is interested in obtaining the maximum amount of attention possible from the lawyer in relation to his problem. Clearly a conflict of interest potentially exists and furthermore, is likely to exist at least to some extent.

In terms of information asymmetry, the client may simply be unaware of what courses of action the lawyer can take and how they would each affect him. It may even be the case that, after the lawyer has taken which ever action he decided upon, the client may remain unaware of which action was taken.

4. The goal of achieving this situation of alignment of incentives and maximisation of joint payoffs, prompts consideration of contingency fees where the level of remuneration solicitors are paid in any given transaction is contingent on the outcome of the work completed for the client. This is clearly applicable to certain transactions that clients hire solicitors for but for others where there is a single end solution, eg. conveyancing, it is difficult to imagine how contingency fees would operate.

5. Economics has, through it's preoccupation with developing theories of the firm, become interested in the role of, and nature of, contracts. In doing so it has attempted to synthesise both economic and behavioural influences within the firm. Transactions cost and agency cost theories have been a popular vehicle for development of these ideas in recent years and share contracts at the focus of their analysis, as a common denominator.

For a potted historical development of these ideas *see*; Cyert, R.M. & March, J.C., **A Behavioural Theory of the Firm**. Englewood Cliffs, NJ: Prentice Hall, 1963.; Thompson, J.D., **Organisations in Action**. New York: McGraw Hill, 1967; Macneil, I.R., The Many Futures of Contract, ***Southern California Law Review***, Vol.47, 1974, pp.691-74; Williamson, O.E., (1975) *supra* Note 1. ; Jensen, M.C. & Meckling, W.H., Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. ***Journal of Financial Economics***, Vol.3, 1976, pp. 305-360; Fama, E., Agency Problems and the Theory of the Firm, ***American Economic Review***, Vol.76, 1980, pp.971-983; Macneil, I.R., **The New Social Contract: An Enquiry Into Modern Contractual Relations**. New Haven, Conn.: Yale University Press, 1980.; Williamson O E., (1985) *supra* Note 1.

For an analysis of contracts that reaches far beyond simple classical contracting procedures, where all contingencies are well defined and ex-ante agreed upon, *see*; Williamson (1985) above, who discusses the role of implicit and relational contracting where trust is a major force in agreement. Williamson's 1985 analysis draws heavily on the contractual framework established in Macneil (1980), above. See also; Goldberg, V.P., Relational Exchange: Economics and Complex Contracts, **American Behavioural Scientist**, Vol.23 No.3, pp.337-352. See also; Reve, T., The Firm as a nexus of Internal and External Contracts, in Aoki, M., Gustafsson, B. & Williamson, O.E., **The Firm as a Nexus of Treaties**. Sage, 1990.

6. This type of exchange is described in terms of a relation contract by Macneil (1980), *supra* Note 5. Reve (1990), p.153, *supra* Note 5., alleges that these contracts are characterised by relational norms such as role integrity, trust, preservation of the relation, conflict resolution and supracontract norms.

7. Taken to it's logical conclusion, this situation can result in the development of a 'market for lemons'. This is essentially a situation where, due to information difficulties, the producers of high quality produce (in this case legal services) are unable to signal to consumers that their products are of higher quality than those of low quality producers. Consequently, they are not able to command a higher market price then low quality products as consumers are unable to perceive a differentiated quality As a result, there is no incentive to produce higher quality products and only low quality products are produced. See; Akerlof, G., The Market for 'Lemons': Quality Uncertainty and the Market Mechanism, *QJE*, Vol.84, 1970.

8. Even if the consumer can make the choice, it is often not apparent post-consumption whether the correct choice was made as quality evaluation is problematic, if not impossible, for the typical consumer.

9. Accepting Akerlof's argument, *supra* Note 7, there is little apperent incentive for incentive for producers to supply high quality services in the market. Consequently, competition on quality would not be a likely feature of such a market. The strength of reputation effects, and the ability of consumers to perceive such effects may ameliorate this, resulting in an incentive for producers to produce higher quality services and compete on this basis.

10. These are the very conditions that Akerlof describes as being conducive to the development of a 'lemons market'; *supra* Note 7.

11. Bounded rationality is one of the two critical behavioural assumptions, upon which the transactions cost framework is constructed, the other being opportunism. This pair of assumptions can be seen as a radical departure from Neoclassical orthodoxy, having foundations in behavioural science. The concept of bounded rationality as borrowed by Williamson, essentially means that agents are intendedly rational, but are only limitedly so.

Bounded rationality has been defined by Simon (1957) at p.198 (see below) as describing the situation where: "the capacity of the mind for formulating and solving complex problems is very small compared with the size of the problems whose solution is required for objectively rational behaviour in the real world."

See; Simon, H.A., **Administrative Behaviour**. New York: Macmillan, 1947 (2nd edition, 1961). See also; Simon, H.A., **Models of Man**. New York: John Wiley & Sons. Inc., 1957. See also; Simon, H.A., Theories of Bounded Rationality. in McGuire, C. and Radner, R. (eds), **Decision and Organisation**. Amsterdam: North-Holland Publishing Company, 1972, pp.161-176. See also; Simon, H.A., Rationality as a Process and Product of Thought. *American Economic Review*, Vol.68 (May), 1978, pp.1-16 and; Simon, H.A., On the Behavioural and Rational Foundations of Economic Dynamics. *Journal of Economic Behaviour and Organisation*, Vol.5, 1984, pp.35-56.

12. Opportunism in this context is the type of behaviour categorised by Williamson as lack of candour, or self-interest seeking behaviour with guile. See; Williamson (1975), *supra* Note 1. at p.9.

13. The asymmetry in information that favours the law firm and disadvantages the client, when paired with characteristic high degrees of uncertainty and possible transactional infrequency, quickly exhausts the bounds of rationality of clients leaving them ideal targets for opportunistic behaviour by the law firm. In the relational contract, the party facing the information deficiency, in this case the client, must simply trust that the party with the information advantage, in this case the firm, will not act opportunistically. In the case of the legal profession, established institutional factors such as self-regulation, professional ethics, mutual monitoring and self-enforcement of incentives are expected to reinforce this trust in the client.

14. In relationships with typically unsophisticated private clients it would be difficult for the client to perceive opportunistic behaviour on the part of the law firm. Hence, the chances of being caught are fairly small from the firm's viewpoint. The penalty of being caught is presumably the loss of that client's future business and any other business that may have been directed to the firm by way of referrals via this client. The benefits of behaving opportunistically against such a client are likely to be fairly minimal given the relatively low monetary value of typical private client contracts

In relationships with more sophisticated commercial clients, however, who may have more extensive knowledge of legal problems and the experience of using several law firms, it may be significantly easier for such a client to perceive opportunistic behaviour on the part of the law firm. The chances of being caught may be relatively high, making it a less attractive option. The penalty of being caught is more financially serious than in the case of private clients above. The value of that firms future legal work would be foregone as would any other business gained from referral. In tight business communities, the law firms reputation could be dealt a serious blow resulting in severe losses of business. The benefits of acting opportunistically, on the other hand, may be relatively large given the high monetary value of fees that typically attend commercial and specialist commercial client transactions.

15. In it's strongest form, the lawyer has the ability to inform the client that he has a bigger problem than he has, pretend to spend additional time pursuing these added problems and bill the client at a much higher billing rate than was actually necessary. The client need never know that the lawyer has undertaken such a scheme since it is unlikely that anything exists against which he can make comparisons ie. no repeat purchase, no previous purchase, no purchase from other lawyer, no equivalent purchase by friend or family etc.

This type of abuse would be less easy in routine transactions since;

1. It would be more difficult to justify extras and,
2. A greater risk faces the lawyer since it would be more easily discovered by, or arouse greater suspicion in, the individual.

16. For a rigorous analysis and summary of these aspects of the organisation of the legal profession, from a sociological perspective, an economic perspective and a socio-economic perspective see; Abel, R.L., **The Legal Profession in England and Wales**, 1988, pp.3-31.

17. In his role as a discursive translator, there is a potential for the solicitor to Supplier Induce Demand (SID). This is simply the situation where a provider of a service, through mis-information of the client, creates an inflated demand for his services by convincing the client that he requires services that essentially he does not. In legal services, the potential for this self-evident as it would be relatively simple for the lawyer to create a demand for services, through the use of legalistic jargon which makes the client feel as if he actually requires a described service.

The lawyer's defining skill is as a discursive translator ie. plain english to law and back again. In reality, much work that clients consult lawyers about is not beyond the reasonable man in the street. This certainly becomes obvious when one looks at DIY lawyering books, but DIY lawyering does, however, remain a pastime of few persons. This is probably a function of a number of factors including a general fear of the unknown that people typically possess, a respect for convention and a lack of time to spend attending to their own legal problems

18. The client may largely be unaware of the fact that he is being used as a hostage to extort exorbitant fees, rendering such behaviour essentially riskless to the law firm. As a result the client's voice option of complaint through The Law Society will not be used as he will be unaware that he has been subject to opportunism by the law firm.

Even in the unlikely event that the client does perceive he has been taken for a ride and does voice complaint, The Law Society has a vested interest in preserving the face of the profession and the interests of it's members. The opportunistic lawyer consequently has the ability to abuse his position of trust and confidence and exploit his monopoly power.

19. Quality evaluation is a problem in the ex-ante situation where clients are choosing a solicitor. Here, they will face a deficiency of information regarding the relative qualities and prices of competing suppliers in the market. The heterogeneity characteristic of legal services makes any possible comparisons difficult. Repeat purchase is not usually a characteristic of legal services, but in the case where it is, it may still be difficult to determine relative costs and quality with any accuracy. Relying on traditional information sources eg. advertising etc is unreliable as this information is not disinterested. Relying on disinterested sources of information is unreliable also as the person providing the referral or judgement on quality will be likely to be similarly compromised in his ability to judge quality.

In the ex-post consumption situation, it is possible that the client will still be unable to determine the quality of the legal services he has been provided. There will seldom be past experience of consuming legal services of a similar type from a range of competing suppliers or experience of consuming a range of services from the same supplier, making quality evaluation difficult.

20. The attainment of self-set goals which are towards the lower end of the spectrum of quality standards in legal services are likely to be perceived here by clients as being of reasonable standard. The absence of repetition in purchase or purchasing from various suppliers will fail to uncover this type of behaviour. It is also unlikely due to high search costs that consumers will seek opinions from competing suppliers in the pre-purchase situation. If this pre-purchase behaviour did occur then the setting of low goals would be penalised by non-hiring by the consumer.

21. A body of literature exists that argues the validity of this concept, particularly in relation to medical services. See; Anderson, R.K., House, D. & Ormston, M B., **A Theory of Physician Behaviour with Supplier Induced Demand.** See also; Evans, R.G., Suppler Induced Demand: Some Empirical Evidence and Implications, in Evans, W.G. & Trebilcock, M.J. (eds), **Lawyers and the Public Interest**, Toronto, Butterworth, 1987. See also; Perlman, M. (ed), **The Economics of Health and Medical Cases.** Macmillan, 1974. See also; Reinhardt, V.E., The Theory of Physician Induced Demand: Reflections after a Decade. ***Journal of Health Economics***, Vol.4, 1985, pp.187-193. (editorial).

22. The paradoxical anomaly thrown up here is that most lawyers regard their respective Law Societies with contempt, if not overwhelming indifference.

23. A discussion of the expertise and altruism of the legal profession, in the context of differing sociological perspectives of the professions, is presented in Abel, R.A. (1988), *supra* Note 16

24. It is interesting to note here that what constitutes 'best interests' is solely judged by the lawyer and the consumer is in no manner sovereign in the client/ lawyer relationship.

25. It would be ridiculous to assume that ordinary men in the street could distinguish between matters of incompetence and the mere operation of the judicial system, when they are insufficiently sophisticated to rationally choose a lawyer, or assess quality of legal services post-consumption.

26. Many of these issues form the basis of discussion in Chapters One, Two and Three of this thesis.

27. The professions have a desire to preserve their privileged status in society and respect the trust invested in them by society. As a result they will tend to exhibit a low tendency to act opportunistically or abuse their monopoly status. The relationship between society and the professions is categorised by the relational contracting characteristics noted above, *supra* Note 13.

28. See; Abel, R.A. (1988), *supra* Note 16.

29. It will be remembered that Ricketts (1987) *supra* Note 3., p.40, argued that in order for the agency relationship to be interesting, two important features had to be present. These are, firstly, a conflict of interests and, secondly, an asymmetry in information available to the principal and agent.

It is also argued that if there is no conflict of interest in the agency relationship, then the existence of asymmetric information between the two contracting parties ceases to be a problem. The lawyer would perceive no incentive/ advantage in recommending a course of action that did anything other than accord with the interests of the client. Where it is assumed by the client that the lawyer can be trusted and will thus avoid any conflicts of interest, the client simply perceives no information asymmetry and thus no potential for opportunism. Even if he does, however, there is little he can do to reduce the size of the wedge of ignorance driven between him and the lawyer and little he can do to protect against opportunism, or reduce it's impact should it occur.

30. This is of prime importance to the solicitor as, in the absence of formal advertising and in the domain of experience goods/ services, the best advertisement for the law firm is it's own satisfied clients. Even where advertising does take place, it is likely that in the typical consumer's choice regarding which law firm to consult, disinterested referral information would be more highly weighted in any evaluation than self-promoting advertising. Hence, reputation creation and sustainment is an essential behavioural determinant of the law firm.

31. The law firm, it is fair to say, will most likely equate reputation maximisation with maximisation of the quality of it's service to clients. In attempting to maximise it's reputation, the firm will have some notion of what it perceives clients perceive as quality in legal services. Once it has identified these, the firm will attempt to tailor it's service to satisfaction of these perceived criteria, thus apparently maximising it's reputation. This is fraught with problems of determining what consumers perceive as being quality in legal services, firms facing the difficult task of identifying these consumer perceptions and at the base line, determining what constitutes actual quality in legal services.

32. Williamson (1975), *supra* Note 1., argues that transactions are costly to perform due to a combination of behavioural and external influences surrounding the transaction. Those factors thought to be central in causing transactional difficulties are;

1. Opportunism - actors seeking self-interested goals with guile.
2. Bounded rationality - actors facing perception and cognitive limitations.
3. Information impactedness - asymmetric information distribution between the parties to the exchange process.
4. Small numbers - the number of alternative suppliers in the market.

These difficulties are enhanced, raising transactions costs in situations where the above interact with one or more of the following transaction characteristics;

1. Uncertainty - ambiguity surrounding contractual specification/ definition and performance measurement.
2. Asset specificity - where assets are particular to that transaction and have less or no value outwith that contract.
3. Contractual frequency - the repetitiveness of the transaction between the parties.

In terms of Williamson's transactions cost framework, whose major features are outlined above, the typical private client transaction suffers from information impactedness, severe uncertainty, quickly exhausted bounds of rationality and contractual infrequency. The relational contract is viewed as an efficient response to the combination of these characteristics.

33. Search costs are essentially the costs of acquiring information/ knowledge. One of the major criticisms of Neoclassical economics is that it implicitly assumes that economic actors have perfect knowledge and that such knowledge is costless to obtain. This criticism is most perhaps most forcibly argued from an 'Austrian' school perspective, where the emphasis is on the pivotal role of the entrepreneur in the process by which information is disseminated in the economy. Even theorists in the Neoclassical tradition soon recognised that information was not costless to obtain and that it had a real value. Such theorists developed analytical tools to handle information and saw it in the context of rational maximising behaviour where individuals acquired information in the market. The seminal article in this area is widely accepted as being Stigler, G., The Economics of Information, ***Journal of Political Economy***, Vol.69, 1961, p.213 from which a burgeoning literature on search and information thereafter emanated. The basic posit of this paper was that individuals, as rational maximisers, will invest resources in acquiring information up until the point where the marginal expected benefits of acquiring that information equals the marginal costs of obtaining it.

For an introduction to the corresponding 'Austrian' perspective on information and 'discovery' as opposed to search, see; Kirzner, I.M., **Perception, Opportunity and Profit.** University of Chicago Press: University of Chicago, 1979.

34. It is not possible for producers to signal a quality premium by higher price if consumers cannot perceive the differential quality of products in the market. In this situation a 'market for lemons' could arise. See; Akerlof, G., (1970), *supra* Note 7.

35. *supra* Note 11. While Bounded Rationality more usually describes a situation of the amount of information being vast in relation to the ability of the person to process it, even if the individual did not face a deficiency of information in respect of legal services, he would typically not have the knowledge to be able to interpret it so that he could make a rational choice and evaluate quality of the legal service chosen.

36. Hudec, A.J. & Trebilcock, M.J., Lawyer Advertising and the Supply of Information in the Market for Legal Services. ***University of Western Ontario Law Review,*** Vol.20, No.1, 1982.

37. Network theory is useful in explaining informal relationships where high degrees of implicit trust are involved. See; Beije, P. Markets, Hierarchies and Inter-organisational Relations: A Network Approach. E.A.R.I.E. (European Association for Research in Industrial Economics), 15th Annual Conference, 1988. See also; Mattsson, Lars-Gunner., Management of Strategic Change in a Markets-as-Networks Perspective, in Pettigrew, A., **The Management of Strategic Change.** Blackwell, 1987. See also; Jarillo, J.C., On Strategic Networks. ***Strategic Management Journal,*** Vol.9, 1988, pp 31-41.

38. In the case of commercial clients, there may be a whole host of other important factors in the consumption of legal services which are desirable/ preferred by the typical client.

39. Some commercial clients will undoubtedly be more sophisticated than the typical private client. Such clients may, therefore, not share a similar degree of ignorance and indifference to that of the private client.

40. There have been several articles in recent years that have focused on the role of advertising in professional services in the broader context of it's information enhancing role. See; Benham, L., The Effect of Advertising on the Price of Eyeglasses, ***Journal of Law and Economics***, Vol.15, 1972, pp.337-352. See also; Cox, S.R., De Serpa, A.C. and Canby, W.C., Consumer Information and the Pricing of Legal Services, ***Journal of Industrial Economics***, Vol.30, 1982, pp.305-318. See also; Schroeter, J.R., Smith, S.L. & Cox, S.R., Advertising and Competition in Routine Legal Service Markets: An Empirical Investigation. ***Journal of Industrial Economics***, Vol.36, 1987, pp.49-60. See also; Trebilcock, M.J., Competitive Advertising, in Evans, W.G., & Trebilcock, M.J. (eds), **Lawyers and the Public Interest**, Toronto: Butterworth, 1987 (Chapter 5). See also; Hudec, A.J. & Trebilcock, M.J., Lawyer Advertising and the Supply of Information in the Market for Legal Services, ***University of Western Ontario Law Review***, Vol.20, No.1, 1982. See also; Nelson, P. Information and Consumer Behaviour. ***Journal of Political Economy***, Vol.78, 1970, pp.311-329. See also; Nelson, P.J., Consumer Information and Advertising in Galatin, M. & Leitler, R.D. (eds), **Economics of Information**. Martinus Nijhoff, 1981, pp.42-68. (Comments by Alcaly, R.E. pp 78-82). See also, Stigler, G., The Theory of Price. (4th edition) Macmillan, 1987, Ch.14 **The Economics of Information**, pp.236-247

41. The regulatory issues surrounding advertising in legal services are the focus of many academic works. See; Hudec, A.J. & Trebilcock, M.J., Lawyer Advertising and the Supply of Information in the Market for Legal Services, ***University of Western Ontario Law Review***, Vol.20, No.1, 1982, pp.53-99 at p 95.; Mitchell, C.N., The Impact, Regulation and Efficacy of Lawyer Advertising, ***Osgoode Hall Law Journal***, Vol.20, No.1, 1982, pp.119-137. Murdock, G.W. & White, J., Does Legal Service Advertising Serve the Public's Interest? A study of Lawyer Ratings and Advertising Practices, ***Journal of Consumer Policy***, Vol.8, No.2, 1985, pp.153-165 at p.162., Hazard, G.C. Jr., Pearce, R.G. & Stemple, J.W., Why Lawyers Should be Allowed to Advertise: A Market Analysis of Legal Services, ***New York University Law Review***, Vol.58, (Nov) 1983, pp.1084-1113; Harris, M.C., Solicitors Right to Advertise: A Historical and Comparative Analysis, ***Georgia Journal of International and Comparative Law***, Vol.15, Summer 1985, pp.317-350.; Attanasio, J.B., lawyer Advertising in England and the United States, ***The American Journal of Comparative Law***, Vol.32, 1984, pp.493-541.

42. See; Trebilcock, M.J., Competitive Advertising, in Evans, W.G. & Trebilcock, M.J. (eds), **Lawyers and the Public Interest**. Toronto: Butterworth, 1987 Ch.5 at p.147.

43. *supra* Note 41

44. In the case where price advertising does stimulate cost cutting behaviour/ increased competition, this may result in increased access to consumers whose quantity

demanded of those legal services is price sensitive/ relatively price elastic. These consumers may previously have been extra-marginal consumers and the price reduction has infra-marginalised them.

The demand for most legal services, however, is likely to be typically inelastic and consequently fairly insensitive to price changes. Although the demand for certain legal services could be expected to be less price inelastic, and also dependant on the relative service type mix offered by the firm, the overall effect may be a reduction in firms' profit margins. This is the basis of the fear of many in the legal profession that this will drive lawyers out of business, reducing market coverage and actually worsening consumer access. This self preservation goal stirs many of the legal profession to hold a hostile view towards advertising and gradual liberalisation in regulation of advertising.

45. With reference to production innovativeness being stimulated by price advertising, it is argued that the pressure to reduce costs in order to become price competitive may force firms to introduce greater standardisation in documentation and procedures and utilise better capital equipment and wider categories of labour, eg. paralegals, legal executives and licensed conveyancers. Advertising can effectively be used as a tool to attempt to generate higher volumes of business that can more readily justify the cost of introducing often costly elements of standardisation.

46. This is not to say that price advertising is not a feature of many subsectors and areas within the overall UK legal services market.

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47. A series of studies have recently been undertaken by the University of Strathclyde Department of Economics to examine levels and dispersions of fees across markets in Scotland and England in the period since liberalisation of advertising and other practising restrictions. The recent deregulation has had the effect of removing anticompetitive practices and evidence of this shift in government policy away from protectionism can be seen most readily in terms of, for example, the removal of the monopoly in conveyancing, the abolition of scale fees and the removal of some prohibitions on advertising and promotion.

See; Love, J.H., Stephen, F.H., Gillanders, D.D., & Paterson, A.A., Spatial Aspects of Deregulation in the Market for Legal Studies (forthcoming); Love, J.H., Stephen, F.H., Gillanders, D.D., & Paterson, A.A., Deregulation and Price Discrimination in the Conveyancing Market, Mimeo, University of Strathclyde; Paterson, A.A., Farmer, L., Stephen, F.H. & Love, J.H., Competition and the Market for Legal Services, ***Journal of law and Society***, Vol.15, pp.361-373; Stephen, F.H., Love, J.H., Gillanders, D.D., & Paterson, A.A., Testing for Price Discrimination in the Market for Conveyancing Services, ***International Review of Law and Economics***, (Forthcoming)

48. The dead weight social cost argument - here the cost of advertising is simply passed on to the consumer as a new component of the cost of legal services . This is valid only under restrictive assumptions whereby there is totally inelastic demand and further, the existing level of productive efficiency is the optimum attainable.

49. Artificial product differentiation - here the competitive performance of the market is seen to be impaired since suppliers are seen as having non-comparable products. It does, however, make consumers more aware that alternatives in the market do exist. Because of the importance of reputation effects in legal services of many types, it is unlikely that primary advertising would have much effect. The result is that systematically unjustified supplier preferences would tend not to occur.

50. Unhealthy market concentration - the argument here is that only the largest firms can afford advertising expenditure and they will thus grow even bigger. This could result in fewer firms in affected legal market sectors but there would be little overall structural change. Due to the increased scale of production necessary, a further barrier to market entry could be established. Advertising appears to be aimed at local markets and hence, this may not be a significant worry. What does seem to be more significant is brand name loyalty where advertising may actually lower barriers to entry and act as a more efficient form of self-promotion than the current informal social intercourse/ network methods.

51. Potential for supplier induced demand - here, loss leader policies and manipulation of tastes etc. are voiced as a worry. Since demand is likely to be inelastic, this would not be much of a problem.

52. Price advertising would seem to be inappropriate in any case since most legal services are non-standardizable.

53. Deterioration of quality of services - it is proposed that increased price competition could cause high quality firms to be squeezed out of the market if they are incapable of signalling the superior quality of their services to their consumers. Consumer perceptions of quality are such that they preclude making a rational estimate as to whether quality would deteriorate or not in the presence of some form of price advertising.

54. The problem in this instance is that the reduction of prices would reduce margins from which lawyers can cross-subsidise work. It is not the case that lawyers have a moral or political mandate or any inherent advantage in performing this redistribution of wealth function.

55. Where price advertising does occur in an appropriate standardisable legal market segment, monitoring costs of the professional body in relation to service quality may be fairly modest. Potential increases in quantity demanded may facilitate and require alterations to improve productive processes possibly leading to enhancement of internal quality control mechanisms. These may be in the form of;

1. Increased specialisation.
2. Increased standardisation.
3. Greater emphasis on the monitoring processes.

Lawyer objections to standardisation.

Standardisation of services may be unattractive to many lawyers since it;

1. Offers substantially reduced rewards to those striving for intellectual challenge,
2. Removes the stimulus of complex problems and,
3. Removes the satisfaction of doing a job worthy of a professional person.

Consequently, it could be the case that legal clinics, if set up in the UK along lines such as those in USA to offer a set of standardised services, may only attract certain types of lawyer personnel.

56. This deficiency arises through a lack of both personal knowledge, and reputation evaluation ability.

57. In order to control production costs, an incentive is created to innovate in production. Price advertising, if successful, has the potential to generate sufficiently high volumes of business to justify high capital expenditure and training costs associated with production innovations.

In the case where several firms in a given market price advertised, the quantity of legal services demanded ceteris paribus could be expected to rise. As additional volumes of legal services are produced by firms to meet this increased demand, the cost of these services for any given firm could be expected to fall as fixed costs would be spread over a greater number of units. This would of course only be the case if economies of scale were not already exhausted. The extent of economies of scale in legal services is a moot point.

Traditional economic theory suggests that such economies of scale could be achieved in legal services as a result of one or more of the following;

1. Specialisation.

2. Labour input mix (ie. use of qualified assistants, paralegals etc.)

3. Alterations to client expectations as to the degree of personalised service to be provided.

It is expected that advertising should facilitate the normal forces of the market to operate efficiently on the delivery of legal services. There may be a consequent effect on supply methods, since average cost reductions should permit further price cutting and stimulation of extra demand.

58. The measurement of comparable quality in legal services is very subjective and problematic and it is unclear how it can be measured in both absolute and relative terms.

59. *supra* Note 41. at pp.154-155.

It is interesting to view the expected result of institutional advertising in the context of the concept of advertising noted by Telser, L.G., Advertising and Competition, Journal of Political Economy, Vol.72, No 6, (December) 1964, pp.540-541, where he argues that there is some theoretical reason to expect that competition to be stiffer in oligopolistic markets than in atomistically competitive ones. In the case where consumers regard the products of rival firms to be close substitutes, and individual firms are small in relation to market size, then a product may tend to be advertised less, because one firm's advertising expenditures will promote the product as much as it promotes the actual brand of the product of the advertiser. The advantages of advertising are thereby greatly reduced. This describes the situation that persists in legal services where the value of individual advertising to producers is frequently questioned as is the purpose of institutional advertising.

60. Given that the price elasticity of demand for many legal services is likely to be relatively inelastic, advertising may be unlikely to expand the demand for lawyers' services significantly. It may, therefore, simply have the zero-sum game effect of redistributing market shares of the total market demand between lawyers in a particular

market. When account is taken of the probable accompanying reduction in fees during this redistribution process, those lawyers in aggregate are likely to face a situation that is worse than a zero-sum game.

One thing is certain, that being the fact that those receiving revenues as a result of selling advertising space and services etc. will benefit from the overall process.

Some of the more problematic features of advertising expenditure are listed below;

1. It has a high initial cost,
2. It most often requires repetition to be effective and,
3. It's effects are often uncertain and effectiveness difficult, if not impossible, to ascertain.

61. This naturally assumes that law firm does not behave in any manner which would have the effect of discounting the value of the firm's reputation, as this would provide undesirable information to consumers, which would not be costless.

62. It is argued by Getzen (1984) that in situations where output is of highly variable quality and the cost of obtaining quality information is much greater for consumers than it is for producers, transactions are ideally governed in a relationship known as a 'brand name contract'. Consumers base their purchase decisions on reputation information and detectable lapses in service quality are penalised by losses of expected future business. See; Getzen T.E., A 'Brand Name Firm' Theory of Medical Group Practice, *The Journal of Industrial Economics*, Vol.XXXIII, No.2, Dec. 1984, pp.199-215 at p.200.

63. It is difficult to pin down price changes, for instance, following liberalisation in advertising rules, to any one factor as advertising is only one of many factors that affect price levels and the dispersion of fees in any market.

64. For a lengthy discussion of the role of Licensure in the legal profession see; Trebilcock, M.J. & Reiter, B.J., Licensure in Law. in Evans, W.G. & Trebilcock, M.J. (1987), *supra* Note 21.

65. *supra* Note 41.

66. For a discussion of the role that could be played by licensure in the context of formal speciality designations and formal segmentation of the legal services market see; Trebilcock (1987), *supra* Note 41, at pp.155-156.

67. These sources of information in addition to, and complementary to, advertising, are discussed elsewhere in this chapter.

68. See Trebilcock (1987), *supra* Note 41 at p.156, where it is argued that a wide spectrum of clients demanding legal services of differing sophistication in their abilities to both access and evaluate information, exists. Clients types are subsequently examined to assess the extent of their information deficiency.

In the case of large corporate clients it is argued that the selection process is relatively easy since particular lawyers will be needed for particular functions. Here there is a

good chance that the client will be a repeat user who may have developed methods to evaluate approximate quality. There is likely to exist an informal business communications network which will feed the client with reliable reputation information.

Many smaller corporate clients may more usually have a demand for less specialised services than larger corporate clients. They are likely to be fed from similar informal information sources. Although they will tend to have less need for specialisation of services, choice may be still relatively easy for this sector.

For many clients in the household sector, the information deficiencies are quite significant. A general lack of sophistication, lack of repeat purchasing and varied usage of a wide range of services when paired with a variety of lawyers, renders choice difficult.

69. See; Trebilcock (1987) *supra* Note 41. at p.158, where it is argued that arguments against liberalisation in advertising regulations are unpersuasive and wrongly founded, and it is claimed that information breakdowns impairing the client/ lawyer matching process are amenable to significant amelioration via relaxation of restrictions on lawyers' advertising.

70. See; Trebilcock (1987) *supra* Note 41. at p.158 where he also claims that it would not be advantageous for the law firm to specialise in the market for non-complex legal services if consumers merely chose on a random basis. The choice process is, therefore, not likely to be a random one for the private client as a consumer of legal services.

71. The typical consumer in the case of the majority of products is confronted with an abundance of relevant, and irrelevant, information to help evaluate purchase options in the pre-purchase phase of the purchase decision. A significant proportion of this information comes from direct and indirect advertising sources. In the case of an unliberalised advertising regime there is a deficiency of this potentially valuable product information available to clients This underpins the desire of proponents of liberalisation in advertising rules to create greater freedom in legal service advertising.

72. Proponents of advertising rule relaxation argue that such an act would enhance welfare by reducing information deficiencies in the market. As a result, consumers would be likely to reap twin benefits of reduced search costs and the ability to make a more rational selection of services through enhanced consumer awareness of market alternatives.

Opponents of advertising relaxation allege that advertising rule relaxation would,

1. Cause service quality to deteriorate,
2. Cause a spreading of misinformation,
3. Alter market structure undesirably.

It must be noted, however, that these opposing arguments are not terribly specific since they are concerned with advertising as a concept and, hence, ignore many different subtle facets of actual advertising.

73. In any discussion regarding liberalisation of regulation of legal service advertising it would appear appropriate to examine;

1. What benefits proponents of advertising rule liberalisation expect to accrue from liberalisation,
2. What the objections to liberalisation are and,
3. What actual information sources are available to the consumer of legal services and how these would be enhanced by liberalisation.

It is not the intention of this thesis to explore these issues as a burgeoning literature in the arena of regulation of the professions in general, and liberalisation of advertising rules regarding legal services in particular, serve this function. supra Note 40 .

74. It must be noted that they need not actually be a higher quality firm but they nevertheless have the ability to extract more producer surplus due to consumer misperception.

75. Hudec and Trebilcock (1982) *supra* Note 36. at p.67. It is claimed here that;

1. Clients may be made aware of the existence of legal problems of which they were previously unaware.
2. Clients may also lose misconceptions that have previously prevented them from seeking legal advice.
3. In reducing search costs, advertising may facilitate comparative shopping for routine standardised services and consequently improve legal market efficiency.
4. Advertising is relatively costless to the consumer, being typically embedded in entertainment media which is pleasurable to the reader/ viewer.

76. Hudec and Trebilcock (1982) *supra* Note 36. at p 67. It can, nevertheless, convey information such as academic background, years experience and specialisms etc. which may be perceived by potential clients as indicative of probable expertise.

77. In the absence of prior consultation with the client, the law firm could not accurately assess the probable cost of the work required.

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78. See; Hudec and Trebilcock (1982) *supra* Note 36. at p 67.

79. For a discussion on franchising see; Caves, R.E. & Murphy, W.F.II, Franchising: Firms, Markets and Intangible Assets, ***Southern Economic Journal***, Vol.42(4), April 1976, pp 572-586; Inaba, F.S., Franchising - Monopoly by Contract, ***Southern Economic Journal***, Vol.47(1), July 1980, pp 65-72; Blair, R.D. & Kaserman, D.L., Franchising - Monopoly by Contract: Comment, ***Southern Economic Journal***, Vol.48(4), April 1982, pp.1074-1079; Inaba, F.S., Franchising - Monopoly by Contract; Reply, ***Southern Economic Journal***, Vol.48(4), April 1982, pp 1080-1082; Klein, B. & Saft, L.F., The Law and Economics of Franchise Tying Contracts, ***Journal of law and Economics***, Vol.XXVII(2), 1985, pp.345-362; Mathewson, G.F. & Winter, R.A., The Economics of Franchise Contracts, ***Journal of Law and Economics***, Vol.28(3), Oct. 1985, pp.503-526.

80. Licensure and it's effectiveness as a quality/ reputation signalling mechanism is the focus of Trebilcock, M.J. and Reiter, B.J., Licensure in Law. in Evans, W.G & Trebilcock, M.J. (eds), **Lawyers and the Public Interest**. Toronto: Butterworth, 1987.

81. Advantages of group/ team practice has been a focus of economists seeking explanations beyond that of simple economies of scale, for the observed phenomena of large scale joint production (particularly in services). See; Newhouse, J.P., The Economics of Group Practice, ***Journal of Human Resources***, Vol.8, Winter 1973, pp.37-56; Alchian, A.A. & Demsetz, H., Production, Information Costs and Economic Organisation, ***American Economic Review***, Vol.62, Dec. 1972, pp.777-795.

In relation to private practice in the medical profession see; Getzen, T.E., A 'Brand Name Firm' Theory of Medical Group Practice, ***Journal of Industrial Economics***,

Vol.XXXIII No.2, Dec. 1984, where the concepts discussed are equally applicable to partnership practice of the legal profession in private practice.

In relation to the legal profession and partnership group production see; Gilson, R.J. & Mnookin, R.H, Sharing Among the Human Capitalists: An Economic Enquiry into the Corporate Law Firm and how Partners Split Profits, ***Stanford Law School Working Paper***, Vol.37 No.16, 1984.

82. *supra* Note 62.

83. The view of Getzen (1984) *supra* Note 62., echoes that of held by Williamson whereby, in the absence of transactions costs, the size of the organisation can be viewed as indeterminate as scale economies and diseconomies are argued to be a direct consequence of transaction costs. See; Williamson, O.E., **The Economic Institutions of Capitalism.** Free Press, 1985.

84. *supra* Note 62. at p.200

Here, Getzen acknowledges the strong dependence his analysis has on the transactions cost framework and the concept of the agency relationship. See in particular; Williamson, O.E. (1985),*supra* Note 1. for a summarised development of the Transactions Cost Framework and see both; Jensen, M.C. & Meckling, W.H., Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure, ***Journal of Financial Economics***, Vol.3, 1976, pp.305-360 and Fama, E. Agency Problems and the Theory of the Firm, ***American Economic Review***, Vol.76, 1980, pp.971-983 which are commonly regarded as the seminal works in agency theory.

In relation to the quality premium argument it is acknowledged that the important feature of the brand name services is that they are of consistent and homogeneous quality rather than that they are of high quality. Consumers are willing to pay differing quality premia for different brand names and it will be the case that the expectations of quality will be different across cases. So long as the supplier provides services that satisfy the expected quality of the purchaser of the brand name regardless of absolute quality the consumer will be satisfied.

85. Getzen, T.E. (1984) *supra* Note 62. This argument relies on consumers/ the market being efficient in evaluating reputation and discounting the values of firms' reputations for poorer than expected service quality. It is argued by Akerlof, G.A. (1970) that where consumers face an information deficiency in terms of being able to evaluate reputation and service quality, they will not be able to signal quality premia to consumers as consumers will not be able to perceive differential quality levels in the market. See Akerlof, G.A., The Market for Lemons - Quality Uncertainty and the Market Mechanism, ***Quarterly Journal of Economics***, Vol.90, August 1970, pp.488-500.

86. This is to a large extent dependent upon the receptiveness and ability of consumers in the market to process such reputation information. It will be remembered that imperfections in the real life market for legal services are likely to result in consumers selecting lawyers in the face of deficient and incorrect information.

87. See; Klein, B. and Leffler, K., The Role of Market Forces in Assuring Quality, ***Journal of Political Economy***, LXXXIX (August), 1981, pp.615-641.

88. Getzen, T.E. (1984) *supra* Note 62. at p.201.

89. Reputation and brand name of the firm is not a mobile asset and may only present a lawyer leaving the practice with a relatively small residual effect. This residual effect may be of greater significance to another firm who is interested in hiring him, than to clients. To this extent, brand name capital may act as a disincentive to leave the firm and therefore constrain the behaviour of members of the firm accordingly.

Legal practice in firms of more than two lawyers could be argued to be more effective at creating brand name capital as the lawyer can benefit from both internal sources from colleagues, and external sources from clients, in significant quantities. Hence, the creation of brand name capital may be easier and cheaper in practices consisting of more than one lawyer.

90. Getzen, T.E. (1984) *supra* Note 62. It is argued here that the process of sharing clients and income provides an incentive for the existing members of the firm to hire good quality new members and also devote time and resources to monitoring them, in order that the firm remains a thriving venture. Additionally, this provides clients with a guarantee or signal that the quality of service provided by the new member will at least meet expected quality standards.

It is interesting to note the similarity of Getzen's analysis to that of Gilson, R.J. & Mnookin, R.H. (1984) *supra* Note 81, where the concept of the trade-off between creation of lawyer specific and firm specific capital is a major focus of analysis. This transfer of clients could result in problems for the firm in terms of it providing lawyers with specific capital which could provide them with a hostage to act opportunistically against the firm and it's existing partners. Gilson and Mnookin's analysis explores the nature of incentives and behavioural implications of the subtleties of the type of sharing bargain existing between the partners of the law firm.

The fact that established partners are compensated for their shares in brand name capital by receiving a disproportionate share of the law firms income, in relation to new entrants into the practice is an interesting observation in the context of Gilson and Mnookin's analysis of partnership income division. New partners will be willing to receive rewards of this nature as firstly, they will receive clients and share in reputation/ brand name immediately, and secondly, they will know that in future years they will be receiving a disproportionately high level of income as they transfer clients and the business down to new members of the firm.

91. New partners may require to 'buy-into' the partnership and this could be seen as a payment to the firm (ie. existing members) for a share in brand name capital.

92. For a discussion of the function of licensure at the macro level of the profession see, Trebilcock, M.J. and Reiter, B.J., (1987) *supra* Note 21.

Getzen, T.E. (1984) *supra* Note 61., therefore, argues that any lapse in quality affects all of the partners. This view may be in certain circumstances over-simplistic.

Firstly, this assumes that consumers will be able to identify quality in the first instance and evaluate actual quality against expected quality. Thus, perhaps rather naively, implicitly assumes a high degree of client sophistication which may be unlikely for many consumers.

Secondly, in addition to the fact that poor quality services may go largely undetected for reasons directly above, the lawyer who acts to provide a sub-standard product, may go undetected by his partners depending on their monitoring capabilities. The 'guilty' lawyer may also yield personal benefits if he has provided low effort intensity completing the poor quality service for essentially the same rewards.

93. Getzen, T.E. (1984) *supra* Note 61.

94. Getzen, T.E. (1984) *supra* Note 61. at p.202.

95. Getzen, T.E. (1984) *supra* Note 61. at p.202. It is not clear exactly what Getzen means here by independent perpetual identity. If it is intended that this relates to perpetual succession, then surely it is the case that the reputation of the firm stems from the lawyers who provide the service in the firm. Perpetual succession, which relates to the transferability of assets between successive generations, is irrelevant, since the asset in question is the brand name which is not transferable.

It could, however, be that what is intended is simply a brand-name for the firm which does not change as the firm's members come and go through time. It is more likely that this is the interpretation intended and, in this respect, the maintenance of law firm names that bear no resemblance to their constituent members' names, may be evidence of real life law firms' attempts to ameliorate the brand name reputation problems highlighted by Getzen.

96. Getzen, T.E. (1984) *supra* Note 61. at p.202. This argument draws on Alchian & Demsetz, *supra* Note 81.

Although it is argued here that the consumer disregards the internal effects of differences in quality between practitioners, one interesting aspect from the firm's perspective is the resultant implications for members of the firm, where blame can be assigned through mutual monitoring and penal systems within the firm.

97. Getzen, T.E. (1984) *supra* Note 61. at p.202.

98. See the beginning of this section of Chapter Four.

99. Getzen, T.E. (1984) *supra* Note 61. at p.202.

100. Getzen, T E. (1984), *supra* Note 61. at p.202. In terms of the Gilson and Mnookin (1984) analysis, *supra* Note 81. transferability of clients takes on a more strategic role, as there are argued to be wider considerations for the lawyer. Implicitly, Getzen assigns a kinder character to the typical firm member than do Gilson and Mnookin, who view them as more strategic and opportunistic.

101. Getzen, T.E. (1984), *supra* Note 61. at p.203. Here, it is argued that the group practice performs a function analogous to a department store whose reputation is utilised as a guarantee of the quality of any product bought regardless of type.

102. Getzen, T.E. (1984), *supra* Note 61. at p.203. In relation to Getzen's analysis of group medical practice, he argues that groups are less likely to be formed where quality is more easily measured be patients. Furthermore he argues that groups will tend to specialise in areas in which they have a comparative advantage relative to solo practitioners, that is in technical (physician evaluated) quality rather than bedside manner (patient evaluated) quality.

He further argues that the value of brand name, and hence the advantages of group practice rises (and indeed the advantage of large relative to small group practices rises) with increases in; 1) the cost of search, 2) the value of outcome differences, 3) the variability of outcomes, 4) infrequency and variability of disease occurrence, 5) jointness in production, 6) producer and/ or consumer turnover (mobility) and 7) technical (as opposed to bedside manner) quality.

Striking parallels are obviously apparent in relation to the practice of the legal profession, when viewed in terms of Getzen's analysis above.

103. A franchise operation can be regarded as a nexus of contracts in which each of the franchised firms hold contracts with the franchiser/ brand name firm. Relative to each other, each of the franchised firms are legally separate, though they share the common feature of being contractually tied to the franchiser. It is noted by Ricketts, M., **The Economics of Business Enterprise: New Approaches to the Firm**. Wheatsheaf, 1987, that Rubin, P.H., The Theory of the Firm and the Structure of the Franchise Contract, ***Journal of Law and Economics***, Vol.21, 1978, at p.225 that this combined closeness and independence served to emphasise the often arbitrary nature of the distinction between inter and intra-firm transactions, thereby reinforcing the notion that the firm has blurred boundaries. See also Note 93.

104. For a discussion of the principal and agent relation in the context of internal structure of the firm with particular focus on franchise contracts see; Ricketts, M. (1987) *supra* Note 103.

105. This type of operation is very interesting from an economic viewpoint as many interesting theoretical questions are raised, such as how the large London firm selects firms with whom it wishes to be associated (ie. franchisees), how does this firm check the quality of their work to ensure their reputation is not being damaged by their association with such firms?, how does the partnership agreement work?, how formal is the arrangement?, how independent do the firms remain? to name but a few. These issues, however, are not strictly among those covered by this thesis, but nevertheless are worth mentioning at this juncture.

106. This is essentially analogous to the locking process resulting from transaction specific characteristics, in this case human asset specificity. A well matched team can evolve, whose success is the result of a complex network of inter-relationships, with the creation of attendant high levels of brand name capital. See; Williamson, O.E. (1985), *supra* Note 1., for a description of the role of asset specificity, as one of the three key dimensions of the transactions cost framework (the other two being uncertainty and frequency). Williamson arguably views asset specificity as the most important and distinctive of the three key dimensions of his framework.

-Chapter Five-

Empirical Analysis of the organisation of relationships between lawyers and clients:

Section One: Questionnaire Section Two - The client/ firm relationship:

Introduction:

The function of this chapter is to examine and analyze information gathered during the series of interviews conducted for the empirical survey relating to the organisation of relationships between lawyers and clients. In doing so the background literature outlined in the previous chapters of this thesis and issues raised therein will provide the framework within which these issues are analyzed.

This chapter will focus specifically on section two of the questionnaire as this deals with the features thought to be important in relationships between clients and law firms. The aim of this chapter is to discover the true nature of the typical client/ firm relationship and test a number of propositions relating to the information deficient characteristics of this relationship suggested by theory discussed in previous chapters.

1.1 Information asymmetry and uncertainty - relational contracting:

It is recalled from discussion in earlier chapters that the lawyer/ client relationship is surrounded by vast information asymmetries in favour of the firm, inducing potentially high levels of uncertainty in the client. In view of the high levels of uncertainty created by information deficiency, Williamson (1985) would predict that the transaction should be sheltered within some form of relational contract [1]. It could be expected that such a contract would require that there was sufficient repetition to facilitate creation of a bilateral monopoly type relational contract. Even where there was very infrequent repetition, Williamson (1985) would argue that the attendant levels of uncertainty would make the option of returning to the same law firm preferable to returning to the market for each transaction [2]. This of course assumes that the client is satisfied with previous service he has received from the firm. It will be recalled that this will tend to be the case since his range of experience of legal services is unlikely to be extensive enough to compare the quality of this service to previous service received from that firm, or from another firm.

(I) Dual party benefits of relational contracting:

Williamson (1985) would predict within his contractual framework that a relational contract between client and firm would be typically established [3], the benefits of which could be expected to be shared between the firm and the client. The benefits to the client are that the relationship created should place the firm in an advantageous position (in relation to that

client) over other firms for future services that the client may require. The benefits to the client should be reduced transactions costs, reduced search costs, reduced levels of uncertainty and reduction in speed of exhaustion of the bounds of rationality.

The role of the firm in respect of actions taken to create this bilateral monopoly is examined within this section. If it successfully creates this relational contract, the firm will benefit, firstly, from repeat business from that client and, secondly, potentially from that satisfied client referring the firm to other would-be clients.

Given the obvious value of the relationship to the firm, the firm could be expected to invest time and other resources in its creation. In this context, the emphasis of the firm will shift towards discovering as much about the client as possible to signal to the client its interest in providing personal service and the extent of the loss which would arise from termination of the relationship. The firm will also wish to stress the long term nature of relationships it wishes to create to signal to the client that it will not act opportunistically against him. The firm, in essence, will desire to use its client information advantage to heighten the typical client's inertia within a present relationship.

(II) The use of client information to create a relational contract:

The firm's use of client specific information will be examined in the above context. Information could be expected to;

1. Signal to the client that the firm has made investments in creating the relationship and that it will, thereby, be in a better position to satisfy the client's legal service requirements than competing firms.

2. Signal to the client that the firm, by wishing to discover this information, desires to encourage a long term relationship with the client.

3. Thereby reduce the potential for opportunism which would breach the trust relationship thus created. Here, the firm would stand to lose the value of that client's future requirements for legal services and any potential referrals the client would have otherwise made.

(III) First mover advantages and high cost termination:

Williamson (1985) would suggests that an incumbent firm will enjoy first mover advantages over other firms in relation to that client [4]. Additionally, it could be expected that client information would also be utilised to attempt to sustain the relationship which would have a

high cost of termination to both client and firm. In this respect the firm may attempt to feed the client with information regarding other services that the firm can offer, to preempt other firms attempting to provide such information to the client first.

(IV) Quality signalling to reduce clients' uncertainty:

This section also attempts to discover what signals of quality the firm believes are perceived by consumers in their evaluation of law firm reputation (both in relation to current clients attempting to evaluate the service they are receiving, and prospective clients attempting to evaluate the firm when selecting a lawyer). In this regard, Williamson (1985) would argue that the firm would attempt to provide the client/ prospective client with any form of information which could reduce the information impactedness and, therefore, uncertainty of the client [5].

(V) The viability of opportunism in relational contracts:

High levels of information impactedness in the law firm and high levels of client uncertainty, paired with the complexity of the transaction from point of view of the boundedly rational client, appear to characterise an ideal setting for opportunistic behaviour against the client by the firm. It is not, however, in the interests of the firm to be opportunistic since its long run viability and survival depends to a large extent on repeat business and referrals as its life=blood.

Poor performance on the part of the law firm could be expected to result in termination of the contract. It is near impossible for the majority of typically unsophisticated clients to grade the performance of the law firm in rendering the services required either pre or post consumption. The firm must, therefore, attempt to signal to the client the quality of the service it can provide. After a client relationship has been instigated, the firm must then convince the client that good quality service has been delivered. All the firm can do in this respect to assure quality to clients (both pre and post consumption) is to simply claim that only good quality service is provided by the firm. The client must entirely trust the firm to remain be true to its word. The client must trust the firm, firstly, that it will perform services to the expectations/ specifications of the contract and, secondly, that after services have been rendered, the contract specifications have been fulfilled.

(VI) The overriding influence of trust in the client/ firm relationship:

The nature of the relationship between client and firm is very much governed by high degrees of implicit trust. In this respect, Williamson (1985) stresses the desirability of repeat business and its function in constraining one shot opportunism on the part of the firm supplying the

services [6]. The client must trust the firm not to act opportunistically, where the potential loss to the firm of abusing client trust acts as a credible commitment to the client that the firm will not act in such a manner [7].

To summarise, the argument Williamson (1985) uses to underpin all of the above is that, in any transaction, the emphasis must be to create a method of governing the transaction which reduces uncertainty and complexity and economises on bounded rationality [8]. In the case of the lawyer/ client relationship, it could be expected that bounded rationality interacting with high degrees of complexity and uncertainty would create an ideal forum for opportunistic behaviour. Williamson (1985) advocates the sheltering of such a situation within a long term relationship, with contractual repetition as a method of precluding opportunistic behaviour [9]. The next section of this chapter will outline a number of propositions concerning relational organisation of the lawyer/ client relationship. These will be tested to discover whether this long term relational view does characterise the client/ firm contract in real life, and whether the relationship is characterised by high levels of implicit trust.

Section Two: Client/ firm Relationship Hypotheses:

Below are the specific hypotheses concerning the characteristic features of the client/ firm relationship, drawn from theory outlined in this and previous chapters, and which will be tested in this thesis:

Hypothesis 1: The firm will attempt to create a long term relational contract with the client and will do so by using client information.

Hypothesis 2: The relationship created will have benefits to both client and firm.

Hypothesis 3: Firms who are already in a relational contract with a client will have first mover advantages over other firms in relation to that client resulting in a bilateral monopoly.

Hypothesis 4: Clients will tend to return to the incumbent firm rather than return to the market due to relation specific advantages that reduce uncertainty for the client.

Hypothesis 5: The firm will attempt to preserve the relationship created as it has a high cost of termination to both parties.

Hypothesis 6: Law firms will attempt to signal quality and reputation to their own and prospective clients as this will reduce client uncertainty.

Hypothesis 7: Law firms will attempt to emphasise personal service and the importance of the

client as this will imbue the client with trust in the firm.

Empirical information derived from questions in section two of the questionnaire will be used to indicate whether the responses of sample firms are consistent or inconsistent with the above hypotheses driven by Williamson's views on relational contracting.

Section Three: Empirical Investigation of the client/ firm relationship.

3.1 Use of standard documents and procedures:

Where firms used standard documents and procedures etc. the benefits summarised in the following table were alleged to accrue.

It is recalled from Chapter Two (TABLE 2.9) that 31 firms used standard documentation to a greater or lesser extent in many if not all transactions. The 2 firms that did not use them, plus one other firm that did not provide information in this section, are recorded as missing values. The use of standard documentation and procedures etc. was overwhelmingly argued to result in lower prices to the client as indicated by 28 of the firms 28 of the 30 remaining firms. No firms indicated that the use of standard documents resulted in higher prices to the consumer, and this is what could be expected. The 2 firms who did not indicate price reductions following use of standard documents did, however, indicate other benefits accruing from their usage.

(TABLE 5.1)

Firm No.	LOWPRICE	HIGHPRICE	HIGHEFF	PROFITUP	FIRMBEN	NECCOMP	MUTBENS
1,2,3,5,8,16, 17,27,28,30,31, 32,33 (13 Firms=39.4%)	Yes	No	Yes	No	No	No	Yes
12,19,21,23,25, 26,29 (7 Firms=21.2%)	Yes	No	Yes	No	No	Yes	Yes
7,14,15,20,24 (5 Firms=15.2%)	Yes	No	No	No	No	No	No
22 (1 Firm=3.0%)	No	No	Yes	No	No	No	Yes
6 (1 Firm=3.0%)	No	No	Yes	Yes	Yes	No	No
4 (1 Firm=3.0%)	Yes	No	No	No	No	No	Yes
18 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No
9 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	No	Yes
10,11,13 (3 Firms=9.1%)	M	M	M	M	M	M	M
TOTAL FIRMS	28	0	24	2	1	7	23
%age FIRMS	84.8	100	72.7	6.1	3.0	21.2	69.7

M-Missing value)

Description of variables:

LOWPRICE-Use of standardised documents results in lower price to client

HIGHPRIC-Use of standardised documents results in higher price to client

HIGHEFF-Use of standardised documents results in higher efficiency to firm

PROFITUP-Use of standardised documents increases firm profit margins

FIRMBEN-Use of standardised documents results in benefits to firm only

NECCOMP-Standardised documents are necessary to compete nowadays

MUTBENS-There are mutual benefits from using standardised documents

13 firms believed that the use of standard documents resulted not only in lower prices to the

client but the firm also enjoyed increased efficiency, and overall there were mutual benefits from using them. A further 7 firms additionally indicated that the use of standard documents was necessary in order to compete effectively in today's market for legal services. 5 firms provided no additional information other than the fact that the usage of standard documents resulted in lower prices to clients. Of the 2 firms that indicated using standard documents did not alter price to clients, 1 revealed that their use merely increased the efficiency of the firm and was mutually beneficial to client and firm, and the other viewed their use as increasing efficiency and profit margins within the firm and exclusively benefitting the firm.

The remaining firms were unique in their responses. One noted that in addition to lower client prices there were mutual benefits to firm and client from using standard documents, and another firm, in addition to lower prices, noted higher efficiency for the firm. The final firm disclosed that standard documents, as well as reducing prices to clients, increased efficiency and profit margins and resulted overall in mutual benefits to client and firm.

3.2 The firm and its use of client information:

The sample firms were questioned on their use of client information and its usefulness. The table below summarises their responses. It is anticipated that what will become apparent is the long term relational nature of the typical client/ firm contract.

(TABLE 5.2)

Firm No.	DATA BASE	CLI PROF	LTD INFO	INFO USE	LTD USE	XSELL	FUTX SELL	DEP TYPE	FUT INFO
11 (1 Firm=3.0%)	No	No	Yes	No	No	No	No	No	No
6,7,8,15 (4 Firms=12.1%)	No	No	Yes	Yes	No	No	No	No	No
20,21,23,24 (4 Firms=12.1%)	Yes	No	No	Yes	No	Yes	Yes	No	Yes
4,22,30 (3 Firms=9.1%)	Yes	No	No	Yes	No	Yes	No	No	No
14,17 (2 Firms=6.1%)	Yes	No	No	Yes	No	No	No	No	No
3,13 (2 Firms=6.1%)	Yes	No	No	Yes	No	No	No	No	Yes
12,31 (2 Firms=6.1%)	Yes	No	No	Yes	No	No	Yes	No	Yes
5,26 (2 Firms=6.1%)	Yes	No	No	Yes	No	Yes	No	Yes	Yes
25,27 (2 Firms=6.1%)	Yes	Yes	No	Yes	No	Yes	Yes	No	Yes
16 (1 Firm=3.0%)	Yes	No	No	Yes	No	No	No	Yes	No
19 (1 Firm=3.0%)	Yes	No	No	Yes	No	Yes	No	Yes	No
28 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	No	Yes	Yes	Yes
2 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	No	No	No
33 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No	No	No
29 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	Yes	Yes	Yes
1,18 (2 Firms=6.1%)	No	No	Yes	No	Yes	No	No	Yes	No
10 (1 Firm=3.0%)	No	No	Yes	No	Yes	No	No	No	No
9 (1 Firm=3.0%)	Yes	No	No	No	Yes	No	No	No	No
32 (1 Firm=3.0%)	Yes	No	No	No	Yes	No	No	Yes	No
TOTAL FIRMS	25	4	9	27	5	14	10	9	14
%age FIRMS	75.8	12.1	27.3	81.8	15.2	42.4	30.3	27.3	42.4

Description of variables:
DATABASE-Client database used
CLIPROF-Client profiles used
LTDINFO-Limited client information kept
INFOUSE-Client information useful for selling other services to client
LTDUSE-Client information of limited use for selling other services to client
XSELL-Information used to cross-sell services to clients
FUTXSELL-Need to cross-sell in future/ cross-sell more in future

DEPTYPE-Use of client information depends on client and work type
FUTINFO-Greater role in future for client information and its use

In 27 of the 33 firms it was indicated that client information was useful in providing that client with other services. In 5 firms the usefulness of information held on clients was viewed as only limited. In only one firm was it the case that client information was not even assigned limited usefulness in this respect. Consequently, this firm indicated that it kept very limited client information.

(I) Firms who found client information useful in providing other services - further breakdown:

Within this group of 27 firms, 4 provided information that, while they found it useful, they kept only limited client information. 4 firms did, however, disclose that they operated a client database and used this to actively cross-sell services. Additionally, they envisaged a requirement to cross-sell more in the future and foresaw a greater role for client information in the future.

Another 3 firms also operated a client database and used it to actively cross-sell services. 2 firms only indicated that they operated a client database whilst another 2 firms indicated this plus the fact they envisaged a greater role for use of client information in future. A further 2 firms supplemented the information provided by the last 2 firms by indicating they would be attempting to cross-sell more in the future.

2 firms disclosed the existence of a database in their firms used to attempt to cross-sell services, also indicating the extended role for client information in the future. In both of these firms it was also the case that the usefulness of client information held was dependent on client and work type.

Another 2 firms revealed their use of client databases and their attempts to cross-sell services, but in these firms client profiles were used to further enrich client information. These firms also foresaw an increased role for client information, and a greater need to cross-sell services, in future.

The remaining firms all uniquely categorised their responses in respect of the use of client information. One firm disclosed that it used a client database, but the extent to which it found information it held useful was dependent on client and work type. Another firm duplicated this response except it also actively attempted to cross-sell services. 1 firm that indicated that it used a database admitted that it kept only limited information and found the usefulness of information to be dependent on client and work type. This firm also envisaged a greater role for client information and its use in future and also disclosed that it would have to cross-sell

more in future.

The remaining 3 firms all used client databases and client profiles to supplement information held on clients. 2 of them mentioned that they actively cross-sold services to clients with 1 of them indicating that the usefulness of client information was client and work type dependent. This firm also envisaged an extended role for client information and a necessity to increase cross-selling in future.

(II) Firms who found information to be of limited use in providing clients with other services - further breakdown:

3 of these 5 firms indicated that they only kept limited information on clients with 2 arguing that its usefulness was determined by client and work type. The other 2 firms both maintained client databases with one of these firms indicating that usefulness of information held is dependent on service and client type.

In this section, evidence has been provided which confirms that the typical firm values client information and attempts to utilise it to; (1) Create a personal client relationship and, (2) sustains and preserve the relationship and emphasise its long term nature.

Firms generally accepted the importance of keeping and using client information to create a long term client relation. Cross-selling was also seen by many firms as an important exercise in this direction. Further, firms typically perceived that client information and its use is likely to become more important in future and that the need to cross-sell services is increasingly important in maintaining the client relationship. This is particularly true in view of the fact that many firms complain that clients are much more demanding and price sensitive, and therefore more mobile between firms, than previously. This has resulted in firms having to fight harder to preserve relationships with clients.

All of the above information can be seen as consistent with Hypothesis 1, which states that the firm will attempt to create a long term relational contract with the firm and will do so by using client information.

3.3 First mover advantages over other firms in relation to established clients:

The table below is a summary of the combinations of responses of the sample firms in relation to first mover advantages accruing to the firm in an established client relationship;

In all but 2 of the firms there was perceived to be an advantage over other firms derived from the holding of client information and being in an established relationship. Of these 2

dissenting firms, 1 perceived no advantages at all and the other only very limited informational advantages over other firms. Of the 31 firms that indicated that client information provided an advantage over competing firms in respect of that client, 5 perceived only limited advantages and 6 reported that the extent of the informational advantage depended on the nature of the client.

(TABLE 5.3)

Firm No	ADV COMP	DEP CLIEN	LTD ADV	REL ATE	CLI BEN	CON FID	TIM MON	SEAR CHAV	KNOW LED	OTHER
4,8,9,12,17										
(5 Firms=15.2%)	Yes	No	No	Yes	Yes	Yes	Yes	No	Yes	No
19,20,22,23										
(4 Firms=12.1%)	Yes	No	No	Yes	No	No	No	No	Yes	No
21,26										
(2 Firms=6.1%)	Yes	No	No	Yes	No	No	No	Yes	Yes	No
2,13										
(2 Firms=6.1%)	Yes	No	No	Yes	Yes	Yes	No	No	Yes	No
14,29										
(2 Firms=6.1%)	Yes	No	No	Yes	Yes	Yes	Yes	Yes	Yes	No
11 (1 Firm=3.0%)	No	No	No	No	No	No	No	No	No	No
10 (1 Firm=3.0%)	No	No	Yes	No	No	No	No	No	No	No
28 (1 Firm=3.0%)	Yes	No	No	No	No	No	Yes	Yes	Yes	No
7 (1 Firm=3.0%)	Yes	No	No	Yes	No	No	Yes	No	Yes	No
30 (1 Firm=3.0%)	Yes	No	No	Yes	No	Yes	Yes	No	Yes	No
31 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	No	No	No	Yes	No
33 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	No	Yes	No	Yes	No
1 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No	No	No	No
15 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	Yes	No	No	No
3 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	Yes	No	Yes	No
32 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	No	No	No	Yes	No
18 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	No	Yes	No	Yes	No
25 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	No	No	Yes	No
6 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	Yes	No	No	No
5 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	Yes	No	Yes	No
27 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	Yes	Yes	Yes	No
16 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	No	No	Yes	No
24 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	Yes	No	Yes	No
TOTAL FIRMS	31	6	6	27	13	13	18	6	28	0
%age FIRMS	94.0	18.2	18.2	81.8	39.4	39.4	54.5	18.2	84.8	0

Description of variables:
ADVCOMP-Client information provides advantage over competition in respect of that client
DEPCLIEN-Informational advantage depends on client
LTDADV-Any informational advantage is very limited
RELATE-Informational advantage of relationship established
CLIBEN-Client benefits from information being held
CONFID-Benefits to client of trust & confidence in firms abilities
TIMMON-Benefits of time saving so money saved for client
SEARCHAV-Client benefits from avoidance of need to search for other lawyer
KNOWLED-Knowledge based advantages over other firms

28 firms in total disclosed that holding client information produced knowledge based advantages for the holding firm over competitors. 27 firms indicated that the relationship established by using client information secured an advantage for the firm over competing firms. This is indicative that firms generally perceive advantages accruing to both firm and client in an established relationship which would be lost or wasted if the client went outwith this firm to the market for legal services.

Of the firms interviewed, 13 indicated that benefits to the firm of holding information did not solely accrue to the firm and that clients also benefits from the holding of information. The advantages perceived to accrue from the holding of information were as follows; 13 firms noted that the holding of client information produced confidence and trust in the client in relation to the firm's abilities. This would provide the firm with an advantage over other firms who would have to work at building trust in what would be to them a new client who was a

complete stranger. 18 firms indicated that holding client information resulted in time savings to the client due to familiarity and 'gears of the relationship being already oiled', reducing costs and fees charged to clients. 6 firms saw holding information as obviating the clients requirement to search in the market for a lawyer, thus reducing client search costs.

The information above appears to be strongly supportive of both hypothesis 2 and 3. It is demonstrated above that the relationship created will;

1. Typically have benefits to both client and firm (affirming Hypothesis 2.) and,
2. That firms who are already in a relational contract with a client will have first mover advantages over other firms in relation to that client, resulting in a bilateral monopoly (offering support to Hypothesis 3.).

3.4 Repetition of client business and client loyalty:

Hypothesis 4. contends that clients will tend to return to the incumbent firm rather than return to the market due to relation specific advantages which reduce client uncertainty. It has been demonstrated above that the client/ firm relationship is characterised by relationship based advantages which are indicative of the desirability, to both client and firm, of remaining locked in long-term contract with each other. It, however, remains to be seen whether clients actually do return to take advantage of the relational contract. Evidence will be examined below which facilitate evaluation of the validity or otherwise of Hypothesis 4.

The table below summarises the firms' responses in relation to the question of firm loyalty and repetition of business;

(TABLE 5.4)

Firm No	COMMCLI	PRIVCLI	STEPRED	LESSLOY	SPECSERV
2,6,11,15,18,20,23,26,27 (9 Firms=27.3%)	Yes	No	No	No	No
4,5,7,12,16,17,19,29 (8 Firms=24.2%)	Yes	Yes	No	No	No
14,30,31 (3 Firms=9.1%)	Yes	No	Yes	No	No
3,9,28 (3 Firms=9.1%)	Yes	Yes	Yes	No	No
22,33 (2 Firms=6.1%)	Yes	No	No	Yes	No
24,25 (2 Firms=6.1%)	Yes	No	Yes	No	Yes
21 (1 Firm=3.0%)	No	No	No	No	Yes
10 (1 Firm=3.0%)	No	No	Yes	No	No
8 (1 Firm=3.0%)	No	Yes	Yes	Yes	No
32 (1 Firm=3.0%)	Yes	No	No	No	Yes
13 (1 Firm=3.0%)	Yes	No	Yes	Yes	No
1 (1 Firm=3.0%)	Yes	Yes	No	Yes	No
TOTAL FIRMS	30	13	11	5	4
%age FIRMS	90.9	39.4	33.3	15.2	12.1

Description of variables:
COMMCLI-Commercial clients provide predictable flow of work
PRIVCLI-Private clients provide predictable flow of work
STEPRED-Repeat work is steady but not predictable
LESSLOY-Clients are generally less loyal than before
SPECSERV-Clients use us for specific specialist services so not much repeat work

30 firms disclosed that established commercial clients tended to provided a fairly predictable

flow of repeat work, with 13 firms indicating the same to be true of private clients. Of these firms, 12 reported that both categories provided a predictable flow of repeat work.

Of the firms that enjoyed predictable repeat work from either or both client categories, 10 preferred to describe repeat work as 'steady' rather than 'predictable'. The important point established in this section, however, is that clients do tend to return to firms indicating that the alleged benefits of continuing the relationship do exist. Hence, the client/ firm relationship is characterised by long-term repetition of business.

Of the 2 firms that indicated business tended not to be of a repetitive nature, either for private or commercial firms, 1 firm indicated that this was due to the fact that clients tended to use the firm for specific specialist services. The other simply said that any repetition of work for clients was at best very unpredictable (and only possibly steady) and it viewed neither private nor commercial clients as a reliable source of repeat work.

Of the 4 firms that indicated clients used their firms for specific services (reducing levels of repeat work), 3 firms, nevertheless, indicated that repeat business was a feature of their relationships with either private or commercial clients.

Finally, 5 firms complained that clients were generally less loyal to the firm than before but thankfully this category of client remained at present in the minority. This would become more worrying if the trend increased in the future. Typically firms reported that where clients went to another firm, due to price undercutting, they would often return to the original firm at a later date. Firms generally argued that clients were much more price sensitive than was previously the case and that, since client expectations were much higher, it was more difficult to retain clients than ever before. Firms required to spend much more time attempting to satisfy these heightened client expectations in order to increase chances of preserving relationships.

The above information is clearly supportive of Hypothesis 4. as it is generally the case that firms will tend to come back to the incumbent firm rather than return to the market. Information derived from TABLE 5.3 of the previous section is viewed as supporting the second part of the hypothesis - that the reason for clients preferring to do so is due to the existence of relation specific advantages that reduce uncertainty for the client.

From TABLE 5.4 it is also apparent that commercial clients are more likely to return more regularly to the firm, this most probably due to the ongoing nature of many types of commercial work with more frequent dealings with the law firm more probable.

3.5 Preservation of the client relationship:

Firms were asked to reveal their probable reaction to a hypothetical situation whereby a long established client informed the firm of his intention to in future use the services of another firm. It was anticipated that this would provide;

1. An indication of the value of the typical client relationship established by the firm and,
2. Information regarding the firm's strategy in attempting to retain clients.

The following table presents information gathered to probe these issues;

(TABLE 5.5)

Firm No	RETAIN	TOOLATE	BEYCONTR	DISCREAS	PATCHUP	CLIMEET	PREVCURE	AUDIT	OTHER2
3,6,12,26,27,32 (6 Firms=18.2%)	Yes	No	No	Yes	Yes	Yes	No	No	No
5,21,25,29 (4 Firms=12.1%)	Yes	No	No	Yes	Yes	Yes	Yes	No	No
2,4,9 (3 Firms=9.1%)	Yes	No	Yes	Yes	Yes	Yes	No	No	No
22,30 (2 Firms=6.1%)	Yes	No	No	Yes	No	No	No	No	No
20,31 (2 Firms=6.1%)	Yes	No	No	Yes	No	Yes	No	No	No
8,14 (2 Firms=6.1%)	Yes	No	Yes	Yes	Yes	Yes	Yes	No	No
23,24 (2 Firms=6.1%)	Yes	Yes	Yes	Yes	No	Yes	Yes	No	No
11,13 (2 Firms=6.1%)	Yes	Yes	Yes	Yes	Yes	Yes	No	No	No
33 (1 Firm=3.0%)	Yes	No	No	No	Yes	Yes	No	No	No
18 (1 Firm=3.0%)	Yes	No	No	Yes	No	Yes	Yes	No	No
7 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	No	No	No	No
16 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	No	No	No	No
19 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	No
28 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No
1,10 (2 Firms=6.1%)	No	No	Yes	Yes	No	No	No	No	No
15 (1 Firm=3.0%)	No	No	No	Yes	No	No	No	No	No
17 (1 Firm=3.0%)	No	No	Yes	No	No	No	No	No	No
TOTAL FIRMS	29	7	16	31	21	25	11	1	0
%age FIRMS	87.9	21.2	48.5	93.9	63.6	75.8	33.3	3.0	0

Description of variables:
RETAIN-Attempt to retain client
TOOLATE-Too late to save so often cannot retain
BEYCONTR-Often leave for reasons beyond our control so cannot retain
DISCREAS-Discover reasons for leaving
PATCHUP-Attempt to patch-up any differences
CLIMEET-Seek meeting with client to discuss problem and possible remedy
PREVCURE-Prefer to prevent rather than cure
AUDIT-Regular client audits to prevent breakup from becoming possible
OTHER2-Other

29 of the 33 firms revealed that they would attempt to retain the client and preserve the relationship with the remaining 4 indicating that they would not.

(I) Firms who would not attempt to retain a client who had decided to leave - further breakdown:

Of the 4 firms indicating this to be their probable reaction to a client leaving the firm, 1 firm noted that often the client deciding to leave was beyond their control (eg. takeover of local firm who will use their own law firm), another firm indicated that it would wish to discover the reason why the client decided to leave, and 2 firms indicated both of these responses.

(II) Firms who would attempt to retain a client who had decided to leave - further breakdown:

Within this group of 29 firms, the following information was forthcoming. 7 firms indicated that by the time a client announces his intention to leave (if in fact the firm is actually informed) it is too late to attempt to rescue the relationship. 13 firms disclosed that clients often left for reasons beyond their control but in 28 cases, firms indicated that they would seek to discover the reason for leaving to attempt to fully understand the situation. Firms typically wanted to make certain any mistake was not repeated in future with other clients. 25 firms reported they would attempt to seek a meeting with the client to discover reasons for leaving, with 21 firms intimating they would do all they could to patch up any differences that existed between the firm and client.

11 firms concentrated on attempting to prevent rather than cure in order to ensure client satisfaction and reduce the possibility of relationships going sour. In this manner, such firms perceived that they could 'nip problems in the bud', before they threatened continuity of the relationship. In this respect, only 1 firm disclosed that it employed a formal system of regular client audits to institutionalise this function.

The information presented above is demonstrative of the firms' desire to sustain client relationships and is broadly corroborative of the view expounded in Hypothesis 5, which states that the firm will attempt to preserve the relationship created as it has a high cost of termination to both parties. It is clearly indicated above that firms typically value client relationships and will take positive steps to preserve or prevent them from breaking down. Firms were typically not overly concerned with clients leaving, as there was always some natural element of client turnover and client portfolios did not rely too heavily on any one client. The concern of firms was, however, to avoid losing clients through dissatisfaction with the firm's services and they would attempt to take reasonable steps to avoid this.

Firms were typically of the opinion that once the client had decided to go, it would be stupid to attempt to make them reverse their decision as they may have lost trust/ confidence in the firm. Such confidence is necessary for the client/ firm relationship to become established and sustainable. The view taken by many firms was that in the end it was the client's right to choose. The firm could, however, benefit from learning not to duplicate any mistake made in future. Firms were typically fairly philosophical in their attitude since they believed it unrealistic to expect to satisfy all clients all of the time and that it was a sound policy to concentrate on satisfied clients. Such clients would be a continuing source of repeat business and referrals and to neglect them to pursue lost causes was viewed as an unsound policy.

3.6 Signals of quality and reputation to clients and prospective clients of the firm:

To reduce client uncertainty, law firms are expected to wish to provide quality and reputation information to clients. The firm's perceptions of what signals clients use to evaluate quality and reputation pre and post consumption are investigated below.

(TABLE 5.6)

Firm No	REAS FEE	EFF WORK	ACC WORK	PERS ONN	PERS ERV	PUBL ART	CLIC ARE	BUSS KILL	PTRI NPUT	OTHER3
2,14,15,28 (4 Firms=12.1%)	No	Yes	Yes	No	Yes	No	Yes	No	No	No
4,22 (2 Firms=6.1%)	No	No	No	No	Yes	No	Yes	No	No	No
10,30 (2 Firms=6.1%)	No	Yes	Yes	No	Yes	No	No	No	No	No
6,8 (2 Firms=6.1%)	No	Yes	Yes	No	Yes	No	Yes	No	Yes	No
7,25 (2 Firms=6.1%)	Yes	Yes	Yes	Yes	Yes	No	Yes	No	No	No
26(1 Firm=3.0%)	No	No	No	No	Yes	No	Yes	Yes	Yes	No
27(1 Firm=3.0%)	No	No	No	No	Yes	Yes	No	No	No	No
1 (1 Firm=3.0%)	No	No	No	Yes	No	No	No	No	No	No
21(1 Firm=3.0%)	No	No	No	Yes	No	No	Yes	No	No	No
11(1 Firm=3.0%)	No	No	Yes	No	Yes	No	No	No	No	No
12(1 Firm=3.0%)	No	No	Yes	No	Yes	No	Yes	Yes	No	No
23(1 Firm=3.0%)	No	Yes	No	No	Yes	No	No	No	Yes	No
19(1 Firm=3.0%)	No	Yes	Yes	No	No	Yes	Yes	No	No	No
17(1 Firm=3.0%)	No	Yes	Yes	No	No	Yes	Yes	No	Yes	No
32(1 Firm=3.0%)	No	Yes	Yes	No	Yes	No	No	Yes	No	No
9 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	No	Yes	Yes	No	No
5 (1 Firm=3.0%)	No	Yes	Yes	Yes	Yes	No	Yes	No	No	No
20(1 Firm=3.0%)	No	Yes	Yes	Yes	Yes	Yes	Yes	No	No	No
29(1 Firm=3.0%)	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	No
31(1 Firm=3.0%)	Yes	Yes	No	No	Yes	No	No	No	No	No
18(1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	No	Yes	No	Yes	No
16(1 Firm=3.0%)	Yes	Yes	Yes	No	No	No	No	No	No	No
3 (1 Firm=3.0%)	Yes	Yes	Yes	No	Yes	No	Yes	No	No	No
13(1 Firm=3.0%)	Yes	Yes	Yes	No	Yes	No	Yes	No	Yes	No
24(1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	No	No	No	No	No
33(1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	No	No
TOTAL FIRMS	9	25	24	10	28	6	23	5	7	0
%age FIRMS	27.3	75.8	72.7	30.3	84.8	18.2	69.7	15.2	21.2	0

Description of variables:
REASFEE-Reasonable fee
EFFWORK-Speed/ efficiency of work done
ACCWORK-Accuracy/ precision of work done
PERSONN-Personnel
PERSERV-Personal service
PUBLART-Published artičles
CLICARE-Client care
BUSSKILL-General business skills
PTRINPUT-High level of partner input
OTHER3-Other

Hypothesis 6. formally states that law firms will attempt to signal quality and reputation to their own and prospective clients, as this will reduce client uncertainty. An analysis of the signals perceived by firms as being important to clients follows below.

The quality signal mentioned by the most firms in the sample was personal service, which 28 of the 33 firms thought to be important to the client. This is taken to strongly affirm our view of the client/ firm relationship as a relational contract founded in trust between client and practitioners of the firm.

The speed/ efficiency of work done was disclosed by 25 firms as being an important quality signal to consumers and 24 firms noted the accuracy/ precision of the work done as being an

important quality signal. 10 firms thought the personnel carrying out the transaction for the client were important in conveying the quality or otherwise of the firm. This emphasises the human nature of the firms services and demonstrates the importance of the firm's labour inputs.

In 23 of the 33 firms, client care was held out to be a quality signal to consumers. Client care is essentially where the firm attempts to make the client feel as informed as possible with a view to reducing uncertainty and information deficiency. In attempting this, the firm will typically display to the client that it will take care of as much, or as little, of the client's problem as the client instructs, thereby accepting the burden of worry of the client.

In 9 of the firms, reasonable fees charged for the work done was seen to be an important quality signal to the client. The typical view of firms here was that reputable firms offering good quality services would not opportunistically charge inflated fees to clients. Implicitly, this confirms the view that high fees do not necessarily result in higher quality services.

High levels of partner input was claimed by 7 firms to be a signal of quality - being perceived as indicative of the importance the firm attached to the client's problem and the level of attention it was receiving. Partner intensive service can be viewed as encouraging trust in the client and reinforcing the personal nature of the services being rendered to the client. The nature of the audience is important here as only a particular type of client would be likely to perceive such signals.

Published articles in reputable legal and business journals and magazines were indicated by 6 firms as providing an indication of quality and reputation of the firm. Finally, the ability of the firm to quickly perceive potential contingent problems in a transaction and thereafter confidently and competently solve business problems, was viewed as a quality signal by 5 firms who indicated that general business skills were important.

The firms provided the information above in relation to what they perceived was important in influencing, firstly, the client's initial choice of law firm and, secondly, the decision to stay with the present firm. It follows logically that if firms perceive clients will use these signals to determine quality and reputation of a firm and its services, then firms will attempt to signal quality and reputation by channelling effort into stimulating activity in these areas identified. The client faces uncertainty in relation to several factors - for instance, fees, accuracy and effectiveness of the work, and the general ability of the firm to complete the legal work required. The firms efforts in creating the signals indicated as being important above, will reduce client uncertainty. This is consistent with confirmation of Hypothesis 6.

The relatively high levels of response of firms in relation to the importance of personal

service (10 firms), client care (23 firms) and high levels of partner input (7 firms) as quality signals, is supportive of the validity of Hypothesis 7. This states that law firms will attempt to emphasise personal service and the importance of the client, as this will imbue the client with trust in the firm.

A problem remains and that is that such quality signals are generally only perceptible to prospective clients in the pre-purchase decision. All quality information that can be relied on (other than self-praising advertising), is secondhand and subjective to the person choosing a lawyer pre-purchase. The issue of published articles as a signal of quality and reputation is an interesting one as this is likely to be fairly disinterested information - it is, however, unlikely to be perceived by a wide audience of potential clients.

3.7 The firm's name as a signal of quality and reputation:

Theory discussed in the previous chapter suggests the firm will wish to create a brand name in order to effectively communicate to clients the quality of its product. This is aimed at reducing uncertainty regarding quality and reputation of the firm. Firms surveyed provided the following information regarding the importance of the firm's name in conveying quality and reputation to clients.

(TABLE 5.7)

Firm No	NAMESIG (significance of firms name)
1,6,15,18,19,22,25,26 (8 Firms=24.4%)	Significant as quality signaller
2,3,4,5,7,8,9,10,11,12,13,14,16 17,20,21,23,24,27,29,30,31,32,33 (24 Firms=72.7%)	Very significant as quality signaller
28 (1 Firm=3.0%)	Not significant yet since new firm

The role of the firm's name in conveying reputation and quality to clients and prospective clients was perceived in all but one of the firms to be at least significant, and by 24 of the firms as being highly significant. This is indicative of the fact that firms generally perceive themselves to have effectively created a brand name. This could be indicative that in future, franchised branch networks may perhaps experience success in demonstrating uniformity in quality of service to clients and prospective clients. The one firm who did not see their firm name as significant, qualified this by indicating that the firm name would be in the future but was not at present since it was a new firm.

3.8 Methods of conveying quality and reputation of firms to clients:

Hypothesis 6. stated that firms will attempt to signal quality and reputation to their own and prospective clients as this will reduce client uncertainty. The methods used by firms to

attempt to convey the signals of quality and reputation to clients are summarised below.

(TABLE 5.8)

Firm No	BROCHURE	SEMINAR	PERSTRAI	PROMO	PERSONAL	BEAUTY	ESTREF	PRCONS	BACKUP	OTHER4	MKTFUT
2,15,16,28,32 (5 Firms=15.2%)	Yes	No	No	No	Yes	No	No	No	No	No	No
8,10 (2 Firms=6.1%)	No	No	No	No	Yes	No	Yes	No	No	No	No
26,30 (2 Firms=6.1%)	Yes	No	No	No	Yes	No	Yes	No	No	No	No
21,23 (2 Firms=6.1%)	Yes	No	No	Yes	Yes	Yes	Yes	No	No	No	No
22,31 (2 Firms=6.1%)	Yes	Yes	No	Yes	Yes	No	Yes	No	No	No	Yes
13 (1 Firm=3.0%)	No	No	No	No	Yes	No	No	No	No	No	No
6 (1 Firm=3.0%)	No	No	No	No	Yes	No	Yes	No	No	No	Yes
11 (1 Firm=3.0%)	No	No	No	No	Yes	No	Yes	No	Yes	No	No
17 (1 Firm=3.0%)	No	No	No	Yes	Yes	No	No	No	No	No	No
1 (1 Firm=3.0%)	No	No	No	Yes	Yes	No	Yes	No	No	No	No
18 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	Yes	No	No	No	No	No
9 (1 Firm=3.0%)	Yes	No	No	No	Yes	No	No	No	Yes	No	No
14 (1 Firm=3.0%)	Yes	No	No	No	Yes	No	Yes	No	Yes	No	No
24 (1 Firm=3.0%)	Yes	No	No	No	Yes	Yes	Yes	No	No	No	No
5 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	No	Yes	No	No	No	No
7 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	No	No	No	No	No	No
4 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	No	No	No	Yes	No	No
19 (1 Firm=3.0%)	Yes	Yes	No	No	No	No	No	Yes	No	No	No
3 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	No	No	No	No	No	No
27 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	No	No	No	No	No	Yes
25 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	No	Yes	No	No	No	No
29 (1 Firm=3.0%)	Yes	Yes	Yes	No	Yes	Yes	Yes	No	No	No	No
20 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	No	Yes	No	No	No	No
12 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	No	No	No
33 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	No	Yes
TOTAL FIRMS	25	11	7	12	32	7	18	2	5	0	5
%age FIRMS	75.8	33.3	21.2	36.4	97.0	21.2	54.5	6.1	15.2	0	15.2

Description of variables:
BROCHURE-Brochure
SEMINAR-Seminars for clients
PERSTRAI-Personnel training
PROMO-Advertising and promotion etc.
PERSONAL-Emphasis on personal service
BEAUTY-Beauty contests for commercial clients
ESTREF-Establish and maintain referral network
PRCONS-PR consultants used
BACKUP-Back up claims made with service quality
OTHER4-Other
MKTFUT-More marketing etc. required in future

All but one of the firms indicated quality and reputation information was conveyed by emphasising personal service, offering support for Hypothesis 7. 25 firms used brochures of some form to provide clients with information and 12 firms used direct advertising and promotional tools to do so. These method of conveying reputation and quality signals to clients tend to provide claims as to what clients can expect in terms of service. There is, however, a real requirement to actually reinforce such claims with quality service. 5 of the firms explicitly indicated the importance of backing up claims made with quality service.

Of the 33 firms, 11 held seminars for commercial clients as a method of informing them of, for example, what the consequences would be for them of changes in a particular new area of legislation. This would signal to such a client the forward thinking nature of the firm, provide additional client information, attempt to stimulate the demand for such services within the firm and reinforce the personal nature of the relational contract.

7 firms regarded personnel training and its intended effect of producing a well informed,

confident labour force throughout the firm, as signalling quality to clients.

A similar number of firms indicated that they entered 'beauty contests' with competing firms to attempt to win contracts from commercial clients (particularly for public sector contracts). In this respect, beauty contests are a way in which the high search costs of the client can be effectively shifted on to the competing providers of the desired service.

Only 2 of the firms had used the services of PR consultants, and the like, to attempt to find better methods of promoting the firm's reputation and the quality of its services.

18 of the firms believed that an effective way of signalling quality and reputation was to attempt to establish an effective referral network and maintain this by providing good quality service so that the network becomes essentially self supportive.

5 firms provided an indication of their belief that marketing the firm using promotional tools etc. would become increasingly important in the future. Of these firms, 1 presently engaged in none of the activities which could be described as 'marketing of the firm'. The other 4 firms were all currently active utilising marketing tools but envisaged their role expanding still further in the future.

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Generally, the mood perceived from interviewing the firms was that many felt the market for legal services becoming more competitive. This, coupled with heightened client expectations, has forced many of the firms in the study to adopt concrete marketing strategies, or at least forced them to become aware of the need to do so. More novel activities in this field range from brochures to mailshots, and 24hr helplines to in-house seminars, with all forms of advertising in between.

Endnotes - Chapter Five

1. See, Williamson, O.E., **The Economic Institutions of Capitalism**. Free Press, 1985

2. See, Williamson (1985), ***supra*** Note 1.

3. See, Williamson (1985), ***supra*** Note 1.

4. See, Williamson (1985), ***supra*** Note 1.

5. See; Williamson (1985), *supra* Note 1

6. See; Williamson (1985), *supra* Note 1.

7. Credible commitments are essentially actions of reciprocity between the parties to an agreement which support exchange by ensuring that payoffs from the relationship are self-enforcing as a result of the design of the relationship itself. For an indepth discussion of credible commitments see; Williamson (1985) *supra* Note. 1 at pp. 163-205.

8. See; Williamson (1985), *supra* Note 1.

9. See; Williamson (1985), *supra* Note 1.

-Chapter Six-

Literature of relevance in understanding internal organisation of law firms and relationships between partners:

Introduction:

This chapter will present some alternative views of partnership organisation and examine many of its specific functions in relation to organising relationships between lawyers practising within the same firm.

Section One: Partnership as a device for rewarding partners and organising their human capital.

The partnership contract which specifies incentives for partners, as the most important party to the contract of the firm, is a primary focus of this thesis. Few writers have examined the role of partnership as a device for remunerating solicitors who wish to practice together within the one firm. While there have been notable exceptions such as Rosen (1992), this chapter will largely comprise a critique of Gilson and Mnookin's (1984) seminal analysis of partnership contract structure for large American law firms [1].

This study notes that large law firms appear to supply a substantial, and increasing proportion of, legal services consumed by businesses in the USA. It must be stressed here that the law firms in their study are of a magnitude beyond probably most, if not all, of the firms currently in the UK. Nevertheless, it is interesting to examine which of their concepts and alleged partnership problems are applicable to the law firms being empirically examined in this thesis and discover the degree to which they are applicable. It is also hoped that this will aid prediction of what problems UK law firms may face in future should they become as large as many USA firms.

In his 1992 paper on partnerships, Rosen argues that the life cycle for solicitors' earnings (like many other professions) is particularly lengthy, and hence partnership has evolved as a response to the simple requirement to encourage and reward lawyers for their slow, lengthy and progressive accumulation of human capital. While this view is undoubtedly correct, unlike the work of Gilson and Mnookin noted above, Rosen's work makes no attempt to detail exactly what mechanisms exist within partnership to encourage and reward difficult and protracted accumulation of human capital by a partnership's lawyers. It is these precisely these mechanisms upon which much of this thesis focuses. Hence, analysis leans heavily on Gilson and Mnookin's work rather than that of any other writer such as Rosen.

1.1 Neoclassical support for the existence of large legal firms:

Traditional Neoclassical micro economic theory proposes several reasons why we might expect that large firms may be advantageous and Gilson and Mnookin identify these as follows [2]:

1. Economies of scale - larger firms may be able to utilize optimal quantities of staff support (legal secretaries, associate legal practitioners, assistants etc.) and assets such (library resources (LEXIS), word processing equipment & other office machinery) [3].
2. Returns to specialisation - real and important elements of increased efficiency can result from concentration on a particular legal speciality (specialists can accomplish in a shorter period what it may take novices far longer to do).
3. Economies of scope - information can be effectively utilised to produce other services where low set up costs result in a significant cost advantage to the incumbent firm over alternative suppliers.
4. Minimum scale - certain areas of legal practice necessitate coordinated efforts of a large team of lawyers, for example, in certain areas of corporate work.

1.2 Neoclassical simplification of the problem:

Recognition of these advantages is only part of the scenario, since many of these benefits can be obtained in organisational units of a smaller scale than many of the large law firms observed today. This is indicative of the existence of other large firm advantages [4].

As will be recalled from previous chapters, a further deficiency of traditional Neoclassical micro analysis its very limited use in analysing the internal organisation of law firms. It inadvertently assumes away internal organisation and views the firm as a "black box" interface between inputs and outputs [5].

The important issue of division of law firm income between partners is related very closely to the internal organisation of the law firm. Neoclassical economics is, consequently, of little use in analysing hierarchical features of organisation, and indeed internal structures of firms, since it assumes such features away in the theory of the firm. It is, therefore, of little or no use in analysing division of partner incomes.

The legal profession has remained largely silent on the issue of income division in law firms - an unsurprising response given the characteristic insular nature of the profession. This, coupled with inapplicability of tools of traditional economic analysis, has resulted in a neglect of enquiry into the organisation of law firms by economic scholars.

1.3 The importance of the system for sharing partnership profits:

The income sharing system is the major contract which binds the partnership together and determines many incentives confronting partners of the firm. A cursory glance at the law firm would suggest that lawyers dissatisfied with their present circumstances within the sharing bargain, would first voice their dissatisfaction. If this did not force desired changes, they would simply exit and join, or form, another firm. This, however, is too simple a scenario which ignores many subtle facets of the sharing bargain. Gilson and Mnookin (1984) undertake a lengthy examination of these subtleties in the context of two extreme models of income sharing within the partnership[6]. These two models (the lock-step seniority based model and the marginal productivity model) will be discussed below.

1.4 A simple seniority sharing model:

In a seniority sharing system, income is basically correlated to length of seniority of partnership service. At first glance, it can be argued, firstly, that partners' incentives are attenuated, secondly, no account of productivity is taken and, thirdly, in the long run, challenges to prosperity, stability and survival of the firm could be expected [7].

Membership of the law firm, however, still has significant benefits to the individual lawyer. To examine the potential gains available to the lawyer, an examination of portfolio theory is required. Gilson & Mnookin (1984) demonstrate a simple portfolio analysis of lawyers' human capital assets [8].

1.5 Portfolio theory and the lawyer's human capital asset:

Portfolio theory proposes that risk aversion of the individual, propels a desire to hold a diversified portfolio of capital assets. Combining assets within a portfolio facilitates risk reduction, without subsequent reductions in expected returns [9]. Risk has two constituent components;

1. Systematic risk - elements of risk that affect the value of all assets.
2. Unsystematic risk - elements of risk that have selective effects on the value of a particular asset.

Portfolio theory suggests that capital assets are of greater value to the diversified investor when combined in an asset portfolio. For the lawyer whose asset is in the form of human capital, the problem is that characteristics of this asset make it difficult to diversify its risk. Gilson and Mnookin (1984) argue that significant elements of organisation of the law firm

can be viewed as a response to efforts of lawyers to diversify risks attending their human capital assets, in the face of difficulties of doing so[10].

The human capital asset of the individual lawyer is the ability to earn fees - not only in the present period, but also in future time periods. The lawyer's present earnings and future earning capacity can be seen as returns to investment in human capital. The critical feature of this asset is that the lawyer only earns returns if he actually renders legal services.
In this context, Gilson and Mnookin (1984) view the large law firm as a means by which the lawyer can diversify away unsystematic risk [11]. In terms of legal services, systematic risk may be characterised as the degree to which earnings from practising law are sensitive to the overall performance of the economy.

Unsystematic risk relates to those characteristics of an individual lawyer which personally affect ability to earn fees. Certain elements of unsystematic risk (death or disability) can be diversified through prudent use of insurance markets, but other elements cannot [12].

Gilson and Mnookin (1984) see the firm, therefore, as providing the means by which unsystematic risk, attached to lawyers' human capital, can be diversified [13]. They argue that it remains questionable why this function is served by the firm, rather than by a contract between independent practitioners. Surely the simple answer to this is that the firm permits diversification in a more contractually efficient and effective manner at lower costs, while capturing synergy benefits of group practice.

By taking a nexus of contracts view of firm organisation (in line with the importance Gilson and Mnookin (1984) place in agency theory) it could be argued that these two ideas above are not mutually exclusive [14]. In essence, the partnership is a set of contracts between independent contracting practitioners to share joint and several liability. The short answer to Gilson and Mnookin's unanswered question is surely that, if the practitioners remained independent, this would imply the absence of a sharing bargain and hence, there would be no risk sharing benefits. If they do have a risk sharing contract, as Gilson and Mnookin (1984) suggest, then surely this is a partnership [15]. This is within the definition of 'a firm', and highlights the definitional problem that troubles economists in determining what constitutes a firm.

1.6 Specialisation and increased risks to human capital:

Specialisation in legal services makes the human capital risk situation even worse. By narrowing his investment still further, the lawyer creates still higher levels of uncertainty and systematic risk. While the earnings from specialised legal services could be expected to be higher, they could be expected to suffer from less stable and predictable levels of demand.

The problem for the specialist lawyer is that he cannot specialise in more than one specialty, and he cannot sell a portion of his earnings in his specialty in the market and use the proceeds to purchase interest in another. Partnership is the mechanism to achieve this portfolio function for the lawyer, where the firm can be seen as a collective agreement between lawyers that each will make human capital investments in different specialties and returns will be distributed on a pre-agreed basis. Hence, partnership can be understood as an organisational innovation which permits lawyers to capture benefits of specialisation, with concurrent risk reduction.

1.7 Membership benefits and agency cost problems:

Partnership permits the lawyer to capture some attractive features, but potential gains are constrained by the existence of agency problems. Benefits anticipated by those entering into a cooperative agreement, are only available if self-interested behaviour is eliminated and behaviour is aligned with that of the original agreement. Where self-interested behaviour occurs, at best one member of the team is made worse off and at worse, all but the opportunist lose. Hence, incentives facing all parties to partnership agreement must be aligned in order for potential cooperative gains to be realised.

In the absence of transactions costs, opportunistic behaviour would produce no gains to the individual; since any deviation from the contract specified behaviour would be costlessly monitored, revealed and remedied. In the real world where transactions costs are non-trivial, opportunistic behaviour of the individual becomes viable. To this extent, cooperative gains are reduced.

1.8 The agency problem of the law partnership:

The law firm agency problem is to design a sharing bargain that creates non-legal constraints on ex-post opportunism in relation to the ex-ante sharing bargain. If the sharing bargain was not, when necessary, capable of legal enforcement, then it is unlikely anyone would enter such an agreement. The potential for vast abuse of contractual imprecision would exist. Partnership is, however, a legally recognised and enforceable form of sharing bargain.

Gilson and Mnookin (1984) propose three main types of opportunism, in the context of the sharing bargain [16];

1. Shirking - the classic free-rider agency problem where one individual sits back, injects a low effort intensity and relies on the others to supply greater effort.
2. Grabbing - the lawyer demands more than his entitlement in the sharing bargain.

3. Leaving - the lawyer discovers his marginal product and exits the firm to earn returns commensurate with his revealed marginal product.

Grabbing and leaving are, however, closely linked since the threat of leaving may result in a greater chance of grabbing being a viable and successful action. The threat of leaving, however, must be perceived as a real threat to the partnership to be effective as a hostage. The dissatisfied lawyer has to demonstrate;

1. He is worth more than he is being rewarded for,
2. He has a credible more favourable alternative and,
3. The law firm stands to be the loser should he decide to leave.

A "locking in" process, due to contract specific compatibility and trust, may make the 'voice' rather than the 'exit' option more viable in resolving partnership disputes. The sharing bargain must attempt to counter these potential threats to cooperative gains. There is a need to create real performance incentives, in the face of measurement difficulties in quantifying marginal productivity. However, a sharing bargain which uses productivity measurement to gauge performance/ constrain shirking can limit gains from diversification.

1.9 The two extreme models of sharing bargain:

Essentially two polar models of sharing bargain exist. The first of these is a lock-step seniority based sharing model at one pole, and the second is the marginal productivity model, at the other. This simple diadic analysis in no way precludes the existence of other sharing bargain models, however, these two extreme cases analytically demonstrate the most important incentives facing lawyers in partnership. The most extreme marginal productivity model, for example, involves no diversification at all.

(I) The lock-step seniority model:

The incoming partner here exchanges his human capital to allow participation in the portfolio of diversified human capital assets of the firm. This portfolio is diversified in respect of;

1. Individual characteristics of particular lawyers and,
2. Increased risks of specialisation.

The incoming partner essentially buys into a mutual fund to share in the future income of lawyers of his same age and experience but also of those lawyers whose expertise and experience are likely to bridge several generations. In a given class of partnership seniority, all lawyers are treated as equals, eventually obtaining a 'full share' in the partnership.

In the seniority model, important factors will be;

1. The length of time taken to become a full share partner and,
2. The distribution of income between the years with the firm.

Where the income is weighted towards the latter years of the lawyer's life (more senior grades of partnership) the lawyer may discount the value of this deferred compensation. The further in the future reward is, the greater is the risk facing the lawyer of the firm declining, going bust, or facing other such risks in the interim period [17]. Where income is weighted towards earlier years, an incentive is created for the lawyer either to shirk, or to leave and join another firm. This, of course, will be heavily dependent on the selected income/ leisure preference trade-off of each particular lawyer.

The essence of the sharing bargain is to facilitate diversification of human capital without these attendant agency problems of shirking, grabbing or leaving. This echoes the Fama and Jensen view that each type of organisation has a particular agency problem to solve [18].

(II) The marginal productivity model:

Measurement problems exist in this model, stemming from the fact that real productivity, and the proxy the firm uses for productivity, are likely to be two quite different things altogether. Partners are provided with incentives to attempt to maximise their own income (and psychic income) by maximising factors measured by the formula, rather than maximising actual productivity [19].

The extreme productivity model is where the partnership agreement is merely to share expenses - the problem here is that each partner essentially remains a sole practitioner, providing no element of diversification of human capital for lawyers of the firm. Within such an arrangement, advanced cost accounting techniques can accurately distribute expenses to each partner's cost centres, where the absence of any jointness in production creates a perfectly attributable measurement of marginal productivity.

(i) Problems with a simple hours worked formula:

In the case of an 'hours worked formula' proxy for productivity, the total firm revenue is determined and profit is divided in the same proportion as the product of the number of hours worked by the lawyer, multiplied by his hourly billing rate, contributes to total firm revenue. This hours worked method is one example of many imperfect proxies which can stand in for actual productivity. The construction of the formula has obvious effects on the incentives, behaviour and sharing bargain situation that results.

In this example, the determination of fees becomes of central importance. If fees are set on some seniority based scale, the result is that certain aspects of the 'pure' sharing model are reintroduced - for any given number of hours worked there will tend to be a higher contribution to total firm revenue the more senior the partner. Hence, more senior partners will tend to attract a greater personal income based on higher billing rates. A ceiling rate could be fixed, beyond which all the firm's lawyers would charge the same, the expectation being that the sharing bargain established would focus on hours worked to constrain shirking.

(ii) Problems with productivity formulae:

The degree of sharing that occurs between partners of the firm, however, will depend;

1. On the 'coarseness' of the productivity proxy formula and,
2. On measurement of lawyers' actual (or what is perceived to be) productivity

Lawyers will attempt to diversify their human capital with respect to all factors omitted by the formula, but which will have a bearing on productivity. The 'coarseness' of productivity measurement also determines the extent to which perverse incentives are created in a productivity based sharing model.

In the absence of complete sharing, the result is that behaviour equivalent to shirking can be expected in the marginal productivity approach. Here, behaviour takes on strategic motives in order to;

1. Satisfy those factors to which the formula appeals and,
2. Ignore those it omits.

The upshot here is that while there sharing may exist with respect to those factors omitted by the formula, there is the creation of a perverse incentive for lawyers to spend a minimum of their time on those omitted elements. This consequently minimises levels of actual sharing that takes place.

Consequently, in common with the sharing model, shirking may result in a reduction in overall output. Incentives, resulting from the coarseness of the productivity measurement, may reduce the size and alter overall distribution of the law firm's profit, under the marginal productivity approach.

(iii) Client generation and firm management:

Gilson and Mnookin (1984) examine the important functions of client generation and firm management [20]. The importance of firm management is self evident and client generation is

necessary to provide stimulus to the firm's growth via an expanded client base, and to generate a stable work load. Client generation is necessary in the absence of 100% repeat business, which is unlikely to be the norm in either private, or corporate areas of law firm business.

Under a marginal productivity scheme, Gilson and Mnookin argue that the lawyer perceives no benefits from attracting more clients than he can himself deal with [21] - no incentive exists to pass clients to other partners, even though they may be more efficient at the type of work in question. This can only enhance inefficiencies within the firm. Gilson and Mnookin's view of the lawyer implicitly assigns him behavioural traits of self-interest, selfishness and opportunism - paralleling those assumed by the transactions cost framework.

Clearly a problem exists since, although some tasks within the firm are vital, there is no direct monetary benefit to the lawyer for undertaking them. The question now becomes, given the need for time to be allocated to such functions, how much credit should be given to the lawyer for engaging in them and what form should the credit take. The simple productivity model gives no credit for time spent on these activities. Inclusion of them in the formula would result in problems of determining what level of credit should be given to the partner for engaging in them (ie. what is the compensation scheme).

The crux of the matter is that, no matter how cleverly designed, or coarse, the productivity measure is, it still is not measuring actual productivity: The result is that the productivity formula, and method of measurement, can create incentives perverse to those they are aimed at creating. This, naturally, determines the extent to which sharing is reintroduced in the productivity model. This feature is also instrumental in determining the extent to which shirking, grabbing and leaving problems, that prompted initial rejection of the sharing model, are reborn in the marginal productivity model.

(iv) Designing a good productivity formula:

The task set, therefore, is to create a productivity formula which, firstly, minimises perverse incentives and, secondly, concurrently minimises shirking, grabbing and leaving problems.

This formula must also create incentives for partners to spend time on generating new business and on more administrative and managerial elements of law firm organisation.

(v) Incentives in attracting clients:

When the lawyer attracts more clients than he himself is able to service, then he can buy associate lawyers time at wholesale (wage of associate) and sell it to clients at retail (partners

billing rate). This obviously increases firm revenues. In terms of the model of the labour managed firm (to be discussed later), this can be seen as an incentive for existing members to hire non-members in order to increase firm revenue.

In an agreement emphasizing sharing, all members will benefit here since individual profit shares will be paid out of an enhanced firm revenue. Here, the wage paid to non-members would determine whether it was viable to buy their time at wholesale and sell it to the client at retail rates, and would determine the effect on total firm revenue. It will most likely always be worthwhile to hire non-member labour as it is a highly profitable way to increase capacity, firm size, and total revenue [22].

The attraction of clients, surplus to the requirements of the attracting partner, would create work for those lawyers who were less successful at attracting clients. This emphasises sharing between the lawyers of the partnership. In this case, there would be the creation of a more even distribution of workload for each lawyer. This would create a more effective utilization of productive capacity through greater ease of planning and strategic decision making through more even, stable predictable case loads. The problem created here, however, is the question of the relative compensations due to partners since the partner passing on the work would receive no direct compensation from doing so. If partners within the firm are willing to pass clients to other partners then this whole problem is mitigated to a large extent. It is likely that partners will have to pass client between themselves as clients may require services outwith the speciality of the attracting or contact partner.

The law firm must attempt to allocate some reward for client generation since it is the lifeline of the firm, and any measurement of productivity should recognise this. As noted previously, however, the productivity formula employed can create incentives for the lawyers to maximise those factors it gives greater weight to, leading to activities that direct effort away from attainment of desired goals.

(vi) Problems of compensation of partners for attraction of new clients:

If partners were rewarded a one time bonus for initially attracting a client, the lawyer is provided with no incentive to participate beyond initial attraction of the client. The attracting partner would not be overly concerned whether the client was satisfied with the service or whether they would become a source of repeat business. The constraint rendering one-shot opportunism unviable here is, of course, reputation effects and fear of a diminution of brand name capital of the firm. A satisfied client may recommend that particular lawyer to his associates, friends etc. and, given extreme information deficiencies facing consumers of legal services, this may play a highly significant role.

The client attraction bonus could be extended and linked to the level of repeat business a new client passes to the firm. This has the disadvantage that lawyers may attempt to prevent his colleagues from breaking into the relationship created, if he perceives his livelihood to be at risk through exposure of his clients to other lawyers of the firm. Partners may, thereby, jealously guard 'their own' clients and the firm may also find the creation of a large individual partner client base, invests that partner with a stronger voice option. Exercising his exit option, with a large tranche of clients, would have a strong adverse effect on the value of the firm. The firm may also view partner client portfolios as a barrier to cross-selling other services of the firm.

An incentive may be created for a partner to reduce rates at which clients are billed to entice clients to give the firm repeat business and create more hours of work. Here, the decision of the lawyer is likely to be based on whether this would have the effect of increasing personal benefits, in terms of a larger share of a smaller total firm income, or not. Here, the problem of the firm is attempting to avoid client substitution of brand loyalty with lawyer loyalty. The firm wishes to avoid enhancing the value and viability of the lawyers grab (voice) and leave (exit) options.

1.10 The importance of creating firm specific capital:

It is possible to capture all the benefits of the sharing model and to simultaneously reduce agency costs. This relates to the notion of firm specific capital, and the distribution of the benefits of firm specific capital between individual lawyers and the firm itself. Firm specific capital is characterised as a benefit of firm organisation, incapable of being removed from that firm by any partner. Additionally, it is not capable of being duplicated outwith that firm by an individual lawyer.

Returns to firm specific capital can only be captured by lawyers who remain within the firm, and not by those who choose to leave. An example of firm specific capital is the existence of a large well respected corporate client within the client portfolio of the firm. This can be perceived by prospective consumers of that firm's services as indicative of quality, and can establish brand name association and reputation effects.

The effect firm specific capital has is that it constrains the value of the lawyer's voice and exit options, in a pure sharing mode of organisation. This is accomplished through an attenuation of the "threat value" of the voice option, and the inviability of the exit option due to capital losses facing the individual lawyer. A lawyer who exits the firm, is likely to be able to duplicate minimum scale requirements and any economies of scale relatively easily. This is likely to be achievable without great cost and thus will have little, or no, effect on a lawyer's evaluation of potential disadvantages of exiting the firm. It is vital to realise that the demand

side (clients), are equally crucial to the survival and success of the firm as the supply side (good lawyers). Clients also have an instrumental role to play in the development of firm specific capital since they are a primary source of this desirable firm asset.

(I) The role of large corporate clients:

It is to the firm's advantage to have large corporate clients within its client portfolio because;

1. They are usually a source of large volume, typically routine, predictable work and,
2. This work can often be delegated to lower levels of the law firm's employees.

Here, the partners can generate a larger 'value added' by purchasing associates' time at wholesale and selling it to clients at retail. This contributes to law firm revenue and earns lawyers returns to their human capital.

From a strategic perspective, a predictable flow of work allows the firm to plan production and output etc. to a finer degree. As already mentioned above, large clients are also an important source of firm specific capital who can directly, and indirectly, feed the law firm with other clients. This is achieved through the process of referrals and reputation effects, which are so heavily relied upon by consumers of legal services due to information deficiency. This difficulty of quality evaluation for consumers, can create incentives for lawyers to develop firm specific capital [23].

An established and diversified portfolio of clients results in a more stable and predictable demand for the law firm. Within this client base, the firm captures economies of scope in terms of start up costs since they will tend to be smaller in established relationships than for other market competitors, yielding cost advantages for the firm. Start up cost advantages are split between the client and the firm, and the law firm will only have to be perceived as best (cost & quality) by the client for that transaction to be selected against competitors.

Hence, the law firm may be able to capture these firm specific benefits and still provide the service to the client at a cost advantage to the consumer. The consumer's purchase decision may not be based on strict price considerations here, but rather on a "better the devil you know than the devil you don't" logic. These elements of firm specific capital, in essence, act as high sunk costs making it unviable for other firms to contest the transaction.

(II) The crucial question of where the client's loyalties lie:

A lawyer who exits the firm will only take clients with him if they are loyal to him, rather than the firm. This will act as an exit constraint, to the extent that the lawyer may not be able

to accurately predict what these clients will do. It will be recalled from previous chapters that the relationship created between law firm and client approaches that of bilateral monopoly, with each side assuming high costs of relationship termination. Hence, transaction/ relationship preservation motivate the parties due to a 'locking-in' process.

The use of a restrictive covenant, could constrain the lawyer's exit option by discounting the value of the lawyer's potential earnings outwith the firm. Recently, restrictive covenants have been seen largely beyond that which is necessary to protect legitimate interests of the covenanting firm [24].

(III) The firm as a signal of reputation:

Recalling earlier arguments, it is difficult for any prospective user of legal services to discover quality of service in advance. Given a low degree of sophistication, the typical client may not even be able to recognise quality ex-post consumption either. The firm must, therefore, signal quality to the consumer and consumers who are satisfied may refer the firm to others. Hence, clients may play a greater role in signalling the quality of the firm than can the firm itself.

Satisfied consumers can demonstrate impartial satisfaction and to that extent, evaluation bias is overcome. The consumer receives no direct benefit from the firm for attracting new business and this should not create partiality problems [25].

Firms are in a position to reduce client search costs, and can signal quality, to a certain extent, in both direct and indirect ways. Client sophistication varies enormously and the methods utilized to demonstrate quality, and reduce search costs, should recognise this disparity. Where search costs are low to the client, due to higher levels of sophistication, it is more likely that selection decisions will be based upon direct information on quality. Higher levels of sophistication, that could be expected to relate to commercial clients, enable the client to more cheaply and precisely garner, and rationally judge, direct quality information.

The ability of the firm to signal quality is another element of firm specific capital that the lawyer could find difficulty in duplicating outwith the firm if he exited.

(IV) Creation of brand name capital as firm specific capital of the firm:

The firm can invest vast sums of money on establishing a brand name using direct advertising methods [26]. It can attempt to demonstrate quality by having impressive offices, etc. which reinforce the established brand name and signal quality. This firm specific capital is difficult for any lawyer to duplicate outwith such a practice and hence, a potential loss of a lawyer's

share in brand name capital, can act as a disincentive to exit the firm. The methods of signalling quality, and reducing search costs, could be expected to vary with client sophistication.

Within the firm, brand name capital may be enhanced by partners of that practice if they write articles for widely read law journals and/ or take seminars and give talks on interesting areas of the law. Here, firm specific capital may be enhanced by the firm's name being associated with the lawyer. This can, however, backfire on the firm since the lawyer may do more to further his career prospects than he does to benefit the firm. The potential earnings he could attract outwith his present situation may make it attractive to exit the firm, even in the face of contributions to firm specific capital that he has created.

The contract of the lawyer may specify restrictions on earning outwith the firm. An incentive dilemma is created here. If outside earnings are banned, then he has no incentive to take part in activities that may enhance firm specific capital. He may, however, not disclose his outside interests and exit the firm, once this option becomes viable when he more than covers his opportunity cost of leaving the job.

If his outside earnings have to be paid to the firm, then there is only an incentive to work if he receives a substantial enough portion of the resultant increased income of the firm to make it worth his while. If all income is 'bona fide', then the problem initially discussed occurs since the value of his exit option is potentially enhanced. It is, paradoxically, under this scheme that there is the greatest scope for the creation of firm specific capital.

There are two opposing forces acting on the lawyer in this situation since the creation of firm specific capital reduces the lawyer's incentives to leave, but the process by which it is created, enhances the viability of his exit option. The act of creating firm specific capital more often than not has spin off benefits for the lawyer in terms of lawyer specific capital.

The firm permits its name to encompass all of the specialised services it offers and this serves to signal quality/ reputation in all its fields of activity. Here, the law firm acts like a department store where it is expected that the consumer perceives that only high quality products would be permitted by the firm to be associated with the its name [27].

(V) The law firm as a reputational intermediary:

Gilson and Mnookin (1984) argue the firm has a role to play as a reputational intermediary and that it can earn returns by, essentially, renting its reputation [28]. This firm specific asset is unavailable to a partner who has left the firm although some residual reputation may be

endowed on such a lawyer having been perceived by a client as having once worked for that firm.

The esteem, independence and trustworthiness of the law firm are all firm specific assets. The degree of independence can be attacked where a conflict of interests occurs and where it is in the interests of the law firm to bow to the wishes of a large and valuable client in order to retain business.

It is difficult for a lawyer who has left a firm to quickly attract a sufficient number of clients to establish the firm name as a reputational intermediary. Here, we can see that established and familiar firm names are preserved through generations even though the personnel in the law firm may contain none of the original partners whose names appear in the name of the firm. The partnership name acts as a timeless asset much like incorporation creates a situation of perpetual succession where the company continues to exist irrespective of the death or demise of its members. An established firm with a good reputation would act to render the lawyers exit option less attractive.

In many cases, the incidence of firm specific capital dilutes the attractiveness and potential value of a lawyer's exit option and hence the credibility and "threat value" of grabbing may be to that extent potentially unsuccessful to the dissatisfied lawyer.

1.11 Type of sharing bargain and creation of firm specific capital:

Where there is a sharing bargain rather than a productivity based partnership bargain, Gilson and Mnookin (1984) argue that firm specific capital may be generated and retained with greater ease [29] - with the sharing bargain model, lawyers stand to gain more from maximising the value of the firm, which in turn is behaviour suited to the creation of firm specific capital. This is a solution to the agency problem of a divergence of incentives between the principal and agents of the firm in that incentives are aligned in an attempt to gain maximum benefits from cooperation in joint production.

A marginal productivity approach creates incentives for the individual lawyer to over-invest in lawyer specific capital (ie. personal reputation) and under-invest firm specific capital. In this model, firm reputation is not the primary focus and the value of the firm is not the perceived maximand.

1.12 The efficiency advantage of the sharing over productivity approach to income division under a no shirking assumption:

Gilson and Mnookin (1984) argue the case for the increased efficiency of the sharing model as against the productivity model [30]. This is based on their belief that;

1. The sharing model allows clients to become firm specific capital more easily, and,
2. The firm as a means of assuring quality plays a greater role.

The major failing of the productivity approach is that it is difficult to design a productivity formula which does not create incentives for lawyers to pursue their own, as opposed to firm, interests. This essentially boils down to an inability to design a productivity based sharing bargain that sufficiently suppresses agency problems. The success of the sharing model in suppressing agency problems is, however, dependent on the attitudes of the firm's partners. For the efficiency advantage of the sharing over the productivity model to exist partners must not shirk and full resultant cooperative benefits rest on the propensity of the partners to supply the effort intensity stipulated in the ex-ante sharing bargain. Consequently a more meaningful comparison must be made by lifting the restriction assumed previously of no shirking in the sharing model.

(I) Relaxing the no shirking assumption:

By lifting the no shirking assumption, analysis now focuses on designing and implementing a system which exposes and penalises partners supplying a lower than agreed effort intensity. The system must, however;

1. Remain independent of the goal of diversification of risks inherent in lawyers' human capital and,
2. Must not simultaneously create perverse incentives like those associated with the productivity based system.

A simple system operating by detailed recording of hours worked in tandem with close personal monitoring, would act to the detriment of both diversification and avoidance of perverse incentive goals as stated above. The rationale behind the sharing model is to protect individual lawyers from fallow periods where there is little or no work in their particular speciality. A simple time keeping and personal monitoring system could not distinguish between this and the occurrence of true shirking behaviour - risk diversification benefits would be to that extent reduced.

Additionally, where lawyers are penalised for billing insufficient hours, a forum would be created for a contest where partners would attempt to avoid billing lower hours than their contemporaries and peers. The disparity between hours worked and productivity is all to evident in such a scheme, and partners would be unwilling to share work with others. In summary, firstly, the diversification problem is to that extent reintroduced. Secondly, the system interferes with the twin goals of efficient performance of legal services and the creation of firm specific capital.

Within the context of the sharing bargain, these problems are not insurmountable. They indeed can be mitigated by the creation of specialised sub-groups whose risks require to be diversified. In doing so any inter-lawyer comparisons are made between specialists whose human capital investment exposes them to a similar level of risk. The residual problem here is that this sub-group system would fail to distinguish between shirking and crisis induced low productivity of an individual lawyer as a result of, for instance, divorce or bereavement. Characteristic features of close team production in legal services would be likely, however, to effectively identify real victims of such circumstances from aspiring actors.

A requirement of a minimum hours worked could be imposed on each sub-group - this could act to reduce elements of strategic behaviour by lawyers in terms of their decision whether to pass work fellow lawyers or to jealously guard and hoard clients. So long as the lawyer with the excess case load has himself worked the minimum hours then he would incur no personal loss from transferring work to a fellow lawyer. It may simply, however, be the case that lawyers are more than willing to pass clients without reward due to mutual reciprocity.

Where an individual lawyer is in a situation where he risks falling below the minimum hours worked constraint, there may be a tendency for individuals to hoard cases[31]. Within such a system there is also a potential risk that the minimum number of hours set becomes viewed as the maximum lawyers are willing to work and the system may induce little above minimum effort. Even accepting this potential but unlikely disadvantage, the system would enjoy the advantage that a minimum threshold level of shirking would be co-established.

The shirking problem does, however, involve much more than a mere hours worked factor. Hours worked is far from perfect proxy for measuring lawyer productivity. More in keeping with true productivity (but less easy to establish than hours worked) is the 'effectiveness' of legal work completed since this is the ultimate mutual aim of both client and lawyer.

The shortcoming of either an hours worked system, or productivity formula system in a productivity based system, is that incentives are created for lawyers to behave in such a way that they maximise elements of the formula rather than maximise firm profit (to the extent that maximisation is possible due to information and rationality constraints) [32].

An individual lawyer's performance is related to a complex set of internal and external motivations and influences at any particular time. Motivation and performance of individuals constantly changes over time and is not constant between different individuals at any point in time. Since many equate motivation with productivity, models which emphasize productivity measurement linked to penalty and reward mechanisms are seen as desirable because they are expected to create motivational incentives.

It is very difficult to devise a monitoring system capable of delineating different motivational levels of individual lawyers. The apparent lack of consideration the true sharing based model affords to incentive or motivation creation is argued to be the reason why it could be expected to fail to achieve that which it sets out to.

(II) A critical element of the monitoring system - self monitoring:

In any form of internal law firm organisation, there is one critical element of the monitoring and incentive system. Williamson (1985) in his discussion of his contractual framework would subsume this within what he calls "contractual atmosphere" [33]. Gilson and Mnookin (1984) introduce the enigma of firm culture, and the notion of the lawyers 'internal monitor', as the critical shirking constraint in the monitoring system of the firm [34].

The firm seeks to develop and instill a conscience in the lawyer which make him at all times wish to be perceived by any observer as exhibiting good standards and proper behaviour. Here, the lawyer bonds his behaviour where costless internal monitoring constitutes a "firm culture/ Jimmney Cricket" method of behavioural self-control. This economises on monitoring costs of the firm as the costs of monitoring are largely borne by those who are being monitored - if successful, self-monitoring is the cheapest form of monitoring.

At a more macro level, the conference of self-regulatory status on the legal profession by the state installs an omnipresent internal monitor to regulate the profession's members. The Law Societies, by being responsible for the practice behaviour of their members, act as the legal profession's conscience to society and the State [35].

The legal profession, through a purposeful combination of selection and socialisation, create a powerful internalised set of ethics and practice behaviour norms within lawyers. Within these bounds, the lawyer attempts to maximise his income in both monetary and psychic terms while avoiding behaviour perceived as bad by other members of the profession and society as a whole.

Social mechanisms serve to instill non-shirking values into the lawyer which their internal monitor/ conscience will help to enforce. The inauguration of professionalism begins at law school where only high quality work is accepted, and where only high achievers are admitted initially. Gilson and Mnookin (1984) argue that the vast percentage of lawyers tend to come from social and ethnic backgrounds more amenable or conducive to instilling those values than others [36]. There is a commitment to strict meritocracy and training techniques with various strict screening processes to weed out undesirables. The length of time taken to achieve partner status in a law firm may facilitate a mentor approach to legal training. The pupil will be influenced through exposure to both the mentor's attitudes and legal skills.

The result is a supportive firm culture which acts to reduce the typical lawyer's propensity to engage in shirking activities. In the same way that the legal profession is self-regulating collectively, individual lawyers can be viewed as largely self-monitoring. Following Alchian and Demsetz (1972), monitors will tend to have less incentive to shirk their monitoring duties if they bear the full cost of their actions/ non-actions, ie. if full, private property rights exist [37]. Shirking could, therefore, be expected to reduce the personal wealth of the monitor and may consequently expose it as a less attractive option.

1.13 Summary of relative merits of the two sharing bargain models taking into account shirking:

Following a Williamson line, it is recalled that transactions cost variations determine the usefulness of certain forms of organisation against others, and that initial contract structures are important. The features of the contract of the firm aimed at dividing partnership profits between partners discussed above, specify individual property rights and formalise the incentive structure confronting partners. Relative merits of both types of income distribution plan have been discussed in detail and at length above.

Under a productivity based plan, partners face a set of incentives more in line with sole practice -maximisation of personal aims reduces benefits of cooperation and diversification [38]. The law firm will tend to base any decision regarding monitoring on a cost versus benefits basis, to the extent that such costs and benefits are capable of being rationally quantified. Each partner is likely to face an incentive to shirk, since current period gains will accrue solely to him and any other resultant losses will be borne mutually in future by all partners.

Under equal shares, individual partner income is more directly dependent on group income and so it is rational for individual partners to behave in a manner consistent with, or at least directed towards, maximisation of the value of the firm. It is assumed by Gilson and Mnookin that the individual lawyer will allocate his time optimally between mutual monitoring and maximising the value of the firm's income [39]. This type of behaviour can lead to a situation whereby too little effort on the part of the lawyer is directed towards maximising firm income, since only a fraction of his increased effort will accrue directly to him - since all other partners stand to make similar gains from that partners increased effort.

As mentioned previously, the contract of the firm may place specific behavioural restrictions on partners. Any shirking activities by those who work part time will have a greater effect on the other full time lawyers than the shirking lawyer and part timers will also have less incentive to take part in general firm management activities. In addition to the problems of lawyers enhancing their income from outside interests (which also benefits the firm through

increased firm specific capital as discussed before), such activities enhance effort monitoring difficulties since external work may be done during company time.

Where an internal hierarchy exists within the partnership (senior partners, partners, junior partners, qualified assistants etc.) mutual monitoring and bonding may be reinforced by peer group pressure within these groups. Rewards and punishments could be usefully applied within these groups (eg. when evaluating quality of work) as it is revealed to and perceived by others in that group. This parallels the 'sub-group' argument discussed within the general analysis of the sharing bargain above.

In relation to the creation of firm specific capital (via a brand name), when a lawyer left, the firms brand name would be retained. The lawyer who exited the firm could not take with him any firm specific capital (brand name capital) and to this extent the use of restrictive covenants would be unnecessary. These would only be necessary where lawyer loyalty, rather than brand name loyalty, may encourage the lawyer to leave with his client portfolio.

As the value of the firm's brand name capital rose, it could be expected that the desire to share between the partners would be enhanced and there would be a desire to enforce the hierarchy by increasing the compensation of senior law firm members relative to new entrants in order to reflect their relative contributions to this brand name capital. The creation of increasing brand name capital would attenuate need for restrictive covenants still further.

1.14 Increases in firm size and partnership problems:

As the law firm's scale increases and its internal organisation becomes more complex, it could be expected that the costs of group organisation would tend to rise and management of the larger and more complex organisation would become more troublesome.

Under a sharing model in an increasingly large organisation, shirking becomes less easily detectable (effort is less easily monitored) and the individual may shirk or inefficiently utilize inputs since he bears a proportionately smaller and smaller fraction its costs. Hence, the scope for undetected shirking and potential inefficiency increases with size.

The costs of instigating an effective contract and discovering partners that are compatible and willing to share may be relatively high, but these can be seen as insignificant when compared to the costs of termination of a firm successful in these areas with a large stock of brand name capital. The difficulty of creating and maintaining internal harmony between parties to that contract is likely to increase with scale.

The logical conclusion of this argument is to call into question the viability of the partnership mode of operation between very large practice groups of lawyers. The agency costs of partnerships could be expected to be very significant at this level and other modes of organisation could be worthy of comparison of their abilities to constrain agency problems of legal practice.

1.15 Sources of agency problems in large partnerships - Delegation problems:

Each partner of the firm is a residual risk bearer who could be expected to wish to take all reasonable steps to protect full property rights attending such a position. By delegating authority, a partner attenuates his control over the residual risk he faces. The delegation issue confronting partners in legal practice is twofold.

(I) Delegation of legal work:

There is firstly the question of delegation of legal work within partnership. With reference to the extent to which lawyers use their delegation authority for routine work, Feinberg (1984) argues that use of paralegals for such work may not be significant [40]. This argument is based on the belief that lawyers may demonstrate a reluctance to delegate and the result may be that paralegals end up doing clerical work that cannot be billed directly to clients. This view appears to contrast with Gilson and Mnookin's view that lawyers delegate in order to buy associates' time at wholesale and sell it to clients at retail for routine transactions [41]. These two would be contrasting views are not necessarily inconsistent and can be reconciled. The delegation decision of an individual lawyer is likely to depend on his risk aversion at any given time since the lawyer, by delegating, places control of his liability in the hands of another. Feinberg's lawyer would appear to exhibit greater risk aversion and less trust of his subordinates' abilities than the typical Gilson and Mnookin lawyer.

In the real life law firm, partners are observed to delegate work right down the hierarchy of employees from qualified assistants, through paralegals, to secretaries. To protect their residual claims, partners have an incentive to monitor this delegated work and ensure that everything leaving the firm is checked by at least one partner. This is a source of agency costs since partners, by saving their time through delegating legal work, consume it again in increased monitoring. More risk averse partners may not take this monitoring role too seriously and only perform a scant check of work leaving the practice. The partnership must design formal procedures to be followed in delegated duties in order that the system is self-monitoring to a large extent and the monitoring duty at the end performed by the partner is minimal - otherwise, delegation becomes a waste of time and ineffective.

(II) Delegation of non-legal work:

Secondly, there is the issue of delegation of non-legal duties within the firm. An increasing problem as the law firm grows is the amount of time that must be consumed merely managing the day to day operation of the firm. Gilson and Mnookin (1984) argued that the lawyer may tend to under-invest his time in certain of the firm's activities where there is no direct compensation [42]. Management and administration is one area where this may occur.

Clever design of the partnership income division bargain can help create incentives for lawyers to engage in activities other than straight client-billable legal work. In areas of firm management and administration, and supervision and training of new labour inputs, there are consequences for large partnerships whose partners under-invest time in these activities. The potential solution to this problem is to assign particular partners to these functions, either by relieving them of all legal work duties, or striking some deal with them where they spend a specified percentage of their time on each function [43].

One potential solution to managing a large partnership more effectively is to delegate management functions to non-lawyers specialised in particular desired areas. When a partnership becomes large, existing partners will more than likely not possess the requisite management skills to manage the practice efficiently and effectively. From the point of view of the partners in the firm, this option is attractive as it totally frees their time to allow them to concentrate on what they know best and what brings in fee income - legal services. On the other hand, it is not attractive for partners to voluntarily weaken control of their property rights by delegating such an important function to non-solicitors. The problem with this is that any non-lawyer brought in to serve in such a function would have no residual claim in the firm - delegation to such individuals may appear unattractive. On the other hand there is the advantage of these persons having specialist skills in areas in which lawyers of the partnership do not.

The basic problem the partnership faces is a reluctance of partners to delegate decision making authority either;

1. To lower levels of staff to process legal work,
2. To one of the partners (a group of the partners) to concentrate on management and administration etc. or,
3. To specialist non-lawyers who can effectively concentrate on day-to-day running of the practice whilst the partners get on with the legal work.

The root of the problem is that due to the fact that all partners are residual claimants, there is a reluctance generally to delegate decision making authority to any non-partners or even

subset groups of the partners as this weakens control over personal residual claims through slight attenuation of property rights. In larger partnerships, delegation and specialisation in management and other non-client billable functions become almost essential effective and efficient operation - otherwise decision making can become unwieldy and cumbersome.

Consequently, major partnerships could be expected to have well structured internal organisation, perhaps broadly based on corporate management structures, with well specified linkages between decision-making functions. Each decision making function will have some decision making authority invested in it by one or all of the partners. Accountability and monitoring between such functions will also be well specified and the full partnership (or a board/ committee of the full partnership which reports to the full partnership) is expected to retain the overall monitoring function.

Feinberg (1984) recognised that three categories of partner could be applicable in larger law firms [44].

1. Finders - search for and introduce clients who will hopefully be a source of substantial and repeat work for the firm.
2. Minders - take care of existing clients and make sure they are satisfied so that they will become repeat users of the firm.
3. Grinders - do the actual legal work in the firm.

It can be seen that these roughly approximate the entrepreneur, managers and workers in the paradigm capitalist firm and they will exist if the firm assigns partners specific specialised functions within the firm.

The extent of specialisation of partners of the firm in non-legal tasks and legal work areas, as well as the extent of delegation to subsets of the partnership and to non-lawyer specialists, will be explored in the empirical study in the following chapter.

Section Two: Partnership as a labour managed firm (LMF):

Introduction:

The theory of the Labour Managed Firm highlights some interesting theoretical parallels and poses questions for the internal organisation of law firms [45]. This section examines some of these issues and their implication for the internal organisation of the law firm.

2.1 What factors could be expected to determine law firm input and output?:

The law firm's core 'members' are its partners and as such they have decision-making authority to decide whether to hire new 'members' (partners) and 'non-members' (qualified assistants, trainees and general staff), or to pursue a non-hiring policy.

Much of the literature of the labour managed firm is concerned with the issue of a 'perverse supply response'. This is where an expected expansionary policy to enlarge the firm, as a response to prevailing market conditions, does not materialise - instead, firm membership size is deliberately limited in order to enhance the existing members' per capita income. Given its similar ownership structure to the LMF it is clear that a similar perverse incentive could equally apply to partnership. The firm's partners may attempt to restrict their numbers (or those of qualified assistants) to enhance their returns in terms of shares of the firm's profit.

The usual situation within a conventional market is that for any given price reduction (ceteris paribus) quantity demanded increases - when quantity demanded increases (ceteris paribus) price increases, and when price increases (ceteris paribus) quantity supplied increases. In the case of lawyers in partnership, this simple economic logic may break down a decision may be taken to constrain output and workload dependant upon certain factors, including:

1. The process used by partners to determine number of hours they wish to work,
2. Non-work activities from which partners benefit and their leisure/ work trade-off,
3. Whether partners have a target (or minimum) level of fee income in mind.

Hence, an increase in quantity demanded (stimulated through price reduction) may not provoke behaviour predicted by conventional demand theory, and a parallel is drawn between behaviour of the law firm and the behaviour of the LMF [46]. The LMF, therefore, bears striking similarities to the organisation of legal partnerships and this parallel will be developed throughout this section of Chapter Six.

For instance, it would be predicted by conventional demand theory that a general increase in competitiveness in the market for legal services (in terms of determination of fees charged), result in an increase in total firm input and output. The LMF Literature would suggest the opposite to be true of the typical LMF when faced with similar circumstances [47].

Kwon has applied the 'equal revenue cooperative sharing model' of the LMF to the legal partnership. Sisk challenges the appropriateness of this application of the LMF model on the grounds that non-members (non-partners) may also be hired by the law firm. Kwon defends the validity of his analysis, retorting that predictions of the model are valid irrespective

whether or not, firstly, an equal sharing bargain exists, and secondly, non-members can be hired [48].

In the legal partnership, employees will be paid a wage, whereas it is the usual case that partners are paid a share of residual income of the firm - partners are residual risk bearers. In some firms, a category of salaried partner often exists but this is more usually a short term temporary situation before full profit sharing status is permitted [49].

The structure of the existing partnership will be determinative of the attitudes of qualified assistants towards partner status. The incentive structure will attempt to encourage qualified assistants to strive to reach partnership by working extremely hard for the firm. Where the incentive structure is weak due to low perceived chance of being made a partner, qualified assistants interested in becoming partners will be discouraged from working hard and may in fact leave to increase chances elsewhere. Important features of this incentive structure for qualified assistants will be; ages of existing partners, retirement rate, ratio of employees to partners, projected firm growth and the like. Such signals will be perceived by the ambitious qualified assistant as indicative of promotional chances or otherwise.

2.2 Mitigating the perverse supply response:

(I) The use of tradeable shares - The use of tradeable shares is advocated in the LMF literature as a method of at least partially mitigating the perverse supply response. A precondition of the shares argument is that shares must only be tradeable between persons who have sufficient skill to become potential members of the firm. Within the typical law firm this situation strongly applies since there is a formal screening process for those considered for partnership profit sharing. The partnership agreement may also explicitly make provision for all new members/ partners to buy into partnership - this can be seen as a form of tradeable share [50].

Within the legal profession as a whole, it can be argued that a market for membership certificates exists - in order to practice legally, the individual must be a qualified practitioner. This qualification permits the individual to capture a larger proportion of the value of output arising from his and other non-lawyers' inputs to the firm, than non-lawyers within the firm.

The secondary membership market in legal services is that which exists for partnership places. When the lawyer reaches partner status, he may collectively with fellow partners, exploit non-partners of the firm to capture returns to his investment in human capital. Previously, personal returns to this human capital investment are likely to have been disproportionately small, in relation to his input. After partnership status has been attained

the situation will usually reverse - it is perhaps knowledge that eventually this reversal situation is likely to occur which encourages lawyers to suffer pre-partnership 'exploitation'.

(II) The nature of utility functions - The LMF model also advocates that the nature of the utility function of the individual concerned, can also mitigate the perverse supply response. There is an inherent difficulty here since, although utility functions are a plausible and useful theoretical abstraction, their role is severely limited beyond this. It is difficult enough to identify all constituents of an individual's utility function, never mind aggregate them and then maximise their resultant sum. This problem is compounded further when it becomes necessary to conceptualise, and attempt to determine, the utility function of the partnership as a whole. As a result of this and other reasons, it is, therefore, impossible (outwith theory) to pursue, without conflict, the sum of these objectives to utility maximise and mitigate the perverse supply response.

The utility function argument, although theoretically neat and plausible, is therefore too unrealistic a concept to pursue at great length. While the nature of individual lawyer's utility functions and preferences, and their interaction with those of other lawyers within the partnership, would be important in partnership, it is difficult to imagine how one might theoretically model this, never mind empirically test any hypothesis derived there-from. In any case, if one accepts the plausible and more realistic 'Simon' view of human rationality, maximising behaviour is not a characteristic of individuals - individuals are far more likely to exhibit satisficing than maximising behaviour according to Simon [51].

There is a difference between the perverse supply response of the collective group and the 'supply curve' of an individual member of that collective bending backwards. This latter instance is akin to shirking, where a lawyer free-rides on other members' efforts. Clearly, such behaviour is independent of the supply responses of the overall firm. The firm could be responding to market forces in a non-perverse manner and simultaneously, one or more of the lawyers in the firm, could be shirking. The partners as a group can also supply a low effort intensity and free-ride on non-member workers of the firm - this can take the form of extensive delegation and lawyers who engage in this type of activity may simply act like professional signatories.

The law firm can be seen as being a 'closer' cousin of the LMF than of the standard Neoclassical firm, since pursuit of a strict Neoclassical profit maximising objective is unlikely in legal practice. Firstly, profit maximisation may be incompatible with ethical legal practice, and secondly, profit maximisation is unrealistic given bounded rationality.

2.3 The theory of the LMF - a deeper investigation:

The basic model of the externally financed LMF is the result of a progressive refinement of a concept first introduced by Ward (1958) [52]. Major examinations, and analytical refinements, of the model were made by Vanek (1970) and Meade (1972), with the full blown model adopting the title of the Ward-Vanek-Meade LMF [53].

The model is constructed on four principal assumptions, summarised below;

1. The firms management function is invested in the workers of the firm, who are at liberty to set output and employment at any level they should choose.
2. Non-labour inputs are hired at market clearing prices. Initially, the model assumes capital to be the only non-labour input, and it is rented at a rate (r).
3. Decisions made within the firm, are assumed to be motivated by a desire to maximise the net income per worker, where all workers are seen as homogeneous. Further simplification requires that all of the output of the firm is sold at a parametric price (P).
4. Uncertainty is assumed away.

The important characteristic of the LMF is that it exhibits a short run perverse supply response to changes in parameters of the model [54]. This is characterised by a reduction in the labour force in response to a rise in price or fall in rental of capital. This is the opposite comparative static response to that expected of the LMF's capitalist counterpart espoused in Neoclassical theory.

An essential feature of the labour managed firm, is that labour is only hired in situations where it increases the value of its marginal product.

(I) Internal financing of the firm:

Vanek (1970) argued that an examination of the internally financed LMF may be a more realistic analysis than that of the externally funded LMF [55], based on his belief that the LMF will lean heavily on the internal financing option in a capitalist society. He bases this assertion on two reasons:

1. The external capital market is unlikely to provide the necessary investment due to lack of incentives. In the case of the law firm, external financing is not an issue anyway since all firm members must be qualified solicitors.

In the case of legal partnerships, there is no real incentive either for solicitors to have purely equity interests in a partnership as a sleeping partner. In the case of legal practice the external capital market would be unlikely to provide investment funds since investment would appear

unattractive, given the lack of control over risk available to investors due to monitoring difficulties. Secondly, in the specific case legal partnerships, the need for ethical considerations would constrain a profit maximising objective. This would render other forms of investment more attractive to profit motivated external investors, due to higher expected returns.

2. The ideological stance of those forming a cooperative, is likely to demand an avoidance of reliance on established capitalist institutions.

If external finance was a necessary consideration for law firms, this may certainly be true of lawyers since they are perceived to be members of a very insular profession, who have a desire to remain as independent as possible to retain absolute control over their operations [56].

Exclusive reliance on internal capital investment precipitates two main problems. Firstly, there is the question of property rights. Existing members of the firm will have no right to income beyond their term of employment and, hence, they are devoid of the ability to sell their membership rights to others after their term expires. It is rational, therefore, for them to demand a rate of return on their capital investment which embodies a premium, beyond their simple rate of time preference.

In the context of legal partnership, this earnings life-cycle argument can be seen to partially explain the high income levels of established partners in relation to newly accepted partners and other non-partner lawyers within the firm. This is a justifiable attempt to obtain as quick a rate of return on their human capital investments as possible since it is a continuously and swiftly depleting asset - at retiral it is worth nothing.

Secondly, Vanek (1970) argues that the maximand of the internally financed LMF is different from the external capital funded LMF [57]. For the internally financed LMF facing a technology exhibiting constant returns to scale, long run maximisation of per member income implies a gradual running down of the labour force and membership.

(II) The forces of self extinction of the firm:

Vanek (1970) views the forces above leading to eventual self-extinction [58]. A decrease in the labour force can augment per member income, in the face of diminishing returns to labour. In the absence of compulsory expulsion via natural wastage through leaving or retiring, it is relatively easy to decrease the labour force. Hence, a deliberate non-replacement policy can augment per member income and through reductions in labour, the labour:capital ratio ceases to be optimal. To reestablish this optimum, the capital stock is adjusted downwards and

through time, a cycle is established whereby the combination of forces will ensure eventual extinction of the firm [59].

Pursuit of the original maximand of the firm (maximisation of per member income), will create a tendency for under-investment in the internally financed LMF. In an externally financed LMF, optimal utilisation of capital implies that capital should be employed up to the point where the value of its marginal product equals its price. If it is accepted that the marginal product of capital diminishes, it can be expected that the internally financed LMF will (ceteris paribus) employ lower levels of capital than the externally funded LMF [60].

An inevitable consequence of this longer term process of continual readjustment of sub-optimal capital:labour ratios to achieve temporary optima (through increasing or decreasing capital stocks, or decreasing the labour force), is that the labour force is never expanded - this action would of course reduce per member income in the long run. The existence of a technology initially exhibiting increasing, and thereafter decreasing, returns to scale partially obviates the previously discussed effects on the internally financed LMF.

This may be of direct relevance to law firms since it is likely to be the case that, in many areas of legal work, there may not exist significant economies of scale. In other areas there may be almost immediate exhaustion of economies of scale. In the instance of increasing returns to scale, any reduction in membership size results in a forfeiture of scale economies.

(III) The hiring of non-member labour:

The hiring of non-member labour can lead to a partial mitigation of the perverse supply response. It is to the advantage of existing members to substitute hired labour for leaving or retiring firm members. It is this process which is alleged to result in a loss of internal democracy in the LMF. To this extent, non-member labour substitution undermines the whole ethos of, and rationale underpinning, the LMF.

The hiring of non-member labour alters the comparative static responses of the LMF to the extent that its behaviour broadly resembles that of its capitalist counterpart, the sole difference being that the LMF will use a less capital intensive input mix. In this context, the law firm has a production process which is very human capital (labour) intensive. It is also worth noting at this juncture that it is normal practice for the lawyer to delegate a fair amount of legal work to non-partner, ie. non member, employees of the firm. This can be viewed as a perfectly rational response as the law firm can buy in cheaper labour units' time and sell it to the client at members' (ie. partners') rates.

The extent of delegation authority in legal partnerships is bound by legal rules which state that certain types of work may only be conducted by qualified practitioners. This legitimacy attaches itself more specifically to the ownership of the law firm than delegation, so delegation within that law firm can be extensive (ie. to non-lawyer personnel, so long as it is checked by legally qualified staff). It is likely to be the case that in certain circumstances the checking procedure is not carried out and what effectively exists is non-legally qualified personnel undertaking work that can only legally be undertaken by legally qualified staff.

Overall, the legal profession can be seen to have a very labour intensive productive process as a result of the human capital intensive characteristic of professional services. This is due to the nature and form of regulation of legal services, rather than a reflection of the mode of organisation employed to render them to clients.

(IV) Unequal members' shares and the hiring of new members:

The concept of unequal member shares, further attenuates the internal democracy of the LMF. In the context of legal partnerships, it is often the case that the members (partners) have unequal shares of profits. The implications of different types of profit sharing bargains has been the subject of extensive discussion above in this chapter.

In order that existing hired workers may be accepted into membership, the value of the incoming workers marginal product must rise. It is only under this condition that it is to the benefit of existing members to permit admission. The inegalitarian cooperative, avoids the short run perverse supply response by altering membership size in the necessary and desired direction. This process is achieved by equating the externally determined wage, received by labour, to the value of the marginal product of labour. The counterpart real life law firm has a similar process involving the employment of salaried partners and other categories of non-partner lawyer labour.

The trade-off existing in LMF organisation, is that efficient economic behaviour can only be procured at the expense of a truly egalitarian income distribution within the firm. This situation can be altered by the issuing of marketable membership shares. Relating this concept to law partnerships, this process can be seen in terms of the existing partners inviting prospective partners to buy into the partnership. Here the marketable share is an opportunity for the successful entrant to share in the brand name capital of the firm. The partnership will set the price of this sharing opportunity to reflect a fair and true valuation of the collective goodwill/ brand name capital of the partnership [61].

There will be a number of factors that will affect the law firm's willingness to employ qualified assistants. The partners will hire/ fire and control the firm and they will have sole

decision making authority regarding whether to increase membership size and/ or the numbers of non-members, to increase firm size. It will be perceived by the existing members to be desirable to increase partnership size and/ or increase non-members if this will increase their income shares, or if it will satisfy some other component of their utility function (eg. reduced workload, increased leisure etc). It appears not unreasonable to suggest that the lawyer, like the typical worker in most situations, may be conscious of his workload/ leisure trade off which will be subject to constant change depending on numerous factors. The trade-off aimed for may be consistent with some personal target level of fee income where he adjusts his activities to yield this combination. The problem the lawyer faces in this respect is determining whether the costs in terms of foregone leisure of the increased workload is worth it in terms of the benefits of the resulting increased personal income. This calculation will not be scientifically quantified and a simple and crude qualitative determination of the decision will be made. This is necessary because of a lack of information and rational capacity to evaluate such decisions.

Any income target and corresponding workload/ leisure trade-off will be based on his training, historical experience and continuously revised expectations of future contingencies, amongst a multitude of factors. The resultant outcome selected, at any moment in time, could be construed as a static personal independent attempt to maximise his utility, to the extent that maximisation is possible - in fact, the selection is more likely to be that which satisfies him most at that point in time[62].

In very simple terms the partnership decision can be seen as a game between existing non-members of the firm and the partners. The outcome of the game solves the conflicting aims of qualified assistants (who have a desire to be promoted), and existing partners (who have a desire to limit their numbers in order to preserve per member income). Partners, however, may perceive it to be in their interests to keep the promise of partner status as 'a carrot' for qualified assistants, to prevent loss of discontented qualified assistants (possibly with clients in tow).

A finite, though not necessarily coinciding, time period is involved here for both parties. Qualified assistants will have expectations regrading the time period after which they could reasonably expect an offer of partnership. Should an offer fail to materialise after this expected period, they will discount the credibility of any future promises made by partners. The ultimate demonstration of their discontent will be their action of leaving the firm - this termination imposes costs on both sides and is at best a zero-sum game for the partnership [63].

Literature of the LMF argues that it is in the interests of partners not to promote qualified assistants to partner level in order to preserve per partner income. Partners face a dilemma

here since, if they do promote they may lose some personal income, but if they do not they may lose the QA (and perhaps some clients), some fee income, and work will no longer be able to be delegated to those QAs that do leave. It is likely, therefore, that partners will wish to promote the qualified assistants within their particular expected time period to prevent them leaving. The problem faced by partners is that it is difficult to calculate the particular time periods involved, and it is likely to be a gut feeling whether or not to promote to partner or not. A whole range of factors will enter the partnership decision, beyond that of the effect on income shares (if, in fact, this could be calculated with any degree of accuracy).

The process strictly requires that partners can identify the period of time in which each qualified assistant expects to be offered partnership. Alternatively, partners could promote the qualified assistant when he threatens to leave, but this may sour good relations between them[64].

To maintain the long term viability of the partnership, promotion of qualified assistants is essential at some point in time to prevent mass exodus from the partnership by qualified assistants [65]. In the longer term, the non-partner hiring firm may face difficulty in recruiting QAs if its non-promotion reputation is made public. The process by which this whole complex issue is resolved will hopefully become more apparent in examination of the results of the empirical study and discussion of employment relations in partnerships in Chapter Eight of this thesis.

The fundamental issue arising from discussion above is the issue of the process by which the legal partnership attains long term growth and survival. It is not unrealistic to assume, that law firms will be subject to some form of natural/ organic growth as a result of reputation effects, and the resultant expanded client base. Contrary to the expectations of the theory of the labour managed firm, there may also be a conscious and deliberate expansion policy for the partnership. This will be revealed in the empirical analysis conducted in the following chapter.

(V) What is the maximand of the firm?:

In the model of the utility maximising LMF, the maximand of per member income assumed in the simple LMF model is criticised as over simplistic. The U-max LMF model is, therefore, augmented by introduction of the parameter 'number of hours worked by each worker'. This involves introduction and use of both individual, and group, utility functions.

By introducing the number of hours worked parameter, certain problems are created within the model. A number of unanswered questions remain including major ones such as, how the group utility function is determined and how the total number of hours worked is distributed

between the members. The link used here is that, in all probability, the shape of the utility function would determine the spread of hours worked between the members. Analyses employing individual utility functions, in the LMF, are indicative of the importance of observing the number of hours worked, rather than membership, as the important short run variable in advancement and refinement of a useful theory of the LMF.

A useful analysis of the legal partnership, follows a broadly similar path, since a primary focus is the nature of the sharing bargain between partners of the law firm - relative productivity/ hours worked, as well as membership criteria, are important and are the subject of empiric examination to determine roles they both play in legal partnership organisation.

Such analysis aims to discover how partners of law firms determine the hours they will work respectively, and also how their relative incomes are determined. In attempting this it is anticipated that analysis will provide some indication of the nature of constituents of individual lawyer's utility functions. This of course will involve generalising since every lawyer is likely to have a unique set of utility preferences and behavioural motivations.

Partners of a law firm may attempt to maximise net income per member, much like members of a LMF. The law firm can be seen in terms of a joint venture/ production, where the partners share assets and liabilities, pay receipts to the firm, collectively pay expenses and then distribute pre-determined shares of income between themselves. In partnership, partners should avoid any pure personal financial interest in client work since this would be work done behind the backs of other partners purely for self-gain. This does not, however, preclude partners from having their own client portfolios and this allocation of clients issue is but one of the multitude of other problems the partnership seeks to solve via its profit sharing bargain. Many of these issues have been discussed in theoretical terms above, and will be empirically examined in the following chapter.

Certain elements of group decision making are essential in partnership and there is, consequently a strong requirement for collective cooperation. Kwon argues that, in the case of the equal sharing law firm, partners will only agree to admit the marginal lawyer, so long as the value of this marginal lawyer's output is such that it enhances each infra-marginal lawyers income [66]. He argues that this can lead to paradoxical behaviour (known in the LMF literature as the perverse supply response) directed at increasing per member income.

It may be difficult for partners to accurately evaluate this decision based on comparative revenue calculations since information on income, before the new admission, and projections as to what it will be after the new admission, is unlikely to be available. In any case, the decision may not be as simple as Kwon suggests[67]. It is anticipated the empirical study will

demonstrate that the partnership decision will typically encapsulate many more features than simple income considerations and will play a central role of screening prospective partners.

The law firm can be regarded as a multiproduct firm employing multiple inputs, where the relative size of product groups it processes is determinative of income and risk attending the firm. An expansion of the firm's membership can cause the productive possibilities to widen, as can the introduction of non-member labour. In the short run, the law firm can alter combinations of its services to satisfy demand. In the long run, additional workers may be hired, or disposed of, in order that some perception of "optimal firm size" is achieved. This optimal size, in the context of the simple labour managed firm model, will be that which maximises per member income, with the corresponding efficient capital stock. The addition of non-lawyer workers changes the situation in terms of delegation authority, where there are more workers to delegate work to. This may enable more effective, and efficient, use of the firms categories of labour input.

The lawyers in the partnership could be expected to be required to supply a certain level of effort intensity to the firm, by the other partners. This will reflect their case loads, and the quantity of capital they employ. In the law firm, partners have complete property rights so any instances of under-employment could result in wealth losses to the partners since they are the owners of the capital of the firm. Sisk argues, therefore, that an incentive is created to avoid under employment to circumvent wealth losses to the partners [68]. He further argues that creation of a non-equal sharing bargain can effect this. This can be seen as paralleling the effect that unequal membership shares have in constraining the perverse supply function in the inegalitarian cooperative model. This of course undermines true sharing and enhances inegalitarian features of what should be a very democratic form of organisation.

In fact, lawyers may achieve efficient levels of output and employment through hiring workers at fixed salaries from the labour market at market clearing rates. These are typically law school graduates, paralegals and the like.

The nature of the group utility function in the labour managed firm poses problems for economic analysis. The only simplifying factor here is that it is likely that its constituent members may demonstrate, through setting up such a collective, that they are like-minded - to that extent, their behaviour may be relatively homogeneous as a group.

The partnership can be viewed as a complex long term contract where there is a mutual desire to maximise the sum of monetary, and psychic, income per member. Clever design of the partnership profit sharing bargain aims to achieve this whilst concurrently attenuating incentives for individuals to act opportunistically, and shirk on the agreement.

It is not unreasonable to assume that each partner has an objective of attempting to maximise income. The pursuit of this goal is likely to impair at least one, if not several, of the other lawyers' activities aimed at maximising his personal income - all lawyers in the practice do not practice independently but inter-dependently. The objective assigned to the LMF of maximisation of per member income, therefore, requires that every members' objective can be simultaneously achieved. Alternatively, a sharing bargain exists which operates and ensures the outcome occurs whereby each partner ends up with that level of income which coincides with that which he perceives as his maximum attainable - this sum of monetary and psychic income could be seen as some measure of his utility.

Practising in partnership allows lawyers to capture returns to their human capital investments, and the theory of the LMF proposes that such an organisation facilitates this. In the case of a corporation, external shareholders would also benefit to some extent and reap some returns to lawyers' human capital but it is likely that the practising lawyers of the firm would act like opportunistic managers would in a managerial discretion model, given incentives they face and weak external monitoring.

(VI) Problems facing the LMF in a capitalist environment:

Williamson (1985) notes the nature of the dilemma facing the LMF in a capitalist economy [69]. Social scientists argue that the advantage of the LMF is that of mitigating problems arising from authority relationships. Given this alleged advantage, there is a surprising lack of adoption of this form of industrial organisation to be observed in reality. This can be seen to be a result of a number of factors:

1. The cooperative will experience difficulty in attracting sufficient levels of external capital.
2. Low levels of wages are usually paid to the workers of the cooperative.
3. Irrespective of the potential efficiency of the LMF, it is difficult for such a firm to survive in a capitalist environment. This is due to difficulties;
    a) in obtaining sufficient bank and trade credit,
    b) in retaining good management who see higher returns in capitalist firms and,
    c) in sustaining the firm due to an unwillingness to admit new members due to a reduction in per member income (the short run perverse supply response).

In terms of analysis of law firms, it is the case that partnerships have relied successfully and exclusively on internal finance (external capital provision being specifically prohibited). This is most likely due to the fact that the largest investment in the law firm is that of human

capital. It has also managed to retain staff - most probably due to limited opportunities open to lawyers outwith private practice. Additionally, very few, except the largest firms, actually employ non-lawyer practice managers. These two features are increasingly under threat as opportunities are opening up for lawyers outwith private practice and also, many firms are now realising the benefits of specialised practice management by non-legally trained personnel.

As for the perverse supply response, behaviour of law firms is uncertain. This will of course be consequent on the nature of lawyers' utility and the nature of the sharing bargain. This non-expansion/ non-hiring issue will be pursued in the empirical analysis in the following chapter.

Recent discussion concerning mixed and corporate practice, as a response to meet the needs of the modern market in professional services, may be indicative that the partnership form cannot continue to be viable indefinitely. This is with particular reference to the increasing reliance on the market in modern capitalist society. Partnership organisation is challenged as becoming increasingly unable to meet the demands imposed on it by the market for legal and other services. This may turn out to be a real world example of Williamson's argument concerning the sustainability of LMF's in capitalist economies.

In modern times we also witness an increasing tendency for lawyers to enter non-private practice fields of business ie. merchant banking, stockbroking etc. after they have completed their law degree. This could be indicative of a change in the type of person that now enters and passes through law school or that attitudes of those coming through now are characteristically different.

The modern corporation, in Williamson's view, has been the result of a series of organisational innovations that have aimed at economising on transactions costs. He also recognises the quest for monopoly power, and the imperatives of technology as important factors that have shaped modern corporate firms. In the case of legal practice, corporations have previously been outlawed, but they have been discussed lately as a viable option worthy of consideration for legal practice. Recent legislation has reduced the solicitors monopoly over certain services and now, in parallel with the above arguments, the legal profession is finding it more difficult to survive in its present form.

It can also be argued that there are different behavioural implications for the individual faced with either a capitalist or a cooperative form of organisation. These differences are outlined below:

1. Incentives differ.
2. Short run adjustments differ.

3. Free entry is of greater importance in the cooperative system.
4. Monopolistic behaviour differs since one could expect a greater number of firms in a cooperative system. These firms are, however, likely to be of a smaller scale generally.
5. Macroeconomic effects differ.

The law firm could be argued to act along similar lines to the Participation and Profit Sharing Firm that Meade (1972) proposes [70]. In this type of firm, the same rules apply to the suppliers of both capital and labour. Such a set up would be a combination of an inegalitarian joint stock company (so far as capital was concerned) and an illegalitarian cooperative (so far as the supply of labour was concerned). Meade calls this firm an 'illegalitarian joint-stock-cooperative-firm'.

While property owners can spread their risks by putting small bits of their property into a large number of concerns in a portfolio of property interests, the worker cannot easily put small bits of his effort into a large number of different jobs. Hence, typically the situation we have is risk bearing capital holders hiring labour, rather than risk bearing labour hiring capital. In the case of the law firm the major capital injection is of a human nature and therefore is tantamount to labour as it exhibits the same characteristics.

Labour is unable to diversify its risks, so cooperatives will tend to exist where risk is small in terms of the activity undertaken by labour. By small risks we mean that the risk of fluctuations in demand is small. Cooperative organisation is also more probable where the activity is labour intensive (where the surplus accruing to labour does not constitute a small difference between sales revenue per unit and the cost of raw materials plus capital hiring costs per unit). This is true of production in legal services.

The labour partnership is a continual conflict between efficiency and equality, as the pursuit of one of these goals encroaches on the attainment of the other. The problem is essentially the nature of the sharing bargain existing, firstly, between old and new members and, secondly, also between members of one peer group. The issue of risk spreading of human capital assets of these members, is also of prime importance. These two issues have been addressed at great length in earlier sections of this chapter which introduced portfolio theory and the nature of the partnership sharing bargain.

Chapter Six - Endnotes

1. See: Gilson, R.J. & Mnookin, R.H., Sharing Among the Human Capitalists: An Economic Enquiry into the Corporate Law Firm and How Partners Split Profits. Stanford Law School Working Paper, No. 16, Chapter Vol. 37, 1984 See also; Rosen, S., The Market for Lawyers, Journal of Law and Economics, Vol. XXXV, October 1992, pp.215-246.

2. See; Gilson and Mnookin (1984), *supra* Note 1. at p.316

3. The word optimal in this context presupposes that the firm has the information and ability to make such optimal allocations. Given bounded rationality and information deficiency, it is likely that they would be unable to optimise. It is, however, undoubtedly the case that they are likely to be able to make better use of inputs to the firm's production process.

4. Many economies of scale can be achieved in smaller scale operations. The existence of specialist firms (both large and small) demonstrates that specialisation itself is relatively independent of firm size. There is no reason why the firm, rather than the client, should capture the returns to economies of scope. In many areas of legal practice, the minimum scale and necessary size of production team is not sufficient to warrant the absolute size of many law firms of today, even in areas of corporate client work.

5. See Chapter Three for a lengthy discussion of these deficiencies.

6. See; Gilson and Mnookin (1984), *supra* Note 1.

7. It should be noted here that this argument exhibits parallel features to those presented in analysis of the labour managed firm later in this chapter.

8. See; Gilson and Mnookin (1984), *supra* Note 1. at p.321.

9. Risk, in the context of economic analysis, encapsulates both upside and downside risk ie. anything that can cause the asset to deviate either negatively, or positively, from its expected value.

10. See; Gilson and Mnookin (1984), *supra* Note 1. at p.326.

11. See; Gilson and Mnookin (1984), *supra* Note 1. at p.329

12. Such elements are unlikely to become diversifiable through insurance markets in the foreseeable future. These elements such as alcoholism, divorce etc. suffer from twin problems of moral hazard, and adverse selection, and are thus seen as, and are likely to remain, uninsurable risks.

13. See; Gilson and Mnookin (1984), *supra* Note 1. at p 329.

14. See; Gilson and Mnookin (1984), *supra* Note 1. at p.332.

15. See; Gilson and Mnookin (1984), *supra* Note 1.

16. See; Gilson and Mnookin (1984), *supra* Note 1. at p.330.

17. This risk may not be as large as Gilson and Mnookin (1984), *supra* Note 1., tend to suggest as most major law firms, at least in the UK, are relatively stable and long term ventures. The same may not, however, be true of USA law firms.

18. See; Fama, E. and Jensen, M.C., Separation of Ownership from Control, ***Journal of Law and Economics***, Vol. XXVI, 1983, pp.301-326. See also, Fama, E. and Jensen, M.C., Agency Problems and Residual Claims, ***Journal of Law and Economics***, Vol. XXVI, 1983, pp.327-352.

19. It should be noted here that maximising behaviour requires that the partner has the relevant information and sufficient rationality in order maximise. It has been argued at various points throughout this thesis that neither this level of information, nor rationality, attends the typical individual within the firm. As such the partner may satisfice rather than maximise.

20. See; Gilson and Mnookin (1984), *supra* Note 1. at p.349.

21. See; Gilson and Mnookin (1984), *supra* Note 1. at p.348

22. It is worth noting at this point the similarity between this discussion and that of the labour managed firm which will follow on in the next section of this chapter.

23. It should be noted that Chapter Four discusses this in great detail.

24. The law will tend not to enforce covenants that are more widely restrictive than necessary. They are often part of the co-partnery agreement and, if freely entered into at the time of agreement, could be perceived as reasonable by those party to the overall agreement. As we are dealing with solicitors, it is further reasonable to presume that they are fully aware of the legal consequences of signing such an agreement. The geographical area is important, as is the length of operation of the restriction, with restrictive covenants. It tends to be the case that the courts will look at what the effect is on the clients in question. They will tend to go against the agreement, where the clients right to go to whom he chooses for his legal services is affected by such a covenant and hence, the public interest is diluted (balance of convenience). See Dallas McMillan & Sinclair vs Simpson. Court of Session Outer House, Lord Mayfield Oct.28, 1988. in Scotsman Law Report 6/1/89.

25. Here, it is possible that the client and law firm could collude to attract business. The law firm could provide incentives to the client to do so, eg. low billing rates, free services etc. It is difficult to imagine how this situation could come about in all but long established corporate client relationships but business networking of this sort clearly occurs. It is, however, difficult to analyze these types of relationships in economic theory.

26. This concept has been discussed in-depth earlier in this chapter.

27. By undertaking such a strategy, the law firm runs the potentially high risk of poor quality, not only adversely affecting consumers' perceptions of the quality of the particular specialty involved, but also that of it's other specialties. Hence, the output of a multi-service firm requires to be of a relatively uniform quality, at all times, to avoid the aforementioned inevitable consequences of poor quality practice.

In the case of the single specialty firm, quality assurance of this type of 'department store' practice is not available. The argument for mixed disciplinary practice employs the department store analogy and further relies on an expectation of lower search costs, procured by the physical proximity of different professional functions.

28. See; Gilson and Mnookin (1984), *supra* Note 1. at p.360.

29. See; Gilson and Mnookin (1984), *supra* Note 1. at p 354.

30. See; Gilson and Mnookin (1984), *supra* Note 1. at p.390.

31. It may be desirable from a firm production plan point of view and evening out of caseload perspective for that lawyer to actually do the work himself even though there may be associated efficiency losses.

32. There is a clear difference between behaviour directed at maximising elements in a formula/ proxy for productivity, or working requisite minimum hours, and actual productivity/ constructive effort.

33. See; Williamson, O.E., **The Economic Institutions of Capitalism.** Free Press, 1985.

34. See; Gilson and Mnookin (1984), *supra* Note 1. at p.371.

35. See; Chapter One for an in-depth discussion of the function of socialisation of the Profession, in this regard.

36. See; Gilson and Mnookin (1984), *supra* Note 1. at p.378.

37. See; Alchian, A.A. and Demsetz, H., Production, Information Costs and Economic Organisation, ***American Economic Review***, Vol.62, 1972, pp.777-795.

38. In this respect, the pursuit of personal satisfaction and not necessarily personal maximisation, may be a more realistic description of likely behaviour. Nevertheless, other behaviours reduce benefits of productivity based partnerships.

39. See; Gilson and Mnookin (1984), *supra* Note 1. It is, however, likely to be the case that such an optimal allocation would be impossible for the individual to instigate, given information problems and bounded rationality.

40. See; Fenberg, R.M., Paralegals and Substitution among Labour Units in the Law Firm, ***Journal of Industrial Economics***, Vol.XXXVI No.1, Sept. 1984.

41. See; Gilson and Mnookin (1984), *supra* Note 1.

42. See; Gilson and Mnookin (1984), *supra* Note 1. at p.349.

43. There is a problem here since working full time, for example, in a management function would perhaps mean that the partner could lose track of his client base and suffer losses in this respect. The clients may also leave the firm if they feel they no longer have the point of contact of that partner in their relationship with the firm.

44. See; Fenberg (1984), *supra* Note 40

45. The Labour Managed Firm literature is associated with the pioneering work completed in this area of theory by the following authors; Meade, J.E., The Theory of Labour Managed Firms and Profit Sharing, *Economic Journal*, Vol.82, 1972, special issue, pp.402-428; Ward, B., The Firm in Illyria: Market Syndicalism, *American Economic Review*, Vol.48, 1958, p.429; Vanek, J., **The General Theory of Labour-Managed Market Economies**. Cornell University Press, Ithaca, 1970; Vanek, J.(ed), **Penguin Modern Economics Readings in Self-Management**. Penguin, Harmondsworth, 1975; Vanek, J., **The Labour Managed Economy**. Cornell University Press, Ithaca, 1977. See; Stephen, F.H., **The Performance of Labour Managed Firms**. Macmillan, 1982, and; **The Economic Analysis of Producers Cooperatives**. Macmillan, 1984, for a comprehensive analysis and summary of the Ward-Vanek-Meade model of labour managed firms.

46. The LMF is an organisational form, popular and prevalent in the Yugoslavian economy.

47. At the same time it could be anticipated that the degree of conflict between the objectives of the law firm and its clients may be diminished through greater competitive pressures in the market. Free entry and exit from the system would also be more in keeping with conditions tending towards Pareto optimality - a condition allegedly attained by the theoretical labour managed firm in the Socialist economy

48. See; Kwon, J.K., A Model of the Law Firm, *Southern Economic Journal*, Vol.45, No.1, pp 63-74 and; Sisk, D E., A Model of the Law Firm: Comment, *Southern Economic Journal*, Vol.48, No.1, pp.227-233.

49. The importance of the selection and screening function of this apprenticeship period is discussed elsewhere in this thesis.

50. This tradeable shares concept has still further relevance in the context of the legal firm. In debate of the issue of corporate legal firms, many of the profession are concerned that it is essential that membership of the corporate law firm is restricted to qualified members of the profession. This concern may be derived from a desire to retain professional control within the profession as much as it is founded in the concept of sufficient skill. These two concerns are not, however, unrelated.

51. See; Simon regarding his emphasis on satisficing rather than maximising behaviour - Simon, H.A., **Models of Man**. John Wiley & Sons, New York, 1957; **Administrative Behaviour: A Study of Decision Making Processes in Administrative Organisation**. 3rd Edition, New York, Free Press, 1976, Rationality as a process and as a product of thought, *American Economic Review*, Papers and Proceedings, 1978, at p.1; Rational decision making in business organisations, *American Economic Review*, Vol. 69, 1979, at p.493.

52. See; Ward (1958) *supra* Note 45.

53. See; Vanek (1970) and Meade (1972), *supra* Note 45.

54. In this instance, the Marshallian view of the short run is employed, where capital stocks are assumed to be fixed. In the long run, it is expected that capital will also be subject to an adjustment process in response to changes in price and cost conditions.

55. See; Vanek (1970), *supra* Note 45.

56. As a result of monitoring difficulties, it is unlikely that external investment would be forthcoming in the event of the development of corporate law practices. The organisation would be likely to remain a quasi-partnership with the lawyers, who were previously partners, assuming the role of managers and investors (shareholders).

The net result of this would be that the change in organisational form would not affect the behaviour of the lawyer to any great extent. The risk facing the lawyer would change, however, depending on the limit of liability deemed to be appropriate for corporate practice. High potential levels of corporate debt may render the combination of corporate practice and unlimited liability unsuitable, but in any case, the issue appears to revolve primarily around the question of availability and extent of adequate professional indemnity insurance.

57. See; Vanek (1970), *supra* Note 45.

58. See; Vanek (1970), *supra* Note 45.

59. Should the firm decide not to adjust its capital stock in a downward direction, then this is behaviour inconsistent with maximisation of per member income assumed in the model. This behaviour is only rational behaviour if it is consistent with the maximand of the firm as viewed in terms of some other stated utility function which does not simply solely constitute maximisation of per member income.

60. This is a direct consequence of the fact that the marginal product of capital is always above the worker-manager's rate of time preference.

61. The firm may attempt to expose the maximum amount the prospective entrant is willing to pay for entry. It is anticipated that the empirical study will expose the nature of the process involved, when it is desired that membership should be increased. The mechanism that facilitates choice between prospective partners will also be of empirical interest.

Theory suggests that it would be advantageous to set up a contest between prospective applicants, with a system similar to sealed bids or tenders of the amount they are prepared to buy into the partnership at. The firm would require some selection process in order to reduce the number of suitable candidates to a manageable number. This choice could be based on fairly spurious criteria and employed in a rather one off ad-hoc manner to situations as they arise. If this is the case it may be reasonable to conclude that such firms may have no formal hiring policies. Such firms are unlikely to disclose in the empirical study the choice methods they do employ and may in fact indicate they have no fixed policy.

The use of internal labour contests could be appropriate, if suitable candidates are available within the firm. In such a situation, the costs of discovering the information relating to prospective candidates can be significantly reduced, and risk and uncertainty play a smaller role, facilitating choice.

62. In previous discussion within this thesis, the idea of supplier induced demand has been introduced and the lawyer's selection in respect of the above does not preclude SID from occurring. The lawyer may be short of work and his potential workload is inconsistent with his desired effort level and income level. He therefore, creates extra work (and fees) for himself by creating in clients a perceived need for certain services they do not require. If he is provided with an incentive, or is feeling altruistic, he may induce demand to help another of his partners, in the event of a shortfall of work for his colleagues. The flip side to SID is the situation whereby the workload selection of the lawyer is such that he shirks and free rides on his colleagues. Such behaviour would enhance his income relative to his effort intensity expended - the overall effect being nominally enhanced personal income. This personal shirking behaviour and the use of SID, can be employed by individual lawyers to adjust activities to yield his personal desired income/ leisure outcomes. This, of course, requires that where necessary, the 'slack' or 'excess' is taken up somewhere else within the firm by the other partners, or employees.

At the level of the firm as a whole, SID creates a desirable increased workload which will doubtless result in increased revenue. It may, however, not be welcomed by individuals where they are already at full capacity. In such a circumstance, the extra workload could be delegated by the partner, if he wishes, down to the level of qualified assistant (or even lower). This may require very little marginal increase in workload for the delegating partner, for example, through increased supervision/ checking etc.

Alternatively, it is possible for him to pass 'created' additional work to one of his fellow partners, given the correct incentives. Such incentives could include a payment for attracting new business, or a payment for inter-partner transfer of clients or the like. Where appropriate this incentive could be one of the many that can be featured within the sharing bargain.

The nature of the partnership sharing bargain will be central to the incentives that confront the lawyer in his allocation of time, effort and expertise in various directions. Where his income share depends on personal productivity (however measured) then it is likely that he will perceive and receive fairly direct benefits to increased effort. Where there is equal sharing, or fixed shares of income irrespective of personal productivity, then any increased effort will be shared between the partners on this predetermined basis. Hence, the partner supplying the increased effort will receive a disproportionately small increase in personal income in relation to his increased income. Even with weak (or missing) incentives, partners when confronted with this situation may still be willing to supply increased effort, since they recognise that from time to time each and every one of the partners may find themselves in a similar situation. This is the essence of true sharing and exposes the ethos of true partnership, where it is perceived that costs and benefits will average out in the long run. The problem that can arise in this respect is where one or more of the partners free ride on the increased effort of one or more of the other partners. Should hard working partners perceive this they will be provided with the incentive to stop supplying increased effort. If they do not perceive it or let it persist unchallenged, lazy partners have an incentive to preserve the status quo. This type of inter-partner strategic behaviour would be likely to undermine the partnership in the longer run as tensions would doubtless grow.

63. Each qualified assistant will have his own unique expectations as to how long it will take before being offered partnership. Partners will also be aware that different qualified assistants will be more willing to wait for longer periods of time until they are offered partnership. It is in the partners' interests to exploit this heterogeneity in

perception of qualified assistants. This may go unnoticed if it can be conveyed to qualified assistants that differences in pre-partnership service, reflect performance and a whole range of other subjective/ invisible characteristics of qualified assistants.

Qualified assistants will wish to avoid any acts that will reduce their prospects for promotion to partner. They are also likely to find it in their interests to establish long term client relations (lawyer specific capital). This has the dual effect of signalling to the partners that they are hard working, they can attract clients and can develop personal client relationships, but also creating the potential situation that, should they leave the firm, clients may follow. This could provide the qualified assistant with a fair degree of leverage or bargaining power, where he will possess a hostage (the threat of leaving) to make reasonable demands, either for more money or for a partnership place. An important factor here will be whether the firm would perceive and treat this as a real threat, or if the firm could essentially call the qualified assistant's bluff, tell him he is free to leave, and hope clients do not leave. A crucial factor here in determination of the value of the threat will be whether the firm perceives the clients to be loyal to the firm or loyal to the lawyer, and the perceived value to the firm of that QA as a partner and future source of clients.

64. A *discontented qualified assistant* may find it *relatively easy, upon leaving* the law firm, to start up his own firm, if he has a willingly mobile client base who are prepared to follow him to a new location. This could be used as a hostage to extract a favourable partnership decision from the partners of the firm. This desire of clients to follow the exiting lawyer may be founded upon a desire to retain a valuable "family lawyer" type of relationship they perceive themselves as being in. This is viewed as worth preserving, due to the relation specific information that has evolved around the relationship, which has a clear high opportunity cost of abandonment. There may also be *significant search costs* and *levels of uncertainty facing the consumer*, in *setting* up a new client/ practitioner relationship.

65. It is interesting to note, that law firms do not appear to rely on restrictive covenants to restrain the behaviour of exiting qualified assistants. This could be seen as supportive of the assumption that law firms have great faith in the ethics of the individual lawyer to self-check such behaviour. Alternatively, it questions the ability of the law firm to design such agreements that would be legitimate and effective.

66. See; Kwon *supra* Note 48.

67. See; Kwon, *supra* Note 48.

68. See; Sisk, *supra* Note 48.

69. See, Williamson (1985), *supra* Note 33 . for his discussion of the survivability of labour managed firms in the modern capitalist economy

70. See; Meade (1982), *supra* Note 45 at p.425.

-Chapter Seven-

The Internal Organisation of Law Firms - Empirical Analysis.

Section One: Questionnaire Section Three - Inside the Firm:

Introduction:

The third section of the questionnaire relates to the internal hierarchical features of the organisation of law firms. Within true partnership organisation no real hierarchy exists between the firm's partners. A hierarchical element will exist, however, between the partners as a collective group and individuals at lower levels of the partnership. As the size of the partnership increases the management of the practice assumes greater importance and becomes more difficult and costly. Consequently, it is hypothesized that, the larger the partnership is, the more formal will be its management structure.

1.1 The significance of residual claimant status in firm management and organisation:

It will be recalled from earlier discussion that property rights literature, as expanded in scope via literature of agency theory, emphasizes strongly the role of residual claimant status in terms of incentives facing individuals within an organisation. Within partnership the partners are all residual claimants of the firm and as such will wish to exercise their full property rights in relation to protecting that residual claim. In effect, this means that all partners of the firm have a desire to be actively involved in the management of the firm. This is not so much of a problem in small to medium sized partnerships but in the large partnership, potential problems this causes can be significant.

The ammunition at the disposal of each partner to defend his residual claim/ property right is his decision making authority, which is fairly extensive in the typical partnership. Property right theorists would argue that the individual partner would wish to jealously guard his decision making authority to control his residual claim. This implies that in the large partnership all partners will wish to retain full control over decisions concerning all matters relating to the partnership. The obvious limitation here is that decision making becomes at least unwieldy, if not completely inefficient.

1.2 The requirement to separate ownership from control in large partnerships:

It is recalled from Chapter Three that agency theorists would argue the obvious solution to the above is to be found by divorcing ownership from control where, agency costs can be regarded as the optimal costs of the divorce of ownership from control. The implication for

the large partnership here is that there has to be some element of delegation of decision making authority to subsets of the partnership group.

The problem is that those who have given up some of their decision making authority and invested it in other agents, will still desire to control their property right. As a result, it could be expected that some form of formal monitoring function would evolve to check uses and abuses of the delegated decision making authority. This section of the questionnaire, therefore, explores the hypothesised mismatch between the requirement to delegate decision making authority and partners' general unwillingness to do so. In doing so it is anticipated that individual partnerships' solutions to the delegation problem and monitoring function will be concurrently exposed.

1.3 The extent of delegation and the extent of resultant problems:

The delegation problem is limited in the respect that those partners giving up their decision making authority (investing it in other agents) will be delegating to agents who themselves are partners and thereby owners of the business. To this extent, their incentives are broadly aligned and resultant agency problems are lessened as the agents should be to a large extent self-monitoring.

A more pressing agency problem could be expected where decision making authority is delegated to non-lawyer specialists within the firm, since as non-lawyers they are precluded from owning a share of the firm. As a result, partners confront a far stronger attenuation of their property rights than in the previous scenario. It is hypothesised that the overwhelming reluctance to delegate decision making authority to non-residual claimant agents would perhaps preclude this occurring in many partnerships. Delegation to non-partner decision managers could therefore be expected to be a relatively rare phenomena in law firms.

This section investigates specialist roles in management for individual partners, subset groups of the partners and non-lawyer specialists to reveal the roots of decision management and decision control within each partnership. In doing so, monitoring structures of each partnership will be simultaneously revealed.

1.4 Fama and Jensen's organisational structure hypotheses:

In next conducting a critique of Fama and Jensen's monitoring based view of organisation, it is necessary to examine three basic hypotheses employed by Fama and Jensen in their discussion of determinants of organisational structure [1] since;

1. Their basic argument forms the basis of much of the brief discussion above and,
2. Their theoretical analysis of organisational form prompted this empirical study to investigate the nature of internal hierarchical organisation of partnerships within Section 3 of the questionnaire.

Fama and Jensen (1983) suggest three main hypotheses in relation to organisational structure [2].

1. Contract structures separate ratification and monitoring of decisions (decision control) from initiation and implementation of decisions (decision management).
2. If both decision management and decision control functions are invested in the same agents then these agents will also be residual claimants.
3. The separation of residual risk bearing from decision management leads to decision systems which separate decision management from decision control.

These complementary hypotheses form the basis of Fama and Jensen's theoretical discussion of the determinants of organisational form and appear to have been derived from their observations of how differing types of organisations are organised. The importance of these three main organisational features (decision management, decision control and residual risk bearing) and the relationship existing between these interacting functions, has been noted for each type of organisation they have analyzed. Fama and Jensen generalise across organisational types to abstract their three general hypothesis. It will become apparent below whether it makes sense to test these basic hypotheses or if it is more sensible to test other hypotheses derived from these initial ones.

In partnership, it is known in advance of empirical observation, who the residual claimants are. These agents are the partners, who could also be expected to be the decision managers and decision controllers. It is, therefore, apparent that Fama and Jensen's second hypothesis should be tested in the empirical study for the sample firms.

Hypothesis 1, in its strongest form, would suggest, as Williamson (1983) notes, that the condition and incidence of residual risk bearing is fully determinative of organisational form [3]. Williamson (1983) argues that while this is an important factor, it assigns unwarranted importance to residual risk bearing [4].

In the large partnership, where devolved decision making systems have evolved, hypothesis 3 is under direct scrutiny. An examination of practising arrangements of large partnerships in the empirical study will test whether hypothesis 3 is true for the sample of firms under examination. The nature of decision systems adopted as a result of any divorce of residual risk bearing from decision management in the large partnership will be scrutinised and

compared with predictions of the hypothesis.

In testing Fama and Jensen's hypotheses, the empirical study must seek to identify for each of the sample firms who the decision managers and who the decision controllers are. The observed separation or combination of these functions will either lend support to or refute Fama and Jensen's hypotheses.

1.5 Separation of ownership from control in the large partnership:

Fama and Jensen (1983) argue that the separation of ownership from control in the large partnership has two inherent advantages [5]:

1. Permits specialisation in management, driving a wedge between residual risk bearing and decision management.
2. Facilitates a common approach to control agency problems caused by such a separation.

The anticipated result is development of well designed decision systems whose efficiency will be reinforced by the incentive structures that reward agents both for initiating and implementing decisions and for ratifying and monitoring the decision management of other agents.

1.6 Decentralised decision making in large partnerships:

Fama and Jensen (1983) argue important decisions can be effectively delegated through a committees system with a partnership board exercising decision control [6]. Consequently, decision control devices in large partnerships are similar to other organisational types which have diffuse residual claimants. In partnership, however, residual claimants are experts in the organisation who can, thereby, effectively monitor board decisions. Consequently, external monitoring of the board, which comprises solely of partners, is not necessary. Examples of decisions taken by the board would be; new offices, new admissions to partnership, dismissals, and negotiation of partnership profit shares, etc.

A partnership board (more usually called a committee) can combine specific top level knowledge with individual partner information. Fama and Jensen (1983) argue that committees exist to manage agency problems between the firm's partners [7]. The main advantage of the committee is that it can examine, evaluate and determine policy issues at a lower cost that if it were performed jointly by all partners.

Fama and Jensen (1983) argue, for this reason, that decentralised decision making in large partnerships, combined with decisions made locally concerning legal matters in client transactions, is more effective [8]. At a local/ team level, services are rendered to clients and decision control takes place within teams (where interaction between team members and mutual monitoring is strongest). Fama and Jensen (1983) view large partnership as a fluid association of small partnerships where client services are rendered from teams/ groups [9].

Fama and Jensen (1983) argue professionals have an incentive to purchase monitoring and consulting to help limit losses in the value of their human capital [10]. Consequently, mutual monitoring and consulting is encouraged where liability is shared between partners [11]. In partnership, the threat of external takeover resulting in board members losing their positions is absent as a constraint on abuses of decision control authority of the board. Internal takeover is possible where the partnership has an election system for board membership. This could act as a potential constraint on abuse of decision control authority of the partnership board.

Fama and Jensen provide a fairly robust view of partnerships and large partnerships within the analysis described above. Information derived from the empirical study will be compared with this stylised view to refute it or lend support to it.

1.7 Specific partnership decision making hierarchy hypotheses to be empirically tested:

Hypothesis 1: The partners, as residual claimants of the firm, will have the combination of functions of decision managers and decision controllers of the firm invested in them.

Hypothesis 2: Delegation of decision management and/ or decision control to non-residual claimants will be uncommon due to monitoring problems and severe attenuation of partners' property rights.

Hypothesis 3: Any observed separation of residual risk bearing from decision management will tend to exist in large firms and this will lead to decision systems that separate decision management from decision control.

1.8 Inside the law firm - an exploration of its hierarchical features:

The information collected from Section Three of the questionnaire is analyzed and presented here. The first item of information requested from each firm was an outline of the salient features of its hierarchical management structure. The table below reports their responses.

(TABLE 7.1)

Firm No	MANS TRUC	COMM ITT	MANB OARD	MANG PTR	MPTR INT	SENP TR	SENE XT	CEO	COO	NONL AWY	FULL TIME	FEEE ARN	EXNO NEX	FORM AL
5,8,11														
(3 Firms=9.1%)	No	No	No	No	No	Yes	No	No	No	No	No	Yes	No	No
13(1 Firm=3.0%)	No	No	No	No	No	No	No	No	No	No	No	Yes	No	No
6 (1 Firm=3.0%)	No	No	No	No	No	No	No	No	No	Yes	No	No	No	Yes
16(1 Firm=3.0%)	No	No	No	Yes	No	Yes	No	No	No	No	No	Yes	No	No
21(1 Firm=3.0%)	Yes	No	No	No	No	No	No	Yes	No	Yes	Yes	Yes	No	Yes
9 (1 Firm=3.0%)	Yes	No	No	Yes	No	No	No	No	No	Yes	Yes	No	Yes	No
17(1 Firm=3.0%)	Yes	No	No	Yes	No	Yes	No	No	No	Yes	Yes	No	Yes	No
22(1 Firm=3.0%)	Yes	No	No	Yes	No	Yes	No	No	No	Yes	Yes	Yes	No	No
25(1 Firm=3.0%)	Yes	No	No	Yes	No	Yes	No	No	No	Yes	Yes	Yes	Yes	No
29,33														
(2 Firm=6.1%)	Yes	Yes	No	Yes	No	Yes	No	No	No	Yes	Yes	Yes	Yes	No
2,15,31														
(3 Firms=9.1%)	Yes	Yes	No	No	No	Yes	No	No	No	Yes	No	Yes	No	No
10(1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	No	No	No	No	No	No	No	Yes
1 (1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	No	No	No	No	No	Yes	No	No
4 (1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	No	No	No	No	Yes	Yes	Yes	No
14(1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	No	No	No	Yes	No	Yes	Yes	No
3 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	No	No	No	No	No	No	No	No
12(1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	No	No	No	No	No	Yes	No	Yes
30(1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No	No	No	No	No	Yes	No	No
19(1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	Yes	No	No	No	Yes	No	Yes	No
7,18														
(2 Firms=6.1%)	Yes	No	Yes	Yes	No	Yes	No	No	No	Yes	No	Yes	No	No
32(1 Firm=3.0%)	Yes	No	Yes	No	No	Yes	No	No	No	No	No	Yes	No	No
20(1 Firm=3.0%)	Yes	No	Yes	Yes	No	Yes	No	No	No	No	No	Yes	No	No
28(1 Firm=3.0%)	Yes	No	Yes	Yes	No	Yes	No	No	No	Yes	Yes	Yes	No	No
27(1 Firm=3.0%)	Yes	No	Yes	Yes	No	Yes	No	No	No	Yes	Yes	Yes	Yes	No
24(1 Firm=3.0%)	Yes	Yes	Yes	No	No	No	No	Yes	Yes	No	Yes	Yes	Yes	No
26(1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	Yes	No	No	Yes	Yes	No	Yes	No	No
23(1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	Yes	No	Yes	Yes	No	Yes	Yes	No	No
TOTAL FIRMS	27	16	9	18	1	26	1	3	3	17	12	28	9	6
%age FIRMS	81.8	48.5	27.3	54.5	3.0	78.8	3.0	9.1	9.1	51.5	36.4	84.8	27.3	12.2

Description of variables;
MANSTRUC-Formal management structure
COMMITT-Committees structure
MANBOARD-Management board
MANGPTR-Managing partner
MPTRINT-Managing partner internal affairs
SENPTR-Senior partner
SENEXT-Senior partner external affairs
CEO-Chief executive officer
COO-Chief operational officer
NONLAWY-Non lawyers in management positions
FULLTIME-Partners in full time management positions
FEEEARN-Partners in management positions still fee earn
EXNONEX-Executive and non-executive positions
FORMAL-Moving to more formal structure in future

On initial inspection of TABLE 7.1 it is immediately apparent that methods of structuring management across firms are diverse and in many cases unique. There are, however, shared characteristics across firms which the following description of responses identifies and highlights.

27 firms identified themselves as possessing a formal management structure. Of the 6 firms identifying themselves as not having a formal management structure, 3 firms revealed they had a senior partner and all partners jointly performed management tasks but all remained fee earners. Another of these 6 firms only revealed that all partners jointly managed the firm and remained fee earners. 1 firm employed non-lawyers in management roles and further indicated it was having to move towards a more formal structure in future. The final firm in this group indicated it had senior and managing partner positions but all partners jointly managed the firm and remained fee earners.

The above 6 firms, were not surprisingly all small/ medium sized firms who generally perceived their scale not justifying or requiring a formal management structure. Within these

firms it is still possible (in most situations) for partners to jointly make decisions and manage the firm without creating problems of inefficient and burdensome decision making.

Of the 27 firms which had formal management structures, 5 firms did not use a system of committees or a partnership board to aid decision making.

(I) Firms with no committee system or partnership board - further breakdown:

These firms all revealed unique characteristics but shared certain common features. All firms revealed they had both non-lawyers and partners (non-fee earning) in full-time management positions. 4 of the firms also had managing partners and, in the firm that did not, a partner was designated chief executive officer. The firm with the CEO also revealed that some of the partners with management positions still fee earned (although others had full-time management positions) and the firm would be moving to a more formal structure in future.

3 of the above 4 firms also indicated the existence of senior partners within their firms, the firm with no senior partner also describing the existence of executive and non-executive positions within that firm. Of the 3 remaining firms, 1 also revealed the existence of executive and non-executive positions within the firm, 1 revealed that while some partners had management positions and still fee earned, others held full-time management positions. The final firm revealed both of these characteristics. Within this overall group of 5 firms, 2 were large firms and 3 were small/ medium sized.

(II) Firms with committees and no management board - further breakdown:

This group of 13 firms again shared certain characteristics and exhibited unique features. 3 firms indicated they had a senior partner, non-lawyers in management positions and also that all partners still fee earned even though they actively jointly managed the firm. 2 firms had both senior and managing partner positions, had non-lawyers and partners in full-time management positions, whilst other partners with management inputs still fee earned, and had executive and non-executive positions.

The remaining 8 firms uniquely designated themselves. 4 firms revealed they had senior partners. Of these 4 firms, 1 indicated it would be moving to a more formal management structure in future and another disclosed that partners still fee earned regardless of management interests. 1 firm indicated some partners had full-time management positions whilst others combined management interests with fee earning, and executive and non-executive positions existed. The final firm disclosed that non-lawyers held management positions, partners with management interests still fee earned and that executive and

non-executive positions existed within the firm.

2 of the 8 firms indicated that a managing partner existed, this being the only revealed characteristic of one of these firms. The other, however, also indicated that partners with management interests still fee earned, and that they would be moving to a more formal structure in future.

Both of these 2 remaining firms of the original 8, disclosed the existence of both senior and managing partner positions. In 1 firm, however, the managing partner dealt with internal matters concerning the partnership and the senior partner with external matters. In this firm, additional information was provided indicating the existence of partners in full-time management positions and both executive and non-executive positions. In the other firm, all partners remained fee earners regardless of management interests.

This overall group of 13 firms was occupied by 6 large firms and 7 small firms.

(III) Firms with partnership boards but no committees system - further breakdown:

A total of 6 firms occupied this grouping, all of whom indicated they had a senior partner and that where partners had interests in management of the firm, they remained fee earners. This was all the information disclosed by one of the firms. The remaining 5 firms all had a managing partner, and all but one had non-lawyers in management positions. Two of these firms provided no more information. The firm that did not employ non-lawyers in management positions also provided no additional information.

The remaining two firms both disclosed the existence of non-lawyers and full time partner positions in management, with one of them also indicating the existence of executive and non-executive positions within the firm.

Of this total group of 6 firms, 5 were large and only 1 was small/ medium sized.

(IV) Firms with both partnership boards and a committees system - further breakdown:

All 3 firms in this category had positions of chief operational officer and also indicated that where partners had interests in management, they also remained fee earners. 1 firm also indicated that a chief executive officer position existed, there were non-fee earning partners in full-time management positions, and that executive and non-executive positions existed.

The two remaining firms additionally disclosed the existence of both managing and senior partner positions. 1 indicated that non-lawyers also held management positions and the other

reported it had a chief executive officer and partners in full-time management positions. As could be expected, all 3 firms of this type were large firms.

It is demonstrated above that 4 main types of firms with formal management structures can be identified over and above the sample firms which have no formal management structure.

The use of partnership boards can be viewed as an attempt to make decision making more efficient within the large firm. Committees perform a similar role by smoothing decision making and delegating decision making authority in specific areas of the firm's management to specialised partner sub-groups. Where a partnership board and a system of committees existed, committees sat below board level and were accountable to the board.

The use of non-lawyers in management positions within the firm was surprisingly commonplace, occurring in 17 of the 33 firms interviewed. Another surprising feature reported was the relatively common occurrence of partners holding full-time management posts whereby they did not fee earn, this being reported by 12 firms.

9 firms specifically indicated the existence of executive and non-executive positions in the firm revealing that some partners had given up their decision making authority and others had been invested with it via committee or board membership or through holding a full-time or 'combined with fee earning', management position.

4 firms indicated they were attempting to increase the formality of their management structure at present to cope with problems which were likely to become more dramatic in the future. Of these firms, 3 were small (two of which already had a formal management structure) and 1 was a large firm currently with a formal management structure.

(V) The importance of the role of partnership boards and committees:

The partnership board is typically a subset of the full partnership invested with decision making authority. The board usually comprises of the senior and/ or managing partner (or their corporate style namesakes) and a handful of appointed partners. In firms where there is a committee system, the board is essentially a management committee under which there is a system of sub-committees which all report back to the board. In firms where there is no committee system, the board acts as a decision making filter which typically processes information for the whole partnership to vote on.

In relation to Hypothesis 1. which states, the partners, as residual claimants of the firm, will have the combination of functions of decision managers and decision controllers of the firm invested in them, evidence is mixed. In firms which do not have a partnership board (24

firms), the full meeting of partners (residual claimants) will typically be invested with full functions of decision management and decision control. This evidence initially appears to confirm Hypothesis 1. However, delegation of decision management authority within 13 of these firms, via a committees system, is evidence of an attenuation (or at worse complete delegation) of partners' decision management authority.

In the 9 firms that have a partnership board, delegation of either decision management or decision control authority is extensive. The precise role of the board in this respect, while important, was not pursued since it is outwith the ambit of this study. In the 3 firms that have a partnership board and committees, the board typically assumes the role of decision controller and committees act as decision management units. The full partnership will very seldom require to formally control or manage decisions since delegation is almost absolute. In the 6 firms which have a partnership board but no committees, the board typically plays the decision management role with full partnership exerting decision control.

It appears to make most sense to jointly examine Hypotheses 1 and 3 in this section - if empirical evidence fails to confirm Hypothesis 1, it is logical to seek confirmation (refutation) of the assertion made in Hypothesis 3.

The existence of committees in 16 of the firms, and of management boards within 9 firms (3 firms exhibiting both features), is indicative of delegated decision making authority. The existence of non-lawyers in management positions in 17 of the firms, of full-time partner management positions in 12 of the firms, and of executive and non-executive positions in 9 of the firms, is also strongly indicative of delegation of decision making authority. This evidence points to the refutation of Hypothesis 1 for firms where individual partners or non-lawyers, or subsets of the partners, are invested with decision management/ decision control authority. This results in an attenuation of the combination of functions outlined in Hypothesis 1.

The strongest refutation of Hypothesis 1. occurs within the 9 firms which operate a partnership board. This board exists because other partners of the firm give up either their decision management or decision control authority to board members. The overall partnership no longer combines the functions of decision management and decision control in all of its residual claimants. Hence, the wedge driven between these functions points to the refutation of Hypothesis 1.

Hypothesis 1. is only confirmed for those 6 firms which do not have partnership boards, committee systems, full-time partner managers, executive and non-executive positions and non-lawyers in management positions. Even 1 of these 6 firms fails on the last of these criteria since it employs non-lawyers in management positions.

Attention now turns to Hypothesis 3, which argues that any observed separation of residual risk bearing from decision management will tend to exist in large firms and this will lead to decision systems that separate decision management from decision control.

1. In the 6 firms where the decision management function is performed by a partnership board (where no committees system exists), those partners who are not board members experience a separation of their residual risk bearing from their decision management authority.

2. In the 3 firms where the partnership board assumes the function of decision control (where a committees system operates), those partners who are not board members experience a separation of their residual risk bearing from their decision control. The decision management function in such firms is performed by committees -committee members, while retaining their residual claimant status, lose much of their decision control authority to the partnership board.

3. In the 13 firms with a committees system but no partnership board, subsets of the partners who constitute committees are decision managers and the entire partnership will typically perform the decision control function. Partners sitting on committees will specialise their decision management authority in respect of the committees they sit on.

Partners will lose their decision management authority in respect of those committees they do not sit on. Hence, there is an observed separation of residual risk bearing from decision management in respect of some areas of management for all partners. The decision system separates decision management from decision control as stated in Hypothesis 3.

In the above 3 cases, evidence supports the assertion made in Hypothesis 3. with the exception of the claim concerning firm size. Taking firm size into the equation, over the 3 categories of firms outlined above, 14 firms are large and 8 small. This is indicative of the tendency for the assertion made in Hypothesis 3 to occur in large firms.

The above arguments are summarised in the following table which indicates who performs management functions in different partnership management structures.

(TABLE 7.2)

	DECISION MANAGEMENT	DECISION CONTROL	RESIDUAL RISK BEARING	NO. OF FIRMS	NO. OF LARGE	NO. OF SMALL
SIMPLE PARTNERSHIP	All partners	All partners	All partners	11	2	9
PARTNERSHIP BOARD	Board	All partners	All partners	6	5	1
COMMITTEES	Committees	All partners	All partners	13	6	7
BOARD & COMMITTEES	Committees	Board	All partners	3	3	0

Hypothesis 2, states that delegation of decision management and/. or control to non-residual claimants will be uncommon, due to monitoring problems and severe attenuation of partners' property rights. Contrary to the anticipations of this hypothesis, in 17 of the 33 firms, non-lawyers hold decision management and/ or decision control positions (8 within small/ medium sized and 9 within large firms). These positions were typically practice manager, partnership secretary or the like, and often their incumbents enjoyed board or committee membership. This observed popularity among firms to employ the services of non-lawyers in management positions refutes Hypothesis 2.

In relation to management structure existing, firms were typically keen to stress the distinction between the management hierarchy/ power structure existing between partners and the income division hierarchy of the firm. Almost all of the firms in the study said that an egalitarian power structure existed between the partners, irrespective of the method of income division within the partners group.

1.9 Partner specialisations within the firm:

TABLE 7.3 below summarises the firms' responses in relation to special functions performed by partners within firms.

Firm No	MANSPEC	LEGSPEC	COMCONV	DEPTHEAD	SPECFUTU
3,5,7,9,11,16,17,18,20 21,22,23,25,27,28,32 (16 Firms=48.5%)	Yes	Yes	No	Yes	No
1,4,12,14,24,26,29,30, 33 (9 Firms=27.3%)	Yes	Yes	Yes	Yes	No
15,19,31 (3 Firms=9.1%)	No	Yes	Yes	Yes	No
10,13 (2 Firms=6.1%)	Yes	Yes	No	No	No
6 (1 Firm=3.0%)	No	Yes	No	No	Yes
8 (1 Firm=3.0%)	Yes	No	No	No	No
2 (1 Firm=3.0%)	Yes	Yes	Yes	No	No
TOTAL FIRMS	29	30	13	28	1
%age FIRMS	87.9	90.9	39.4	84.9	3.0

Description of variables:
MANSPEC-Management specialties
LEGSPEC-Legal specialties
COMCONV-Committee convenors
DEPTHEAD-Department heads
SPECFUTU-Need for greater specialisation in future

29 firms and 30 firms respectively disclosed the existence of specific management functions and legal specialisms for partners of their firms. In 28 of these firms, certain partners performed both of these functions. 13 firms indicated that some partners were committee

convenors and 28 firms indicated that partners were heads of specialist legal departments of the firm. In only 1 of firm was it perceived to be necessary for partners to further specialise in future - it must be said, however, this firm was a small/ medium firm with as yet no management specialisations for partners.

1.10 Departmental leadership:

The issue of departmental leadership was investigated further to facilitate a clearer understanding of internal organisation with respect to departmentalisation within the firms.

(TABLE 7.4)

Firm No	PTRHEAD	PTRSHEAD	QAHEADS	DEPTCOMM	PYRAMID
1,3,5,9,11,15,16,18,19, 20,21,22,23,24,25,28,30 31,32 (19 Firms=57.6%)	Yes	No	No	No	No
7,26,27,29,33 (5 Firms=15.2%)	Yes	No	No	No	Yes
6,10 (2 Firms=6.1%)	No	No	No	No	No
12,17 (2 Firms=6.1%)	Yes	No	Yes	No	No
8,13 (2 Firm=6.1%)	M	M	M	M	M
2 (1 Firm=3.0%)	No	Yes	No	No	No
4 (1 Firm=3.0%)	Yes	No	No	Yes	No
14 (1 Firm=3.0%)	Yes	Yes	No	No	No
TOTAL FIRMS	28	2	2	1	5
%age FIRMS	84.8	6.1	6.1	3.0	15.2

(M-Missing value)

Description of variables:
PTRHEAD-Partners head departments
PTRSHEAD-More than one partner heads a department
QAHEADS-Qualified assistants head departments
DEPTCOMM-Departments have their own committees
PYRAMID-Pyramid teams in departments

In TABLE 7.4, 3 firms provided no information simply because they did not have a departmental structure. Partners appeared the most natural choice for departmental head reflected by the fact that 28 of the 30 firms disclosed partners to hold such positions in their firms.

2 firms indicated that more than one partner headed departments, and in 1 of these firms, it was the case that either a single partner or more than one partner would head a department. In only 2 firms did qualified assistants head departments - these firms also both indicating that certain departments were headed by a partner.

1 firm operated a committee system whereby each department essentially had its own management committee to ensure its proper functioning. Curiously, this occurred in one of the small/ medium sized firms, since one would have anticipated that this would have been more likely in a large firm if it existed at all.

5 firms operated pyramid teams within each department - where a partner headed the department with subsequent layers of partners, qualified staff, unqualified staff and ancillary

staff beneath. Within this overall pyramid team structure there was also smaller clusters/ associations. This fluid team structure was argued to be effective since it was dynamic and responsive, creating team spirit and enforcing both peer group and hierarchical monitoring.

The tendency for departmentalised firms to rely on partners, or groups of partners, and typically not qualified assistants to head departments, is indicative of the necessity of partners to closely monitor each transaction within the firm. Qualified assistants within these departments can be closely monitored and evaluated by the partner head, facilitating the screening mechanism to assess suitability for partnership and easing the partnership decision. The departmental head will typically be best equipped to evaluate the qualified assistant working in his department, through the delegation process and the proximity of the working/ mentor relationship thus created.

Training of qualified assistants in one area of the firm's work/ speciality could perhaps make the qualified assistant's skills more firm specific, thereby reducing their value to other firms. Conversely, it may simply provide the qualified assistant with a specialist legal training which may be sought by other firms, thereby increasing his inter-firm mobility.

1.11 Firms descriptions of the nature of their partnership hierarchy or democracy:

The information collected aimed to discover the extent to which the typical partnership adhered to its characteristic feature of democracy, or if democracy was diluted through a formal seniority based hierarchy.

(TABLE 7.5)

Firm No	FORMSEN	INFOSEN	EGAL	JUNSEN	SALEQUIT	VOTING
1,4,5,13,18,20,24,26,28, 30,33 (11 Firms=33.3%)	No	No	Yes	No	No	No
6,19,21,22,25,31 (6 Firms=18.2%)	No	No	Yes	No	Yes	No
8,9,11,12,17,27 (6 Firms=18.2%)	No	Yes	Yes	No	No	No
23,29 (2 Firms=6.1%)	No	No	Yes	Yes	Yes	No
14,32 (2 Firms=6.1%)	No	Yes	No	No	No	No
10 (1 Firm=3.0%)	No	Yes	No	No	Yes	No
3 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	No
2 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	Yes
16 (1 Firm=3.0%)	No	Yes	Yes	Yes	Yes	No
7 (1 Firm=3.0%)	Yes	No	No	No	Yes	Yes
15 (1 Firm=3.0%)	Yes	No	Yes	No	No	No
TOTAL FIRMS	2	12	29	3	13	2
%age FIRMS	6.1	36.4	87.9	9.1	39.4	6.1

Description of variables:
FORMSEN-Formal partner seniority
INFOSEN-Informal partner seniority
EGAL-Egalitarian partnership
JUNSEN-Junior and senior partner distinction
SALEQUIT-Salaried and equity partner distinction
VOTING-Unequal voting rights

29 firms described the relationship existing between partners as egalitarian. 2 firms specifically indicated the existence of a formal seniority based hierarchy between the partners.

In one of these firms, the partnership was still described as egalitarian, but in the other, formal seniority was reinforced by a system of unequal voting rights. One other firm indicated a system of unequal voting rights existing between partners but chose, paradoxically, to describe the firm as egalitarian and characterised by informal partner seniority. 12 firms described a system of informal seniority existing between the partners, 9 of whom also described the partnership existing as egalitarian.

3 firms indicated the existence of junior and senior partner categories, while 13 disclosed that two categories of partner existed, namely salaried and equity partners. These features can both be regarded as reinforcing hierarchy and undermining true partnership democracy. They are likely, however, to exist more importantly as a vital screening mechanism to evaluate lawyers in the time preceding full equity participation. The granting of salaried partner/ senior associate status prior to full partnership was generally viewed as a carrot to QAs by permitting them increased status by placing their name on the partnership notepaper. The firm, of course, also benefits from this as it signals to clients they are being attended to by personnel worthy of appearing on the firm's notepaper.

It was commonplace within firms that seniority tended simply to reflect notepaper seniority rather than accurately reflect its power structure.

Section Two:Questionnaire Section Four - Allocation of Clients.

2.1 Clients as a source of firm specific and lawyer specific capital:

The motivation for examining allocation of clients within the firm is to pursue the issue of creation of firm specific and lawyer specific capital. Clients are the life-blood of the firm and the success of the firm in creating and sustaining client relationships is paramount. Attempts made by firms in this direction have been examined within Section Two of the questionnaire.

Section Four of the questionnaire deals more specifically with the issue of creation of firm and lawyer specific capital. Gilson and Mnookin (1984) argue that shirking, grabbing and leaving are all barriers to capturing gains from diversification in partnership [12]. They further posit that within partnership, the relationship between the creation of firm specific capital and lawyer specific capital can act to constrain grabbing and leaving by lawyers.

The basic thesis of Gilson and Mnookin (1984), in this context, is that firm specific capital can constrain grabbing and leaving in a partnership reliant upon a sharing model of income division [13] - to this extent, firm specific capital binds such an organisation together.

2.2 The trade-off between creation of firm specific and lawyer specific capital:

The dilemma facing the firm in client relationships is that it wishes the client to become familiar with certain agents of the firm in order that a personal relationship is created between the firm and clients. However, what is likely to occur simultaneously is that the client will become locked into a personal relationship with particular agents of the firm. The balance of loyalty of the client towards either firm or particular agents of the firm, will determine the extent to which the client can be viewed as a source of firm specific or lawyer specific capital.

Clients can be seen as a source of firm specific capital in so much as a partner leaving the firm would be unlikely to be able to duplicate the necessary client base to produce predictable flows of work. This, of course, is a feature of his present firm, where a firm's diverse client portfolio is an example of firm specific capital.

Where a lawyer perceives a client to be his own (and therefore likely to follow if he left his firm) the lawyer is provided with a significant hostage to either grab (demand more money) or leave. The firm has a great deal to lose since the lawyer will leave and take with him that client, and perhaps others. The firm could be expected to take measures to prevent this situation occurring, or at least reduce the risk of it occurring or minimise the effect it would have. Options here are problematic, however, since they may simply cause the firm more problems than they seek to solve.

2.3 Client portfolios:

As has been argued previously, it is in the firm's interests to encourage lawyers to bring in new clients and form close personal relationships with existing ones. The law firm would, therefore, appear to wish to encourage lawyers to develop their own client portfolios. This, however, creates a tendency for lawyers to jealously guard their own clients. This is problematic in four respects;

1. That particular lawyer may not be the best person within the firm for the client to see, depending on the nature of his current legal problem.

2. The lawyer who creates a large personal portfolio of personal clients poses a significant grab and/ or leave threat to the firm since he will possess, or will be perceived as possessing, high levels of lawyer specific capital.

3. The lawyer may be reluctant to refer his clients to other lawyers within the firm.

4. Jealous hoarding of clients can act as a barrier to cross-selling of services which can positively enhance and prolong established client/ firm relationships.

The firm may, therefore, seek to discourage personal client portfolios in favour of encouraging its lawyers to view clients as belonging to the firm. This can obviate, or at least attenuate, problems like those stated above but can lead to others. Having a large client portfolio is more in keeping with conditions encouraging creation of firm specific capital.

2.4 Restrictive covenants:

Other methods firms could employ to attempt to reduce risks of lawyers leaving with clients are as follows. The use of restrictive covenants can be viewed as a specific constraint on the likely success of a lawyer exiting the firm competing with this firm for existing clients. Problems surrounding use of restrictive covenants have been discussed at length elsewhere and largely render this constraint a futile option.

2.5 Contact partners and referrals across legal specialities:

The firm may attempt to ensure clients do not become too attached to any particular lawyer by attempting to introduce the client to more than one of the firm's lawyers. On becoming a client of the firm, the client could be assigned a contact partner (partners), who would be the initial point of contact for the client. This partner would then introduce the client to the lawyer/ lawyers who were conducting the his work and, thereafter, act as a liaison between firm and client checking that his requirements were being fulfilled [14].

2.6 The importance of the destination of the client's loyalties:

A crucial factor in how the firm allocates clients and attempts to create firm specific capital without exposing itself to risks of lawyer specific capital, is whether the firm perceives clients to be loyal to the firm or loyal to the lawyer. This could be expected to vary considerably across clients given numerous other factors which may affect any client decision to stay with the firm or follow an exiting lawyer to his new place of work. At the end of the day, it is the ultimate choice of the client whether to stay with the firm or go with the exiting lawyer. To this extent, the attempts by the firm to reduce the risks of such a choice being made unfavourably against them may be worthless.

An examination of client allocation methods of sample firms will reveal whether firms view

the creation of firm specific capital and potential grabbing and leaving as a problem. Where they do see it as a problem, the methods they have employed to counter it will be examined In this section of the questionnaire, factors firms believe act as constraints on lawyers leaving will be probed with the aim of indicating the extent to which they see clients as being firm specific capital or lawyer specific capital.

2.7 Bilateral monopoly and the nature of specificity of clients as an asset:

The issue of bilateral monopoly raised in section two of the questionnaire is again important in the context of firm and lawyer specific capital. Gilson and Mnookin (1984) indicate the advantages to the law firm of operating under bilateral monopoly conditions compared with those within a competitive market [15]. Paired with the inability of a lawyer leaving the firm to duplicate that relationship outside the firm, this creates an important source of firm specific capital which can be perceived as a significant constraint to leaving the firm.

The strength and nature of the relationship between client and firm is examined in Section Two of the questionnaire to determine whether or not there is support for the hypothesis that the relationship is characterised by bilateral monopoly. Information derived from this section of the questionnaire will be utilised here in this section dealing with client allocation to help determine if the client/ lawyer relationship is firm specific, or capable of being moved outwith the firm where a lawyer leaves.

2.8 The firm as a means of quality assurance:

Due to clients' characteristic lack of sophistication and inability to measure quality pre and post consumption, it is argued by Gilson and Mnookin (1984) that the means by which firms assure clients of the quality of their services, provides another important source of firm specific capital and, hence, another important constraint on lawyers leaving the firm [16]. The means by which law firms attempt to signal quality to different classes of consumer will be empirically examined in this section together with information derived from Section Two of the questionnaire.

2.9 The overall aim of the firm in relation to clients:

From the firm's viewpoint, it is advantageous to create as much firm specific capital as possible to reduce;

1. The attractiveness, and possibility, of lawyers of the firm leaving and,

2. The potential use of clients as a hostage to grab by lawyers threatening to leave.

The two major instruments the firm has to accomplish this are, (i) clients and, (ii) the firm as an assurance of quality. Sample firms' attempts to create firm specific capital are investigated in this respect.

2.10 Specific allocation of client hypotheses to be tested empirically:

Hypothesis 1: The law firm will favour a situation where clients are viewed as belonging to the firm as this is more conducive to the creation of firm specific capital and suppression of lawyer specific capital.

Hypothesis 2: The firm will avoid the use of restrictive covenants to prevent client losses through lawyers of the firm leaving as they are likely to be futile.

Hypothesis 3: The law firm will encourage clients to form relationships with many of the firm's lawyers as this will lessen risk posed to the firm by creation of lawyer specific capital.

Hypothesis 4: The lawyers exit option will be constrained by other factors in addition to the value of the firm specific capital he has amassed within the firm.

2.11 Empirical discussion of sample firms and allocation of clients:

As noted above, the major issue here is the ability of the firm and its lawyers to create either firm specific and/ or lawyer specific capital. The sample firms were investigated to determine firstly, the potential for the creation of both of these within the firm and secondly, firms' views on potential problems that can arise as a consequence of their creation.

The table below summarises firm responses to the issue of their allocation of clients;

(TABLE 7.6)

Firm No	FIRM PORT	PART PORT	QUAL PORT	REDH OARD	FEAR EXIT	BARR IER	HOWL ONG	HOAR DLES
1,10,12,16,22,30								
(6 Firms=18.2%)	Yes	Yes	Yes	No	No	No	No	No
33 (1 Firm=3.0%)	Yes	Yes	Yes	No	Yes	Yes	No	Yes
23 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	No	No	Yes
21 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	No	Yes	No
3,31 (2 Firms=6.1%)	Yes	Yes	Yes	No	No	No	Yes	No
2,8,25,29								
(4 Firms=12.1%)	Yes	Yes	No	No	No	No	No	No
20 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No	No
25 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No	Yes
11,17,19,24,26								
(5 Firms=15.2%)	Yes	No	No	No	No	No	No	No
3,13,14,18,28								
(5 Firms=15.2%)	No	Yes	No	No	No	No	No	No
27 (1 Firm=3.0%)	No	Yes	No	Yes	No	Yes	No	No
6 (1 Firm=3.0%)	No	Yes	No	Yes	Yes	No	No	No
5,7,9								
(3 Firms=9.1%)	No	Yes	Yes	No	No	No	No	No
32 (1 Firm=3.0%)	No	Yes	Yes	No	No	No	Yes	No
TOTAL FIRMS	22	28	15	6	2	4	4	3
%age FIRMS	66.7	84.8	45.4	18.2	6.1	12.1	12.1	9.1

Description of variables:
FIRMPORT-Firm client portfolios
PARTPORT-Partner client portfolios
QUALPORT-Qualified assistant client portfolios
REDHOARD-Firm attempting to reduce hoarding of clients
FEAREXIT-Firm fears lawyer exiting and resultant client loss
BARRIER-Hoarding of clients seen as barrier to cross selling
HOWLONG-Who has their own clients depends on how long they have been with the firm
HOARDLES-Hoarding is reducing due to increased specialisation and team work

5 main groupings of firms can be identified with respect to client allocation between firm and personal portfolios. Each of these identified groups will be described below.

(I) Firms with firm, partner and qualified assistant client portfolios - further breakdown:

This group comprised 11 firms - 6 large and 5 small/ medium firms. 6 of the firms revealed no further information regarding allocation of clients and two firms disclosed additionally only that, those who have their own clients depends primarily on how long they have been with the firm.

1 firm indicated they feared lawyers leaving with clients, that personal client portfolios acted to impede effective cross-selling, and that hoarding of clients is reducing due to increased specialisation requiring internal referral and the existence of teams. The 2 remaining firms in this group indicated they wanted to reduce client hoarding by attempting to dilute personal portfolios. One of these firms disclosed that the extent to which clients were viewed as belonging to particular lawyers rather than the firm, depended on how long the lawyer in question had been with the firm. The other firm was pleased to indicate that hoarding of clients and personal portfolios were diluting due to increased specialisation and the operation of teams.

(II) Firms with firm and partner client portfolios - further breakdown:

Of this group of 6 firms, 4 were large and 2 were small/ medium sized. 4 firms provided no additional information, but the remaining 2 both reported that they were attempting to reduce client hoarding, and that personal portfolios acted as an impediment to cross-selling. 1 firm additionally mentioned that hoarding was reducing due to via increased specialisation and the existence of teams.

(III) Firms where clients all belong to one large firm portfolio - further breakdown:

Unfortunately, all 5 firms (3 large and 2 small/ medium sized) occupying this group provided no additional information.

(IV) Firms where all clients belong to partner portfolios - further breakdown:

Of the 7 firms in this category, 3 were large and 4 were small/ medium firms. 5 firms provided no additional information to facilitate further categorisation. Both the remaining firms indicated a current desire to reduce hoarding and dilute personal portfolios, 1 indicating they acted as a barrier to cross-selling and the other fearing lawyers leaving with clients.

(V) Firms with partner and qualified assistant client portfolios - further breakdown:

4 firms occupied this grouping, 1 large and 3 small/ medium, 3 of which provided no additional information. The other firm disclosed that those who had their own clients depended on how long they had been with the firm.

Hypothesis 1. conjectures that the firm will favour a situation where clients are viewed as belonging to the firm, as this is more conducive to the creation of firm specific capital and suppression of lawyer specific capital. The evidence above is fairly mixed in this respect. Certainly, 6 firms indicated they currently wished to reduce client hoarding by their lawyers. Of the firms that indicated reasons for this, 3 saw it as impeding cross-selling and only 1 firm feared lawyers leaving. This evidence is not strongly supportive of the expectation that law firms will fear lawyers exiting if they have personal portfolios since these are a major source of lawyer specific capital. The only other firm that feared lawyers leaving did not indicate a current desire to reduce client hoarding but did, however, reveal that it was reducing anyway through increased specialisation and use of teams. This is indicative that perhaps this firm felt that this would have the desired effect of reducing hoarding sufficiently, without the firm

antagonising its lawyers by deliberately attempting to dilute existing personal portfolios.

Only 5 firms in the entire sample rely exclusively on one large firm portfolio of clients, indicating that in by far the majority of firms, clients are a significant source of lawyer specific capital. Evidence is strongly suggestive that firms generally perceive little risk of lawyers leaving the firm and capitalising on any specific capital they have derived from establishing personal client portfolios. Firms typically view personal portfolios more as a problem in relation to detracting from cross-selling - upon which there is an increasing emphasis in contemporary law firms.

It can be thus concluded that firms generally will want to create a situation where clients are viewed as belonging to the firm, initially corroborating Hypothesis 1. However, the reason given in Hypothesis 1. for this desire is not empirically confirmed.

Although it was typically the case that lawyers tended to have clients they regarded as their own, it was the case that the client need not always be seen by that person. Many firms operate a system whereby a link/ contact partner exists, who will have been the port of entry for the client to the firm. If any service the client requires is outwith the contact partner's speciality, that partner will introduce the client to another within the firm.

It is also true that, while many firms did recognise that qualified assistants could have clients they regarded as their own, separate portfolios did not formally exist. Work is often delegated by partners to qualified assistants and in the course of providing the required service, a client relationship can develop between QAs and clients. The implication here is that the extent to which clients can provide partners and/ or qualified assistants with a hostage (with which they can hold the firm to ransom to obtain a greater level of income or promotion) is not as great as is stressed by Gilson and Mnookin (1984) [17]. Interestingly, it will become evident below that many of the very senior firm members interviewed had difficulty in answering who they believed clients were loyal to - firm or lawyer. It could be argued this is strongly indicative that it would be perceived a high risk strategy by lawyers to rely upon client loyalty to them, rather than the firm, as a real and perceptible threat to the firm.

2.12 Client loyalty to the firm and its members:

(TABLE 7.7)

Firm No	FIRMLOY	INDIVLOY	LESSLOY2	TEAMLOY	RESEARCH
5,7,9,10,12,13,14,15,19,20 25,26,29,33 (16 Firms=42.4%)	Yes	Yes	No	No	No
18,22,30,32 (4 Firms=12.1%)	Yes	Yes	No	Yes	No
21 (1 Firm=3.0%)	Yes	Yes	No	No	Yes
1,3,4,6,8,16,31 (7 Firms=21.2%)	Yes	Yes	Yes	No	No
23 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes
2,11,24 (3 Firms=9.1%)	Yes	No	No	No	No
17 (1 Firm=3.0%)	No	Yes	No	No	No
28 (1 Firm=3.0%)	No	Yes	No	Yes	No
27 (1 Firm=3.0%)	No	No	No	Yes	No
TOTAL FIRMS	30	29	8	7	2
%age FIRMS	90.9	87.9	24.2	21.2	6.1

Description of variables:
FIRMLOY-Clients loyal to firm
INDIVLOY-Clients loyal to individuals within the firm
LESSLOY2-Clients less loyal than before
TEAMLOY-Clients loyal to team within firm
RESEARCH-Market research done by firm to discover client loyalty

Many respondents found the question of whether clients were loyal to the firm or to individuals within the firm a difficult one to answer. 27 firms believed clients to be loyal both to the firm and to particular individuals. 3 firms believed clients to be loyal exclusively to the firm as an entity, and 2 firms viewed clients as being exclusively loyal to individuals within the firm.

8 firms felt clients had generally become less loyal than previously, typically as a result of them becoming much more fee conscious and firms also noticing reductions in repeat business across clients. 2 firms had actually commissioned market research amongst its clients to discover more about client loyalty.

7 firms (all large) believed clients to be loyal to teams of the firm's lawyers, this most probably being a function, firstly, of the specialised nature of services often provided by these large firms and, secondly, the fact that few alternative providers within that specialised legal field exist in the market. Of these 7 firms, 5 also believed clients were loyal to the firm and to individuals, 1 perceived clients to be exclusively loyal to teams, and the final firm believed clients also to be loyal to individuals, rather than the firm as an entity.

2.13 Assignation of clients to individuals within the firm:

(TABLE 7.8)

Firm No	SAMEIND	IFSAME	CONTPTR	CONTPTRS
1,3,4,5,6,7,8,10,11,12,14,16, 17,18,19,20,21,23,24,25,26,27, 29,30,31,33 (26 Firms=78.8%)	No	Yes	Yes	No
2,9,15,22,28,32 (6 Firms=18.2%)	No	Yes	Yes	Yes
13 (1 Firm=3.0%)	Yes	No	No	No
TOTAL FIRMS	1	32	32	6
%age FIRMS	3.0	97.0	97.0	18.2

```
Description of variables:
SAMEIND-Clients always see the same lawyer regardless of work type
IFSAME-Clients only see the same lawyer if same work type
CONTPTR-System of client contact partner and referral if outside work type
CONTPTRS-System of client contact partners and referral if outside work type
```

Typically, where possible, the client was seen by the same person at all times with a view to preserving continuity of the trust relationship created - this was true of all sample firms. In only 1 firm did the client see the same person regardless of the type of legal work wanted by the client. In all the remaining 32 firms, the client saw the same person within the firm only if that person was specialised in the work type demanded by the client.

The remaining issue is what happens when the client requires a service outwith the services which are the forte of that particular lawyer. In 26 cases, the client would be referred to the most appropriate person in the firm, who would be initially introduced to the client by the contact partner and thereafter would deal directly with the client. In such firms, each client would be assigned a contact partner. In the other 6 firms, the same system would operate except clients may have more than one contact partner depending on their requirements.

Hypothesis 3. states the firm will encourage clients to form relationships with as many of the firm's lawyers as possible, as this will lessen risks posed to the firm via the creation of lawyer specific capital. From the information above it is apparent that the typical firm has a desire to provide the client with a readily identifiable point of contact/ port of entry into the firm. Increasing specialisation by lawyers of the firm in particular legal specialties has, however, required the frequent referral of clients and work between lawyers of the firm.

The designation of many contact partners, typically representing different legal specialisms (a feature of 6 firms) encourages clients to become familiar with many of the firm's lawyers. This is aimed at making the client feel comfortable dealing with many firm members and increasing the client's chances of receiving immediate attention upon contacting the firm. The designation of many contact partners is evidence supportive of Hypothesis 3. From TABLE 7.8 it is recalled that 7 firms believe clients are loyal to a team of lawyers within the firm, also providing support for this Hypothesis.

From TABLE 7.7 it is recalled that 6 firms expressed a desire to reduce hoarding of clients and this is indicative of a desire by the firm for clients to see as many of the firm's lawyers as possible.Reasons given by firms for wanting to reduce hoarding are mixed in relation to Hypothesis 3. for similar reasons to those for Hypothesis 1. To recall, the popular reason given to reduce client hoarding was not to lessen risks posed by creation or existence of lawyer specific capital but rather to remove barriers to cross-selling. This is not strongly consistent with Hypothesis 3. to the extent that it does not refer to lessening of risks posed by lawyer specific capital. It is not, however, completely inconsistent with the Hypothesis as removal of barriers to cross-selling would result in clients having contact with a greater

number of the firms members than would otherwise be the case.

The root of the problem here is the difficulty of discovering whether the observation that the client may typically forge relationships with many lawyers of the firm nowadays is due to a conscious attempt by the firm to precipitate such a change, or if it is simply due to increasing specialisation and resultant functionalisation within firms. To be sure, the fact that clients are seen by many lawyers of the firm (often due to type of business changes and different legal specialisation requirements) should reduce the propensity for unhealthy coalitions between clients and partners or QAs to evolve - still further reducing the already evidently low risk firms currently perceive from client derived lawyer specific capital.

2.14 The use of specific restrictions to prevent lawyers leaving with clients:

(TABLE 7.9)

Firm No	RESTCOV	RCEMP	QARESTCO	INEFFECT	NEVER	DOLEAVE	CLICHOIC
1,8,9,13,16,18,19, 25,27,30 (10 Firms=30.3%)	No	No	No	No	No	No	No
14,26 (2 Firms=6.1%)	No	No	No	No	No	No	Yes
24 (1 Firm=3.0%)	No	No	No	No	No	Yes	Yes
6 (1 Firm=3.0%)	No	No	No	Yes	No	No	No
3 (1 Firm=3.0%)	No	No	No	Yes	No	No	Yes
2 (1 Firm=3.0%)	No	No	No	Yes	No	Yes	Yes
28 (1 Firm=3.0%)	No	No	Yes	No	No	No	No
15,21,33 (3 Firms=9.1%)	Yes	No	No	No	No	No	No
17 (1 Firm=3.0%)	Yes	No	No	No	No	No	Yes
31 (1 Firm=3.0%)	Yes	No	No	No	No	Yes	No
23 (1 Firm=3.0%)	Yes	No	No	No	Yes	No	Yes
10,32 (2 Firms=6.1%)	Yes	No	No	No	Yes	No	No
7,12 (2 Firms=6.1%)	Yes	Yes	Yes	Yes	Yes	No	No
11 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No
22 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	Yes
5 (1 Firm=3.0%)	DK	No	No	No	No	No	No
20 (1 Firm=3.0%)	DK	DK	DK	No	No	Yes	Yes
4 (1 Firm=3.0%)	DK	DK	DK	DK	No	No	Yes
29 (1 Firm=3.0%)	M	M	M	M	M	M	M
TOTAL FIRMS	12	2	5	5	5	4	10
%age FIRMS	36.4	6.1	15.2	15.2	15.2	12.2	30.3

(DK-Don't know, M-Missing)

Description of variables:
RESTCOV-Restrictive covenants used in partnership agreement
RCEMP-Restrictive covenants used for employees
QARESTCO-Restrictive covenants used for qualified assistants
INEFFECT-Restrictive covenants likely to be ineffective anyway
NEVER-We have never had the situation of lawyers leaving with clients
DOLEAVE-Lawyers do leave but do not take clients
CLICHOIC-It is always the choice of the client at the end of the day

One firm provided no information regarding the use of restrictive covenants and 3 others did not know whether they were used in the partnership agreement or not - 2 of whom did not know whether they applied to employees or qualified assistants either. These 2 firms also indicated it was the client's choice whether to stay or go with an exiting lawyer in any event.

(I) Firms using restrictive covenants in the partnership agreement - further breakdown:

12 firms used restrictive covenants in their partnership agreement, 3 of which provided no additional information. 3 firms indicated they have never had the situation of lawyers leaving

the firm with clients, 1 firm also claiming that it is the choice of the client whether to stay or go in any case. 1 firm only indicated this client choice aspect whilst another indicated that lawyers do leave but they tend not to take clients with them when they do.

2 firms indicated the existence of restrictive covenants for employees and qualified assistants but thought they would likely be ineffective anyway. They both disclosed they had never experienced a situation of lawyers leaving the firm with clients. 2 firms utilised restrictive covenants for qualified assistants, with one also indicating that, in the end, the client's choice was paramount in such situations.

(II) Firms with no restrictive covenants in the partnership agreement - further breakdown:

All 17 of these firms (bar one exception) did not use restrictive covenants for QAs or employees either - the exception was a firm which used them for its QAs. 10 firms failed to give reasons for not using them but the remaining 6 did offer further explanation. 3 firms anticipated they would likely be ineffective in any case, 2 of them also indicating the role of client choice in such situations and 1 indicating that lawyers do leave the firm but do not take clients with them. 3 firms disclosed the client choice argument solely as a reason for not using restrictive covenants, with one further disclosing that lawyers did leave the firm but without taking clients with them.

Hypothesis 2. states the firm will avoid use of restrictive covenants to prevent client losses through lawyers of the firm leaving, as they are likely to be futile. The evidence presented above, when combined with the fact that 15 firms expressly indicated they did not use restrictive covenants, and that 2 firms who do use them think they would be ineffective anyway, is supportive of Hypothesis 2.

Those firms which did utilise them were generally open in admitting their unlikely enforceability and doubtful effectiveness, but nevertheless typically relied upon such mild restrictions to have moral rather than legal enforceability.

2.15 Constraints on lawyers leaving the firm:

(TABLE 7.10)

Firm No	FIRM LOY2	PRES REW	PROS PECT	CAR EER	DIFF EXIT	PRES FIRM	VALUE	DUPT EAM	OTHER5
3,4,5,7,8,9, 10,12,13,14, 15,16 (12Firms=36.4%)	Yes	Yes	No	No	No	No	No	No	No
2,17,24,33 (4 Firms=12.1%)	Yes	Yes	Yes	Yes	No	No	No	No	No
20,23,30 (3 Firms=9.1%)	Yes	Yes	No	Yes	No	No	No	No	No
6(1 Firm=3.0%)	Yes	Yes	No	No	No	No	Yes	No	No
32(1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	Yes	Yes	No
22,27,28 (3 Firms=9.1%)	Yes	No	No	No	No	No	No	No	No
19(1 Firm=3.0%)	Yes	No	No	Yes	No	Nor	No	No	No
31(1 Firm=3.0%)	Yes	No	Yes	Yes	No	No	No	No	No
25,26 (2 Firms=6.1%)	No	Yes	No	No	No	No	No	No	No
1(1 Firm=3.0%)	No	Yes	No	Yes	No	No	No	No	No
21(1 Firm=3.0%)	No	Yes	Yes	Yes	No	No	No	No	No
11(1 Firm=3.0%)	No	No	No	No	Yes	No	No	No	No
18(1 Firm=3.0%)	No	No	Yes	Yes	No	No	No	No	No
TOTAL FIRMS	27	26	8	13	1	2	2	1	0
%age FIRMS	81.8	78.8	24.2	39.4	3.0	6.1	6.1	3.0	0

Description of variables:
FIRMLOY2-Loyalty to firm
PRESREW-Present rewards
PROSPECT-Prospect of promotion and partnership
CAREER-Good career path
DIFFEXIT-Difficulty of divorce from present partnership
PRESFIRM-Status of working for present firm
VALUE-Value is greater in present employment than in other firm
DUPTEAM-Difficulty of duplicating team outside firm
OTHER5-Other

In view of the fact that few firms relied on specific constraints on lawyers leaving the firm with clients and that those that did were less than confident of their likely success, what follows is an investigation of non-specific constraints on lawyers leaving the firm.

A myriad of combinations of intangible and non-specific constraining factors were presented as reasons why lawyers did not leave their present employment position, with or without clients. A combination of loyalty to the firm and their other partners and satisfaction with present rewards was viewed by 12 firms as a constraint on leaving. 4 firms supplemented this by additionally mentioning prospects of promotion and partnership, and the existence of a good career structure combining to constrain exit.

In addition to firm loyalty and present rewards, 3 firms viewed career structure and another, the value of remaining in the present firm being greater than in another firm, as exit constraints. Another firm viewed firm loyalty, the value of present rewards, the status of working for the present firm, his value being greater in his present firm than in other firms, and difficulty of duplicating established teams elsewhere as all constraining a partner's exit.

3 firms thought loyalty to the present firm was a sufficient constraint to prevent leaving, whilst one firm also added career structure and another further added the prospect of promotion and partnership, to the list of exit constraints. 2 firms believed present rewards were sufficient to prevent lawyers leaving. 1 firm added career structure to this and another

also added prospect of promotion and partnership. 1 firm believed difficulties facing a lawyer in divorcing himself from his present partnership was the important constraint on leaving. Prospects of promotion and partnership combined with a good career structure, were seen by the final firm to constrain exit.

The typical absence of reliable formal organisational constraints is strongly indicative that within a law firm, mechanisms which rely primarily on self-enforcement can be successfully relied upon to regulate behaviour and prevent opportunism. It would appear from TABLE 7.10 that the perceived loyalty of the partners in most firms is strong, resulting in little need for formal constraints on the individual. In this respect, the reliance and trust firms place in the moral, rather than legal, value of restrictive covenants may not be misplaced.

The evidence above can be regarded to be forcibly supportive of Hypothesis 4. where the lawyer's exit option is claimed to be constrained by other factors, in addition to the value of firm specific capital he has amassed within the firm. The problem of the lawyer in this respect is that it is difficult, if not impossible, to firstly identify, and secondly evaluate, the value of his client derived specific capital in the event of him using this as a consideration in a decision to leave his firm. It is not practically possible for the lawyer to ask clients (pre-decision) whether, if he decided to leave, they would follow him to his new firm or not. If in the unlikely event this was brazenly attempted, and he decided exit was not viable, this behaviour would have probably undermined clients' confidence in him as a committed member of that firm.

2.16 Recognition of different client sophistication levels and how firms cope with these:

(TABLE 7.11)

Firm No	PRIVCLI2	COMMCLI2	REPLEVEL	BROCUSED	HANDHOLD	SEEKOUT	OTHER6
2,4,7,12,15,16, 28,32 (8 Firms=24.2%)	No	No	Yes	Yes	Yes	Yes	No
10,11,17,25 (4 Firms=12.1%)	No	No	Yes	No	Yes	Yes	No
27,23 (2 Firms=6.1%)	No	No	Yes	Yes	No	No	No
29,33 (2 Firms=6.1%)	No	No	Yes	Yes	No	Yes	No
21,26 (2 Firms=6.1%)	No	No	Yes	Yes	Yes	No	No
22(1 Firm=3.0%)	No	No	No	Yes	No	No	No
6 (1 Firm=3.0%)	No	No	Yes	No	No	No	No
18(1 Firm=3.0%)	No	No	Yes	No	No	Yes	No
20,32 (2 Firms=6.1%)	No	Yes	Yes	Yes	No	Yes	No
30(1 Firm=3.0%)	No	Yes	Yes	Yes	No	No	No
8 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	Yes	No
9 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	Yes	No
14,24 (2 Firms=6.1%)	Yes	Yes	No	No	No	No	No
5,13 (2 Firms=6.1%)	Yes	Yes	Yes	No	Yes	Yes	No
1 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	No
19 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	Yes	No
3 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	Yes	No
TOTAL FIRMS	9	10	29	22	19	23	0
%age FIRMS	27.3	30.3	87.9	66.7	57.6	69.7	0

Description of variables:
PRIVCLI2-Differing sophistication of private clients more noticeable

COMMCLI2-Differing sophistication of commercial clients more noticeable
REPLEVEL-Alter reporting intensity depending on sophistication
BROCUSED-Brochures used to inform less sophisticated clients
HANDHOLD-Handhold less sophisticated clients
SEEKOUT-Seek out clients requirements and tailor activities accordingly
OTHER6-Other

This section was aimed at discovering how firms responded to differing levels of sophistication across clients. All 33 firms admitted recognising differing degrees of client sophistication existed and that it was important to tailor services accordingly. 2 firms recognised that differing degrees of sophistication were more noticeable across private clients and 3 firms recognised this to be the case across commercial clients. 7 firms recognised that depending on the nature of particular clients, differing sophistication levels were sometimes more noticeable across private clients and other times across commercial clients.

The remaining 21 firms, while noting differing degrees of sophistication was important and noticeable across clients, did not indicate whether this was more pertinent in the case of commercial or private clients.

29 firms altered their reporting levels and intensity/ frequency of reporting on details and progress of the transaction depending on client sophistication levels and the level of interest the firm perceived the client would have in such matters. 22 firms used some format of firm brochure to attempt to inform less sophisticated clients of important information regarding services offered by the firm, with a view to present and future dealings with the client.

23 firms disclosed that efforts were made to discover as much about the client and his needs, firstly, to initially determine their sophistication level, secondly, to determine individual requirements and, finally, to customise service given depending on information discovered. 19 firms recognised a need to 'handhold' less sophisticated clients through services if this was what the client wanted, but typically noted that often less sophisticated clients were uninterested in details of the service being provided. These firms believed that such clients did not want to be bothered and would rather the firm only contacted them if essential, or to indicate the completion.

Section Three: Questionnaire Section Six - The Partnership Sharing Bargain:

Introduction:

As a result of the theoretical emphasis and importance assigned to the methods of sharing residual income between partners of the law firm, and the amount of empirical information that was collected regarding this feature, the remainder of this chapter will be devoted to an empirical examination of sharing bargain issues and the function of partnership as a remuneration device for lawyers pooling human capital. These issues will be examined in the

light of empirical information gathered from the sample firms.

3.1 The sharing bargain and incentive structure of the partnership:

The more popular practice mode for lawyers in the UK at present is partnership. It is apparent from the examination of relevant theoretical literature earlier in this thesis that the partnership sharing bargain is a central focus of attention in partnership organisation. This is justified since it is this contract which specifies the respective claims each partner has to the residual of the practice after he has pooled his human capital with fellow practitioners. It is, thereby, an important mechanism for creating and shaping incentives/ disincentives which face each partner of the firm. The strength of the incentives the sharing bargain creates and the resulting individual behavioural responses it evokes largely determines many features of the internal organisation of the law firm.

The incentive structure within any organisation determines the degree to which individual behaviour can be coerced to become compatible with the overall aims of the organisation, and, therefore, in the case of partnership, determines the extent to which cooperative gains between partners will be realised.

The characteristic features of the law firm sharing bargain are, therefore, regarded as instrumental in influencing individual partner behaviour and as such they are important to examine empirically - this is the purpose of the sixth section of the questionnaire.

3.1 The concern of the firm to identify and measure productivity:

In certain partnerships an attempt will be made to tie individual partners' productivity to their income share. It is vital to identify how these firms circumvent the problem of identifying and measuring partner productivity. The resultant productivity measure taken will influence how the individual will allocate his time and what level of effort intensity he will supply to various elements of law firm business.

Measures of productivity create both incentives and perverse incentives and account must be taken of both effects when looking at how the firm measures productivity.

3.2 The influence of seniority in partnership income division:

Some partnerships can be expected to shy away completely from problems of productivity measurement and simply tie income shares broadly to seniority within the firm. The problems

and advantages of this policy on income sharing are extensively examined elsewhere in this thesis.

The sharing bargain may thus be purely seniority based, purely productivity based, some hybrid intermediate system, or merely a pure expense sharing agreement whereby individuals remain quasi-sole practitioners. In this context, given the potentially infinite refinements which could produce many unique share bargain types, it was perceived to be advantageous to reduce this number by consolidation using questions which would categorise sharing bargain types into a small number of usefully differentiable groupings.

3.3 Problems of partners under-investing their time in activities for which no direct compensation is given:

At the level of the individual partner, as party to the contract of the firm, it is of particular interest to attempt to understand how partners will select and allocate how much time they will spend on activities they receive direct compensation for and how much they will spend on activities that either results in no compensation, or very indirect compensation. It is recalled that within Chapter Six, where incentive features of sharing bargains were discussed in depth, it was argued that if lawyers in the firm are perceptive and rationally react to incentives they face, they may underinvest their time in activities which produce little or no direct compensation. In this context, empirical analysis conducted in this chapter will examine the nature of incentives confronting lawyers within the firm which stimulate them to engage in such activities.

It is anticipated that empirical investigation of these issues will help rationalise why partnership organisation underpins the current structure of the legal profession. Alternative practice modes can be expected to result in those within the firm facing a different set of incentives. The effect such a change would precipitate would, of course, be dependant more specifically on the actual organisational forms such alternatives would constitute. These and other related issues will be examined more specifically and thoroughly in the concluding section of the questionnaire, to be discussed in Chapter Nine.

3.4 The lawyer's internal monitor and firm culture - invisible behavioural constraints:

Gilson and Mnookin (1984) can be regarded as the seminal work in the area of analysis concerning partnership income division [18]. In this paper, which has been subject to lengthy critique in the previous chapter, an exposition of the relative merits of sharing and productivity based partnership income division models is presented.

In the case of both models, Gilson and Mnookin (1984) emphasise the importance of the strength of the internal monitor of the typical lawyer and firm culture as constraints on behaviour within the organisation [19]. This is expected to result in the lawyer being willing to take part in firm activities where their would appear to be no rational incentive to participate.

The formality of incentives and compensation systems within the firm will be examined here for the sample firms to discover whether the firm can rely on the internal monitor of the lawyer to provide sufficient incentive to take part in certain areas of law firm activity without direct compensation, or whether direct compensation is required to provide direct incentives. It is anticipated that the strength of internal monitor of the typical lawyer operating in partnership will be indicated.

3.5 Challenges posed to internal monitoring and firm culture:

It is apparent that newer entrants to the legal profession may require more direct incentives and constraints within the firm since their internal conscience/ monitor may not be as strong as those of the existing lawyers of the firm and the profession in general. This may require a change in emphasis in terms of the internal organisation of partnership. Where sample firms indicate a need to change the ways in which this type of law firm problem is currently solved, this may be indicative of a changing breed of more self-interested lawyer entering the profession and legal partnership. This may force firms to change, for instance, the finer details of their sharing bargain to emphasise productivity measurement in an attempt to preempt or constrain shirking - where this would have previously been effectively constrained by the lawyer's internal monitor, firm culture, and peer/ mutual monitoring.

The concepts of shirking, grabbing and leaving as discussed by Gilson and Mnookin (1984) will also be examined empirically [20]. This has been discussed at a previous point in this chapter but in relation to the issue of creation of firm and lawyer specific capital. The firms reaction to an attempt by a lawyer to grab, or threat to leave in an attempt to grab more successfully, will be investigated with the aim of providing some indication of whether or not shirking, grabbing and leaving are as significant a problem as Gilson and Mnookin (1984) suggest [21].

A stated above, Gilson and Mnookin (1984) also suggest that where partners are not directly compensated for certain law firm activities, they will tend to underinvest their time in performing such duties [22]. Internal monitor and firm culture arguments come into play here again where it could be expected that the result will be that some persons will gravitate towards these tasks in the firm and others will be willing to let them do them.

The firm can attempt to at least partially circumvent this potential underinvestment problem

using principles of delegation and specialisation and this is investigated in this section of the questionnaire. The manner and method of any resultant delegation is examined to determine how problems the firm may experience in this direction are overcome.

3.6 The formality of partner specialisations:

An examination of the functions performed by each partner within the firm is required. It could be expected that larger firms are likely to more formally functionalise partners into management specialities. It is unlikely that there will be much additional specialisation beyond management and legal specialities, such as those envisaged by Feinberg (1984) where he creates the Finder - Minder - Grinder distinction [23] (Finders specialise in attracting new clients, Minders in keeping current clients happy, and Grinders actually perform most of the legal business). The empirical study will, therefore, investigate the extent of partner specialisation in all of the above directions.

It is expected that larger law firms will appoint a managing/ senior partner to whom all partners will be ultimately accountable. Larger firms are also expected to have formal hierarchical partner structures with committees, boards, and formal chains of command and may create distinct partner groups such as, junior and senior partners. In smaller firms there is less scope for and far less requirement for such extensive specialisation and it is, therefore, expected that smaller firms will have a far less complex and formalised organisational structures. The empirical study will examine the extent and nature of formal management structures within the sample of law firms and aims to offer some explanation of why they are organised as they are.

3.7 Specific sharing bargain hypotheses to be empirically tested:

Hypothesis 1: The partnership sharing bargain will be almost unique for each firm, although broadly similar features will be revealed across firms.

Hypothesis 2: Firms that measure productivity as a determinant of income will do so in a fairly subjective and unsystematic manner.

Hypothesis 3: Firms will use seniority as at least a minor determinant of partner income shares.

Hypothesis 4: Lawyers will respond to incentives other than monetary ones in their decision to undertake certain activities within the firm.

Hypothesis 5: The lawyer's internal monitor and the culture of the firm will be strong enough to obviate the provision of specific incentives for lawyers to engage in many activities within the firm.

Hypothesis 6: The influence of the lawyer's internal monitor and the culture of the firm will weaken in larger firms requiring more formal constraints and incentives for partners of the firm.

Hypothesis 7: The strength of the lawyer's internal monitor is likely to result in a low tendency to shirk, grab and leave.

Hypothesis 8: In large firms the formality of partner specialisations will be greater than in small firms.

3.8 The partnership sharing bargains and incentive structures of sample firms:

In this section, the nature of each firm's method of apportioning income between partners of the firm is investigated. It is anticipated this will facilitate understanding of incentives facing individuals within the typical law firm. This will make it possible to compare the manner in which theory predicts they would behave when faced with such incentives, with the information received relating to actual individual partner behaviour within sample firms.

(I) The type of partnership sharing model:

(TABLE 7.12):

Firm No	EXPSHARE	EATKILL	PTRCENTR
1,2,3,4,5,6,7,8,9,10,11,12,13,14, 15,16,17,18,19,20,21,22,23,24,25, 26,27,28,30,31,32,33 (32 Firms=97.0%)	No	No	No
29 (1 Firm=3.0%)	No	Yes	Yes
TOTAL FIRMS	0	1	1
%age FIRMS	0	3.0	3.0

Description of variables:
EXPSHARE-Simple expense sharing model
EATKILL-'Eat what you kill' model
PTRCENTR-Partners are individual profit/ cost centres

From the table above it is apparent that none of the firms were simply quasi-partnerships - whereby each partner essentially remains a sole practitioner but collective practice permits them to share overheads etc.

Only 1 firm came close to this type of arrangement, to the extent that, firstly, each partner remained an individual profit/ cost centre and, secondly, the firm employed an 'eat what you kill' method of income distribution. Curiously, this occurred in one of the large firms but this

can be rationalised as a response to control the twin problems of shirking (which can become a significant problem in a large partnership employing a strict sharing model of income distribution) and measuring relative productivity (which is problematic in any partnership model aimed at measuring partners relative productivity). Using partner profit/ cost centres it is much easier to discover and apportion marginal product and thus relative income shares - it is also not viable to shirk since the cost of doing so will be borne solely by the shirker.

3.9 The role of seniority in income share determination between partners:

(TABLE 7.13)

Firm No	SENGROUP	PRTPOINT	POINTINC	SALFIX	SALPROF	EQUAL
1,4,5,11,15,18,26,27,30, 32 (10 Firms=30.3%)	Yes	No	No	No	No	No
3,6,12,16,19 (5 Firms=15.2%)	Yes	No	No	Yes	No	No
14,21 (2 Firms=6.1%)	No	No	No	No	No	No
13,17 (2 Firms=6.1%)	No	No	No	No	No	Yes
8 (1 Firm=3.0%)	No	No	No	Yes	No	Yes
23 (1 Firm=3.0%)	No	No	No	Yes	No	No
9,20,22,24,25,28,33 (7 Firms=21.2%)	No	Yes	Yes	No	No	No
2,7,29,31 (4 Firms=12.2%)	No	Yes	Yes	Yes	No	No
10 (1 Firm=3.0%)	No	Yes	No	Yes	Yes	No
TOTAL FIRMS	15	12	11	12	1	3
%age FIRMS	45.5	36.4	33.3	36.4	3.0	9.1

Description of variables:
SENGROUP-Income share depends on seniority group
PTRPOINT-Partners of similar seniority get same number of points
POINTINC-Number of points increases with seniority
SALFIX-Salaries of salaried partners are fixed by equity partners
SALPROF-Partners get salary and equity profit share
EQUAL-Equity partners get equal shares of the profits

Basically 3 broad types of income sharing model could be identified here and firms will be analyzed accordingly below.

(I) Firms with seniority groupings where income share depends on seniority grouping - further breakdown:

All 15 firms of this type assigned partners to seniority groupings with their income shares being at least a function of the seniority grouping they inhabit. In 5 of these firms, it was also revealed that salaries of non-grouped salaried partners were fixed by the equity partners. This entire grouping comprised of 8 small/ medium firms and 7 large firms.

(II) Firms where partners of similar seniority are assigned similar numbers of points - further breakdown:

Of the 12 firms of this type, 11 indicated the number of points partners were assigned increased with seniority, 4 of them also noting salaries of no-point partners are fixed by the equity partners. The remaining firm also indicated this for salaried partners, but additionally disclosed that all partners received a basic salary plus a 'number of points' related profit share of total partnership profits. Of this grouping, 5 were small/ medium and 7 were large firms.

(III) Firms who do not rely on seniority or numbers of points groupings to determine profit shares - further breakdown:

The 6 remaining sample firms were categorised in this grouping. 2 firms provided no information beyond merely indicating that partners are not assigned to seniority or numbers of points groupings. 3 firms (all small/ medium) disclosed partners receive equal shares of partnership profits irrespective of seniority, one of them additionally disclosing that salaries of non profit sharing partners are fixed by the equity partners.

The remaining firm only provided information indicating that the equity partners determined the salaries of the non equity sharing partners. This profit sharing grouping housed 4 small/ medium firms and 2 large firms.

3.10 Income shares and seniority - further investigation:

(TABLE 7.14)

Firm No	INCSEN	INCPOINT	ACCDECEL	DETCOMM
8,13,17,21,23 (5 Firms=15.2%)	No	No	No	No
14 (1 Firm=3.0%)	No	No	No	Yes
2,7,9,10,20,22,24,33 (8 Firms=24.2%)	No	Yes	No	No
25,29,31 (3 Firms=9.1%)	No	Yes	Yes	No
28 (1 Firm=3.0%)	No	Yes	Yes	Yes
1,3,5,6,11,12,15,16,18,27,32 (11 Firms=33.3%)	Yes	No	No	No
4,26,30 (3 Firms=9.1%)	Yes	No	Yes	No
19 (1 Firm=3.0%)	Yes	No	No	Yes
TOTAL FIRMS	15	12	7	3
%age FIRMS	45.5	36.4	21.2	9.1

Description of variables:
INCSEN-Income share depends on seniority group
INCPOINT-Income share depends on number of points
ACCDECEL-Partners can be accelerated or held back on ladder
DETCOMM-Income shares of equity partners determined by committee

TABLE 7.14 above, demonstrates that for the 15 seniority grouping firms, and the 12 point grouping firms, additional information disclosed permits further categorising of sample firms.

Firstly, of the group of 6 non-seniority influenced firms identified above, 5 provide no additional information in TABLE 7.14. However, 1 firm indicated partners' relative income shares were determined by a committee of partners established to perform this function.

(I) Seniority grouping firms - further breakdown:

11 of these 15 firms provide no additional information which could be used to refine categorisation, however, 3 firms did indicate that although partners are assigned to seniority groupings they can be accelerated or held back on the ladder of seniority groupings for good or bad performance. The final firm disclosed that a committee reviewed the groupings and to that extent, largely determined relative income shares of the equity partners.

All 4 of the firms where seniority groupings are flexible, either because of performance penalties/ rewards, or committee review, are large firms. This is indicative that reliance on a seniority based sharing model in large firms may be problematic, requiring adjustment of the sharing mechanism to alter the incentive structure of the firm.

(II) Point related grouping firms - further breakdown:

Of these 12 firms, 8 provided no additional categorisation information. 4 firms did, however, indicate that numbers of points assigned to partners could be altered to penalise/ reward performance - in 1, a committee performed this assignment of points (contingent on performance) role. Of these 4 firms, 3 were large and 1 was small/ medium, again indicating the requirement to dilute pure seniority sharing models in larger firms to accommodate at least minimal performance contingent incentives.

Where firms incorporate acceleration/ restraint mechanisms to seniority based models (of either a groupings or points based type), partners can be penalised or rewarded contingent on performance. More precisely, partners jump up seniority groups or are allocated more points as a reward for good performance. Conversely, poor performance is penalised by a partner remaining in a seniority group longer than his peers by not being allocated points along with his peers (or at worst moving down groups by surrendering points already allocated). Hence, even in these models which emphasise sharing rather than productivity, a performance related penalty/ reward system provides incentives and peer group pressure to enhance performance. Performance evaluation encroaches into 4 of the 15 seniority groupings firms, and into 4 of the 12 points based firms.

In the 3 firms where income shares of partners are determined by a committee, the following applies. In the firm where formal seniority groups exist, the committee determines and periodically reviews which seniority group partners should belong to. In the firm where a points based system exists, modified by a performance contingent acceleration/ restraint mechanism, the committee evaluates partner performance and determines point allocations for partners. The final firm employs a system where the committee exclusively determines partners relative income shares.

It is apparent that seniority plays a significant, if not exclusive, role in methods of assigning income shares to partners in all but 6 of the partnerships examined. To this extent, Hypothesis 3, which states that firms will use seniority as at least a minor determinant of partner income shares, is supported by empirical evidence discussed above.

It is also apparent from preceding TABLES 7.12, 7.13 & 7.14 that, while firms exhibit

common features in respect of profit sharing methods, each firm has its own customised mechanisms within its partnership sharing bargain. This is supportive of Hypothesis 1, which states the partnership sharing bargain will be almost unique for each firm, although broadly similar features will be revealed across firms.

3.11 The basis of differentiation of income of similar seniority partners:

(TABLE 7.15)

Firm No	SGSHARE	PTSSAME	CONTRIB	MERIT	PRODUC	COMMDEC2	BOARDDEC	PTRDEC
1,5,6,11,12, 13,16,17,18, 27,32 (11Firms=33.3%)	Yes	No	M	M	M	M	M	M
2,7,9,10,20, 22,24,33 (8 Firms=24.2%)	No	Yes	M	M	M	M	M	M
19,21,25,26, 28,29,31 (7 Firms=21.2%)	No	No	Yes	No	No	Yes	No	No
3,4,30 (3 Firms=9.1%)	No	No	Yes	No	No	No	No	No
14(1 Firm=3.0%)	No	No	Yes	No	No	Yes	No	Yes
23(1 Firm=3.0%)	No	No	Yes	Yes	Yes	Yes	No	No
15(1 Firm=3.0%)	No	No	No	Yes	No	No	No	No
8 (1 Firm=3.0%)	M	M	No	No	No	No	No	Yes
TOTAL FIRMS	11	8	12	2	1	9	0	2
%age FIRMS	33.3	24.2	36.4	6.1	3.0	27.3	0	6.1

(M-Missing value)

Description of variables:
SGSHARE-All partners of the one seniority group have equal shares
PTSSAME-All partners with the same number of points earn the same
CONTRIB-Contribution causes share differentials within groups
MERIT-Merit payments causes share differentials within groups
PRODUC-Productivity causes share differentials within groups
COMMDEC2-Committee decides share differentials within groups
BOARDDEC-Board decides share differentials within groups
PTRDEC-Senior/ managing partner decides share differentials within groups

(I) Firms where partners in the same seniority group earn the same share of profit - further breakdown:

11 firms indicated the above was the case, including 2 of the 3 firms that indicated partners received equal profit shares in TABLE 7.14. Of the firms in this grouping, 8 were small/ medium and 3 were large firms.

(II) Firms where partners with similar numbers of points earn the same share of profit - further breakdown:

The 8 firms that solely indicated that partners' income shares depended on the number of partner points in TABLE 7.14 all disclosed, as is evident from TABLE 7.15, that partners of similar pointage earn similar partnership income shares with no intra point group differentials existing. These 8 firms comprised 50% large and 50% small/ medium firms.

(III) Firms where partners of similar seniority earn differing shares of partnership profits - further breakdown:

This category of firms totalled 14 firms, 5 of which were small/ medium and 9 of which were

large firms, and all of which are described in greater detail below.

From TABLE 7.14, 11 firms mentioned only that partners' income shares are dependent on seniority groupings. 2 of these firms (Firm Nos. 3 and 15) additionally disclose in TABLE 7.15 that partners within these seniority groups need not necessarily earn similar income shares. In 1 of these firms, assessment of individual partner 'contribution' can cause minor income differentials between partners of a single group. In the other firm, it is disclosed that merit payments can have a similar effect within a single seniority grouping.

The following firms provided little or no information in TABLE 7.14. - from TABLE 7.15 it can be seen that in 1 firm (Firm No.8), the senior partner/ managing partner decides on partners' relative profit shares and, thereby, creates income differentials. In another firm (Firm No.23), a committee decides on income differentials and 'contribution', merit payments and differences in individual productivity (as evaluated and decided upon by this committee) creates income differentials between partners. In 1' firm (Firm No. 14), a committee and the managing/ senior partner jointly decide to create income differentials between partners based on their relative 'contribution'.

In 3 firms (Firm Nos. 3, 4 & 30), relative 'contribution' creates income differentials between partners. Firm No.3 is discussed above and requires no further description. Firm Nos. 4 & 30 can be seen from TABLE 7.14 to be firms that have seniority groups and an acceleration/ restraint mechanism. The basis of the acceleration/ restraint mechanism is relative individual partner 'contribution', as revealed by TABLE 7.15.

In the remaining 7 firms, partner income differentials are decided by a committee who assess individual partners' relative 'contribution' to the firm and award income shares on that basis.

1 firm (Firm No.19), mentioned in TABLE 7.14 that it had seniority groups and that a committee of partners decided on initial grouping and subsequent review of groupings. Information in TABLE 7.15 indicates the basis of the decision of this committee is partners' relative 'contribution'. In Firm No.21, TABLE 7.14 indicated that seniority did not have a bearing on partners' profit shares and Table 7.15 indicates that a partnership committee decides on partners' relative profit shares based exclusively upon their individual relative 'contribution'.

In 3 firms (Firm Nos.25, 29 & 31), TABLE 7.14 indicated that partners were awarded points and that a mechanism existed to alter assignment of partnership points contingent upon performance. TABLE 7.15 reveals this mechanism is a partnership committee which determines points and, therefore, income differentials between partners on the basis of relative 'contribution'. In Firm No.28 it was disclosed in TABLE 7.14 that a committee performed the

assignment of points to create income differentials. In TABLE 7.15 it is revealed further that the committee creates income differentials by assessment of relative 'contribution'.

For the final firm (Firm No.26), TABLE 7.15 indicates a committee either accelerates or restrains partners movement up through partnership seniority groups (as indicated in TABLE 7.14) by assessment of partners' relative 'contribution'.

3.12 Identification of 'true sharing model' firms:

The combined group comprised 11 firms, in which all partners within a similar seniority group earn the same profit share, and 8 firms, in which partners with the same number of points earn the same profit share, can be regarded as the 19 firms which are closest to true 'sharing model' firms. Within these 19 firms, 12 of whom are small/ medium sized and 7 of whom are large, there is no measurement of productivity whatsoever. There is hence, a more frequent incidence of true sharing models in small/ medium firms than in large firms - an intuitively pleasing and expected result.

In the remaining 14 firms, while 10 mention seniority is a factor in determining income shares (6 in terms of partner seniority groups and 4 in terms of points), they all introduce measurement of partner productivity to a greater or lesser extent to the determination of partners' relative income shares. Of the 14 firms that have productivity based models, 9 are large and 5 are small/ medium firms, confirming the expectation that larger firms will tend to rely to a greater extent on productivity measurement to control agency problems which become more prevalent in large firm practice.

3.13 Identification of 'productivity' based profit division model firms:

(I) The measurement of partners' relative 'contribution'-

12 firms use the measure of individual partners' 'contribution' to the firm as a proxy for individual partner productivity and as a measure to differentiate income shares of partners of similar seniority. Firms typically gave the impression they found no difficulty in assessing each partners' relative 'contribution' to the firm and, consequently, believed they could thus systematically determine partners' relative shares using this highly subjective measure. Firms generally did not have a strict formula to calculate 'contribution' - most likely because its components are difficult to observe and measure and quantify objectively. What firms relied on typically was a general impression of each partners' contribution and worth to the firm.

9 of the 12 firms that used 'contribution' as an income differential measurement were large firms. 2 firms used merit payments to differentiate income of similarly senior partners, one of which also used some measure of 'contribution'. This firm was also the only firm who

explicitly indicated that they attempted to measure individual partners' 'productivity'. Income differentials within this firm were argued to reflect differences in partner productivity, relative contribution, and the consequent award of merit payments.

(II) Who measures partners' relative 'contribution' ?-

9 firms indicated that a partnership committee was;

1. Entrusted with identifying individual partners' 'contribution' to the firm and,
2. Subsequently invested with authority to determine partners' relative income shares.

In 1 of these 9 firms, the senior/ managing partner jointly performed the above function with a committee. In 1 other firm there was no committee to perform such a task and the senior/ managing partner was invested with exclusive authority to assess performance and impose penalty/ rewards on the partners. Curiously, it was the case, however, that this firm was one of the 2 firms that indicated all partners received the same share of profits - while the senior/ managing partner possessed the authority to differentiate income, this authority had not yet been exercised.

Within the $\overline{14}$ firms which attempt to create income differentials between partners of similar seniority and experience, it is true to say that this is done in a fairly crude, subjective and largely unsystematic manner. This offers support to Hypothesis 2, which alleges that, where firms measure productivity as a determinant of income, they will do so in a fairly subjective and unsystematic manner.

The firms in the sample have, therefore, been identified and categorised as having two basic income division methods and belonging to two size categories. The table below groups firms in terms of their revealed characteristics in relation to these two factors.

(TABLE 7.16)

	True Sharing Model Firms		Productivity Based Firms	
	Seniority Groupings	Pointage Groupings		
Small Firms	1,5,6,11, 12,13,16, 17 (8 Firms)	2,7,9,10 (4 Firms)	3,8,14,15,25 (5 Firms)	
			(Total 12 Firms)	(5 Firms)
Large Firms	18,27,32 (3 firms)	20,22,24 33 (4 Firms)	4,19,21,23,26, 28,29,30,31 (9 Firms)	
			(Total 7 Firms)	(9 Firms)
Total Firms	11 Firms	8 Firms		
Total Sample			19 Firms	14 Firms

3.14 The relationship between income levels of different partner seniority groups:

(TABLE 7.17)

Firm No	LOCKSTEP	POINTSCH	PRODINC
3,4,14,15,19,21,23,26,30,31 (10 Firms=30.3%)	No	No	Yes
1,5,6,11,12,16,18,27,32 (9 Firms=27.3%)	Yes	No	No
2,7,9,10,20,22,24,33 (8 Firms=24.2%)	No	Yes	No
25,28,29 (3 Firms=9.1%)	No	Yes	Yes
8,13,17 (3 Firms=9.1%)	M	M	M
TOTAL FIRMS	9	11	13
%age FIRMS	27.3	33.3	39.4

(M-Missing value)

Description of variables:
LOCKSTEP-Fixed ratio of income between seniority groups
POINTSCH-Ratio variable since number of points change
PRODINC-No fixed ratios since productivity included

The 9 firms within which there was alleged to exist a fixed ratio between seniority groups, were all true sharing models (as identified above in TABLE 7.15.) which grouped partners into formal seniority groupings. This describes the lockstep seniority partnership model.

10 firms indicated, as a result of inclusion of partner productivity (however measured), ratios between seniority groups did not make sense. All of these firms were naturally productivity model based partnerships.

8 firms indicated ratios were variable, because the number of points in the partnership changed from year to year, and these were all true sharing models who relied upon pointage rather than formal groupings to denote seniority. These firms can be regarded as point based

modified lockstep models.

3 firms noted that income ratios between partners of similar seniority were not fixed, firstly, as a result of productivity measurement and, secondly, because the number of points in the partnership changes year to year. These 3 firms were all productivity based firms, where productivity was rewarded (penalised) by allocation (retention) of partnership points.

2 of the 3 firms that failed to provide information here were true sharing model firms, and 1 was a productivity model partnership.

3.15 Time taken by partners from initial assumption as partner to reach full seniority status:

(TABLE 7.18)

Firm No	NOTSEN	CAPCONT	YEARS05	YEARS610	YEAR1115	YEAR1620	PERFORM1
2,6,9,12,18,22, 24,25,27,30,31, 32(12 Firms=36.4%)	No	No	No	Yes	No	No	No
11 (1 Firm=3.0%)	No	No	Yes	No	No	No	No
10 (1 Firm=3.0%)	No	Yes	No	No	No	No	No
14 (1 Firm=3.0%)	No	Yes	No	No	No	Yes	No
17 (1 Firm=3.0%)	No	Yes	Yes	No	No	No	No
1,7,8,16,20,28,33 (7 Firms=21.2%)	Yes	No	No	No	No	No	No
3,4,19,21,23,26,29 (7 Firms=21.2%)	Yes	No	No	No	No	No	Yes
15 (1 Firm=3.0%)	Yes	No	No	No	No	Yes	No
5 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No
13 (1 Firm=3.0%)	M	M	M	M	M	M	M
TOTAL FIRMS	16	3	3	12	0	2	7
%age FIRMS	48.5	9.1	9.1	36.4	0	6.1	21.2

(M-Missing value)

Description of variables:
NOTSEN-No full seniority class
CAPCONT-Depends on capital contribution
YEARS05- 0-5 years
YEARS610- 6-10 years
YEAR1115- 11-15 years
YEAR1620- 16-20 years
PERFORM1- Depends on performance

Firms can be regarded as occupying two major categories here - firstly, firms in which a full seniority partner group exists, and secondly, firms in which no full seniority group exists. 1 firm (a small/ medium firm with a true sharing model) provided no information and is hence coded as a missing value.

(I) Firms in which there exists a full seniority partner group - further breakdown:

This grouping comprises 16 firms, of which 9 are small/ medium and 7 are large, and of which, 12 employ a true sharing model, and 4 firms a productivity based model.

12 firms disclosed that partners reached full seniority class in 6-10 years. In 9 of these firms, a true sharing model applied and in 3 firms, a productivity model operated. 5 of the 12 firms were small/ medium firms and 7 were large firms.

The remaining 4 firms are all small/ medium firms, 3 of which employ true sharing models and 1 of which employs a productivity based model. 2 of these firms indicated that full seniority class was reached in 0-5 years, but in 1 of them this was dependent on the rate of capital contribution to the firm during this period. The 2 remaining firms also noted the time to reach full seniority was dependent on the rate of capital contribution, but only one could provide a typical period, this being 16-20 years.

(II) Firms in which no full seniority partner group exists - further breakdown:

This grouping comprises of 16 firms, of which 7 are small/ medium and 9 are large. 6 of these 16 firms are true sharing model firms and in 10, a productivity model exists.

7 firms (4 small/ medium and 3 large) indicated that no full seniority partner class existed within the firm. Of these 7 firms, 5 employ a true sharing model and 2 employ a productivity based model.

7 firms (1 small/ medium and 6 large) indicated that no full seniority existed as a result of the inclusion of performance as a determinant of partner income shares. Naturally, all of these partnerships rely on productivity models for income division.

1 firm (a small/ medium firm) employing a productivity based model of income division, indicated that full seniority did not exist but that partners' incomes generally peaked after 16-20 years as a partner.

The last firm (a small/ medium, true sharing model firm) disclosed that full seniority did not exist but that partners' incomes generally peaked after 0-5 years as a partner.

3.16 The skewing of partnership share of income during the period as a partner:

(TABLE 7.19)

Firm No	STEADY	EARLY	LATTER	PLATEAU	TAILSOFF	PERFORM2
2,5,7,8,10,16,20,24,27, 30,31,32,33 (13 Firms=39.4%)	Yes	No	No	No	No	No
3 (1 Firm=3.0%)	Yes	No	No	No	No	Yes
6,18 (2 Firms=6.1%)	Yes	No	No	Yes	No	No
9,25 (2 Firms=6.1%)	Yes	No	No	Yes	Yes	No
14,22 (2 Firms=6.1%)	No	Yes	No	Yes	No	No
15 (1 Firm=3.0%)	No	Yes	No	Yes	Yes	No
12 (1 Firm=3.0%)	No	Yes	No	No	No	No
11 (1 Firm=3.0%)	No	No	Yes	No	No	No
1 (1 Firm=3.0%)	No	No	Yes	Yes	Yes	No
4,19,21,26,29 (5 Firms=15.2%)	No	No	No	No	No	Yes
17,28 (2 Firms=6.1%)	No	No	No	No	No	No
23 (1 Firm=3.0%)	M	M	M	M	M	Yes
13 (1 Firm=3.0%)	M	M	M	M	M	M
TOTAL FIRMS	18	6	2	8	4	7
%age FIRMS	54.5	12.2	6.1	24.2	12.2	21.2

(M-Missing values)

Description of variables:
STEADY-Income rises steadily
EARLY-Income skewed to earlier years
LATTER-Income skewed to latter years
PLATEAU-Income plateaus at maximum level
TAILSOFF-Income tails off towards retirement
PERFORM2-Income skewing depends on performance

As a precursor to categorising firms using information from TABLE 7.19, some of the firms' responses will be initially described - some firms will thereby escape categorisation. One small/ medium firm, employing a true sharing model, provided no additional information here. One large firm employing a productivity model, indicated solely that productivity determined the skewing of partner income during the period as a partner - its other answers being missing values. 2 firms (a small/ medium firm employing a true sharing model, and a large firm employing a productivity based model) answered no to all categories in this question, thereby escaping categorisation. The remaining firms are, however, capable of being categorised by shared characteristics.

(I) Firms whose partner income share basically rises steadily during the period as a partner - further breakdown:

This group contained 10 small/ medium and 8 large firms, of which 13 utilised a pure sharing model and 5 utilised a productivity based model.

The main category in this group of firms comprised of the 13 firms who indicated simply that partnership income share tended to rise steadily during the period as a partner. 6 of these firms were small/ medium and 7 were large, with 10 employing a sharing based model and 3 using a productivity based approach.

One small/ medium firm which employed a productivity model, noted that the share of partnership income share of a partner tended to rise steadily, even though productivity was included to differentiate between partners.

2 firms (1 small/ medium and 1 large), both of which used true sharing based models, noted that partners' income shares tended to rise steadily but later plateaued at a maximum level.

2 other small/ medium firms (1 employing a true sharing model, the other a productivity based model), noted a similar situation to the above but additionally disclosed that income, thereafter, tended to tail-off towards retirement.

(II) Firms whose partner income share is skewed towards the earlier years as a partner - further breakdown:

This group enjoyed 4 members, 3 of whom were small/ medium firms and 1 of whom was a large firm, with equal numbers employing true sharing and productivity based approaches.

2 firms (1 small/ medium utilising a productivity model, the other large and employing a true sharing model) both indicated that income share was skewed to the earlier years as a partner and later plateaued after a period.

1 small/ medium firm which utilised a productivity model, added to the response of the above firm that income share also tailed-off towards retirement. The last firm, also a small/ medium firm but this time utilising a true sharing based approach, noted only that income share was skewed to the earlier years as a partner.

(III) Firms whose partner income share is skewed towards the latter years as a partner - further breakdown:

2 firms (both small/ medium firms employing a true sharing model) noted that income share was skewed to the latter years as a partner. 1 additionally noted, however, that income share plateaued and, thereafter, tailed-off towards retirement.

(IV) Firms whose partner income share is solely dependent upon productivity - further breakdown:

All 5 firms in this category were large firms employing a productivity based system of income division. In such a system, partners were responsible for the skewing of their own income, to the extent, firstly, that income was related to performance and, secondly, that those responsible for assessing this and altering income shares fulfilled their task effectively.

3.17 The measure of productivity taken to determine partners' income shares:

(TABLE 7.20)

Firm No	PARTPROD	ADHOC	CONTRIB2	FORMULA	UNDEREX
1,2,5,6,7,8,9,10,11,12,13, 16,17,18,20,24,32,33 (18 Firms=54.5%)	No	No	No	No	No
22,27 (2 Firms=6.1%)	No	No	No	No	Yes
3,4,14,15,19,21,23,26,31 (9 Firms=27.3%)	Yes	No	Yes	No	No
29 (1 Firm=3.0%)	Yes	No	Yes	Yes	No
28 (1 Firm=3.0%)	Yes	No	No	No	No
25 (1 Firm=3.0%)	Yes	No	No	Yes	No
30 (1 Firm=3.0%)	Yes	Yes	No	No	No
TOTAL FIRMS	13	1	10	2	2
%age FIRMS	39.4	3.0	31.0	6.1	6.1

Description of variables:
PARTPROD-Partner productivity
ADHOC-Adhoc measure taken
CONTRIB2-Contribution
FORMULA-Formula used
UNDEREX-Under examination at present

In relation to discovering how mechanistic the process of productivity measurement of partners is in each of the firms, the above information was collected. From TABLE 7.20 it is apparent that 20 firms do not utilise any form of measurement of partners' productivity to

determine income. The 19 firms identified as true sharing firms are all naturally part of this group. The 20th firm is that firm (Firm No.8), which was categorised as a productivity based firm, where the senior/ managing partner has exclusive authority to determine individual partners' profit shares - it is recalled that this authority has not been utilised and currently all partners of the firm earn the same profit share.

TABLE 7.20 also illustrates that 2 firms (both large incidentally) are currently examining moving from a true sharing model to one which incorporates partner productivity. This is indicative of potential problems that can confront a large firm relying upon such a sharing model, where agency problems are no longer suppressed effectively by firm culture and self-enforced monitoring and incentives.

(I) Firms whose income division method is productivity based - further breakdown:

9 firms (6 large and 3 small/ medium) indicated that the measurement of partner productivity taken within the firm was 'contribution'. Another large firm which disclosed the use of this measure, also disclosed it used a formula to calculate individual partners' 'contribution'.

Another 2 large firms revealed that an attempt was made to measure partner productivity and distribute income to partners on that basis - one of these firms disclosing that measurement of productivity was conducted in a crude and ad-hoc manner. The remaining small firm of the total group of 13 firms, indicated it attempted to measure partner productivity utilising a formula constructed to do so.

Again, evidence is presented above which confirms that measurement of productivity within firms to create income differentials is subjectively and often unsystematically accomplished, lending support to Hypothesis 2.

3.18 The formal time recording of hours spent on client business:

(TABLE 7.21)

Firm No	BILLING	MANAG	TARGET	TIMINC	BUDGET
10,13,14,15,16 (5 Firms=15.2%)	Yes	No	No	No	No
1,2,3,4,6,7,12,19,21,22,24,25, 30,31,33 (15 Firms=45.5%)	Yes	Yes	No	No	No
9,11,20,26,27 (5 Firms=15.2%)	Yes	Yes	No	No	Yes
29 (1 Firm=3.0%)	Yes	Yes	No	Yes	No
5,17,28 (3 Firms=9.1%)	Yes	Yes	Yes	No	No
23,32 (2 Firms=6.1%)	Yes	Yes	Yes	No	Yes
8,18 (2 Firms=6.1%)	No	No	No	No	No
TOTAL FIRMS	31	26	5	2	7
%age FIRMS	93.9	78.8	15.2	6.0	21.2

Description of variables:
BILLING-Time recorded for billing purposes
MANAG-Time recording for management purposes
TARGET-Fee income/ time billing targets
TIMINC-Time spent is direct determinant of partner income
BUDGET-Partners have time/ fee income budgets

Formal time recording of hours spent on client business was, as expected, fairly widespread throughout the sample, with only 2 firms indicating that this was not recorded. 1 of these firms was large and utilised a true sharing bargain - this type of sharing model arguably renders time recording, at least as a check on partner productivity, less important since levels of trust between partners not to shirk must be high for a true sharing model to survive.

The other firm in which there was no formal time recording, was small and utilised a productivity model (again this was the firm in which the senior/ managing partner has exclusive authority to determine partners' relative profit shares but where partners at present earned identical profit shares). This firms' organisational structure was atypical and exceptional in many respects, defying logical explanation across many of its dimensions.

A total of 5 firms (all small) used time recording for billing purposes only. Of these firms 3 employed sharing models and 2 employed productivity models. In small/ medium firms, regardless of type of sharing/ productivity model, time recording for management and monitoring purposes is arguably less important than in large firms - time spent by partners is more easily identified and attributed to individuals and mutual monitoring is strong.

A total of 26 firms, 12 small/ medium and 14 large firms, used time recording both for the purposes of billing clients and management purposes. 15 of these firms used true sharing models, and 11 utilised productivity based systems.

The first main category that can be identified, as a subset of this group of 26 firms, is that group of 15 firms (7 small/ medium and 8 large) which indicate only they use time recording for both of the aforementioned purposes. Of these firms, 8 employ true sharing models and 7 employ productivity models - time recording can be viewed as having an equally high incidence in both types of sample firms.

Given its overwhelming presence in firms of both types of partnership income division, time recording can be viewed as desirable. In true sharing firms, time recording can simply reinforce mutual and self-enforced monitoring, where it is known by partners that such information is being constantly collected, regardless of whether it is actually used or not. It was indicated by many firms that while time information was collected for management purposes, it was seldom used. However, it remains perceived as a potential weapon which could be brought in to stop a shirking problem. In productivity based systems, shirking is expected to be less of a potential problem. Time recording in that respect does not have to perform a monitoring function, but will still be desirable feature of the firm to help evaluate partners' relative 'contribution', where time spent attending to clients is likely to be an important constituent of such a productivity measure.

In 5 firms (3 large and 2 small/ medium) it was also indicated that, in addition to time recording for both purposes, partners have their own time/ fee income budgets. 4 of these firms utilised a true sharing based model and 1, a productivity model.

In one large firm employing a productivity approach, time spent by a partner attending to client business was disclosed as a direct determinant of a partner's income share. 3 firms (2 small sharing based and 1 large productivity based firm) indicated that, in addition to time recording for billing and management purposes, fee income/ billing targets were used.

The remaining 2 firms (both large but one of each income division type), in addition to time recording for management and billing purposes, also employed fee income/ billing targets and partner time/ fee income budgets.

3.18 The formal requirement for partners to spend at least a set minimum time on client business:

(TABLE 7.22)

Firm No	MINSET	NORMREC	CONBUDG	DEPTBUDG
1,2,7,8,10,13,17,18,21,25,29,30 (12 Firms=36.4%)	No	No	No	No
9,11,20,24,26,27,28,32 (8 Firms=24.2%)	No	No	Yes	No
5 (1 Firm=3.0%)	No	No	Yes	Yes
6,12,14,15,16,19,31,33 (8 Firms=24.2%)	No	Yes	No	No
23 (1 Firm=3.0%)	No	Yes	Yes	No
4 (1 Firm=3.0%)	No	Yes	Yes	Yes
3 (1 Firm=3.0%)	Yes	No	No	No
22 (1 Firm=3.0%)	Yes	Yes	No	No
TOTAL FIRMS	2	11	11	2
%age FIRMS	6.1	33.3	33.3	6.1

Description of variables:
MINSET-Minimum hours to be spent on client business set in contract
NORMREC-No minimum set but norm recognised
CONBUDG-Number of hours spent on client business is consistent with individual partner budgets
DEPTBUDG-Number of hours spent on client business is consistent with individual department budgets

In only 2 firms (1 small productivity based firm and 1 large true sharing based firm) was there a formal minimum set in partners' contracts relating to the amount of time which had to be spent attending to client business. Within this large firm a norm above this minimum was recognised in terms of time expected to be spent on client business.

In a total of 11 firms (including the large firm above) it was held to be the case that a norm was recognised and expected. Of these 11 firms, 3 were small true sharing based firms, 1 was a large true sharing based firm, 3 were small productivity based firms and 4 were large productivity based firms.

In 2 of above 11 firms (1 large sharing based firm and 1 small/ medium productivity based firm) time spent on client business was also viewed as consistent with individual partners' budgets. In the large firm, time spent on client business was consistent with departmental budgets.

Of those 21 firms in which neither a minimum was set, nor a norm was recognised, the following patterns were observed between respondents. 9 small firms and 5 large firms employed true sharing based models, and 2 small firms and 5 large firms utilised productivity based models of income division.

12 firms (6 small and 1 large true sharing based, and 1 small and 4 large productivity based) were members of the group which revealed no information in the above table, other than the fact that they set no formal minimum time to be spent attending to client business.

8 firms (2 small and 4 large true sharing based, and 2 large productivity based) formed the next grouping. These firms all disclosed that time spent on client business was only contingent upon the need to satisfy the requirements of individual partner budgets. Another small sharing based firm, in addition to the information disclosed by these last 8 firms, also revealed that the time spent on client business was related also to departmental budgets.

3.19 The enforcement of time spent attending to client business:

(TABLE 7.23)

Firm No	PEER	FEETARG	EXPBUDG	TIMEREC
8,10,16,17,18 (5 Firms=15.2%)	No	No	No	No
12,14,15,24 (4 Firms=12.1%)	Yes	No	No	No
4 (1 Firm=3.0%)	No	Yes	No	No
11 (1 Firm=3.0%)	No	No	Yes	No
1,2,3,5,6,7,13,30,33 (9 Firms=27.3%)	No	No	No	Yes
9,19,21,22,25,29,31 (7 Firms=21.2%)	Yes	No	No	Yes
23,32 (2 Firms=6.1%)	Yes	Yes	Yes	Yes
20,26,27 (3 Firms=9.1%)	No	No	Yes	Yes
28 (1 Firm=3.0%)	No	Yes	No	Yes
TOTAL FIRMS	13	4	6	22
%age FIRMS	39.4	12.1	18.2	66.7

Description of variables:
PEER-Peer pressure
FEETARG-Fee income targets
EXPBUDG-Expenses budgets
TIMEREC-Time recording

The previous table examined the factors firms believed to establish a minimum, or in the absence of a formal minimum, a norm, in relation to time spent by partners on client business. TABLE 7.23, above, presents mechanisms within firms which act to enforce any stated formal minimum, or established norm, in relation to time spent on client business.

5 of the respondents here did not indicate the existence of any enforcement mechanism to ensure partners spent time on client business, 4 of them being true sharing firms. It is expected that in pure sharing firms, partners are strongly relied on to self-motivate as this is a necessary condition for the survival of a sharing based system, thereby negating the need for formal constraints/ enforcement mechanisms. 4 firms mentioned only that peer group pressure was the enforcement mechanism to ensure partners spent time on client business. 2 of these firms were again true sharing based firms and the other 2, although being productivity based,

were small/ medium firms where mutual monitoring is expected to be strong due to small group practice. 2 firms, 1 large productivity-based and 1 small sharing based, saw fee income targets and expenses budgets, respectively, as coercing partners into spending time on client business.

Of the 31 firms which indicated in TABLE 7.21 time recording was used either for billing, or management purposes (or both), 22 revealed they thought this enforced either a minimum, or norm, in relation to time spent on client business. In 9 of these firms (7 of which were true sharing based), this was perceived to be the only enforcement mechanism in the firm which ensured partners spent time on client business. This time recording constraint was seen as successfully operating regardless of its formality and its use/ non-use as a management tool aimed at checking on shirking. Time recording and peer group pressure was seen in combination by a further 7 firms to act as the enforcement mechanism to ensure partners spent time on client business - only 2 of these firms relied on a true sharing model, whereas 5 relied on a productivity based system. 5 of the 7 firms were also large firms, where mutual monitoring could be expected to be less effective and weaker due to increased partner numbers.

In 2 large firms, 1 from each category of income division type, a combination of time recording, fee income targets, expenses budgets and peer group pressure was disclosed as enforcing any formal minimum or established norm in relation to time spent on client business. The resultant enforcement mechanism appears to be fairly strong in these 2 firms since they rely on 3 mechanisms in combination to bolster peer group monitoring - which could be expected to be weaker in such firms due to large practice size. 3 large firms (2 true sharing based and 1 productivity based) indicated they believed the combination of time recording and fee income targets would act as the enforcement mechanism. Again in these firms, it is demonstrated that reliance on more formal constraints is preferred - there was no mention of the existence of peer group pressure by these firms. This is indicative of low levels of peer group monitoring existing in these 3 large firms, resulting in the requirement to rely on more formal time enforcement mechanisms. The final firm, a large productivity based firm, again fails to mention peer group pressure as being relevant here, preferring instead to mention the combined enforcement role of time recording and fee income targets.

Of the firms that mention peer group pressure and its importance as a constraint in the firm, 5 are small, 3 are large sharing based firms, and 5 are large productivity based firms which also rely on either time recording, expenses budgets or fee income targets (or all 3). This is an intuitively pleasing result since it indicates those firms where peer group pressure could be expected to be stronger and those where it could be expected to be weaker, thus requiring bolstering by more formal constraints.

It is apparent from TABLE 7.23 that incentives facing lawyers within the firm are typically fairly weak and indirect, offering support to Hypothesis 4. This states that lawyers will respond to incentives other than monetary ones in their decision to undertake certain activities within the firm. From TABLE 7.21 it will be recalled that in only 1 firm is it the case that partners are directly compensated for time spent attending to client business. In 13 firms, compensation is at best linked indirectly to time spent on client business through some form of productivity based income division system. In such systems, time spent attending to client business is typically but one of many components of the productivity measure used to assess partners' relative profit shares. In the 19 true sharing based firms, partners are simply expected to spend time on client business and appear generally willing to do so as the firms mutual monitoring and self-enforcing incentive structures are strong and effective.

3.20 Incentives encouraging partners to spend more than minimum time on client business:

(TABLE 7.24)

Firm No	DIRCOMP	PROFIT	NECWORK	COMMONIT	PROMHOPE	CONTWORK	LOYFIRM	INCINCOM	RETAINC	PRESTSUC	ENHANCE	CONSIDER	OTHER9
2,17(2 Firms=6.1%)	No	No	Yes	No	No	Yes	Yes	No	No	No	No	No	No
8,24(2 Firms=6.1%)	No	No	No	No	No	No	Yes	No	No	No	No	No	No
25 (1 Firm=3.0%)	No	No	No	No	Yes	No	No	No	No	No	Yes	No	No
33 (1 Firm=3.0%)	No	No	No	Yes	No	No	No	No	No	No	No	No	No
23 (1 Firm=3.0%)	No	No	No	Yes	No	No	Yes	No	No	No	No	No	No
18 (1 Firm=3.0%)	No	No	No	Yes	No	No	Yes	No	Yes	No	No	No	No
1 (1 Firm=3.0%)	No	No	Yes	No	No	No	No	No	No	No	No	No	No
7 (1 Firm=3.0%)	No	No	Yes	No	No	Yes	No	No	No	No	No	Yes	No
6 (1 Firm=3.0%)	No	No	Yes	No	No	Yes	No	No	Yes	No	No	No	No
10 (1 Firm=3.0%)	No	No	Yes	No	Yes	Yes	No	No	No	No	No	No	No
14 (1 Firm=3.0%)	No	No	Yes	Yes	No	No	No	Yes	No	No	Yes	No	No
11 (1 Firm=3.0%)	No	Yes	No	No	No	No	No	No	No	No	No	No	No
3 (1 Firm=3.0%)	No	Yes	No	No	No	No	No	Yes	No	No	Yes	No	No
5 (1 Firm=3.0%)	No	Yes	No	No	No	No	No	Yes	Yes	No	No	No	No
16 (1 Firm=3.0%)	No	Yes	No	No	No	No	Yes	No	No	No	No	No	No
27 (1 Firm=3.0%)	No	Yes	No	No	No	No	Yes	No	No	No	No	Yes	No
32 (1 Firm=3.0%)	No	Yes	No	No	No	No	Yes	No	No	Yes	No	No	No
20 (1 Firm=3.0%)	No	Yes	No	No	No	No	Yes	Yes	No	No	No	No	No
22 (1 Firm=3.0%)	No	Yes	No	No	No	No	Yes	Yes	No	No	No	Yes	No
15 (1 Firm=3.0%)	No	Yes	No	No	No	Yes	Yes	No	No	No	Yes	No	No
30 (1 Firm=3.0%)	No	Yes	No	No	Yes	No	No	No	No	No	No	No	No
28 (1 Firm=3.0%)	No	Yes	No	No	Yes	No	Yes	Yes	No	No	No	No	No
26 (1 Firm=3.0%)	No	Yes	No	Yes	No	No	No	Yes	No	No	No	No	No
31 (1 Firm=3.0%)	No	Yes	No	Yes	Yes	No	No	No	No	No	Yes	No	No
21 (1 Firm=3.0%)	No	Yes	No	Yes	Yes	No	Yes	Yes	No	No	Yes	No	No
13 (1 Firm=3.0%)	No	Yes	Yes	No	No	Yes	No	Yes	No	No	No	No	No
12 (1 Firm=3.0%)	No	Yes	Yes	No	No	Yes	Yes	Yes	Yes	No	No	Yes	No
9 (1 Firm=3.0%)	No	Yes	Yes	No	No	Yes	Yes	Yes	Yes	Yes	No	No	No
4 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	No	Yes	Yes	No	Yes	Yes	No	No
19 (1 Firm=3.0%)	No	Yes	Yes	Yes	Yes	No	Yes	Yes	No	No	Yes	No	No
29 (1 Firm=3.0%)	Yes	Yes	No	No	No	No	Yes	Yes	Yes	No	Yes	No	No
TOTAL FIRMS	1	20	12	8	8	9	19	14	6	3	9	4	0
%age FIRMS	3.0	60.6	36.4	24.2	24.2	27.2	57.6	42.4	18.2	9.1	27.2	12.1	0

Description of variables:
DIRCOMP-Direct compensation for time spent on client business
PROFIT-Profit motive
NECWORK-Necessity when working in law
COMMONIT-Committees monitor time spent
PROMHOPE-Hope of promotion
CONTWORK-Control personal workload
LOYFIRM-Loyalty to the firm
INCINCOM-Increase personal income
RETAINC-Retain and increase client base
PRESTSUC-Prestige and success
ENHANCE-Enhance contribution
CONSIDER-Considering new sharing model at present
OTHER9-Other

The formality of incentives within the firm which operate to encourage partners to spend

more than a minimum on client business, are now examined in this section. In view of the diversity of sample firms' responses in this section, firms are categorised as follows to facilitate ease of analysis:

(I) Firms in which there is a direct monetary incentive to spend more than a minimum of time on client business - further breakdown:

This first group enjoys only 1 inhabitant (Firm No.29) - that being the aforementioned firm in which partners are directly compensated for time spent on client business. This direct incentive is a result of the formality and mechanistic nature of the productivity based income division model used by this large exceptional firm. Direct incentives are thus very rare among firms of this sample, indicating that firms generally rely on indirect incentives.

(II) Indirect monetary incentives perceived by partners to encourage them to spend more than a minimum of time on client business - further breakdown:

In this firm grouping the following indirect monetary incentives are examined; 1) Profit motive, 2) Committees monitoring time spent, 3) Hope of promotion, 4) Increase personal income and 5) Enhance contribution.

20 firms noted a profit motive, 14 disclosed a desire to increase personal income, 8 noted that committees monitored time spent, 8 indicated hope of promotion, and 9 firms recognised a desire to enhance 'contribution'. All of these were viewed as indirect incentives which are, to a greater or lesser extent, linked in some way to increased personal or firm income.

(III) Indirect non-monetary incentives perceived by partners to encourage them to spend more than a minimum of time on client business - further breakdown:

In this grouping the following indirect non-monetary incentives are examined; 1) Necessity of work, 2) Control workload, 3) Loyalty to the firm and other partners, 4) Retain current clients and increase client base, 5) Prestige and perceived success of working for current firm. These incentives are not strongly linked directly with increasing either personal, or total firm income.

In this group, 12 firms noted the necessity of spending long hours attending to client business in the legal profession as being a characteristic feature of being a lawyer. 9 firms indicated the desire of partners to control their personal workloads, and 19 firms noted loyalty to the firm and other partners, as providing an incentive to spend time on client business. Finally, 6 firms recognised a desire by partners to retain clients and increase the current client base, and 3 viewed the personal prestige and success of being a partner in that firm, as creating incentives for partners to spend more than the minimum required time on client business.

4 firms further disclosed that they were currently considering a new sharing model, presumably because they felt that the existing mechanisms were failing to provide partners with sufficient incentive to spend more time than a minimum attending to client business - all of these firms were true sharing based firms.

(IV) Firms who rely exclusively upon indirect non-monetary incentives - further breakdown:

Overall, 7 firms relied exclusively on indirect non-monetary incentives to encourage partners to spend more than a minimum of time attending to client business. These firms (Firm Nos. 1,2,6,7,8,17 & 24), in all but one case used true sharing based income distribution methods. The one productivity based small firm again is the firm where the managing partner has exclusive authority to determine partners respective profit shares, but at present all partners earn the same share of profits. For the purposes of examining the current segment of the incentive structure under observation, this firm essentially operates as a true sharing partnership. This firm disclosed that partners loyalty to each other and to the firm, provided sufficient incentive to spend more than a minimum time attending to client business.

Essentially all of the firms relying exclusively on indirect non-monetary incentives are true sharing based firms. This result confirms the intuitive proposition that firms where these types of incentives are likely to be reliable in encouraging partners to spend more than a minimum time on client business, will be sharing oriented - where mutual monitoring and self-enforcement of incentives are typically strong.

Where there is reliance upon indirect incentives, there is a property rights problem since increased effort by one partner not only benefits that partner, but also his colleagues. As a result of this appropriability problem, the partner will receive a disproportionately small return from the total benefits from his increased effort. This is not a problem if all partners of the firm do this at some point since costs and benefits will be shared in the longer term.

In an organisation where sharing is a primary feature, such weakly defined incentives can be expected to be sufficient to motivate individuals to behave in a manner in which personal benefit is not always a prime consideration. This is the essence of true sharing !

(V) Firms who rely exclusively upon indirect monetary incentives - further breakdown:

7 firms (Firm Nos. 3,11,25,26,30,31 & 33) indicated they relied exclusively upon indirect monetary incentives to encourage partners to spend more than a minimum time on client business. 5 of these 7 firms relied upon productivity based income division models, with the remaining 2 relying on a true sharing based system. Of these 2 true sharing based firms, 1

was large, indicating that mutual monitoring and self-enforcement of incentives may be unreliable in large firms, and 1 was small, simply indicating that the desire to increase firm profits was the sole motivation of the partner.

(VI) Firms who rely on both indirect monetary and non-monetary incentives - further breakdown:

Of the 18 remaining firms, 7 were productivity based firms and 11 were true sharing based firms. Of the true sharing based firms, 6 were small/ medium and 5 were large, and of the productivity based firms, 2 were small/ medium and 5 were large. In these firms, it is generally perceived that the revealed incentive structures are required to encourage partners to spend more than a *minimum* of time attending to client business. In these firms, bolstering of indirect non-monetary incentives with indirect monetary incentives is required as it is perceived that non-monetary ones would fail to provide sufficient incentive on their own.

It is apparent from the above table, and from previous tables, that the law firm typically places a fair degree of reliance on the lawyers' internal monitor/ conscience, combined with peer group pressure to provide sufficient incentive to engage in non-directly compensated activities within the firm. It is also apparent that the culture of the firm is sufficiently strong in certain firms to enable them to rely exclusively on indirect non-monetary incentives. Such firms (and many other firms), rely greatly on peer group pressure to encourage mutual monitoring between partners and loyalty of partners to the firm and colleagues, and the like, to provide a large part (if not all) of the incentive structure of the firm. It is, therefore, concluded that in the typical law firm, the lawyer's internal monitor and the culture of the firm is strong enough to obviate the provision of specific incentives for lawyers to engage in many activities within the firm. This supports Hypothesis 5, which states this will be the case.

3.21 The likely success of grabbing using a threat of leaving as bargaining chip:

(TABLE 7.25)

Firm No	MORE SUC	LESS SUC	NOT WAY	PTRN OTQA	NEVE RHAD	DEPI NDIV	ADVA NCE	PROB FUT
6,16,18,22,24,27,29,32 (8 Firms=24.2%)	No	No	Yes	No	No	No	No	No
2,5,13,23,33 (5 Firms=15.2%)	No	No	Yes	No	No	No	Yes	No
25,31 (2 Firms=6.1%)	No	No	Yes	No	No	Yes	No	No
4 (1 Firm=3.0%)	No	No	Yes	No	No	No	No	Yes
28 (1 Firm=3.0%)	No	No	No	No	Yes	Yes	No	No
10 (1 Firm=3.0%)	No	No	No	No	Yes	Yes	No	Yes
19,21,26 (3 Firms=9.1%)	No	No	No	No	No	Yes	No	No
8 (1 Firm=3.0%)	No	No	No	Yes	Yes	Yes	Yes	No
30 (1 Firm=3.0%)	No	Yes	No	No	No	No	No	No
1,14,17 (3 Firms=9.1%)	No	Yes	Yes	No	No	No	No	No
9,11,20 (3 Firms=9.1%)	No	Yes	Yes	No	Yes	No	No	No
15 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	No	Yes	No
3 (1 Firm=3.0%)	No	Yes	Yes	Yes	No	No	No	No
7 (1 Firm=3.0%)	Yes	No	No	No	No	Yes	No	No
12 (1 Firm=3.0%)	Yes	No	No	No	No	Yes	No	Yes
TOTAL FIRMS	2	9	24	2	7	10	7	3
%age FIRMS	6.1	27.2	72.7	6.1	21.2	30.3	21.2	9.1

Description of variables:
MORESUC-Grabbing more successful if threat to leave firm
LESSSUC-Grabbing less successful if threat to leave firm

NOTWAY-Not done this way
PTRNOTQA-May work for a partner but not a QA
NEVERHAD-We have never had the situation arising before
DEPINDIV-Depends on who it is that is grabbing/ threatening to leave
ADVANCE-Income shares are agreed in advance so cannot grab
PROBFUT-May become more of a problem in the future

In relation to the situation of a partner threatening to leave the firm, and using this as a hostage to grab a larger share of income, the information contained in TABLE 7.25 is presented for analysis.

The most significant fact here is that 24 of the 33 firms indicated that this was just simply not a situation which would arise within their partnerships.

In only 2 firms was it indicated that using the threat to leave would be likely to render a partner's attempt to grab a larger share of firm profits more successful. Both of these firms indicated that it would depend very much on the individual in question, with one firm additionally disclosing that this type of problem may occur with increasing frequency in future. Strangely, both of these firms currently employed true sharing based income division methods - such grabbing would be largely inviable as partner shares are mutually agreed in advance.

Of those 9 firms that indicated that using a threat of leaving to grab a larger share of firm profits, would be likely to render this attempt less successful, 4 were productivity based firms and 5 were true sharing based. All but 1 of these firms indicated that this was simply not the manner in which such things happened within their firms. This firm indicated no information other than the fact that the attempt would be likely to be less successful. 4 firms also disclosed that they had never experienced such a situation as yet, with 1 additionally indicating that such an attempt would be unviable as shares are pre-agreed in advance. The final firm disclosed that while threatening to leave would be likely to render a claim for increased profit shares, such a claim may work for a partner in exceptional cases but would definitely not work for a QA.

22 firms (12 sharing based firms and 10 productivity based firms) indicated that threatening to leave would neither increase or decrease chances of grabbing being successful. 16 of these 22 firms indicated this was simply not the manner in which things were done, 5 of whom indicated that shares were agreed in advance, rendering such behaviour inviable. 2 productivity based firms disclosed the success or otherwise of such behaviour would depend on the individual in question. The last of these 16 firms merely added that this behaviour may become more prevalent and cause problems in future.

All remaining 6 of the initial 22 firms, indicated that the success or otherwise of such an act would depend on the individual concerned. 3 firms disclosed that they had never as yet

encountered such a situation, 1 of them adding that this may become more of a problem in the future, and another adding that such an attempt may work for a partner but not for a QA.

It has been previously demonstrated that lawyers within the firm are likely to typically exhibit a low tendency to shirk. It is apparent from the information contained in TABLE 7.25 that the strength of the lawyer's internal monitor is likely also to result in a low incidence of grabbing (and threatening to leave to facilitate grabbing) in law firms. This information affirms Hypothesis 7, which states that the lawyers internal monitor will typically be strong, resulting in a low tendency to shirk, grab and leave.

3.22 Individual partner compensation for time spent on non-client billable activities:

(TABLE 7.26)

Firm No	NEWCLI	NONBILL	SUPTRAN	MANADMIN	NODIRCOM	MAYCHANG
1,2,3,4,5,6,8,9,10,11,13,						
14,15,16,17,18,19,20,21,						
23,24,25,26,28,30,31,32,						
33 (28 Firms=84.8%)	No	No	No	No	Yes	No
7,12,22,27 (4 Firms=12.2%)	No	No	No	No	Yes	Yes
29 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	No
TOTAL FIRMS	1	1	1	1	32	4
%age FIRMS	3.0	3.0	3.0	3.0	97.0	12.2

Description of variables:
NEWCLI-Compensation for attraction of new clients
NONBILL-Compensation for non-billable client attention
SUPTRAN-Compensation for supervision and training of staff
MANADMIN-Compensation for management and administration
NODIRCOM-No direct compensation for such activities
MAYCHANG-Compensation system may change in the future to accommodate such activities

In relation to activities engaged in by partners (other than client billable ones), the information contained in TABLE 7.26 above was gathered in relation to compensation.

It is immediately evident that in all but one of the firms, there was no direct compensation for partners spending time on activities other than those which were client billable. In this exceptional firm, partners received direct compensation for time spent on attraction of new clients, non-billable client attention, supervision and training of staff, and time spent on management and administration. In 4 of the firms it was indicated that the compensation system may change in the future to accommodate partner compensation for such activities. All 4 of these firms currently employed a true sharing approach to income division.

In the remaining 28 firms there was no compensation for time spent on these activities. 15 of these firms were true sharing based firms who simply expected partners to engage in such activities (and whose partners expected to do so). In such firms reliance is placed upon partners' internal monitors which, in combination with peer group pressure, should jointly coerce partners into participating in these activities without direct or indirect compensation. In the remaining 13 firms productivity systems operate and consequently, such activities should be attractive for partners to engage in.

Hence, in general, the typical law firm does not provide direct incentives for partners to engage in such activities, reaffirming Hypothesis 6. This would suggest that either indirect incentives are sufficient, or that such activities are functionally delegated to individuals. Initially, indirect incentives will be examined in the following text.

(I) Non-monetary incentives for partners to engage in non-client billable activities:

(TABLE 7.27)

Firm No	REFCONTR	FLAIR	FIRMGOOD	NECESS	DELEG	OTHER10
33 (1 Firm=3.0%)	No	No	No	No	Yes	No
9 (1 Firm=3.0%)	No	No	No	Yes	Yes	No
8,32 (2 Firms=6.1%)	No	No	No	Yes	No	No
22,27 (2 Firms=6.1%)	No	No	Yes	No	No	No
2,6,13,17,18,24 (6 Firms=18.2%)	No	No	Yes	Yes	No	No
5,12 (2 Firms=6.1%)	No	No	Yes	Yes	Yes	No
21,23,25,26,31 (5 Firms=15.2%)	Yes	No	No	No	No	No
19 (1 Firm=3.0%)	Yes	No	No	No	Yes	No
15 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	No
4,28 (2 Firms=6.1%)	Yes	No	Yes	No	No	No
3,14 (2 Firms=6.1%)	Yes	No	Yes	Yes	No	No
1,7,10,16 (4 Firms=12.2%)	No	Yes	Yes	Yes	No	No
30 (1 Firm=3.0%)	No	Yes	Yes	No	No	No
11 (1 Firm=3.0%)	No	Yes	Yes	No	Yes	No
20 (1 Firm=3.0%)	No	Yes	No	No	No	No
29 (1 Firm=3.0%)	M	M	M	M	M	M
TOTAL FIRMS	11	7	20	18	7	0
%age FIRMS	33.3	21.2	60.6	54.5	21.2	0

(M-Missing)

Description of variables:
REFCONTR-Reflected indirectly in contribution
FLAIR-Some partners demonstrate a flair for them so specialise in them
FIRMGOOD-Done for the good of the firm
NECESS-Done out of necessity
DELEG-Delegated by partners committee/ meeting
OTHER10-Other

The firm which provided no information here is, of course, the firm that used direct monetary incentives to compensate partners for engaging in these activities.

11 firms (all of whom employed a productivity based model) indicated that partners engaging in such activities would have this reflected in their assessed 'contribution'. Within this group of firms, 4 firms noted that partners engaged in such activities for the good of the firm, 3 noted that they were engaged in out of necessity, and 2 noted that certain tasks of this sort were engaged in primarily because they were delegated to particular persons.

Of the remaining 21 firms (15 true sharing based and 6 productivity based) 7 indicated that certain individuals demonstrated a flair for certain activities, therefore, gravitated towards them, 16 noted that such activities were engaged in for the good of the firm, 15 disclosed that they were done out of necessity, and 5 firms noted that such tasks were engaged in because they were delegated to certain individuals within the firm.

Overall, there existed a delegation procedure in 7 of the firms which essentially obviated much of the problem of providing sufficient direct and indirect incentives to engage in these

activities. The extent of delegation in these activities across firms is examined in greater detail below. With a view to providing evidence in support of Hypothesis 6, which states that the influence of the lawyers internal monitor, and the culture of the firm, will weaken in larger firms requiring more formal constraints and incentives for partners of the firm, it is necessary to examine the following;

1. Whether formal incentives more commonly exist in large firms and,
2. Whether greater functionalisation occurs in large firms.

3.23 Functional responsibility in the firm for non-client billable activities:

(TABLE 7.28)

Firm No	PARTRESP	PTRTRAIN	PTRMAN	PTRNOBIL	PTRNEWCL	DEPTRESP	DEPTTRAI	DEPTMAN	DEPTNOBI	DEPTNEWC	COMMRESP	COMMTRAI	COMMMAN	COMMNOBI	COMNEWCL	NONRESP	NONTRAIN	NONMAN	NONNOBIL	NONNEWCL	DOWNLOAD
13	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No
6	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	Yes	No	No	No
2	No	No	No	No	No	No	No	No	No	No	Yes	Yes	No	No	No	No	No	Yes	No	No	No
15	No	No	No	No	No	No	Yes	No	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No
4	No	No	No	Yes	No	No	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	Yes
1,12,19,20 (4 Firms=12.2%)	No	No	Yes	No	No	No	No	No	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No
7,14,33 (3 Firms=9.1%)	No	No	Yes	No	No	No	No	No	No	No	No	Yes	Yes	No	No	No	No	Yes	No	No	No
5,16 (2 Firms=6.1%)	No	No	Yes	No	No	No	Yes	No	No	No	No	No	No	No	No	No	No	No	No	No	No
8	No	No	Yes	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No
9	No	No	Yes	No	No	No	No	No	No	No	No	No	No	No	No	No	No	Yes	No	No	No
10	No	No	Yes	No	No	No	No	No	No	No	No	Yes	No	No	No	No	No	No	No	No	No
31	No	No	Yes	No	No	No	No	No	No	No	Yes	Yes	No	No	No	No	Yes	Yes	No	No	No
18	No	No	Yes	No	No	No	No	Yes	No	No	No	No	No	No	No	No	Yes	Yes	No	No	No
27	No	No	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No	No	Yes	No	No	No
24	No	No	Yes	No	No	No	No	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No	No
11,32 (2 Firms=6.1%)	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No	No	No	No	No	No
21,25 (2 Firms=6.1%)	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No	No	Yes	No	No	No
17	No	Yes	Yes	No	No	No	No	No	No	No	No	No	No	No	No	No	No	Yes	No	No	No
3	No	Yes	Yes	No	No	No	No	No	No	No	No	No	Yes	No	No	No	No	No	No	No	No
20	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No	No	No	No	No	Yes
22	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No	Yes	Yes	No	No	No
29	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No
28	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	Yes	No	No	No
26	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No
23	No	Yes	Yes	Yes	Yes	No	Yes	Yes	No	No	No	Yes	Yes	No	No	No	No	No	No	No	No
TOTAL FIRMS	0	12	28	2	1	0	14	14	1	0	0	15	18	1	0	0	4	15	0	0	3
%age FIRMS	0	36.4	84.8	6.1	3.0	0	42.4	42.4	3.0	0	0	45.5	54.5	3.0	0	0	12.2	45.5	0	0	9.1

Description of variables:
PARTRESP-Individual partners specialise in all these activities
PTRTRAIN-Individual partners specialise in training
PTRMAN-Individual partners specialise in management
PTRNOBIL-Individual partners specialise in non-billable client attention
PTRNEWCL-Individual partners specialise in attraction of new clients
DEPTRESP-Departments specialise in all these activities
DEPTTRAI-Departments specialise in training
DEPTMAN-Departments specialise in management
DEPTNOBI-Departments specialise in non-billable client attention
DEPTNEWC-Departments specialise in attraction of new clients
COMMRESP-Committees specialise in all these activities
COMMTRAI-Committees specialise in training
COMMMAN-Committees specialise in management
COMMNOBI-Committees specialise in non-billable client attention
COMNEWCL-Committees specialise in new client attraction
NONRESP-Specialist non-partners responsible for all these activities
NONTRAIN-Specialist non-partners responsible for training
NONMAN-Specialist non-partners responsible for management
NONNOBIL-Specialist non-partners responsible for non-billable client attention
NONNEWCL-Specialist non-partners responsible for attraction of new clients
DOWNLOAD-Work downloaded onto QAs so that partners can concentrate on client care

In table 7.27; 7 firms indicated that delegation occurred in respect of certain non-billable

activities, and this was regarded as a reason why partners performed them irrespective of the existence of, or lack of, incentives to do so. This section aims to specifically examine the extent of delegation in all sample firms with a view to exposing the existence of functionalisation with respect to the following activities: 1) Training and supervision of staff, 2) management and administration, 3) non-billable client attention and, 4) attraction of new clients.

Delegation of these tasks to individual partners, departments within the firm, committees within the firm, and to non-partner specialists of the firm is examined, and as expected, firms generally exhibited unique methods of delegating and functionalising these tasks.

(I) Individual partner specialisations - further breakdown:

12 firms indicated that individual partners specialised in training and supervision within the firm, 8 of them large firms and 4 of them small/ medium firms. In all but 5 firms (4 small/ medium and 1 large) it was the case that individual partners specialised in management and administration of the firm. In 2 large firms, partners assumed specialist roles in non-billable client attention, with 1 of these firms also disclosing that partners (called rainmakers) specialised in attracting new clients.

In terms of functionalisation of these tasks using specialist partners, it is clear that there is a greater incidence of this in large firms than in small/ medium firms - providing support for Hypothesis 8, which states that the formality of formality of partner specialisations will be greater in large firms than it will be in small/ medium sized firms.

(II) Departmental specialisations - further breakdown:

14 firms disclosed that departments specialised in training and supervision, with training in some cases being done centrally from an inhouse training department. Of these 14 firms, 9 were large and 5 were small/ medium. A similar total number of firms disclosed that departments had management specialities where certain management functions were the responsibility of departments. In this case, 11 of the firms were large and 3 were small/ medium sized. One large firm indicated that departments had responsibility for non-client billable attention.

With reference to the functionalisation of such tasks through departments, it is apparent that again there is a higher incidence of this occurring in large rather than in small/ medium firms. In larger firms there is generally greater functionalisation through departments with responsibility for certain non-client billable activities resting with such departments.

(III) Committee specialisations - further breakdown:

15 firms disclosed that committees performed specific training and supervision functions with attendant responsibilities. 9 of these firms were large firms and 6 were small/ medium firms. A total of 18 firms indicated that committees were invested with management responsibilities and performed specific management and administration duties. Of these 18 firms, 10 were large and 8 were small/ medium. 1 large firm also indicated that committees had responsibilities for non-billable client attention.

Although less clearcut than it was for partner and departmental specialisations, committee specialisations in non-billable client activities enjoys more frequent occurrence in large than in small/ medium firms.

(IV) Non-partner specialisations - further breakdown:

Only 4 firms noted that non-partners performed specialist training and supervision functions within the firm. All of these firms were large firms. 15 firms disclosed that specialist non-partners performed specific management and administration functions within the firm. Of these firms, 8 were large firms and 7 were small/ medium.

In relation to specialist non-partners having responsibility for non-client billable activities, the situation is mixed. In relation to training, this is not a feature of any of the small/ medium firms in the sample. In relation to management and administration, this features only marginally more frequently in large firms than in small/ medium firms within the sample.

In summary, the existence of departments, committees and non-partner specialists to perform these functions could be construed as indicative of the failure of the organisation to provide partners with sufficient incentives to engage in such activities - undoubtedly there are also exists strong specialisation and efficiency/ effectiveness reasons for their existence.

In 3 firms, it was mentioned that work would be 'downloaded' to qualified assistants in order that the partners could concentrate on client care. This can be seen as a convenient strategy from the lawyer's point of view since he can concentrate on adding polish to the service, buy QAs time to perform the major elements on the service and sell it to the client at his (far higher) billing rate. From the client's point of view, it appears that he is receiving a very personal and partner intensive service.

3.24 The remuneration of partners for the attraction of new clients:

(TABLE 7.29)

Firm No	NEWCLI2	TIMEALSO
1,2,3,4,5,6,7,8,9,10,11,12,13,14,15,16,17,18,19, 20,21,22,23,24,25,26,27,28,30,31,32,33 (32 Firms=97.0%)	No	No
29 (1 Firm=3.0%)	Yes	No
TOTAL FIRMS	1	0
%age FIRMS	3.0	0

Description of variables:
NEWCLI2-Partners compensated for attraction of new clients
TIMEALSO-Partners compensated only if they spend time on client work for the new client

In all but one of the firms, partners received no direct compensation for attracting new clients to the firm. In the 1 firm where attraction of new clients did produce compensation for that partner, it was not the case that this compensation was contingent on that partner spending time on that client. It is suggested by Gilson and Mnookin (1984) that where partners are not compensated for attracting new clients they may under-invest their time in doing so [24]. They also contend that where partners do receive compensation merely for attracting the client, a perverse incentive can be created for partners simply to get as many clients through the door as possible regardless of the firm's ability to cope with them thereafter. Willingness of partners to pass clients between each other is examined below.

3.25 The passing of clients between partners of the firm:

(TABLE 7.30)

Firm No	PASSCLI	PASSWILL	PASSTYPE	CONTACT
18,22,31,33 (4 Firms=12.2%)	No	No	Yes	Yes
6 (1 Firm=3.0%)	No	No	Yes	No
25,30 (2 Firms=6.1%)	No	No	No	Yes
1,3,8,9,10,11,12,13,14,16,19,21,23,24, 26,27,28,29,32 (19 Firms=57.6%)	No	Yes	Yes	Yes
2,4,5,7,15,20 (6 Firms=18.2%)	No	Yes	Yes	No
17 (1 Firm=3.0%)	No	Yes	No	Yes
TOTAL FIRMS	0	26	30	26
%age FIRMS	0	78.8	90.9	78.8

Description of variables:
PASSCLI-Partners are compensated for passing clients on
PASSWILL-Partners are willing to pass clients on with no compensation
PASSTYPE-Partners must often pass clients since outwith speciality
CONTACT-Attracting partner is still contact on client file

None of the sample firms disclosed the existence of any form of partner compensation for passing clients on to their colleagues - this even being the case in the one firm which did compensate partners for attracting new clients. This firm did not view the potential perverse incentive problem which can be created to be a problem in its partnership.

26 firms claimed it to be normal for partners to be quite willing to pass clients to colleagues, as this was part of the general and accepted reciprocal nature of inter-partner relationships within the firm. 30 firms noted it to often be the case that partners required to pass clients between each other as services demanded by clients were outwith their own particular

speciality. 26 firms disclosed they operated a system whereby the partner introducing the client to the firm is noted as the contact on the clients file - thereby clients are attributable to partners.

Chapter Seven - Endnotes

1. See, Fama, E. and Jensen, M., Separation of Ownership from Control, *Journal of Law and Economics*, Vol.XXVI, 1983, pp.301-326, and also; Fama, E. and Jensen, M., Agency Problems and Residual Claims, *Journal of Law and Economics*, Vol.XXVI, 1983, pp.327-352.

2. See, Fama and Jensen (1983), *supra* Note 1.

3. See, Williamson, O.E., Organisational Form, Residual Claimants and Corporate Control, *Journal of Law and Economics*, Vol.XXVI, 1983.

4. See, Williamson (1983), *supra* Note 3.

5. See, Fama and Jensen (1983), *supra* Note 1.

6. See, Fama and Jensen (1983), *supra* Note 1.

7. See, Fama and Jensen (1983), *supra* Note 1.

8. See, Fama and Jensen (1983), *supra* Note 1.

9. See, Fama and Jensen (1983), *supra* Note 1.

10. See, Fama and Jensen (1983), *supra* Note 1.

11. Personal indemnity insurance could perhaps be expected to weaken incentives in the aforementioned direction. It must be stressed, however, that this will only

cover losses to clients and not losses to the value of human capital caused by incompetent or mal-practice.

12. See; Gilson, R.J. and Mnookin, R.H., Sharing Among the Human Capitalists: An Enquiry into the Corporate Law Firm and how Partners Split Profits, Stanford Law School Working Papers, Vol.37 No.16, 1984.

13. See; Gilson and Mnookin (1984), *supra* Note 12.

14. From the firm's perspective this appears to surmount the problem of wishing to offer a personal service without creating the risks associated with one lawyer becoming perceived by the client as worth following if he left the firm.

15. See; Gilson and Mnookin (1984), *supra* Note 12. at p.360.

16. See; Gilson and Mnookin (1984), *supra* Note 12.

17. See; Gilson and Mnookin (1984), *supra* Note 12.

18. See; Gilson and Mnookin (1984), *supra* Note 12.

See also; Rosen, S., The Market for Lawyers, Journal of Law and Economics, Vol.XXXV, October 1992. While Rosen does not tackle this specific issue head on, his analysis of lawyers earnings is nevertheless tangential to this issue albeit at the market rather than firm level. His analysis examines three main issues:

1. The determinants of average differences in income among occupations,

2. The structure of, and distribution of, relative incomes within occupations, and,

3. The mechanism of adjustment for earnings, entry and exit to changing market conditions in professional labour markets.

Analysis in this thesis is principally concerned with mechanisms existing at the level of the firm rather than at the level of the overall market.

19. See; Gilson and Mnookin (1984), *supra* Note 12.

20. See; Gilson and Mnookin (1984), *supra* Note 12.

21. See, Gilson and Mnookin (1984), *supra* Note 12.

22. See, Gilson and Mnookin (1984), *supra* Note 12.

23. See, Feinberg, R.M., Paralegals and Substitution Among Labour Inputs in the Law Firm, *Journal of Industrial Economics*, Vol.XXXVI No.1, 1984.

24. See, Gilson and Mnookin, 1984, *supra* Note 12.

-Chapter Eight-

Employment relationships between partners and qualified assistants in law firms - theoretical and empirical analysis:

Introduction:

This chapter will focus on relationships between partners and qualified assistants (QAs) of the law firm. In particular the precise and important screening role of partnership will be described.

Section One: Employment within the law firm:

Considerable information regarding participant labour units is necessary in order that individuals can be placed in different positions in any labour market. This is true in the case of both external labour markets, with lateral entry, and internal labour markets, characterised by promotional contests/ rank order tournaments [1].

It can be argued that promotion (and its attendant financial and non-pecuniary rewards) is likely to be a major motivating factor for individuals within any organisation. It is reasonable to expect well-motivated individuals to desire to outperform those within their peer group, thereby enhancing prospects of promotion.

1.1 Labour input categories within legal partnerships:

In the context of the law firm four major employment groups can be identified:

1. General staff, secretaries, etc.
2. Newly qualified trainee lawyers,
3. Qualified assistants (QAs),
4. Partners.

At lower ends of the organisational hierarchy, it is expected that the firm will rely almost exclusively hire labour it requires from the external labour market. This is likely to be the case for the general staff category and for recently qualified graduates who will be seconded straight from law school [2].

Further up the law firm hierarchy, at the level of qualified assistant and partner, it is likely that the story will be quite different. It is expected that the majority of qualified assistants

(QAs) will have been promoted to this level after serving their trainee-ship within the firm. Some, however, may have been hired from the external labour market to enter at QA level.

At the partner level, it is anticipated that, in all but exceptional cases, partners will appointed from within the firm from the pool of QAs who will have been with the firm for a number of years - promotional contest and tournament processes may be prevalent. It is likely, however, that given this broad picture, each firm will possess its own unique hiring strategies, depending on its size and specialism etc. The empirical analysis conducted later in this chapter aims to disclose these elements of similarity and diversity across cases.

Neoclassical theory of the labour market is incapable of explaining why certain transactions involving hiring of labour are removed from the market and take place within a hierarchical organisation. This is essentially due to the reliance of this theory on simplifying assumptions including; an equilibrium wage set in the market, homogeneity of labour inputs, complete mobility of labour (both occupational and geographical) and exogenous acquisition of skills.

Clearly, in the case of law firms (as with many other types of organisation) this picture is too restrictive and narrow - commonly observed features such as internalised labour market hiring via promotional contests and rank order tournament processes are ignored. Additionally, wages are determined, not solely in the external market, but also through rules and scales developed as an integral part of the process of hierarchical internal organisation.

1.2 Promotion contests and the nature of the information problem:

In any situation whereby an employer seeks a potential employee, both parties suffer from having small quantities of information or knowledge regarding each other's characteristics - a classic situation characterised by extreme information deficiency and high levels of uncertainty. This information is not costlessly or easily discovered or disclosed by either party. At the commencement of a contest between individuals for a position within a firm, neither the firm nor the candidates for the position know who is best suited to the vacancy due to information deficiency. Candidates compete for the position by the disclosure of information (skills, aptitudes etc.) to the hirer to demonstrate their suitability [3].

The individual is, therefore, likely to supply greater effort in which ever direction he perceives will best influence chances of selection. This effort will tend to be beyond that which is necessary for his present job in order to signal suitability for promotion.

1.3 Reducing information deficiency via signalling and information disclosure:

Market signals play a vital role in reducing information deficiency in this situation. Signalling theory provides insights here - the thrust of the argument being that potential employees will make investments in creating market signals which convey some information regarding their underlying traits and characteristics which are difficult to observe [4].

The applicability of this in the context of the law firm and its process to appoint new partners from its pool of internal QA candidates is clear - prospective partners (QAs) may during the process of an internal labour market/ rank order tournament, make signalling investments to attempt to become partners [5]. It is rational for the individual to make such investments where they are viewed as increasing promotion chances. Should the contestant perceive the contest to lack credibility, he will discount his chances of promotion and not undertake such investments - a contest must appear fair with a reasonable chance of payoff.

A fair contest and reasonable chance of payoff is required to provide the individual with incentives to disclose aptitudes and supply greater effort intensity. The employer will undertake to reward contest winners by promotion. The overall result in terms of productivity will be uncertain - there may simply have been a temporary (yet significant) gain in productivity during the period of the contest due to all participants enhancing their effort intensity to signal suitability. After the contest has been run, those who have been unsuccessful may simply let their productivity fall back to previous levels, or worse still lower levels, depending on how they react motivationally to rejection in the contest.

Continuing failure of an employee in an information revealing promotion game, may be perceived by that employee as opportunism on the part of the firm. In such a situation, the firm could be cynically perceived as attempting to trick employees into supplying greater effort on the strength of a promise of promotion that never materialises. Should this be perceived, individuals may discount the value of entering future contests, in a manner not unlike that outlined in Goldberg's Relational Exchange Framework, whereby deferred compensation was discounted under certain circumstances [6]. It must be pointed out here that the actual process to select successful candidates for promotion could even be randomly based, so long as candidates do not perceive (or discover) the final choice has been made on this basis. It is unlikely, however, that random selection will characterise many contests.

1.4 Problems of hiring labour in law firms:

Broadly speaking, the law firm will enter both inter-firm and intra-firm contests to hire labour. Prior to hiring from the external market, the law firm has to decide on the important characteristics it seeks in its new employees. These characteristics will be wide-ranging, some of which will be relatively easily identified or discovered, and others which will be difficult (at the extreme - impossible) to identify or discover. A major consideration for the law firm,

given its close- knit/ homogeneous nature, may be for instance, ability to fit in with existing team members and relationships established within the firm. At lower levels of the organisational hierarchy, this is likely to be less important and use of external labour hiring is unlikely to pose difficulties in assessment of labour suitability.

However, at higher organisational levels, a greater reliance on internal promotion, and the functioning of internal labour markets and contests, is likely to facilitate easier and more effective assessment of suitability [7]. In the case of the law firm the most important behavioural characteristic of those being considered for partnership is trust - ie. they must be trusted, in the absence of formal incentives and monitoring, to self-monitor, pull their weight in the partnership, and avoid acting wholly self-interestedly. While it is difficult in any situation for individuals to assess a person's trustworthiness and propensity to behave in these directions, it is far less difficult to do this, the longer is the period of observation of their characteristics. Hence, it is rational for partnerships to prefer to rely on internal assessment of its QAs for potential partner positions than external labour market transactions where the information deficiency is far greater.

To reduce problems of assessing heterogeneous labour units, the firm by using a promise of contingent financial and non-pecuniary rewards can create incentives for labour units to develop and reveal their talents - ie. provide incentives to engage in signalling. This naturally further complicates the allocation of costs and benefits between the firm and the employee of signalling and disclosing information and discovering and processing it to facilitate choice.

1.5 Hiring strategies and growth of the law firm:

The employment policies adopted by the firm essentially determine the growth pattern of the firm. It is perhaps the case that, due to the diverse hiring policies that will almost certainly exist, there may be a spectrum of aims, ranging from a desire for a quiet life through to desire for exceptional growth, within law firms. The firm could be expected to be subject to the process, whereby the larger the firm becomes, the faster it is able to grow through synergy [8]. Prospects and processes for the growth of the law firm and obstacles to its growth will be examined within the empirical study later in this chapter. Given the importance of the QA to partner transformation, it is this aspect of employment within the law firm which will be focused upon.

1.6 The importance of the relationship between the firm's qualified assistants and its partners - the USA system of 'up or out':

A recent paper by Gilson and Mnookin (1988), examines changes in the career patterns of qualified assistants in large USA corporate law firms, while Carmichael (1988) examines a tangentially similar situation concerning academics in universities [9]. While Carmichael, through examining the internal labour market process and the existence of tenure, argues tenure is necessary so that incumbents are willing to hire people who may actually transpire to be better than themselves, Gilson and Mnookin note that previously basically two categories of lawyer, namely partner and associate (qualified assistant) existed - this being a direct result of a promote or fire (up or out) system. They argue this system appears to be changing, whereby lawyers not promoted to partner positions are not fired but rather assigned to a new category. This has resulted in new levels of non-partner employee lawyers being created within the organisation. This internal organisational change poses two interesting questions:

1. Why did the old up or out system dominant for so long when it appears, on initial inspection, to be to the advantage of neither firm nor employee ?

2. What factors account for this sudden change in such a fundamental aspect of law firm organisation ?

The first question is interesting since, under an 'up or out' system, the firm is forced to fire individuals who, while making a valid contribution to the firm, are not thought to be suitable for promotion to partner. Additionally, the system denies an individual the choice of remaining within the firm and pursuing a career option other than as a partner [10]. Gilson and Mnookin (1988) address these two questions by examining the nature and function of the implicit contract which determines associate career patterns in large corporate law firms [11].

1.7 The nature of implicit contracts in the firm:

The requirement to emphasize unwritten or implicit contracts here can be seen to demonstrate the requirement for a contractual relations approach to organisations to embody such 'informal' relationships. Such an approach is often criticised for failing to recognise that important elements within an organisation are not subject to written contract. It is also the case that it is much easier, as Klein (1980) has argued, to assume rather than demonstrate the efficiency of the observed pattern of contractual relations within an organisation [12]. These two features offer support to the view that, without detailed empirical examination of actual organisations, a nexus of contracts view of organisations lacks positive predictive power.

Within the law firm, it is anticipated that the firm will wish to very carefully select, evaluate and retain good employees due to the high levels of human capital intensity which characterise the firm's input (and output). Gilson and Mnookin (1988) argue that the system aimed at achieving this and which has been dominant among corporate law firms in the USA has been the 'up-or-out' system [13]. Within this system, the associate progresses over a period of years towards some decision as to whether promotion to partner will occur or not. Gilson and Mnookin (1988) argue on first inspection this appears to work against the interests of both the firm and its pool of associates [14].

1.8 The firm's side of the problem:

From the firm's perspective, there is a problem of how to devise an efficient career pattern for employee lawyers who fail to make partnership but remain within the firm - a problem whose solution is sought within literature of labour economics.

Initially, the firm faces a problem of extreme information deficiency concerning its associate (QA) entrants. In particular, the firm is largely ignorant of many of the qualities though to be traditionally important in making the partnership decision, for instance; personal qualities such as cooperativeness, ability to gain respect of clients and colleagues, maturity etc. [15]. The firm responds to its uncertainty and information deficiency relating to associate lawyers, by operating an apprenticeship system for them covering the period between initial hiring and the decision of partnership. This period provides the associate with a forum from within which legal skills and personal characteristics can be developed effectively and personally demonstrated to the partnership decision making authority.

During this apprenticeship period, the associate is also provided with an incentive to invest in firm specific capital and bond himself to the firm, making himself more indispensable. The associate could hold the firm to ransom by threatening to exit, should returns to these firm specific investments fail to be shared in a more favourable manner which apportioned a greater share of the benefits towards the associate. The firm can attempt to defer compensation, by a promise of partnership. This can be regarded as a payment to those associates who successfully acquire firm specific capital - this will serve to largely constrain opportunistic behaviour on the part of associates.

The apprenticeship/ screening idea, operating in the pre-partner period after initial hiring, can thus be seen as a rational action on the part of the law firm prior to it requiring to make a decision on partnership. The firm's behaviour is, however, far less rational at the time of making the decision on partnership since;

1. Often more senior associates are a major source of income to the partnership.

2. In the period prior to any decision being made, the firm must have regarded its lawyers to be competent otherwise they would have been fired much earlier.

By using such a strict system, the firm appears to lose out on a substantial amount of potential income. The up-or-out system, therefore, seems difficult to reconcile - the firm appears to discard potential profits by not continuing to employ 'unsuccessful' associates in non-partner positions.

1.9 The associates side of the problem:

From the associate's viewpoint the situation is also puzzling. It could be expected that the greater is the individual's investment in difficult to diversify human capital, the stronger would be his risk aversion in relation to his human capital investment. Faced with the choice of a law firm which employs a system of up-or-out, or one which retains associates within the organisation in some non-partner capacity, it would appear more rational for the risk averse associate to shy away from the up-or-out system. This poses the question, why might would-be associates join or (worst still) prefer to join, a firm which only offered all or bust.

1.10 The Dual Uncertainty Framework:

Gilson and Mnookin (1988) offer a framework to unravel this puzzle, based on what they call 'dual uncertainty' [16]. Firstly, they examine the initial hiring situation where the firm and the associate face a different kind of uncertainty in relation to the associate's career path. The up-or-out system is thereafter rationalised in terms of an organisational response to this 'dual uncertainty' present at the initial hiring stage.

(Diagram 8.1)

DUAL UNCERTAINTY		
PARTY		UNCERTAINTY
The firm		Associates personal characteristics and legal skills
The associate		Opportunism by the firm.

(I) Uncertainty of the firm:

When a firm intends to hire an associate from the market, it faces an extreme deficiency of information regarding which of the total pool of associates to select in terms of legal skills and personal characteristics. The apprenticeship process provides an opportunity for those associates chosen initially by the firm to reveal their attributes, signalling their suitability for the firm and ultimately partnership.

The system must, however, hold some appeal to the associate in order that he enters this implicit 'contract'. Paradoxically, in attempting to reduce the uncertainty it faces, the firm actually creates the problem of the associate's uncertainty.

(II) Uncertainty of the associate:

The uncertainty facing the associate arises from the possibility of opportunism on the part of the firm. Winners in the system obtain partnership places creating large incentives and a high potential payoff for associates. Associates' uncertainty upon initial hire is whether the firm will play a fair game at the time when the partnership decision is being made. This is of prime concern to associates since the firm faces incentives to opportunistically evaluate their performance.

This incentive arises since the awarding of partnership places (as an alternative to continuing employment as an associate) results in diminished profit shares accruing to existing partners. This problem is similar to that discussed in earlier chapters of the thesis which outline theory of the labour managed firm (LMF) and focus on problems of a perverse short-run supply decision [17]. The associate is also compromised in his ability to force the firm to act fairly if need be - substantial investments in firm specific human capital have been made by the associate, the value of which is significantly less in any other situation outwith that firm.

From the associate's point of view, the bottom line of the dual-uncertainty problem is that, even if the firm acts opportunistically by not offering a partner place, and alternatively offers to retain him as an associate, he is almost bound to accept the firm's decision, even in the face of the opportunism. This is a consequence of the 'locking-in' of the associate to that particular firm due to specificity of his human capital investment. It is likely that the firm's non-partnership offer will be more attractive than any other offer the associate could obtain elsewhere - firm-specific capital is non-transferable and worthless to potential alternative employers.

From the perspective of the associate, the problem with the apprenticeship period is that its purpose is to encourage the associate to invest in firm-specific capital. During this period the firm also collects invaluable information regarding the associate's characteristics and abilities. It is possible that the associate's time could be used more profitably and effectively in the absence of this screening contest - for instance, less time would require to be devoted to supervision and the like, and more important work could perhaps be delegated.

Information disclosed to the firm regarding associates' skills and characteristics, is also largely firm-specific since it cannot be transferred effectively to other employers. Should an

associate leave after not being promoted to partner, the problem facing the associate is that other employers may perceive failure to be selected as a partner as an obvious signal of general unsuitability for partnership, even where the original firm had a clear information advantage in making such a decision. A consequence of this for the associate is that his legal skills (even those which could be expected to be more general) may also transpire to be relatively firm specific. Consequently, the associate who has failed to be offered partnership may face particular difficulties in seeking alternative employment outwith his original firm.

1.11 The apprenticeship period as a bonding mechanism:

Gilson and Mnookin (1988) argue the up-or-out system acts as a bonding device which assures associates when they are initially hired, that they will be treated fairly at the time of the partnership decision [18]. It would not be viable to solve this using a written contract since;

1. The selection process involves subjective evaluation of individual characteristics (eg. performance, leadership qualities, client relations etc.) which are highly individualistic.

2. The above are characteristics, behind which opportunistic persons may be able to hide their true character fairly easily.

3. Such traits escape easy or unambiguous specification within a written contract, and are incapable of being enforced reliably or impartially by a third party.

If it were possible, a formal contract would do very little to reduce levels of uncertainty for associates, and its most likely effect would be the introduction of high levels of uncertainty for the firm. This is a direct result of characteristics being by their very nature incapable specification with sufficient precision to permit formal enforcement. Enforcement, therefore, remains informal by processes of reputation evaluation in the market, or within the organisation by clever design of the relationship itself [19].

In the context of the law firm, given information processing capacity limitations of individuals, it is almost impossible that any person (either a third party or the associate himself) could subjectively determine whether the partnership decision outcome was fair or not. Unless opportunism by the firm is perceived by associates, or by third parties, the firm will not suffer reputation diminutions. It is unlikely that opportunism could be perceived if it existed.

The idea of reputational control of firm behaviour in making the partnership decision here is clearly not particularly useful and consequently, we are forced to search for a greater

understanding elsewhere. Williamson (1985) discusses the notion of "credible commitments" which are essentially self-enforcing relationships. An examination of these could point us in the correct direction and aid understanding of the partnership decision [20]. In the guise of a credible commitment, the up-or-out system can be rationalised as a structural bonding device which is subjectively evaluated by both parties at the point of time of the initial hire.

The option to fire the associate, instead of promoting to partner, signals to the associate that the incentive to retain the associate in a non-partner position (even though they have reached partner standard) is entirely removed. The firm, thereby, effectively eliminates the incentive to undertake the opportunistic behaviour which lies at the heart of associates' uncertainty. Hence, the firm cannot strategically use the partnership decision to retain associates who have attained partner standard, in non-partner capacities, after the partnership decision has been made in an up-or-out system.

1.12 The remaining problem of why the system still enjoys willing participants:

Gilson and Mnookin (1988) argue the one remaining problem is one of attempting to understand the apparent willingness of risk averse associates to participate in the up-or-out system [21]. This willingness appears irrational in view of the fact that it is the system itself which is the source of the increased risk facing associates.

They note that the traditional response of the firm to this problem is that the firm offsets this increased risk by facilitating outplacement of associates who do not attain partner positions. The problem of providing for employment of associates in non-partner positions, after the partnership decision has been made, is that this actually undermines the credibility of the partnership decision. The offer of a 'consolation prize' within the firm is not viable as it does not remove the incentive for the firm to act opportunistically. Provision of an external 'consolation prize' can provide an answer to risk reduction without simultaneously undermining the partnership decision.

Gilson and Mnookin (1988) argue this external 'consolation prize' could be a partner position in a less prestigious law firm, or a job in the general council's office of a major client, for instance [22]. This, however, requires inter-firm and/ or client-firm agreements for outplacement. For successful outplacement to occur, the firm must overcome the firm-specific nature of the human capital investments made by the associate during the signalling process. Here, the firm can make unsuccessful associates appear more attractive to employ by an implicit promise to feed the recipient firm with business and referrals. This involves the creation of a network in which credible commitments and trust are to the fore.

Risk can also, however, be reduced by increasing the likelihood of the associate becoming a partner. This may be regarded as the more expensive of the two risk reducing options. The exact decision process involved in the firm choosing between these options remains a puzzle. This is further reinforced by the apparently irrational behaviour whereby firms tend to choose the more expensive method - increased likelihood option as against outplacement.

The existing ratio of associates to partners will be a crucial variable in the associate's perception of the likelihood of successful promotion to partner status - Gilson and Mnookin call this ratio the firm's leverage. It is further argued that the higher the firm's leverage, the more successful must be that firm's efforts at reducing associate risk by external means. This is because the higher the ratio, the lower is the likelihood of becoming a partner and the higher is the internal risk faced by the associate to his human capital investment.

1.13 Choice between internal and external risk reduction for associates:

Several empirical patterns have been identified by Gilson and Mnookin (1988), as being relevant to a firm's choice between internal and external approaches to reducing risks facing associates [23]. These draw on American studies where firm leverage has been observed to be directly related to firm profit (degree of leverage also appears to be geographically based).

1. With reference to the firm profits link, as the likelihood of being chosen for promotion decreases, the size of the winners prize must increase in to attract even risk neutral players to the game.

2. With reference to the geographical effect, city firms tend to have higher associate to partner ratios (greater leverage) than those outside the city (in this case the city was New York). This is, however, consistent with at least one other explanation, namely that these firms are likely to be larger scale firms where an effective way of controlling costs while expanding is to increase the ratio of associates to partners.

In the city, it could be expected to be easier to outplace associates, due to the increased presence of opportunities for council positions in corporate headquarters of client firms. Non-city firms would be faced with attempting to reduce risk faced by associates internally, through increasing the likelihood of becoming a partner, since fewer opportunities exist for reducing risk via outplacement.

The whole story can be captured in terms of viewing firms' attempts at reducing the risk faced by associates, as a function of alternatives/ opportunities facing them. Firms that are successful at outplacement will be able to sustain a greater leverage than other firms in the same, or in another, geographical area. The less successful the firm is at outplacement, the

more reliant the firm becomes on reducing risk through increasing the associate's promotion prospects. As a result, per partner profitability is to that extent decreased.

Gilson and Mnookin (1988) [24] provide two reasons why the up-or-out system has become less popular recently, and these are;

1. The nature of the standards used by firms to make the partnership decision, is related to the conditions which require employment of a bonding mechanism in the first instance.

2. The substantial increase in demand for associates has had a similar, although less direct, consequence.

Gilson and Mnookin argue that associates now have an increased ability to monitor the fairness of the firm's partnership decision, through accessing and viewing the firm's time keeping and billing records [25]. Since these records are vital to the efficient operation of the firm, there would be a great cost to the firm in keeping intentionally inaccurate records [26]. Thus, increasing observability of the criteria used to judge the partnership decision may result in more direct associate monitoring of the fairness of the decision. The requirement for the bonding function of the up-or-out system is less relevant given this decrease in information impactedness in the firm. There are, however, other elements beyond mere hours worked which will enter any partnership decision.

1.14 The relationship between the partnership sharing bargain and the partnership decision:

The standards required of partners may be regarded as becoming more observable, due to the manner in which many partnerships assign partners' respective shares of profit. Gilson and Mnookin (1984) noted a general shift from a sharing model which solely emphasises sharing, towards one in which productivity measurement is emphasised [27]. The relative merits of these two systems are discussed at length and in great detail elsewhere in this thesis.

Gilson and Mnookin (1988) argue a more mechanistic method of income division which accounts for differential productivity, at the extreme, can eliminate the requirement for an apprenticeship period [28] - taken to its logical conclusion, at its most extreme, it can even eliminate the concept of partnership.

Elimination of the apprenticeship period would be possible since the more mechanistic the measurement process becomes (eg. including hours worked, clients attracted, amounts billed etc.), the less subjective become the standards required for partnership appointment - the

damage resulting from an erroneous partner decision is vastly reduced [29]. The source of the firm's uncertainty regarding the associate's quality, at the time of the initial hire, becomes insignificant in the mechanistic/ productivity based income division partnership - uncertainty will be eliminated as a result of its consequences being eliminated. Associates will be paid exactly what they are worth, and the partnership will not have to pay associates a disproportionately high level of income in relation to their relative contribution to the firm.

The apprenticeship period ceases to be necessary as a precursor to being selected as a partner. The extreme situation would be the end of the present clear distinction between partner and associate. The focus of such a firm would now centre on instigating an efficient screening procedure at the time of the initial hire. This would be necessary in order that associates whose inability would be detrimental to the operation and efficiency of the firm, would not be hired.

1.15 The impact of the increased demand for associates:

Gilson and Mnookin (1988) also argue that the increased demand for associates can be seen as another factor that can partially explain the move away from the up-or-out system [30]. This is independent of the manner in which the firm chooses to divide its profits among partners.

It is argued that in the large corporate law firms, business is expanding so rapidly that traditional sources of new associates are unable to feed law firms with sufficient personnel. The evidence claimed to support this is that it was previously claimed that such firms chose graduates picked from, for example, the top half of their class in the top 20 law firms. Some firms even claimed that graduates were picked from nowhere near as many as the top 20 schools. It is now claimed to be the case that many firms have had to choose graduates that would have been previously viewed as less capable, in order to satisfy demand. Supply of "good" graduates is quickly exhausted and law firms are becoming generally larger.

This raises the question of whether the up-or-out system is flexible enough to cope with increased numbers of 'higher risk' associates entering the firm, where flexibility relates to the screening function of apprenticeship, and successful outplacement of associates not chosen as partners. This has three consequent effects on the firm's ability to evaluate the quality of the associates it hires;

1. It could be expected that the resultant increase in qualified assistants per partner (before longer-run adjustment takes place) would increase the burden on evaluatory processes since there will be an increased pool of potential candidates.

2. The decrease in the quality of the pool of associates, could be expected to decrease the mean ability, and increase the variance of ability, of new associates. The result is likely to heighten still further the already difficult evaluation of candidates.

3. It could be expected that any resultant deterioration in the screening process, may increase the likelihood of erroneous partnership decisions being made in respect of both newer, lower quality, and traditional, higher quality associates. The result could make the firm less attractive to traditional associates with the potential for the creation of a "lemons market" through time [31]. High quality producers would be no longer able to signal to consumers that their product is of a higher quality than those of low quality producers in the market. The strongest form of this is that a higher price, reflecting a quality premium, cannot be charged and only low quality products are produced.

The increased number of associates entering the firm, obviously further compromises the ability of the firm to successfully screen contestants for partner positions. There is likely also to be an increase in the number of associates requiring to be outplaced.

Demand for these unsuccessful associates is likely to be affected due, firstly, to an absolute increase in their numbers paired, secondly, with a decrease in their general quality. It is recalled that successful outplacement requires the firm to create certain conditions. The firm must appear to be very selective in order that unsuccessful associates are not perceived as undesirable to hire by outsiders. Outplacement may be made more difficult through an increase in variance of the quality of the marginal group of associates. This causes it to be more difficult for the outsiders to perceive the fairness of the partnership decision, and the underlying true quality of persons to be outplaced.

As a result it is more difficult for the firm to offset the increased risk faced by associates in the up-or-out system, since there are no permanent associate positions. Gilson and Mnookin see these factors as being a threat to the continuing viability of the up-or-out system [32].

1.16 Replacement of the up or out system:

By departing from the up-or-out system, firms can respond partially to problems arising from, firstly, the increased number of associates required, secondly, the decrease in their average quality and, thirdly, the increase in variance of associates' quality.

In previous parts of their paper, Gilson and Mnookin (1988) argue there is an increased ability of associates to monitor the fairness of the partner decision [33]. However, responding to the above problems also requires a more positive effort by the firm. The firm must attempt to

expand the number of associates being hired, without diminishing the quality of the apprenticeship. This requires the firm to avoid an increase in screening errors and reduction in outplacement success. The firm can attempt to accomplish this by creating two separate streams of associates from the point they are initially hired [34].

The first of the two streams created comprises those derived from the traditional pool of associates and they are treated as they would be under an up-or-out system. The second stream of associates are advised upon hiring that they will never be considered for partnership, thereby creating no additional burden on the screening process of the apprenticeship. This also obviates any problem otherwise created in attempting to outplace unsuccessful associates from the first stream.

The creation of a separable category of associate lawyer (not considered for a partner position) can facilitate, for instance, employment of contract/ temporary lawyers. Additionally, this provides greater opportunity and flexibility for the firm to be more discriminatory in the manner in which it assigns different types of legal work to these two separate streams. This should enrich evaluatory and screening processes by stimulating signalling activities by associates in desired directions.

1.17 Determinants of the firm's choice between an 'up-or-out' or 'two-stream' system:

One main question remains unanswered - what type of firm characteristics are likely to be determinative of a firm's choice of one screening system against another. In their study, Gilson & Mnookin (1988) have argued the firm's increased ability to monitor the partnership decision could be expected to result in creation of new categories of non-partner associate positions [35]. These firms are likely to divide law firm income on a productivity basis.

Additionally, it is likely to be the case that this method of income distribution has recently largely replaced a system that was more concerned with risk sharing, than creating productivity incentives. The argument underpinning increased demand for associates is that this involves the firm hiring associates of a lower mean ability and greater variance of ability than before. Further, it is predicted that such firms are likely to have increasing amounts of work which can be competently accomplished by lawyers of a lower absolute quality [36].

Section Two: Questionnaire Section Five - Internal Promotion and Firm Growth:

Introduction:

In this section some of the theoretical issues surrounding firms' attempts to become larger will be pursued empirically. Theoretically, all things considered, the law firm faces fairly

substantial barriers to growth irrespective of attempts by other firms to prise market share from it.

2.1 The expansion problem of the law firm:

For reasons outlined above, certain characteristics of the law firm make its expansion per se more difficult than other types of firms. To expand the labour force within other firms, they typically simply go to the market and hire suitable extra labour at the appropriate wage rate. The decision of the law firm is not so simple since it has the choice of hiring more labour from at least three main inter-related categories available to it. These three main categories, each of which pose particular problems for the law firm, are as follows;

1. Unqualified staff - the problem here is that this category of labour is limited in its ability to undertake many types of legal work. Consequently, fairly high levels of training and supervision are required if the firm wishes to offer a realistic service. There are also problems in delegating too much work to such staff since this can lead to loss of control over property rights, in the absence of excess time spent on costly monitoring.

2. Qualified staff - this category can be either trainees or fully qualified staff from other firms. As such they will be able to complete more types of work with lower levels of supervision. In the short term they will be a solution to expanding the firm but in the longer term these people will require some offer of a career opportunity within the partnership. As will be recalled from earlier in this chapter and from the chapter dealing with the LMF, an increase in partner numbers may not be desirable for those who are already partners.

3. Partners - partnerships have, however, traditionally avoided direct hiring of partners from other firms for reasons discussed above and elsewhere in this thesis.

Other methods of increasing firm scale are mergers, take-overs and bolt-ons but these are all problematic as compatibility is difficult to ensure and screening functions are largely absent. Hence, there may be a tendency for the law firm to resist fast expansion and for those within the firm to have to work fairly hard - the firm will typically work near full capacity most of the time. For this and other reasons it is expected that lawyers within the firm will typically require to work long hours and shirking may not be a significant problem.

Firms of differing sizes and types may have different hiring strategies - for instance, hire labour from the external labour market, or solely rely on internal labour market contests. It is expected that there will likely be variations in hiring and selection techniques across

categories of labour within the typical law firm. These are issues that have not been dealt with before in any great detail by economic theory and particularly in the specific context of the law firm. By pursuing these issues within this section of the empirical study, the variety of policies firms have adopted in relation to hiring of labour and firm growth in general, will be exposed.

The size of the law firm is also related closely to risk sharing benefits and specialisation. Partners of specialised law firms could be expected to be exposed to greater levels of risk than those of an unspecialised firm due to lower degrees of diversification of their human capital. The most specialist services, however, could be expected to be in areas of corporate work where overall larger scales of organisation may be necessary. Hence, increased risks to human capital of strong competition may be attenuated where only a few firms exist in a highly specialised market. It is apparent that, whether they realise it or not, partners in law firms of differing types and scales, face differing degrees of risk to their human capital.

2.2 The over-arching requirement to screen labour for compatibility:

There has been previous discussion above regarding the desirability, importance and necessity of a screening process for the firm to choose between qualified assistants who are being considered for partnership. The requirement for a rigorous filtering/ selection process to choose between qualified assistants to fill partnership places makes it difficult for the firm to quickly expand per se. The empirical study will thus determine;

1. Whether the theoretically expected emphasis on screening and its importance is a feature of real life law firms and,

2. The nature and extent of screening processes actually adopted.

As a direct consequence of the desirability of having as comprehensive an information set regarding qualified assistants as possible at the partnership decision point, it is additionally expected that the majority of new partner admissions will be qualified assistants from within the firm. It is anticipated that such labour will typically have served an apprenticeship during which time will have demonstrated the suitability of their characteristics to the firm. The firm will have a larger information set regarding these qualified assistants upon which to base a partnership decision than for other qualified assistants outwith the firm.

The firm may not, however, have a big enough pool of qualified assistants to permit the desired level of growth in the firm in terms of numbers of partners. Additionally, the firm may require partner specialisations in the short run which are not found within the current pool of qualified assistants within the firm. Consequently, the firm facing this problem may be forced

to hire new lawyers straight in at partner level. This lateral entry could be expected to be the far rarer case since the firm will possess little information regarding the suitability of such candidates for partnership.

To permit the firm to attract such partners, whilst at the same time retaining screening, it is expected that new admissions will require to serve a probationary period during. During this period the new partner will typically salaried, thereafter becoming an equity partner if satisfactory during probation. The probationary period is expected to reduce potential risks of making external partner appointments. The same situation could be expected for bolt-ons where a specialist partner team is brought into the firm on broadly similar terms from another firm. In the case of takeover or merger, the equity partners of each firm could be expected to have a joint meeting in which they would thrash out the joining process [37].

In any case, the decision to increase to number of partners is broadly expected to be a formal one with a voting or consensus mechanism being used by the partners to jointly authorise the decision. This voting/ consensus based decision process will be one element in the whole screening process the law firm is expected to apply to candidates for partnership from whatever source. These features will be empirically examined in this section.

2.3 Incentives facing the qualified assistant:

Qualified assistants who are interested in becoming partners, where this is the expected norm, will each have a perception of, firstly, their relative chances of being offered partnership and, secondly, the period of time they can be expected to wait before such an offer is made.

In this context, the decision of the firm to increase the number of partners is expected to be influenced by, amongst many other things, a desire to avoid losing good qualified assistants who become disillusioned when an offer of partnership is not forthcoming during the period of time in which they expect such an offer to be made. It will be recalled that previously it was argued that the potential loss to a firm of a good lawyer leaving can be significant if he has amassed a portfolio of clients as lawyer specific capital. It will also be recalled that it has been argued that use of restrictive covenants is likely to be futile in discounting the value of a lawyer's exit option.

It is evidently necessary to aim to understand what factors are instrumental in maintaining the interest of the qualified assistant in working for the firm and striving for a partnership position. The qualified assistant will more than likely be largely ignorant of the finer details of what an offer of partnership would mean to him in terms of the actual payoff. The motivating factor is likely, therefore, to be his perception of what the likely benefits will be - these are likely to include non-monetary aspects (status etc.). It is intended that information

from the previous section of the questionnaire will provide some indication as to reasons why the qualified assistant lawyer will not exit the firm.

It is likely that peer group pressure and monitoring will be strong between QAs, and that an ongoing contest between those QAs striving to become partners will exist. This contest will enable them to signal to the partners their suitability for partnership by supplying a high level of effort intensity to demonstrate their abilities. This process could be expected to constrain the exit option of QAs. Those QAs who are satisfied to remain QAs would presumably not see themselves as party to such an ongoing contest. As has been argued above, this category of lawyer is of value to the firm since it permits expansion without having to offer a further career step and expand the numbers of partners. The previous discussion of Gilson and Mnookin's analysis of the up-or-out system provides an indepth discussion of this area above [38]

The QA's perception of his chances of becoming a partner are hypothesised as being likely affected by the following;

1. The partnership gearing (ie. ratio of QAs to partners) and,

2. The expected period of time for the QA to be with the firm before being offered partnership.

This will provide QAs with some notion of what the chances of promotion are, and how long they could expect to wait before being offered partnership. It will of course signal to QAs who have waited shorter times, and been offered partnership, that the firm thinks very highly of them. To those who have waited longer, it will signal that the firm is still waiting for them to demonstrate their suitability, or perhaps that they should start looking elsewhere. The above two features will be examined for each of the sample firms to expose the differing incentives that are expected to face QAs in different firms.

2.4 The law firm viewed as a Labour Managed Firm (LMF):

It had been demonstrated at great length elsewhere in this thesis that an examination of the literature of the Labour Managed Firm (LMF) literature points to the applicability of many of its ideas to analysis of the law firm organisation.

Theory of the LMF suggests firm members are provided with an incentive to restrict their numbers, since this will maximise per member income. The firm's policy on hiring partners and other categories of firm labour will be investigated in this respect to determine if there appears to be any such tendency within the real life law firm to behave as an LMF.

2.5 Specific internal promotion and firm growth hypotheses to be empirically tested:

Hypothesis 1: Law firms will tend to rely on internal promotion of qualified assistants rather than external hiring as the mechanism of growth of the partnership.

Hypothesis 2: The law firm will employ formal screening mechanisms to discover suitability of potential partners for the firm.

Hypothesis 3: The decision to increase partnership number will be very formal and subject to a strict procedure.

Hypothesis 4: Where the firm permits lateral hiring of partners from the external labour market, a probationary period as salaried partner will be used to reduce risks to the firm.

Hypothesis 5: Qualified assistants will not exit the firm as the promise of partnership will act as an exit constraint and incentive to supply high levels of effort.

Hypothesis 6: Partnership gearing (ratio of qualified assistants to partners) will be higher in larger firms/ corporate client firms due to the requirement to work in teams and do so cost effectively.

Hypothesis 7: Law firms may have a tendency to restrict membership, like the Labour Managed Firm (LMF) as this will preserve per member income.

Section Three: Internal promotion and firm growth within the sample firms:

Introduction:

In this section, responses of firms in the study are analyzed to elicit information regarding how promotion decision systems operate in real life law firms. It is thereby anticipated that the manner in which law firms grow will become apparent.

3.1 Partnership size decision processes:

Firstly, in relation to the decision to increase the number of partners, the nature of the decision process was determined for the sample firms. The following table summarises their responses;

(TABLE 8.2)

Firm No	FORMAL2	FULLPTR	COMMPTRS	PTRVOTE	COMMDEC	CANDNOM	SENREQ	THIRD	PREVENT
1,3,8,9,11,16,18,32 (8 Firms=24.2%)	Yes	Yes	No	No	No	No	No	No	Yes
30 (1 Firm=3.0%)	Yes	Yes	No	No	No	No	Yes	No	Yes
10,13,15,17 (4 Firms=12.1%)	Yes	Yes	No	No	No	No	No	No	No
2,12,14 (3 Firms=9.1%)	Yes	Yes	No	Yes	No	No	No	No	No
6,25,31 (3 Firms=9.1%)	Yes	Yes	No	Yes	No	No	No	No	Yes
5,7 (2 Firms=6.1%)	Yes	Yes	No	Yes	No	No	Yes	No	No
4,26,27,28,33 (5 Firms=15.2%)	Yes	Yes	No	Yes	No	Yes	No	No	Yes
22,29 (2 Firms=6.1%)	Yes	Yes	No	Yes	Yes	Yes	No	No	Yes
24 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	Yes	No	Yes
21 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No	Yes	Yes
19 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	Yes	Yes	No	Yes
20 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	Yes	No	No	No
23 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	Yes	Yes	No	Yes
TOTAL FIRMS	33	30	3	19	5	11	6	1	23
%age FIRMS	100	90.9	9.1	57.6	15.2	33.3	18.2	3.0	69.7

Description of variables:
FORMAL2-Formal decision process to increase partner numbers
FULLPTR-Decision of full partners meeting
COMMPTRS-Decision of committee of partners
PTRVOTE-Partners have votes on candidates
COMMDEC-Committee decides on new partners
CANDNOM-Partnership candidates are nominated
SENREQ-Seniority requirement before consideration
THIRD-Third party tests on all prospective candidates
PREVENT-Need to prevent good QAs leaving

In relation to increasing partnership numbers, all 33 firms indicated they employed a formal decision process.

(I) Increasing partner numbers by full meeting of partners - further breakdown:

In 30 firms the decision was taken by a full meeting of the partners, reflecting the importance of the decision. 4 firms provided no additional information. In 8 firms the basis of the decision was often the need to prevent good QAs leaving the firm. In 1 firm, qualified assistants additionally required to be of a suitable seniority before being considered.

3 firms indicated that the decision of the full partners meeting employed a formal voting procedure. In another 3 firms this voting procedure applied, but in addition the need to avoid good QAs leaving influenced the decision process. In 2 firms the voting procedure and a seniority requirement comprised the decision making process.

All of the remaining 9 firms, employed a voting system and recognised the importance of avoiding good QAs leaving the firm. In 2 of these firms, a partners committee decided who should become partners, nominating prospective candidates to be voted on by the full partners meeting. In 5 of the firms, candidates are nominated by individual partners, departmental heads and the like, with the full meeting of partners voting on them. 1 firm revealed it had a seniority requirement, this being the only additional information. Within the last firm, candidates are nominated by individual partners, departmental heads and the like, for the full partners meeting to vote on, but additionally all prospective partner candidates are subject to third party psychological tests.

(II) Increasing partner numbers by a committee of partners - further breakdown:

In only 3 firms was this vitally important decision entrusted to a committee of partners. In these firms, candidates are nominated by individual partners, departmental heads and the like, the committee decides which candidates will be accepted and the committee makes the partnership decision. In 2 of these 3 firms, partners on the committee vote to choose between candidates. In the firm not mentioning voting, a seniority requirement was mentioned, as was the need to prevent good QAs leaving. These two features were also recognised by one of the 2 firms mentioning the voting system.

All 3 firms above using the committee system to make the partnership decision were large firms - indicating that the size of the partners group was perhaps too big to facilitate the decision being taken by the full meeting of partners.

While the full complement of partners does not make the decision, it is unlikely in the above situation that an obviously erroneous partnership decision would go through as;

1. It would be unlikely to get past the committee stage and,

2. Even if it did, one or more non-committee partners would be likely to discover the proposals and attempt to get the decision over-ruled before implementation.

It is thus apparent that the decision process is typically formal and tends to follow an established procedure offering support for Hypothesis 3. which states that the law firm's decision to increase partnership numbers will be very formal and subject to a strict procedure.

It is also apparent that the formality of the decision process and particularly the use of nomination and voting procedures, seniority requirements and often several levels of decision making filters via committees, is indicative of the kind of procedures Hypothesis 2. argues will be typical of the law firm. Hypothesis 2. states the firm will employ formal screening mechanisms to discover the suitability of potential partners for the firm. Evidence above is corroborative of Hypothesis 2 in this respect.

3.2 Candidates for partnership - the issue of internal promotion and external hiring:

(TABLE 8.3)

Firm No	INTONLY	EXTCAND	SALARY	HEDHUNT2	INTMERG	HEADFUTU
1,5,8,9,10,16,17,20,24, 30,32,33 (12 Firms=36.4%)	Yes	No	No	No	No	No
6,15 (2 Firms=6.1%)	Yes	No	No	No	No	Yes
13,25 (2 Firms=6.1%)	Yes	No	No	No	Yes	No
18 (1 Firm=3.0%)	Yes	No	No	Yes	No	No
22 (1 Firm=3.0%)	Yes	No	No	Yes	No	Yes
4 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	Yes
2 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	No
26,27 (2 Firms=6.1%)	Yes	Yes	No	Yes	No	Yes
11 (1 Firm=3.0%)	Yes	Yes	No	No	No	No
14 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	No
28 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	Yes
19,21,23,29 (4 Firms=12.1%)	Yes	Yes	Yes	Yes	No	Yes
3,12 (2 Firms=6.1%)	Yes	Yes	Yes	Yes	No	No
31 (1 Firm=3.0%)	Yes	Yes	Yes	No	No	Yes
7 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	No
TOTAL FIRMS	33	13	9	12	7	12
%age FIRMS	100	39.4	27.3	36.4	21.2	36.4

Description of variables:
INTONLY-Internal promotion to partnership
EXTCAND-External candidates considered for partnership
SALARY-If external then salaried probation first before equity sharing
HEDHUNT2-Headhunting of partners
INTMERG-Internal candidates except if takeover/ merger etc.
HEADFUTU-Will have to consider headhunting in future

2 main categories of firms can be identified with reference to hiring/ promotion of QAs to partner level, and these will be examined below.

(I) Firms who use internal promotion - further breakdown:

As was expected, this group enjoyed the majority of respondents, totalling 20 of the 33 firms. Of this group of 20 firms, 12 provided no additional information regarding QAs and promotion to partnership. 2 firms perceived that they may have to headhunt partners in future and another 2 firms indicated that only internally promoted QAs became partners, except in the rare situation where the firm merged with another.

3 firms disclosed that although it was their policy to only internally promote to partnership, exceptional circumstances had forced them to headhunt very occasionally in the past. Of these firms, 2 felt that there would be an increased role for headhunting in future within their firms, one of them also indicating that merger situations could result in them deviating from their only internal promotion policy.

The last firm in this group also noted that mergers could result in rare contravention of their only internal promotion policy. Where this occurred, however, new partners that were not internally promoted would be initially salaried to retain the screening process.

(II) Firms who used internal promotion and external hiring - further breakdown:

The 13 firms in this group broke down further into two basic types, those that used a salaried partner screening period and those that did not. 5 firms did not use a salaried period for new

externally hired partners, during which suitability for equity sharing can be assessed. Of these 5 firms, 2 indicated they headhunted partners and reckoned this activity would play a greater role in the future, and 2 firms indicated that often mergers could result in new non-internally promoted partners. The last firm provided no additional information.

The group of firms that did use a salaried partner screening period for externally hired partners totalled 8. Of these 8 firms, half indicated they headhunted partners at present and foresaw an increase in this for the future. 3 other firms disclosed they used headhunting, one of them also indicating that mergers were a source of new non-internally promoted partners. The final firm foresaw an increase in headhunting activities in future; this being the only additional information provided.

It is apparent from the information presented above that the typical firm will rely primarily on internal promotion of QAs to fill partner vacancies since such candidates will be more easily evaluated than external ones for suitability. Where external hiring occurs, there is a much higher incidence of salaried partner categories existing within the firm. This can be regarded as a screening mechanism/ apprenticeship during which time the partners can assess the true suitability of such persons for full equity partnership participation. This highlights the apparent importance of screening partner entrants in order that the firm can confidently rely on self-enforcing monitoring and incentive systems to constrain behaviour of its lawyers.

This evidence is consistent with Hypothesis 4, which states that where the firm permits lateral hiring of partners from the external labour market, a probationary period as salaried partner will be used to reduce risks to the firm.

Generally, even firms who indicated they did externally hire at partner level, expressed their preference for internal promotion. External hiring, new partner additions via firm mergers and headhunting were all activities generally necessary because the firm could not itself internally produce enough QAs of the type or calibre necessary to fulfil its needs at a particular time. Essentially there is internal market failure and the firm has to go to the external market, thereby increasing uncertainty and risks etc. The firm must, therefore, attempt to protect itself from these increased risks and uncertainty and typically chooses to do this via a salaried probationary period.

The evidence above is broadly consistent with Hypothesis 1, which states that law firms will tend to rely on internal promotion of qualified assistants rather than external hiring as the mechanism of growth for the partnership.

12 firms admitted to headhunting partners from the external labour market, and this included 3 firms who indicated it was their usual policy to exclusively rely on internal promotion of

qualified assistants and avoid external hiring in all but rare occasions. 12 firms anticipated that (typically as a result of increasing specialisation in legal services) they would be likely to require to rely on headhunting of partners in the future. Notably, 2 of these firms currently attempt to avoid external hiring at all times, 2 rely typically on internal promotion (only hiring externally in rare exceptional circumstances) and the remaining 8 have a hiring policy that could accommodate external hiring (6 of whom have headhunted in the past).

3.3 Partners buying into the firm:

(TABLE 8.4)

Firm No	PARTBUY	NOTINIT	DEFDRAW	NOGWILL	WORKCAP
28,29 (2 Firms=6.1%)	M	M	M	M	M
5,7,8,15,16,18,22,25,30,32 (10 Firms=30.3%)	No	No	No	No	No
4 (1 Firm=3.0%)	No	No	No	Yes	Yes
17 (1 Firm=3.0%)	No	No	Yes	No	No
21,24 (2 Firms=6.1%)	Yes	No	No	No	Yes
1,9,12,13,14 (5 Firms=15.2%)	Yes	No	No	No	No
23 (1 Firm=3.0%)	Yes	No	No	Yes	Yes
26 (1 Firm=3.0%)	Yes	No	Yes	No	Yes
11,20 (2 Firms=6.1%)	Yes	No	Yes	No	No
6,10,27,19,31,33 (6 Firms=18.2%)	Yes	Yes	No	No	No
3 (1 Firm=3.0%)	Yes	Yes	No	Yes	No
2 (1 Firm=3.0%)	Yes	Yes	Yes	No	No
TOTAL FIRMS	19	8	5	3	5
%age FIRMS	57.6	24.2	15.2	9.1	15.2

(M-Missing)
Description of variables:
PARTBUY-New partners have to buy into the partnership
NOTINIT-Partners may have to buy in but not initially
DEFDRAW-Partners buy in by deferring drawings ie. leave capital behind
NOGWILL-No goodwill in partnership
WORKCAP-New partners only have to make a small contribution to working capital

It is expected that new partners may be required to buy into the partnership, or at least make some contribution to its working capital. The contents of TABLE 8.4 above will now be examined with reference to partners' capital contributions - contribution of capital can be regarded as a bonding mechanism which further bonds partners to each other, and the firm.

When asked the question of whether new partners had to buy themselves into the partnership, 19 firms indicated that this was the case, with the remaining 14 disclosing that partners do not have to buy-in (2 firms provided no information and are thus coded missing).

(I) Firms where new partners do not have to buy-in - further breakdown:

Of these 12 firms (14 minus 2 coded missing), 10 provided no additional information, merely indicating that partners did not have to buy-in. 1 firm indicated that there was no goodwill in the partnership and that new partners may only have to make a nominal contribution to working capital. The other firm indicated that partners may have to defer drawings, ie. leave capital behind, periodically depending on the working capital situation. There was, however, no strict requirement for partners to buy-in.

(II) Firms where new partners have to buy-in - further breakdown:

Of these 19 firms, 8 additionally disclosed that although new partners had to buy-in, they did not have to do so initially. 6 of these firms provided no additional information, but 1 indicated that no goodwill existed in the firm, with the other indicating that partners buy-in by deferring drawings (leaving capital behind).

Of the 11 firms whose partners had to make an initial contribution to buy-into the firm, 5 provided no additional information. 4 firms noted that partners had to make a contribution to the firm's working capital, 1 of them noting that there was no goodwill in their firm and another noting that partners deferred drawings in order to make their working capital contribution. In the 2 remaining firms, partners had to buy-in initially by deferring drawings.

3.4 The selection mechanism to choose between partnership candidates:

(TABLE 8.5)

Firm No	SELMECH	PERFQA	PTRVOTE2	CONSENS	SPECNEED	OTHER7
5,6,7,12,14,23,24,29,33 (9 Firms=27.3%)	Yes	Yes	Yes	No	Yes	No
2,20,21,25,26,28,31 (7 Firms=21.2%)	Yes	Yes	Yes	No	No	No
32 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	No	No
22 (1 Firm=3.0%)	Yes	Yes	Yes	Yes	Yes	No
3,9,11,15,16,17,18,19 (8 Firms=24.2%)	Yes	Yes	No	Yes	Yes	No
10 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No
4 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No
1,30 (2 Firms=6.1%)	Yes	Yes	No	No	No	No
8,13 (2 Firms=6.1%)	Yes	Yes	No	No	Yes	No
27 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	No
TOTAL FIRMS	33	32	19	12	21	0
%age FIRMS	100	97.0	57.6	36.4	63.6	0

Description of variables:
SELMECH-Formal selection mechanism
PERFQA-Performance as QA
PTRVOTE2-Partners vote on candidates
CONSENS-Consensus is arrived at by the partners
SPECNEED-QA is in specialty required
OTHER7-Other

It is recalled from TABLE 8.2, firstly, that all firms employed a formal decision process to increase the number of partners of the firm and, secondly, that 19 firms employ some voting mechanism to facilitate choice between candidates.

All but 1 of the firms explicitly cite the relative performance (however measured) of candidates during their time with the firm as a QA as an important choice criteria for selecting between candidates for partner positions. This is hardly surprising as it could be expected that a QA's performance is likely to be a strong signal of suitability (or otherwise) of candidates which would facilitate the choice by the present partners. The goal of every firm can be seen to be broadly similar in this respect - that being to assume partners who can be relied on to self-monitor. This, if successful, will reduce consumption of the firm's resources directed at policing partners to make sure they are not free-riding on others' effort.

In this respect, Hypothesis 5. is offered support since evidence above is consistent with its claim that QAs will not exit the firm where the promise of partnership will act as an exit constraint and provide an incentive to supply high levels of individual effort. It will also be recalled from TABLE 8.2 that 23 firms recognised the importance of the partnership decision in relation to making sure that good QAs do not leave. Presumably these QAs will be provided with at least some indication of how long they can expect to wait before being offered partnership - if the decision is not made within the period perceived by the QA as reasonable, then the firm stands to lose good QAs. It is only if the promise of partnership is not fulfilled by the firm that it will not act as an exit constraint or an incentive to supply high levels of effort intensity.

12 firms disclosed that 'consensus' was generally reached between the partners regarding choice of new partners. In 2 firms the reaching of consensus went hand in hand with the existence of a formal voting mechanism, where as in the other 10, 'consensus' was achieved without a formal voting mechanism. Where a voting and consensus system operated, the formal vote was seen as strictly necessary only where 'consensus' could not be reached for certain partnership candidates.

21 firms indicated that the decision made between prospective partners in the firm was also dependent on surpluses and deficiencies in the respective areas of law firm business. It could be, for instance, that a certain area of work was experiencing a boom and that department in the firm was running at 100% capacity with unmet demand, requiring some form of expansion. This could result in quicker than normal promotion to partnership of certain QAs (more as a function of demand and supply rather than their ability as compared with QAs working in other areas of the firm). It was disclosed that QAs of similar abilities would be more likely to be promoted faster if they were legal specialists in an area in which it was decided partner appointments were needed to soak up excess demand/ create new capacity.

Thus, policies firms have for increasing number of partners are based on numerous factors. A common reason for expansion of partner numbers is to help cope with the sheer volume of work in a particular area and the demands of business, or pressure on a particular department. Another main reason is the desire to retain good quality QAs, arguably demonstrating the value of the training the firm gives to its QAs and the fact that dissatisfied QAs exiting the firm could represent a significant loss to the firm. This loss would have two main components;

1. The loss of trained personnel that would generate positive externalities to any firm that re-employs these highly trained QAs and,
2. Potential loss of clients.

In almost all cases it was emphasised that the decision to increase partner numbers would require to be cost effective, or at least be projected to become cost effective quickly. Typically, this was reinforced with stringent assessment procedures that would screen entrants to the partnership and ensure that any new partner chosen would be compatible with the existing group of partners. Determination of the cost effectiveness of extra partners being appointed would presumably involve existing partners evaluating whether such a move would result in lower levels of personal income, or whether the increased level of fee income that such a move could be expected to generate would more than offset the impact of the reduced share of income that each partner would receive as a result of any new admission. Due to perceptive and rationality limitations it would be difficult for partners to make this calculation accurately and they may view the likely reduction in their workload, consequent on extra partners being appointed, as outweighing any reduction in income they may suffer as a result. The firm may or may not, therefore, exhibit labour managed firm (LMF) tendencies which promote longer term self-degeneration through non-replacement of partners, or pursuit of a deliberate non-hiring policy.

3.5 The expected length of QA service (post qualifying) prior to being offered partnership:

(TABLE 8.6)

Firm No	PERIODQA	QUALQA	USUAL03	USUAL46	USUALGT6	SENASSOC	OTHER8
1,5,16,17,25 (5 Firms=15.2%)	Yes	Yes	Yes	No	No	No	No
2,3 (2 Firms=6.1%)	Yes	Yes	Yes	Yes	No	No	No
12 (1 Firm=3.0%)	Yes	Yes	Yes	No	No	Yes	No
4 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No
6,7,10,11,15,18,20, 21,22,23,31 (11 Firms=33.3%)	Yes	Yes	No	Yes	No	No	No
9 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No
27 (1 Firm=3.0%)	Yes	No	No	Yes	No	No	No
24,26,32,33 (4 Firms=12.2%)	Yes	Yes	No	No	Yes	No	No
30 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	Yes	No
13,14,19,28 (4 Firms=12.2%)	Yes	Yes	No	No	No	No	No
8 (1 Firm=3.0%)	Yes	No	No	No	No	Yes	No
29 (1 Firm=3.0%)	M	M	M	M	M	M	M
TOTAL FIRMS	32	29	9	15	5	4	0
%age FIRMS	97.0	87.9	27.3	45.5	15.2	12.2	0

(M-Missing value)

Description of variables:
PERIODQA-Period as QA before partnership offer varies
QUALQA-Period pre-partner depends on quality of individual QA
USUAL03-Period pre-partner usually 0-3 years
USUAL46-Period pre-partner usually 4-6 years
USUALGT6-Period pre-partner usually greater than 6 years
SENASSOC-Senior associate category between QA and partner
OTHER8-Other

As one would expect, 32 of the firms providing information for this question indicated that the period served as a QA before being offered partnership varied. Only 1 firm did not answer this question (coded as a missing value), but almost all of the remaining firms were able to give a typical pre-partner period for their QAs.

(I) Firms whose usual pre-partner period for QAs is 0-3 years - further breakdown:

Of this group of 9 firms, 8 indicated that the period was dependent on the quality of the QA amongst other factors. 1 firm disclosed the existence of a 'senior associate' category and another also indicated that other QAs could typically be in the firm as a QA for 4-6 years pre-partnership. Of this group of 9 firms, 7 are small/ medium and 2 are large.

(II) Firms whose usual pre-partner period for QAs is 4-6 years - further breakdown:

12 of these 13 firms indicated the period is typically 4-6 years pre-partnership and that this period also depended on quality of the QA amongst other factors. 1 of these firms additionally disclosed the existence of 'senior associate' positions and another provided no information other than the 4-6 year typical period. Of the 13 firms in this group, 6 are small/ medium and 7 are large.

(III) Firms whose usual pre-partner period is greater than 6 years - further breakdown:.

All 5 firms in this group indicated the expected period, although usually being greater than 6 years, is also dependent upon the quality of the QA amongst other factors. 1 of these firms also disclosed the existence of the senior associate category in the firm between QA and partner. All 5 of these firms are large firms.

(IV) Firms who could not indicate a typical pre-partner period - further breakdown:

In addition to the 1 firm who provided no information whatsoever to this question, 5 firms could not provide a typical period of time for QAs to be with the firm before being offered partnership. 4 of these firms indicated only that the period would be dependent on the quality of the QA and many other factors. The remaining firm indicated only that the period varied between QAs and that a 'senior associate' category existed within the firm.

The 4 firms that used a 'senior associate' category between QA and partner, did so in an attempt to provide good QAs with a career move and additional status. This could be used to buy time before the partnership decision required to be made to avoid good QAs leaving. It was pointed out by many of the firms that some QAs never become partners, typically because they demonstrate no desire to become partners and are content with QA status.

3.6 The replacement of partners after a depletion in partner numbers:

(TABLE 8.7)

Firm No	AUTOREPL	DEPDEPT	CAPACIT	EXPAND	QUALPROF	RETPLAN
2,3,4,5,6,11,13,14,18, 19,20,21,22,23,25,26, 27,28,29,30,31,32,33 (23 Firms=69.7%)	No	No	No	No	No	No
1,10,16 (3 Firms=9.1%)	No	No	No	No	No	Yes
24 (1 Firm=3.0%)	No	No	No	No	Yes	No
15 (1 Firm=3.0%)	No	No	Yes	No	Yes	No
8,17 (2 Firms=6.1%)	Yes	No	Yes	No	No	No
7,12 (2 Firms=6.1%)	Yes	No	No	Yes	No	No
9 (1 Firm=3.0%)	Yes	No	No	No	No	No
TOTAL FIRMS	5	0	3	2	2	3
%age FIRMS	15.2	0	9.1	6.1	6.1	9.1

Description of variables:
AUTOREPL-Partnership vacancies are automatically filled
DEPDEPT-Decision to replace or not depends on department etc.
CAPACIT-Usually replacement occurs to maintain capacity
EXPAND-Replacement occurs since firm is expanding
QUALPROF-Depends on balance between maintaining partner quality and firm profitability
RETPLAN-Retirements planned for in advance

In 28 firms, depleted partner numbers did not result in automatic replacement. In 3 of these firms retirements would generally be planned for and the necessary adjustments made, but automatic replacement need not necessarily occur. In 2 firms, it was mentioned that the necessity of maintaining profitability and quality of the partnership resulted in a trade-off situation. This means that a conflict can arise between the need to maintain the previous size of partnership in order to remain profitable and maintain capacity, and the fact that there are no suitable candidates to become partners. As a result, it may make sense not to replace. While this will maintain the quality of the partners (and the firm), it will cause capacity problems - this may be preferable to promoting to partnership someone who is not of sufficient quality, merely to maintain capacity. Of the 2 firms that noted this profitability/ quality trade-off, 1 also noted that typically replacement would occur since maintenance of capacity is usually crucial.

5 firms disclosed that automatic replacement would generally occur. 2 firms viewed this as necessary in order to maintain capacity with a similar number indicating this would occur as a consequence of the firm currently expanding and increasing capacity.

In this section, firms tended not to have a strict policy regarding replacement and firms typically provided answers to the question based on their experience of what had happened in past situations. The fact that very few firms had a formal policy regarding replacement is arguably indicative of a general desire of partners to restrict (not automatically replace or expand) membership numbers in order to maintain, or better, their own position within the firm. In this context, this could be seen as supportive of Hypothesis 7. which argues that firms may have a tendency to restrict membership, like the Labour Managed Firm (LMF), as this will preserve per member income. From TABLE 8.6 it is recalled that 4 firms created a category of senior associate between QA and partner. This could cynically be seen as an

attempt by partners to restrict their numbers for as long as is practicable, risking losing good QAs who may otherwise become disillusioned at the length of the pre-partner period.

It is the case that membership restriction can be effectively accomplished by partners by hiring non-membership labour (ie. more QAs and other employees) rather than extra partners. In the longer run, at least some of these additional QAs would require to be offered partner positions, or it is likely that they would leave the firm. A firm that consistently pushes up its partnership gearing, ie. increases its ratio of QAs to partners, will signal to its QAs that the pre-partner period will become longer and/ or the chances of becoming a partner will be reduced. As a result, highly geared partnerships may have to utilise permanent associate categories to sustain high gearing and/ or provide a more incentive rich career path for QAs in the pre-partner period. A firm perceived as opportunistically using QAs to over-gear the partnership, and doing this consistently, may tarnish its reputation - it could consequently find it difficult to attract good QAs since they would perceive little or no chance of partnership.

The replacement of partners in modern day firms also appears to be tied very much to the area of law in which the retiring/ leaving/ dying partner was specialised. Any partnership vacancy created will only be filled if there is still a demand for the services in which such a partner was specialised. In view of the fact that legal services have changed dramatically in contemporary lawyers' lifetimes, it is likely that certain areas of the law firm's businesses will be dying and others will be thriving. This change in emphasis is likely to result in mismatches between vacancies created and the need for partners in other expanding areas of the law firm's business. As a result, it is also likely to further obscure the issue of replacement/ non-replacement of partners.

3.7 The issue of partnership gearing:

(TABLE 8.8)

Firm No	AWARE	GEARRED	GEARINC	OVERALL	DEPTGEAR	TEAMGEAR
1,5,8,10,11,13,16,30, 31 (9 Firms=27.3%)	Yes	No	No	No	No	No
7,14,28,29,32 (5 Firms=15.2%)	Yes	No	No	No	Yes	Yes
23 (1 Firm=3.0%)	Yes	No	No	No	Yes	No
2,3,12,17,19,22,25, 27,33 (9 Firms=27.3%)	Yes	No	No	Yes	No	No
18,21,24,26 (4 Firms=12.2%)	Yes	No	No	Yes	Yes	Yes
4,6,20 (3 Firms=9.1%)	Yes	No	Yes	No	No	No
15 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	No
9 (1 Firm=3.0%)	Yes	No	Yes	Yes	No	No
TOTAL FIRMS	33	0	5	14	11	9
%age FIRMS	100	0	15.2	42.4	33.3	27.3

Description of variables:
AWARE-Firm is conscious of need to watch gearing
GEARRED-Gearing reducing ie. QAS:PTRS reducing
GEARINC-Gearing increasing ie. QAS:PTRS increasing
OVERALL-Attempt to maintain constant overall gearing
DEPTGEAR-Gearing varies between departments
TEAMGEAR-Gearing varies between teams

All firms indicated they were aware of the need to keep a close watch on gearing between partners and QAs to maintain their quality and profitability. In none of the firms interviewed was it the case that gearing was reducing (ie. the ratio of QAS:PTRS was reducing).

5 firms indicated the gearing of the overall firm was dependent on the gearing of individual departments and teams. Gearing was disclosed as varying across different work types, departments and teams dependent upon labour input requirements. 1 firm noted only that overall firm gearing was dependent on variations in gearing between individual departments.

13 firms disclosed they attempted to maintain the overall gearing of the firm, 4 of whom noted that gearing varied between both departments and teams within the firm. 5 firms noted their partnership gearing was increasing (ie. the ratio of QAS:PTRS was increasing). Of these 5 firms, 1 firm noted that gearing varied between departments of the firm and another disclosed that it attempted to maintain an overall partnership gearing.

One of the problems that became apparent when interviewing the firms was that, although firms were generally aware of the importance of gearing, the variation in 'ideal' gearing requirements across teams and departments resulted in difficulties for the firm in its attempts to maintain a fairly constant overall gearing between partners and QAs. Teams were particularly troublesome in this respect as, due to their fluid nature and the fact that they are temporarily formed to perform project type tasks, they can temporarily upset gearing in departments. This can upset gearing to such an extent that the remaining labour in the departments can become imbalanced with either 'too many chiefs and not enough indians', or too many inexperienced staff with no experienced leadership.

Many of the firms, although being aware of the partnership gearing and its importance, tended to possess the attitude that so long as it did not noticeably become too low or too high, it would take care of itself. It would only be if these limits were breached that alarm bells would ring, causing the firm to consciously seek to address the imbalance to avoid damaging the overall structure of the firm.

Hypothesis 6, which states the partnership gearing ratio (ratio of qualified assistants to partners) will be higher in larger firms/ corporate client firms, due to the requirement to work in teams and do so cost effectively, was tested and confirmed earlier in this thesis.

Chapter Eight - Endnotes

1. For an enlightening discussion of the concept of rank order tournaments see; Ricketts, M., The Economics of Business Enterprise: New Approaches to the Firm, Wheatsheaf, 1987.

2. It may be the case that trainees the firm hires have been employed during their time at law school during vacation and that this will enable the firm to make a more informed choice of which trainees to employ.

3. This is, however, a fairly haphazard process since the candidate will not be aware of the rules of the game - he, therefore, selects a strategy which he perceives will be most conducive to selection. At this early stage, effort can easily be directed in completely the wrong direction and an incorrectly selected strategy may have the opposite effect to that of increasing chances of selection.

See; Baker, G., Gibbs, M. & Holmstrom, B., Hierarchies and compensation - a case study, European Economic Review, 1993, Vol. 37, No. 2-3, pp. 366-378; O'Flaherty, B. & Siow, A., Promotion Lotteries, Journal of Law, Economics and Organisation, 1991, Vol. 7, No. 2., pp. 401-409; Drago, R., & Turnbull, G.K., Competition and cooperation in the workplace, Journal of Economic Behaviour and Organisation, 1991, Vol. 15, No. 3, pp. 347-364. These papers all serve to provide a good introduction to the role of internal labour market tournaments within organisations.

See also: Galanter, M. & Palay, T. Tournament of Lawyers - The transformation of the big law firm: Chicago (1991), which deals with the promotion to partner tournament in the specific case of the law firm.

4. For an introduction to signalling theory see; Gelatin, M., Search, Information and Market Structure in; Gelatin, M. and Leitler, R.D., Economics of Information. Martinus Nijhoff, 1981; Spence, M.A., Job Market Signalling, *Quarterly Journal of Economics*, August 1983, pp.355-374; Spence, M.A., Market Signalling- Information Transfer in Hiring and Related Screening Processes. Cambridge Mass., Harvard University Press, 1974.

5. This activity can have the paradoxical effect of reducing promotion chances - increased productivity is perceived by the employer that the candidate is better suited to his present job. In such a situation, attempting to demonstrate a high degree of ability within a current position, may convince the employer that the individual is ideally suited to that current post. Here, the individual's investment in information disclosure/ aptitude revealing, yields no personal returns, with the organisation capturing all of the gains of increased effort. Of course, in the longer run failure to attain promotion would be likely to become demotivating to that individual.

6. See; Goldberg, V.P., Relational Exchange: Economics and Complex Contracts, *American Behavioural Scientist*, Vol.23, No.3, pp.337-352, and more specifically; A Relational Exchange Perspective on the Employment Relationship, in Stephen (1984), for an exposition of his relational exchange framework and discussion of the concept of 'deferred compensation'.

7. Where firm scale is sufficiently large and specialisation/ functionalisation permits, it may be to the advantage of the firm to shuft around labour within the organisation to reveal their strengths and weaknesses and allow them to voluntarily and sub-consciously disclose aptitudes. This process will enable the employer to evaluate prospective contestants for particular jobs more easily, and in a more normal work setting which avoids forcing workers to work unrealistically hard temporarily. It may be desirable to hire an employee from the external labour market, even in the presence of firm specific capital, in order to break up unhealthy coalitions that may have formed. Such coalitions have the potential to appropriate rents away from the firm towards themselves. The introduction of an alien worker may also serve as a check on the quality and efficiency of the existing internal labour's work. In such cases there is a desire to reduce information impactedness to attenuate opportunistic possibilities.

8. The growth process of firms has long since been a topic of analysis of economists. For an early account of this process see, for example, Gibrat, R., Les Inegalities Economiques. Paris, 1931. Gibrat believed that the proportionate change in the size of a firm was independent of it's absolute size, and this law became known as 'the law of proportionate effect'.

9. See, Gilson, R. and Mnookin, R., Coming of Age in a Corporate Law Firm: The Implicit Contract for Associates, Stanford Law School Working Papers, No.42, 1988. For an interesting parallel situation in the case of incentives facing academics in Universities see; Carmichael, H.L., Incentives in Academics: Why is there Tenure?, Journal of Political Economy, Vol. 96, no. 3, 1988, pp. 453-472. In this paper, Carmichael examines the internal labour market process and the existence of tenure - which she argues is necessary since its absence would result in incumbents being unwilling to hire people who may actually transpire to be better than themselves. See also; O'Flaherty, B. & Siow, A., On the job screening, up or out rules, and firm growth, Canadian Journal of Economics, Vol. 25, No. 2, pp. 346-368, 1992; Waldman, M., Up or out contracts - a signalling perspective, Journal of Labour Economics, Vol. 8, No. 2, 1990, pp. 230-250; Kahn, C. & Huberman, G., 2-sided uncertainty and up or out contracts, Journal of Labour Economics, Vol. 6 No. 4, 1988, pp. 423-444; Tybor, Jr., What up or out means to women lawyers, American Bar Association Journal, 1983, Vol. 69, pp. 756-759.Other tangentially relevant papers which deal with the issue of tenure include: Topel, J., Specific capital, mobility and wages - wages rise with job seniority, Journal of Political Economy, Vol. 99 No. 1, 1991, pp. 145-176; Brown, J.N., Why do wages increase with tenure - on the job training and life-cycle wage growth observed within firms, American Economic Review, Vol. 79, No. 5, pp. 971-991.

10. It is simply naive to think that every solicitor has a universal desire to become a partner - some may prefer to practice law without the attendant pressures that accompany life as a partner in a law firm. Certainly, irrespective of this desire, remaining within the firm in a non-partner category is likely to be a far preferable option to a lawyer than being fired.

11. *supra* Note 9.

12. See, Klein, B., Transactions Cost Determinants of Unfair Contractual Relations, *American Economic Review*, Vol.70, 1980, pp.356-362.

13. *supra* Note 9.

14. *supra* Note 9.

15. See, Gilson, R. and Mnookin, R., Sharing Among the Human Capitalists: An Economic Enquiry into the Corporate Law Firm and How Partners Split Profits, Stanford Law School Working Papers, Vol.37, No.16, 1984. Gilson and Mnookin stress another important characteristic for lawyers to embody - namely a personal commitment to professionalism/ internally driven work ethic. In this paper this characteristic is viewed as mitigating lack of incentives in an income division system that emphasises purely risk sharing.

16. *supra* Note 9.

17. It will be recalled that the principle of short run perverse supply is that the existing profit sharing workers in the firm have an incentive to stop hiring other profit sharers, as this would counter a maximisation of net income per existing member objective. The firm has a natural inbuilt tendency to self extinguish in the long run.

18. *supra* Note 9.

19. In this case, and in many others, the problem of examining reputation effects is that any opportunistic behaviour commensurate with reputation dimensions must be assumed to be communicated with all parties who could be expected to play a part in the evaluation of such a reputation. It is not always the case that this occurs and as a result the market cannot efficiently evaluate reputations, with the strong possibility of systematic error being a prevalent feature.

20. See, Williamson (1985), for a discussion of credible commitments.

21. *supra* Note 9.

22. *supra* note 9.

23. *supra* Note 9.

24. *supra* Note 9.

25. *supra* Note 9.

26. The associate can record his own time anyway, as a check against the firm's records. These could be revealed among associates to determine whether the firm is prejudicing time-keeping records, to facilitate an opportunistic partnership decision. It is also unlikely that the firm would keep two sets of books, to attempt to support opportunistic partnership decisions, due to the importance of such records.

27. See, Gilson and Mnookin (1984), *supra* Note 15.

28. *supra* Note 9.

29. The *shirking* unproductive partner in this type of firm, will receive what he has earned - whereas in a *sharing* model firm, he will receive a *disproportionately* large proportion of the firm's income. In the productivity model, the amount will presumably be much lower than the productive partners' income, whereas in the sharing model, it will be the same as the productive partners.

30. *supra* Note 9.

31. See, Akerlof, G.A., The Market for Lemons-Quality Uncertainty and the Market Mechanism, *Quarterly Journal of Economics*, August 1970, pp.488-500.

32. *supra* Note 9.

33. *supra* Note 9.

34. This contrasts with the situation, outlined above where the argument was that there was an increased ability to monitor - all associates were treated alike until the partnership decision divided them into partners and permanent associates.

35. *supra* Note 9.

36. Consequently, it would be interesting to examine;

1. Whether firms which have two categories of associates have productivity based partnership sharing bargains and,

2. Whether firms, that have moved from sharing to productivity based profit division, process types of work particularly suited to lower quality lawyers.

37. If the details of such a typically difficult marriage can be agreed upon, it could be expected to be likely the newly created firm will have a fair chance of successfully weathering the fusion process. Due to each firm having a unique and strong firm culture, it is characteristically difficult to bring two firms together since they will both want to hold on to their own culture. This chauvinism makes the joining process difficult, promotes partnership instability and has been known in the recent past to cause subsequent demerger between what ostensibly appeared compatible firms.

38. See, Gilson, R.J. and Mnookin (1988), *supra* Note 9..

-Chapter Nine-

The Future Organisation of Law Firms - Theoretical and Empirical Analysis:

Section One: Alternative practising arrangements for lawyers in private practice:

Introduction:

Previous chapters have examined some of the characteristic features and problems of partnership practice for law firms, particularly large law firms. What follows is a discussion of alternative practice options which would be open to lawyers in private practice, contingent on removal of practising restrictions. The aim is to expose whether these problems are unique to partnership practice or whether they would remain in other organisational modes.

It is helpful to categorise differing organisational modes open to the lawyer in private practice. Within these options, certain organisational features determine and shape incentives facing the firm's agents - evoking differing behavioural responses where alternative contract specifications among the firm's agents (and their interaction) are expected to yield different resultant behavioural outcomes.

The unrestricted set of organisational options available are as follows:

1. Sole practice.
2. Law partnership.
3. Mixed professional partnership.
4. Corporate law firm.
5. Mixed corporate practice.

1.1 The organisational form as a structure of property rights:

It will be recalled from previous chapters that different organisational forms reflect alternative structures of property rights. Choice of organisational form specifies;

1. Potential advantages of further specialisation, or team production.
2. The extent to which exchange relationships, thus created, give rise to problems of moral hazard.
3. Returns to monitoring.
4. The trade off between risk sharing benefits and incentives.

A common element within all practice modes being considered is the presence of consumers and potential consumers of legal services. However, the type of client attracted by different types of firm may be different if it is accepted that certain structures are perhaps more amenable to particular aspects of legal business. Much debate surrounding the issue of

alternative practice modes appears to implicitly, and incorrectly, assume that legal services are a homogeneous output. Arguments largely fail to consider the major differences between private and commercial clients.

An organisational form which is too restrictive, may not permit the law firm to produce the kinds of legal services demanded by the modern consumer. Even if such services can be produced by the current form, they could perhaps be processed more effectively and efficiently through an alternative, but currently illegitimate, practice mode. It is precisely this type of argument that has prompted consideration of alternative practice modes for the legal profession. Present arrangements have been challenged as too restrictive, and increasingly incapable of meeting the dynamic changes in the market for legal services.

In the vast majority of cases the typical private consumer is unlikely to know what type of organisation his lawyer belongs to, whether he is a partner or a qualified assistant and may be unaware (even if he could discern between different organisational modes) what difference alternative practice modes make anyway.

There is a need to as fully as possible understand why current structure (sole practice and partnerships) has arisen prior to informed and rational consideration of other organisational forms. The easy answer to this question, in the context of the legal profession, is that it has arisen because all other forms are banned. It is necessary to take a further step back, however, and discover the rationale for creating restrictions in the first instance.

In taking a nexus of contracts view of the firm, each organisational option can be analyzed in terms of relations between the various, and sometimes wider set of, parties to the nexus of inter-related contracts. It is an examination of these relationships, which facilitates critical evaluation of the attendant problems and potential hazards of each practice modes. In simple terms, a move from sole practice to partnership through to incorporation has the effect of extending and widening the nexus of contracts at each stage. Mixed disciplinary practice (MDP), in either partnership or corporate form, similarly results in an expansion of contractual agents and specifications/ problems. In addition, such a move also involves the introduction of particular problems, through the introduction of members of other professions into the firm, the influence of their professional regulatory bodies and the demands of a new breed of multi-product customer.

1.2 Sole Practice:

In sole practice, the lawyer practices on his own and is thus the sole residual claimant. At present, sole practice is the only alternative option to partnership and is the far less common of the two practice options. As the sole residual claimant, the solicitor has full private

property rights within his practice.

There are numerous inter-related disadvantages to the sole practitioner;

1. Severe capital constraints (human and monetary),
2. Undiversified human capital investment with high risk,
3. Time constraints, limited attention span and cognitive limitations - information processing ability (bounded rationality),
4. Uncaptured potential economies of scale and scope, however limited,
5. Inability to realistically and effectively specialise in more than one (or a few) areas of the law - specialisation also further enhances risk.

The major advantages to the lawyer are;

1. He only has to monitor the small staff he employs - this may be relatively easy.
2. He receives all the fruits of his employees' efforts to transfer into the final service.
3. He has no mutual monitoring of partners to contend with, and,
4. He has the sole right to the residual of the firm.

He has direct control over his destiny, the future of the firm, his liability and his exposure through mal-practice to negligence claims - he has full and accurately specified private property rights.

The sole practitioner cannot offer much of a career opportunity for incoming members of the profession. They may find it difficult to attract other solicitors (as employees) as they find it impossible to offer competitive salaries. Consequently, it is difficult for the sole practitioner to expand his firm. Many lawyers commencing their careers may not wish to join a sole practitioner practice since there would be little or no prospect of becoming a partner of the original sole practitioner.

On weighing up the advantages and disadvantages of sole practice it is apparent that for the majority of lawyers it is not as attractive a practice option as partnership.

1.3 Partnership Practice:

This is by far the more common of the two practising options in the UK at present. This can be attributed to the twin benefits attainable through partnership;

1. Economies of scale and scope and,
2. Specialisation and risk sharing benefits revealed by portfolio theory [1].

Partnership permits a far greater capital (human and monetary) injection. Consequently, any economies of scale capable of being captured may be more fully exhausted, since a larger organisational scale is now viable. Our previous discussion of portfolio theory suggests that lawyers can diversify risks inherent in their human capital investments by forming a partnership with other lawyers.

Personal risk in legal service provision is relatively high since partner lawyers of the practice are residual claimants. The existence of joint and several liability is expected to reinforce the lawyer's commitment to ethical practice and attainment of high standards of quality in service. It is also expected that the jointness exhibited in this respect, will encourage mutual monitoring between partners of the firm. Full private property rights are attenuated in partnership to the extent that all partners in the practice will be residual claimants - as a result of partner's liability not only being exposed to personal malpractice, but also malpractice of fellow partners, there is a strong incentive created for mutual monitoring.

The residual income of partners now rests on the joint efforts of the whole team of partners and not merely on personal performance. Since low effort intensity is difficult to detect and assign to particular partners, it could be expected that an incentive to shirk is created - shirking being where a partner free-rides on efforts of other partners. It will be recalled, however, that effective partnership screening will screen out shirkers before they become partners.

The nature of the sharing bargain, will play an instrumental and central role in shaping partners' incentives within the firm. Inadvertently, through incompleteness in sharing bargain specification, incentives to shirk can be created (or at least remain unsuppressed). Such incompleteness may not be too much of a problem in partnership since it is expected that partners' propensity to shirk will be low due to ethical dedication and screening. It has been rehearsed at greater length previously why self-monitoring is expected to be relatively successful in the legal profession in general and in law firms in particular [2].

(I) The contract structure of the partnership:

The contractual structure of the partnership can be outlined as follows. Lawyers enter a contract with other lawyers which, firstly, specifies the sharing of practice incomes and, secondly, formalises joint and several unlimited liability between them [3].

Any residual shirking problems that exist, unconstrained by self and mutual monitoring can be mitigated (at least partially) by the nature of the sharing bargain, whereby partners' personal incomes are related to their effort intensity, or some proxy therefore.

It is advantageous for lawyers to construct productive teams with their colleagues to take advantage of benefits revealed by conventional economic theory, for instance, specialisation/ division of labour, and economies of scale and scope. A time constraint renders sole practice unattractive since it takes a long time, and much hard work, to start and develop a sole practice into a thriving business. Previous chapters have highlighted the fact that time costs for lawyers can be expected to be fairly high - there is a finite time in which to quickly recoup returns to protracted investments in human capital which is a quickly depleting asset.

(II) Non-partner labour units within the partnership:

It will be recalled from the previous chapter that hiring of labour in partnership will be done from both internal and external labour markets. It is expected that there will be a greater emphasis on promotion by internal promotion contests with a lesser reliance on lateral entry, particularly at partner level. Lateral entry via the external labour market may only apply in the minority of cases, particularly for partner positions. Lower level jobs may, however, be filled from the external market, eg. general employees and newly qualified graduates, with the majority of internal promotion occurring from QA to partner level. There will tend to be an identifiable hierarchy in partnership which runs from partners down through QAs to trainees, and down to general and ancillary staff.

All employees are essentially in a contract with the group of partners, rather than a faceless organisation, for the supply of their labour input. This may have the effect of enhancing the individual's effort intensity, due to a perceived direct accountability to higher hierarchical levels of the organisation - employees may recognise and respect the fact that partners have been through the organisation from lower levels to the top and consequently should be more able to objectively and effectively evaluate performance through experience [4].

(III) The size of partnership and monitoring processes:

The size of the partnership is limited to a certain extent by the wealth of the constituent partners, since the external capital market is inaccessible to partners who may collectively wish to expand the firm's capacity. However, it is expected that capital constraints will not be a significant problem facing the firm in this respect since by far the more important input to the firm is human capital and not monetary capital. As the size of a partnership grows, there is likely to require to be a divorce of ownership form real control within the firm, or at least a heightening of authority problems. These are a potential and likely consequence of pursuit of partnership growth and increased specialisation.

Where appropriate, different liability classes could be assigned to different authority levels to

check abuse of authority and constrain shirking. It is probable, however, that this would be as difficult to administer and control as the original authority problem itself, since control and monitoring problems are inherently complex. In any case, only qualified solicitors are permitted to share liability in legal partnerships.

Partnerships are more likely to evolve, where the monitoring process is itself routine and susceptible to some degree of accountability. They are not as likely to be formed where the effort of each partner is impossible to detect. Joint and several liability enhances the partners' incentives to monitor inter-alia, in the face of such monitoring difficulties. Rather than making the monitoring task any easier; joint and several liability simply enhances accountability. While it remains difficult for partners to monitor each other, it would be a fairly routine task for partners to monitor each other if they desired.

As the number of partners in the firm increases, the incentive to shirk increases, since it becomes increasingly difficult to detect low effort intensity of any one individual, and assign blame to the shirker. Such moral hazard problems are expected to be constrained by the incentive properties of the sharing bargain, partnership screening, and by the lawyer's internal monitor/ ethics.

The property rights of the firm's partners, who are unlimitedly jointly and severally liable for each other, are not freely tradeable. Transactional difficulties are inevitable here as a consequence of this, since partners have the authority to contract on each other's behalf. Potential problems of partners suing each other would have the effect of essentially cancelling risk sharing and mutual monitoring benefits - this could be expected to be a very rare and atypical situation. However, given the increased potential for problems the larger the partnership group becomes, partnerships, in many areas of work, have been limited in their growth potential by the imposition of sensible membership limits either in terms of regulatory requirements or the imposition of rigorous screening by partners.

(IV) Situations conducive to the formation of partnerships:

The size of the partnership can be restricted by the increasing cost of management and/ or increasing costs of monitoring shirking behaviour. Paroush (1985) argues that partnerships are more common in consulting services and function in this manner in order that consumers' time is saved and levels of fees are controlled [5]. It is also argued by Paroush that partnerships exist because non-sequential decision rules are preferred. An individual's demand for consulting services is seen by Paroush to be dependant on two factors [6]:

1. Cost of services.
2. Individual risk aversion.

Alchian and Demsetz (1972) argue that self-monitoring partnerships, rather than employer/ employee contracts, would serve to check excessive dilution of efforts through shirking more effectively [7]. Professional persons are argued to have the internal conscience to undertake this self monitoring. Paroush (1985) argues that partnerships, therefore, arise where the following features are relevant [8]:

1. The consulting process could be expected to increase users' expected benefits of using the service.
2. Where the verb 'to consult' is the applicable term to describe the productive process, ie. you 'consult' a lawyer.
3. Where the usual course of events is to obtain more than one opinion for the problem in hand. Here, the partnership is more likely to be formed since the consultant will back his judgement fully.

There could be expected to be time savings to the consumer - the nature of partnership is such that it is possible to consult more than one member to obtain an independent opinions. The creation of a forum where inter-partner advice is facilitated enhances the probability of a competent opinion being given, and thus enhances the user's expected benefits.

Skill variances within partnerships could be expected to be smaller than between different partnerships, and this could act to cut down freeriding/ shirking. It may be the case that partner lawyers may not shirk against their peers but may free-ride on lower levels of the firm's hierarchy. It is also the case that only crude and often meaningless measures of failure can be attached to the professional, for example, number of law suits lost, number of patient deaths, etc.

Partnerships are likely to develop with property rights invested in the individual person, rather than his position. Hence, residual claimant status is conferred on each team member and profit sharing schemes are likely to develop to distribute residual earnings. Jones (1983) argues that transactions costs determine the emergence of different systems of property rights and a resultant firm culture emerges [9]. 'Firm culture' can be viewed as synonymous with Williamson's (1985) notion of 'contractual atmosphere' and is also a crucial feature of Gilson and Mnookin's (1984) analysis of large US law partnerships [10].

(VI) Firm size as a limit on the success of firm culture as a transactions cost controller:

Jones (1983) argues that firm culture (trust laden atmosphere) developed through socialisation/ training/ education/ professionalisation etc., should limit severity of transactions costs within the firm [11]. Firm size, however, imposes limits on the success of firm culture as a

transactions cost controller. This is due to the following:

1. Increased team size increases the incentive to shirk, since it is more difficult and costly to detect and monitor.
2. Increased firm size almost definitely implies greater specialisation.

Jones (1983), therefore, predicts the result will be a move towards bureaucratic systems to manage the exchange process between professional employees [12]. The structure of property rights, he argues, will weaken to accommodate a different level of transactions costs. As a result, reciprocal exchange will tend to be replaced by exchange based more on hierarchical control and specialisation in management functions.

1.4 Mixed professional partnership/ Multi-disciplinary partnership (MDP):

Introduction:

Multi-disciplinary practice (MDP) involves members of the solicitors profession practising within the same organisation as members from other professions. The essence of problems MDP requires to solve stem from monitoring and screening difficulties.

MDP could be expected to provide professionals with a greater opportunity to diversify their human capital investments. This would, however, depend on the degree to which incomes from professional sub-units were correlated. More extensive specialisation may be facilitated, and achieved, without attendant risk increases.

(I) The contract structure of MDP:

In this organisational mode, members of the legal profession and members from other professions practice within one partnership. As a result, the firm's residual claimants come from diverse professional backgrounds. As with any partnership, partners will share joint and several liability, this representing a dilution of each partner's control over his property rights in relation to his residual claim. In a single profession partnership, partnership screening and mutual monitoring act as a constraint on the behaviour of the partners in relation to shirking and malpractice. In the MDP mutual monitoring and partnership screening are problematic.

(II) Difficulties of mutual monitoring in MDP:

Here, the problem stems from the fact that the residual claimants are from differing professional backgrounds. While individual partners may be generally able to mutually monitor partners from their own profession, they are unlikely to possess the requisite skills to monitor those from outwith their own profession. As a result, there is potential for..

professional sub-groups of the firm to free-ride on each other. MDP partners would also be deficient in ability to mutual monitor in relation to seeking to avoid acts that may be regarded as malpractice - which would thereby result in liability losses to the partnership. Essentially, three major problems face MDP partnerships as follows:

1. Individual partners have an increased incentive to shirk in the face of enhanced mutual monitoring difficulties,
2. Partners may be largely unwilling to share liability with relatively unknown quantities - lawyers cannot effectively screen persons from other professions seeking to become partners in the MDP firm. (joint and several liability is also inappropriate),
3. Divisional freeriding of sub-groups on other sub-groups of the firm may occur.

Now that three main disadvantages of MDP partnership have been identified, attention will be focused upon potential solutions to these problems.

(III) The importance of screening and selection of MDP members:

Just as is the case in sole-profession partnerships, the mutual monitoring problem in MDPs may not be an all pervasive problem, incapable of being overcome. The attractiveness (or otherwise) for some individuals to practice in MDP may be more dependant on the individual personalities in question rather than the professions to which they belong. In this respect, the problem is essentially the same as that which faces the legal partnership in its selection of new partners. As important as the monitoring function may be, the firm's screening and selection procedures are crucial to creating the desirable 'firm culture' discussed above (which will also be reinforced by each profession's individual socialisation process). Screening, monitoring, socialisation and firm culture are all inter-related and very important to the extent that they are jointly determinative of the behaviour of the professional persons involved. For example, certain lawyers would perhaps favour practising with some of the accountants they know than some of the solicitors they know.

In an organisation whose efficient operation rests upon the partners being able to self-monitor, selection of members who can be trusted to do this effectively irrespective of their professional backgrounds, appears to be the major concern of MDP organisation - and one which will largely determine the success or failure of such an organisation [13].

(IV) Personal indemnity (PI) insurance to circumvent liability problems:

The concept of joint and several liability does not entirely make sense within MDP. It would not appear sensible, for instance, that lawyers within the firm should be held personally liable

for a problem caused by the accountants within the same firm (or vice versa) should malpractice occur. The issue of liability sharing can be largely circumvented by the utilisation of PI insurance cover. The issue thereby shifts to the relative risks attending each sub-group, the resultant relative PI premiums and the issue of a willingness to cross subsidise in this respect between sub-groups of the MDP.

(V) Divisional autonomy and sub-group shirking:

In relation to the problem of sub-groups shirking and ability to mutual monitor, this problem already exists to a certain degree in the large law firm. This problem is characterised by divisions within the firm shirking on others. In the case of the large single profession law firm the attempted solution has been the imposition of more formal constraints on partners of the firm via a more mechanistic sharing bargain. This has manifested itself in more direct performance/ productivity measurement and tighter controls via departmental budgets and greater accountability etc.

In MDP the sharing bargain between the various members from different professions in the firm is likely to be extremely difficult to establish and police due to the wider and more diverse set of agents involved. In MDP the sharing bargain would require to be similarly designed to take into account the various professional sub-groups and how best to measure their productivity. Professional sub-group budgetary controls and the creation of individual cost centres could serve as more direct monitoring procedures. The more autonomous the professional divisions become as a consequence of these difficulties, the more blurred become the actual advantages of MDP that prompted its discussion in the first instance. This highlights the more general fragmentation - integration/ centralisation - decentralisation puzzle facing the typical modern firm in any industrial sector.

The expectation is that normal partnership reciprocal exchange would be replaced (or at least supplemented) by more costly and bureaucratic monitoring systems. These will be required to convince each of the firm's sub-groups that others are pulling their weight. This, of course, results in imposition of costs on the firm and is not particularly conducive to creating 'firm culture' - argued by Jones (1983) to control transactions costs within the firm [14].

There is likely to be still yet another different hierarchical structure within this type of organisation, with greater divisionalisation of tasks and sub-units. This would create a role for a central monitor who could overlook the functions of all professional divisions. A parallel can be drawn here between the functions of this central monitor and the functions performed by the head office in Williamson's (1985) analysis of the M-form corporation [15]. It is difficult to surmise exactly what form this central monitor would take but a partnership board would perhaps be the most likely practical manifestation of this concept.

(VI) Difficulties in the formation of MDPs:

There is the practical difficulty of whether members of different professions would be willing to practice with each other under one organisational umbrella. It has been demonstrated above that this unwillingness theoretically justifies itself in terms of enhanced monitoring and screening problems. Mutual monitoring and screening between professional sub-units, is problematic since each would be a relatively unknown quantity to the others. There is not only the situation whereby individuals shirk, but a further problem of sub-group shirking characterised by divisions within the firm freeriding on each other.

This would be likely to result in an unwillingness on the part of separate interest groups within the MDP to share liability with a relatively unknown quantity. However, it has been argued that use of personal indemnity (PI) insurance can circumvent this problem and, in tandem with selection procedures, well designed sharing bargains, and elements of divisional autonomy and accountability, MDP may still be a viable organisational option.

A more practical problem is that of deciding which professional body's regulatory rules should take precedence within the MDP to constitute a common professional code of ethical practice. This would require representations from the professions concerned drawing up common practice rules covering MDPs. The nexus of contracts is wider in this MDP organisation, because more than one profession is party to the contract of the firm. Each profession's regulatory body will now also be in contract with the organisation, and could be expected to wish to subject those practising therein to a common code of practice/ disciplinary procedure etc.

(VII) Solicitor fears concerning MDPs:

Solicitors have so far resisted the introduction of other professions within legal practice perhaps due to a fear they hold that large accounting and financial conglomerates could swallow them up. This, of course, would hail the end of the legal profession as we know it. MDP could, however, now be viewed as an effective way for the legal profession to defend itself - a defensive strategy to ensure survival in the long term.

A major fear of MDP voiced by many is the possible attenuation of professional ethics. This tends to be promoted by those lawyers who suffer from professional xenophobia. It can be argued that within any profession there is a widely accepted (and expected) uniform standard of ethical practice. It is difficult to see how solicitors, by practising in an organisation with members from other professions, would be likely to suffer from lower standards of professional ethics given the process of socialisation and professionalisation which has been argued to largely determine the self-regulation and self-monitoring nature of their behaviour

as individuals and as an overall professional group.

The cost of accountants hiring good commercial lawyers as employees is high and this high cost is paired also with a shortage in the supply of good lawyers, sufficiently qualified in the required commercial fields. It is difficult to see why it would be attractive to the typical lawyer to join an accountant's practice in such a position, given the lack of partner prospects, since he would be a lawyer 'alien' in an accountant's firm. Additionally, the job may be insufficiently varied and interesting when compared to private practice.

Consequent upon the introduction of MDP, the fear is that there will be problems of unfair client referral between departments. This is the source of the potential conflicts of interest between client and firm. A "Chinese Walls" solution can be advocated, where the important role of ethics in the professions, paired with a reliance on successful self-regulation, can be viewed as encouraging their likely success. These factors combine to provide an ideal setting for Chinese Walls to work - if these can be expected to work anywhere, then this is the ideal organisational setting where strong firm culture and other professional standards can be expected to obviate many such potential problems. Chinese walls could be expected to have a strong chance of success here if it is the case that, within the profession, a strong ethical code is upheld and honoured.

A combination of "Chinese Walls" and disclosure provisions could jointly act to frustrate unfair attraction of business between sub-units of a combined practice. With disclosure provisions, the consumer could be advised fully of the interests (and therefore conflicts of interest) of all parties in any specific transaction, and could further be advised that if he desires he has the option to pursue the next part of the service outwith the firm, or to continue in-house. The more risk averse the client is, the greater can be expected the tendency to favour the latter option, as this will avoid uncertainty of subsequent use of the market for the next transaction - this will economise on further search costs and the consumer may perceive the first mover advantages the current organisation will have [16].

The possible result of increased inter-professional ties could be the existence of supplier induced demand (SID) discussed previously, whereby organisational sub-units could collude in order to feed each other with work. This could be achieved by informing clients that this is the best option, when in reality it is really only the best option from the point of view of the firm. The organisational rules discussed above could go some way to frustrating potential problems that could occur.

(VIII) Areas of legal practice/ types of legal firm where MDP could be advantageous:

Theory discussed fails to provide any firm indications as to areas of legal practice or types of

legal work where MDP would be advantageous. As a result, it is intended that the empirical study will shed light on the potentials for MDPs within legal practice.

In order that MDP is to be understood and assessed, it is vital to determine potential jointness of professional services. If MDP is worth considering, it would be interesting to establish whether there would be an actual demand for joint services. If no effective demand exists, cost savings on the supply side may be the sole justification for their consideration. Theory would suggest that search costs and transactions costs facing consumers would be reduced, given the reduced number of contracts that would need to be entered. It is difficult to predict what effect this would have on the final price of services. Where close proximity and jointness in service provision exists, this could facilitate 'packaging' of service bundles which could be expected to reduce costs and prices of services. On the other hand, the consumer may be charged a premium for the reduced levels of uncertainty and lower search costs etc. involved in a 'packaged' service.

The typical MDP customer may be characteristically different from those of the typical conventional law firm. Commercial clients could be expected to require a wider range of professional services and on a more frequent basis than private clients. On the face of it they could, therefore, exert a demand on the services of the typical MDP. They could, however, be expected to require fairly specialised services that require use of particular specialist firms who may work together on an informal network basis in any case. Consequently; the commercial client may not actually want a professional 'supermarket' and specialist suppliers may prefer to retain flexibility by remaining separate nodes in a professional network fed by referrals and reputation effects.

In the domain of private clients, the story may be different - it may be attractive to the typical unsophisticated, risk averse client to obtain all his required services under one roof.

In any case, it is anticipated the empirical study will reveal areas of legal work and types of firm where MDP may offer advantageous features either to firms or clients (or both).

9.5 The Incorporated Law Firm:

Introduction:

The issue of incorporation of law firms is a puzzling one, much of the confusion fuelled by a misunderstanding or misconception on the part of those party to such discussions as to the implications of such a transformation for the firm involved. Traditional arguments for and against incorporation of solicitors firms from partnership have largely focused on issues such as taxation of profits or the appropriate limits to liability. These issues; although warranting discussion, largely eschew some of the more important factors surrounding incorporation.

Consequently, before examining these and other arguments it is useful to examine implications of organisational metamorphosis from partnership to incorporated legal practice.

(I) Implications of incorporation for the firm - divorce of ownership from control:

The normal simple corporate structure is where the owners of the firm are shareholders, and the controllers of the firm are the managers. Directors form an interface between these two parties, appointed by shareholders, but essentially representing dual interests. The traditional problem of this structure is the fact that due to the divorce of ownership from control, incentives are expected to be most usually incompatible between owners and controllers. This is further complicated by the role of the board who have their own interests to serve and also mediate between shareholders and managers.

Theoretically, controllers of the firm have an incentive to attempt to maximise their own interests and this is likely to be achieved by them attempting to maximise their incomes in both monetary and non-pecuniary terms. The owners (shareholders) of the firm have an incentive to attempt to maximise the capital and dividend returns to their equity investments and this is clearly achieved if the firm has a goal of maximising profits (along strict Neoclassical lines).

The traditional argument here is that there is room for managerial discretion in terms of managers behaving in a manner that is inconsistent with profit maximisation. It is not intended that a full discussion relating to this is entered into at this juncture - rather, the issues have at least been alluded to in passing [17]. Managerial discretion is analyzed at great lengths in the literature of managerial theories of the firm and literature of agency theory is also directly relevant here.

(II) Forcing at least partial alignment of owners' and controllers' incentives:

Agency theory argues, firstly, that managerial discretion would be penalised by the market and hence, the incentive for managers to engage in such behaviour would be attenuated. Secondly, the market would penalise firms that did not profit maximise since non-profit maximising behaviour would be reflected in reduced dividends to shareholders and a reduced share price which would leave the firm open to threat of takeover in the capital market.

Those in control of such a firm (managers) would thus be subject to greater risk of losing their positions in the event of takeover - even if a takeover situation did not occur, the market would discount the value of their services, making them less attractive for others to employ. It is argued that the combination of these factors and the efficient market will ensure broad alignment of incentives of owners and controllers of the firm and to a great extent these

problems will be obviated, or at least significantly diluted.

The basic problem with this efficient markets view of the firm is that the necessary information is not likely to be processed by the market with sufficient efficiency to bring about these effects. Indeed, it is questionable whether the market would receive some of these signals at all - even if they did, effective penalising of managers would be doubtful. Directors who monitor managers for shareholders will monitor managerial performance by assessing information obtained from managers themselves - there is an obvious problem of managers selectively passing on self-benefitting information and suppressing information which is not self-benefitting. Evaluation bias is endemic in the system and the efficiency and effectiveness of the monitoring process questionable [18].

(III) The move from partnership to incorporation for the law firm - divorce of ownership from control?:

In the case of existing law firms, the move to become incorporated would not change the nature of the firm to any great extent - the legal partnership transformed into a corporate legal practice would simply result in partners ceasing to be partners and becoming directors. Attention is then focused on who would be the shareholders in such a venture. There are basically two main options here;

1. The internally financed legal firm and,
2. The externally financed legal firm.

(i) The internally financed private corporate legal firm:

In this situation, the partners of the existing partnership would become directors and shareholders of the newly formed corporate legal practice. In this dual capacity, incentives facing them would essentially be the same as within partnership since they remain sole residual claimants of the firm. The system of property rights would not significantly change.

Essentially what would be created is a private corporate legal practice with no external shareholding. The lack of external shareholding has not traditionally been a problem for legal firms since they have successfully managed to rely on internal provision of capital - in any case human rather than monetary capital is the key input to the firm. It is the case, however, that in future, sources of external capital may become attractive or even necessary to facilitate legal firms to practice efficiently and effectively as large scale organisations.

The internally financed corporate legal firm could result from the following situations;

1. A prohibition on shareholding by anyone who is not qualified as a solicitor or,

2. A failure to attract external sources of capital in the absence of such a prohibition - the specific reasons why this situation may occur will be examined below in the section concerning externally financed corporate legal practice.

The profession has a obvious desire to create the first of these conditions, but it may be the case that this would automatically come about. This would be due to a lack of control over property rights/ residual claims by external shareholders - an examination of this will be preceded by a discussion of why the profession might wish to restrict shareholders in the corporate firm.

The profession has publicly intimated a desire to limit any shareholdings in incorporated legal practices to qualified solicitors only. This would appear to be to safeguard against outside interests creeping in and diluting control of practice by its lawyers. If the situation should arise where corporate practice was permitted subject to the condition that all shareholders required to be qualified solicitors, then the conventional divorce of ownership from control argument would not cease to become a problem. The functions of shareholders and managers/ directors would be combined in the same agents [19].

If there was a specific restriction on non-lawyer shareholdings, the law firm could forego potential expected benefits of employee share ownership - this being that employees' incentives are consequently made more compatible with those of the firm. This is achieved since employees' behaviour will be more aligned with profit seeking since this will have a positive and direct wealth effect for employees, as a portion of employee income will now be dependant on the profit levels of the firm. It is expected that a more loyal and productive workforce will be the result.

One potential area the law firm could benefit from employee shareholdings in this respect would be in retaining good QAs (who, as lawyers would be permitted to be shareholders) since their mobility would be reduced to the extent they held shares in the firm. Problems rehearsed at length in earlier chapters in relation to monitoring performance of and screening and selecting QAs would be to that extent reduced.

It may be the case that some problems demonstrated to result from the characteristic structure of partnership organisation would disappear upon incorporation.

(ii) The externally financed corporate legal firm:

If the situation came about where no specific restriction on shareholdings within a corporate legal firm existed, it would be possible for non-legally qualified persons to hold shares in such practices. It must be said, however, that the reasons why persons would wish to become

equity holders in such a firm are not obvious. Although profitability could be expected to be high, the ex-partners rather than external shareholders would attempt to appropriate the vast majority of profit towards themselves - in view of the fact that the importance of human as against monetary capital in the practice of law, this would appear to be justified.

From a monitoring perspective, such a shareholder is undoubtedly compromised in his ability to monitor performance of the firm's lawyers (far more compromised than other lawyers). It is recalled, however, that in the UK shareholders are characteristically apathetic - it may be the case that this inability to monitor is not a relevant consideration to the individual in any decision to become a shareholder in the firm. To that extent equity investment in the law firm may be no more or less attractive than investment in many other types of firm.

The returns that any shareholder could be expected to gain from holding equity capital in an incorporated legal practice would be dependant on the relative levels of external and internally provided capital. The internal providers of capital could be argued to have a vested interest in attempting to maximise the profits of the firm, to the extent that their personal incomes are correlated with firm profits (just as partners have in partnership). If their income is derived from profit in terms of dividends per unit of capital, then the incentives of shareholders in the firm are broadly aligned to those of the internal capital providers physically rendering the actual legal services. To that extent, external providers of capital, if they earn returns commensurate with their levels of capital input in relation to internal providers, could benefit from mutual monitoring between the worker-managers of the firm. The relevant factors here will be;

1. The proportion of capital provided internally in relation to externally,
2. The degree to which the worker-manager's income is determined by behaviour perceived as maximising firm profits,
3. The degree to which worker managers can enhance their income at the expense of the external providers of capital without being noticed.
4. The relative valuations of internally provided capital (human and monetary) and externally provided monetary capital.

To this extent, external capital providers could make fairly good returns on their investment as the high degree of worker-manager capital input provides incentives for the attainment of similar profit goals to those of the external capital providers. For the external capital provider, the law firm may be seen as a fairly safe bet as it is rare to hear of law firms going out of business and even rarer to come across a poor lawyer.

In the situation where capital is mostly provided by external sources, these providers of capital could be at the mercy of those within the firm who are controllers. The problems in

this type of externally funded firm would be essentially the same as those in the typical corporation discussed above at the start of the section concerning the corporate law firm. The difficulties would basically stem from the fact the such shareholders would face a difficulty of monitoring lawyers' performance in the firm [20].

In any case, whether there exists shareholder qualification requirements or not, the major interest in the firm could be expected to belong to those who control the firm (the ex-partners). To this extent, the primarily externally financed corporate law firm could be expected to be very rare, in the situation where it was a legal practice option.

Where there was a situation of absence of residual risk bearing status on the lawyer controllers of the firm, there would be little incentive for mutual monitoring between such individuals. An interface between the lawyers who control the firm and the external shareholders would be required as a central monitor. In the normal corporation, the board of directors perform this function. In this situation, however, it is the managers of the firm that pass directors information up through levels of the organisation. Such information can be filtered and shaped to suit the purposes of the managers. This type of managerial discretion, and its consequences for investors and employees, has prompted calls for both worker and shareholder participation on the boards of directors in corporations. In the corporate law firm, those permitted to sit on the board of directors would be a matter of strategic consideration.

The division of income of the practice would be a matter of agreement between these agents, as is the partnership sharing bargain under partnership. The relative sizes of directors shareholdings in the firm would be likely to be a feature of any profit sharing arrangement.

(IV) Limit of liability and corporate practice:

When incorporation is discussed in the context of law firms, it is usually perceived by lawyers as a vehicle to enable them to practice with limited liability. To a large extent, this misses the point as debate then tends to focus on whether practice with limited or unlimited liability would be appropriate for lawyers in incorporated firms. If client protection is high on the agenda in such a discussion, then the function of professional indemnity (PI) insurance largely renders discussion of appropriate levels of liability irrelevant.

In any case, the liability of lawyers within the firm, even if limited, would be questionable. Malfeasant lawyers could not hide behind the 'veil of incorporation' and would be held personally liable - creating essentially a similar situation to that which existed in partnership. The only difference would be that joint and several cross-partner liability would not apply.

At a cursory glance it would be easy to immediately render corporate practice with unlimited

liability an unviable option from the point of view of the individual lawyer. On the face of it, such a situation would expose practitioners of the firm to unacceptable risk of potentially massive corporate debt. Hence, this would appear to be an incompatible combination. It is, however, the case that in many of the large corporate legal service specialist partnerships at present, transactions which expose partners to potentially catastrophic levels of debt are freely entered into. The role of PI insurance as a supplement to joint and several liability is crucial, even in the partnership situation. Well defined PI insurance requirements would perform this role in the corporate firm.

Lawyers in a corporate practice could be expected to face greater incentives to shirk through attenuation of their property rights, via removal of residual risk bearing status within their guise of controllers of the firm. However, in their membership (shareholder) guise they would retain residual claimant status, and incentives would be retained in this direction. Joint and several liability would no longer exist, however, and this would be likely to result in a change in the individual lawyer's perception of risk, and maximum potential loss, of malfeasant practice. In the case of lawyers, limited liability could not assist malfeasant lawyers to recover their loss of prestige, and human capital, in the case of failure/ malpractice etc.

There is a fear that the removal of unlimited liability would reduce quality of legal services and it is argued that limited liability is inconsistent with the obligations of professional practice. It can be argued that the obligations of the individual should be such that they are upheld regardless of any exogenous change in practice mode. This is due to lawyers' practice methods being primarily influenced by personal rather than organisational conditioning, although firm culture remains an important feature.

In terms of property rights the removal of joint and several unlimited liability would, on the face of it, destroy incentives to mutual monitor and perhaps weaken incentives to practice with the same care as before. It is the case, however, that the lawyers in the practice would still wish to avoid negligent practice as this would damage;

1. The reputation of the firm and,
2. The reputations of those practising under the firm's name.

The issue of liability limits is clouded to a certain extent by the role that insurance plays. Insurance is playing an increasing role in legal services to protect the lawyer from potentially huge claims for negligence in handling a client's affairs. To this extent, what is important is not the limit to liability but rather the issue of PI insurance and whether the solicitor will continue to practice with the utmost of care in the presence of such a 'cushion'. The market could be expected to play a role here as the reckless lawyer could expect;

1. To find obtaining PI insurance cover increasingly difficult as he would be a high risk,
2. To pay higher premiums as a result of the higher levels of risk and,
3. To suffer reputation losses by practising recklessly and relying on PI insurance cover to mop up any mess that results.

It is not clear whether the abolition of unlimited liability would make practitioners more careful or whether they would become more reliant on their PI insurance cover should anything go wrong[21].

(V) The market for corporate takeovers in law firms:

The discussion of incorporation usually provokes discussion of takeovers - incorporation with external shareholdings allows the opportunity for takeovers to arise. At present there is a fair degree of merger and takeover activity between law firms. The problems of doing so in the current organisational setting are significant as partnerships tend to exhibit very unique and heterogeneous characteristics rendering it difficult to fuse two partnerships together and make them compatible. Since corporate law firms would tend to be private companies, the difficulties experienced in merging or taking over partnerships would largely remain.

Any creation of larger practices through incorporation and resultant mergers and takeovers, in areas of law that are amenable to this practice mode, could be expected to lead to increased concentration of these law firm types. This is not as immediate a worry as would have been the case if economies of scale applied across the board in legal services - where firms would wish to become larger, increasing concentration, reducing market coverage, and increasing areas of unmet need. The empirical study aims to delineate areas in which economies of scale are likely to be applicable in legal services and, hence, where creation of law-practices of a scale beyond that achievable under partnership is desirable [22].

(VI) The potential for incorporation in legal services:

Many see the potential for incorporation in terms of creating the correct environment for legal practices to grow to scales beyond that which partnership can cope with. Due to the fact that the partnerships if anything would merely change into private companies with partners becoming dual shareholder/ directors, problems of large scale partnership practice would remain. This problem is namely that there is reluctant delegation of decision making authority due to a desire to protect personal property rights. Incorporation, in the guise in which it would most likely occur, would do nothing to circumvent this problem.

It is argued that incorporation permits the organisation to be better structured but it is the

case that within partnership there is nothing to stop the partners forming such structures, other than the aforementioned problem of reluctant delegation of decision making authority. The introduction of incorporation would not change the extent of this reluctance.

Larger organisations are likely to be in a better position to undertake certain types of corporate work, which may involve using teams of staff and the use of substantial financial resources for long periods of time. In this respect it does not matter whether the firm is a partnership or a corporation, the limit on its size is the reluctant delegation problem again. Incorporation would not in itself facilitate practice on a larger scale.

It is argued that the personal/ confidential nature of legal services may render corporate practice inappropriate. This argument fails on account of the fact that trust is placed in the individual and not in the organisation. Hence, organisational form would not be expected to be determinative of the level of trust expected from the individual.

Several traditional arguments for incorporation can be identified;

1. Perpetual succession.
2. Centralisation of management.
3. Limited liability.
4. Transferability of interests.
5. Financial instruments.
6. Facilitation of commercial dealings.
7. Compensation systems.

Several disadvantages can also be identified;

1. Loss of flexibility.
2. Costs.
3. Inconsistency with professional obligations.

To a certain extent perpetual succession exists within partnership at present as the partnership name/ firm can last for several generations and can outlast a complete change in partners.

The centralisation of management in legal practice is a problem that incorporation does not solve. The firm's ability to centralise its management is quite independent of its organisational mode. It is dependent more on the willingness of its partners to give up some of their decision making authority to some more centralised decision making authority. It is thus a problem of residual claims/ property rights whose consequences, for reasons that have been discussed at-

length above, would not be changed by the most likely metamorphosis that partnership would experience (from partnership to private company).

The transferability of interests via shareholdings would be a potential advantage. Unless it were possible to transfer the shares within a family to another lawyer it is difficult to see who the shareholding could be sensibly transferred to.

The increased availability of financial instruments is only really an advantage if the partnership suffers from an inability to raise cash or capital. This has traditionally not been the case in the UK. The same would apply to the sixth advantage above as the typical legal partnership in the UK has not been compromised in its ability to enter into commercial deals.

In relation to the compensation systems argument it is not possible for partnerships to retain profits in the form of reserves. It is, therefore, not possible to even out good and bad years by retaining profit reserves in good years and releasing them in bad years. In this regard, compensation systems could become more flexible but this would likely merely serve to augment the sharing of profits problem that would still exist in the corporate form.

Any loss of flexibility disadvantage of incorporation would be a function of how the partners of the partnership formed the corporate firm. They could make it as flexible as the partnership was or as tight as company law will permit it to be. This would be a matter of choice for the partners.

There would be likely to be costs of transferring from partnership to a corporate form for the partners. The one-off tax burden due to the taxation of profits argument above would be perhaps the most significant cost.

In relation to the third disadvantage above, it can be argued that the nature of law school training, lawyer discipline and all pervasive ethics of the solicitor should render their practice methods largely independent of organisational form. Their standards of professional conduct should shine through in every situation.

(VII) The importance of the taxation system and partnership versus incorporation:

The taxation system in operation at a particular period of time may act to the advantage, or disadvantage, of particular organisational forms. At present, the tax situation between partnerships and corporate forms of organisations is fairly neutral and as a result choice between them is likely to be based on non-tax criteria. It was the case that previously the balance tipped in favour of incorporation but now the scales are balanced if not even slightly favouring partnership as against incorporation. The main problem with reference to the

taxation of profits, however, is that there would be a massive one-off tax burden for the partners by transferring their partnership into an incorporated practice [23].

(VIII) Issues regarding the quality of legal services post-incorporation:

The major capital assets of the legal partnership are owned by the partners in the form of human capital. It is perhaps inappropriate that upon incorporation the law firm should enjoy full attendant rights of incorporation. The full private property right to the human capital asset, in the case of the sole practitioner or partner in the partnership, could be expected to encourage the lawyer to take such steps as are necessary to protect these property rights.

It is expected that such an incentive is weakened through any attenuation of property rights. The actions of lawyers, after any attenuation, could be expected to be dependent on the degree to which any action/ non-action on their behalf would affect them either directly or indirectly through any consequent loss, or gain, to the firm. Here, the attenuation is essentially a form of a sale of partners' property rights to the firm.

A move from partnership to corporation (other than in private company form) could be expected to weaken many of those aspects of team production and self-monitoring systems present where like-minded people practice in a joint and several liability partnership team. In order that they could pursue similar objectives and initially form the firm, such persons would be well informed of each others' tendencies to shirk etc.

Incorporation could weaken those forces, in the case of the introduction of external shareholders and where limited liability was permitted since partners would no longer be personally responsible for each others' actions. Consequently, it could be expected that they need not take the same degree of care, or supply the same effort intensity demanded by fully held private property rights. In this situation, individuals need no longer confront the true cost of their actions. It is in this respect that some fear 'incorporation' could result in a tendency for lower standards of quality in legal services. This argument is, of course, dependant to some extent on the existence of external shareholdings, an attenuation of ex-partners property rights and reduced liability risks.

1.6. Mixed corporate practice:

In this practice mode, the advantages and disadvantages discussed in sections 1.4 and 1.5 above will be relevant. The actual form such a practice mode would take is as uncertain as is the case with incorporated legal practice and MDP. The interaction of the two sets of problems of these two practice modes when combined in mixed corporate practice may result in even greater practising problems. Alternatively, incorporation may solve some of the

potential problems of MDP partnership and to that extent the two may be complementary.

Section Two: Questionnaire Section Seven - The Future of The Profession:

2.1 Perceived advantages and disadvantages of alternative practice modes for law firms:

The concluding section in the questionnaire relates to current, ongoing attempts to reshape the profession. The viewpoints of various persons within the profession from differing types and sizes of firms were required in relation to the current proposals for change. It was thought this would help clarify areas where current restrictions act as a hinderance, and hence change would be advantageous and welcomed, and others where the current system can be viewed as facilitating service requirements of modern legal practice. Consequently, an empirical examination of the advantages and opportunities, and disadvantages and limitations, of each of the organisational forms (partnership, incorporated legal firm and MDP practice) is conducted below.

2.2 The importance of risk facing lawyers and their desire to practice with each other:

A determination of attitudes of lawyers to risks inherent in their human capital would be indicative of whether risk aversion was a significant determinant of a lawyer's desire to practice with other lawyers. Where they typically demonstrate indifference towards such risks there may be other more important perceived advantages of group practice. An important link established here is the issue of the appropriate degree of liability for legal practitioners and the use of the insurance market to diversify away elements of risk facing lawyers.

2.3 Issues surrounding quality in legal services:

A grave concern of many opponents to changes in practising arrangements is that a potential consequence could be worrying quality reductions in legal services. It is recalled from earlier chapters that the characteristic feature of legal services in this respect is that they are experience goods - as such, consumers face vast information deficiencies in evaluating quality ex-ante consumption. Indeed an unsophisticated client, as are most private clients (if not many commercial clients), may even face similar problems ex-post consumption.

The implication of the above is that the present study must take account of the diverse degrees of consumer sophistication that attend different classes of consumer, both at the level of theory and empirical analysis. The problem the study confronts here is that behavioural responses of the consumer, even recognising the aforementioned, must be assumed since the study does not directly ask consumers of legal services how they judge quality pre-purchase or evaluate quality post-consumption. The study, therefore, relies on the assumption that it may not be unrealistic to expect law firms to be a good judge of how consumers perceive

quality in legal services (if not second best to consumers themselves). The rationale behind this assumption is that such considerations must play a major part in firms' assessments of ways to attempt to attract business.

In doing so, the law firm must attempt to maximise factors it believes as being important to the consumer in his perception and evaluation of quality. To this end, it was thought to be of value to examine what law firms believed quality in legal services consisted of - Section Two of the questionnaire investigates quality signals. This information integrates law firm behaviour with the issue of quality in legal services, in the absence of a full blown survey of actual consumer opinion regarding what constitutes quality in legal services. Overall, the implications of organisational change regarding quality of legal services may be more easily predicted in the presence of such information.

2.4 Specific future of the Profession hypotheses to be empirically tested:

Hypothesis 1: The risk attending the lawyers human capital could be expected to render group practice with other lawyers an attractive option.

Hypothesis 2: The limits of partnership are likely to be determined by authority and delegation problems rather than capital or size problems.

Hypothesis 3: Incorporation of legal practices is not likely to yield significant advantages to the law firm.

Hypothesis 4 In the case of incorporated legal firms there will be a tendency to want to restrict membership of the firm to lawyers only due to property rights problems.

Hypothesis 5: In the case of Multi-disciplinary practice sharing of liability with other professionals will be unattractive due to monitoring and property rights problems.

Section Three: The Future of the Profession - Empirical Analysis of sample firms:

Introduction:

This section aims to provide an insight into some of the potential problems those interviewed feared may be a consequence of the introduction of new practice modes for solicitors.

3.1 The disadvantages of practising as a sole practitioner:

(TABLE 9.1)

Firm No	LACK SUPP	RISK SOLE	INAB SPEC	NOTP RAC	STAFF	OTHER 11
19,23,31 (3 Firms=9.1%)	No	No	No	Yes	No	No
2,4,11,16,20,21 (6 Firms=18.2)	No	No	Yes	Yes	No	No
8,24 (2 Firms=6.1%)	No	Yes	Yes	Yes	No	No
17,18 (2 Firms=6.1%)	Yes	No	No	Yes	No	No
22 (1 Firm=3.0%)	Yes	No	No	No	No	No
27 (1 Firm=3.0%)	Yes	No	Yes	No	No	No
32 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	No
5,6,9,10,12,13,26,28 (8 Firms=24.2%)	Yes	No	Yes	Yes	No	No
1,3,7,14,33 (5 Firms=15.2%)	Yes	Yes	Yes	Yes	No	No
25 (1 Firm=3.0%)	Yes	Yes	Yes	No	No	No
15 (1 Firm=3.0%)	Yes	Yes	No	No	No	No
30 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No
29 (1 Firm=3.0%)	M	M	M	M	M	M
TOTAL FIRMS	21	10	24	28	1	0
%age FIRMS	63.6	30.3	72.7	84.8	3.0	0

(M-Missing value)

Description of variables:
LACKSUPP-Lack of support
RISKSOLE-Exposure to high levels of risk
INABSPEC-Inability to specialise
NOTPRAC-Not practical today with volume & complexity of legislation
STAFF-Difficulty in attracting staff and retaining them
OTHER11-Other

A number of factors were identified by firms as disadvantages of sole practice. 28 firms thought being a sole practitioner was not practical nowadays due to the volume and complexity of legislation. The inability to specialise and focus down on particular areas of the law was revealed by 24 firms. 21 firms disclosed that lack of support from colleagues and inability to consult them would be a serious disadvantage of sole practice.

Only 1 firm indicated that it would be likely to be difficult to initially attract (and thereafter retain) staff in a sole practice situation. 10 respondents explicitly indicated a dislike for what they saw as exposure to high levels of risk associated with sole practice.

Given that clearly the sole practice option was seen by all but 1 of the firms (a missing value firm) to be an unattractive option, the next section aims to reveal whether partnership solves these disadvantages.

3.2 The advantages of practising in a legal partnership:

(TABLE 9.2)

Firm No	SPEC ADV	SUPP ORT	RISK SPRE	SYNE RGY	LTD EOS	GTTE CHIN	FINC ONT	GTCA PIN	RESR ISK	TEAM PROD	OTHER 12
17 (1 Firm=3.0%)	Yes	Yes	No	No	No	No	No	No	Yes	Yes	No
19 (1 Firm=3.0%)	Yes	Yes	No	No	No	Yes	No	No	Yes	Yes	No
6 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	No	No	No	No	Yes	No
2 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	Yes	No	No	No	Yes	No
32 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No	No	Yes	No	Yes	No
26 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	Yes	No	No	Yes	No	No
28 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	No	No	No	No	No
31 (1 Firm=3.0%)	Yes	Yes	No	Yes	Yes	Yes	No	Yes	No	No	No
11,13,18 (3 Firms=9.1%)	Yes	Yes	No	No	No	No	No	No	No	No	No
5,10,16 (3 Firms=9.1%)	Yes	Yes	No	No	No	No	No	No	No	Yes	No
4,9,12 (3 Firms=9.1%)	Yes	Yes	No	Yes	No	Yes	No	No	No	Yes	No
20,27 (2 Firms=6.1%)	Yes	Yes	No	Yes	No	Yes	No	No	No	No	No
3 (1 Firm=3.0%)	Yes	Yes	Yes	No	No	No	Yes	No	No	Yes	No
14 (1 Firm=3.0%)	Yes	Yes	Yes	No	No	Yes	Yes	No	No	No	No
7,24,25,30 (4 Firms=12.2%)	Yes	Yes	Yes	No	No	No	No	No	No	No	No
1,8 (2 Firms=6.1%)	Yes	Yes	Yes	No	No	Yes	No	No	No	Yes	No
15 (1 Firm=3.0%)	No	Yes	Yes	No	No	No	No	No	No	No	No
33 (1 Firm=3.0%)	No	Yes	Yes	No	No	Yes	No	No	No	No	No
22 (1 Firm=3.0%)	Yes	No	No	No	No	No	No	No	No	No	No
21 (1 Firm=3.0%)	Yes	No	No	No	Yes	Yes	No	No	No	No	No
23 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	Yes	Yes	No	No	No	No
29 (1 Firm=3.0%)	M	M	M	M	M	M	M	M	M	M	M
TOTAL FIRMS	30	29	10	10	6	16	3	2	3	14	0
%age FIRMS	90.9	87.9	30.3	30.3	18.2	48.5	9.1	6.1	9.1	42.4	0

(M-Missing value)

Description of variables:
SPECADV-Specialisation possible
SUPPORT-Supportive framework
RISKSPRE-Risk spreading
SYNERGY-Synergy
LTDEOS-Limited economies of scale
GTTECHIN-Greater technical input
FINCONT-Financial control
GTCAPIN-Greater capital input
RESRISK-Motivation through sharing residual risk bearing
TEAMPROD-team production
OTHER12-Other

With reference to advantages of practising within the partnership form of organisation, law firms interviewed provided the information contained in the table above. 30 firms felt that partnership provided an opportunity to specialise, and 29 indicated that partnership was a supportive framework from within which to practice law - this being strongly indicative of the existence of the alleged mutual consultation advantage of partnership. Similarly, 16 firms indicated that practising in partnership permitted partners access to the diverse and often extensive technical inputs brought to the firm by its partners - this is absent in sole practice.

14 firms specifically mentioned the team production advantages of group practice in partnership, with 10 firms mentioning the synergy aspects of the partnership practice mode. 10 firms noted the risk spreading role that partnership performed, with 6 firms mentioning (at least limited) economies of scale, 3 firms indicating greater financial control advantages, 3 firms indicating the benefits of motivation through sharing of residual risks, and 2 firms recognising advantages of greater capital input - as partnership advantages.

To summarise, the partnership mode of organisation was viewed by all firms (excepting the

missing value firm) as providing significant advantages over sole practice for lawyers in private practice.

From TABLES 9.1 and 9.2 it is apparent in the case of 10 firms that risk is perceived as a significant problem of sole practice. Additionally, risk spreading is a feature these firms perceive to be an advantage of partnership practice. This offers support to Hypothesis 1, which states that risk attending the lawyer's human capital could be expected to render group practice with other lawyers an attractive option.

It is, however, the case that many other features were identified as disadvantages of sole practice and advantages of partnership practice. As respondents were not asked to rank advantages/ disadvantages, it cannot be determined which are the most significant advantages/ disadvantages relevant in the choice of practice mode of the lawyer.

3.3 Limitations of partnership forms of organisation:

Now that advantages of the partnership mode over sole practice have been established, the purpose of this section shifts to attempting to discover potential disadvantages/ limits attending the partnership mode of organisation.

(TABLE 9.3)

Firm No	PART LIM	LTDL IAB	TRAD SHAR	STRU CLIM	SIZE LIM	CAPL IM	DECM AK	RELU CT	RESE RVE	BURD EN	CARE ER2	OTHE R13
2,3,5,8,9,10,12, 15,16,17,24,31 (12 Firms=36.4%)	No	No	No	No	No	No	No	No	No	No	No	No
28 (1 Firm=3.0%)	No	No	No	No	Yes	No	No	No	No	No	No	No
14 (1 Firm=3.0%)	No	No	Yes	No	No	No	No	No	No	No	No	No
11 (1 Firm=3.0%)	No	Yes	No	No	No	No	No	No	No	No	No	No
21,23,32 (3 Firms=9.1%)	Yes	No	No	No	No	No	Yes	Yes	No	No	No	No
7,27 (2 Firms=6.1%)	Yes	No	No	No	Yes	No	No	No	No	No	No	No
30 (1 Firm=3.0%)	Yes	No	No	No	No	No	No	No	No	No	Yes	No
6 (1 Firm=3.0%)	Yes	No	No	No	No	No	No	No	Yes	No	No	No
26 (1 Firm=3.0%)	Yes	No	No	No	No	No	Yes	Yes	Yes	Yes	No	No
18 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	No	No	No	No	No	No	No
22 (1 Firm=3.0%)	Yes	No	No	Yes	Yes	No	Yes	Yes	Yes	No	No	No
1,4,13,25 (4 Firms=12.2%)	Yes	Yes	No	No	No	No	No	No	No	No	No	No
20,29,33 (3 Firms=9.1%)	Yes	Yes	No	No	No	No	Yes	Yes	No	No	No	No
19 (1 Firm=3.0%)	Yes	Yes	No	No	No	No	Yes	Yes	Yes	No	No	No
TOTAL FIRMS	18	9	1	2	5	0	9	9	4	1	1	0
%age FIRMS	54.5	27.3	3.0	6.1	15.2	0	27.3	27.3	12.2	3.0	3.0	0

Description of variables:
PARTLIM-Partnership limiting
LTDLIAB-Unlimited liability is limiting
TRADSHAR-Inability to trade shares is limiting
STRUCLIM-Structure is limiting
SIZELIM-Size is limiting
CAPLIM-Capital access is limiting
DECMAK-Decision making is problematic
RELUCT-Reluctance to delegate authority is problematic
RESERVE-Inability to create reserves is limiting
BURDEN-Reduced working capital burden if outside equity permitted
CAREER2-Career structure and status groups are problematic
OTHER13-Other

12 of the firms interviewed (10 small/ medium firms and 2 large firms) indicated the partnership form of organisation suffered from no serious limitations. This is perhaps indicative that limitations are more likely to be reached and noticed in large firms rather than

in small ones. A further 3 firms (2 small/ medium firms and 1 large firm) initially disclosed they believed the partnership form of organisation did not suffer from limitations, but subsequently revealed limitations. Consequently, these firms will be treated as belonging to the group of 18 firms who did reveal limitations of the partnership mode in the context of legal practice. This brings the total of this group of firms to 21 (ie. 18+3), of which 7 are small/ medium firms and 14 are large firms.

9 firms perceived the existence of unlimited liability as a limitation on the practice of law from within a partnership nowadays. 9 firms disclosed that problematic decision making was a limitation, with the same 9 firms also complaining of an unwillingness of partners to delegate decision making authority. All of these 9 firms were large firms - not an unexpected result since, if decision making were to become problematic within a partnership, it would be more likely this would occur in a large firm.

5 firms viewed partnership size as a limitation of the partnership form, 1 of whom was paradoxically a small/ medium sized firm. In 4 firms (1 small/ medium and 3 large), the inability of the partnership to retain reserves out of partnership profits was held to be a limitation. The following limitations each enjoyed the response of only one firm; 1) the inability to trade shares in the organisation with others, 2) the difficulty of providing a career structure and the necessity to create different status groups, and 3) the burden of having to internally provide working capital.

2 firms indicated that the conventional/ characteristic structure of partnership was limiting. No firms indicated that an inability to access the external capital market was a problem of practising in the partnership mode of organisation. It can be concluded from the above information that evidence is supportive of Hypothesis 2, which states that limits of partnership are likely to be determined by authority and delegation problems, rather than capital or size problems.

3.4 The appropriate degree of liability for an incorporated law firm:

(TABLE 9.4)

Firm No	UNLTD	LTD	PIIMP	PERSLIA	ISSUE
4,11,13,18,19,22,24,27,29,33					
(10 Firms=30.3%)	No	No	Yes	No	No
23 (1 Firm=3.0%)	No	No	Yes	Yes	Yes
2,3,8,9,14,17 (6 Firms=18.2%)	No	No	No	Yes	No
1,12,20,21,25,28 (6 Firms=18.2%)	No	Yes	No	No	No
16 (1 Firm=3.0%)	No	Yes	Yes	No	No
15 (1 Firm=3.0%)	No	Yes	Yes	Yes	No
5,6,7,10,26,30,31 (7 Firms=21.2%)	Yes	No	No	No	No
32 (1 Firm=3.0%)	Yes	No	Yes	Yes	No
TOTAL FIRMS	8	8	14	9	1
%age FIRMS	24.2	24.2	42.4	27.3	3.0

Description of variables:
UNLTD-Unlimited liability
LTD-Limited liability
PIIMP-PI insurance is the important factor

PERSLIA-Personal liability since veil of incorporation will not protect anyway
ISSUE-Limited liability is only an issue if can no longer practice because cannot obtain PI insurance

The issue of the limit of liability appropriate for incorporated solicitors firms provoked very mixed responses. 10 firms saw the issue of client protection as being the important factor and to this end, requirements for adequate personal indemnity (PI) insurance cover overshadowed the issue of the appropriate degree of liability. 7 firms would have been satisfied to see the retention of unlimited liability, as presently exists in the partnership form.

6 firms reckoned that personal liability would exist even if limited liability was granted to corporate legal firms. This was based on their belief that the limit to liability would be in respect of trading debts, and not PI in respect of professional negligence. It would not be possible for the malfeasant solicitor in such a firm to attempt to hide behind the 'veil of incorporation' as this would not protect him from personal liability.

Another 6 firms believed that liability should be limited in the case of a corporate legal firm. The remaining 4 firms were all unique in their answers to this issue. All 4 were, however, united in their belief that the issue of PI insurance was the crux of the problem surrounding the question of liability for the incorporated law firm. One firm believed;

1. That limited liability would only become an issue if it became impossible for practitioners to obtain PI cover to enable them to practice and,
2. Personal liability would exist anyway as the veil of incorporation would not protect malfeasant solicitors in any case.

Two firms shared the view that the firm should be permitted limited liability. One of these firms, however, supplemented their view saying that they anticipated personal liability would overthrow this in certain circumstances. In the final firm, it was argued that the firm should retain unlimited liability as it was likely to be the case that malfeasant solicitors would be held personally liable in appropriate circumstances.

3.5 Areas of work/ types of firm where incorporation would be ideally suited:

(TABLE 9.5)

Firm No	NOTYPE	NOWORK	LARGE	PRIVCLI3	COMMCLI3	OTHER14
2,4,5,8,9,13,14,15,16,18, 19,20,21,22,23,24,26,27, 29,30,31,32,33 (23 Firms=69.7%)	Yes	Yes	No	No	No	No
7 (1 Firm=3.0%)	Yes	Yes	Yes	No	No	No
10,17 (2 Firms=6.1%)	No	Yes	Yes	No	No	No
11 (1 Firm=3.0%)	No	Yes	No	No	Yes	No
1,12 (2 Firms=6.1%)	Yes	No	No	No	Yes	No
3 (1 Firm=3.0%)	Yes	No	No	No	No	No
28 (1 Firm=3.0%)	No	No	Yes	No	No	No
6 (1 Firm=3.0%)	No	No	Yes	No	Yes	No
25 (1 Firm=3.0%)	M	M	M	M	M	M
TOTAL FIRMS	27	27	5	0	4	0
%age FIRMS	81.8	81.8	15.2	0	12.2	0

(M-Missing value)
Description of variables:
NOTYPE-No type of firm
NOWORK-No area of work
LARGE-Very large firms
PRIVCLI3-Private client firms/ work
COMMCLI3-Commercial client firms/ work

Overall, the concept of incorporated solicitors firms largely failed to grab the attention of many firms. 27 firms envisaged no type of firm, and an identical number envisaged no area of work, ideally suited to corporate practice. Of those firms, 24 of them saw no type of firm or area of work in which corporate practice would be ideally suited - only one of these firms conceded it could perhaps be envisaged that incorporation may yield advantages in particularly large firms.

Of all other respondents, another 4 firms shared this belief that large firms may benefit from the ability to practice in a corporate form, bringing the total of firms who shared this view to 5. 4 firms indicated that commercial client oriented firms may similarly benefit, mainly I suspect as a result of their probable scale rather than legal specialism. What is intriguing is that the 4 firms who thought that commercial client oriented firms may benefit from incorporation, were actually small/ medium sized firms with a definite bent towards private client work. Likewise, 4 of the 5 firms that believed incorporation may of benefit to large firms, themselves were small/ medium sized. It can be concluded from the above analysis that, as Hypothesis 3. states, incorporation of legal practices is not likely to yield significant advantages to the law firm.

3.6 The likely shareholders in an incorporated legal practice:

(TABLE 9.6)

Firm No	PREVPART	EMPSHAR	OUTEQUIT	LAWONLY	OUTFUT	OTHER15
1,2,4,5,6,7,8,9,11, 12,14,15,17,18,19, 21,22,23,24,25,26, 27,29,30,31,32,33 (27 Firms=81.8%)	Yes	No	No	No	No	No
16,28 (2 Firms=6.1%)	Yes	No	Yes	No	Yes	No
3 (1 Firm=3.0%)	Yes	No	Yes	No	No	No
13,20 (2 Firms=6.1%)	Yes	Yes	No	No	No	No
10 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	No
TOTAL FIRMS	33	3	3	0	3	0
%age FIRMS	100	9.1	9.1	0	9.1	0

Description of variables:
PREVPART-Previous partners
EMPSHAR-Employee share ownership
OUTEQUIT-Outside equity interest
LAWONLY-Legally qualified persons only
OUTFUT-Outside equity interests perhaps further in future
OTHER15-Other

In all 33 firms, it was the case that the partners were anticipated to become the directors/ shareholders in the new corporate firm transformed from partnership. In only 6 cases was it envisaged that shareholding could extend beyond this. In 3 of these 6 firms it was envisaged that this could be extended by employees holding shares in the corporate firm. In one of these

3 firms it was indicated that this could perhaps be extended still further to include external equity interests - this was argued, however, to be much further in the future, if at all. The other 3 firms argued that outside equity interests may be permissible at present, but it was conceded by 2 of these firms that outside equity interest may only be an issue much further in the future.

In the main, it is demonstrated above, as Hypothesis 4 states, that in the case of incorporated legal firms, there will be a tendency to want to restrict firm membership to lawyers only as a result of property rights problems. Thus, evidence supports acceptance of Hypothesis 4.

3.7 Potential disadvantages of incorporated solicitors firms:

(TABLE 9.7)

Firm No	DISADINC	DISADLTD	CONFOI	PROFSTAT	ONEOFF	OTHER16
4,6,8,14,20,21,29,31						
(8 Firms=24.2%)	No	No	No	No	No	No
11 (1 Firm=3.0%)	No	No	No	No	No	Yes
15 (1 Firm=3.0%)	No	No	No	No	Yes	No
9,16,18,19,22,24,30						
(7 Firms=21.2%)	Yes	No	No	No	Yes	No
2,27,28 (3 Firms=9.1%)	Yes	No	No	No	No	Yes
7,12 (2 Firms=6.1%)	Yes	No	No	Yes	No	No
13 (1 Firm=3.0%)	Yes	No	No	No	No	No
23,25,32,33						
(4 Firms=12.2%)	Yes	No	Yes	No	No	No
3 (1 Firm=3.0%)	Yes	No	Yes	No	No	Yes
26 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	No
5,10,17 (3 Firms=9.1%)	Yes	Yes	No	No	No	No
1 (1 Firm=3.0%)	Yes	Yes	No	Yes	No	No
TOTAL FIRMS	23	4	6	3	9	5
%age FIRMS	69.7	12.2	18.2	9.1	27.3	15.2

Description of variables:
DISADINC-Disadvantages of incorporation exist
DISADLIA-Limited liability may put clients off
CONFOI-Conflict of interests
PROFSTAT-Professional status compromised
ONEOFF-Oneoff tax burden due to differences in taxation of profits
OTHER16-Other

In relation to the issue of disadvantages of incorporated solicitors firms, a strong theme emerged throughout respondents - although there were not really any significant disadvantages, it was difficult to perceive just exactly what the advantages were. 8 firms mentioned that they perceived no disadvantages of incorporation whatsoever.

A total of 9 firms disclosed the one-off tax burden a transformation from partnership to corporate form would impose on partners, as a significant disadvantage - this burden would arise as a consequence of differences that currently exist between taxation of partnership profits and taxation of corporate revenue.

6 firms viewed the potential conflicts of interest that could arise from incorporation, as being a disadvantage to incorporation. 4 firms thought that if incorporation was permitted with limited liability then clients could be put off by "Ltd" being attached to the firm name. 3 firms thought that practising as a solicitor within an incorporated legal firm compromised the

professional status of solicitors and as such, was a disadvantage of incorporation.

The 5 firms that appear in the OTHER16 column in the above table provided these additional disadvantages;

1. Dilution of control and monitoring problems where external shareholders existed,
2. Less friendly atmosphere in the firm as partner camaraderie would be lost,
3. Lawyers would be more mobile as directors than as partners of the firm and,
4. The same decision making problems would exist in the corporate form that did in partnership, ie. reluctance to delegate and inefficient decision making.

In view of the disadvantages expressed above by respondents, it is apparent that, not only do few significant advantages to incorporation over partnership exist, but also potential problems/ disadvantages of incorporation exist. Some disadvantages of partnership, which incorporation is often viewed as solving, would actually be shared features of incorporated and partnership law firms. Most significant is that decision making and reluctance to delegate decision making authority (heralded as a disadvantage of partnership) would simply re-emerge in an incorporated practice - offering additional support to Hypothesis 3.

3.8 Firm types and work types where MDP would be advantageous:

(TABLE 9.8)

Firm No	MDPADV	MDPTYPE	MDPWORK	LESSSOPH	MDPPRIV	MDPCOMM	INCMDP	RURALMDP	PROPMDP	FINMDP	PATMDP	MULTINAT	CONFED	NETWORKS	OTHER17
3,18,27,28,31 (5 Firms=15.2%)	No	No	No	No	No	No	No	No	No	No	No	No	No	Yes	No
8,23 (2 Firms=6.1%)	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No
26 (1 Firm=3.0%)	No	No	No	No	No	No	No	No	No	No	No	Yes	No	Yes	No
33 (1 Firm=3.0%)	No	No	No	No	No	No	No	No	No	No	No	Yes	Yes	Yes	No
29 (1 Firm=3.0%)	Yes	No	No	No	No	No	No	No	No	No	No	Yes	No	Yes	No
22 (1 Firm=3.0%)	Yes	No	No	No	No	No	No	No	No	No	Yes	No	No	Yes	No
2 (1 Firm=3.0%)	Yes	No	No	No	No	No	Yes	No	No	No	No	No	No	No	No
1,9,13,14 (4 Firms=12.2%)	Yes	No	Yes	No	No	No	No	No	Yes	Yes	No	No	No	Yes	No
10,17 (2 Firms=6.1%)	Yes	No	Yes	No	No	No	No	No	Yes	Yes	No	No	No	No	No
12 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No	No	No	No	Yes	No	No	Yes	No
16 (1 Firm=3.0%)	Yes	No	Yes	No	No	No	No	Yes	Yes	No	No	No	No	Yes	No
7 (1 Firm=3.0%)	Yes	No	Yes	No	No	Yes	No	No	Yes	Yes	Yes	No	No	No	No
11 (1 Firm=3.0%)	Yes	No	Yes	No	No	Yes	Yes	No	Yes	No	No	No	No	Yes	No
4,5 (2 Firms=6.1%)	Yes	No	Yes	No	Yes	No	No	No	Yes	Yes	No	No	No	Yes	No
30 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	Yes	No	No	No	Yes	No	No	No	Yes	No
19 (1 Firm=3.0%)	Yes	No	Yes	No	Yes	Yes	No	No	Yes	Yes	No	Yes	No	No	No
20,21 (2 Firms=6.1%)	Yes	No	Yes	Yes	Yes	No	No	Yes	Yes	Yes	No	No	No	Yes	No
6 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	No	No	No	No	Yes	No	No	No	Yes	No
15 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	No	No	No	Yes	No	No	No	No	No	No
32 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	No	No	Yes	No	No	No	No	No	Yes	No
24 (1 Firm=3.0%)	Yes	No	Yes	Yes	Yes	No	No	Yes	Yes	Yes	No	Yes	No	Yes	No
25 (1 Firm=3.0%)	Yes	M	M	No	No	No	No	No	No	No	No	No	No	No	No
TOTAL FIRMS	24	0	20	6	10	4	2	5	16	15	2	5	1	24	0
%age FIRMS	72.7	0	60.6	18.2	30.3	12.2	6.1	15.2	48.5	45.5	6.1	15.2	3.0	72.7	0

(M-Missing value)

Description of variables:
MDPADV-Advantages of MDP
MDPTYPE-Ideal types of firm exist for MDP
MDPWORK-Ideal types of work exist for MDP
LESSSOPH-MDP good for less sophisticated clients
MDPPRIV-MDP good for private client work

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MDPCOMM-MDP good for commercial client work
INCMDP-MDP good if combined with incorporation
RURALMDP-MDP good in rural areas
PROPMDP-MDP good in property transactions
FINMDP-MDP good in personal financial services
PATMDP-MDP good in patents work
MULTINAT-Multinational practice is more attractive than MDP
CONFED-Confederations of solicitors is more attractive than MDP
NETWORKS-Networking is sufficient and has many of the advantages of MDP without the problems
OTHER17-Other
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24 firms noted that potential advantages of MDP existed. 17 of these firms also, however, disclosed that existing informal networking works well and that it offers many of the advantages promised by MDP, only without the accompanying problems. A further 7 firms who envisaged no advantages of MDP, also argued that networking was sufficient, bringing this total to 24 firms.

No firms identified particular types of firm which would be ideally suited to MDP, but 20 identified work areas that would be amenable to MDP. 10 firms thought MDP would be good for private client work, 7 of which paradoxically were large commercial based firms. 4 firms anticipated that MDP would be amenable to commercial client work, 2 of whom paradoxically were small/ medium private client oriented firms. 6 firms believed MDP may be advantageous where dealing with less sophisticated clients. Paradoxically, 4 of these firms were large commercial firms, who dealt mainly with sophisticated, well-informed clients.

2 firms believed that the advantages of MDP could perhaps be more fully exploited if it was combined with incorporation. 5 firms indicated that perhaps MDP would be better in the context of rural areas as these communities may have more of a demand for the one-stop shop idea. Again, paradoxically it was the case that this view came from firms of whom 4 out of 5 were large City firms, and all of whom had no experience of rural practice.

In 16 of the 33 firms, MDP was expected to yield advantages in the case of property transactions of all types, primarily due to the compatible nature of the professional inputs typically attending such transactions. The other major area of business thought to be amenable to MDP and yielding potential benefits was that of personal financial services. This area of amenable business was noted by 15 of the 33 firms, whilst only 2 firms noted the applicability of MDPs in relation to patents work.

Amongst the large firms, 5 firms indicated that multi-national/ transnational linkups between law firms offered greater appeal than MDP. 1 of these firms additionally indicated that confederation arrangements between UK solicitors would also be a more attractive area of practice innovation than MDPs.

Overall, although the concept of MDP held greater appeal to a wider set of firms than did incorporation, there was still by not by any means overwhelming enthusiasm for MDPs. Firms tended to look upon MDP as yielding potential benefits for firms other than their own,

often without appearing to fully appreciate of understand the nature of other firms' business. The strongest message received when interviewing firms was that informal networking between professionals from different professional disciplines appeared to work well currently. Firms were quick to point out that this avoided many of the potential problems envisaged in the MDP situation.

3.9 The attractiveness of sharing liability with other professionals in an MDP:

(TABLE 9.9)

Firm No	LIABUNAT	LIABNOT	NECEVIL	RULESPI	PERSONN2
4 (1 Firm=3.0%)	No	No	No	Yes	No
1 (1 Firm=3.0%)	No	No	Yes	No	No
7,13,14 (3 Firms=9.1%)	No	Yes	No	Yes	No
25 (1 Firm=3.0%)	No	Yes	No	No	No
6 (1 Firm=3.0%)	No	Yes	No	No	Yes
2,3,8,9,11,15,16,18,19,20,21, 22,23,26,27,28,29,30,31,32,33 (21 Firms=63.6%)	Yes	No	No	No	No
17 (1 Firm=3.0%)	Yes	No	No	Yes	No
24 (1 Firm=3.0%)	Yes	No	No	Yes	Yes
10,12 (2 Firms=6.1%)	Yes	No	Yes	Yes	No
5 (1 Firm=3.0%)	Yes	No	Yes	No	No
TOTAL FIRMS	26	5	4	8	2
%age FIRMS	78.8	15.2	12.2	24.2	6.1

Description of variables:
LIABUNAT-Liability sharing unattractive
LIABNOT-Liability sharing not unattractive
NECEVIL-Liability sharing a necessary evil
RULESPI-Would depend on the practice rules and PI requirements
PERSONN2-Would depend on the personnel in question rather than the profession to which they belong

Partners in the study were asked whether they would find sharing liability with non-lawyers, in an MDP situation, attractive or unattractive. 26 respondents indicated they would find liability sharing with non-lawyers unattractive, 5 indicated that it would not be unattractive, 1 said it would depend on the PI rules drawn up to regulate MDP, and 1 indicated that it would be a necessary evil if one wanted to practice from within a MDP.

4 firms in total indicated that liability sharing would be a necessary evil, 8 disclosed that the attractiveness/ unattractiveness of liability sharing would be dependent on the PI rules drawn up, and 2 indicated that it would depend on the personnel in question, rather than the profession to which they belonged.

Only 1 firm unconditionally indicated that liability sharing would not be unattractive, with the 4 others that indicated it would not be unattractive, conditioning this answer as described in the paragraph above. The 2 firms that did not indicate whether they would find it unattractive or not unattractive, also conditioned their answers as in the paragraph above. 21 firms unconditionally indicated that they would find liability sharing unattractive, with an additional 5 conditioning this response as described in the table.

This evidence is persuasive of the validity of the view of Hypothesis 5, which proposes that, in the case of a MDP, sharing of liability with other professionals will be unattractive due to

monitoring and property rights problems.

3.10 Potential practice problems in MDP organisations:

(TABLE 9.10)

Firm No	CONFLICT	SWALLOW	SOPHCOMM	COMPLOSS	DESIGN	OTHER18
7,8,10,12,13,15,16,17,29						
(9 Firms=27.3%)	No	No	No	No	No	No
27 (1 Firm=3.0%)	No	No	No	Yes	Yes	No
6,24,31 (3 Firms=9.1%)	No	No	Yes	No	No	No
20,21,25 (3 Firms=9.1%)	No	No	Yes	No	Yes	No
14,19 (2 Firms=6.1%)	No	Yes	No	No	Yes	No
9 (1 Firm=3.0%)	No	Yes	No	No	No	No
11 (1 Firm=3.0%)	No	Yes	No	Yes	No	No
28 (1 Firm=3.0%)	No	Yes	Yes	Yes	Yes	No
1,2,5,32 (4 Firms=12.2%)	Yes	No	No	No	No	No
3,22,23,33 (4 Firms=12.2%)	Yes	No	No	No	Yes	No
18,26 (2 Firms=6.1%)	Yes	No	Yes	No	Yes	No
4 (1 Firm=3.0%)	Yes	No	Yes	No	No	No
30 (1 Firm=3.0%)	Yes	Yes	No	No	Yes	No
TOTAL FIRMS	12	6	10	3	14	0
%age FIRMS	36.4	18.2	30.3	9.1	42.4	0

Description of variables:
CONFLICT-Conflict of interests
SWALLOW-Legal firms swallowed up by large accountancy firms
SOPHCOMM-Sophisticated commercial clients do not want them
COMPLOSS-Loss of healthy competition between professional groups
DESIGN-Designing and administering common practice rules
OTHER18-Other

In relation to potential problems arising in the situation of MDP, the above information was collected. The most common problem identified was that of practicalities involved in attempting to design and administer a common set of practice rules which would legitimately regulate all who practised within a MDP firm. This was indicated by 14 of the 33 firms.

In 12 firms, the potential conflict of interests which would be likely to occur in MDP practices was seen as a potential problem. 10 firms noted that sophisticated clients do not want MDPs since such clients tend to prefer to use 'horses for courses'. This concern was particularly evident within the large commercial firms, who constituted 8 of the 10 firms disclosing this as a problem. 3 firms actually voiced concern over the loss of healthy competition that would result from the creation of these MDP firms.

Section Four: Future Characteristics of Law Firms and Legal Practice:

Introduction:

It is naturally very difficult to predict the likely future characteristics of the organisation of law firms and legal practice at present given uncertainty surrounding the nature and extent of proposed changes [24]. In view of uncertainty surrounding which of the proposed changes will be implemented and what form they will constitute, the following can be regarded as a personal view of likely future characteristics based upon information drawn from the empirical study:

4.1 Predictions regarding the future of the UK legal services market:

(I) It is likely the current trend for the profession to split into two specialist divisions with small firms serving private clients and large firms serving commercial clients will become more pronounced. This has been, and will continue to be, a necessary consequence of the increase in volume and complexity of legislation (particularly on the commercial side) necessitating teams of specialist lawyers practising as sub-units of large firms (especially in large commercial contracts). Consequently, commercial firms will tend to develop on larger scales developing a portfolio of specialist services, with greater internal specialisation and divisionalisation, allocating work to fluid teams of its membership almost like projects.

Smaller firms will become more specialised by narrowing down their focus onto their core area of legal business. Larger firms will also tend to become more selective in terms of the work they are willing to take on and will generally wish to get rid of their private client base. This, combined with a desire of the small private client to have a more personal service, will result in more specialist allocation of private clients to smaller firms and commercial clients to large firms.

Among both commercial and private client work areas, smaller boutique type firms will develop to serve particular niche markets they have secured a foothold in and which can be regarded as their area of specialist competence.

(II). To facilitate necessary scale increases larger firms will increasingly look beyond traditional internal methods of increasing partner numbers. Hence, among large firms, it is likely there will be an increasing tendency to headhunt partners/ teams/ departments etc. from other firms and use bolt-ons and mergers to increase scale. There may also be an increasing tendency for larger commercial clients to develop their own in-house legal departments where this is viable and makes sense. This would present increased alternative employment opportunities for lawyers outwith law firms. The upshot of these combined tendencies would be that lawyers would enjoy more occupational mobility than was previously the case due to greater opportunities both outwith the firm in other law firms, and in other non-law firm organisations [25].

The advent of larger firms is also likely to create a situation where there will exist lawyer categories within the firm beyond the simple partner/ qualified assistant distinction, for example, permanent associates and salaried partners. These will help the law firm maintain an important screening function and also provide alternative career paths for QAs who do not wish to become partners.

(III). Should regulation change to permit MDP, it is unlikely that MDPs will become popular

practice modes, especially among large firms and those in commercial client areas of work. Depending on the nature of regulations surrounding MDP it could be possible that solicitors' firms would be swallowed up by, for example, the large accountancy conglomerates. This could threaten the future of the legal profession in its present form, and solicitors could simply become a professional sub-function of services offered by large accountancy firms.

If fear of this scenario prevented it from becoming a possible practice option, this would have the arguably undesirable effect of denying MDP as a practice option to small private client firms, who may desire to set up such organisations in order to bring to fruition, for example, the 'one-stop property shop' idea. In the interests of the profession as a whole it would be more rational for the larger firms to support MDPs since, should they become a legal practice option, the choice still rests with the individual firm. Hence, at the level of the large firm nothing need change, but at the level of the small firm it may allow a stronger strategic and competitive position from which to save the profession's foothold on the domestic conveyancing market and other areas of private client work.

Without this widened set of practice options, the wider competitive implications for the profession (perhaps even at the larger firm/ commercial end of the client spectrum) may prove serious. The government may attempt to introduce MDPs through the Solicitors Acts regardless of the desires of the Law Societies [26].

(IV). In the future, small firms are likely to find it increasingly difficult to maintain a full service function due to expansion of legislation both in terms volume and complexity so one could expect in general increasing specialisation independent of size.

(V). Within the domain of large firms (which are likely to become still bigger through time) there may be a greater requirement to shift to more mechanistic and formal sharing bargains to split partnership profits between partners. This will be required because of increased numbers and greater emphasis on external based hiring, which in combination substantially weaken screening and monitoring processes, present and effective in traditional internal QA contests in smaller numbers of partners situations.

(VI). It is likely that in future, the domestic conveyancing market will be characterised by increased competitive pressures from sources internal (other law firms) and external (licensed conveyancers, banks and building societies, etc.) to the legal profession. Lawyers may be presented with increased employment opportunities within these external organisations, and this may soak up lawyers who may be displaced from smaller law firms who fail to maintain market shares in the more competitive market. The impact of this is unlikely to be as strong in, for example, rural areas where any increase in competitive pressures will tend to be very peripheral.

(VII). Law firms will increasingly become involved in formal associations with each other in the form of legal groups and/ or joint ventures. This will permit firms to increase their market coverage to clients without having to open up offices around the country. This will have the effect of increasing and formalising professional networking and may counter the requirement of firms to become larger scale, and thus act against the trend of firms becoming larger. Firms will be able to duplicate scale and specialism/ competence requirements using joint venture/ strategic alliance type agreements which avoid many of the pitfalls of large scale partnership practice discussed at length in this thesis.

(VIII). Should firms feel able to cope with these large partnership practice problems and design systems etc. which circumvent them, or minimise their impact, large commercial firms (particularly those in London) may decide they wish to continue the current trend of merging with each other. If this can be done successfully, this sector of the market for legal services may in future resemble that of accountants firms, where there will be a 'big six' group of firms, then a larger grouping of medium sized firms (of far smaller scale than the 'big six'), and finally a multitude of small scale firms.

4.2 Increasing globalisation of the market for legal services:

Outwith the domestic scene, law firms in the UK are now perceiving increasing potential globalisation of their activities. For example, the impending completion of the single European market, with its attendant harmonisation of laws etc., has prompted many of UK corporate law firms to consolidate their links with foreign law firms. Such practices have also endeavoured to enhance their capacity to advise and assist clients in their various commercial activities in this context. Some firms have opened up offices abroad in Europe and also further afield in locations throughout the world. More formal foreign inter-firm alliances/ affiliations, and even full blown foreign offices, are likely to become more commonplace and indeed necessary in years to come.

4.3 The quality of legal services in the future:

A major anxiety concerning the future of the profession, particularly in the context of changing its regulatory environment, is quality of legal services and how to maintain standards of quality. As we have learned from discussion throughout this thesis, the most important element which ensures quality of legal services comes from within the lawyer himself [27]. To this extent, it is vital to ensure that the profession maintains its rigorous selection and filtering processes to enforce self-regulation both at the level of the individual lawyer and at the level of the profession as a whole. It is at this early stage that desirable practising characteristics are instilled in the lawyer and undesirable characteristics eradicated.

4.4 The role and importance of the market for PI insurance:

The insurance market has become an increasingly important feature of legal practice in the past and it is likely that it will become even more so in future. Lawyers are required to be insured against professional liability via PI insurance. The importance of the degree of liability with which any firm to which he belongs may practice, takes a back seat to the issue of ensuring adequate PI insurance. This cover is costly and it is not unreasonable to suggest that lawyers are provided with a fairly direct incentive to practice in a manner which will minimise the possibility of claims for negligence being made against them. This is consistent with behaviour directed at attempting to preserve the reputation of the firm. Continual claims could be expected to see the law firm faced with increasing costs of insurance which will push up costs to that law firm. It will not be possible for the firm to pass on this increased cost to consumers as a premium for quality as this would clearly be unjustified. Should consumers in the market perceive the divergence created between price and quality the firm will be forced out of business.

If it is accepted that lawyers bow to their ethical requirements and self-regulate effectively at a personal and overall professional level, this should constrain "moral hazard" use of insurance markets - where the firm chooses to fall back on the insurance rather than take sufficient care. The efficiency of the insurance market in perceiving and penalising such behaviour are of utmost importance here, as is its capacity to accept increased demands for cover. Law firms who have no need to use their cover and protection are required to pay premiums which reflect delinquent firms negligence. Such risk spreading is the fundamental function of any insurance market. If the market is seen as efficient then negligent firms would tend to be squeezed out of the market before insurance premiums would rise to such an extent that they unduly penalised innocent firms. In the context of the legal profession, it could be expected that the proportion of claims being made would be small, if self-regulation was effective. If all firms were suffering from prohibitive premia and restricted cover then this would tend to suggest that tighter and more effective self-regulation may be required.

Professional ethics are believed to be sufficient an assurance of quality services for the consumer. The whole rationale behind permitting the legal profession monopoly power and self-regulatory status is that their trust and professionalism warrants such a position of independence. The use of insurance may, therefore, be perceived as a failure on the part of the profession to provide the necessary guarantees itself with the real guarantee coming from an external agency in the form of insurance cover. It does, however, afford the client real protection should rogue members of the profession act opportunistically against them.

Hence, there is no a priori reason to suspect that the quality of legal services will fall consequent upon changes to the regulatory environment surrounding the practice of law

firms. The goal of the law in relation to legal services is perhaps best viewed as one of protecting the client from the information asymmetry existing in favour of the lawyer in the client/ lawyer relationship. As the lawyer is the least cost avoider in relation to negligence then it makes sense for the ultimate liability to be imposed on the lawyer for acts of negligence. The law firm pays for PI insurance to cover itself against claims for negligence and hence shoulders part of the cost of client protection. Ultimately, however, the consumer pays for this cover via higher service costs, but is probably amenable to increased costs where they do afford real protection in the event of things going drastically wrong.

Chapter Nine-Endnotes

1. These benefits, and others, of partnerships have been discussed in detail at great length above.

2. See earlier chapters and previous discussion in this chapter for a comprehensive discussion of this.

3. It will be recalled that lawyers are also in a contract with the relevant Law Society, and in an implicit contract with the legal profession as a whole. Ultimately, they are also in a contract with society and The State to render legal services to the general public.

4. This can be seen to be akin to the "rule by fear" type of relationship (found, for instance, in the army) albeit in a much diluted form in the case of partnership. It may also be true that a higher level of respect may be accorded to someone who has been through the ranks. Those who enter straight at the top, may be seen as less well informed of the activities of lower levels of the organisation, and less able to appreciate lower level work procedures etc.

5. See, Paroush, J., Notes on Partnerships in the Services Sector, *Journal of Economic Behaviour and Organisation*, Vol.6(1), March 1985, pp.79-87.

6. See Paroush (1985), *supra* Note 5.

7. See, Alchian, A.A. & Demsetz, H., Production, Information Costs and Economic Organisation, *American Economic Review*, Vol. 62, pp.777-795, 1972. Reprinted in Putterman, L. (ed), **The Economic Nature of the Firm**. Cambridge, C.U.P. 1991.

8. See, Paroush (1985), *supra* Note 5.

9. See, Jones, G.R., Transactions Costs, Property Rights and Organisational Culture: an Exchange Perspective, *Administrative Science Quarterly*, Vol.28, 1983,

pp.454467.

10. See; Williamson, O.E., The Economic Institutions of Capitalism. New York: The Free Press, 1985. and also; Gilson, R.J. & Mnookin, R.H., Sharing among the human capitalists: an economic enquiry into the corporate law firm and how partners split profits, Stanford Law School Working Paper Series, No. 16, 1984. at p.371.

11. See; Jones (1983), *supra* Note 9.

12. See; Jones (1983), *supra* Note 9.

13. The creation of a firm culture via selection of highly self-motivated partners, who require low levels of mutual monitoring, will at least partially mitigate the problems of individual shirking and sub-group shirking. Effective screening and selection procedures should choose persons with low propensity to shirk, facilitating formation of a mutually supportive and compatible partnership team.

14. See; Jones (1983), *supra* Note 9.

15. See; Williamson (1985), *supra* Note 10.

16. It is unlikely that he will choose to execute the next stage of the transaction elsewhere through lack of trust in the organisation, since such a lack of trust would have made him look else where in the first instance.

17. For a concise overview of literature concerning managerial theories of the firm, in relation to other theories of the firm see; Stephen, F.H., Economics and Work Organisation, in; Firms, Organisation and Labour: Approaches to the Economics of Work Organisation. Macmillan, 1984. pp.3-24.

18. Additionally, in the UK, shareholders other than institutional ones tend to be fairly apathetic. This, paired with the fact that due to their vast numbers they are generally immobile and largely inert as a group, results in an indifference towards many of the circumstances that directly affect their shareholdings. For example;

1. They are likely to be completely disinterested in who the directors are or proposed changes to this group,

2. They are unlikely to attend AGMs etc. or vote in company matters,

3. They are unlikely to even read any company reports etc. sent to them.

As a result, they may exercise very little pressure over the controllers of the firm to protect themselves from monitoring difficulties associated with the divorce of ownership from control. In this respect the directors, via proxy voting, may largely be able to run the show with a free hand with shareholders placing utmost confidence in their ability to do so. What little control they have over their property right in the firm via voting rights is handed straight back to the directors in the form of proxy votes.

19. In the absence of specific exclusion, this situation would appear to not rule out one potential source of external capital. It would be possible for solicitors to provide capital for other legal firms. It is difficult to imagine why there would be an incentive for solicitors to undertake such shareholdings. A possible motive could be to attempt to mount a takeover bid, but given the fact that the majority of the shares will be held by the in-practice directors of the firm this would appear an unviable option for the would-be bidder in a takeover situation. In fact, this would be almost impossible as it would be tantamount to attempting to take-over a private company as an outside bidder. To even attempt to attain a controlling interest in such a firm would be difficult if not impossible. The only other motive that can be assigned to lawyers to invest in other firms is to further a goal of self preservation of the profession. This would be unlikely to be a sufficient motive in order to provide external capital.

20. As we have argued before, there is a strong characteristic of shareholder apathy and immobility in the shareholders of many corporations. Consequently, shareholders may not demonstrate any strong desire to exercise any control they have in terms of protecting themselves against the monitoring difficulties they face arising from any resultant divorce of ownership from control.

21. A parallel can be drawn with recent liberalisation that has been enjoyed by chartered accountants in private practice. Although there has been an increase in the numbers of cases passing through the courts involving claims for professional negligence, this could be seen as indicative of a more litigious client as much as a reflection of lower standards of care of accountants. This coupled to an increased reliance on professional indemnity insurance, paired with an expanding area of negligence law, has resulted in increased legal activity in this area. A floodgates argument may also be applicable here, where the success of actions has increased the confidence, and therefore willingness, of greater numbers of persons to undertake actions. In this context, the cost and availability of appropriate insurance cover has become an increasing problem as potential risks are higher and the situation is only likely to get worse.

22. A recent example of this can be found in the field of chartered accountancy where, liberalisation of many of their practice rules coincided with increased merger activity and the market is now characterised by three main strata of firms now; The Big 6, the intermediate size firms and the small firms.

Accountants have appeared to have placed greater reliance on the external labour market in recent years and this is likely to be due to the expansion of the accounting profession witnessed in recent times. There could be a similar situation in the legal profession in years to come if similar liberalisations take place.

It is now commonplace to see adverts for solicitors in appointments pages in the many of the daily newspapers. Many of these are placed by specialised recruitment consultants and this is indicative of 'headhunting' activities, made necessary as a result of increased specialisation of legal services (particularly commercial) paired with general shortages in the supply of lawyers

23. This is due to the fact that partnerships are taxed on previous years profits and corporations on current year profits. As a result there would be a double tax burden

in the year of transfer.

24. For example, the initial Green Paper proposals for reform of the legal profession advocated by Lord Mackay in 1989 can be summarised as follows:

1. Ombudsman to replace Lay Observer, with wide powers to investigate complaints and recommend compensation.
2. Barristers and solicitors to practice as certified advocates depending on training and qualification. Rights of audience in different courts to depend on level of certification.
3. Transitional rights for existing solicitors to act as advocates in all Crown Court cases except jury trials.
4. All advocates with appropriate certificate eligible for appointment as QCs and judges.
5. Development of specialist expertise with appropriate standards of education, training and qualification.
6. Lord Chancellor's committee to review education, training and specialisms and to advise on codes of conduct.
7. Solicitors able to enter into partnerships with members of other professions, and into multi national practices.
8. Banks and Building Societies to offer conveyancing.
9. Lawyers allowed limited contingency fee arrangements.
10. Direct access of lay clients to barristers.

These proposals, albeit in an amended form, are still in the process of passing through parliament and their final form is uncertain.

25. This set of other institutions could also encompass banks and building societies etc. and other licensed conveyancers, depending on legislative provisions.

26. In Scotland (where incorporated solicitors practices are permitted) there has been no support for this option. This can be rationalised in terms of a fear held by large commercial firms of takeover by other firms, taxation problems, and generally no perceived advantages of such an option. Particularly in the domain of the small firm, such a move yields no apparent inherent advantages. In the case of large law firms, mergers are always likely to be difficult due to personality clashes and a desire to keep a firm name intact.

27. This is essentially an internally driven and enforced incentive which is a function of training and socialisation, and instilled professional ethics and expected standards of care/ service. It could be argued that a lawyer who cannot supply the same degree of ethical practice regardless of situation or organisational form is not worthy of the levels of trust invested in his fellow colleagues and is, therefore, an undesirable member of the profession both from the point of view of the profession and the public. A lawyer's ethics should stand above all and should at all times act to constrain him from engaging in behaviour that would undermine confidence in his abilities.

-Chapter Ten-

Summary and Conclusions:

Introduction:

This thesis has focused on salient features of the current and future structure and internal organisation of the legal profession. The resultant economic analysis conducted examines these features using the prism of newer, primarily contractual based, theories of the firm. These have played a central role in providing building blocks which together constitute the analytical environment from within which the behaviour of a sample of real life law firms has been empirically observed.

The thesis commenced by examining issues in the current structure and organisation of the solicitors profession and describing a methodology suitable for conducting an economic analysis thereof. The remainder of the thesis followed four major themes. Chapters Three, Four and Five presented the broad theme of economic organisation of relationships between the firm and its clients - Chapter Three examining general literature of the economics of organisation not specific to law firms, Chapter Four outlining its specific relevance to the law firm, with Chapter Five presenting empirical observation of the client/ firm relationship.

Chapters Six and Seven shared a common theme of the organisation of economic relationships between the partners of the law firm. The internal organisation and ownership structure of the partnership as a mechanism for dividing income between partners and binding partners together was examined in Chapter Six. Chapter Seven presented the empirical observations of these issues for sample firms.

The theme of Chapter Eight was the examination of the organisation of economic relationships between partners and QAs of the law firm, focusing on screening mechanisms, promotion tournaments and the up-or-out rules employed in partnership. This chapter also examined the empirical information collected to investigate these issues for sample firms.

Chapter Nine's theme was future oriented, looking towards the future of the legal profession considering alternative practising modes given the questionable longer term survivability of partnership as a mode of governing economic relations across all dimensions discussed in previous chapters.

Summary and Conclusions - Chapter One:

Chapter One comprised an initial discussion of the background and general issues

surrounding the current structure, organisation and regulation of the profession. Within this chapter, the current practising arrangements were highlighted in the context of the wider regulation problem, plausible government objectives in legal service provision and proposals to alter structure via regulatory change. This chapter was also devoted to an explanation of current legal restrictions on law firm organisation. This served the dual purpose of detailing the legal impediments currently frustrating structural change in the legal profession, and outlining the inter-dependence existing between structure and internal organisation.

The latter part of Chapter One was assigned to a primarily sociological discussion of the concept of a profession. It was perceived necessary to engage in such a discussion for two main reasons. Firstly, characteristics which typify a profession required to be identified, and secondly, some attempt had to be made to disclose exactly what demands these revealed characteristics could be expected to exert on regulation, legislation and the relationship between the profession, Government and the general public as consumers of legal services. This discussion, as a consequence of its primarily sociological base, serves to clearly illustrate the requirement for economics as a progressive social science to develop and positively encourage a more permissive methodology which reaches out to other academic disciplines for inputs to theory and discussion. It further reinforces the merits of a more holistic approach to describing situations of capricious human/ economic behaviour. This holistic perspective is stressed as a continual and recurring theme throughout the thesis.

Summary and Conclusions - Chapter Two:-

Chapter Two comprised a theoretical and empirical methodology. It was herein concluded that the law firm appeared to be an ideal organisational backdrop against which to examine newer contract based theories of the firm. Additionally, it was concluded that the law firm (as a service provider characterised by high levels of human capital input) could suffer particular economic problems ideally suited to examination through the prism of newer theories of economic organisation. This was viewed as being both timely and significant since, as the UK economy increasingly relies on service industries, the types of economic and organisational problems typically suffered by the law firm may become more widespread. It was concluded this reinforced the case for developing a comprehensive understanding of the law firm. It was also concluded that while the strands of theory reviewed in latter chapters appeared more appropriate to a comprehensive understanding of the law firm than traditional Neoclassical theory, economics as a scientific discipline nevertheless still suffers from certain intrinsic, and unrectifiable, problems.

Chapter Two continued and built on the theme introduced earlier in this chapter, of developing an appropriate empirical methodology for the current law firm study. This

involved presentation of a personal view of what procedure empirical testing should follow in economics. It was noted here that testing almost invariably involves the entrance of value judgements of the researcher and the procedure used for empirical investigation in economics should explicitly recognise this. It was further concluded that due to the methodology employed and the testing procedures commonly used, economic analysis too often overlooks the most important and relevant aspects of the problem under investigation. While these aspects are typically incapable of being measured for one reason or another, it is concluded that this should not force the researcher to ignore them in favour of those which are easily measurable, or to force items into inappropriate categories merely for the sake of keeping analysis tidy.

Chapter Two also discussed the specific methodology of the actual questionnaire used to abstract empirical information from the sample firms. In doing so, the nature of the information requested in each of its seven sections was detailed, as was the manner in which it was intended it would be coded and analyzed.

The specific aims of the empirical study (which can be viewed below as being fourfold) were also presented. These are summarised as follows;

1. Firstly, provision of a rationale for the current existing structure,
2. Secondly, justification of the theoretical method chosen,
3. Thirdly, assistance in evaluation of alternative practice options and,
4. Fourthly, provision of descriptive analysis and testing of hypothesised circumstances.

The first section of the questionnaire was dealt with in Chapter Two, this being Section One - The Firm. This section comprised a detailed description of the sample firms and introduced and discussed some initial theoretical issues and empirical puzzles examined in the first section of the questionnaire. Specific hypotheses derived from discussion of these issues were examined and tested in the light of detailed empirical information collected and the results presented.

The first section of the empirical information, discussed in section three of Chapter Two, essentially described the sample of 33 law firms examined in the overall study.

Questionnaire Section 1 - Description of sample firms:

PARTNERSHIP SIZE:

The first conclusion of this section of the survey was that large firms (of 30 or more partners) employed a statistically significantly higher gearing (ratio of qualified assistants to partners)

than small/ medium firms (of fewer than 30 partners).

SPECIALISATION OF BUSINESS:

Secondly, it was concluded that larger firms tended to specialise to a greater degree in commercial rather than private client business. It was typical for large firms to indicate they did not actively seek private client work, with any such work only being offered either to existing private clients or to commercial clients. Large firms tended to view private client work as burdensome and far less cost effective and profitable than commercial client work, some indicating that they would welcome its complete demise from their operations. While there was a definite trend of large firms serving commercial clients and small ones serving private clients, this split, although pronounced, was not absolute. Those firms interviewed noted, however, that the profession was increasingly dividing into two distinct sectors wherein small firms served private clients and large firms commercial clients. No firms indicated further specialisation in the form of offering services solely to a specialist section of either of these client type sectors at present.

ORGANISATIONAL STRUCTURE:

Whether sample firms had one or multiple offices, each office tended to perform a general rather than specialist function (ie. firms tended not to have one office dealing with domestic conveyancing and another with civil and criminal court work, or the like). Many large firms had fairly well developed hierarchical internal organisational structures and many disclosed the existence of full branches or affiliated offices in various international locations outwith the UK. It was concluded that larger firms tended to exhibit greater degrees of specialisation and fragmentation within their offices than smaller firms. Within smaller firms, specialisation and fragmentation was less well developed internally (perhaps less necessary also), and occasionally some extent of specialisation existed between offices (usually branches).

Overall, there was general heterogeneity between firms in relation to their overall organisation, leading to the conclusion that law firms are typically complex and unique in terms of their internal and external organisation.

PARTNERSHIP GROWTH:

As was anticipated, law firms relied more on internal driven organic growth than external growth via mergers, takeovers, bolt-ons, headhunting, and agency placements. It was concluded that internal growth methods are desirable and preferred by law firms due to the necessity of effective screening and filtering in the partnership mode. Other external methods were, nevertheless, utilised in some firms to complement, and more importantly supplement,

internal promotion. Headhunting occurred with statistically significantly greater frequency within large firms than in small to medium sized ones - leading to the conclusion that this may be a necessary activity within large firms in their quest for growth in certain specialised areas of legal work. There may be a failure of traditional internal/ organic growth processes to produce a sufficient quantity of new partners of the desired specialisation when required. This demonstrates the struggle the large law firm faces in attempting to attain desired levels of growth and degree of functional specialisation in the short term, whilst maintaining quality and reputation, using traditional (far longer term and rigid) internal growth processes.

Standardisation in documentation was widespread throughout sample firms, with standard documentation and routinised procedures being utilised so far as they are applicable, in all transactions amenable to such standardisation. Firms typically viewed this to be essential to suppress costs while allowing the firm to offer quality service in modern markets for legal services. Many firms admitted standardisation was on the increase generally, many additionally indicating that they wished to further increase standardisation/ routinisation in future.

Table 10.1

Summary of Hypotheses results: Section One - The Firm

	Evidence
Hypothesis 1: Larger firms will tend to specialise to a greater degree in commercial rather than private client business which will be the specialism of small/ medium size firms.	Consistent
Hypothesis 2: Larger firms will tend to have greater degrees of specialisation and fragmentation within their offices than small/ medium firms whose specialisation will tend to be between offices.	Consistent
Hypothesis 3: Larger firms can be expected to employ a higher gearing (ie. ratio of qualified assistants to partners) than small/ medium firms.	Consistent
Hypothesis 4: Larger firms will be more likely to have foreign offices and affiliated offices abroad than small/ medium sized firms.	Consistent
Hypothesis 5: Larger firms can be expected to have used bolt -ons and headhunting to a greater degree than small/ medium sized firms.	Consistent

Summary and Conclusions - Chapter Three:

The third chapter of this thesis examined both Neoclassical and newer institutional attempts at explaining industrial organisation. Some deficiencies of Neoclassical theory of the firm were highlighted as were advantages of employing newer, primarily contract based, theories of the firm in addressing some of these major deficiencies. Theories of property rights, agency

and transactions costs, and network organisation were discussed at length in this context. It was stressed that a major advantage of these newer theories is their emphasis on the dual organisational importance of both firm and market, and interactions between these transactional modes. It was concluded, however, that although these newer theories offer considerable advantages over conventional theory, they nevertheless still suffer from limitations, mainly stemming from their Neoclassical inheritance and emphasis on maximising behaviour (even paradoxically where agents are viewed as boundedly rational). An attempt was made in this chapter to synthesise more useful elements of these newer theories to indicate the direction in which economic theory of organisation could most fruitfully evolve.

An important conclusion of this chapter is that economic theory, as it stands, faces major problems in attempting to explain the capricious behaviour of individual actors and organised groups thereof in situations of uncertainty and imperfect information and knowledge. The development of more useful theories of information and knowledge is an area upon which economics, with input and assistance from other related social sciences, should more sharply focus. This shift in emphasis would involve importing to economics a greater input from other sciences such as behavioural psychology and the like, along lines similar to those envisaged by Simon in his major works [1]. It is concluded that theoretical development in this direction would render economics a much more powerful science in explaining individual and collective human behaviour within firms and markets.

Summary and Conclusions - Chapter Four:

Chapter Four examined in depth the nature of the client/ lawyer relationship. The main thrust of the argument in this chapter was that in order that this agency relationship survived, it was crucial that high levels of trust in the lawyer by the client existed. This relational and fiduciary contract between client and firm (being characterised by typically high levels of information impactedness in the lawyer) appears initially to be an ideal setting for opportunism by the lawyer against the client. It is concluded in this chapter, however, that opportunism by the firm against the client will not typically be present as a feature of relationships between client and firm. This claim is made because of the conditions and atmosphere that typically surrounds and characterises this relationship. These features essentially render opportunistic manipulation of information asymmetry and impactedness unviable behaviour in the context of the client lawyer relationship.

Continuing this theme of the role of information and deficiencies of information in legal services, the role of advertising as a source of information in legal services was examined next in Chapter Four. It was concluded here that the potential role of advertising as an information enhancement in the typical consumer's search and choice process was fairly

limited. The importance of advertising information to the consumer essentially depended on how this information was perceived and utilised in relation to other sources of information, where other sources of reputation information would be likely to take precedence over advertising information. The concluding section Chapter Four explored the potential situation whereby reputation (possibly in combination with and reinforced by advertising) could create a brand name. The brand-name firm concept and the dual benefits to brand-name firm members and consumers of its services were discussed here within the context of information problems in service provision and consumption.

Summary and Conclusions - Chapter Five:

Chapter Five examined the second section of the questionnaire, this being Section Two - The Client/ Firm Relationship. This section comprised a detailed description of sample firms' responses to questions in this section of the questionnaire. Theoretical issues and empirical puzzles were examined and specific hypotheses derived from discussion of these issues were examined and tested in the light of detailed empirical information collected with results of hypothesis testing formally presented.

Questionnaire Section 2. The client/ firm relationship:

Where standard documents were used within the client/ firm relationship, firms typically viewed this as resulting in benefits to clients, or as resulting in mutual benefits to both client and firm. The use of standard documentation was commonly viewed as facilitating increased efficiency in the relationship itself and within the firm in general. Some firms argued use of standard documentation was essential in transactions within modern markets for legal services to survive competitive pressures.

It was generally concluded that law firms perceived advantages of using standard documentation in transactions with their clients, whereby benefits typically accrued not merely to the firm, but also the client.

CLIENT INFORMATION:

Firms generally recognised the importance of maintaining client information, with some firms who already retained client information and others that as yet did not, both arguing that client information and its usage would likely become more important in future. Many firms held such information on a master client database, with some also utilising sophisticated client profiling methods. Client information was recognised by many firms as a useful tool in providing clients with other services should they desire them. Some of these firms actually utilised existing client information to actively cross-sell services to existing clients. Some

firms that already participated in cross-selling and others that as yet did not, both envisaged a greater role for cross-selling of services in the future. Many also perceived a similarly enhanced role for client information in general in future.

It was concluded that client information is an important commodity to the law firm in attempting to generate repetitious business from clients, particularly in modern markets for legal services wherein some firms complained that clients were typically more price sensitive and less firm loyal than before. Such information was generally perceived to be a vital cornerstone of creating and sustaining a long-term relational contract between firm and client.

Such information was perceived almost universally as providing benefits either to the firm, the client, or to both firm and client, in terms of client/ firm relationships. Client information was argued to yield advantages to the incumbent firm over other firms in relation to established clients. It was therefore concluded that the client/ firm relationship created will typically appropriate benefits to both client and firm, where firms who already enjoy a relational contract with a client will possess a first mover advantage over other firms in relation to that client.

At least a high proportion of established clients of many firms were disclosed as providing them with repeat business, thereby continuing client/ firm relations (overall commercial clients providing a more predictable flow of repeat work than private ones). Some firms noted that clients were typically less loyal than before and, therefore, less likely in general to engage in long-term relational contracting with only one law firm. Other firms, who did not typically enjoy repetitious business from clients argued this was a function of many of their clients only using them for specific specialist services. These firms were typically large commercial oriented firms.

It was concluded that, in general, clients do perceive uncertainty reducing advantages of returning to their current law firm due to long-term relational contracting advantages of the client/ firm relationship (excepting where they use specific firms for specific specialist services).

Many firms indicated that, where circumstances were appropriate and it was not impossible, they would actively take remedial action to attempt to preserve client/ firm relationships where breakdown had occurred. It was concluded that this is consistent with the view that the typical client/ firm relationship has a high cost of termination to both firm and client and that relationship preservation ('voice' rather than 'exit') is preferable.

SIGNALLING REPUTATION AND QUALITY TO PROSPECTIVE AND EXISTING CLIENTS:

In an attempt to reduce characteristically high levels of client uncertainty, most firms argued

that personal service, typically paired with speedy, efficient and accurate legal work, and client care, were essential to clients. It was concluded that these features surround and essentially create the trust based relational contract between client and firm. In only one firm was it the case that the firm name was not perceived as significant, or very significant, as a signal of quality and reputation to clients and prospective clients - the dissenting firm here was a new firm which had simply not as yet established its name and concomitant reputation). It was, thereby, concluded that firms perceive the firm name to be vitally important in conveying reputation information to clients and prospective clients.

Many firms utilised direct advertising and promotional tools to provide information to existing and prospective clients. It was concluded from information provided by firms in this section that although these methods of conveying reputation and quality signals provide clients with some indication of characteristics of the service they could expect to receive, there is an overwhelming requirement to reinforce such claims with quality personal service. Over half of the firms disclosed a reliance on referrals from other customers and businesses for much of their work and as such they attempted to establish, develop and maintain this referral network through offering consistently good service. Some firms noted that marketing/ promotional activities would be likely to command a more significant role within law firms in future.

It was concluded, therefore, that although the legal profession has traditionally deliberately refrained from engaging in sales and marketing activities, many firms now feel forced to at least consider engaging in such activities. The profession in general appears to be becoming more pro-active in its self-promotion at least at the level of the individual firm.

Table 10.2

Summary of Hypotheses results: Section Two - The Client/ Firm Relationship

	Evidence
Hypothesis 1: The firm will attempt to create a long term relational contract with the client and will do so by using client information.	Consistent
Hypothesis 2: The relationship created will have benefits to both client and firm.	Consistent
Hypothesis 3: Firms who are already in a relational contract with a client will have first mover advantages over other firms in relation to that client resulting in a bilateral monopoly.	Consistent
Hypothesis 4: Clients will tend to return to the incumbent firm rather than return to the market due to relation specific advantages that reduce uncertainty for the client.	Consistent
Hypothesis 5: The firm will attempt to preserve the relationship created as it has a hign cost of termination to both parties.	Consistent
Hypothesis 6: Law firms will attempt to signal quality and reputation to their own and prospective clients as this will reduce client uncertainty.	Consistent
Hypothesis 7: Law firms will attempt to emphasise personal service and the importance of the client as this will imbue the client with trust in the firm.	Consistent

Summary and Conclusions - Chapter Six:

Chapter Six housed theoretical discussion and analysis of the sharing bargain existing between the profit sharing partners of the law firm. It was concluded that the sharing bargain can be viewed as the most important single component of the overall set of incentive properties of partnership. Hence, discussion of its salient features comprised a large part of Chapter Six. This discussion was based primarily on a critique of the Gilson and Mnookin (1984) discussion of partnership profit sharing arrangements [2]. It was concluded that this analysis has both major strengths and serious weaknesses and in Chapter Six, strengths and weaknesses of the Gilson and Mnookin analysis were simultaneously exposed and discussed.

It is recalled that Gilson and Mnookin viewed the primary function of partnership as a vehicle to diversify risks to human capital of the partners of the law firm. The analysis presented highlighted the main incentive properties and expected behavioural responses thereto of both sharing based and productivity based partnership profit division methods. Advantages and drawbacks of each method were characterised within this chapter, and it is concluded that neither method is unambiguously superior in its quest to efficiently and effectively organise collective legal practice between partners of a law firm. It is, therefore, concluded that both partnership income division modes suffer from advantages and disadvantages in relation, for example, to partners shirking, grabbing and leaving, and engaging in client generation, firm management, and any other non-fee generating activity, all of which are nevertheless essential for the firm's continuing survival.

It is also recalled that the important trade-off and interaction existing between the creation of lawyer specific and firm specific capital in the partnership is discussed here. It is concluded that, by responding to incentives existing within the firm, the lawyer can inadvertently cause simultaneous furtherance of both firm and personal goals. It is recalled that the monitoring function of the partnership, its incentive structure and income division method, in addition to that of partners inter alia, was discussed in Chapter Six. It was concluded here that one of the crucial features for successful partnership practice was the existence of effective self and mutual-monitoring, reinforced by strong conformist traits instilled in partners by the culture of the firm. An important conclusion drawn from this and preceding chapters is the crucial importance of cultural factors and self-monitoring for effective and efficient operation of the legal profession, both at the level of the firm (partnership) and at the level of the overall profession.

Chapter Six was also given over to a discussion of problems of increasing partnership size and the resultant problems that increased size can bring to the law firm. It was concluded here that potential severity of these problems may have acted as the primary catalyst for proponents of regulatory change for the legal profession to call for introduction of a wider set

of practising options for law firms (including most notably, incorporated and multi-disciplinary [MDP] firms).

In the second section of Chapter Six, the law firm was subsequently characterised as a labour managed firm. This involved an examination of the literature of the labour/ self-managed firm [LMF], an institutional arrangement commonly found within the economy of Yugoslavia. It is concluded that the LMF model, while being analytically restrictive, does nevertheless expose potential problems associated with hiring additional members and achieving expansion in an organisation where the workers (partners) own and manage the business (as is the case in the law firm). A discussion whereby the law firm is viewed in the context of the LMF was presented in this chapter, developing possible parallels between the theorised behaviour of the LMF and possible real life behaviour of the law firm partnership.

Summary and Conclusions - Chapter Seven:

Chapter Seven comprised an analysis of the information derived from sections 3, 4 and 6 of the empirical study and questionnaire.

Questionnaire Section 3. The interior of the firm:

MANAGEMENT STRUCTURE:

The ways in which firms organise their interiors in relation to their formal management structures/ hierarchies were, to say the least, diverse. In the smaller firms there was typically a main group of partners paired with a senior or a managing partner (or both). Larger firms tended to have a structure built around committees of partners, or a partnership board (or both) aimed at facilitating smoother, more effective decision making. In over half of the sample firms, non-lawyers held positions within the firm's management structure. This was a surprising result since it was expected that delegation of decision management and/ or control to non-residual claimants would be rare due to monitoring difficulties and severe attenuation of partners' property rights.

In the majority of cases, partners still remained fee earners of the firm where they simultaneously also held specific formal management positions. In over a third of the sample firms, however, at least some of the partners held full time positions in management and did not simultaneously combine this with fee earning activities. Four firms envisaged moving to a more formal management structure in future as they were facing decision making problems presently.

In conclusion, partnership boards and committees play a vitally important role in facilitating

decision making within the large modern law firm partnership. It is simply impractical and inefficient for all partners to become involved day-to-day in every decision that must be taken within the firm. Hence, decision making is smoothed by assigning decision making authority in specific areas to various committee/ board subsets of the entire partnership. It was expected that partners, as residual claimants of the firm, will have the combination of functions of decision managers and decision controllers invested in them, within traditional partnership organisation. It is concluded from evidence from sample firms in the empirical study that this necessarily breaks down in larger partnerships due to consequent inefficient and ineffective decision making. It is also concluded, however, that where there is observed separation of residual risk bearing from decision control, this does occur within large firms, where it is typically the case that decision systems separate decision management from decision control.

In relation to management hierarchy existing between partners of the firm, almost all sample firms were keen to point out that, regardless of any hierarchy and irrespective of the way in which income was divided among partners, the power structure of the partnership remained egalitarian.

PARTNER SPECIALISATIONS:

Partners were typically specialised in one or more of the specific areas of legal services in which the firm specialised. In addition, this legal specialisation was typically combined with some specialised management function. In most cases, partners also headed specialist legal departments within the overall firm. In over a third of the firms, partners acted as convenors of specific committees established to perform specific management functions within the firm. Only one firm perceived there to be a need for greater specialisation in future. It can be concluded, therefore, that partners within law firms commonly have specialisms both in terms of their legal work and in one of more of their firm's management activities.

PARTNERSHIP DEMOCRACY:

In almost all firms interviewed, the relationship existing between partners was described as egalitarian. Even in situations where firms described the existence of unequal partner voting rights and/ or formal or informal seniority existing between the partners, firms typically claimed the partnership remained very egalitarian. Over a third of the firms described the existence of salaried and equity sharing partners - a feature reinforcing hierarchy and undermining true partnership democracy. It is concluded, however, that the function of this (rather than to create power differentials) is as a formal screening mechanism to aid evaluation and assessment of the suitability of lawyers in the period before granting of equity partnership.

It is concluded for the firms interviewed that partnership as an organisational form appeared fairly democratic. Any hierarchy existing within the partners grouping (including all partnership categories whether salaried or equity sharing) appeared to be simply part of the incentive structure and screening mechanism of the firm as opposed to some conscious attempt to undermine true partnership democracy.

Table 10.3

Summary of Hypotheses results: Section Three - Inside the Firm

	Evidence
Hypothesis 1: The partners, as residual claimants of the firm, will have the combination of functions of decision managers and decision controllers of the firm invested in them.	Consistent
Hypothesis 2: Delegation of decision management and/ or decision control to non-residual claimants will be uncommon due to monitoring problems and severe attenuation of partners' property rights.	Not Consistent
Hypothesis 3: Any observed separation of residual risk bearing from decision management will tend to exist in large firms and this will lead to decision systems that separate decision management from decision control.	Consistent

Questionnaire Section 4. The allocation of clients:

CLIENTS AS A SOURCE OF FIRM OR LAWYER SPECIFIC CAPITAL:

In the majority of sample firms it was perceived to be impossible (in many instances) to distinguish between clients who could be regarded as part of partners' client portfolios and those could be viewed as clients of the firm. Consequently, it was not so clearcut whether clients could be viewed exclusively as firm or lawyer specific capital. In just under half of the firms, qualified assistants were perceived to have their own set of clients, with such client accumulation being encouraged as a vital component of the information signaling process in the qualified assistant partnership 'contest'. Very few firms positively discouraged personal accumulation of clients by partners (or other lawyers of the firm for that matter)' with less than one fifth of the firms interviewed disclosing they were actively attempting to reduce client hoarding. Only two firms explicitly admitted they feared lawyers leaving the firm with clients 'in tow'. Where reduction of client hoarding was actively pursued, this was typically to remove internal barriers to cross-selling of services within the firm, rather than guard against client loss via lawyers leaving the firm. A few firms noted that client hoarding was becoming increasingly difficult and was automatically reducing due to increasing specialisation of legal services and the frequent requirement for teams of lawyers within the firm (rather than an

individual lawyer) to serve clients nowadays. It is concluded that firms in general typically preferred the situation where clients were viewed as those of the firm rather than those of an individual lawyer within the firm. However, specialisation often required that partners passed clients between each other on a reciprocal basis, willingly and without compensation. Information provided by sample firms in relation to the allocation of clients between lawyers of the firm is contrary to the stylised view of Gilson and Mnookin whereby passing of clients between partners assumed a strategic significance [3]. In addition, it is concluded that it is not clearcut whether the client is loyal to the firm or to the individual within the firm. To that extent, it may prove risky for the lawyef to rely on clients as a bargaining hostage in 'grabbing' and 'leaving' activities. In conclusion, firms generally did not perceive there to exist a significant risk from lawyers using clients (lawyer specific capital) in such a manner.

CLIENT LOYALTY:

Those questioned regarding whether they perceived clients to be loyal to the firm or to individual lawyers within the firm found this question very difficult to answer. Most believed clients to be loyal to both firm and individuals within the firm. Just fewer than one quarter of the firms perceived clients to be generally less loyal than before, with a similar number believing lawyers to be loyal to a team of individuals within the firm. It is concluded from this that it may be unreliable for lawyers within the typical firm to view clients as a source of lawyer specific capital which can be used as a hostage against the firm to grab a larger share of profits by reinforcing the threat value of leaving the firm.

CONSISTENCY OF CONTACT WITHIN THE CLIENT RELATIONSHIP:

Within the typical law firm it was seen as desirable that, where possible, clients should see the same person on each contact with the firm. This naturally could only occur where the client did not require services that were outwith the legal speciality of the partner with whom he usually dealt. The typical response of firms was to assign each client a contact partner, who would channel and refer the client to one or more of his colleagues should he require services outwith the contact partner's specialisms. In just fewer than one fifth of the firms, each client was assigned a number of specialist contact partners. In conclusion, where possible, clients would be seen by the same lawyer of the firm to breed familiarity, engender trust and create the client/ firm relational contract emphasising personal service. Where circumstances dictate, the client may require to see lawyers other than this contact lawyer, depending on the service categories required. The firm will typically encourage the client to be introduced by the contact partner to the requisite lawyers and will encourage the client to

form relationships with as many individuals via introduction as is necessary. Clients who require a range of services typically form relationships with many of the firms lawyers and this will lessen any potential risk posed to the firm via the creation of lawyer specific capital through client loyalty to one specific lawyer of the firm.

FORMAL RESTRICTIONS ON LAWYERS LEAVING THE FIRM WITH CLIENTS:

It is concluded that use of restrictive covenants to prevent lawyers leaving the firm with clients is likely to be largely ineffective. Those firms that did utilise them (either within the partnership agreement or to apply to qualified assistants and/ or employees of the firm) recognised they would likely be difficult to legally enforce. Their most probable ineffectiveness was a popular reason for their absence in many firms. Many firms appeared to be fairly philosophical regarding lawyers leaving the firm with clients in tow, arguing that at the end of the day it was the choice of the client whether to follow or stay put, and that this client decision should be respected. A few firms disclosed that it was difficult to envisage the 'leaving with clients' scenario occurring since, as yet, it never had occurred. A handful of other firms, who did have direct experience of lawyers of the firm leaving, admitted that those lawyers that had left had taken no clients with them. To conclude, the prospect of lawyers leaving the firm with clients was not one which law firms commonly feared. To that extent, this would be unlikely to act as a powerful bargaining chip for the dissatisfied lawyer to use against the firm to which he belongs in an attempt to increase his rewards.

CONSTRAINTS ON LAWYERS LEAVING THE FIRM:

In view of the fact that few firms relied on specific constraints on lawyers leaving the firm with clients and also that those who did were less than confident of their likely success, the issue of non-specific constraints was probed. In by far the majority of firms, loyalty to the firm and/ or the value of present rewards were cited as constraints on lawyers leaving. Other popular stimuli to which lawyers of the firm were argued to respond were the presence of a good career path providing an incentive to remain within the firm, and the prospects of promotion and partnership which would do likewise. Within the typical law firm (where there is a characteristic absence of formal organisational constraints) reliance is placed in mechanisms which rely on self-enforcement to regulate behaviour. Consequently, it is concluded that high levels of personal self-discipline and loyalty to the firm largely obviates the requirement for formal constraints and results in the probable success of informal constraints.

It is concluded that it is very difficult, if not impossible, for the lawyer to initially identify and subsequently evaluate the value of his specific capital derived from clients. As a consequence of this evaluation difficulty, clients may not be as significant in terms of their threat value for grabbing and leaving behaviour by lawyers of the firm as Gilson and Mnookin suggest in their analysis [4]. It is thereby concluded that this may provide a cogent reason why firms examined did not appear, firstly, to rely on formal constraints in this respect and, secondly, to perceive danger from the potential threat of lawyers who may perceive themselves to have amassed significant client derived specific capital. It is also concluded that, judging by responses of sample firms, it is not the case that grabbing and leaving problems are commonplace behavioural responses within law firms. Many firms indicated that events such as these would simply not occur as this type of behaviour was completely at odds with the whole ethos of the typical law firm. Screening mechanisms will have successfully screened out persons who would contemplate behaving in this manner.

Table 10.4

Summary of Hypotheses results: Section Four - Allocation of Clients

	Evidence
Hypothesis 1: The law firm will favour a situation where clients are viewed as belonging to the firm as this is more conducive to the creation of firm specific capital and suppression of lawyer specific capital.	Mixed
Hypothesis 2: The firm will avoid the use of restrictive covenants to prevent client losses through lawyers of the firm leaving as they are likely to be futile.	Consistent
Hypothesis 3: The law firm will encourage clients to form relationships with many of the firm's lawyers as this will lessen risks posed to the firm via the creation of lawyer specific capital.	Consistent
Hypothesis 4: The lawyers exit option will be constrained by other factors in addition to the value of the firm specific capital he has amassed within the firm.	Consistent

Questionnaire Section 6. The partnership profit sharing bargain:

Only one firm described itself as allocating partnership profits on an 'eat what you kill' basis, whereby each partner essentially comprised an individual cost/ profit centre. In all other firms more 'conventional' profit sharing arrangements applied.

THE ROLE OF PARTNER SENIORITY:

In relation to partner seniority, firms were assigned to three main groupings dependent upon their revealed characteristics. Slightly fewer than half of the firms described themselves as

having seniority groupings into which partners were placed and which determined relative income shares. The second group of firms, comprising slightly more than one third of the sample interviewed, disclosed partners of similar seniority were assigned similar numbers of points, where the number of points mapped directly onto partnership profit share. The third grouping, which enjoyed just fewer than one fifth of the respondents, comprised firms which did not rely either on seniority or numbers of points groupings to determine partners' relative shares of partnership profits.

Within some of the firms in the first two of the three groupings described above, flexibility in relative income determination was retained via the ability to either accelerate or restrain partners' acquisition of points or movement up seniority groupings. It is thereby concluded that (within these firms) it was perceived desirable to retain some discretionary element and incorporate some performance/ productivity incentive in overall income share determination. It is also concluded that seniority is, nevertheless, an important factor within most firms since seniority plays at least a minor role in partner relative income share determination in all but six of the firms interviewed.

It is also worthwhile noting here that although firms share broad characteristics/ features in relation to their partnership sharing bargains, each firm uses a more or less unique manner to mechanistically determine partners' relative profit shares.

THE BASIS OF INCOME DIFFERENTIALS BETWEEN SIMILARLY SENIOR PARTNERS:

In firms where similarly senior partners (ie. same seniority grouping or number of points) earned differing shares of partnership profits, this was typically due to the desire to reflect differences in their relative 'contribution' to the firm, or differences in productivity/ merit. In firms featuring such a discretionary element, the decision regarding the determination of differentials was taken either by the full meeting or a committee of partners, or in the case of two firms, by the senior/ managing partner.

TRUE SHARING MODEL FIRMS:

This grouping of firms comprised solely of those firms who did not reveal the existence of any form of productivity measurement affecting income determination via discretionary assignment of partnership profit shares to partners. Within this grouping of 19 firms it was concluded that there was a more frequent incidence of true sharing model characteristics amongst small/ medium firms than there was among large firms.

PRODUCTIVITY MEASUREMENT:

The remaining 14 firms revealed the existence of productivity measurement and discretionary elements in some shape or form within the mechanistics of their sharing bargain. Of these firms, almost two thirds were large firms, with the remainder being small/ medium sized. It is concluded here that this is indicative of the requirement to rely on more explicit incentives and productivity measurement to control more pressing agency problems of large partnership practice and organisation.

Within the 14 firms that incorporated productivity measurement within partnership income determination, it is concluded that this process was often performed in a fairly adhoc, subjective and unsystematic fashion.

RELATION BETWEEN INCOME LEVELS OF DIFFERENT SENIORITY GROUPINGS:

Nine of the true sharing model firms disclosed that a fixed ratio existed between seniority groupings, these firms being described as 'lockstep seniority' based firms. It is concluded that where measurement of partner productivity was included within partners income determination, or where the numbers of partnership points changed annually, the relationship between seniority groupings was constantly changing. Hence, this facet of the incentive structure was not determined in advance, as in the case of the lockstep partnership. Further, the incentives it embodies can be regarded as being subject to constant change year on year.

THE LENGTH OF TIME TAKEN FROM INITIAL ASSUMPTION TO REACH FULL SENIORITY STATUS:

Slightly fewer than half of the firms indicated that no full seniority class existed within their firm. Of those firms that indicated the opposite to be true, by far the most common period to reach full seniority status was 6-10 years. In some firms this period could be as low as 0-5 years and in others as long as 16-20 years. It was fairly common for the period in question to be variable depending on matters such as the personal performance of the partner, or the level of capital contribution to the firm of each partner. It is, therefore, concluded that the time to reach full seniority status (if it exists) can vary markedly both within and between firms. Further, it can involve evaluation of personal characteristics of the partner involved as well as the nature of the formal sharing bargain struck between the partners of the firm. For certain firms it makes no sense to talk of 'full seniority' in the context of the characteristics of their method for sharing income.

SKEWING OF SHARE OF PARTNERSHIP INCOME:

In over half of the firms interviewed, partners' shares of income rose steadily throughout their time as a partner. It was far less common for income shares to be skewed towards either the earlier or latter years as a partner. In just fewer than one quarter of firms, income eventually 'plateaued' and in half this number again, partners' income shares tailed off towards eventual retirement. It was also disclosed by slightly fewer than one quarter of the firms that the skewing of partners income depended at least to an extent on personal performance.

It was common for respondents to indicate that the importance of the skewing of partners shares was far outweighed by the importance of overall partnership profitability, in terms of the magnitude of the final share partners received from overall partnership profits. It is, therefore, concluded that the importance attached to income skewing by Gilson and Mnookin, in terms of incentive linking to leaving and grabbing behaviour, appears to be overstated (at least for the firms in this sample)[5].

MEASURING PARTNER PRODUCTIVITY:

In approximately two fifths of the sample firms, partner productivity was measured to determine relative profit shares. It is concluded, however, that methods firms used to do this were typically crude, subjective and adhoc. Two large firms indicated they were presently considering shifting from true sharing to a partner productivity based model. It is concluded that this is indicative of problems the large partnership may face relying on true sharing, where agency problems are no longer effectively suppressed by firm culture and self-enforced monitoring and incentives. Further, this may be seen as representative of what is likely to become a more commonplace shift as firms in future generally become larger and are forced to confront pressing problems associated with large partnership practice.

TIME RECORDING:

Almost all firms recorded time spent by partners attending to client work either for billing or management purposes, or both. Some firms used time recording as a component in fee income/ time billing targets and/ or individual partner time/ fee income budgets. In only one firm was time spent and recorded against client work a direct component determinant of individual partner income shares. It is concluded that while time recording was a feature of most firms, its role was typically that of a background supplement to reinforce mutual and

self-enforced monitoring. Furthermore, budgeting and targeting procedures, common in some firms (particularly large ones), could be regarded simply as a component part of the wider firm cost control and pricing strategy, rather than a crude check on partner productivity. No firms indicated that such systems performed a 'monitoring of partners' function as such, and whilst time information collected and accessible could be used to perform such a role, it had typically not been used for this purpose to date.

Very few firms insisted partners spent a specified minimum of time attending to client business with firms typically indicating that an implicit norm had been developed and recognised. Time spent was viewed by some firms as reflecting the requirements of individual partner and/ or departmental budgets. The conclusion here is that few firms enforce a formal minimum time requirement but rather rely on informal incentives to encourage partners to spend time attending to client business.

INCENTIVES AND ENFORCEMENT OF TIME SPENT ON CLIENT BUSINESS:

It was perceived by two thirds of the firms that time recording (in isolation or in combination with other factors) did assist in enforcing the amount of time partners spent on client business. Other notable factors were disclosed as being budgets and targets, but more importantly peer group pressure. When it is recalled that there was an almost universal absence of formal time requirements, it is concluded that firms typically rely on fairly weak and indirect incentives to encourage partners of the firm to spend time on client business. It is further concluded that lawyers are just as responsive to incentives other than direct monetary ones in making decisions concerning the undertaking of certain activities within the firm. To conclude, it is apparent mutual monitoring and self-enforcing incentive structures work effectively in the context of the typical law firm obviating a requirement for more visible and formal constraints.

INCENTIVES TO ENCOURAGE MORE THAN MINIMAL ATTENTION TO CLIENT BUSINESS:

In only one firm was there a direct monetary incentive for partners to spend time on client work since personal compensation was directly linked to hours spent. In other firms, indirect monetary incentives, such as;

1) profit motive,
2) committees monitor time spent,
3) hope of promotion,

4) increase personal income and,

5) enhance contribution,

either in combination or individually, were viewed as important incentives to stimulate partners in this direction. Other firms relied on indirect non-monetary based incentives such as;

1) necessity of work,

2) control workload,

3) loyalty to firm and other partners,

4) retain current clients and increase client base and,

5) prestige and perceived success of working for current firm,

either in combination or individually, as motivating factors. In some firms, combined reliance on elements from both of these sets of incentives was disclosed. Upon examining this section it is concluded that the typical law firm places a fair degree of reliance on the lawyers internal monitor/ conscience, combined with peer group pressure, to overcome otherwise weakly defined incentives to engage in activities which do not directly and personally compensate the lawyer. Further, it is concluded that often the strength and depth of the culture within the law firm can enable exclusive reliance upon indirect non-monetary incentives. The incentive structure of such firms is built upon mutual loyalty, mutual monitoring where the rigorously screened lawyer provides, and responds to, his own set of internal incentives.

To conclude, within the typical law firm, the strength of lawyers' internal monitors and the culture of the firm is such that it obviates any requirement for the firm to provide specific incentives for lawyers to engage in various 'unrewarded' activities within the firm.

GRABBING AND LEAVING:

It was overwhelmingly the case that firms argued they would simply not be responsive to the situation where partners attempted to grab greater profit shares by threatening to leave. It was proposed that this was simply not the way things happened within the majority of firms. In over one quarter of the firms it was disclosed that threatening to leave in order make grabbing more successful, would be likely to result in less success for a partner. Firms typically had never experienced this occurring and some firms argued that success would be likely to depend on the individual involved. Some firms were quick to point out that income shares were agreed in advance and, therefore, it was impossible to grab. 3 firms thought that

grabbing and leaving may become more of a problem, and therefore a more relevant issue, in the near future.

It is concluded from the above that appears to be the case that lawyers typically have a low tendency to shirk and this is likely to extend to a low tendency to grab, threat to leave and even actually leave the firm. This is at odds with the Gilson and Mnookin view of the typical large partnership lawyer [6]. To conclude, the lawyers internal monitor tends to be characteristically strong and will typically resist externally provided and presented incentives to shirk, grab and/ or leave. This is consistent with the argument in this thesis that effective ex-ante screening largely obviates the requirement for ex-post monitoring of contractual performance.

COMPENSATION FOR NON-LEGAL WORK:

In only one firm were partners directly and personally compensated for time spent attending to non-client billable requirements of the firm such as; attraction of new clients, non-billable client attention, supervision and training, and management and administration. 4 firms disclosed that current tensions within their respective firms may require that in future their compensation systems change to accommodate such activities. It is concluded that the typical law firm does not (as yet) provide direct incentives for partners to engage in such activities. It can also be concluded that, at least in the past, indirect incentives have been sufficient to ensure that such activities are carried out within the law firm irrespective of compensation. Additionally, functional delegation of such tasks to specific persons has been possible and sufficient to ensure their completion. From interpreting the general mood within many firms that due to changes and forces currently sweeping through many firms, the adequacy and success of present typical arrangements may not guarantee success in the future.

NON-MONETARY INCENTIVES TO ENCOURAGE NON-LEGAL WORK:

Partners generally engaged in these activities because they typically recognised they necessarily required to be done for the good of the firm. Within firms who measured productivity, lawyers were seen to engage in such activities to enhance their perceived contribution to the firm. Some firms disclosed that those who had a flair for certain aspects of these activities tended to insist in doing them and that others were more than willing for them to do so. In a similar number of firms these tasks were delegated to specific individuals either by the full partners meeting or a committee thereof. It is thereby concluded that generally partners are willing to engage in these activities without direct recompense either because

they are interested in those activity, and/ or because it is recognised that they simply require to be done out of necessity, or for the good of the firm. In certain firms, although direct compensation is not forthcoming, indirect recompense via contribution appears to be sufficient incentive.

FUNCTIONAL RESPONSIBILITY WITHIN PARTNERSHIP FOR NON-CLIENT BILLABLE ACTIVITIES:

When specifically delegated, the above activities within firms were assigned to one or more of the following categories; individual partners, departments, committees and specialist non-lawyers/ non-partners.

DELEGATED RESPONSIBILITY TO PARTNERS:

It was commonplace for individual partners to be delegated with management and administration and/ or supervision and training responsibilities. It was not common within sample firms, however, for individuals to be delegated with responsibility for non-billable client attention and/ or attraction of new clients.

DELEGATED RESPONSIBILITY TO DEPARTMENTS:

It was relatively commonplace for departments to be delegated with responsibility for management and administration and/ or supervision and training. It was not popular, however, for departments to be delegated with responsibility for non-billable client attention. No firms indicated that attraction of new clients was a delegated responsibility of departments.

DELEGATED RESPONSIBILITIES TO COMMITTEES:

Again, it was relatively commonplace for committees to be delegated with responsibility for management and administration and/ or supervision and training. It was not popular, however, for committees to be delegated with responsibility for non-billable client attention. No firms disclosed that attraction of new clients was a delegated responsibility of departments.

DELEGATED RESPONSIBILITIES TO NON-LAWYER/ NON-PARTNER SPECIALISTS:

The delegation to specialist non-lawyer/ non-partner specialist of responsibility for

management and administration activities was a feature of marginally fewer than half of the firms. 4 firms used specialist non-lawyers/ non-partners to perform a delegated training and supervision function. No firms assigned such non-lawyer personnel specific roles in either of the areas of responsibility of non-billable client attention or attraction of new clients.

It is concluded that overall, firms exhibited broadly unique methods of delegating and functionalising all of these essential and important partnership functions. Furthermore, the existence of such functionalisation, satisfying requirements to delegate, could be construed as being indicative of the inability of the typical law firm to provide partners with sufficient incentives to engage in these functions, without direct reward. Alternatively, it may simply be that delegation is perceived by the firm as the most efficient and effective way of ensuring that these functions are more efficiently and effectively performed.

ATTRACTION OF NEW CLIENTS BY PARTNERS:

In only one firm were partners directly compensated for attracting new clients. It is concluded that the concern voiced by Gilson and Mnookin that this may cause lawyers to underinvest their time in attracting new clients, may be a potential problem [7]. It is, however, important to recall that Gilson and Mnookins' analysis assigned the typical lawyer the greedy characteristic of being unwilling to pass clients on a reciprocal basis without commensurate compensation. Information provided by firms in this respect points leads us to conclude that in by far the majority of cases, partners were willing to pass clients between each other without direct reward. Often it was the case that clients simply had to be passed since, although the partner who introduced the client remained the contact partner, often the services required by the client were outwith the contact partner's particular legal speciality/ forte.

Table 10.6

Summary of Hypotheses results: Section Six - The Sharing Bargain

	Evidence
Hypothesis 1: The partnership sharing bargain will be almost unique for each firm although broadly similar features will be revealed across firms.	Consistent
Hypothesis 2: Firms that measure productivity as a determinant of income will do so in a fairly subjective and unsystematic manner.	Consistent
Hypothesis 3: Firms will use seniority as at least a minor determinant of partner income shares.	Mainly Consistent
Hypothesis 4: Lawyers will respond to incentives other than monetary ones in their decision to undertake certain activities within the firm.	Consistent
Hypothesis 5: The lawyer's internal monitor and the culture of the firm will be strong enough to obviate the provision of specific incentives for lawyers to engage in many activities within the firm.	Consistent
Hypothesis 6: The influence of the lawyer's internal monitor and the culture of the firm will weaken in larger firms requiring more formal constraints and incentives for partners of the firm.	Consistent
Hypothesis 7: The strength of the lawyer's internal monitor is likely to result in a low tendency to shirk, grab and leave.	Consistent
Hypothesis 8: In large firms the formality of partner specialisations will be greater than in small firms.	Consistent

Chapter Eight - Summary and Conclusions:

Chapter Eight explored more explicitly issues surrounding the employment practices of law firms and employment relationships between partners and qualified assistants in law firms. It will be recalled that such issues were perceived to be worthy of empirical investigation as a result of discussion of theory of the labour managed firm [LMF] and of the 'tournament' of the qualified assistant (associate) in the period before an offer of partnership. This involved probing the underlying rationale for both firm and associate to concurrently tolerate high levels of uncertainty during this period. The role of information signalling and the incentive properties of the partnership decision were discussed in terms of the Gilson and Mnookin (1988) analysis of the 'up-or-out' partnership decision process and their framework of dual uncertainty [8]. The continuing viability and survival of the 'up-or-out' system was also discussed in this section of Chapter Eight. From this chapter it can be concluded that the 'up-or-out' system owes its survival to its attractiveness to both firm and associate in reducing characteristically high levels of uncertainty. Consequently, it is further concluded that this up-or-out system is likely to remain a feature of the typical law firm in the absence of a suitable risk reducing replacement.

Questionnaire Section 5. Internal promotion and firm growth:

THE FORMALITY OF THE PARTNERSHIP DECISION:

As was expected, all firms interviewed disclosed that there was a formal decision mechanism for increasing the number of partners of the firm. In almost all cases a full meeting of partners either made the final choice and took the decision, or had a final vote on recommendations received from a committee (or similar subset) of the full partnership. In only three firms was it the case that the final decision was entrusted to a decision making authority other than the full partners meeting. These firms argued that the likelihood of an erroneous partnership decision being made was minimal as implicitly decisions were taken with authority of the full partnership (ie. if no objections were raised by any of the partners, acquiescence was assumed to grant authority to the decision). In under one fifth of the firms was it the case that a seniority requirement need be met prior to consideration, but in almost three quarters of the firms it was the case that the decision was driven largely by the requirement for a decision to be made in order to prevent good qualified assistants from leaving. It is concluded that the decision process to increase the number of partners of the firm is typically formal and subject to strict procedure. Furthermore, it is concluded that the formality of voting procedures, seniority requirements, committee recommendations and the like, are all consistent with the overwhelming desire of the legal partnership to subject potential partners to pre-partnership screening mechanisms in to ensure the set of desired and requisite characteristics are present in candidates being considered for partnership.

INTERNAL PROMOTION AND EXTERNAL HIRING:

All firms interviewed indicated that the traditional and preferred manner in which to increase partner numbers, via internal promotion of qualified assistants, was used where possible. Just fewer than two fifths of the firms indicated that external hiring of lawyers straight in at partner level was also common procedure. Where this was the case, those newly (externally) hired partners were typically subject to a probation period of initial salaried status, permitting the firm to engage in a filtering/ checking process (some degree of screening mechanism retained). In some firms, the sole reason for the occurrence of external hiring was that the firm was merging with or taking over another firm. In over one third of the firms (including a few that attempted to rely solely upon internal promotion) it was disclosed that the firm had in exceptional cases/ circumstances headhunted specific partners in the past. In over a third of the firms it was indicated that headhunting of partners would likely become more necessary in future, thereby requiring firms to consider and integrate headhunting activities into their overall partner screening, hiring and promotion strategy.

It is concluded that, although firms would generally prefer to rely on internal promotion, this

is not always possible, necessitating direct external hiring, or mergers/ takeovers, or headhunting. Firms typically used the screening safeguard of initial salaried partner status for externally hired partners in order to maintain screening procedures and to ensure full commitment to the firm by such partners. In order to permit sufficient specialisation and desired firm growth rates future, headhunting of partners of specific desired specialisms may become increasingly more frequent, where internal candidates are not available. Furthermore, it is concluded that more frequent infiltration of 'outsiders' into the law firm partnership in future may undermine and affect significantly the traditional implicit behavioural constraints on lawyers of the firm. This may require more stringent filtering and screening mechanisms and the introduction of more formal explicit constraints on lawyer behaviour within the typical firm in the future since ex-ante screening may become more difficult to retain.

BUYING INTO THE PARTNERSHIP:

In fewer than a third of firms interviewed was it disclosed that partners did not have to buy into the partnership. In over half of the firms, new partners did have to buy into the partnership, although in some cases this requirement was not immediate. In a few firms, partners 'bought-in' by deferring drawings to which they were entitled via their share of partnership profits. Similarly there was a requirement in a few firms for new partners to make only a nominal contribution to the partnership's working capital. It was concluded that firms generally did not perceive the buying-in process to the partnership to be particularly significant. Often the sums of capital involved were small and/ or payable over a period of time. Where capital contribution was required this did not appear to be required in order to perform a bonding function in relation to the firm and existing partners, but rather that a nominal boost to working capital was provided. No firms, however, indicated capital starvation to be a problem which compromised the ability of partnership to perform effectively and efficiently. To conclude, the impression given by many firms was that the buying-in process continued more or less out of respect for tradition.

DETERMINANTS OF SUCCESSFUL SELECTION FOR PROSPECTIVE PARTNERS:

Almost all firms cited good performance of qualified assistants as being a determinant of their successful selection for partner positions. In almost two thirds of the firms the specialism of the qualified assistants and the requirement to boost partner numbers in particular legal specialisms was viewed as important in determining selection. In over half of the firms the partner voting system and decision procedure utilised was viewed as a vital component of the selection process in deciding which of the firm's qualified assistants should become new partners. Over a third of the firms disclosed that consensus amongst the partners was very important in the overall decision process and success of candidates for partner places. It is concluded that clearly performance of the qualified assistant in the pre-partnership stage is a

vital determinant of successful selection. In this respect, the carrot of partner status can be used within the law firm to stimulate qualified assistants who are receptive to this signal/ incentive to compete with each other by demonstrating their suitability for partnership.

LENGTH OF PRE-PARTNERSHIP SERVICE OF THE QUALIFIED ASSISTANT:

The pre-partner period of the qualified assistant was variable in almost all firms, being dependent largely on the performance and quality of the qualified assistants in question, typically in combination with the changing demands of the practice in certain legal specialisms. The most common average expected period, however, was 4-6 years post qualifying, with the second and third most common being 0-3 years and greater than 6 years respectively. It is concluded that the qualified assistant faces an uncertain period regarding the length of time before being offered partnership (if at all). Perhaps the best indication of likelihood of success in being offered partnership is obtained by directly observing comparative progress of his peers. Not every qualified assistant has a desire to become a partner, and this was recognised to be the case within some of the sample firms interviewed (these firms disclosed the existence of permanent associates within their ranks).

Four firms also possessed senior associate categories between the ranks of qualified assistant and partner, this apparently performing the role whereby the firm could buy time before committing itself to making the partnership decision. This may avoid the situation of good qualified assistants leaving before an offer of partnership is forthcoming - by granting this more senior title the Q will experience an increase in status, typically accompanied by an increase in remuneration and his/ her name on the headed notepaper. It is concluded that this may successfully avoid good qualified assistants leaving, whilst retaining the carrot of full partnership status. By offering this position the Q will perceive that the firm has thought highly enough of him to differentiate him from the others. It is also concluded that this may open up the career options for lawyers who have no desire to become partners, yet nevertheless, want to move beyond the qualified assistant stage.

MAINTAINING AND EXPANDING PARTNERSHIP SIZE:

In by far the majority of firms, a decrease in partner numbers through death, retirement or resignation of an existing partner did not result in automatic replacement. Where automatic replacement was argued to be likely this was more usually viewed as necessary to maintain capacity of the firm or simply to maintain the expansion path of the firm. It was argued that it was possible (and desirable) to plan in advance for partners retiring - clearly the same could not be possible for the death or unexpected resignation/ exit of partners. It is concluded that firms tended not to have formal replacement policies and would only replace partners if this was viable and necessary. This non-replacement could inadvertently result in increased

personal income shares for remaining partners, but their was no evidence of any deliberate attempt to pursue non-replacement policies in order to effect this situation - behaviour which would mirror theorised behaviour of the [LMF].

It is further concluded that replacement of partners in the contemporary partnership is also tied very closely to shifts in emphasis in the mix of the specialisms of the law firm's business. Non-replacement of partners could occur where that area of business is no longer viable, but presumably in a thriving partnership, this area of work will have been superseded by another, which may perhaps require expansion of partner numbers in that area of legal work. Certain areas of work require different ratios and mixes of partners to assistants thereby rendering the examination of the firm in the absence of an understanding of its internal organisation, incomplete. For example, it is too easy to incorrectly conclude that where the ratio of qualified assistants to partners overall for a given firm was continually increasing, partners were deliberately restricting their numbers. It could simply be the case that the firm is moving into areas of work which require larger numbers of QAs working in teams under the leadership of a partner. The gearing of the partnership (ie. ratio of qualified assistants to partners) is vital to understand and this requires examining the legal specialisms and functionalisation within the law firm, and understanding the gearing requirements of individual units of the firm thereof. The issue of changing emphasis in areas of the firm's business and unique gearing requirements thereof, tends to obscure the issue of replacement and non-replacement of partners.

PARTNERSHIP GEARING:

The gearing between qualified assistants and partners of the firm was recognised as being important by all firms interviewed. Many firms noted either that gearing requirements varied between departments and/ or teams and that it was, therefore, difficult to deliberately either increase or decrease overall partnership gearing. Just fewer than one half of the firms attempted to maintain a constant overall gearing level at which they knew the firm operated effectively and efficiently.

Slightly fewer than one sixth of the sample firms noted that partnership gearing was increasing (ie. the ratio of qualified assistants to partners was increasing), whereas, no firms revealed the reverse to be the case. It is concluded that, in general, there appears a stronger tendency for partnership gearing to be increasing rather than decreasing in contemporary law firms, this being particularly true in large, corporate client firms where the requirement to work in teams and to do so cost effectively, is of paramount importance.

Table 10.5

Summary of Hypotheses results: Section Five - Internal Promotion and Firm Growth

	Evidence
Hypothesis 1: Law firms will tend to rely on internal promotion of qualified assistants rather than external hiring as the mechanism of growth of the partnership.	Consistent
Hypothesis 2: The law firm will employ formal screening mechanisms to discover the suitability of potential partners for the firm.	Consistent
Hypothesis 3: The decision to increase partnership number will be very formal and subject to a strict procedure.	Consistent
Hypothesis 4: Where the firm permits lateral hiring of partners from the external labour market, a probationary period as salaried partner will be used to reduce risks to the firm.	Consistent
Hypothesis 5: Qualified assistants will not exit the firm as the promise of partnership will act as an exit constraint and incentive to supply high levels of effort.	Consistent
Hypothesis 6: Partnership gearing (ratio of qualified assistants to partners) will be higher in larger firms/ corporate client firms due to the requirement to work in teams and do so cost effectively.	Consistent
Hypothesis 7: Law firms may have a tendency to restrict membership, like the Labour Managed Firm as this will preserve per member income.	Not Consistent

Summary and Conclusions - Chapter Nine:

It is recalled that the first section of Chapter Nine involved a comprehensive discussion of a full range of potential practice options for law firms, in the situation where practising prohibitions were absent. The implications for lawyers practising within each of these modes was discussed in the context of the respective incentive structure which would apply in each case.

In relation to the incorporated and multi-disciplinary [MDP] practice options in particular, their respective potential advantages and disadvantages were discussed against the backdrop of some popular arguments forwarded during debate of their possible introduction. It was concluded within this section that many of these popular arguments endorsing or denouncing such proposals often appeared incorrectly based, simply overlooking many important consequences which would likely stem from lawful introduction of alternative practice modes.

Chapter Nine also presented a discussion of the future of The Profession, wherein the empirical information collected was used to examine hypotheses established in the early part of the chapter. The following summarises the conclusions of the penultimate chapter of this thesis.

Questionnaire Section 7: The future of the profession:

Disadvantages of sole practice:

Sole practice in contemporary markets for legal services was perceived as being fraught with difficulties by almost all firms interviewed. Lack of specialisation opportunities and impracticality were frequently cited disadvantages, as were lack of support and exposure to high levels of personal risk. It is concluded that sole practice as an organisational mode for processing modern legal services is under increasing strain from current and ongoing changes that have been taking place in legal service provision over recent years.

Legal partnership advantages:

Almost all firms believed partnerships overcame sole practice difficulties of inability to specialise and lack of professional support. Consequently, partnerships are perceived to facilitate both advantages of mutual consultation and concurrent specialisation. Just fewer than half of the firms indicated partnerships permitted access to a greater range of technical inputs, with slightly fewer again mentioning team production advantages. Marginally fewer than one third mentioned risk sharing benefits of partnership practice, with other less significant advantages also being mentioned by firms. It is concluded that firms were in general agreement as to the existence of clear advantages of partnership practice over sole practice. Additionally, although fewer than one third explicitly indicated the risk sharing advantage of partnership practice, almost all firms disclosed this as a disadvantage of sole practice. Hence, group practice in partnership with other lawyers is generally perceived to be a preferable option to sole practice to the lawyer concerned with reducing high levels of diversifiable personal risk associated with legal practice.

Partnership limitations:

Those firms comprising over half of those interviewed, which believed partnership to be limiting as an organisational mode, most commonly and significantly disclosed the following;

1) Decision making,
2) Reluctance to delegate decision making authority and,
3) Unlimited liability,

either individually or in combination, as limitations of partnership (other less significant disadvantages were disclosed by other firms). The most significant conclusion forthcoming from examination of the disadvantages disclosed by firms is that limits of partnership are determined more by authority and delegation problems than by capital or simple scale problems.

THE ISSUE OF APPROPRIATE EXTENT OF LIABILITY FOR AN INCORPORATED LAW FIRM:

Over one third of firms interviewed perceived the issue of provision of adequate professional indemnity (PI) insurance to cover liability losses and afford client protection, to be a more important issue than the more academic question of the appropriate extent of liability. Firms were generally confused regarding this issue with an equal number arguing that unlimited liability should remain and that limited liability should apply. 9 firms reckoned that malfeasant solicitors within an incorporated law firm would be personally liable at the end of the day in any case. It is thereby concluded from this confusion that the issue of degree of liability is rather academic. The issue of adequate PI cover and the ability to take personal action against incompetent solicitors would appear to take precedence with regard to ensuring client protection.

OPPORTUNITIES FOR INCORPORATION:

Overall, it is concluded that incorporation appears to be a 'lame duck' since almost all of the firms could envisage no specific areas of work and/ or type of firm where incorporation would be ideally suited. A small number of firms thought that perhaps large firms and/ or corporate client work may be amenable to this practice mode but conveyed uncertainty regarding exactly why this should be the case, or exactly what the advantages would likely be..

SHAREHOLDERS OF THE INCORPORATED LAW FIRM:

All firms envisaged partners of the then partnership becoming the shareholders/ directors of the new incorporated practice. A few firms envisaged employee share ownership as an additional possibility, as did as similar number, outside pure equity interests. It was generally conceded, however, that outside pure equity interests may be perhaps further in the future, if at all. It is, therefore, concluded that information provided here was indicative that the profession has a definite desire to restrict firm membership to lawyers only, to seek to prevent potential property rights problems. This restriction may also importantly aid screening.

DISADVANTAGES OF THE INCORPORATED LAW FIRM:

Over two thirds of those interviewed believed that there to be potential disadvantages to incorporated law firms. The best summary of this section is to conclude that very few advantages over partnership could be envisaged, raising the remaining question, 'what are the real advantages of incorporation ?'. It is additionally concluded that the major disadvantages of partnership, namely decision making problems and a resistance to delegate decision

making authority, would fail to be solved via incorporation - they would simply re-emerge albeit in a slightly different form.

Opportunities for MDP:

Almost three quarters of those interviewed believed MDP could yield potential advantages for the legal profession. No firms, however, were capable of identifying a type of firm which would be ideally suited, but many firms indicated specific areas of work which they perceived would be. In answering this question, however, by far the majority of firms indicated that the perceived advantages of MDP were presently available via effective networking with other law firms and providers of professional and other services. Networking also avoided potential problems that MDP may give rise to. It is thereby concluded that, although MDP appeared substantially more popular than incorporation, there was by no means overwhelming enthusiasm for its introduction.

MDP and liability sharing with non-lawyers:

It is concluded here, as was expected would be the case, that by far the majority of those interviewed would find sharing liability with non-lawyers unattractive. Very few firms indicated that they would find it not unattractive. Some firms from both of these groups qualified their answers by indicating that it may be a necessary evil, or that it would depend on rules regarding PI insurance and practising, or that it would depend very much on individual persons concerned rather than their professional labels. It is concluded here, therefore, that the general attitude expected of the lawyers interviewed (ie. that liability sharing would be unattractive due to monitoring and property rights problems) appeared to be fairly widespread.

MDP problems:

The most commonly cited problem envisaged was that of the difficulty of designing and administering a common set of mutually acceptable practising rules. Other disadvantages, such as the potential for conflicts of interest to arise, and the fact that sophisticated commercial clients would be unlikely to use MDPs were cited by a few firms. Fewer firms indicated that MDP could cause the legal profession to be swallowed up by, for example, large accountancy practices, with still fewer mentioning the undesirable effect MDP would be likely to have of seriously diluting healthy competition between professional groups.

To conclude, it is not difficult to imagine that should MDPs become legally sanctioned and there is subsequent adoption of this practice form by those able to partake, many if not all of these problems could be resolved or ameliorated to a large extent. This would permit the full

potential of MDP as an advantageous practice option in appropriate circumstances to be realised.

Table 10.7

Summary of Hypotheses results: Section Seven - The Future of the Profession

	Evidence
Hypothesis 1: The risk attending the lawyers human capital could be expected to render group practice with other lawyers an attractive option.	Consistent
Hypothesis 2: The limits of partnership are likely to be determined by authority and delegation problems rather than capital or size problems.	Consistent
Hypothesis 3: Incorporation of legal practices is not likely to yield significant advantages to the law firm.	Consistent
Hypothesis 4 In the case of incorporated legal firms there will be a tendency to want to restrict membership of the firm to lawyers only due to property rights problems.	Consistent
Hypothesis 5: In the case of Multi-disciplinary practice sharing of liability with other professionals will be unattractive due to monitoring and property rights problems.	Consistent

Agenda for future research:

It is recalled that many of the features of law firms eluded to by Gilson and Mnookin in their analysis of law partnerships were not found to exist in many of the firms examined in this UK study [9]. Nevertheless, their framework provided a useful reference point at which to start the current empirical investigation. It would be interesting to investigate the issues covered in this thesis for the same sample of firms at some point in the near future.

It is fair to say that many of the Gilson and Mnookin problems were argued to exist in large USA firms, of which few firms in the UK come close to in terms of size measured by numbers of partners. However, in the context of the sample covered within this thesis, it was evident that within the larger firms interviewed, many of the Gilson and Mnookin type management and sharing bargain issues were already viewed as increasingly relevant. Many large firms disclosed that they were already starting to face similar problems, or that they perceived they would have to soon deal with them. Accepting that current trends are likely to continue, large firms in the UK are likely to continue to experience growth in their partner members, and it is therefore proposed that it would be useful to re-visit such firms to examine the extent to which Gilson and Mnookin problems of large partnership practice had emerged. Had such problems become more commonplace and germane, this follow up would permit determination of how firms had responded to cope with such problems. For example, this would permit us to determine whether those firms who currently indicated that they were considering switching from a true sharing bargain to a productivity based one, had effected the change, and what the overall effect had been where sharing methods had changed.

It would also be useful to return to the same sample firms to see if they had increased the extent of their specialisation in terms of the range of legal work offered and/ or formal functionalisation of this into specialised departments of the firm.

Firms currently noted a general shift towards complementing their internal hiring process with external hiring via headhunting, mergers and acquisitions and the like. If this shift became more pronounced as a response to cope with increased scale and specialisation requirements, it would be interesting for the follow up study to determine, amongst a whole range of others, issues such as;

1) Whether this trend had required them to place more formal constraints on partners via, for example, measurement of productivity and/ or the introduction of more explicit incentives tied to direct compensation for certain activities.

2) Whether this trend had required that the firm introduced more explicit screening procedures to cope with greater numbers of externally hired partners, whose suitability for that firm is less visible and less readily assessable.

Additionally, it would be interesting to examine whether the current trend for the profession to increasingly split into two distinct sectors, namely private and commercial client firms, had become more pronounced, and if so, what effect this had on the internal structure of those firms previously interviewed. For example, the internal structure may have altered to accommodate new or more precisely defined categories of non-partner lawyer such as, permanent associate, salaried partner, senior associate, and the like, to facilitate growth and specialisation.

The role for information within the client/ firm relationship was currently predicted by many firms to be likely to assume greater importance in the future. Returning to the sample firms would permit us to determine whether this actually was the case or not, and if it was, what changes to firm behaviour this had effected.

It would also be useful within a follow up study to determine whether firms were experiencing any greater incidence of shirking, grabbing and leaving activities. It was concluded that this could be a possible consequence of potential breakdown of traditional screening mechanisms within the typical law firm in the future. If a future study could investigate this, it would permit us to determine how firms were attempting to react to any such problem, and disclose the nature of any mechanisms firm had introduced to attempt to suppress such behaviour.

It would be of interest to examine in future the extent to which growth in joint ventures/ formal associations of law firms, both at a national and international level, had occurred. In this context, it would be interesting to examine the extent to which law firms were achieving internationalisation/ globalisation, what benefits this was expected to precipitate, what form it was taking, and what specific problems were being encountered in the process.

In the area of proposed and continuing deregulation of legal services, especially in the specific area of legitimate practice options, it is currently uncertain exactly when (and perhaps even if) the proposed changes are likely to occur. It would be interesting to interview the same firms post deregulation to determine how, if at all, their overall practising arrangements had altered.

A follow up study, repeating exactly the current empirical survey for the same sample of firms, but modified to take on board any interim changes in regulation of the legal profession, could address many if not all of the above issues.

In terms of development of theory of organisational relationships, more work requires to be done regarding the how effective ex-ante screening for suitable contractual agents may reduce the requirement for formal ex-post monitoring of contractual performance[10] .

Chapter Ten-Endnotes

1. See; Simon, H.A., *Models of Man.* John Wiley & Sons, 1957. See also; Theories of decision making in economics and behavioural science, *American Economic Review*, Vol.49 (June), 1959, pp.253-58. See also; *Administrative Behaviour.* 2nd edition, New York, Macmillan, 1961.

2. See; Gilson, R.J. & Mnookin, R.H., Sharing among the human capitalists: An economic enquiry into the corporate law firm and how partners split profits, *Stanford Law School Working Paper*, Vol.37 No.16, 1984.

3. See; Gilson and Mnookin (1984) *Supra* Note 3.

4. See; Gilson and Mnookin (1984) *Supra* Note 3.

5. See; Gilson and Mnookin (1984), *Supra* Note 3.

6. See; Gilson and Mnookin (1984), *Supra* Note 3.

7. See; Gilson and Mnookin (1984), *Supra* Note 3.

8. See; Gilson, R. & Mnookin, R., Coming of Age in a Corporate Law Firm: The Implicit Contract for Associates, *Stanford Law School Working Paper*, No.42, 1988.

9. See; Gilson and Mnookin (1984), *Supra* Note 3.

10. See: Stephen, F.H. & Gillanders, D.D., Ex-post monitoring versus ex-ante screening in the New Institutional Economics, *Journal of Institutional and Theoretical Economics (JITE)*, Vol. 149/4 (1993), pp. 725-730.

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APPENDIX I: THE ORGANISATION OF LAW FIRMS - QUESTIONNAIRE

The information requested in the following questionnaire will be used solely for the purposes of my research and can be given with confidence that a duty of confidentiality will apply at all times. In addition any subsequent conditions imposed by a prospective respondant will be respected. The principal aim of my research is to investigate what factors have brought about the current structure of the legal profession in the UK and also to examine any features of legal practice that place specific organisational requirements upon those who seek to render legal services to the consumer. Concurrently I would like to obtain the opinions of various members of the profession on current or prospective developments within the profession and discover any fears or reservations they may hold in relation to certain practice rule amendments. In relation to this it would be particularly useful to obtain opinions of lawyers from a broad spectrum of firm types and firm sizes.

INTRODUCTION:

The purpose of this questionnaire is to abstract information pertaining to the organisation of law firms. The study of the professional partnership form of organisation with its characteristic features has been neglected to a great extent in economic analysis. It is my purpose to gather information from law firms which will foster an understanding as to the reasons why law firms are organised in the manner in which they are.

SECTION ONE: THE FIRM

The first section of questions relate to the type of law firm being questioned and it is anticipated that it will be possible to categorise respondent firms into groups using some simple classification arrangement. The following information is necessary in order to facilitate this categorisation.

1.Name of Firm (FIRMNAME): ___

2.Location of Main Office (MAINLOC): __

3.Number of Offices/Branches (NUMOFF): ___

4.Total number of individuals employed by the overall organisation (NUMINDIV): ____

5.Number of Partners (PTR): ___

6.Number of Qualified Assistants (QA): ___

Number of Legal Executives (LEX): ___

Number of Articled Clerks (ARTCLAR): ___

7.Proportion of business transacted with commercial clients (PROPCOMM): _ _

8.Proportion of business transacted with private clients (PROPPRIV): _ _

9. Do you use standard documents, precedents, routines etc. in transactions ?:

Standard documents/ precedents etc. (STDDOC)	0	1	7	8	9
In all transactions (ALLTRANS)	0	1	7	8	9
In some transactions (SOMETRAN)	0	1	7	8	9
Document networking (NETWORK)	0	1	7	8	9
Flow charting (FLOWS)	0	1	7	8	9
Depends on work type (DEPWORK)	0	1	7	8	9
Cannot use std. docs (NOTSTD)	0	1	7	8	9
Work too specialised (SPECWORK)	0	1	7	8	9
Increasing standardisation (INCSTD)	0	1	7	8	9
Need to introduce this more in future (FUTSTD)	0	1	7	8	9

10.How are the firm's offices organised?:

One office with specialised depts (ONESPEC)	0	1	7	8	9
One office/ no depts. (NODEPTS)	0	1	7	8	9
Specialist vertical departments and horizontal teams (VERTHORI)	0	1	7	8	9
>1 office/ general offices (GENOFFIC)	0	1	7	8	9
>1 office/ specialised offices (SPECOFFI)	0	1	7	8	9
Foreign offices (FOROFF)	0	1	7	8	9
Affiliated offices abroad (AFFOFF)	0	1	7	8	9
UK Groupings/ Joint ventures (UKGROUP)	0	1	7	8	9
Difficult work referred to head office (HEADOFF)	0	1	7	8	9
Puppet offices to gather business or for meetings only (PUPPET)	0	1	7	8	9
Local & international partnership (LOCINT)	0	1	7	8	9

11. How would you describe the firm?:

Full service private client (FULLPRIV)	0	1	7	8	9
Full service commercial client (FULLCOMM)	0	1	7	8	9
Specialist commercial (SPECCOMM)	0	1	7	8	9
Specialist private (SPECPRIV)	0	1	7	8	9
If private then tied to commercial clients (TIEDCOMM)	0	1	7	8	9
Full service comm. with niches (COMMNICH)	0	1	7	8	9
Full service priv. with niches (PRIVNICH)	0	1	7	8	9
Most types of private client work (MOSTPRIV)	0	1	7	8	9
Most types of commercial client work (MOSTCOMM)	0	1	7	8	9

12.Please provide a brief outline of the history of the firm and how it now reached its present form.

Organic growth (ORGANIC)	0	1	7	8	9
Mergers (MERGERS)	0	1	7	8	9
New firm (NEWFIRM)	0	1	7	8	9
Takeover (TAKEOVER)	0	1	7	8	9
Bolt-ons (BOLTS)	0	1	7	8	9
Headhunting (HEADHUNT)	0	1	7	8	9
Agencies contacting firm (AGENCIES)	0	1	7	8	9

SECTION TWO: THE CLIENT/FIRM RELATIONSHIP

The questions in this section relate to the relationship between the firm and the client and the characteristic features of this relationship in the law firm context.

1.Where standardisation can be introduced into transactions does this lead to lower service prices to the client?:

Lower price to client (LOWPRICE)	0	1	7	8	9
Higher price to client (HIGHPRIC)	0	1	7	8	9
Greater efficiency for firm (HIGHEFF)	0	1	7	8	9
Greater profit margins (PROFITUP)	0	1	7	8	9
Only firm benefits (FIRMBEN)	0	1	7	8	9
Necessary to compete (NECCOMP)	0	1	7	8	9
Mutual benefits (MUTBENS)	0	1	7	8	9

2.Is information held on a particular established client of the firm useful in providing other services to the client if he should wish them?:

Client database (DATABASE)	0	1	7	8	9
Client profiles (CLIPROF)	0	1	7	8	9
Limited info kept (LTDINFO)	0	1	7	8	9
Info useful (INFOUSE)	0	1	7	8	9
Info limited use (LTDUSE)	0	1	7	8	9
Cross-selling services (XSELL)	0	1	7	8	9
Need to X-sell more in future (FUTXSELL)	0	1	7	8	9
Depends on service type (DEPTYPE)	0	1	7	8	9
Greater need in future for database & use of client info (FUTINFO)	0	1	7	8	9

3.Does such client information provide the firm with an advantage over other firms who would have to discover such information in order to start their own client file in order to initiate services?:

Advantages over other firms (ADVCOMP)	0	1	7	8	9
Depends on client type (DEPCLIEN)	0	1	7	8	9
Limited advantages (LTDADV)	0	1	7	8	9
Relationship established (RELATE)	0	1	7	8	9
Benefits to clients also (CLIBEN)	0	1	7	8	9
Confidence/trust in firms abilities (CONFID)	0	1	7	8	9
Time so money saved (TIMMON)	0	1	7	8	9
Search avoidance (SEARCHAV)	0	1	7	8	9
Knowledge based advantages (KNOWLED)	0	1	7	8	9
Other (OTHER)	0	1	7	8	9

4.Do established clients provide a predictable flow of work?:

Commercial clients (COMMCLI)	0	1	7	8	9
Private clients (PRIVCLI)	0	1	7	8	9
Steady but not predictable (STEPRED)	0	1	7	8	9
Most clients return but less loyal than before (LESSLOY)	0	1	7	8	9
Clients only use us for particular specialised services (SPECSERV)	0	1	7	8	9

5.An important long established client informs you that he is in future going to employ the services of another law firm. What is the firm's reaction?:

Attempt to retain client (RETAIN)	0	1	7	8	9
Clients don't inform until too late (TOOLATE)	0	1	7	8	9
Often beyond our control (BEYCONTR)	0	1	7	8	9
Discover reasons (DISCREAS)	0	1	7	8	9
Patch up differences (PATCHUP)	0	1	7	8	9
Seek a meeting with the client (CLIMEET)	0	1	7	8	9
Prevention rather than cure (PREVCURE)	0	1	7	8	9
Regular client audits (AUDIT)	0	1	7	8	9
Other (OTHER2)	0	1	7	8	9

6.What factors do you believe to be important signals of quality and reputation to your own and prospective clients?:

Reasonable fee (REASFEE)	0	1	7	8	9
Speed/efficiency of work done (EFFWORK)	0	1	7	8	9
Accuracy of work completed (ACCWORK)	0	1	7	8	9
Personnel (PERSONN)	0	1	7	8	9
Personal service (PERSERV)	0	1	7	8	9
Published articles (PUBLART)	0	1	7	8	9
Client care (CLICARE)	0	1	7	8	9
General business skills (BUSSKILL)	0	1	7	8	9
High level of Partner input (PTRINPUT)	0	1	7	8	9
Other (OTHER3)	0	1	7	8	9

7.How significant do you believe the firm name to be in conveying reputation and signalling quality to your own and prospective clients? (NAMESIG):

0 NOT SIGNIFICANT AT ALL
1 LIMITED SIGNIFICANCE
2 SIGNIFICANT
3 VERY SIGNIFICANT
4 NOT SIGNIFICANT YET SINCE NEW FIRM
7 FTA
8 DK
9 WS

8.In what way does the firm respond to such client quality perceptions?:

Brochure (BROCHURE)	0	1	7	8	9
Inhouse/ client seminars (SEMINAR)	0	1	7	8	9
Personnel training (PERSTRAI)	0	1	7	8	9
Sponsorship/mailshots/advertising etc. (PROMO)	0	1	7	8	9
Personal service (PERSONAL)	0	1	7	8	9
Beauty contests for comm. clients (BEAUTY)	0	1	7	8	9
Establish referral network (ESTREF)	0	1	7	8	9
PR consultants (PRCONS)	0	1	7	8	9
Give service to back up claims (BACKUP)	0	1	7	8	9
Other (OTHER4)	0	1	7	8	9
More marketing needed in future (MKTFUT)	0	1	7	8	9

SECTION THREE: INSIDE THE FIRM

The following questions relate to the internal organisation of the law firm. Here, I endeavour to investigate some of the features within the firm that act to determine how individuals within the firm react to the incentives that confront them.

1.Does a formal hierarchical management structure exist between the partners?:

Management structure (MANSTRUC)	0	1	7	8	9
Committees/ subcommittees system (COMMITT)	0	1	7	8	9
Management Board (MANBOARD)	0	1	7	8	9
Managing partner (MANGPTR)	0	1	7	8	9
Managing partner internal (MPTRINT)	0	1	7	8	9
Senior partner (SENPTR)	0	1	7	8	9
Senior partner external (SENEXT)	0	1	7	8	9
Chief executive officer (CEO)	0	1	7	8	9
Chief operational offices (COO)	0	1	7	8	9
Non-lawyer managers/ directors/ controllers (NONLAWY)	0	1	7	8	9
Full time ptr managers (FULLTIME)	0	1	7	8	9
Managers still fee earning (FEEEARN)	0	1	7	8	9
Executive and non-executive positions (EXNONEX)	0	1	7	8	9
Moving to more formal structure in future (FORMAL)	0	1	7	8	9

2.Do any of the partners assume specialised individual functions?:

Management specialities (MANSPEC)	0	1	7	8	9
Legal specialities/ Depts. (LEGSPEC)	0	1	7	8	9
Committee comveynor (COMCONV)	0	1	7	8	9
Departmental heads (DEPTHEAD)	0	1	7	8	9
Greater specialisation in future (SPECFUTU)	0	1	7	8	9

3.Where the firm has specialised individual departments, are these headed by individual partners or do qualified assistants head departments?:

Partner dept. heads (PTRHEAD)	0	1	7	8	9
>1 Partner heads a dept. (PTRSHEAD)	0	1	7	8	9
QA dept. heads (QAHEADS)	0	1	7	8	9
Committee/ conveynor in each dept. (DEPTCOMM)	0	1	7	8	9
Pyramid teams (PYRAMID)	0	1	7	8	9

4.If a formal partner hierarchy exists, is this based on seniority or is some other factor involved?:

Formal seniority (FORMSEN)	0	1	7	8	9
Informal seniority (INFOSEN)	0	1	7	8	9
Egalitarian (EGAL)	0	1	7	8	9
Junior & Senior partners (JUNSEN)	0	1	7	8	9
Salaried & Equity partners (SALEQUIT)	0	1	7	8	9
Unequal voting rights (VOTING)	0	1	7	8	9

SECTION FOUR: ALLOCATION OF CLIENTS

This section *relates to the* manner in which the firm allocates clients between individuals and also to the possible problems that could *arise in the event of a partner* or qualified assistant leaving.

1.Do partners have their own client portfolios or are all clients part of one large firm portfolio?: If one large firm portfolio exists, omit next question.

Firm portfolio (FIRMPORT)	0	1	7	8	9
Partner portfolios (PARTPORT)	0	1	7	8	9
Qualified assistants (QUALPORT)	0	1	7	8	9
Attempt to reduce hoarding (REDHOARD)	0	1	7	8	9
Fear of lawyer exit (FEAREXIT)	0	1	7	8	9
Barrier to X-sell (BARRIER)	0	1	7	8	9
Depends how long they have been with firm (HOWLONG)	0	1	7	8	9
Hoarding reducing due to specialisation (HOARDLES)	0	1	7	8	9

2.Do you believe clients to be loyal to the firm as an entity or to a particular individual within the firm?

Firm loyalty (FIRMLOY)	0	1	7	8	9
Individual loyalty (INDIVLOY)	0	1	7	8	9
Less client loyalty than before (LESSLOY2)	0	1	7	8	9
Loyal to team within firm (TEAMLOY)	0	1	7	8	9
Client research (RESEARCH)	0	1	7	8	9

3.Are clients continually assigned to the same individual within the firm or is the client assigned to whoever is available at the time?:

Same individual regardless of work type (SAMEIND)	0	1	7	8	9
Only same individual if within that speciality (IFSAME)	0	1	7	8	9
System of contact partner and referral (CONTPTR)	0	1	7	8	9
>1 contact partner (CONTPTRS)	0	1	7	8	9

Should a partner or qualified assistant announce to the firm his intention to leave, this may be of concern to the firm in that some clients may also leave with him. The following questions relate to this possibility.

4.Are restrictive covenants used within the firm to ensure that the above could not occur?:

Restrictive covenants in partnership agreement (RESTCOV)	0	1	7	8	9
Restrictive covenants for all employees (RCEMP)	0	1	7	8	9
Restrictive covenants for QA'S (QARESTCO)	0	1	7	8	9
Likely to be ineffective anyway (INEFFECT)	0	1	7	8	9
Never had to enforce them (NEVER)	0	1	7	8	9
Partners & QAs do leave but do not take clients (DOLEAVE)	0	1	7	8	9
Choice of client at end of day (CLICHOIC)	0	1	7	8	9

5.In the absence of restrictive covenants and specific organisational systems what do you believe prevents partners and/or qualified assistants from leaving with clients in tow?:

Loyalty to firm (FIRMLOY2)	0	1	7	8	9
Present rewards (PRESREW)	0	1	7	8	9
Prospect of promotion (PROSPECT)	0	1	7	8	9
Good career structure (CAREER)	0	1	7	8	9

Difficulty of exit (DIFFEXIT)	0	1	7	8	9
Prestige of firm (PRESFIRM)	0	1	7	8	9
Value > inside firm than outside (VALUE)	0	1	7	8	9
Could not duplicate team outside (DUPTEAM)	0	1	7	8	9
Other (OTHER5)	0	1	7	8	9

6.Does the firm recognise that different classes of clients have differing degrees of sophistication and tailor their activities accordingly?:

More with private clients (PRIVCLI2)	0	1	7	8	9
More with commercial clients (COMMCLI2)	0	1	7	8	9
Alter reporting levels (REPLEVEL)	0	1	7	8	9
Brochures used (BROCUSED)	0	1	7	8	9
Handhold if necessary (HANDHOLD)	0	1	7	8	9
Seek out clients requirements (SEEKOUT)	0	1	7	8	9
Other (OTHER6)	0	1	7	8	9

SECTION FIVE: INTERNAL PROMOTION AND FIRM GROWTH

The following questions relate to the manner in which the firm hires individuals to fill positions at different levels within the firm. Here it is anticipated that some explanation of how the firm grows will be exposed.

1.What is the mechanism for deciding to increase the number of partners?

Formal decision process (FORMAL2)	0	1	7	8	9
Decision of full partners meeting (FULLPTR)	0	1	7	8	9
Decision of committee of partners (COMMPTRS)	0	1	7	8	9
Partners vote (PTRVOTE)	0	1	7	8	9
Committee accepts/ rejects nominations (COMMDEC)	0	1	7	8	9
Candidates nominated by dept./ committee etc. (CANDNOM)	0	1	7	8	9
Seniority requirement (SENREQ)	0	1	7	8	9
3rd party tests (THIRD)	0	1	7	8	9
Prevent good QAs leaving (PREVENT)	0	1	7	8	9

2.When it is decided that another partner should join, are individuals attracted from outwith the firm or are qualified assistants promoted to partner level?

Internal promotion (INTONLY)	0	1	7	8	9
External candidates (EXTCAND)	0	1	7	8	9
If external then salaried first (SALARY)	0	1	7	8	9
Headhunting of partners (HEDHUNT2)	0	1	7	8	9
Internal except if merger/ takeover or bolt-on (INTMERG)	0	1	7	8	9
Headhunting in future (HEADFUTU)	0	1	7	8	9

3.Do new partners have to buy into the partnership?

New partners buy into partnership (PARTBUY)	0	1	7	8	9
Not initially & salaried first (NOTINIT)	0	1	7	8	9
Deferrance of drawings (DEFDRAW)	0	1	7	8	9
No payment for goodwill (NOGWILL)	0	1	7	8	9
Only contribution to working capital (WORKCAP)	0	1	7	8	9

4.If qualified assistants fill the firm's partner vacancies, what is the mechanism of selection between prospective applicants/candidates?

Selection mechanism (SELMECH)	0	1	7	8	9
Performance as QA (PERFQA)	0	1	7	8	9
Partners vote (PTRVOTE2)	0	1	7	8	9
Consensus (CONSENS)	0	1	7	8	9
Specialism needed (SPECNEED)	0	1	7	8	9
Other (OTHER7)	0	1	7	8	9

5.What is the average expected period of time for a qualified assistant to be with the firm before being offered a partnership?

No fixed time as QA (PERIODQA)	0	1	7	8	9
Depends on quality of QA (QUALQA)	0	1	7	8	9
Usually 0-3 years (USUAL03)	0	1	7	8	9
Usually 4-6 years (USUAL46)	0	1	7	8	9
Usually more than 6 years (USUALGT6)	0	1	7	8	9
Senior associate status between QA & Partner (SENASSOC)	0	1	7	8	9
Other (OTHER8)	0	1	7	8	9

6.When the number of partners decreases due to retirement, death or leaving is the vacancy created always filled?

Automatic replacement (AUTOREPL)	0	1	7	8	9
Depends on which dept./ speciality (DEPDEPT)	0	1	7	8	9
Usually to maintain capacity (CAPACIT)	0	1	7	8	9
Usually due to firm expanding (EXPAND)	0	1	7	8	9
Need to maintain quality and profitability (QUALPROF)	0	1	7	8	9
Retirements planned for in advance (RETPLAN)	0	1	7	8	9

7.When the firm expands, is a fixed ratio of partners to qualified assistants maintained or is only the number of partners or qualified assistants increased? (GEARING):

Aware of gearing ratio (AWARE)	0	1	7	8	9
Ptr:QA increasing (GEARRED)	0	1	7	8	9
QA:Ptr increasing (GEARINC)	0	1	7	8	9
Attempt to maintain constant overall gearing (OVERALL)	0	1	7	8	9
Gearing varies between depts./ work type (DEPTGEAR)	0	1	7	8	9
Depends on the composition of teams (TEAMGEAR)	0	1	7	8	9

SECTION SIX: THE SHARING BARGAIN

In this section of questions, the manner in which the firm distributes the firm's residual income between the partners of the firm, after all expenses and costs, is the focus of attention. The sole purpose here is to understand the mechanism of sharing the income between the partners and hence figures are of little importance.

1.Does the partnership have the sole function of sharing expenses between individual practitioners on the basis of accounting techniques?:

Expenses sharing model (EXPSHARE)	0	1	7	8	9
Eat what you kill model (EATKILL)	0	1	7	8	9
Partners are individual cost/ profit centres (PTRCENTR)	0	1	7	8	9

2.Are partners assigned to groups dependant on seniority?

Seniority groups based on years as partner (SENGROUP)	0	1	7	8	9
Partners given points on becoming equity partner (PTRPOINT)	0	1	7	8	9
Points increase with seniority (POINTINC)	0	1	7	8	9
Salaried partners salaries fixed by equity partners (SALFIX)	0	1	7	8	9
Salaried partners get uniform profit share (SALPROF)	0	1	7	8	9
Partners split profits equally (EQUAL)	0	1	7	8	9

3.Does the partner's income depend on the group to which he is assigned?:

Income share depends on seniority group (INCSEN)	0	1	7	8	9
Income share depends on number of points (INCPOINT)	0	1	7	8	9
Partners can be accelerated or held back on ladder for performance (ACCDECEL)	0	1	7	8	9
Income shares of equity partners determined by committee (DETCOMM)	0	1	7	8	9

4.Do all partners of a single seniority class earn the same?:
If answer is yes, omit next question.

All members of a single seniority group earn the same share (SGSHARE)	0	1	7	8	9
All partners with the same number of points earn the same share (PTSSAME)	0	1	7	8	9

5.If partners of a single seniority class earn differing amounts, what is the basis of the differentiation?:

Contribution (CONTRIB)	0	1	7	8	9
Merit payments (MERIT)	0	1	7	8	9
Productivity (PRODUC)	0	1	7	8	9
Committee decides (COMMDEC2)	0	1	7	8	9
Board decides (BOARDDEC)	0	1	7	8	9
Senior/ managing partner decides (PTRDEC)	0	1	7	8	9

6.Where class incomes are the same for each partner of a seniority class, do incomes between classes vary in a fixed predetermined ratio?:

Ratio is fixed since lockstep model (LOCKSTEP)	0	1	7	8	9
Ratio variable since number of points changes (POINTSCH)	0	1	7	8	9
No fixed ratios since productivity included (PRODINC)	0	1	7	8	9

7.What length of time does it take to reach full seniority class from the time of initial promotion from qualified assistant to partner?:

No definite time since no full seniority (NOTSEN)	0	1	7	8	9
Depends on capital contribution (CAPCONT)	0	1	7	8	9
0-5 Years (YEARS05)	0	1	7	8	9
6-10 Years (YEARS610)	0	1	7	8	9
11-15 Years (YEAR1115)	0	1	7	8	9
16-20 Years (YEAR1620)	0	1	7	8	9
Depends on performance (PERFORM1)	0	1	7	8	9

8.Is the weighting of income skewed towards the early or later years of partnership or does it rise steadily at a constant rate?:

Rises steadily (STEADY)	0	1	7	8	9
Weighted to earlier year (EARLY)	0	1	7	8	9
Weighted to latter years (LATTER)	0	1	7	8	9
Plateaus at maximum level (PLATEAU)	0	1	7	8	9
Tails of towards retirement (TAILSOFF)	0	1	7	8	9
Depends on performance (PERFORM2)	0	1	7	8	9

9.Is some measure of individual partner productivity incorporated in income determination?:

Partner productivity determinant of income (PARTPROD)	0	1	7	8	9
Adhoc measure taken (ADHOC)	0	1	7	8	9
Contribution (CONTRIB2)	0	1	7	8	9
Precise formula (FORMULA)	0	1	7	8	9
Special fund for productivity payments (SPECFUND)	0	1	7	8	9
Under examination at present (UNDEREX)	0	1	7	8	9

10.Is the time spent by a partner attending to a client's business measured in any way?

Time recorded for billing (BILLING)	0	1	7	8	9
Time recorded for management purposes (MANAG)	0	1	7	8	9
Partner time/ billing targets (TARGET)	0	1	7	8	9
Time spent direct determinant of income (TIMINC)	0	1	7	8	9
Individual partner budgets (BUDGET)	0	1	7	8	9

11.Are partners required to spend a minimum number of hours per week attending to client business within the organisation?:

Strict minimum set in contract (MINSET)	0	1	7	8	9
Norm recognised (NORMREC)	0	1	7	8	9
Consistent with budget (CONBUDG)	0	1	7	8	9
Departmental income budgets/targets (DEPTBUDG)	0	1	7	8	9

12.Is there any organisational system which ensures any minimum hours requirement is upheld?

Peer group pressure (PEER)	0	1	7	8	9
Fee income targets (FEETARG)	0	1	7	8	9
Expense budgets (EXPBUDG)	0	1	7	8	9
Time recording (TIMEREC)	0	1	7	8	9

13.Do any incentives exist to encourage a partner to spend more hours than the minimum on client business?

Direct compensation (DIRCOMP)	0	1	7	8	9
Profit at end of day (PROFIT)	0	1	7	8	9
Necessity of work (NECWORK)	0	1	7	8	9
Committees monitor (COMMONIT)	0	1	7	8	9
Hope of promotion (PROMHOPE)	0	1	7	8	9
Control workload (CONTWORK)	0	1	7	8	9
Loyalty to firm and other factors (LOYFIRM)	0	1	7	8	9
Increase income share (INCINCOM)	0	1	7	8	9
Retain clients & increase client base (RETAINC)	0	1	7	8	9
Prestige/ success (PRESTSUC)	0	1	7	8	9
Enhance contribution (ENHANCE)	0	1	7	8	9
Considering new sharing model (CONSIDER)	0	1	7	8	9
Other (OTHER9)	0	1	7	8	9

14.Where a partner demands an increase in his income is such a request likely to be more successful if he threatens to leave?

More successful (MORESUC)	0	1	7	8	9
Less successful (LESSSUC)	0	1	7	8	9
Not done this way (NOTWAY)	0	1	7	8	9
May work with partner but not QA (PTRNOTQA)	0	1	7	8	9
Never had situation (NEVERHAD)	0	1	7	8	9
Depends on individual (DEPINDIV)	0	1	7	8	9
Agreed in advance so can't (ADVANCE)	0	1	7	8	9
May be problem in future (PROBFUT)	0	1	7	8	9

15.Are partners directly compensated for time spent on the following activities?:

Attraction of new clients (NEWCLI)	0	1	7	8	9
Non-billable client attention (NONBILL)	0	1	7	8	9
Supervision and training (SUPTRAN)	0	1	7	8	9
Management and administration (MANADMIN)	0	1	7	8	9
No direct compensation (NODIRCOM)	0	1	7	8	9
May change in future (MAYCHANG)	0	1	7	8	9

If answer is yes for all four, omit next question.

16.If they are not compensated for these what motivates them to engage in such activities?:

Reflected in contribution (REFCONTR)	0	1	7	8	9
Flair or ability so left to them (FLAIR)	0	1	7	8	9
Done for the good of the firm (FIRMGOOD)	0	1	7	8	9
Necessity (NECESS)	0	1	7	8	9
Delegated by ptr meeting/committee (DELEG)	0	1	7	8	9
Other (OTHER10)	0	1	7	8	9

17.Does a partner/ department/ committee of the firm specialise in any of these activities?:

Specialist Partners are responsible for all these activities (PARTRESP)	0	1	7	8	9
Training & supervision by specialist partners (PTRTRAIN)	0	1	7	8	9
Man & Admin by specialist partners (PTRMAN)	0	1	7	8	9
Non-billable attention by specialist partners (PTRNOBIL)	0	1	7	8	9
New client attraction by specialist partner (PTRNEWCL)	0	1	7	8	9
Depts. are responsible for all these activities (DEPTRESP)	0	1	7	8	9
Training and supervision by depts. (DEPTTRAI)	0	1	7	8	9
Man & Admin by depts. (DEPTMAN)	0	1	7	8	9
Non-billable attention by depts. (DEPTNOBI)	0	1	7	8	9
New client attraction by depts. (DEPTNEWC)	0	1	7	8	9
Committees are responsible for all these activities (COMMRESP)	0	1	7	8	9
Training & supervision by committees (COMMTRAI)	0	1	7	8	9
Man & Admin by committees (COMMMAN)	0	1	7	8	9
Non-billable attention by committees (COMMNOBI)	0	1	7	8	9
New client atraction by committees (COMNEWCL)	0	1	7	8	9
Specialist non-partners responsible for all these activities (NONRESP)	0	1	7	8	9
Training & supervision by specialist non-partners (NONTRAIN)	0	1	7	8	9
Man & Admin by specialist non-partners (NONMAN)	0	1	7	8	9
Non-billable attention by specialist non-partners (NONNOBIL)	0	1	7	8	9
New client attraction by specialist non-partners (NONNEWCL)	0	1	7	8	9
Download work onto QAs so that partners can work on client care (DOWNLOAD)	0	1	7	8	9

18.When a partner attracts new business does he receive compensation merely for attracting the new client or must he also spend time on the client's business and conclude the transaction before he is compensated?:

Partners compensated for new clients (NEWCLI2)	0	1	7	8	9
Partners must spend time as well as attract (TIMEALSO)	0	1	7	8	9

19.Should a partner attract more clients than he himself can attend to; does he receive compensation even though he has to pass the client on to one of his fellow partners?:

Partners compensated for passing on clients (PASSCLI)	0	1	7	8	9
Partners willing to pass clients on (PASSWILL)	0	1	7	8	9
Often must pass on due to work type (PASSTYPE)	0	1	7	8	9
Partner is still contact person (CONTACT)	0	1	7	8	9

SECTION SEVEN: THE FUTURE OF THE PROFESSION

The next part of the questionnaire attempts to obtain the opinions of members of the profession to matters that are currently the focus of attention in ongoing discussions between the UK professions and the Director General of Fair Trading. Last year a major Office of Fair Trading consultative document called for significant and far reaching reform in order to relax restrictions which currently inhibit free organisational choice within the professions in the UK. The two major issues of particular moment to the legal profession were consideration of incorporation of law firms and also mixed professional practice between lawyers and members of the other UK professions. These were not new proposals since they had been previously rehearsed in 1979 by the Benson Commission (The Royal Commission for Legal Services) and in 1980 by the Hughes Commission (The Royal Commission for Legal Services in Scotland). It is interesting that the Law Society of Scotland now permits

incorporation of law firms with limited liability but this option has not been taken up as yet by any Scottish law firms. In Scotland the question of mixed professional practice has been the focus of a recent Scottish Home and Health Department discussion paper (November 1987) called "The Practice of the Solicitor Profession in Scotland". The proposal called for the lifting of restrictions that currently ban lawyers from sharing fees with any party except other lawyers as it is anticipated that new and novel practicing arrangements which are currently stifled could emerge. This issue together with the incorporation question has prompted comment from various would be affected parties, but it would be useful to obtain opinions on such matters from individuals within the profession since many of the published opinions are aggregate viewpoints of the groups involved with the proposals.

1.What do you believe to be the major disadvantages of sole practice?:

	0	1	7	8	9
Lack of support (LACKSUPP)	0	1	7	8	9
Risk (RISKSOLE)	0	1	7	8	9
Inability to offer range of specialist services (INABSPEC)	0	1	7	8	9
Not practical (NOTPRAC)	0	1	7	8	9
Difficult to get and retain staff (STAFF)	0	1	7	8	9
Other (OTHER11)	0	1	7	8	9

2.Do you believe that partnerships overcome these disadvantages and what are the advantages of partnerships?: (ADVPART)

	0	1	7	8	9
Specialisation (SPECADV)	0	1	7	8	9
Support (SUPPORT)	0	1	7	8	9
Risk spread (RISKSPRE)	0	1	7	8	9
Synergy (SYNERGY)	0	1	7	8	9
Limited economies of scale (LTDEOS)	0	1	7	8	9
Greater technical input (GTTECHIN)	0	1	7	8	9
Financial control (FINCONT)	0	1	7	8	9
Greater capital input (GTCAPIN)	0	1	7	8	9
Motivation due to residual risk (RESRISK)	0	1	7	8	9
Team production (TEAMPROD)	0	1	7	8	9
Other (OTHER12)	0	1	7	8	9

3.Is the partnership form limiting in any way to the practice of law firms and could practising in an incorporated form offer any advantages?:

	0	1	7	8	9
Partnership limiting (PARTLIM)	0	1	7	8	9
Limited liability (LTDLIAB)	0	1	7	8	9
Trading in shares (TRADSHAR)	0	1	7	8	9
Structural limits (STRUCLIM)	0	1	7	8	9
Size limitations (SIZELIM)	0	1	7	8	9
Capital limitations (CAPLIM)	0	1	7	8	9
Decision making unwieldy (DECMAK)	0	1	7	8	9
Reluctance to delegate decision making authority (RELUCT)	0	1	7	8	9
Retention of profit for reserves (RESERVE)	0	1	7	8	9
Reduced working capital burden if outside equity (BURDEN)	0	1	7	8	9
Career structure/ promotion & status groups (CAREER2)	0	1	7	8	9
Other (OTHER13)	0	1	7	8	9

4.What do you believe would be the appropriate degree of liability for an incorporated solicitor's firm?:(LAIBINC)

	0	1	7	8	9
Unlimited (UNLTD)	0	1	7	8	9
Limited (LTD)	0	1	7	8	9
Irrelevant since PI is the important factor (PIIMP)	0	1	7	8	9
Will be personally liable anyway since veil of incorp not protec (PERSLIA)	0	1	7	8	9
Ltd liability only an issue if cannot get PI insurance to permit practice (ISSUE)	0	1	7	8	9

5.In which areas of legal work/type of legal firm would incorporation be ideally suited?:

No type of firm (NOTYPE)	0	1	7	8	9
No type of work (NOWORK)	0	1	7	8	9
Very large firms (LARGE)	0	1	7	8	9
Private client practice (PRIVCLI3)	0	1	7	8	9
High value commercial client work (COMMCLI3)	0	1	7	8	9
Other (OTHER14)	0	1	7	8	9

6. In the case of an incorporated solicitors practice who would you envisage being the shareholders?

Previous partners (PREVPART)	0	1	7	8	9
Employee share ownership (EMPSHAR)	0	1	7	8	9
Outside equity interest (OUTEQUIT)	0	1	7	8	9
Lawyers only if outside (LAWONLY)	0	1	7	8	9
Outside equity further in future (OUTFUT)	0	1	7	8	9
Other (OTHER15)	0	1	7	8	9

7. Are there any major disadvantages of incorporation of solicitors' firms or any insurmountable problems?:

Disadvantages exist (DISADINC)	0	1	7	8	9
Limited liab. may put off clients (DISADLTD)	0	1	7	8	9
Conflict of interests (CONFOI)	0	1	7	8	9
Professional status comprimised (PROFSTAT)	0	1	7	8	9
One-off tax burden due to differences in the taxation of profits (ONEOFF)	0	1	7	8	9
Other (OTHER16)	0	1	7	8	9

8.Would an organistion consisting of lawyers and members of other professions offer any advantageous features?:

MDP advantages (MDPADV)	0	1	7	8	9
MDP ideal types of firm (MDPTYPE)	0	1	7	8	9
MDP ideal types of work (MDPWORK)	0	1	7	8	9
Less sophisticated clients (LESSSOPH)	0	1	7	8	9
Private client work (MDPPRIV)	0	1	7	8	9
Commercial client work (MDPCOMM)	0	1	7	8	9
If combined with incorporation (INCMDP)	0	1	7	8	9
In rural areas (RURALMDP)	0	1	7	8	9
Property transactions (PROPMDP)	0	1	7	8	9
Personal financial services (FINMDP)	0	1	7	8	9
Patents (PATMDP)	0	1	7	8	9
Multinational practice is more attractive (MULTINAT)	0	1	7	8	9
Confederations more attractive (CONFED)	0	1	7	8	9
Networking sufficient (NETWORKS)	0	1	7	8	9
Other (OTHER17)	0	1	7	8	9

9.In the case of a mixed professional partnership would you find sharing liability with non-lawyers attractive/unattractive?:

Liability sharing unattractive (LIABUNAT)	0	1	7	8	9
Liability sharing not unattractive (LIABNOT)	0	1	7	8	9
Liability sharing necessary evil (NECEVIL)	0	1	7	8	9
Would depend on rules and PI (RULESPI)	0	1	7	8	9
Would depend on personnel (PERSONN2)	0	1	7	8	9

10. Are there any other problems with MDPs?:

Conflict of interests (CONFLICT)	0	1	7	8	9
Swallowed up by accountants (SWALLOW)	0	1	7	8	9
Sophisticated commercial clients don't want them (SOPHCOMM)	0	1	7	8	9
Loss of healthy competition between professional groups (COMPLOSS)	0	1	7	8	9
Designing practice rules (DESIGN)	0	1	7	8	9
Other (OTHER18)	0	1	7	8	9

I would like to express my thanks for your cooperation in completing this questionnaire for the purposes of my research.