OPEN SESSION
AGENDA ITEM

703 JULY 2018

DATE: July 19, 2018

TO: **Members, Board of Trustees**

FROM: Randall Difuntorum, Program Manager, Professional Competence

SUBJECT: State Bar Study of Online Delivery of Legal Services – Discussion of Preliminary Landscape Analysis

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EXECUTIVE SUMMARY

This matter is before the Board of Trustees ("Board") for discussion. After the January 2018, planning session, the Board added objective d to Goal 4 of the strategic plan, directing the study of online legal service delivery models to determine if regulatory changes are needed to support or regulate access through the use of technology. The Bar contracted with Professor William D. Henderson[1] to conduct a landscape analysis of the current state of the legal services market, including new technologies and business models used in the delivery of legal services, with a special focus on enhancing access to justice.

BACKGROUND

The State Bar's 2017-2022 Strategic Plan sets forth among the goals and objectives of the Bar, the following:

> Goal 4: Support access to justice for all California residents and improvements to the state's justice system.

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[1] Professor William Henderson is on the faculty at Indiana University Maurer School of Law, where he holds the Stephen F. Burns Chair on the Legal Profession. Prof. Henderson focuses primarily on the empirical analysis of the legal profession and has appeared in leading legal journals, including the *Stanford Law Review*, the *Michigan Law Review*, and the *Texas Law Review*. In addition, he regularly publishes articles in *The American Lawyer*, *The ABA Journal*, and *The National Law Journal*. His observations on the legal market are also frequently quoted in the mainstream press, including the *New York Times*, *Wall Street Journal*, *Los Angeles Times*, *Atlantic Monthly*, *The Economist*, and National Public Radio. Based on his research and public speaking, Prof. Henderson was included on the *National Law Journal's* list of The 100 Most Influential Lawyers in America (complied every ten years). In 2015 and 2016, he was named the Most Influential Person in Legal Education by *The National Jurist* magazine. In 2010, Prof. Henderson co-founded Lawyer Metrics, an applied research company that helps lawyers and law firms use data to make better operational and strategic decisions. Lawyer Metrics (now LawyerMetrix) was acquired by AccessLex Institute in 2015. In 2017, he founded Legal Evolution, an online publication that chronicles successful innovation within the legal industry.

Objective d: Commencing in 2018 and concluding no later than December 31, 2019, study online legal service delivery models and determine if any regulatory changes are needed to better support and/or regulate the expansion of access through the use of technology in a manner that balances the dual goals of public protection and increased access to justice.

To begin the work outlined in this objective, the Bar contracted with Professor Henderson to lay the groundwork for future regulatory changes by capturing the many online legal service delivery models that have developed and the ways states across the country have addressed those business models.

DISCUSSION

Professor Henderson's report is provided as Attachment A. The report is the first step in the Bar's study of delivery of legal services through the use of technology.

The goal is to survey the landscape of the current and evolving state of the legal services market with a particular emphasis on new business models developed for delivering legal services using methods that are distinct from traditional delivery systems. This includes models that provide full-service legal representation and models focused on limited scope services either combined with, or independent of, other available law related or non-legal professional services. Other law related services might include: document drafting; legal information consulting; self-help resources; access to legal information and forms/templates databases; pre-paid or subscription legal service plans; dispute resolution services; and lawyer client matching services provided through interactive online directories, lead generation or other technology based techniques for pairing a prospective lawyer and client. Non-legal professional services include accounting, investment, research, information technology and counseling services. Non-lawyer involvement in these new business models may take the form of either active or passive participation, including passive capital investment. In addition to the above, the landscape analysis includes a discussion of the emerging "gig economy."

Next steps include Board consideration of a task force to prepare policy and implementation recommendations.

FISCAL/PERSONNEL IMPACT

None

RULE AMENDMENTS

None

BOARD BOOK AMENDMENTS

None

STRATEGIC PLAN GOALS & OBJECTIVES

Goal 4: Support access to justice for all California residents and improvements to the state's justice system.

Objective d: Commencing in 2018 and concluding no later than December 31, 2019, study online legal service delivery models and determine if any regulatory changes are needed to better support and/or regulate the expansion of access through the use of technology in a manner that balances the dual goals of public protection and increased access to justice.

RECOMMENDATION

Staff recommends that the Board of Trustees approve the following resolution:

> **RESOLVED**, that the Board of Trustees receives and accepts Professor William Henderson's landscape report on the legal services market; and it is
>
> **FURTHER RESOLVED**, that the Board of Trustees authorizes the formation of a Task Force to analyze the landscape report and conduct a study of possible regulatory reforms, including but not limited to the online delivery of legal services, that balance the State Bar's dual goals of public protection and increased access to justice; and it is
>
> **FURTHER RESOLVED**, that the Board of Trustees directs staff to work with the Chair and Vice-Chair of the Programs Committee to draft a task force charter and a recommendation for the categories of expertise that the members to be appointed to the Task Force should possess in order to ensure that the Task Force represents a broad range of interests.

ATTACHMENT(S) LIST

A. Legal Market Landscape Report (July 2018) by Prof. William D. Henderson

B. Excerpts from the Terms of Use Provisions for LegalZoom and AVVO.COM

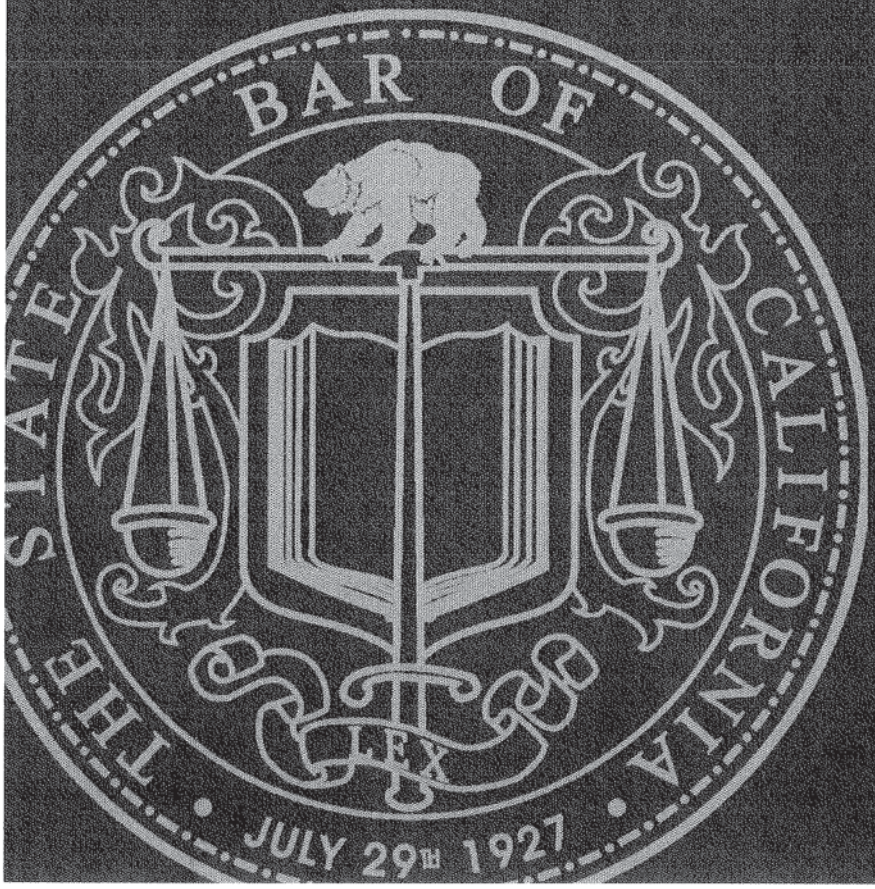
ATTACHMENT A

Legal Market Landscape Report

Commissioned by the State Bar of California

July 2018

William D. Henderson



Legal Market Landscape Report
Commissioned by the State Bar of California
July 2018

Executive Summary

Throughout the United States, legal regulators face a challenging environment in which the cost of traditional legal services is going up, access to legal services is going down, the growth rate of law firms is flat, and lawyers serving ordinary people are struggling to earn a living. The primary mechanism for regulating this market is lawyer ethics, including the historical prohibition on nonlawyer ownership of businesses engaged in the practice of law. However, private investors are increasingly pushing the boundaries of these rules by funding new technologies and service delivery models designed to solve many of the legal market's most vexing problems.

There is ample evidence that the legal profession is divided into two segments, one serving individuals (PeopleLaw) and the other serving corporations (Organizational Clients). These two segments have very different economic drivers and are evolving in very different ways. Since the mid-1970s, the PeopleLaw sector has entered a period of decline characterized by fewer paying clients and shrinking lawyer income. Recent government statistics reveal that the PeopleLaw sector shrank by nearly $7 billion (10.1%) between 2007 and 2012. Throughout this period, the number of self-represented parties in state court continued to climb. The Organizational Client sector is also experiencing economic stress. Its primary challenge is the growing complexity of a highly regulated and interconnected economy. Since the 1990s, corporate clients have coped with this challenge by growing legal departments and insourcing legal work. More recently, cost pressure on corporate clients has given rise to alternative legal service providers (ALSPs) funded by sophisticated private investors. Both responses come at the expense of traditional law firms.

What ties these two sectors together is the problem of lagging legal productivity. As society become wealthier through better and cheaper good and services, human-intensive fields such as law, medical care, and higher education become relatively more expensive. In contrast to medical care and higher education, however, a growing proportion of U.S. consumers are choosing to forgo legal services rather than pay a higher price.

The legal profession is at an inflection point. Solving the problem of lagging legal productivity requires lawyers to work closely with professionals from other disciplines. Unfortunately, the ethics rules hinder this type of collaboration. To the extent these rules promote consumer protection, they do so only for the minority of citizens who can afford legal services. Modifying the ethics rules to facilitate greater collaboration across law and other disciplines will (1) drive down costs; (2) improve access; (3) increase predictability and transparency of legal services; (4) aid the growth of new businesses; and (5) elevate the reputation of the legal profession. Some U.S. jurisdiction needs to go first. Based on historical precedent, the most likely jurisdiction is California.

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1. Size and Composition of the U.S. Legal Market

There is widespread consensus among lawyers, judges, legal academics, regulators and sophisticated clients that the legal market is in a period of significant tumult. Further, there is also agreement that this tumult may be the early stages of a fundamental transformation. Yet, what is new and disconcerting for many is that these changes are not being driven by licensed lawyers or the organized bar. Rather, the causes are powerful external market forces that cannot be easily categorized using our familiar and well-established frameworks. At a minimum, our frameworks need updating.

Effective regulation requires (1) an understanding of the marketplace, and (2) the ability to clearly articulate how duly enacted rules, policies and procedures are serving the public interest. The purpose of this landscape report is to describe the rapidly evolving structure of the U.S. legal market (the first prong) so that Trustees of the State Bar of California can better evaluate vital regulatory questions that bear on the protection of the public as required under the State Bar Act.[1]

To establish a clear baseline, Section 1 begins with the most current government statistics on legal services. It then describes facets of the emerging legal economy that are not captured by traditional categories yet reflect significant new business models and novel ways of legal problem-solving. In most cases, these changes require close collaboration between lawyers, technologists, data scientists, and several other disciplines.

1.1. Legal Services Data from the U.S. Census Bureau

Every five years, the U.S. Census Bureau conducts the Economic Census, which is a comprehensive measurement of American business.[2] The most recent Economic Census was conducted in 2012. The information is organized based on the North American Industry Classification System.[3] The four-digit NAICS number for legal services is 5411. In 2012, the U.S. legal services market (NAICS 5411) totaled approximately $261.7 billion in revenue.

As show in Figure 1, the legal services sector has experienced significant growth over the last two decades. It is noteworthy, however, that the pace of growth appears to be slowing. Between 1997 and 2002, the sector grew 43.3 percent ($127.1 to $182.1B), followed by 31.5 percent growth between 2002 and 2007 ($182.1 to $239.4B). However, between 2007 and 2012, growth slowed to 9.3 percent ($239.4 to $261.7B). Further, total employment in the legal services sector has declined by approximately 55,000 jobs since the 2007 high-water mark. In fact, in terms of employment, the legal sector is smaller now than it was in 2002.[4]

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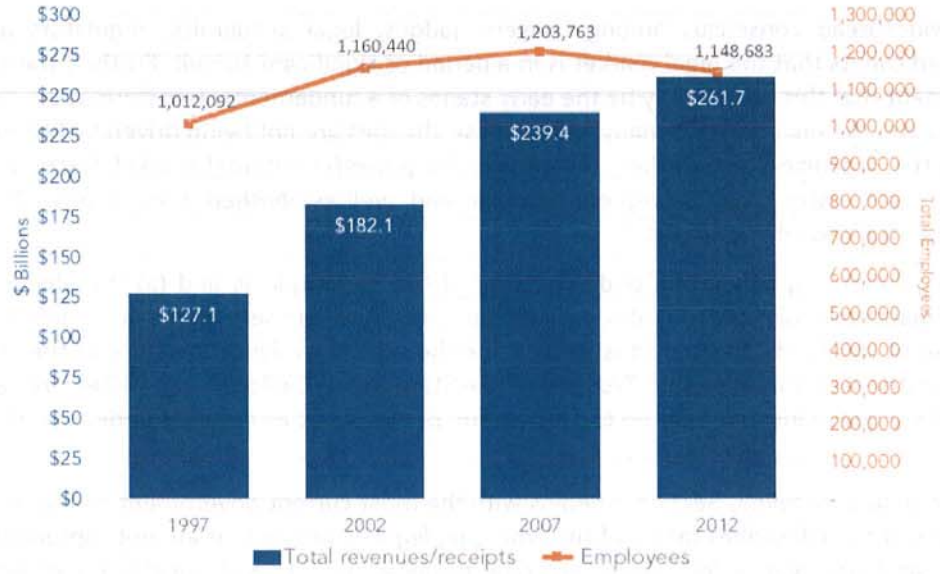
[1] See Business and Professions Code section 6001.1 State Bar— Protection of the Public as the Highest Priority ("Protection of the public shall be the highest priority for the State Bar of California and the board of trustees in exercising their licensing, regulatory, and disciplinary functions. Whenever the protection of the public is inconsistent with other interests sought to be promoted, the protection of the public shall be paramount."). See also, Business and Professions Code sections 6055 et seq., operative Jan. 1, 2018¬ (describing the creation of a voluntary nonprofit association that is a non-governmental entity separate from the State Bar, that assumes the responsibilities and activities of the former sections of the State Bar).

[2] See https://www.census.gov/programs-surveys/economic-census.html (last visited June 22, 2018).

[3] The NAICS system was first introduced in 1997, replacing the Standard Industrial Classification (SIC) system. Thus, we do not have commensurable data for the pre-1997 time period.

[4] According to the U.S. Census County Business Patterns data set, employment in the legal services sectors (5411) totaled 1,137,480 in 2016, which suggests continued stagnant employment.

Figure 1. U.S. Legal Services (NAICS 5411), Receipts and Employment, 1997 to 2012



Sources: U.S. Census Bureau, Economic Census. Graph generated by Legal Evolution PBC

An important caveat regarding the Figure 1 statistics, however, is that in the Economic Census data, law firm partners are owners rather than employees. Thus, partners are *not* part of the employment count. Data from the ABA suggests that the U.S. legal profession has gotten significantly older over the last half century, with the median age climbing from 39 in 1980 to 49 in 2005.[5] Therefore, it is quite possible that the diminution in legal services employment is occurring because law firms contain more partners who are, on balance, older and less leveraged in terms of associates, paralegals and staff.

The emphasis on law firms is important because, as the official government statistics show, the vast majority of the legal services sector is comprised of offices of lawyers (95.1%). Nonprofit legal service organizations are included in this category but make up a small fraction of the overall market (1.0%). The remaining balance of the legal services sectors is comprised of title abstract and settlement offices (541191) and all other legal services (541199). These figures are summarized in Table 1.

[5] See Bill Henderson, *Is the Legal Profession Showing its Age?*, LEGAL WHITEBOARD, Oct. 13, 2013, http://professorhenderson.com/downloads/Is_the_Legal_Profession_Showing_Its_Age.pdf (last visited June 23, 2018).

Table 1. U.S. Legal Services Market, 2012

Legal Services (5411)	Receipts (5-digit) (thousands)	Receipts (6-digit) (thousands)	Percentage
Offices of Lawyers (54111)	$248,884,540		**95.1%**
Law firms (5411101)		$246,141,231	94.1%
Nonprofit legal aid organizations (5411102)		$2,743,309	1.0%
Other legal services (54119)	$12,810,105		**4.9%**
All other legal services (541199)		$3,256,378	1.2%
Title Abstract and Settlement Services (541191)		$9,553,727	3.7%
Total	**$261,694,645**	**$261,694,645**	**100.0%**

Source: U.S. Census Bureau 2012 Economic Census

According to the same Economic Census data, the California legal services market (5411) in 2012 totaled $38.6 billion, which was 14.7 percent of the $261.7 billion U.S. legal services sector. As shown in Table 2, the composition of California is very similar to the overall U.S. market. The only noteworthy difference is an "all other legal services" sector that is, proportionally, twice the size of the national market (2.5% versus 1.2%).

Table 2. California Legal Services Market, 2012

Legal Services (5411)	Receipts (5-digit) (thousands)	Receipts (6-digit) (thousands)	Percentage
Offices of Lawyers (54111)	36,920,644		**95.7%**
Law firms (5411101)		$36,506,552	94.6%
Nonprofit legal aid organizations (5411102)		$414,092	1.1%
Other legal services (54119)	$1,670,893		**4.3%**
All other legal services (541199)		$717,802	2.5%
Title Abstract and Settlement Services (541191)		$953,091	2.5%
Total	**$38,591,537**	**$38,591,537**	**100.0%**

Source: U.S. Census Bureau 2012 Economic Census

It is noteworthy that since 2002, the "all other legal services" market in California has more than doubled, growing from $312.7 to $717.8 million. Drawing upon the Dun & Bradstreet Reports that tracks private company data, including their NAICS number, there is a wide variety of companies in this space, such as a document retrieval company called Macro-Pro (Long Beach, $12 million in annual reviews, 156 employees); a cloud-based e-discovery software company called Case Central (Pasadena, $7.5 million, 60 employees); a company that files and serves court documents called One Legal (Los Angeles, $4.million, 60 employees); and a company that provides full-service patent and literature search capabilities (San Diego, $1.1 million, 10 employees).

The key takeaway from Tables 1-2 is that official measures of the legal services in the U.S. show a market overwhelmingly comprised of law firms. What is not included, but nonetheless economically significant, consists of:

- In-house lawyers working directly for corporations and nonprofits
- Lawyers working in federal, state and local government
- Lawyers working as part of the gig economy
- Lawyers and allied professionals working in a burgeoning technology and publishing sector that is focused on legal issues and problems

1.2. In-House and Government Lawyers

The U.S. Bureau of Labor Statistics (BLS) compiles information on specific occupations, with breakdowns based on geography and industry. This provides a reliable method of tracking the income and growth of lawyers by sector, including those working in-house or in government.

According to the latest government statistics, there are currently 628,370 lawyers employed as W-2 employees working in various parts of the U.S. (Similar to the Economic Census, these government data also do not include law firm partners and solo practitioners.)[6] The largest industry category of employer is legal services (5411), with 388,670 lawyers, followed by lawyers working in government (local 54,920, state 42,250, federal 37,210).[7] For the purposes of this analysis, in-house lawyers are professionals working as lawyers in industries other than legal services or government. In 2017, this number totaled 105,310, which is roughly equivalent to the number of lawyers working in the domestic offices of the 200 largest U.S. law firms based on revenues (Am Law 200).

AMLAW 200

In house counsel

Figure 2 below shows the growth of lawyers by practice setting with 1997 as the baseline. The most striking feature is the rapid growth rate for in-house lawyers. Note also how employment rates for in-house lawyers tracked the economic downturn in 2008 to 2010. Yet it is also noteworthy that since the mid-2000's, the growth rate for law firm employment has lagged behind the rate for government lawyers. Among the three practice settings, in-house lawyers had the highest incomes ($162,242) followed by law firms ($147,950) and government lawyers ($108,411).

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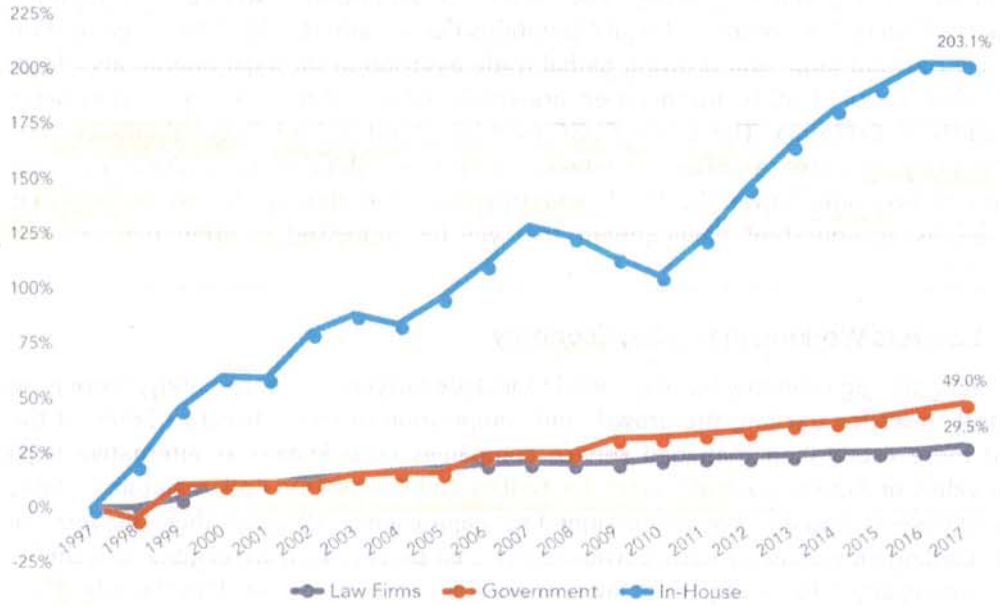
[6] According to ABA statistics, in 2018 there are 1,338,678 active resident attorneys in the U.S. See https://www.americanbar.org/content/dam/aba/administrative/market_research/Total_National_Lawyer_Population_1878-2018.authcheckdam.pdf (last visited July 11, 2018). Thus, it is reasonable to estimate that slightly more than half of lawyers are either law firm partners, shareholders, or solo practitioners. Unfortunately, the number and income of lawyers as business owners is not something tracked and published by the U.S. government. Data on employed lawyers, particularly over time, remain a useful barometer of the vitality of the overall legal economy.

[7] See Occupational Employment and Wages, May 2017, 23-1011 Lawyers, https://www.bls.gov/oes/current/oes231011.htm (last visited June 23, 2018).

Figure 2. Percent Change in Employed Lawyers by Practice Setting, 1997 to 2017



Sources: Bureau of Labor Statistics. Graph generated by Legal Evolution PBC

1.3. Employed Lawyers Working in California

As of May 2017, there were 79,980 "employed" lawyers working in the state of California. This number includes lawyers working in legal departments, public interest organizations and government. It also includes associates, staff attorneys and counsel working in law firms, but excludes partners and shareholders (i.e., owners of the firm). The metro areas of Los Angeles-Long Beach-Glendale and San Francisco-Redwood City-South San Francisco are both in the top 10 for U.S. metropolitan areas based on total employment of lawyers (#3 LA with 27,210 jobs, #9 San Francisco at 11,580).

According to the BLS, employed lawyers in California earned an average of $168,200 per year, which is the highest income among the 50 states, trailing only the District of Columbia at $189,560. When ranked by average income, six of the top 10 metropolitan areas are located in California:

- #1 San Jose-Sunnyvale-Santa Clara ($198,100, 5,470 lawyers)
- #2 San Francisco-Redwood City-South San Francisco ($189,660, 11,580 lawyers)
- #3 Anaheim-Santa Ana-Irvine ($189,150, 7,700 lawyers)
- #5 San Rafael ($180,530, 560 lawyers)
- #9 Oxnard-Thousand Oaks-Ventura ($174,420, 1,200 lawyers)
- #10 Los Angeles-Long Beach-Glendale ($170,210, 27,210 lawyers)[8]

Although limitations in available data make it difficult to pin down the composition and drivers of California's relatively vibrant legal services economy, the author believes that one factor is California's role in the in-house legal department growth movement. California is home to

[8] See Occupational Employment and Wages, May 2017, 23-1011 Lawyers, https://www.bls.gov/oes/current/oes231011.htm (last visited June 23, 2018).

CLOC as the disruptor

many of the nation's leading technology companies. Personnel from these legal departments – including Cisco, Google, Oracle, NetApp, Yahoo, Facebook and Adobe – were the driving force behind the creation of the Corporate Legal Operations Consortium (CLOC).[9] This organization is a relatively new but large and growing global trade association for legal operations ("legal ops") professionals. All CLOC board members are employed in Fortune 500 legal departments based in northern California. The 1000+ CLOC members tend to be influential in how their organizations buy legal services, often demanding better use of data, process, and technology. This flexing of economic power by legal departments—often through teams of legal ops professionals—is an important development that will be addressed in other parts of this report.[10]

1.4. Lawyers Working in the Gig Economy

ALSPs as Disrupting

In recent years, the gig economy has expanded to include lawyers.[11] Unfortunately, there is no reliable mechanism for tracking the growth and composition of this subsector. Some of the larger and more established managed service companies (also known as alternative legal service providers or ALSPs), such as Axiom, UnitedLex and Counsel On Call, maintain a stable of employed lawyers who are regularly assigned to major clients. Although these lawyers are technically contingent workers, a large portion are W-2 employees who are eligible for benefits through the company.[12] However, these lawyers are the exception rather than the rule. Most lawyers in the gig economy are independent contractors with no guaranteed flow of work and relatively little leverage to negotiate for higher rates or wages.[13]

G.G economy

Lawyers working in the gig economy are likely to be counted through the U.S. Census Bureau's Nonemployer Statistics Program. NES is an annual series on businesses that are subject to federal income tax but have no paid employees.[14] Thus, to be clear, if a solo practitioner employs a secretary, paralegal or associate, this arrangement would qualify as a law firm and would therefore be tracked by other Census Bureau programs.[15] In 2016, the legal services sector (NAICS 5411) had 285,603 nonemployer establishments. Of this number, 54,742 (19.2%) generated revenues in excess of $100,000 per year; 15,312 (5.4%) exceed $250,000 per year. At the other end of the spectrum, 83,439 (29.2%) had revenues of less than $10,000 per year. Table 3 contains a breakdown for the United States and California based on type of entity.

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[9] See www.cloc.org (last visited July 11, 2018).

[10] See Sections 2.4 and 4.2, *infra*.

[11] See, e.g., Claire Bushey, *The gig economy comes to law*, CRAIN'S CHICAGO BUSINESS, May 6, 2017 (reporting on growth of contract lawyers used by major staffing agencies, typically for document review for corporate clients); Emma Ryan, *The gig economy: How freelancing is set to change the business of law*, LAWYERS WEEKLY (Australia), Nov. 30, 2017 (reporting greatest utilization of gig lawyers among in-house legal department); *How the Gig Economy is impacting Legal Services*, TRANSLATEMEDIA, Jan. 13, 2017 (reporting on changing attitudes among younger lawyers but also noting difficulty of simultaneously using contingent worker and maintaining data security).

[12] See William D. Henderson, *Efficiency Engines: Building Systems for Corporate Legal Work*, ABA JOURNAL, June 2017, at 37 (discussing managed services business model and identifying the largest managed services providers).

[13] For a detailed look into the rise and conditions within this subsector, see ROBERT A. BROOKS, CHEAPER BY THE HOUR: TEMPORARY LAWYERS AND THE DEPROFESSIONALIZATION OF THE LAW (2011).

[14] See https://www.census.gov/programs-surveys/nonemployer-statistics.html (last visited June 25, 2018).

[15] Employment within law firms is tracked annually by the County Business Patterns (CBP) program. Annual receipts are captured every five years through the Economic Census.

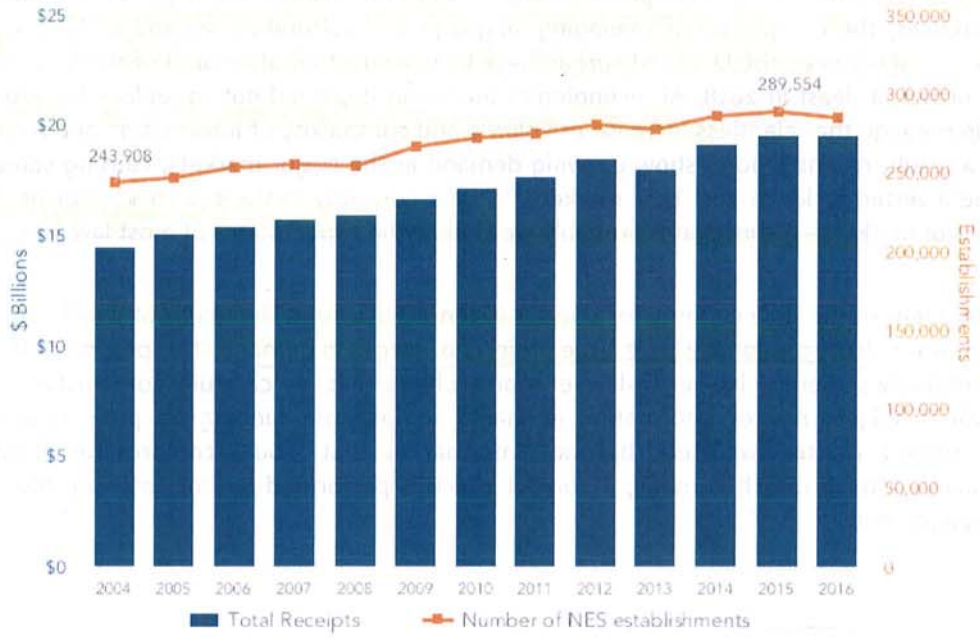
Table 3. 2016 Nonemployer Statistics: Count, Receipts, Average Revenue

Type of Entity	United States			California		
	Number	Total Receipts (thousands)	Avg. Rev.	Number	Total Receipts (thousands)	Avg. Rev.
Individual proprietorships	258,987	$15,987,423	$61,731	43,364	$3,250,949	$74,969
S-corporations	16,070	$1,598,720	$99,485	1,900	$262,889	$138,363
Partnerships	7,421	$1,675,755	$225,813	1,147	$337,061	$293,863
C-corporations / Other	3,125	$304,103	$97,313	649	$82,591	$127,259
All establishments	285,603	$19,566,001	$68,508	47,060	$3,933,490	$83,585

Source: U.S. Census Bureau 2016 Nonemployer Statistics

Despite the imprecision of NES groupings, the NES trends reveal significant changes in the legal economy that are likely connected with the growth of the gig economy for lawyers. Figure 3 shows the growth of receipts and number of nonemployer establishments in the 2004 to 2016 time period.

Figure 3. Total Receipts & Number of Nonemployers, 2016 Legal Services (NAICS 5411)



Sources: U.S. Census Bureau, Nonemployer Statistics. Graph generated by Legal Evolution PBC

Figure 3 should be contrasted with Figure 1, which tracks changes in revenue and employment in the broader legal services industry (overwhelmingly law firms). Whereas employment peaked in the broader legal services market in 2007 and is now lower than 2002 levels, the nonemployer segment, which fully contains the gig lawyer economy, has been moving upward in both receipts and number of establishments. Between 2004 and 2016, the count increased by more than 41,000 establishments (i.e., contract lawyers and/or solos without employees). During this

same period, total employment in the legal services sector declined by 80,870 jobs.[16] These trend lines suggest that traditional law firm employment is slowly giving way to a workforce that is more contingent. This is likely occurring because traditional legal employers are struggling to grow and thus are seeking ways to reduce the risk of adding w-2 employees.

As the gig economy grows and matures, it is also segmenting. One of the most established segments is the market for contract lawyers doing document review for major litigation and information requests from the FTC/DOJ related to antitrust review of proposed mergers. For nearly 20 years, this work has slowly moved out of law firms to contract attorneys provided by a large number of national and regional staffing agencies[17] or managed service firms.

One of the best windows on this market is the Posse List, which is a website founded in 2002 that maintains a large number of Listservs based on geography, subject matter expertise and foreign language proficiency. The staffing agencies and managed service firms post jobs; in turn, interested Posse List subscribers respond. According to a recent story in *Chicago Crain's Business*, the number of attorneys who subscribe to the Chicago portion of the Posse List increased from 1,520 in 2006 to over 5,000 in 2017.[18] The California market has robust coverage, with a statewide Listserv along with separate lists for the Los Angeles, San Francisco, San Diego and Sacramento markets.

In theory, the work brokered by the Posse List is the type of labor-intensive work most susceptible to replacement by legal process outsourcing and artificial intelligence. Yet time zone differences, the complexity of managing language and cultural issues and a shrinking wage differential between the U.S. and abroad have keep a substantial amount of this work in the U.S. Further, at least in 2018, AI technologies are being deployed not to replace lawyers, but to help manage the relentless increase of volume and complexity of information and legal tasks. As a result, recent reports show growing demand in the major markets, causing some work to be diverted to lower-cost U.S. markets.[19] Pay is currently in the $32 to $35 per hour range in major markets – a sum that is probably well below the expectations of most law school graduates.

AI

Another segment of the gig economy for lawyers is centered around the needs of smaller and midsize law firms that occasionally have large projects or surges in demand. This portion of the bar is increasingly served by lawyer-to-lawyer marketplaces that are carefully constructed so that sufficient subject matter information is shared to facilitate bidding on projects and matching subject matter expertise, but not information that would compromise client confidentiality. After a match is made, a conflict check is performed before entering into a project engagement.

Small + M.d.-sized firms/contract/6'8

[16] Calculated by Legal Evolution PBC from U.S. Census Bureau County Business Patterns data. In 2004, there were 1,218.350 employers in the legal services sectors (5411). In 2016, that number had declined to 1,137,480.

[17] Many of these staffing agencies are either publicly held companies or owned at least in part by private equity firms. For example, Kelly Law Registry (owned by Kelly Services, traded on the NASDAQ), Special Counsel (owned by Adecco Group, a publicly traded Swiss company), Robert Half Legal (owned by Robert Half International, traded on the NYSE).

[18] See Bushey, *supra* note 11.

[19] See, e.g., Greg P. Bufithis, *Tales from the trenches: the explosion of e-discovery projects in D.C. and NYC*, THE POSSE LIST, June 18, 2018, at http://www.theposselist.com/2018/06/18/tales-from-the-trenches-the-explosion-of-e-discovery-document-review-projects-in-d-c-and-nyc/ (last visited June 26, 2018).

One of the most established marketplaces is Hire An Esquire, which claims to maintain a network of 8,000+ legal professionals in 50 states that have been vetted for quality. Some of these professionals are Hire An Esquire employees, while others are independent contractors. According to a 2017 article Hire An Esquire charges out attorneys at an average of $70/hour, taking a 12 percent fee for 1099 projects and 40 percent for W-2 projects.[20] Hire An Esquire is financed by a combination of angel and venture capital funding.[21]

Other more recent entrants to the lawyer-to-lawyer marketplace space include LawClerk.legal and Lawyer Exchange. In contrast to Hire An Esquire, both of these portals let the price of work float between the contracting law firms and contract lawyers. Further, both enable the contracting firm and contract lawyers to rate their experience with each other, thus enabling a market that reflects not only price but also quality of work and collegial nature of the work environment. In the case of LawClerk.legal, the company appears to elide the risk of multijurisdictional practice and the unauthorized practice of law by holding itself out as "a marketplace through which persons holding a law degree ("Lawclerks") may be engaged in the capacity of a paraprofessional (verses as a lawyer) by attorneys that are admitted to and in good standing with their respective state's bar association ("Attorneys")[.]"[22] The range of typical services includes "preparation of memorandums, pleadings, written discovery, and agreements."[23]

Lawyer Market Places

The business model for lawyer marketplaces usually requires the entity running the marketplace to act as a transparent and trustworthy conduit for payment. In most cases, but not all,[24] payment is tied to the amount or volume of work. Although this raises nominal questions related to Rule 5.4 of the ABA Model Rules of Professional Conduct[25] concerning fee-splitting – a fact that all of these businesses took into account before launching – the tension is with the text of the existing rules rather than the underlying policy, which is to safeguard lawyer independence.[26] Thus, when evaluating the propriety of these marketplaces, legal regulators should fully weigh the benefits of these services to both clients and lawyers and require a clear factual basis to show that lawyer judgment is at risk of being compromised to the detriment of clients. The fact that these marketplaces are springing up in such numbers, often backed by professional investors, is a telling sign that buyers and sellers need better pathways to find each other.

Rule 5.4

Fee-Splitting

[20] See *Need a Freelance Lawyer? 3 Online Contract Marketplaces Compared,* CAPTERRA LEGAL SOFTWARE BLOG, Sept. 26, 2017, at https://blog.capterra.com/need-a-freelance-lawyer-3-online-contract-lawyer-marketplaces-compared/ (last visited June 26, 2018).

[21] See Crunchbase, https://www.crunchbase.com/organization/hire-an-esquire/funding_rounds/funding_rounds_list (last visited June 26, 2018).

[22] See Ethics White Paper, https://www.lawclerk.legal/ethics_whitepaper (last visited June 26, 2018) (focusing on Model Rule 5.3, "Responsibilities Regarding Nonlawyer Assistants" and Model Rule 5.5 "Unauthorized Practice of Law").

[23] Id.

[24] For example, MPlace is a marketplace for contract attorneys working on large corporate project that also maintains and shares ratings on clients and contract lawyers. However, its business model is a single-price annual subscription based on number of review "seats" the client hopes to fill.

[25] Unless otherwise noted, all rule references are to the ABA Model Rules of Professional Conduct.

[26] See Rule 5.4, Comment [1] ("The provisions of this Rule express traditional limitations on sharing fees. *These limitations are to protect the lawyer's professional independence of judgment*." (emphasis added)).

1.5. Alternative Legal Service Providers (ALSPs) and LegalTech

In 2018, it is hard to overstate the tremendous economic and technological ferment of the legal ecosystem growing up within and around the traditional legal services market. Various organizations now produce "market maps" of the legal tech and legal startup space. Appendix A contains a representative sample published by Thomson Reuters,[27] which breaks down this crowded and diverse marketplace into the following categories (with number of companies in parentheses).

- Business Development / Marketplaces (19)
- Litigation Funding (6)
- Legal Education (13)
- E-Discovery (11)
- Practice Management (20)
- Legal Research (17)
- Case Management Analytics (10)
- Document Automation (17)
- Contract Management / Analysis (12)
- Consumer (11)
- Online Dispute Resolution (11)

Several of the companies mentioned in this report were launched *after* the creation of the 2016 Thomson Reuter map. The rapid change in this space makes it very difficult to accurately track.

AI

Another window on the massive amount of innovation occurring in the legal services space can be seen in the large number of legal startups that are using artificial intelligence to create "point solutions" related to legal problem-solving.[28] For example, Tel Aviv-based LawGeex is a company that makes automated contract review technology that helps businesses sift through the myriad of contracts that are entered into during the normal course of business, such as NDAs, supplier agreements, purchase orders and SaaS licenses. As of April 2018, it had raised more than $21 million from a syndicate of venture capital companies.[29]

To help distinguish itself within a crowded marketplace, LawGeex recently launched a content marketing campaign[30] that included the creation of its LegalTech Buyer's Guide. This remarkable document provides a detailed breakdown of venture capital funding ($233 million in

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[27] See David Curle, *Legal Tech Startups: Not Just for Silicon Valley Anymore*, LEGAL EXECUTIVE INSTITUTE, August 2, 2016, http://www.legalexecutiveinstitute.com/legal-tech-startups/ (last visited June 26, 2018). CBInsights, which caters to professional investors, also regularly produces a legal tech market map. See, e.g., https://www.cbinsights.com/research/legal-tech-market-map-company-list/ (last visited June 26, 2018).

[28] A point solution is a tech-driven way to handle a narrow category of work. Many point solutions require lawyers and staff to learn many new technologies, which slows overall tech adoption.

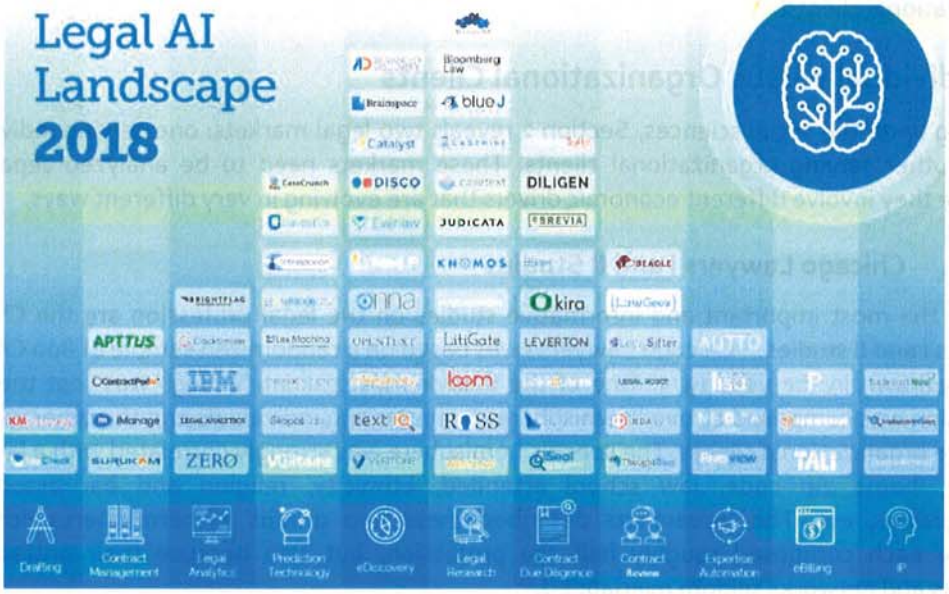
[29] See Steve O'Hear, *LawGeex raises $12M for its AI-powered contract review technology*, TECHCRUNCH, Apr. 17, 2018, at https://techcrunch.com/2018/04/17/lawgeex-raises-12m-for-its-ai-powered-contract-review-technology/ (last visited June 28, 2018).

[30] Content marketing is strategy where a company raises awareness for its products and services by providing prospective clientele with information that aids them in their business, often by educating them on complex technical topics. High quality content is a way to signal expertise within a crowded market. Thus, when a prospective client moves closer to a buy decision, they are favorably disposed toward the company that helped educate them. Within the legal industry, see generally JORDAN FURLONG & STEVE MATTHEWS, CONTENT MARKETING AND PUBLISHING STRATEGIES FOR LAW FIRMS (Ark 2013).

2017 across 61 deals) along with information on recent mergers, acquisitions and industry consolidation. What is most useful to buyers, however, is the careful categorization of more than 130 technology companies into 16 different categories. This includes a capsule summary of all 130+ companies, touching on issues of price, user experience, relative drawbacks and limitation compared to competitors and occasional pithy commentary from insiders. What makes the document credible is the fact that LawGeex is described in only *one* of the 16 legal tech categories.

Figure 4 below is a summary of the many AI-enabled legal tech companies based on "use case."

Figure 4. Legal Tech Companies-based Artificial Intelligence Use Case



Even to a researcher focusing on the legal industry, this is a bewildering array of offerings. The author is reminded of an observation made 25 years ago by software engineer Paul Lippe, a legal tech entrepreneur who was then general counsel of Synopsys, an electronic design automation company based in Mountain View, California: "It's only AI when you don't know how it works; once you know how it works, it's just software."[31] This anecdote makes a very important point: there is a lag between the development of new innovations and the ability of laypeople (including lawyers) to accurately understand, contextualize and categorize how these innovations fit into our economy, society and system of government.

The combining of law with technology is driven by powerful economic forces. Now more so than at any other time in history, law is in the process of moving from a pervasive model of one-to-one consultative legal services to one where technology enables one-to-many legal solutions.[32] As momentum grows, more pressure will be placed on a regulatory framework

1-to-1
1-to-many

[31] See Paul Lippe and Daniel Martin Katz, *10 Predictions about how IBM's Watson will impact the legal profession*, ABA JOURNAL, Oct. 2, 2014 (Legal Rebels Series), at http://www.abajournal.com/legalrebels/article/10_predictions_about_how_ibms_watson_will_impact/ (last visited June 28, 2018).

[32] See generally RICHARD SUSSKIND, TOMORROW'S LAWYERS (2nd ed. 2017) (discussing the transition for one-to-one consultative legal services to one-to-many productized legal solutions).

Ding-
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premised on one-to-one legal services. This raises very difficult questions for regulators, as paradigm shifts are rare events that are difficult to recognize. Rather than amend an ethics framework built for a bygone era, the public interest may be better served by a new regulatory structure that includes traditional lawyering side by side with one-to-many legal services, products and solutions created by a wide range of professionals from multiple disciplines. This is the path taken by Australia and the United Kingdom with the likelihood of Canada going next.[33]

Section 2 of this report has additional descriptions and examples of other alternative legal businesses. However, that discussion requires a deeper understanding of how the U.S. legal market is functionally divided into two markets: one serving individuals and a second serving organizational clients.

2. Individual versus Organizational Clients

Drawing upon the social sciences, Section 2 reveals two legal markets: one serving individuals and another serving organizational clients. These markets need to be analyzed separately because they involve different economic drivers that are evolving in very different ways.

2.1. Chicago Lawyers I and II Studies

Two of the most important and informative studies on the legal profession are the Chicago Lawyers I and II studies.[34] Chicago Lawyers I was based on a randomized sample of 800 Chicago lawyers drawn in the year 1975. One of the study's most salient findings was that the legal profession was comprised of two "hemispheres," one serving individuals and the other working for large organizational clients. The specific hemisphere was strongly correlated with a lawyer's income, home zip code, law school attended, ethnicity, religion and bar association memberships, etc. The researchers described these two groups as hemispheres not only because each composed roughly half the profession, but also because their professional interests and networks seldom overlapped.[35]

In 1995, the same core researchers conducted Chicago Lawyers II, which replicated the original study based on a new sample of Chicago lawyers. Over the intervening two decades, the organizational client hemisphere experienced a dramatic surge in work from corporate clients. As a result, the amount of time lawyers devoted to organizational clients doubled compared to the time spent on personal and small-business clients. Thus, the term "hemisphere," as in half, no longer applied. Typical large law firm income increased from $144,985 in 1975 to $271,706 in 1995. In-house counsel also fared well. In contrast, the most economically challenged group was solo practitioners, as these lawyers were much more likely to serve individuals through personal injury, family law, criminal defense and trusts-and-estates work. In 1975, a solo practitioner in the sample earned a median income of $99,159 (in 1995 dollars). By 1995, this

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[33] See, e.g., Judith A. McMorrow, *UK Alternative Business Structures for Legal Practice: Emerging Models and Lessons for the US*, 47 GEORGETOWN L. INT'L L. 665, 669-70 (2016) (discussing liberalization of legal regulatory changes in the U.K., Australia, continental Europe and Canada).

[34] John P. Heinz & Edward O. Laumann, Chicago Lawyers: The Social Structure Of The Bar (rev. ed. 1994) ("Chicago Lawyers I"); John P. Heinz et al., Urban Lawyers: The New Social Structure Of The Bar 6–7 (2005) ("Chicago Lawyers II").

[35] HEINZ ET AL., *supra* note 34, at 29 ("Only in the most formal of senses ... do the two types of lawyers constitute one profession.").

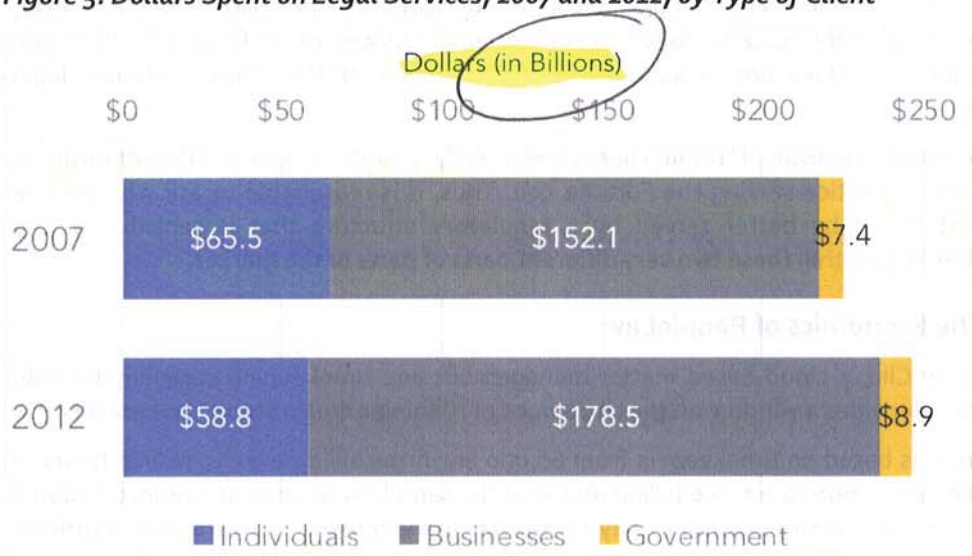
figure had dropped to $55,000. Further, in 1995, 32 percent of these lawyers were working second jobs compared to 2 percent in 1975.

In the remainder of this report, I will refer to the portion of the bar focused on individuals as the PeopleLaw sector. The portion of the bar focused on corporate clients will be referred to as the Organizational Client sector.

2.2. How Type of Client Shapes the Economics of Practice

The Chicago Lawyers hemisphere framework is a very useful lens for understanding the changes that are occurring within the legal profession. The most fruitful place to apply this framework is the U.S. Census Bureau's Economic Census, which includes breakdowns of economic activity based on "class of customer." Figure 5 below compares total spending on legal services in 2007 and 2012 based on individual, business, or government client:

Figure 5. Dollars Spent on Legal Services, 2007 and 2012, by Type of Client



Source: 2007 and 2012 Economic Census, Receipts/Revenues by Class of Customer

© Legal Evolution PBC

The most striking feature of Figure 5 is that over a five-year span, the total dollar amount for individual clients (PeopleLaw sector) declined by nearly $7 billion. During the same time, the amount allocated to business (Organizational Client sector) increased by more than $26 billion. Although solo and smaller incomes were in the decline in Chicago Lawyers, the actual *shrinkage* of the PeopleLaw sector suggests we are in the midst of an irreversible structural shift..

The stark differences between the PeopleLaw and Organizational Client sectors are made more concrete when the data is broken down by client type. Table 4 presents an estimated breakdown of average legal expenses by type of client:[36]

[36] For a complete discussion of data sources and methodology, see William D. Henderson, "The Legal Profession and Legal Services: Nature and Evolution," in LEGAL ETHICS, PROFESSIONAL RESPONSIBILITY, AND THE LEGAL PROFESSION § 1-1.2 (Gregory C. Sisk, ed., 2018).

Table 4. Breakdown of 2012 Law Firm Receipts by Type/Size of Client

Type of Client	Number	Total Receipts for Legal Services (thousands)	Avg. Payment per Client	% of Total Receipts
Individuals	314,000,000	$58,827,000	$187	23.9%
Business: < $1M to $5M	5,359,731	$41,310,000	$7,707	16.8%
Business: > 5M to $100M	344,037	$65,604,000	$774,910	26.7%
Business: > 100M to $4.75B	21,892	$41,500,000	$1,895,670	16.9%
Business: Fortune 500	500	$30,000,000	$60,000,000	12.2%
Government Entities	89,055	$8,900,000	$99,938	3.6%
	319,815,215	$246,141,000	$769.64	100.0%

Source: U.S. Census Bureau 2012 Economic Census, Calculations by Legal Evolution PBC

In 2012, the per capita amount spent on legal services by 314 million U.S. residents was $187. For businesses with less than $5 million in annual receipts, the average legal budget was $7,707. In contrast, for the 500 clients in the Fortune 500, the budget was $60 million. Indeed, in 2012, roughly one out of eight (12.2%) dollars spent on legal services came from a Fortune 500 company – and this does not include the economic value of their large in-house legal departments.

A law practice serving individual "retail" clients is obviously going to require a different business model than a law practice serving the Fortune 500. Thus, it is reasonable to ask whether the public interest would be better served by a regulatory structure that is sensitive to the challenges that exist within these two very different parts of parts of the market.

2.3. The Economics of PeopleLaw

A 2017 study by Clio, a cloud-based matter management and timekeeping company for solo and small firms, provides a window on the challenges of running a "main street" law practice.[37]

The Clio sample is based on timekeepers from 60,000 law firms billing over 10 million hours of time in 2016 totaling more the $2.56 billion. Because the sample is so large and reflects lawyers sophisticated and successful enough to pay for matter management software, it is surprising and disconcerting that the typical small firm lawyer is performing only 2.3 hours of legal work per day. Of that amount, only 82 percent is actually billed to clients; and of the amount billed, only 86 percent is being collected – the equivalent of 1.6 hours. At $260 per hour, which is the average rate for lawyers in the Clio sample, this amounts to a mere $422 a day, or $105,000 in gross receipts over a 50-week year. This is a sum that needs to cover office overhead, health care, retirement, malpractice insurance, marketing, taxes, etc. Of the remaining six hours left in the workday, 33 percent was focused on business development and 48 percent on administrative tasks, such as generating and sending bills, configuring technology and collections.[38]

The average matter in the Clio system was worth approximately $2,500.[39] Building a financially successful law practice out of low-stakes, high-volume cases requires capital for technology and marketing along with significant business acumen and managerial ability. Very few small firm

[37] See 2017 CLIO LEGAL TRENDS REPORT (2017), available online at https://www.clio.com/2017-legal-trends-report/#download (last visited July 1, 2018).

[38] *Id.* at 13.

[39] *See id.* at 8 (calculated from total dollars billed (~$2.56 billion) divided by number of matters (1.03 million matters)).

lawyers possess these resources and skills. Thus, as the Clio data show, they are forced to allocate a lot of their time to relatively ineffective methods of finding work. Under Rule 5.4, which exists in some variation in all 50 states, lawyers must be the exclusive owners of any business that engages in the practice of law.[40] This regulatory constraint may be a primary reason why the PeopleLaw sector has entered a period of serious decline.

5.4 as a constraint

2.4. The Economics of Large Organizational Clients

At the same time that the work of lawyers tilts more toward organizational clients, large corporate legal departments are increasingly seeking ways to control their legal expenses. This pressure is building because of the sheer complexity of a highly regulated and interconnected global economy. Although this pressure is experienced by lawyers and clients as a problem of cost, the root cause is lagging legal productivity, a topic discussed in greater detail in Section 3. This focus of this section, however, is the economics of large organizational clients.

For large corporate enterprises with operations throughout the U.S. and abroad, compliance with the law is a necessity. The sheer complexity of this task favors large law firms with a large array of highly specialized lawyers. Since the mid 1980s, *The American Lawyer* has tracked the financial performance of the nation's largest law firms. In 2012, on the 25th anniversary of the Am Law 100, the following statistics described the changes that had occurred among the nation's 100 largest law firms:

- Total gross revenues increased from $7.2 billion to $71.0 billion (+886%).
- Total lawyer headcounts went from 26,000 to 86,272 (+231% rise).
- Average profits per partner grew from $325,000 to $1.48 million (+355%).

The big getting bigger

During this same time period, the Consumer Price Index climbed 205 percent while the GDP increased 235 percent. Although the overall pie of the U.S. economy was growing, the nation's largest law firms were enjoying a proportionately larger slice.[41] Despite the continued climb of profits in the nation's large firms, the overall demand for corporate legal services, as measured by lawyer hours in law firms, has been relatively flat for the last several years.[42] This reflects a transition period where the firm has a higher proportion of older partners. By dint of experience, these partners bill at higher rates. This will persist in the short- to median term because many senior lawyers do not want to invest in new tools and learning—but neither do their older in-house counterparts. As baby boomer lawyers retire, however, the pace of change will accelerate.

Generational Shifts

The long-term trend is for in-house lawyers to do more with less.[43] Through the year 2018, the most aggressive cost-saving measures have occurred through insourcing—i.e., adding headcount in the legal department, primarily by hiring large firm associates.[44] Indeed, this trend

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[40] See Rule 5.4.

[41] *See* William D. Henderson, *AmLaw 100 at 25*, AMERICAN LAWYER (June 2012).

[42] *See* JAMES W. JONES, ET AL., 2017 REPORT ON THE STATE OF THE LEGAL MARKET (Georgetown Law, Center for the Study of the Legal Profession 2017) ("Overall, the past decade has been a period of stagnation in demand growth for law firm services, decline in productivity for most categories of lawyers, growing pressure on rates as reflected in declining realization, and declining profit margins.").

[43] See SUSSKIND, *supra* note 32, at 12 (discussing more-for-less imperative).

[44] See, e.g., Jacob Gershman, *Law Firms Face New Competition – Their Own Clients*, WSJ LAW BLOG, Sept. 14, 2014 ("This year corporations are shifting an estimated $1.1 billion that they used to spend on outside lawyers to their own internal legal budgets ... . That migration cements a trend that took off during the recession[.]"); Henderson,

Intro Legal Ops

was observed in Figure 2 in Section 1.2. The growth and proliferation of in-house lawyering have resulted in some legal departments, particularly in heavily regulated or IP-intensive industries, that are several hundred lawyers and thus are the functional equivalent of large law firms embedded inside multinational corporations. The largest and most advanced legal departments are now organized into practice groups. Many also include "legal operations" professionals focused on building processes and leveraging technology to cope with the tremendous complexity of running a company in an interconnected and globalized world.

This section is organized around the two-hemisphere framework. Yet, the structure of the Organizational Client sector has changed dramatically since the Chicago Lawyers II study. Thus, to more accurately conceptualize the current variations of organizational clients, the author created Figure 6.

Figure 6. Six Types of Clients

The Type No. 6 client in Figure 6 is an entirely new structure that only came into being within the last 10-15 years.

In addition to the growth of corporate legal departments, a second cost-saving measure is the diversion of work to alternative legal service providers (ALSPs), which includes companies such as Axiom, UnitedLex, Integreon, QuisLex, Elevate and many others. These are private corporations run by a mix of lawyers and business executives. In the majority of cases, they are financed by prominent venture capital and private equity funds.[45] This movement began with legal process outsourcers in the mid-2000's who specialized in large document review projects connected with the proliferation of electronically stored information. Yet these companies now perform work on sophisticated corporate transactions, albeit in each case under the supervision of either law firm or in-house lawyers.[46]

The steady growth of ALSPs is one of the main reasons that the lexicon on law has gradually shifted from discussions of the "legal profession" to a changing "legal industry." As noted by one investment banker who has provided significant funding to companies in the legal industry, "If law firms themselves can't have outside investors, the market will continue to chip away at

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Efficiency Engines, *supra* note 12, at 42 (Axiom CEO Mark Harris tracing growth of legal department back to "Ben Heineman at General Electric.").

[45] See, e.g., Henderson, *Efficiency Engines*, *supra* note 12, at 42 (discussing prevalence of sophisticated investors among managed services providers).

[46] This supervision is done pursuant to Rules 5.1 (responsibilities of supervisory lawyers) and 5.3 (responsibilities regarding nonlawyer assistants).

every part of a law firm that is not the pure provision of legal advice ... . Anything that can be provided legally by a third party will be."[47]

3. The Problem of Lagging Legal Productivity

As discussed in Section 2, the PeopleLaw and Organizational Client sectors are evolving in dramatically different ways. However, they have one crucial commonality: both groups are struggling to afford legal services. In the PeopleLaw market, this manifests itself in more citizens going without access to legal services. In the corporate market, clients cope by insourcing legal work and, when that is not possible, by demanding fee discounts from law firms. Both clients and lawyers view the financial gap between legal budgets and the corporations' legal needs as a problem of price – i.e., that legal services cost too much. Yet, it is more much accurately characterized as a problem of lagging legal productivity.

Crunch

3.1. Cost Disease

Throughout our modern economy, productivity gains vary widely from sector to sector. Because of improvements in design, technology, production processes and logistics, over the last two to three decades the typical consumer has enjoyed declining costs for thing like clothing, computers, long-distance calling, travel, etc. In some cases, the lowering of cost is also accompanied by significant increases in quality (e.g., safer and more reliable cars; the evolution of cellphones into smart devices).

In contrast, there are other sectors, such as education and medical care, where prices tend to go up much faster than worker income. The reason for the upward spiraling price is that these activities are very human-intensive and involve specialized human capital. Unfortunately, it is the *lack* of productivity gains in these sectors that accounts for their higher cost, as these workers have sufficient market power to raise prices to preserve their relative place in the economy.

This phenomenon is what economists refer to as "cost disease." It was first noted in a book by two economists, William Baumol and William Bowen, focused on the performing arts. The authors observed that the time and human effort it takes to perform a 45-minute Schubert quartet has not changed in hundreds of years.[48] Despite the inability of live musicians to improve productivity, the wages of the musicians continued to rise.

3.2. Law Compared to Medical Care and Higher Education

Along with medicine, education and the performing, law is a field afflicted with cost disease.[49] There is strong evidence, however, that society is adapting to higher relative costs for legal services in a different way than medical care and education.

Specifically, over the last three decades, consumers have generally allocated significantly more of their income to medical care and education. In contrast, the proportion of income allocated

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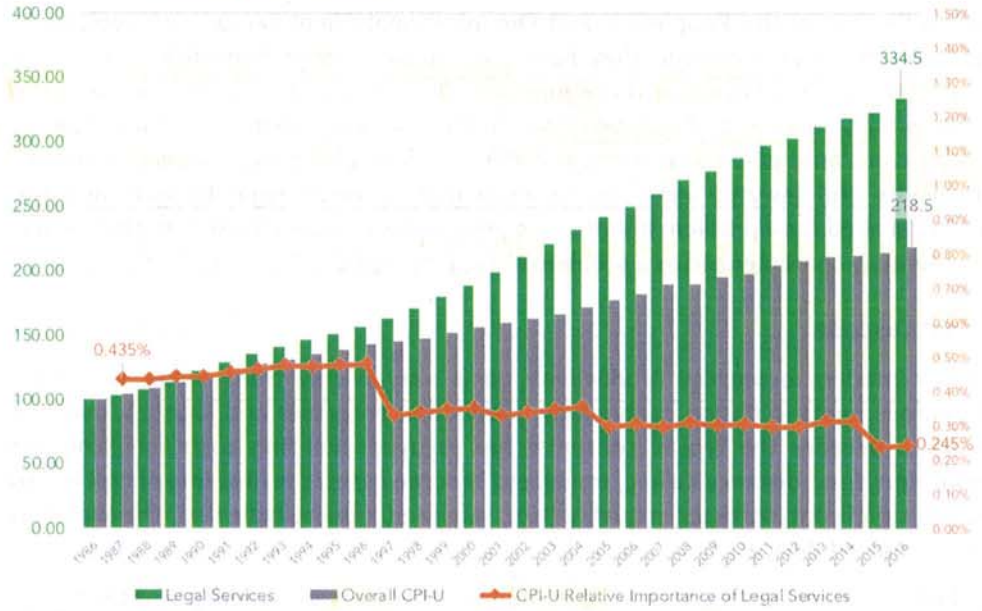
[47] *See* Barbara Rose, *Law, the Investment*, ABA JOURNAL (Sept. 2010) (quoting Nick Baughan of Marks Baughan & Co.).

[48] WILLIAM J. BAUMOL & WILLIAM G. BOWEN, PERFORMING ARTS: THE ECONOMIC DILEMMA 164 (1966).

[49] See generally WILLIAM J. BAUMOL, THE COST DISEASE: WHY COMPUTERS GET CHEAPER AND HEALTH CARE DOESN'T (2013) (discussing industry afflicted by cost disease along with possible public policy responses).

to legal services has declined by almost 50 percent. Stated more concisely, legal services are losing wallet share among U.S. consumers. Figure 7 shows these two trend lines together.

Figure 7. Legal Services Compared to Overall CPI-U and Relative Importance of Legal Services in CPI Basket



Source: Data from U.S. Bureau of Labor Statistics, calculations by Legal Evolution PBC

The left axis (green) in Figure 7 is the Consumer Price Index for All Urban Consumers ("CPI-U") with the base year set to 1986 (Index = 100). The green and gray bars show the cost of legal services rising nearly twice as fast as the overall CPI-U basket. The right axis (orange) measures the "relative importance" of legal services within the CPI basket. Basically, as the relative prices of goods and services change, consumers adjust how they allocate their money. The U.S. Bureau of Labor Statistics tracks these changes and uses this data to periodically reweigh the composition of the CPI-U basket.[50] What we observe is a gradual downward trend in which American consumers are finding ways to forgo legal services.[51]

Table 5 compares the change in wallet share of legal services to medical care and college tuition.

Table 5. Change in Relative Importance in CPI-U for Three Sectors

CPI component	Relative importance in CPI-U		
	1987	2016	Change over time
Legal Services	0.435%	0.245%	-43.7%
Medical Care	4.807%	8.539%	+77.6%
College Tuition	0.840%	1.807%	+120.3%

Source: Bureau of Labor Statistics, calculations by Legal Evolution PBC

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[50] See https://www.bls.gov/opub/hom/cex/home.htm (last visited July 5, 2018).

[51] The orange line in Figure 7 shows a sudden drop in the relative importance of legal services in 1997 (from 0.480% to 0.329% of consumer spending). This drop occurred because the BLS reweighted the CPI basket for the first time in several years. Yet, the CPI basket is now re-weighs the CPI based on a two-year rolling average.

3.3. Impact on the Practice of Law

Cost disease results in increases in relative prices in sectors that are very human-intensive. The price increases then can set off second-order effects, such as shrinking demand or substitution. The legal sector has all three symptoms.

- *Higher relative cost*: Even within the economically stressed PeopleLaw sector, the average hourly rate for a lawyer is $260.[52] In the Organizational Client sector, profits of large firms have increased much faster than the nation's GDP and Consumer Price Index.[53]
- *Shrinking demand*: Between 2007 and 2011, the PeopleLaw sector shrank by nearly $7 billion, or 10.2 percent.[54] This occurred on the heels of the deteriorating economics of lawyers serving individual clients.[55]
- *Substitution*: The PeopleLaw sector is increasingly served by legal publishers such as LegalZoom, Rocket Lawyer and many others that provide access to tech-enabled forms. In effect, this creates a consumer DIY culture where it is difficult to combine high-quality, low-cost forms with legal advice.[56] In the Organizational Client sector, in-house lawyers have become a substitute for law firms; in turn, ALSPs are a partial substitute for both.[57]

Replace-ment

The negative effects of cost disease occur because of lags in productivity between sectors. In the U.S., the market is constrained by the ethics rules with regard to nonlawyer ownership and the unauthorized practice of law. Thus, as a sizable portion of the public struggles to afford a lawyer and a sizable portion of the bar struggles to find sufficient fee-paying client work, legal regulators need to seriously evaluate whether the consumer protection benefits of these ethics rules are worth the cost. This topic is taken up directly in Section 4.

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3.4. Courts and Access to Justice

Courts are on the front line of the legal sector's cost disease problem. Yet, as explained below, courts are also partially responsible for cost disease.

Courts are on the front line because they are dealing with a surge in the number of self-represented litigants. This trend was recently documented in a major study conducted by the National Center for State Courts (NCSC).[58] The study was based on all civil matters in 10 large urban counties that were disposed of in those counties over a one-year period, including Santa Clara County.[59] The sample totaled 925,344 cases (approximately 5% of the total civil case load

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[52] See Section 2.3, *supra* at page 14.

[53] See Section 2.4, *supra* page 15.

[54] See Figure 5 and accompanying text.

[55] See Section 2.1, *supra* at page 12.

[56] This is due the ethics rules on fee-sharing (Rule 5.4) and unauthorized practice of law (Rule 7.2).

[57] See Section 2.4, *supra* at page 15.

[58] *See* PAULA HANNAFORD-AGOR JD, SCOTT GRAVES & SHELLEY SPACEK MILLER, THE LANDSCAPE OF CIVIL LITIGATION IN STATE COURTS (National Center for State Courts 2015) [hereafter LANDSCAPE STUDY] (building sample based on the July 1, 2012 to June 30, 2013 time period).

[59] The counties were Maricopa County (Phoenix, AZ), Santa Clara County (San Jose, CA), Miami-Dade County (Miami, FL), Oahu County (Honolulu, HI), Cook County (Chicago, IL), Marion County (Indianapolis, IN), Bergen

nationally) and was built to be roughly representative of the nation as a whole. Remarkably, 76 percent of cases involved at least one party who is self-represented, roughly double the number for the most comparable study conducted 20 years earlier.[60]

The increase in self-represented litigants is occurring because of the growing gap between the cost of lawyer representation and the value of the underlying claim. Of the 227,812 cases in the NCSC study that resulted in a nonzero monetary judgment, the median value was a mere $2,441. Further, three-quarters of all judgments were less than $5,100. Only 357 judgments were more than $500,000 and only 165 more than $1 million (i.e., the type that might be reported in the mainstream press). According to the NCSC, the median cost per side of litigating a case, from filing through trial, ranges from $43,000 for an automobile tort case to $122,000 for a professional malpractice case. Thus, "in many cases, the cost of litigation likely outstrips the monetary value of the case shortly after initiating the lawsuit."[61]

Although courts are seriously impacted by cost disease, they are also, in part, one of its causes. This is because the judiciary establishes the procedures lawyers must follow to resolve disputes. These procedures are rooted in lawyer tradition and the idiosyncratic preferences of local jurists. Yet rarely is the system evaluated from the perspective of a citizen with a legal problem. For this reason, the British lawyer and futurist Richard Susskind has posed the question, "Is court a service or a place?"[62]

When court is viewed as a service, the judicial process becomes something that can be re-engineered to lower costs and improve quality. Arguably, the most advanced system exists in British Columbia, Canada, where all civil matters under $5,000 and all strata (i.e., condominiums) disputes are required to be resolved through an online system managed by the recently created Civil Resolution Tribunal ("CRT"). Instead of an adversarial system with lawyers, parties without lawyers are guided through a structured online mediation process that is designed to produce early and amicable resolution. Case managers handle most of the work. Less than 5 percent of matters require formal adjudication by the CRT. Users of the CRT (citizens) are giving the system high marks for convenience, cost and fairness. Lawyers would be interested to know that the consulting practice of PwC, the Big Four accounting firm, built the CRT's online platform.[63]

On line Dispute Resolution

In the years to come, online dispute resolution ("ODR") is destined to grow. This is because ODR has the potential to lower government administration costs while improving the citizen experience. The European Union has implemented an ODR for all its consumer and online trading disputes. Its homepage reads, "Resolve your online consumer problem fairly and efficiently without going to court."[64] Similarly, in July 2018, two counties in the Greater Austin

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County (Hackensack, NJ), Cuyahoga County (Cleveland, OH), Allegheny County (Pittsburgh, PA), Harris County (Houston, TX).

[60] *See* LANDSCAPE STUDY, *supra* note 58, at 31.

[61] *See* LANDSCAPE STUDY, *supra* note 58 at 25, citing Paula L. Hannaford-Agor & Nicole L. Waters, *Estimating the Cost of Civil Litigation*, 20(1) Caseload Highlights 1, 2013.

[62] See SUSSKIND, *supra* note 32.

[63] See Richard Rogers & Kandis McCall, The Civil Resolution Tribunal: The World's First Government-Run ODR for Civil Disputes, presentation at the Forum on Legal Evolution, Nov. 9, 2017 (Chicago, IL), at https://forum.legalevolution.org/program/ (last visited July 6, 2018).

[64] See https://ec.europa.eu/consumers/odr/main/index.cfm?event=main.home2.show&lng=EN (last visted July 6, 2018).

area in Texas will commence using an online dispute resolution platform built by Tyler Technologies, a publicly traded company specializing in government services. One of the judges who helped implement the system called it "pajama justice" because "[p]eople can sit at home in their pajamas and get emails from the opposite side and see if they can reach a resolution."[65] Yet, the underlying methodology is grounded in a sophisticated understanding of the psychology of negotiations, mediation and settlement. For example, the new platform enables a litigant to request an apology. That, in turn, tends to reduce the payout.[66]

4. Ethics Rules and Market Regulation

In the U.S., ethics rules are the primary mechanism for regulating the market for legal services.[67] Most jurisdictions adopt some variation of the American Bar Association's Model Rules of Professional Conduct.[68] Although California has long promulgated its own ethics code, the substance of the California Rules has generally tracked with the policies of the broader U.S. legal profession. In November 2018, a new edition of the California Rules of Professional Conduct will go into effect that will utilize the same numbering system as the ABA Model Rules, thus facilitating easier referencing of rules across jurisdictions.

The key point of this section is that the ethics rules, particularly those pertaining to the prohibition on nonlawyer ownership (Rule 5.4) and the unauthorized practice of law (Rule 5.5), are the primary determinants of how the current legal market is structured. Without these rules, the market would look very different, as private businesses would be free to offer legal-oriented goods and services to both clients and lawyers. Indeed, as discussed in Section 1.5 of this report, private investors see ample opportunity in the current legal market.

The best way to orient the Trustees to the issues at hand is to describe how the current ethics rules are shaping the U.S. legal market. As noted in Section 2, the legal market is functionally segmented into the PeopleLaw sectors versus the Organizational Client sectors. The ethics rules affect these sectors in different ways.

4.1. The PeopleLaw Sector: LegalZoom and Avvo

Under the ethics rules, any business engaged in the practice of law must be owned and controlled by lawyers.[69] This prohibition limits both the opportunity and incentive for nonlegal entrepreneurs to enter the legal market. Despite this longstanding policy, private investors are increasingly pushing the boundaries of the existing rules.

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[65] See Claire Osborn & Taylor Goldenstein, *Area judges make plans to try out 'pajama' court*, MY STATESMAN, June 17, 2018, at: https://www.mystatesman.com/news/local/area-judges-make-plans-try-out-pajama-court/8HHpoy1Ip4qEv6USfjWubO/ (last visited July 7, 2018).

[66] See *id.* (quoting one of the Texas judges, "A lot of people are OK with getting less money than they want out of the case as long as the other person apologizes.").

[67] See, e.g., Larry E. Ribstein, *Ethical Rules, Agency Costs, and Law Firm Structure*, 84 VA. L. REV. 1707, 1707 (1998) (noting that "[e]thical rules are a form of professional self-regulation enforced by civil liability or professional discipline.").

[68] See https://www.americanbar.org/groups/professional_responsibility/publications.html (last visited July 7, 2018).

[69] The only exception in the U.S. is the District of Columbia, which permits a minority ownership of nonlawyers who "performs professional services which assist the organization in providing legal services to clients." Rule 5. 4(b) of the D.C. Rules of Professional Conduct. This modification of Rule 5.4 is widely viewed as a benign way to facilitate partnership stakes for nonlawyer professionals to do lobbying work on federal legislation.

There are dozens if not hundreds of companies that touch on some facet of the PeopleLaw sector that are also owned in whole or in part by nonlawyer managers and investors. However, the two most well-known examples are LegalZoom and Avvo. For the sake of clarity and simplicity, the author will focus on these two companies to illustrate how the ethical rules shape the legal marketplace serving individuals.

Legalzoom

Founded in 1999, LegalZoom specializes in tech-enabled legal documents that fit a wide array of individual and small-business needs. In 2012, LegalZoom filed an S-1 with the U.S. Securities & Exchange Commission (a requirement done in preparation for an initial public offering) but ultimately changed course and instead accepted more than $200 million funding from a European private equity firm.[70] Although LegalZoom is not a law firm and therefore cannot engage in the practice of law, its brand recognition, which it largely built through conventional mainstream media advertising, enables it to direct advisory legal work to a network of practicing lawyers. It is able to partially monetize this influence by running prepaid legal service organizations in various U.S. states as permitted under Rule 7.3.[71] At present, LegalZoom offers prepaid legal services plans for both individuals and small businesses.[72]

Avvo

Avvo is an online legal marketplace founded in 2006 by the former Expedia general counsel, Mark Britton. To get started, Avvo used public records of state bar rolls to build a website that included a nearly complete universe of U.S.-licensed lawyer profiles. In turn, the company created a 1-10 Avvo lawyer rating that was based on bar records and information scraped from online lawyer biographies on law firm websites. The algorithm generally gave higher ratings to lawyers who "claimed" their Avvo profile, as the lawyer was able to provide more complete biographical information. Over time, Avvo added Q&A forums by practice area, which enables lawyers to showcase legal knowledge and demeanor to potential clients. Avvo monetizes its platform by enabling lawyers to upgrade their profile page for a fee, essentially providing low-cost turnkey marketing solutions to small firm lawyers. Also, until recently, Avvo used its platform and marketing reach to facilitate the sale of flat-fee legal services between lawyer and clients (called Avvo Legal Services).[73] In exchange for providing these matching services, Avvo received a marketing fee. Avvo was capitalized with $132 million of venture capital funding.[74] In 2017, Avvo was acquired by Internet Brands, which is an online marketplace company that uses consumer-oriented content to create industry-specific sales channels. Internet Brands is currently owned by private equity company Kohlberg, Kravis Roberts & Co. (commonly known as KKR).

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[70] See Jason Smith, *LegalZoom.com Plans to Pull Its IPO, Sell Stake to Permira*, WSJ LAW BLOG, Jan. 7, 2014, at https://blogs.wsj.com/law/2014/01/07/legalzoom-com-plans-to-pull-its-ipo-sell-stake-to-permira/ (last visited July 7, 2018).

[71] The newly enacted California Rule of Professional Conduct 7.3, operative on Nov. 1, 2018, tracks the language of the ABA Model Rule. See MODEL RULES OF PROF. CONDUCT, Rule 7.3(d) ("Notwithstanding the prohibitions [on solicitation of clients] in paragraph (a), a lawyer may participate with a prepaid or group legal service plan operated by an organization not owned or directed by the lawyer that uses in-person or telephone contact to solicit memberships or subscriptions for the plan from persons who are not known to need legal services in a particular matter covered by the plan.").

[72] See https://www.legalzoom.com/attorneys/ (last visited July 7, 2018).

[73] This practice attracted pushback from a several state bars. See Appendix B. In July of 2018, Internet Brands made the decision to end Avvo Legal Services. See Bob Ambrogi, *Avvo Legal Services to be Shut Down*, LAWSITES, July 8, 2018, at https://www.lawsitesblog.com/2018/07/avvo-legal-services-shut.html (last visted July 12, 2018).

[74] See Crunchbase at https://www.crunchbase.com/organization/avvo#section-acquisition-details (last visited July 7, 2018).

Reflecting on the experiences of LegalZoom and Avvo, what is the gap in cost, quality and/or convenience that is attracting the interest of sophisticated professional investors? As discussed in Section 2.3 (declining size of PeopleLaw sector) and Section 3.4 (courts glutted with self-represented), there is ample evidence that ordinary citizens increasingly cannot afford traditional one-on-one consultative legal services. LegalZoom offers partial DIY solutions that help close this gap. Likewise, it is becoming increasingly difficult for lawyers to attract a sufficient and steady stream of paying clients.[75] Both Avvo and LegalZoom offer marketing services that help address this acute lawyer pain point.

Because of their substantial financial backing, LegalZoom and Avvo have been able to establish brand awareness throughout the United States. This high visibility has resulted in a number of run-ins with state regulators and practicing lawyers regarding allegations of the unauthorized practice of law (Rule 5.5, LegalZoom), impermissible fee-splitting (Rule 5.4, LegalZoom and Avvo) and payment of improper referral fees (Rules 7.2-7.3, Avvo).[76] In effect, these two companies have served as de facto test cases to establish the boundaries of private capital in the legal sector.

The author has reviewed a large number of state bar ethics opinions related to both companies. Although LegalZoom and Avvo have fared slightly better in some jurisdictions than in others,[77] what all of these opinions have in common is a careful textual reading of the ethical rules that cautions against activities that could be construed as a violation of the existing language. These opinions are not necessarily the final word, as they are typically advisory opinions from bar ethics committees. After the Supreme Court's ruling in *North Carolina State Board of Dental Examiners v. Federal Trade Commission*,[78] there is some basis to believe that these ethics rules and opinions may be subject to federal antitrust scrutiny. In situations where regulators are also "active market participants in the occupation" they are regulating, state-action antitrust immunity is only available when these regulators state are subject to active supervision by the state.[79] For example, the Antitrust Division of the U.S. Department of Justice has filed a statement of interest to intervene in a Florida Bar unauthorized practice of law case against a legal tech company. The company, TiKD, manages traffic tickets through a smartphone app.[80] The DOJ's statement is heavily based on the *North Carolina Board of Dentists* decision.[81]

SCOTUS

Antitrust Scrutiny

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[75] See Sections 2.3 and 3.4, *supra*.

[76] See Appendix B.

[77] For example, three committees appointed by the New Jersey Supreme Court jointly concluded that Avvo's legal service plan violated Rules 7.2(c), 7.3(d) and 5.4(a) and that LegalZoom (along with Google-based Rocket Lawyer) were operating unregistered legal plans pursuant to Rule 7.3(e)(4)(vii). The N.J. Supreme Court subsequently denied a petition to review the committees' conclusions. See David Gialanella, *Supreme Court Won't Take Up Avvo's Ethics Case*, NEW JERSEY LAW JOURNAL, Jun. 4, 2018, at https://www.law.com/njlawjournal/2018/06/04/supreme-court-wont-take-up-avvo-ethics-case/ (last visited July 7, 2018). In contrast, the North Carolina State Bar has treated Avvo's legal service plan as a payment for marketing rather than a referral fee. See Proposed 2018 Formal Ethics Opinion 1, Participation in Website Directories and Rating Systems that Include Third Party Reviews, Apr. 19, 2018 (not final rule), at https://www.ncbar.gov/for-lawyers/ethics/proposed-opinions/.

[78] See *North Carolina State Board of Dental Examiners v. Federal Trade Commission* (2015) __ U.S. __ [135 S.Ct.] 1101.

[79] Id. at 1114.

[80] See Nathan Hale, Fla. Bar Says Case Law Shows TIKD Is Unlicensed Practice, Law360, June 5, 2018, at https://www.law360.com/articles/1050404/fla-bar-says-case-law-shows-tikd-is-unlicensed-practice (last visited July 9, 2018).

[81] See *United States Department of Justice Supports Tech Start-Up TIKD's Antitrust Lawsuit Against The Florida Bar*, '4-TRADERS, Mar. 13, 2018 (providing link to complaint), at http://www.4-traders.com/news/United-States-

Rules developed w/ ∅ analysis of the marketplace serving consumers

What is missing from essentially all state ethics opinions on LegalZoom and Avvo – and arguably what is required by *North Carolina Board of Dentist Examiners* – is fact-gathering regarding whether consumers are made better or worse off by technical readings of the rules. Arguably, issues of policy (e.g., what construction of the rule best serves the interests of the public?) are not the province of an ethic committee. Yet, as noted earlier, ethics rules substantially determine the structure and functioning of the legal market. In most jurisdictions, the state supreme court has the authority to modify the rules of professional conduct. However, through norms or established procedure, input is sought from a bar committee of lawyers. Further, these groups, with perhaps the historical exception of California, invariably give substantial weight to ABA Model Rules of Professional Conduct. In turn, the Model Rules must be formally adopted by the ABA House of Delegates.[82] Nowhere in all this deliberation, however, is there an analysis of how the current legal market is serving consumers.

To both summarize and crystallize the issues in this section, the rules implicated in the LegalZoom and Avvo matters are premised on harm to clients that flows from lack of lawyer independence (Rule 5.4), incompetent legal service (Rule 1.1), unauthorized practice of law (Rule 5.5), and the dissemination of biased and/or misleading information (Rules 7.1-7.3). But as documented in Sections 2 and 3, there is very serious consumer harm occurring because ordinary citizens increasingly cannot afford traditional legal services. LegalZoom, Avvo and many other nonlawyer-owned businesses claim that they are a market response to that very need.

Professor Gillian Hadfield of the University of Southern California School of Law, who is both a lawyer and an economist, argues persuasively that outside sources of capital are most needed in the PeopleLaw sector to develop and finance innovative low-cost solutions to legal problems.[83] Following an in-depth analysis of the impact of the ethics rules on market structuring and functioning, Professor Hadfield forcefully concludes:

> The prohibition on the corporate practice of law ... hobbles the innovation of lower-cost means of providing legal help to the great majority of ordinary individuals. Many of those lower-cost innovations are within easy reach—if the profession would relax its stranglehold on the practice of law. ... Large-scale data and information systems are now available to provide standardized documents, procedures and protocols to meet the needs of a large segment of the population that now muddles through with no help at all in legal proceedings, imposing huge costs on our courts and other litigants. Innovators with one foot in the law and another in software or enterprise development are already at work but facing unnecessary and costly limits on their business models to comply with corporate practice rules that no one has, or could, demonstrate improve the well-being of ordinary individuals whose alternative to standardized online legal help is no legal help at all.[84]

Department-of-Justice-Supports-Tech-Start-Up-TIKD-s-Antitrust-Lawsuit-Against-The-Flor--26160154/ (last visited July 9, 2018).

[82] See ABA Constitution and By-Laws, Rules of Procedure for the House of Delegates.

[83] See Gillian K. Hadfield, *The Cost of Law: Promoting Access to Justice through the Corporate Practice of Law*, 38 INT'L REV. L. & ECON. 43 (2014).

[84] Id. at 77.

CA/Bar Mission

Under the State Bar Act, the "protection of the public" is the primary governing principle for the State Bar of California. The author encourages the Trustees to take an expansive view of protection that includes greater access to the legal system. Such a view would be consistent with the State Bar's mission statement in its five-year strategic plan.[85]

4.2. The Organizational Client Sector

Over the last 10-15 years, the evolution of the Organizational Client sector has been significantly shaped by the ethics rules, particularly the prohibition on nonlawyer ownership of businesses engaged in the practice of law.[86]

1. in house
2. ALSPs

As noted in Section 2.4, the Organization Client sector is also experiencing cost pressures attributable to lagging legal productivity. The front line of this challenge is a relentless increase in the volume and complexity of legal work that puts pressure on the budgets of corporate legal departments. The first level of response was to grow legal departments to reduce the work going to expensive law firms. The second level of response has been to experiment with ALSPs, particularly for large-scale document reviews.

Because ALSPs are substantially owned by nonlawyer entrepreneurs and investors, they have to navigate ethical duties related to competence (Rule 1.1), effective supervision (Rules 5.1 and 5.3) and unauthorized practice of law (Rule 5.5). In the mid-2000's, a series of California and New York local bar authority ethics opinions were favorable toward the use of ALSPs.[87] In 2008, the ABA issued Formal ABA Ethics Opinion 08-451, which effectively provided ALSP's and their clients with a roadmap for compliance with ethics rules.[88]

This roadmap, however, is somewhat counterintuitive. Despite the fact that most ALSPs employ legions of licensed lawyers, the work of ALSPs is typically characterized as paraprofessional work that must to be supervised by licensed lawyers. This duty, typically memorialized in the engagement letter, assigns supervisor duties to corporate in-house lawyers or outside counsel. This is how ALSPs, many of which are owned and controlled by private equity and venture capital investors, avoid charges of unauthorized practice of law (Rule 5.5) and thus nonlawyer ownership of law firms (Rule 5.4).

Yet this construction of the ethics rules provides a functional exception to Rule 5.4 for nonlawyer-owned companies serving large organizational clients. This is because the majority of legal services in the U.S. are bought by corporations with one or more in-house lawyers.[89] Thus, companies such as Axiom, UnitedLex, Integreon, Pangea3, Elevate and many others have become "lawyer to lawyer" businesses. Likewise, the Big Four accounting firms now routinely supplies legal services to major corporations, albeit under the supervision of the companies' legal departments. For example, roughly 600 tax professionals, many of them lawyers, left the

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[85] See http://board.calbar.ca.gov/Goals.aspx (last visited July 7, 2018).

[86] See Rule 5.4.

[87] See James I. Ham, *Ethical Considerations Relating to Outsourcing of Legal Services by Law Firms to Foreign Service Providers: Perspectives from the United States*, 2 PENN. ST. INT'L. L. REV. 323, 325-26 (2008) (collecting opinions and providing summary and analysis).

[88] See ABA Formal Opinion 08-451, Lawyer Obligations When Outsourcing Legal and Nonlegal Support Services, Aug. 8, 2008, online at https://www.americanbar.org/content/dam/aba/migrated/2011_build/ethics_2020/ethicsopinion08451.authcheckdam.pdf (last visited July 8, 2018).

[89] See Section 2.2, *supra*.

General Electric tax department and were "rebadged" as employees of PwC. In turn, the employees were contracted back to GE to work on their tax compliance tasks.[90]

Despite these inroads by sophisticated investors, Rule 5.4's ban on nonlawyer ownership remains a major roadblock to solving, or mitigating, the lagging legal productivity problem (i.e., cost disease). This is because the efficiency gains of lawyer specialization, which gave rise to law firms, have been fully exhausted. As evidenced by the rise of CLOC and the Type No. 6 client, many legal departments have become as big as large law firms.[91] This is occurring because the complexity of problems facing today's corporate clients requires close collaboration between technologists, process design experts, data scientists and lawyers. Indeed, as suggested by the discussion of artificial intelligence in Section 1.5, the future of law is profoundly multidisciplinary.[92] To foster innovation, the ideal would be to have lawyers and allied professionals working together as co-equals *within the same legal service organization*. Although ALSPs have found a workaround to Rule 5.4, it is still mostly limited to high-volume, highly repetitive legal work. Yet many higher-order quality and productivity problems remain.

Sophisticated clients

The policy that underlies Rule 5.4 is lawyer independence.[93] This independence is necessary because there is a presumption of asymmetric information between lawyers and unsophisticated clients that runs throughout the law of lawyering. If knowledge is asymmetric, clients have little choice but to trust lawyers. Under this policy rationale, lawyers as a group must be completely independent. Yet this asymmetry does not exist in large corporations with legal departments comprised of former large law firm lawyers. In this context, Rule 5.4 is actually *hindering* the creation of solutions most needed by large organizational clients.

4.3. The U.K. and Australian Models

Two other common law jurisdictions, the U.K. and Australia, have already liberalized their rules to permit lawyers to co-venture with other professionals.[94] The primary effect of this change is to create a new layer of "entity regulation" where an organization is responsible for maintaining a system of compliance for ethical rules that protect clients.[95] According to Professor Judith McMorrow, the regulatory changes reflected "a reorientation of legal services from a lawyer-centered focus [such as the Model Rules] to a client and customer-oriented perspective."[96]

Move from lawyer-centric to client + customer-centric

In many respects, the enactment of the State Bar Act of 2017 parallels the U.K.'s Legal Services Act 2007. This UK legislation created the Legal Services Board ("LSB"), which oversees all aspects of the legal services market and is charged with promoting eight regulatory objectives,

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[90] See Alex Berry, PwC strikes innovative deal with GE to take on in-house tax law team, LEGALWEEK, Mar. 17, 2017, at https://www.legalweek.com/sites/legalweek/2017/03/17/pwc-strikes-innovative-deal-with-ge-to-take-on-in-house-tax-law-team/ (last visited July 8, 2018).

[91] See Section 1.3 and 2.4, *supra*.

[92] This is also the conclusion of one of the legal industry's most influential knowledge management consultants who is also a law school graduate. See Ron Friedmann, *A Multidisciplinary Future to Solve Legal Problems*, PRISM LEGAL, May 2018, at https://prismlegal.com/a-multidisciplinary-future-to-solve-legal-problems/ (last visited July 8, 2018).

[93] See Rule 5.4, Comment [1] ("The provisions of this Rule express traditional limitations on sharing fees. *These limitations are to protect the lawyer's professional independence of judgment*." (emphasis added)).

[94] See Section 1.5, *supra*.

[95] See McMorrow, *supra* note 33, at 669.

[96] *Id.*

the first of which is "protecting and promoting the public interest."[97] In addition, three other objectives are explicitly consumer oriented: "(c) improving access to justice; (d) protecting and promoting the interests of consumers of legal services; [and] (e) promoting competition in the provision of legal services[.]"[98] In 2009, the LSB created the Legal Services Consumer Panel, which is composed of citizens and businesses. The Panel's role is to provide independent advice to the Legal Services Board about the interests of users of legal services."[99] This entails "investigating issues that affect consumers and by seeking to influence decisions about how lawyers are regulated."[100] To summarize, the U.S. system is designed to guard against lawyer impropriety; in contrast, the U.K. system focuses foremost on consumer welfare and polices lawyer impropriety through entity regulation.

A comprehensive history and analysis of the regulatory systems of other common law countries is beyond the scope of this report. Nonetheless, the Trustees should be aware that having undertaken analyses far more exhaustive than this report over the course of nearly a decade, these jurisdictions concluded that it was time to end the prohibition on nonlawyer ownership.[101]

5. Conclusion

Law has long been modeled as a self-regulated profession. The primary means of regulation are ethics rules that govern lawyer duties and conduct. However, there is evidence that a large number of clients and potential clients are being underserved by the legal market.

The core market problem is one of lagging legal productivity that, over time, increases the price of traditional consultative legal services relative to other goods and services. In addition to being very harmful to ordinary citizens, this is a major challenge to lawyers trying to earn a living in the PeopleLaw sector. A second problem affecting the legal market is the relentless growth in complexity that flows from living in a highly interconnected and globalized world. Lawyer specialization by itself is no longer sufficient to meet the finite budgets of even the world's wealthiest corporations.

Hurts consumers + lawyers serving consumers

The legal profession is at an inflection point that requires action by regulators. Solving the problem of lagging legal productivity requires lawyers to closely collaborate with allied professionals from other disciplines, such as technology, process design, data analytics, accounting, marketing and finance. By modifying the ethics rules to facilitate this close collaboration, the legal profession will accelerate the development of one-to-many productized legal solutions that will drive down overall costs; improve access for the poor, working and middle class; improve the predictability and transparency of legal services; aid the growth of new businesses; and elevate the stature and reputation of the legal profession as one serving the broader needs of society.

Some U.S. jurisdiction needs to go first. Based on historical precedent, the most likely jurisdiction is California. The public policy that underlies the legal ethics rules is one of consumer protection. Legal regulators should take a capacious view of this policy and acknowledge the harm that occurs when ordinary citizens cannot afford cost-effective legal

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[97] See https://www.legislation.gov.uk/ukpga/2007/29/section/1 (lasted visited July 7, 2018).

[98] See Legal Services Act 2007, at https://www.legislation.gov.uk/ukpga/2007/29/section/1 (last visited July 12, 2018).

[99] See http://www.legalservicesconsumerpanel.org.uk/ (last visited July 12, 2018)

[100] Id.

[101] See generally McMorrow, *supra* note 33.

solutions to life's most basic problems, such as sickness, housing, old age, family planning and access to government benefits. The law should not be regulated to protect the 10 percent of consumers who can afford legal services while ignoring the 90 percent who lack the ability to pay. This is too big a gap to fill through a renewed commitment to pro bono. This is a structural problem rooted in lagging legal productivity that requires changes in how the market is regulated.

The author is grateful and humbled by the opportunity to write this report.

Appendix A

Business Development / Marketplaces
WL
ROCKET LAWYER
foxwordy
lawcus
Avvo
LIBRA
Derecho-24
upcounsel
lawanswers
lawgo
Lawyers Live
LAWGIVES
LEGAL REACH
DirectLaw
Lawpolis
LEXBLOG
HIRE an ESQUIRE
Lexicata
Litigation Funding
LEGAL FUNDING CENTRAL
CASEHUB
CrowdDefend
Litigation Funding
LexShares
CROWD LAW
Legal Education
Quimbee
ADAPTIBAR
LEGALSWIPE
HOTSHOT
ChartaCourse
RainmakerVT
LawMeets
Lawline
LEGAL TALK NETWORK
apex CLE
InterActive Legal
E-discovery
Ategra
detavue
logikcull
lexbe
GoldFynch
Bend Law Group, PC
bitproof.io
kCura
Crayda
Everlaw
Legal Tech Startup Landscape
THOMSON REUTERS
Practice Management
LegalLogs
LAW RULER
CaseFleet
Attorney's Back Office
BIGTIME
Clio
Firmex
LEGAL FLOW
HOUDINIESQ
Intake123
TENDER SCOUT
LawStudio
mycase
MerusCase
NetLex
VINDULA
Smokeball
rocket matter
netlex
Voltaire
Legal Research
BookLawyer
DOCKET ALARM
DATY
KNOMOS
fastcase
Jurify
blueJ
caseflex
PACER PRO
JUDICATA
ROSS
COURT LISTENER
Global-Regulation
AI Patents
BESTLAW
BriefMine
casetext
Case Mgmt /Analytics
TRAKLIGHT
JURISPECT
Lex Machina
KNOMOS
RAVEL
JURISTAT
AppealTrack
ALLEGORY
LEGAL ROBOT
NEOTA LOGIC
Document Automation
FairDocument
WORDRAKE
HOTdocs
Captain Contrat
After1
ROCKET LAWYER
DirectLaw
ALGOVALUE
DraftLaw
Legalix
lubenda
lawdeal
CASERAILS
inkdit
Docasaurus
Contract Management / Analysis
Brevia
Clausehound
Counselytics
Precisely
BEAGLE
LEVERTON
kira
Contractually
ContractCloud
CLEARCONTRACT
avtal
DRAVN
Consumer
Clearpath
coparently
DC2
supportpay
CREDITSWARM
LAR
KINSO
frag-einen-anwalt.de
Thistoo
Online Dispute Resolution
bidsettle
ClaimCast
Zipcourt
MODRIA
FAIR
swiftcourt
Pactanda
Divorce Secure
yurJURY

Appendix B

Table of Ethics Opinions on Avvo*

Jurisdiction	Citation	Digest
Illinois	Client-Lawyer Matching Services Study, Attorney Registration and Disciplinary Commission of the Supreme Court of Illinois (June 25, 2018)	Prohibiting lawyers from participating in or sharing fees with for-profit services that refer clients to or match clients with participating lawyers is not a viable approach, because the prohibition would perpetuate the lack of access to the legal marketplace.
Indiana	Opinion #1-18 (April 2018)	Avvo Legal Services risks violation of Rules 1.2(c), 5.4(a), 5.4(c), 7.2(b), 7.3(d), 7.3(e).
New Jersey	ACPE Joint Opinion 732; CAA Joint Opinion 44; UPL Joint Opinion 54 (June 21, 2017)	Avvo Legal Service improperly requires lawyer to share legal fee with a nonlawyer in violation of Rule 5.4(a) and pay impermissible referral fee in violation of Rules 7.2(c) and 7.3(d).
New York	Ethics Opinion 1132 (Aug. 9, 2017)	A lawyer may not pay the current marketing fee to participate in Avvo Legal Services, because the fee includes an improper payment for a recommendation in violation of Rule 7.2(a).
North Carolina	Proposed Amendment to Rule 5.4 (July 26, 2017 (pending approval)	Proposed amendment to Rule 5.4 by Subcommittee on Avvo Legal Services that would allow paying reasonable portion of a legal fee to a credit card processor or online platform for hiring a lawyer if business relationship will not interfere with lawyers's professional judgment on behalf of client.
Ohio	Opinion 2016-03 (June 3, 2016)	To comply with Rules 7.1-7.3, hypothetical referral service similar to Avvo would need to be registered with the state of Ohio and meet its requirements. Marketing fees raise issues of impermissible fee-sharing (Rule 5.4).

* Avvo Legal Services was discontinued in July of 2018. See Bob Ambrogi, *Avvo Legal Services to be Shut Down*, LAWSITES, July 8, 2018, at https://www.lawsitesblog.com/2018/07/avvo-legal-services-shut.html (last visted July 12, 2018).

Jurisdiction	Citation	Digest
Oregon	Oregon State BarMeeting of the Board of Governors (Nov. 17, 2017)	Giving progress report on proposed changes to 7.3 (liberalizing referral fees affecting Avvo), 5.4 (nonlawyer fee-sharing) and permitting partial ownership of law firms by licensed paraprofessionals.
Pennsylvania	Formal Opinion 2016-200 (Sept. 2016)	Avvo Legal Services product likely violates RPC 5.4(a) and Rule RPC 1.15(i), which requires legal fees paid in advance to be deposited in the lawyer's Trust Account. Also raises issues with Rule 1.2, 1.6, 1.16, 5.3, and 7.7.
South Carolina	Ethics Advisory Opinion 16-06 (2016)	Avvo Legal Services violates Rule 5.4 (a) prohibition of sharing fees with a non-lawyers. Arrangement would also violate the Rule 7.2(c) prohibition of paying for a referral and is not saved by the exceptions found in Rule 7.2(c)(1), (2), or (3).
Utah	Opinion No. 17-05 (Sept. 27, 2017)	Hypothetical legal service similar to Avvo legal services violates Rule 5.4's prohibition on splitting fees with a non-lawyer. It also violates Rule7.2's restrictions on payment for recommending a lawyer's services and may violate a number of other Rules elated to client confidentiality, lawyer independence, and safekeeping of client property.
Virginia	In re Legal Ethics Opinion 1885 (Oct. 27, 2017) (pending Supreme Court approval)	Avvo Legal Services violates Rule 5.4(a) and Rule 7.3(d). Rules should not be rewritten to permit this service, as consumer benefits are not outweighed by anticompetitive effects.

About the Author

Professor William Henderson

Professor William Henderson is on the faculty at Indiana University Maurer School of Law, where he holds the Stephen F. Burns Chair on the Legal Profession.

Professor Henderson's focuses primarily on the empirical analysis of the legal profession and has appeared in leading legal journals, including the *Stanford Law Review*, the *Michigan Law Review*, and the *Texas Law Review*. In addition, he regularly publishes articles in *The American Lawyer*, *The ABA Journal*, and *The National Law Journal*. His observations on the legal market are also frequently quoted in the mainstream press, including the *New York Times*, *Wall Street Journal*, *Los Angeles Times*, *Atlantic Monthly*, *The Economist*, and National Public Radio. Based on his research and public speaking, Professor Henderson was included on the *National Law Journal's* list of The 100 Most Influential Lawyers in America (complied every ten years). In 2015 and 2016, he was named the Most Influential Person in Legal Education by *The National Jurist* magazine.

In 2010, Professor Henderson co-founded Lawyer Metrics, an applied research company that helps lawyers and law firms use data to make better operational and strategic decisions. Lawyer Metrics (now LawyerMetrix) was acquired by AccessLex Institute in 2015. In 2017, he founded Legal Evolution, an online publication that chronicles successful innovation within the legal industry.

ATTACHMENT B

Excerpt from LegalZoom Terms of Use

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Source: https://www.legalzoom.com/legal/general-terms/terms-of-use (Accessed on July 13, 2018.) (Emphasis in original.)

Excerpt from AVVO.COM Terms of Use

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3. Information on the services

Our Services display both Avvo-created content and content that is not created or developed by Avvo (the "Legal Information"). We may review third party-content to determine whether it is illegal or violates our policies, and we may remove or refuse to display content that we reasonably believe violates our policies or the law. But we do not routinely screen third-party content that is published via our Services. This includes the Legal Information that lawyers post on Avvo, and we cannot guarantee the accuracy, adequacy or quality of any such Legal Information, or the qualifications of those posting it.

4. No formation of an attorney-client relationship

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5. Legal services for consumers

Avvo is a platform where lawyers unaffiliated with Avvo can offer information and interact with consumers. We provide a number of methods by which you can purchase legal services or have a direct, confidential discussion of your legal issues with a lawyer. Although some of these methods involve Avvo processing a transaction on your behalf, in all instances, Avvo is simply the intermediary in such transactions. You are liable for paying the lawyer for the services provided. Avvo has no liability, either primarily or secondarily, for paying the lawyer other than as an agent on your behalf. The fees you pay for such services are charged by the lawyer and passed through to the lawyer once services have been rendered. Any attorney-client relationship formed as a result of such discussions is between you and the lawyer you speak with—not between you and Avvo. Furthermore, you understand that Avvo cannot be held responsible for the quality or accuracy of any information or legal services provided by lawyers you connect with via Avvo.

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Source: https://www.avvo.com/support/terms (Accessed on July 13, 2018.)