

**Final report**

**Prepared For:**

Legal Services Board  
7<sup>th</sup> Floor, Victoria House  
Southampton Row  
London WC1B 4DA

# Cost benefit analysis of policy options related to referral fees in legal services

**Prepared by:**

Charles River Associates  
99 Bishopsgate  
London EC2M 3XD

Date: May 2010

---

## TABLE OF CONTENTS

EXECUTIVE SUMMARY .....	1
1. INTRODUCTION.....	8
1.1. APPROACH .....	8
1.2. DEFINITIONS .....	10
1.3. POLICY SCENARIOS .....	12
1.4. METHODOLOGY.....	14
1.5. STRUCTURE OF THE REPORT.....	16
2. CONVEYANCING.....	17
2.1. DEMAND FOR CONVEYANCING SERVICES .....	17
2.2. SUPPLY OF CONVEYANCING SERVICES.....	20
2.3. PRICE OF CONVEYANCING SERVICES .....	24
2.4. ROLE OF REFERRAL FEES IN COMPETITION FOR CONVEYANCING .....	26
2.5. MARKET FAILURE AND POTENTIAL DETRIMENT ARISING FROM REFERRAL FEES .....	29
2.6. CHANGES IMPACTING FUTURE COMPETITION .....	42
2.7. POLICY OPTIONS .....	42
3. CRIMINAL ADVOCACY .....	48
3.1. DEMAND FOR LEGAL SERVICES.....	48
3.2. SUPPLY OF LEGAL SERVICES.....	50
3.3. PRICE OF LEGAL SERVICES .....	54
3.4. ROLE OF REFERRAL FEES AND FEE SHARING ARRANGEMENTS IN COMPETITION FOR ADVOCACY SERVICES .....	58
3.5. MARKET FAILURE AND POTENTIAL DETRIMENT ARISING FROM FEE SHARING ARRANGEMENTS .....	65
3.6. CHANGES IMPACTING FUTURE COMPETITION .....	74
3.7. POLICY OPTIONS .....	78
4. PERSONAL INJURY.....	82
4.1. DEMAND FOR LEGAL SERVICES.....	82
4.2. SUPPLY OF LEGAL SERVICES .....	84
4.3. PRICE OF LEGAL SERVICES .....	88
4.4. ROLE OF REFERRAL FEES IN COMPETITION FOR LEGAL SERVICES .....	90
4.5. MARKET FAILURE AND POTENTIAL DETRIMENT ARISING FROM REFERRAL FEES .....	99
4.6. CHANGES IMPACTING FUTURE COMPETITION .....	108
4.7. POLICY OPTIONS .....	109

## LIST OF FIGURES

Figure 1: Distinction between the payment flows in referral fees and fee sharing arrangements.....	10
Figure 2: Illustrative payments.....	11
Figure 3: Illustrative payments where £100 of other services are also provided .....	12
Figure 4: What proportion of clients choose the conveyancing service to which you refer them? .....	18
Figure 5: Proportion of customers who shop around .....	19
Figure 6: Do you have a panel or list of solicitors/conveyancers to whom you refer customers? .....	21
Figure 7: Since 2004, has the proportion of conveyancing work in your area which is done by national solicitor/ conveyancer firms... ..	24
Figure 8: The average conveyancing fee for a property valued at £200,000.....	25
Figure 9: Customers following the recommendation of the estate agent.....	28
Figure 10: Typical conveyancing fee for a property valued at £200,000.....	30
Figure 11: The average time to complete for conveyancers who pay a referral fee compared to those who do not pay a referral fee .....	35
Figure 12: Queries or complaints regarding referral fees.....	37
Figure 13: Complaints regarding the quality of the conveyancing service.....	38
Figure 14: Disclosure of the referral fee to the client.....	45
Figure 15: How, if at all, have the arrangements under which your firm instructs barristers changed in the past 5 years?.....	53
Figure 16: RTAs and RTA injuries.....	83
Figure 17: Supply of legal services in personal injury .....	84
Figure 18: New authorisations of businesses handling personal injury claims .....	85
Figure 19: Level of referral fees from 2004 to 2009 .....	93
Figure 20: Services and referral fees .....	94
Figure 21: Number of motor claims .....	96
Figure 22: Number of personal injury claims in employers' liability.....	98
Figure 23: RTA claims and success rate 2005-09 .....	100
Figure 24: Employer liability claims and success rate 2005-09 .....	101
Figure 25: Average claims payment for bodily injury in motor claims .....	102
Figure 26: Average time to settle a claim by a major solicitor firm.....	104
Figure 27: Customer satisfaction for a major solicitor firm .....	105

## EXECUTIVE SUMMARY

The Legal Services Board (LSB) appointed Charles River Associates (CRA) to assess the impact of referral fees on the legal services market. The use of referral fees has been permitted for solicitors since 2004. However, they are a controversial issue. Opponents of referral fees have called for them to be abolished arguing that they reduce the quality of legal services. Supporters have argued that abolition would be detrimental arguing that referral fees are an efficient manner of obtaining work and improve access to justice.

As the oversight regulator for legal services the LSB wanted to consider the overall impact of referral fees on the market and determine whether they work in the best interests of consumers. Alongside this research, the LSB Consumer Panel commissioned qualitative consumer research to understand consumer's views regarding referral fees.

Although referral fees were the primary focus of the analysis other payment mechanisms can give rise to similar economic incentives. The potential for economic equivalence between payments made through referral fees, fee sharing arrangements and payments for other services is an important element of the consideration of the functioning of legal services markets and in particular, of the effectiveness of potential policy scenarios.

The research has examined three different parts of legal services: conveyancing; criminal advocacy; and personal injury. We set out our main conclusions on these areas below.

### Conveyancing

It is common for a referral fees to be paid by the conveyancer to the estate agents that refers the customers. Indeed, conveyancing was the second most popular area for the payment of referral fees (after personal injury). Consumers are much more likely to shop around for conveyancers (we use the term to refer to both solicitors and licensed conveyancers) than other areas of the legal services market with 50% of consumers shopping around. Price is considered an important element of competition in conveyancing and forms an important part of the shopping around process.

Before 2004 complex arrangements had been in place to pay fees such as marketing fees or membership fees which have a similar economic effect to referral fees. Changes in 2004 enabled these arrangements to be converted into referral fees that were legitimate under regulation.

There is evidence that the choice of conveyancer is determined by estate agents on the basis of referral fees and this has contributed to the trend towards having panels of conveyancers and national firms and away from using local firms. This trend had already begun before 2004 with large firms seeking to centralise referral arrangements and move towards using more formal panel arrangements. Smaller conveyancers who do not pay referral fees often have other arrangements in place with estate agents such as reciprocal referral arrangements regarding probate work or the need for a valuation in a matrimonial dispute or offering hospitality.

We do not find that referral fees impact the quantity of conveyancing undertaken which is instead based on the number of property transactions and re-mortgages. However, competition to access introducer panels has led to referral fees increasing over time from around £50 - £100 in 2004 to £250 - £400 today. There is no evidence that this is increasing conveyancing fees paid by the consumer which have remained broadly constant over time. In addition, the available evidence also suggests that the average

conveyancing fee for those paying referral fees is lower (at £543) than those who do not pay referral fees (£687). This may reflect that formal arrangements have facilitated investment in technology that reduces the cost of the conveyancing process. Given that referral fees have risen but conveyancing fees have stayed the same, this reflects a transfer from conveyancers to estate agents. It is unclear if this has been passed into consumers in terms of the price that estate agents charge.

There is also no evidence that the quality of conveyancing was being reduced because of referral fees. For example:

- There was no evidence of problems regarding the title of property;
- Referral fees have facilitated significant automation of the conveyancing process and the use of non-qualified staff. While national conveyancers offer a remote service with communication by phone and email, compared to local conveyancers who may offer face-to-face services, there is no evidence that the different approach to communication reduces quality.
- National conveyancers are able to access information regarding searches implying that there is no local advantage. Further, small local conveyancers do not believe that their service suffers when they provide conveyancing advice for long-term clients who have moved out of the locality.
- Evidence on the number of complaints is low, customer satisfaction is high and the speed of transaction appears to be faster for those who pay referral fees - 57% of estate agents thought these firms faster compared to only 2% who thought those who did not pay referral fees were faster.

### *Policy options*

It is important to recognise that since we find no evidence that referral fees are currently causing consumer detriment in the conveyancing market, policy options which are focused on referral fees are unlikely to bring benefits:

- Banning referral fees is expected to lead to a return to the situation seen before 2004 where “creative schemes” were used to get around restrictions on paying referral fees. While small firms may continue to have reciprocal referral arrangements or pay for hospitality, larger firms would opt for more systematic arrangements such as entering into marketing arrangements. The advent of Home Information Packs which conveyancers can provide to estate agents at low cost may provide another way in which firms could “get around” any ban on referral fees. If it were possible to enforce a ban, it is likely that large firms would choose to enter into alternative business structures in which the conveyancer and estate agent become part of the same firm thereby internalising the payment of referral fees.
- Capping referral fees could be useful in theory if there is a group of consumers who are facing high conveyancing fees caused by very high referral fees, but there is no evidence this is the case. A cap would face similar problems to a ban with the additional costs of determining how the cap would be set or reviewed over time with a flat cap potentially distorting arrangements where referral fees vary according to the value of the property.
- Disclosure of information to clients is already required for solicitors, licensed conveyancers and introducers to solicitors. Compliance with these rules has been

poor in the past although large firms have indicated that they have observed increased enforcement efforts and these firms tend to have automated systems that provide the relevant disclosure information. Although consumers favour transparency, there is no evidence that they respond to information related to referral fees partly because they focus on the overall conveyancing fee that they needed to pay. CRA has been provided with disclosure documents from one major firm which gives monetary amounts related to the fees which are passed to the conveyancer and those which are retained by the estate agent. Of around 25,000 conveyancing transactions each year, they are only aware of around 10 cases where customers had raised any issues on the referral fee. The lack of consumer response to disclosure is consistent with evidence from the financial services sector where intermediaries are also common.

- The final policy option is that information on referral fees is provided to the Approved Regulator. It is unclear how gathering this information would enable consumer detriment to be measured in the absence of measures of quality. Since there is no evidence that the conveyancing market has cases where particularly high referral fees are paid alongside a very low quality service it appears more appropriate to gather market-wide information. There appears to be little advantage to the market from publishing aggregate information. National conveyancers currently pay higher fees than small conveyancers but they do so because of competition rather than any lack of information.

### **Criminal advocacy**

Referral fees are not used in criminal advocacy, however, fee-sharing is common and can have similar effects. Clients usually rely on a solicitor to instruct an advocate on their behalf and interviewees agreed that clients were in a very weak position to be able to assess the quality of advocacy services.

Under legal aid, advocates in the Crown Court are paid through the Advocate Graduated Fee Scheme (AGFS) and a similar scheme applies for litigators (LGFS). Fees for the AGFS increased in 2007 and those for the LGFS fell in 2008 hence advocacy became relatively more profitable than litigation. The AGFS also brought in the concept of the "Instructed Advocate" who is the advocate with primary responsibility for the case.

There has been an increased use of solicitor advocates as changes to the AGFS encouraged more solicitors to obtain their higher rights of audience. It is not possible to conclude that this has reduced quality. There has also been an increase in the use of in-house advocates over time although quantitative data is not available on this. There are concerns that a focus on profitability causes advocates to be appointed for cases beyond their competency although we note this has also arisen in response to the changes to the AGFS and is not a function of fee sharing arrangements.

As well as keeping whole cases in-house, interviewees have indicated that cases are kept in-house where clients are expected to plead guilty. If clients then decide not to plead guilty, substitute advocates may be required at short notice. Interview evidence has also highlighted that Instructed Advocates may not always be the trial advocate or conduct the Plea and Case Management Hearing (PCMH) although again quantitative evidence is not currently available on these trends. The primary driver of both issues is the relative profitability of the AGFS compared to the LGFS rather than fee sharing arrangements.

It should be noted that last minute preparation appears common for PCMHs hence no additional consumer detriment arises compared to normal practice. However, there are concerns that the use of inexperienced advocates can adversely impact the defence. The lack of a quality assurance scheme means little prevents this from arising. This also means it is not possible to assess the extent of detriment.

There has also been suggestions that there has been an increase in the use of in-house "straw" junior advocates with external advocates required to use in-house juniors in order to secure the case. Some of the evidence of these arrangements pre-date changes to the AGFS in 2007 although interviews suggest this has increased over time. Concern by the Judiciary resulted in action against junior advocates generally rather than in-house straw juniors which may indicate difficulties in identifying these particular advocates. The impact on clients is mitigated by the actions of the leading advocate although resources are wasted.

Interview evidence has also identified that some solicitors appoint external advocates on the basis of fee sharing. This causes them to prefer:

- Solicitor advocates compared to barristers in order to avoid the Bar Protocol which sets out how fee sharing among barristers should occur under the AGFS; and
- Solicitor advocates who will accept non-Protocol fees in preference to those who are not willing to accept non-Protocol fees.

It seems common for non-Protocol fee sharing arrangements to be set at 80% of the fees that might otherwise have been expected. There is no evidence that 80% fee-sharing is itself reducing quality. Furthermore, the operation of the Bar Protocol means that in some cases substitute advocates would be conducting a particular role for 80% (or less) of the fee that they might expect in other cases. We note that there are also no immediate benefits to either the client or the Legal Services Commission (LSC) from non-Protocol arrangements.

However, there are concerns that a focus on profitability causes solicitor advocates to be appointed for cases beyond their competency although the greatest impact of this is observed on less complex cases. It is also possible that this will lead to a potential reduction of experienced barristers in the future or change in career path for advocacy with more in-house advocates and fewer independent barristers.

There is also evidence of other referral arrangements being in place such as senior barristers within chambers receiving Crown Court work in return for low priced junior barristers for Magistrates Court work. We note that low prices linked to such referral arrangements is unlikely to be distinguishable from low prices linked to increased competition in Magistrates Courts. No consumer detriment was identified from this or from other referral arrangements such as the provision of training, mentoring schemes and secondments in anticipation of receiving referrals.

It is also worth noting that there are a number of changes that are likely to affect the criminal advocacy market over time including:

- Reductions to the fees paid under the AGFS which broadly reverse the increases seen in 2007. This will change the incentives for individuals or firms to undertake advocacy although solicitor firms will continue to assess the relative profitability of conducting advocacy in-house compared to instructing external advocates; and

- Use of one-case-one-fee and best value tendering – once proposals are sufficiently developed on these issues it may be necessary for the LSB to consider their impact on the issues raised in the report. It may also affect the proportionality of intervening in advance of these changes.

### *Policy options*

As noted above there is concern that a focus on profitability causes concerns that both in-house advocates and external solicitor advocates are appointed for cases beyond their competency. The former is driven by the AGFS itself while the latter arises through fee-sharing arrangements.

It should be noted that the absence of a quality assurance scheme at present means that there is little to prevent a deterioration in quality from arising, but also means it is not possible to assess the extent of detriment that occurs.

We consider the potential policy options below:

- Allowing referral fees for barristers (in the same way they are allowed for solicitors) would not have any effect in criminal advocacy since referral fees are currently banned under the LSC's contract.
- Banning referral fees would not have any effect since they are not currently used in criminal advocacy.
- Banning fee sharing arrangements altogether is considered to be disproportionate since timetabling constraints in the Crown Court and uncertainty regarding the length of time that some cases will take means that flexibility to use substitute advocates is required. Under the current AGFS this requires the use of fee sharing arrangements.
- Banning non-Protocol fee sharing arrangements would not address the concerns that a focus on profitability causes in-house advocates to be appointed for cases beyond their competency and may cause firms to employ additional in-house advocates. However, when choosing between external advocates, such a ban would place solicitors and barristers on a level playing field (although this could also be achieved by removing the Bar Protocol) and remove price from the selection process leaving the choice to be made primarily on the basis of quality.<sup>1</sup>

In the absence of a quality assurance scheme, banning non-Protocol fee sharing arrangements would be expected to bring benefits from an increase in quality compared to today by reducing the risk that high quality efficient advocates are undermined by low quality advocates. However, this position only holds while there is no alternative method of assessing quality and we note that the Quality Assurance for Advocates (QAA) scheme is already under development. Once the QAA is in place and enables quality to be assessed, allowing price competition to arise may be beneficial. Indeed this would drive efficiency enabling efficient advocates to gain at the expense of inefficient advocates with the quality assurance scheme protecting the level of quality. We note that this is also the premise behind many of the changes

---

<sup>1</sup> It remains possible that the choice is made on the basis of "other referral arrangements", but broadly this would return the decision making-process to the same factors as that before the revised AGFS where fewer concerns about quality were raised. Hence the removal of price from the decision process implies that quality would be expected to play a greater role in the selection process.



proposed in the Carter Review which saw a quality assurance scheme as a precondition of introducing price competition.

- Capping referral fees is not a relevant policy option in the area of criminal advocacy where referral fees are not paid.
- Disclosure to clients regarding fee sharing arrangements was not supported since the accused is not commonly paying for either the litigation or the advocacy service.
- Disclosure of information related to fee sharing arrangements could be made to the Approved Regulators or to the LSC. In theory this could enable the LSC to assess where prices for certain activities were out of line although this would also require additional information related to the work sharing arrangements. We also note that if future prices for advocacy will be set with reference to best value tendering rather than through administrative price setting by the LSC then the value of gathering this information will be reduced. The large number of cases and the complexity of the different elements which affect fees under the AGFS also limits the extent to which it would be feasible, or useful, to publish information on fee sharing arrangements to allow for more informed negotiation between parties.

### Personal injury

Personal injury is the area of law in which referral fees are most prevalent and where the majority of cases are referred by introducers such as Claims Management Companies (CMCs), insurance companies (for road traffic accidents) and trade unions (for employer liability cases).

The payment of referral fees was found to be an important element (although not the only element) in gaining access to CMC and insurer lists or panels and there was clear evidence that lawyers who pay referral fees receive more work than those that do not. Competition to access these panels has led referral fees to increase from around £250 per case in 2004 to around £800 per case today. We also found evidence that the level of referral fees paid today was linked to the services provided by introducers as well as to issues such as economies of scale and bargaining power.

There was no evidence that increases in referral fees had led to an increase in the price of legal services. Price does not play a strong role in personal injury cases because of the prevalence of “no-win-no-fee” agreements, but the majority of motor cases go through prescribed cost and fast track regimes in which legal fees are regulated.

There was also no evidence that referral fees were causing consumer detriment through a reduction in the quality of services:

- Success ratios for motor claims remained constant over time at over 90% although interviewees indicated that liability was often clear and therefore quality could not be judged on success ratios alone; and
- Information is readily available on the value that different types of standard claims should receive and there was no evidence that increases in referral fees were leading solicitors to under-settle so as to save themselves costs.

Furthermore, arrangements between large introducers and large solicitors usually have service level agreements associated to them in which lawyers must meet certain requirements typically related to communication and speed of response. In part these agreements are in place to help protect the reputation of introducers. Evidence is

available on very high customer satisfaction levels and there are very few complaints made related to referral fees.

Referral fees have helped to facilitate the growth of CMC and insurer referrals through providing an income stream that can be used for both marketing and investment in technology to manage the claims process. Consumer evidence has supported the link between marketing and making additional claims which would not otherwise have arisen. There is no evidence that this has led to a deterioration of cases since success rates have remained constant. The increase in the number of claims has probably led to higher insurance prices although this has been partly offset by referral fee income. It is difficult to describe this as causing consumer detriment where consumers have valid claims. We note that concerns about some fraudulent claims have causes other than referral fees namely the (non-)verifiable nature of some claims.

Instead of using referral fees, lawyers working with some trade unions will instead often provide other legal services to the trade union for low prices or offer to conduct training and education for free. These arrangements have a similar economic effect to referral fees although they do not involve lawyers making payments to the unions. No evidence was found regarding any trend in the value of alternative referral arrangements used by trade unions. No evidence was provided that any change in the number of cases or values of claims in employer liability was linked to referral fees or their equivalent.

#### *Policy options*

Since there was no evidence that referral fees in personal injury cases are causing consumer detriment, policy options focused on altering referral fees are unlikely to bring benefits:

- Banning referral fees was considered likely to lead to a return to the use of referral arrangements which were used before 2004 to get around legislation. Given that CMCs undertake marketing services for which payment could be made, and both trade unions and insurance companies could receive other legal services for low prices, policing a ban would be challenging. Further, in as far as a ban could be enforced, banning referral fees would be detrimental since they have facilitated an increase in claims.
- Capping fees would face the same difficulties of enforcement as a ban but if it was possible to enforce a cap this could distort competition as it would favour business models in which there was a “pure referral” (where referral fees are low) over those businesses in which introducers offer additional services (where higher referral fees were identified as being paid).
- Disclosure of information to clients is already required and while there have historically been concerns about compliance, increased enforcement is understood to have arisen in recent years especially for large firms. However, large firms have reported a lack of response by consumers to information related to referral fees with one stating they had received only two comments compared to 50,000 cases.
- Greater disclosure to regulators could lead regulators to identify outliers in the level of referral fees. However, if the concern is that these reduce quality it would appear better to for regulatory attention to focus on measures of quality. There appears little appetite from businesses to have aggregate information on referral fees published and therefore it seems unlikely that this would have a beneficial impact on the market.

## 1. INTRODUCTION

In January 2010, the Legal Services Board (LSB) asked Charles River Associates (CRA) to assess the impact of referral fees on the legal services market. In particular, the LSB has asked for:

- An assessment of the impact of referral fees on the market;
- A robust analysis of the impact of alternative policy options; and
- A review of the range of costs and benefits for the LSB to consider in its subsequent analysis. The objective was to provide the LSB with a robust evidence base to determine whether any regulatory intervention is required.

The use of referral fees has been permitted for solicitors since 2004. However, they are a controversial issue. Opponents of referral fees have called for them to be abolished arguing that they reduce the quality of legal services. Supporters have argued that abolition would be detrimental arguing that referral fees are a cost-effective manner of obtaining work and improve access to justice.

As the oversight regulator for legal services the LSB wanted to consider the overall impact of referral fees on the market and determine whether they work in the best interests of consumers. Alongside this research, the LSB Consumer Panel commissioned qualitative consumer research to understand consumer's views regarding referral fees.

### 1.1. Approach

We have undertaken a number of tasks during the course of the project which are described below:

**Assessment of existing research:** Background research was conducted on material specific to the issue of referral fees as well as gathering information on different markets where referral fees were commonly used and the role of introducers in these markets. There were a variety of recent reports which were particularly relevant for the assessment of referral fees such as the Jackson Report reviewing Civil Litigation Costs and the recent OFT Market Study on home buying and selling.<sup>2</sup> In addition, there is a range of regulation and proposals regarding regulatory change that needed to be taken into account. This includes the potential development of alternative business structures combining legal and non-legal services into the same firm.

**Initial interviews to understand the range of concerns regarding referral fees:** We undertook a series of initial interviews with the approved regulatory bodies and industry representative bodies. The purpose of these interviews was to understand how the different markets work, whether referral fees were used and whether these were currently a cause of concern. During this stage CRA also attended the LSB consumer panel roundtable discussion regarding the role of referral fees. Based on the results of this interview programme and the issues raised during the course of the roundtable discussion, CRA agreed with LSB that we would focus on conveyancing, criminal advocacy and personal injury.

---

<sup>2</sup> Lord Justice Jackson, Review of Civil Litigation Costs: Final Report, December 2009 – we refer to this as the Jackson Report. OFT, Home buying and selling, A Market study, February 2010, OFT1186.

**Interview programme with market participants:** An extensive programme of over 40 interviews was undertaken with a cross-section of different types of legal service providers, intermediaries and other stakeholders. The objective was to understand how referral fees worked in practice, how these have changed over time and what would happen under the different policy scenarios. Wherever possible, interviewees were also asked to provide evidence from their own businesses on various aspects that might be affected by referral fees. Unless otherwise noted, all information in the report sourced as interview evidence is based on the interviews conducted for this research. The breakdown of interviews is set out in Table 1 below.

**Table 1: Interviews conducted**

	Conveyancing	Criminal advocacy	Personal injury	Across all markets
(Approved) Regulator	1	1	1	3
Barristers		2		
Introducers	3 (1 estate agent, 2 mortgage providers)		8 (2 insurers, 4 Claims Management Companies, 2 trade unions)	
Solicitors (or licensed conveyancers)	7	2	2	
Trade associations	2	2	4	1
Other (Judiciary and Legal Services Commission)		3		
<b>Total</b>	<b>13</b>	<b>10</b>	<b>15</b>	<b>4</b>

Source: CRA.

In addition to the interviews, CRA attended a workshop organised by the Claims Management Regulator on claims management regulation and the development of the personal injury market.

**A quantitative survey of estate agents:** On behalf of CRA, the National Federation of Property Professionals facilitated an electronic survey of estate agents. This resulted in 179 responses to a set of questions designed by CRA regarding the conveyancing sector and the use of referral fees. The survey was conducted during late February and early March 2010.

**Policy assessment:** The final step in the approach was to draw together the different sections of the analysis to understand the different competitive forces that are operating, the reasons behind the development of referral fees in some parts of the legal services market and any detriment they cause. For each of the three areas that we examine, we then set out consider the cost and benefits of alternative policy scenarios (see section 1.3 below for details of these scenarios).

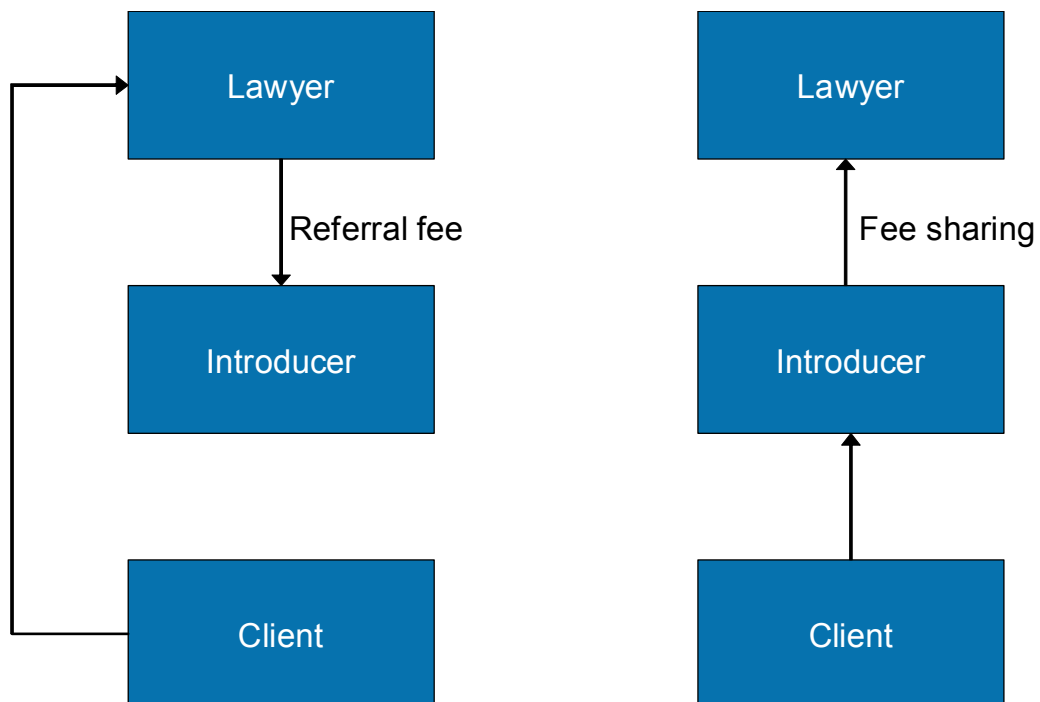
## 1.2. Definitions

CRA was asked to consider the impact of referral fees. It is therefore important to ensure that there is a clear understanding of what a referral fees actually is. In agreement with the LSB we use the following definition of a referral fee,

*“Any payment made for the referral or introduction of any client or potential client”*

In addition, it was considered important to distinguish between a referral fee and a fee sharing agreement with a key element to do with the flow of payments. The distinction is made in Figure 1 below.

**Figure 1: Distinction between the payment flows in referral fees and fee sharing arrangements**



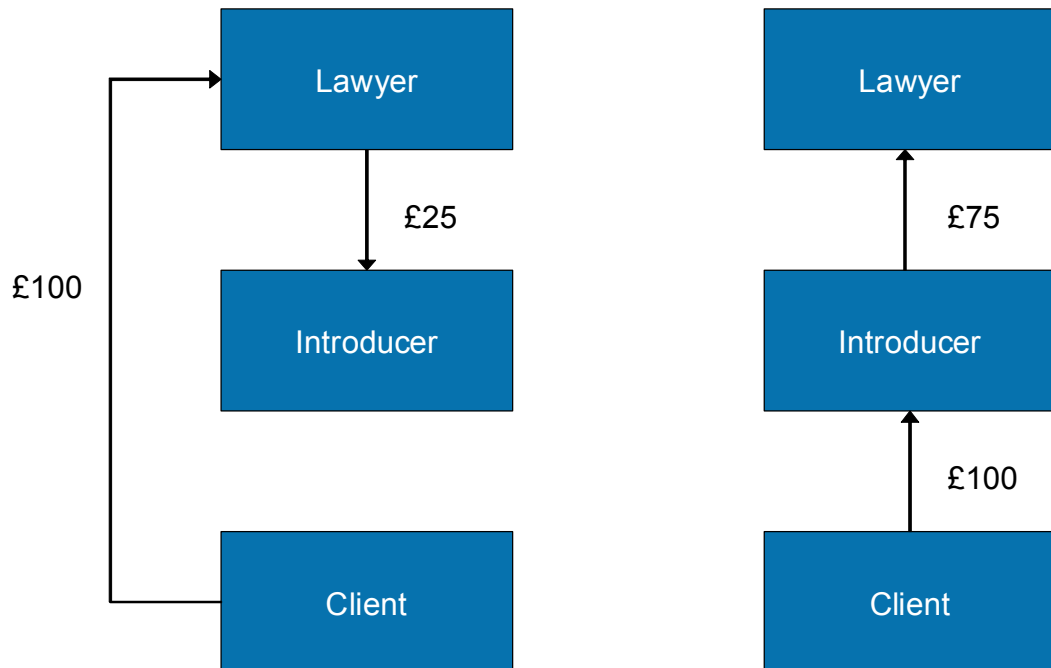
Source: CRA

In the picture above, the arrows represent the flow of money in reflection of an agreement to provide services. In the example on the left of the picture, the client contracts directly with the referred lawyer. The lawyer then pays the introducer for the referral of the client to them. This would be considered to be a referral fee.

In the example on the right of the picture, the client contracts directly with the introducer who receives the full amount of the relevant fee. The introducer then passes on a proportion of this fee to the referred lawyer. This would be considered to be a fee sharing arrangement.

It is important to note that in economic terms a referral fee and a fee sharing arrangement can be equivalent regarding the payments that are made as shown in Figure 2.

**Figure 2: Illustrative payments**



Source: CRA

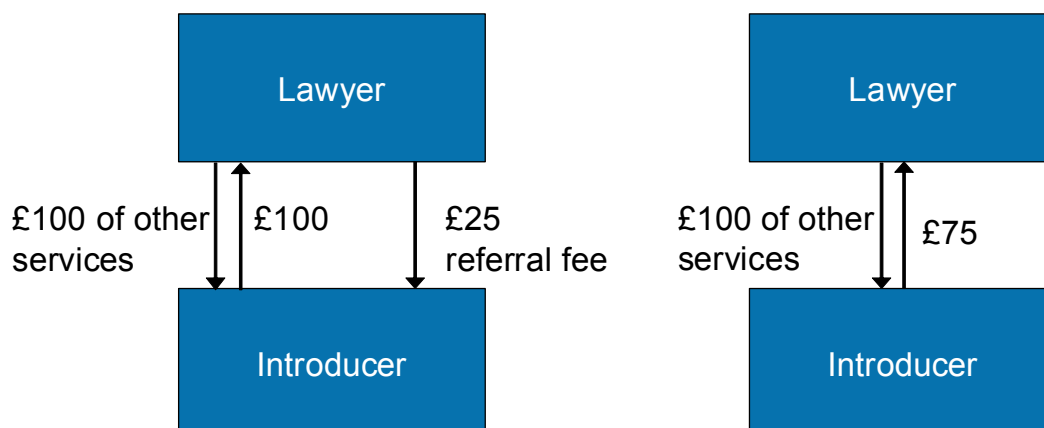
In the picture on the left the client pays £100 to the lawyer who then pays £25 to the introducer. In the picture on the right the client pays the £100 to the introducer who then pays £75 to the lawyer. In both cases, the client pays £100, the introducer receives £25 and the lawyer receives £75. Hence the referral fee and the fee sharing arrangement result in the same outcome in terms of the value of payments which result.<sup>3</sup>

Furthermore, a similar economic effect can also arise where other services are provided by lawyers to the introducer and where the cost of these services is provided at a rate which is lower than would otherwise be the case. A simplification of this is shown in Figure 3 below.

---

<sup>3</sup> There may be differences regarding who the client considers to be acting on their behalf.

**Figure 3: Illustrative payments where £100 of other services are also provided**



Source: CRA

In the picture on the left the lawyer provides £100 worth of other services to the introducer for which the lawyer is paid £100. (These services might include undertaking the defendant cases for an insurance company or providing employment advice to a trade union.) At the same time, the lawyer pays £25 as a referral fee for the introduction of work. In the picture on the right, instead of paying £25 as a referral fee, the lawyer is paid only £75 for work for which they would otherwise have charged £100. The economic effect is the same in both cases but only the picture on the left has a referral fee.<sup>4</sup>

Recognising the potential for economic equivalence between payments made through referral fees, fee sharing arrangements and payments for other services is an important element of the consideration of the effectiveness of the various policy scenarios in each of the three areas that we examine in this research. In particular, we note that where the economic effects of a referral fee can be replicated through other means (such as fee sharing arrangements or reduced fees for other services), policies which are focused on referral fees alone are unlikely to be effective.

### 1.3. Policy scenarios

As with any cost benefit analysis it is important to set out the range of policy scenarios to be investigated. The LSB provided a range of different alternatives that are considered in this report, the detail of which we set out below.

1) **No change to existing rules** – At present, solicitors are allowed to pay or receive referral fees under the Solicitors Regulatory Authority's (SRA's) Code of Conduct.<sup>5</sup> Under the Code of Conduct, solicitors must disclose information regarding the referral fees to clients and must also require that the introducer also discloses this information to clients. The Council for Licensed Conveyancers (CLC) requires that conveyancers disclose information on referral fees to clients, but does not require that they ensure the introducer

---

<sup>4</sup> It may also be possible to replicate similar arrangements through using agency agreements between the introducer and the lawyer such as through the introducer being explicitly paid for providing marketing services or the provision of a call centre.

<sup>5</sup> SRA, Solicitor's Code of Conduct 2007 as amended in March 2009, Rule 9. The rule regarding disclosure does not apply to referrals between lawyers.

does the same.<sup>6</sup> At present, barristers are not allowed to pay or receive referral fees under the Bar Standard Board's (BSB's) Code of Conduct and this scenario assumes that this ban would remain in place for barristers.<sup>7</sup> The Ministry of Justice (MoJ) requires that where Claims Management Companies (CMCs) introduce business to solicitors the CMC must not act in a way that puts the solicitor in breach of rules governing solicitors' conduct hence they would need to disclose any financial arrangement between them and the solicitor.<sup>8</sup>

This scenario represents the rules in place at the time of writing (as well as the current extent to which these rules are complied with) and is therefore used as the baseline scenario against which the other policies are compared. Information provided in the rest of the report regarding the way in which competition works in the various different markets therefore relates to this scenario.<sup>9</sup>

2) **No restrictions on referral fees** – In this scenario we assume that both the SRA and CLC rules remain in place, but the BSB Code of Conduct would be altered such that barristers are allowed to pay or receive referral fees. The effect of this is considered in the chapter on criminal advocacy.

3) **Referral fees are allowed but the referral fees are capped** – In this scenario a “cost council” would be set up to assess the caps. This could be set as a fixed amount per case where annual payments would be allowed but the average payment per case would need to be below the cap. This is similar to one of the proposals in the Jackson Report regarding the personal injury market.<sup>10</sup>

4) **Referral fees are allowed but the referral fees must be disclosed to clients in an agreed format** – Under the existing rules, information regarding referral fees should be disclosed to clients by solicitors or conveyancers and also by those who introduce work to solicitors. However, depending on the arrangements between solicitors/conveyancers and their introducers, the information disclosed may not necessarily include a monetary amount. In this scenario the level of referral fees would need to be disclosed to clients. This would either take the form of the fee which is specifically related to the specific client's case or, where other forms of payment are made (such as annual payments), the average payment per case would need to be disclosed (potentially in addition to the fee for the specific client). It is assumed that this would apply across all the relevant Approved Regulators.

5) **Referral fees are allowed but the referral fees must be disclosed to the Approved Regulators** – Currently referral fees should be disclosed to the customer but this does not require information to be provided to the Approved Regulator. In this scenario referral

---

6 CLC, Licensed Conveyancers' Conduct Rules 2009, Rule 5.2.8 and Guidance Note 6.

7 BSB, Code of Conduct, Paragraph 307(e).

8 MoJ, Claims Management Services Regulation, Conduct of Authorised Persons Rules 2007, Client Specific Rules Rule 8.

9 Throughout the report we will sometimes refer to a particular “market”. The use of this terminology should not be interpreted as implying that this is the appropriate “relevant economic market” for the purpose of competition law.

10 The Jackson Report recommends that referral fees are banned in personal injury cases (see scenario 6) or that referral fees are capped at a “modest” figure which is suggested as £200.



fees would need to be disclosed to Approved Regulators (although we do not assume that there would be changes in what is disclosed to clients). This scenario may also involve publishing market wide information related to referral fees.

6) **Referral fees are banned altogether** – In this scenario, referral fees (as defined in section 1.2) would be banned.

These are the main policy scenarios examined in the report, however, during the development of the report a number of other potential policy options were also worthy of consideration. In particular, this included the management of fee sharing arrangements in the criminal advocacy market.

It should also be noted that we do not consider a policy option of banning all referral “arrangements” as opposed to banning referral fees. This is because such a policy is considered to be detrimental for consumers. Markets where different firms provide different but complementary services and where working together on behalf of clients is in the interest of those clients. This is particularly the case if clients are in a relatively poor position to identify multiple different providers of these complementary services because they only use legal services infrequently. For example:

- Banning referral arrangements would mean that lawyers who provided services to trade unions would not be able to provide advice to trade union members even though these law firms may have been appointed in order that members can currently gain access to them.
- Similarly, if it were possible to ban referral arrangements this may require radical changes to the operation of the independent bar who frequently describe themselves as a “referred profession” as they primarily rely on referrals for work from solicitors rather than having direct access to clients. It could be argued that solicitors do not refer work to barristers but instruct them on behalf of clients. However, this appears sufficiently indistinct as to make banning referral arrangements but allowing the instruction of a barrister on the client’s behalf no different to today. If the intention of such a ban in referral arrangements would be to prevent referrals then this would leave the independent bar only able to seek work directly from clients.

#### 1.4. Methodology

Our approach to the assessment of policy options is to conduct a cost benefit analysis (CBA). Broadly speaking this involves examining how markets currently function, whether consumers face any detriment from the current functioning of the market and whether policy options would bring benefits.

The specific approach which we take in considering the market is to examine the following issues:

- Quantity of legal services: in particular we consider the provision of legal services to particular consumer groups;
- Quality of legal services provided: understanding where there are incentives to improve or reduce quality is important although the metrics by which this is assessed vary from market to market;
- Competition both now and in the future: this is considered in terms of whether competition is working to offer the best value to customers and whether innovation is

encouraged in the services that are provided and the different business models that may be developed in the future; and

- Regulatory cost: this is associated with the introduction and monitoring of the regulation regime which is of relevance both for the firms who are regulated and also in respect of the direct regulatory costs which fall on the regulatory bodies themselves.

This approach is similar to that taken by the Financial Services Authority which is required to conduct a CBA of significant regulatory changes introduced. In common with most CBAs we primarily assess the impact of policy proposals with respect to consumers although we also seek to set out the impact on providers of different types of legal services and other firms which are currently involved in the operation of the markets. The different issues we consider interact with some of the LSB's regulatory objectives. For example:

- protecting and promoting the public interest – this links closely to issues to do with the quality of legal services;
- improving access to justice – this is linked to measures of both the quantity of legal services provided and also the quality of legal services provided;
- protecting and promoting the interests of consumers - this is linked to all of the elements of the evaluation process since the assessment is conducted primarily from the perspective of consumers' interests;
- promoting competition in the provision of services in the legal sector – this will be taken into account both in terms of the way that competition works now (static competition) as well as the impact on competition over time (dynamic competition);
- encouraging an independent, strong, diverse and effective legal profession – this links both to the quantity of legal services as well as to issues of competition which encourage a strong and effective sector;
- increasing public understanding of citizens' legal rights and duties – this links to issues of whether the method through which competition arises impacts consumer understanding; and
- promoting and maintaining adherence to the professional principles of independence and integrity; proper standards of work; observing the best interests of the client and the duty to the court; and maintaining client confidentiality – again this is highly related to issues to do with the quality of legal services which are provided.

Finally, it is important to recognise that even if we identify consumer detriment resulting from referral fees, this is not sufficient to justify regulatory change. The costs of the introduction of the policy must not outweigh the benefits from having the policy for intervention to be appropriate. In doing so, this ensures that any intervention meets the Government's principles for good regulation, in particular that regulation is proportionate and targeted.<sup>11</sup>

---

11 Other elements of good regulation include that regulation is accountable; consistent; and transparent.

## **1.5. Structure of the report**

The rest of the report is structured as follows:

- Chapter 2 examines the role of referral fees in the conveyancing market;
- Chapter 3 examines the role of referral fees in the criminal advocacy market; and
- Chapter 4 examines the role of referral fees in the personal injury market.

In each of these chapters we first set out the demand and supply conditions in each market before considering how prices are set and the role of referral fees in the way that competition arises. We then consider whether this leads to consumers facing detriment in these markets and how any future changes in the market may affect this. We conclude each chapter by explaining whether the various policy options described above would be expected to overcome any detriment identified and in particular whether they would bring benefits that outweigh any associated costs.

## 2. CONVEYANCING

In this chapter we consider the role of referral fees and other referral arrangements in the area of conveyancing. This area was raised as an area of potential concern during the LSB Consumer Panel's roundtable discussion and during the initial interviews. Referral fees are commonly paid by solicitors and conveyancers operating in this area. Indeed, The Law Society's Practice Standards Unit (PSU) identified that, after the personal injury area, conveyancing was the second most popular area in which firms disclosed to The Law Society the presence of referral arrangements.<sup>12</sup>

For convenience throughout the chapter we will refer to conveyancers to mean both solicitors and licensed conveyancers. Where we believe there is a difference between them we make this explicit.

### 2.1. Demand for conveyancing services

The conveyancing process involves the transfer of the "title" of a property or piece of land from the seller to the purchaser. Conveyancing involves a range of legal and administrative tasks focused primarily on searches and pre-contract enquiries. Typically it will also involve ensuring that a mortgage on the property is appropriately recorded if one is required. There are therefore two main reasons for using conveyancing services:

- When purchasing or selling a property; and
- When re-mortgaging a property.

It is possible for individuals to conduct the conveyancing service themselves although it is considered rare for individuals to do so. Typically the purchaser will consider engaging a conveyancer once they have found a home they wish to purchase. In the past, vendors (sellers) would typically choose a conveyancer when they had found a purchaser who is interested in the property. However, the advent of Home Information Packs (HIPs), which have to be made available to potential buyers, has meant that conveyancers are now often appointed earlier in the process (this is discussed further below).

When it comes to the selection of the conveyancer, consumers will frequently use a conveyancer they have used before or seek recommendations from someone they know.<sup>13</sup> In addition, it is common for consumers to use a conveyancer recommended by the estate agents involved in the sale of the property. This is supported by evidence from the survey of estate agents undertaken for this project and shown in Figure 4.<sup>14</sup>

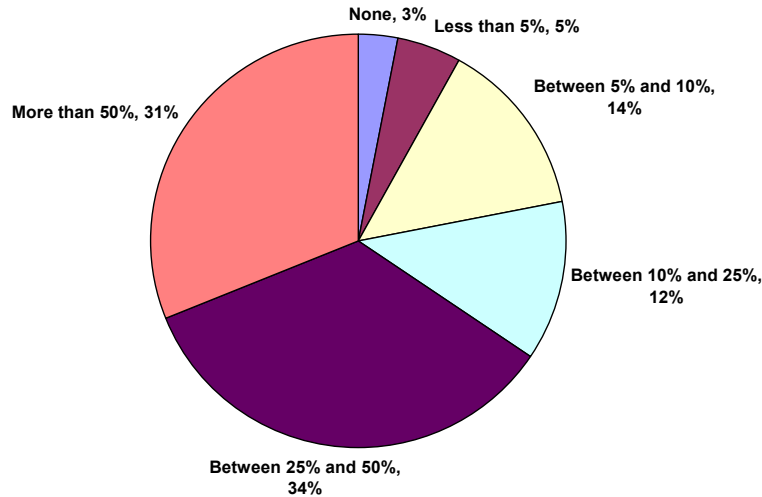
---

<sup>12</sup> The Law Society, Practice Standard Unit, Report on Themed Visits – Referral Fees, July 2006.

<sup>13</sup> ComRes, A survey of public attitudes towards conveyancing services, conducted on behalf of Solicitors Regulation Authority, February 2009.

<sup>14</sup> An electronic survey was conducted of estate agents that were members of National Federation of Property Professionals. This resulted in 179 responses to set of questions regarding the use of conveyancer and referral fees. The survey was conducted during late February and early March 2010.

**Figure 4: What proportion of clients choose the conveyancing service to which you refer them?**



Source: CRA Estate agent survey. Note the figure after the comma represents the proportion of respondents.

Figure 4 shows the responses of estate agents regarding the proportion of their clients who choose the conveyancing service to which the estate agent refers them. Overall we find that 40% of consumers follow the recommendation of the estate agents based on our survey. This figure is also consistent with evidence from a major estate agent provided during interviews which found that around 40% of vendors used the conveyancing service recommended although this figure was lower at around 20% for purchasers.<sup>15</sup> Evidence from the OFT suggests that around 20% of buyers used a conveyancer recommended by the estate agent.<sup>16</sup>

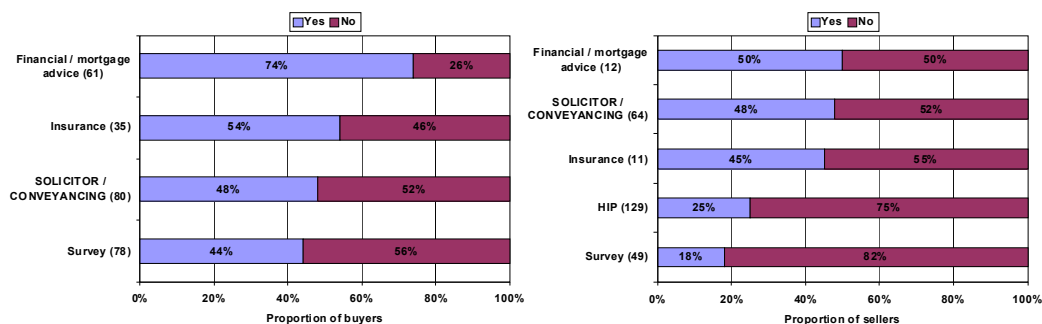
We also find that a significant proportion of consumers shop around for conveyancing services as shown in Figure 5 below.

---

<sup>15</sup> Note that these figures are higher than those found in research for the SRA which identified that 12% of consumers used a conveyancer recommended by an estate agent. Source: ComRes, A survey of public attitudes towards conveyancing services, conducted on behalf of Solicitors Regulation Authority, February 2009.

<sup>16</sup> This is based on 44% of buyers being recommended a conveyancer and 46% taking up the recommendation. Source: OFT, Home buying and selling Market Study, Quantitative Consumer Survey Report, Prepared for the OFT by GfK NOP Social Research, November 2009, OFT 1140.

**Figure 5: Proportion of customers who shop around**



Source: OFT, Home buying and selling: A Market Study, February 2010 OFT 1186.

Figure 5 shows that around 50% of both buyers and sellers shop around for conveyancing services and this level of shopping around compares favourable with shopping around for a structural survey. This level of shopping around is also consistent with the evidence from the interviews undertaken for this project where respondents indicated that a range from 40-60% of consumers were said to shop around.

It is useful to compare this to other parts of the legal services market. For example, research for the LSB found that only 14% of consumers shop around when they choose a lawyer.<sup>17</sup> Hence it is clear that the level of shopping around for conveyancing is considerably greater than the level of shopping around that is observed across legal services more generally.

When choosing a conveyancer, consumers indicated that having a recommendation and being a specialist were the most important factors with “cheapest” the next most important factor.<sup>18</sup>

The importance of price in the choice of conveyancer was also highlighted during interviews. Most interviewees agreed that the estimated level of fees set out by the conveyancer at the beginning of the process was an important element of competition. A number of interviewees indicated that consumers often called a range of conveyancers to ask about the fees to ensure that the conveyancer that they intended to choose was charging a price that was in line with others in the market.<sup>19</sup> Indeed, research finds that when consumers did shop around price was an important factor with 76% asking for different costs from different lawyers.<sup>20</sup>

17 YouGov survey results on behalf of the Legal Services Board, Fieldwork conducted December 2009.

18 It should be noted that these options, along with “being in the same area as property” and “big well known firm” were prompted options with consumers asked to rate their importance. Source: ComRes, A survey of public attitudes towards conveyancing services, conducted on behalf of Solicitors Regulation Authority, February 2009.

19 It is also interesting to note that according to the OFT, 48% of buyers who used a conveyancer recommended by the estate agent investigated other providers before deciding to take up the provider the estate agent had recommended.

20 Although this figure is based on legal services more generally, since customers seeking a conveyancer are found to shop around more than customers seeking other legal services, it seems likely that the basis on which they shop around will more closely reflect those seeking conveyancing services than those seeking other types of legal service. Source: YouGov survey results on behalf of the Legal Services Board, Fieldwork conducted December 2009.

It should be noted that the purchasing process and the role of recommendations was found to vary by different types of customer. For example, the OFT found that first time buyers were more likely to be referred to providers, such as conveyancers, than were experienced buyers. In general these buyers were found to be the least savvy due to their lack of experience and were less equipped to deal with the buying and selling process.<sup>21</sup> This was also noted in research for the SRA which found that younger customers and those who were less experienced appeared to rely more heavily on recommendations by their estate agent.<sup>22</sup>

Turning to the case of re-mortgages, the conveyancer will often be appointed by and on behalf of the new mortgage company rather than by the individual. It is common for mortgage companies to have a small number of conveyancers who are used for re-mortgaging work. In these cases the conveyancer is both appointed and also paid for by the mortgage company. The implication of this is that there are no referral arrangements in place as this relationship operates as a commercial arrangement between the mortgage provider and the conveyancer. As there are no referral fees in place or concerns that they might be used in the future, we do not consider the re-mortgage market further.

## 2.2. Supply of conveyancing services

As described above, although individuals can conduct conveyancing for themselves, it is rare for them to do so. Instead, the great majority of individuals will select a professional adviser who could be either a.

- Solicitor – who is regulated by the Solicitors Regulatory Authority (SRA); or
- Licensed conveyancer – who is regulated by the Council for Licensed Conveyancers (CLC) and which has been allowed since 1985.

According to The Law Society's database, there are 9,078 solicitor firms that conduct conveyancing work of residential properties in England and Wales. According to the CLC's database there are 1,035 licensed conveyancers. It should be noted that The Law Society's figure relates to the number of firms whereas the CLC figure relates to the number of conveyancers and as such the figures are not directly comparable. Interview evidence has suggested that approximately 90% of conveyancing is conducted by solicitors with the remaining 10% conducted by licensed conveyancers.

There do not appear to be any significant systematic differences between licensed conveyancers and solicitors. They are both required to undertake a series of qualifications and have similar rules regarding their behaviour. However, some differences include that:

- Firms of licensed conveyancers are permitted to work for both sides of a property deal provided that this is disclosed, there are no apparent conflicts of interest and there are different individuals working for the different parties;<sup>23</sup> and

---

21 OFT, Home buying and selling: A Market Study, February 2010 OFT 1186 and OFT, Home buying and selling Market Study, Qualitative Consumer Survey Report, Prepared for the OFT by GfK NOP Social Research, September 2009.

22 ComRes, A survey of public attitudes towards conveyancing services, conducted on behalf of Solicitors Regulation Authority, February 2009.

23 CLC, Conduct Rules 2009, Rules 5.1 and 5.2.

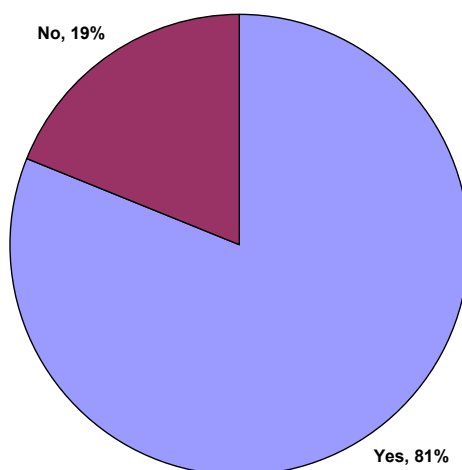
- Prior to 2004, licensed conveyancers were able to pay referral fees while solicitors were only able to do so after 2004.

As well as consumers approaching conveyancers directly, they may also be referred to conveyancers through introducers, the most common of which are estate agents.<sup>24</sup>

### 2.2.1. Estate agents

Evidence from interviews indicated that nearly all estate agents would be expected to have referral arrangements in place regarding conveyancers. Although some of these involve informal arrangements (particularly where local estate agents refer work to local conveyancers), interviewees agreed that over the last ten years, firms have moved towards formalising these arrangements especially through the use of panels. As illustrated in Figure 6 below, the great majority of estate agents employ a panel of conveyancers today.

**Figure 6: Do you have a panel or list of solicitors/conveyancers to whom you refer customers?**



Source: CRA Estate agent survey

The size of the panel varies between estate agents although most estate agents are thought to refer customers only to a small number of different conveyancers. National estate agents, who are more likely to have very formal panels in place, may have changed the number of conveyancers on their panel to match the number of cases that they were referring. For example, some large estate agents who have themselves grown over time have expanded the number of conveyancers over time in order to ensure that there is sufficient capacity available to meet the needs of all of their clients.

Panel members will usually stay on the panel for long periods of time. Indeed, according to our survey of estate agents, only 65% review their panels at least annually. Evidence

---

<sup>24</sup> Alternative introducers could include mortgage brokers or financial advisers but interviewees agreed that estate agents were by far the most common introducer hence we focus only on their role.



from interviews also indicated that it was relatively rare for panel members to change although some estate agents did give examples of removing firms from panels where they the conveyancer could not meet the standards that the estate agent required – the issue of service agreements is covered in section 2.5.2.

The stability of panels could reflect the development of good working relationships between the estate agent and the conveyancer. Indeed, estate agents report good communication as one of the principle advantages of the use of panels.

According to the interviews panel members are chosen on the basis of their ability to meet high levels of service, their ability to integrate technology with that of the estate agents and their capacity to undertake the work – the latter being particularly important for national estate agent chains making national agreements. Based on survey, good communication was the most commonly cited advantage to the estate agent firm when clients use the conveyancers that the estate agent refers them to.

It is also the case that willingness to agree to commercial terms represents an important element of the selection process. Although this varies, this may include panel members agreeing to undertake conveyancing services in line with a particular fee schedule. This includes both how much they will charge for conveyancing as well as their willingness to pay a referral fee.

National conveyancing firms were considered most likely to be willing to pay referral fees and there was no indication from interviews that there were large conveyancing firms that did not pay referral fees. By contrast some smaller, local conveyancing firms indicated that they were unwilling to pay referral fees.

### **2.2.2. Trends in the supply of conveyancing services**

There have been a number of changes in the conveyancing market in recent years which we set out below since these changes affect the way in which competition works in the market.

#### *The use of technology*

Over the last 15 years, the use of technology has had a significant impact on conveyancing with many aspects of the transaction now conducted electronically. In addition, the fact that the great majority of properties are now registered at the Land Registry means that the conveyancing process has become easier over time as some problems associated to the properties would have been resolved at the time that the property was registered. This has meant that conveyancers can now contact the Land Registry online and many of the searches that are undertaken are done using electronic databases.

The increase in technology has enabled the speed of searches to be increased and also the range of searches to increase compared to the recent past. In addition, a number of firms have stressed that there have been significant investments in developing technology driven processes which are used to manage the whole conveyancing process, check that the necessary searches have been conducted and ensure consistency from case to case.

The increased use of technology has also allowed conveyancers to communicate with their customers remotely. In some cases this includes conducting most of the communication with the client by telephone and email rather than face-to-face. It has also enabled some conveyancers to offer “tracking” services for consumers which allow the

client to see where the conveyancing process is up to and what tasks still need to be completed.

Combined, these changes would be expected to have led to a reduction in the cost of the conveyancing process. However, although the ability to undertake searches electronically has improved over the last ten years, it was emphasised to us during the interviews that the assessment and interpretation of the information remains the most an important part of the conveyancing process.

#### *Use of in-house and national conveyancers*

Partly linked to the role of technology, interviewees also report that there has also been a trend towards using in-house conveyancers. However, this term is often used loosely and is applied both to a conveyancing firm on a small panel that works very closely with the estate agent or to a conveyancer within the same commercial group. In some cases estate agents may have both an in-house conveyancing firm that receives a significant amount of referrals with the rest of the referrals going to other firms on the panel.<sup>25</sup> The use of in-house conveyancers is a trend that has been ongoing for some time with, for example, Countrywide, the largest estate agent group, setting up its conveyancing outlet before 2004.

According to interviews, in-house and national conveyancers developed partly as a response to in-house needs and partly due to the scale of the work undertaken for re-mortgaging. For example, mortgage companies were keen to use a small number of firms (or possibly only one firm) to conduct the conveyancing work in the case of re-mortgages. Since this involved large volumes of cases, mortgage companies negotiated competitive rates encouraging automation and efficiency in the process.<sup>26</sup>

These larger conveyancers have a number of characteristics including that they:

- operate remotely and do not have face to face meetings with clients;
- are national and not focused on particular local areas;
- tend to be much more leveraged than small or local conveyancers. For example, a firm may have only five licensed conveyancers out of staff of 200 involved in the conveyancing process; and
- have invested in technology focusing on taking a process driven approach to the conveyancing process.

As the use of in-house and national conveyancers has increased, there has been a trend away from local and small conveyancers. There is limited information available on the extent to which work is conducted by national compared to local conveyancers although some interviewees have suggested that prior to 2004, around 90% of work was conducted by local firms and that this has fallen to around 60 – 70%. The increase in the

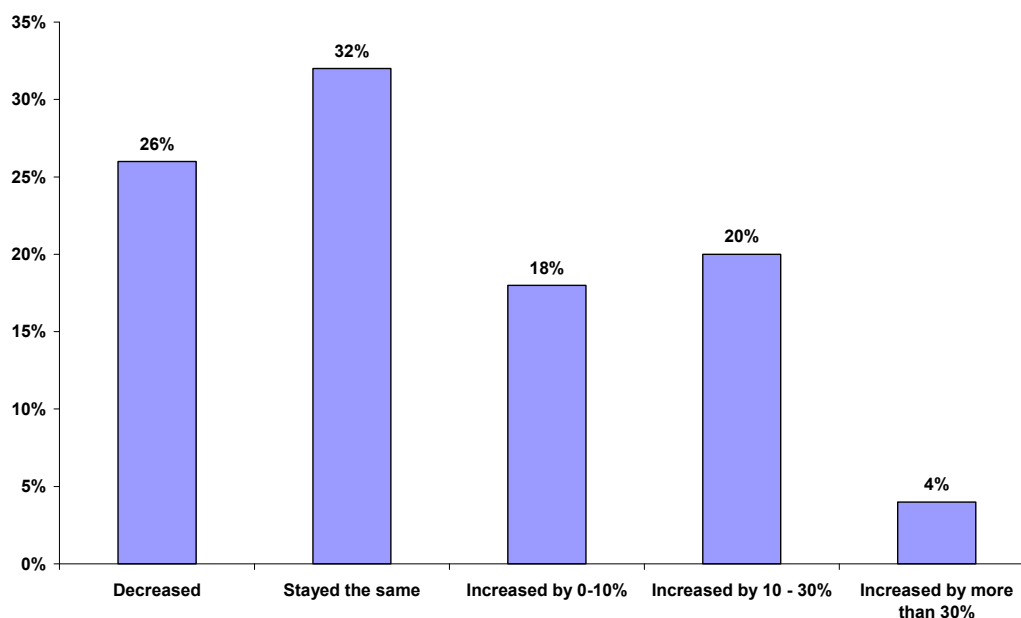
---

25 The extent to which the in-house firm receives relatively more referrals than others on the panel appears to vary between estate agents.

26 The conveyancing fee for re-mortgaging may have been set at an artificially low level as the conveyancer was able to benefit from holding cash during the process and therefore gaining from interest payments. Although this represents a small amount for any given transaction, for high volume work this appears to have represented a considerable revenue flow. With lower interest rates and a lower level of transactions as have been seen during the credit crisis, this particular business model may be under some strain.

use of national firms is consistent with results from our estate agent survey shown in Figure 7.

**Figure 7: Since 2004, has the proportion of conveyancing work in your area which is done by national solicitor/ conveyancer firms...**



Source: CRA Estate agents survey

Overall, 42% of estate agents observed an increase in the use of national conveyancers while only 26% observed a decline in the use of national conveyancers.<sup>27</sup>

### *Home Information Packs*

The introduction of Home Information Packs (HIPs) has also led to significant changes in the market place. According to interviews, prior to the requirement for HIPs, customers (vendors) were more likely to shop around for a conveyancer and would be less likely to accept the conveyancer that the estate agent recommended. However, clients now need to purchase a HIP earlier in the process in order to be able to sell their properties. This has led some estate agents and conveyancers to bundle the sale of HIPs with the conveyancing service. Some conveyancers have sought to market their services through offering the HIP for free when the client uses them for the conveyancing.<sup>28</sup>

## **2.3. Price of conveyancing services**

The price of conveyancing services is set through the usual competitive process that is seen in most markets rather than being prescribed through regulatory intervention. (In

---

<sup>27</sup> The question was also repeated "across the whole market" rather than "in your area". In response to this, 28% thought national firms had decreased while 48% thought they had increased (27% thought they had increased by 10-30%).

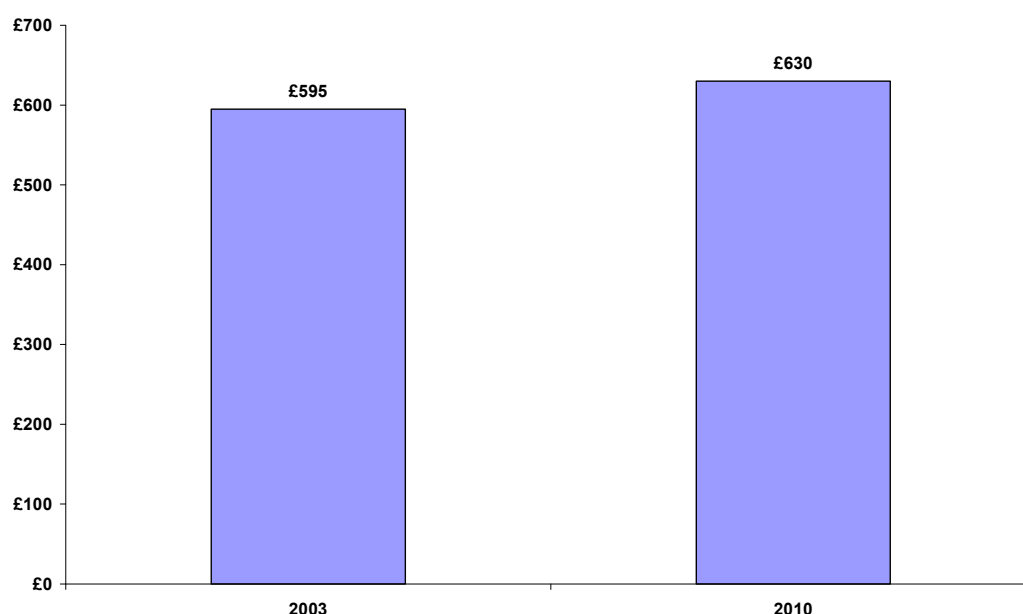
<sup>28</sup> It has been alleged that some clients simply sign a contract unaware that they are entering into an agreement relating to the conveyancing service. However, there is only anecdotal evidence to support this and we do not consider this further.

this way conveyancing is different to the other two markets considered in this report where the price of legal services is prescribed.)

Interview evidence has consistently stated that average conveyancing fees have remained roughly constant in nominal terms (and fallen in real terms) since 2004. Interviewees have indicated that the reason for this is that the conveyancing market is competitive with consumers shopping around, including on the basis of price, as noted in section 2.1. Some conveyancing firms have also started to compete along the lines of “no move, no fee” which has the effect of reducing the price of conveyancing for customers who do not end up moving for some reason.<sup>29</sup>

The conveyancing fee typically varies depending on the value of the property, with higher valued properties leading to higher valued conveyancing fees – fees might increase by around £50 for every £50,000-100,000 increase in the value of the property. Figure 8 below sets out the average conveyancing fee for a property valued at £200,000.

**Figure 8: The average conveyancing fee for a property valued at £200,000**



Source: Woolwich Cost of moving survey and CRA Estate agents survey

As can be seen from Figure 8, the evidence from our survey identifies an average conveyancing fee which has remained roughly constant since 2003. This is consistent with the interview evidence.

In addition to the main conveyancing fees, some firms will also charge additional fees for issues such as where a mortgage needs to be moved, where the property is leasehold rather than freehold and for additional searches that may be required.<sup>30</sup>

---

<sup>29</sup> Interviewees have acknowledged that very little of the conveyancing process would be conducted in advance of offers to purchase being accepted and therefore relatively little cost would have been incurred by the conveyancer at this stage.

<sup>30</sup> We note that in as far as conveyancers may have an incentive to conduct additional activities in order to generate additional fees, this is an incentive which is in place irrespective of whether referral fees are paid.

## **2.4. Role of referral fees in competition for conveyancing**

In this section we consider whether referral fees are affecting competition in the conveyancing market. We focus in this section on whether referral fees have any effect. Section 2.5 then considers whether this causes any detriment to consumers.

Before considering the current market it is useful to set out the position before 2004.

### **2.4.1. Pre 2004**

Prior to 2004, the use of referral fees depended on the type of conveyancers:

- solicitors were not able to pay referral fees to estate agents;
- national conveyancers were able to pay referral fees.

However, even though solicitors were banned from paying referral fees there is general agreement that informal referral arrangements were common. In particular, non-monetary benefits such as hiring football match boxes, entertainment, restaurant meals and cases of wine were seen as common. Interviewees indicated that other arrangements were in place such as solicitors providing free legal services to individuals who managed estate agents in return for obtaining referrals. Some interviewees also suggested that monetary arrangements also arose even though referral fees were banned.

It should be noted that even before 2004 there was a desire to centralise referral arrangements and move towards using more formal panel arrangements. This trend was seen especially among national estate agents who wanted to set out referral arrangements at a centralised level rather than leaving this (and any benefits from it) to the discretion of local managers.

### **2.4.2. Competition over introducers has led to an increase in referral fees**

In 2004, solicitors were allowed to pay referral fees. According to interviews the impact of this was to convert complex arrangements that had been used to pay de facto "referral fees", such as marketing fees or membership fees, into a referral fee that was now legitimate under regulation.

There is no data source available that reports how referral fees have changed since 2004, but interview evidence is consistent that they have increased. According to evidence from interviews, referral fees were around £50 - £100 in 2004 and are around £250 - £400 today.<sup>31</sup> The OFT reports that the typical referral fee is around £250-300.<sup>32</sup>

The increase in the referral fee over time is believed to reflect increased competition by conveyancers for referral work and the passing on of cost reductions which have arisen due to technological change. No interviewee suggested that there had been any significant changes in the services provided by estate agents that would have led them to receive an increase in the referral fee.

The level of referral fees varies depending on the particular estate agents. Indeed, the OFT reports that 28% of estate agents receive referral fees of £100-149 while 38%

---

<sup>31</sup> Some interviewees suggested that the financial crisis and reduction in property transactions has led to referral fees stagnating or in some cases declining although it was anticipated that they would return to previous levels when the housing market fully recovers.

<sup>32</sup> OFT, Home buying and selling: A Market Study, February 2010 OFT 1186, p128.

receive fees of £250-299.<sup>33</sup> There is a small amount of evidence suggesting that the referral fee in some arrangements may vary according to the value of the property.

There was no evidence from interviews that the variation in the level of the referral fee reflected reward for part of the conveyancing service being conducted by estate agents rather than conveyancers (unlike with personal injury cases – see section 4.4.3). However, variation in the level of the referral fee is consistent with evidence from our interviews where it appears to be the case that referral fees are lower where local estate agents refer clients to local conveyancers than where arrangements are made between national firms. This variation may reflect a combination of factors such as economies of scale and the relative bargaining power of the estate agent compared to the conveyancer.

#### **2.4.3. Choice of conveyancer determined by estate agents**

As noted in section 2.2, estate agents have increasingly moved towards formalising their referral arrangements through the use of panels. The willingness of conveyancers to pay a referral fee is typically part of the selection process to get onto these panels.

In addition, we also find from our estate agent survey that even where referral fees are not in place today, other forms of referral arrangements are commonly in place. For example, it was particularly frequent for estate agents to indicate that referrals would work in both directions with solicitors referring clients to the estate agent in return for estate agents referring work to the solicitor. This was especially the case for probate or in the case of the need for a valuation in a matrimonial dispute. As well as mutual referrals, many of the informal referral arrangements such as offering hospitality which were observed before 2004 remained common today.

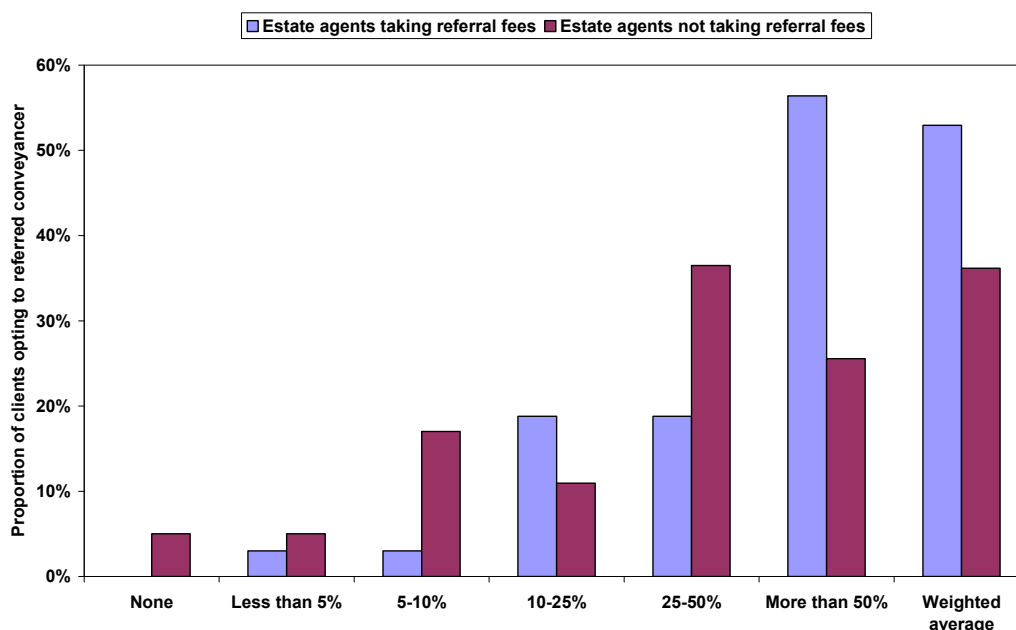
It is clear from the evidence in section 2.4.2 above that referral fees have increased and we would expect this to give estate agents an increased incentive to refer clients to conveyancers. As shown in Figure 9 below, we also find from our estate agent survey that where referral fees are involved, customers appear more likely to follow the recommendation of the estate agent.<sup>34</sup>

---

<sup>33</sup> OFT, Home Buying and Selling Market Study – Survey of estate agents, February 2010. This is based on respondents by estate agents regarding the average amounts received for a transaction on a £200,000 property.

<sup>34</sup> This in itself does not provide evidence that referral fees are detrimental. Indeed, consumers could benefit from referral and may prefer the advantages of a one-stop shop. The OFT report did not find evidence that recommendation represented a hard sell to the consumers. In their survey 82% of consumers reported that the recommendation did not represent a “hard sell”.

**Figure 9: Customers following the recommendation of the estate agent**



Source: CRA Estate agents survey

It is clear from Figure 9 above that estate agents with referral fees are more likely to see clients following the referral which the estate agent makes. This makes sense since the presence of referral fees give estate agents the incentive to seek to refer as many customers as they can to the particular conveyancer.

National conveyancing firms are thought to be particularly willing to pay referral fees while some smaller, local conveyancing firms do not pay referral fees. Furthermore, during interviews a number of small conveyancing firms who did not pay referral fees indicated that they had lost business with estate agents preferring to refer clients to conveyancers who would be willing to pay such fees. Although there are a number of reasons which have driven to trend towards national conveyancers (including technology), interviewees agreed that referral fees played a role in the trend.

The combined effects of these results suggests that the proportion of customers who are referred to conveyancers where a referral fee is paid is likely to have increased over time.

#### **2.4.4. Impact of referral fees on the quantity of conveyancing**

Since conveyancing services are used in the context of property purchases or re-mortgaging it is clear that there is a derived demand for these services. It is possible that the overall price of conveyancing may influence the decision by consumers to seek professional advice for the process rather than conducting the conveyancing process themselves. However, there is no evidence that the level of referral fees is affecting this decision and no interviewees indicated that this was likely. As such there is no evidence that referral fees impact the quantity of conveyancing services demanded.

#### **2.4.5. Summary of the impact of referral fees on competition**

Table 2 below sets out the summary of the impact of referral fees on competition for conveyancing services.

**Table 2: Summary of the role of referral fees in competition for conveyancing**

Issue	Evidence and causation
Competition leading to an increase in referral fees	<p>Strong evidence that referral fees on panels have increased over time.</p> <p>Willingness to pay referral fees is part of panel selection.</p>
Choice of conveyancer determined by estate agents based on referral fees	<p>Competition on referral fees have contributed to trend towards panels and nationals, and away from local firms.</p> <p>Evidence of a movement towards panels before 2004 with changes in 2004 making arrangements more explicit and less complex.</p> <p>Conveyancers who do not pay referral fees often have other arrangements in place.</p>
Referral fees impacting quantity of conveyancing	<p>Conveyancing is a derived demand in the context of property transactions and re-mortgages. No evidence that referral fees impact the decision to conduct own conveyancing compared to seeking professional advice.</p>

Source: CRA

## 2.5. Market failure and potential detriment arising from referral fees

Having identified in section 2.4 that referral fees impact the way in which competition works, in this section we consider, if this is a cause for concern. There are two main ways in which consumer detriment could arise including that referral fees could:

- Result in higher conveyancing fees as estate agents recommend the conveyancer who can pay them the highest referral fee rather than the conveyancer who offers best value for the client; or
- Reduce the quality of conveyancing services as estate agents recommend the conveyancer who is willing to pay the highest referral fee without regard for the quality of the service they offer;

We consider each of these in turn.

### 2.5.1. The impact of referral fees on price

The increase in referral fees which has resulted from competition between conveyancers to be selected on estate agent panels could result in these higher referral fees being passed directly to consumers in the form of an increase in the conveyancing fee.

As noted in section 2.3, the conveyancing fee has remained broadly flat since 2003 despite the fact that referral fees themselves have increased from £50 - £100 to £250 - £400 today.<sup>35</sup> It appears as though this reflects two elements:

- Conveyancing has become less profitable for conveyancers over time. Although we have no quantitative evidence that conveyancing was highlight profitable in the past,

<sup>35</sup> It is not possible to conclude that the £630 average conveyancing fee found in our survey is statistically different to the £595 found in the Woolwich survey. Furthermore we note that even if the average price has increased by £35, referral fees have increased by considerably more than this hence the reasoning described in this section remains relevant.



evidence from interviews supports the contention that profitability of this area of work has reduced. Many interviewees agreed that referral fees have had the effect of transferring profit from conveyancers to estate agents.

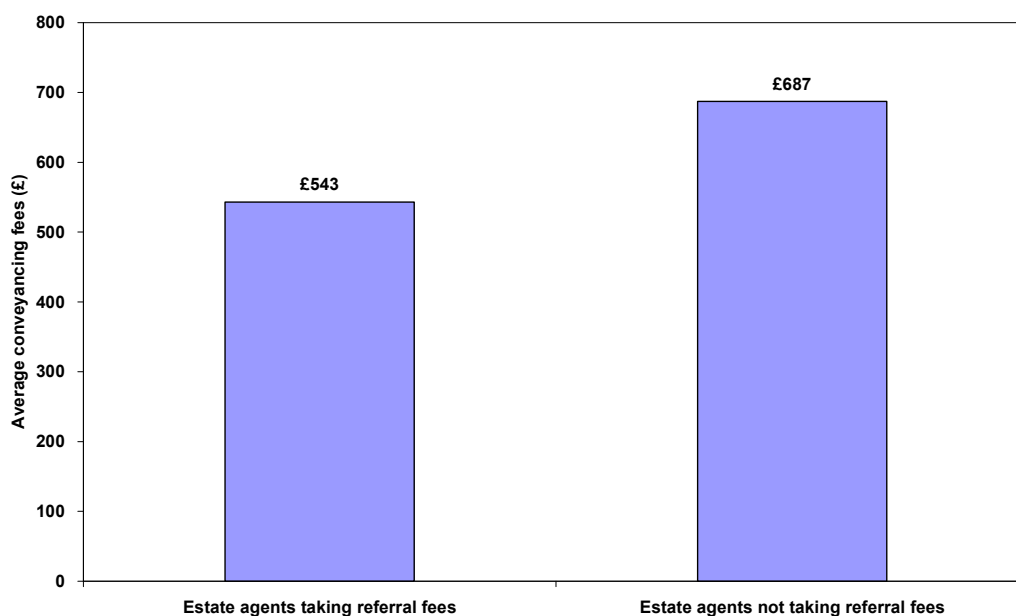
- Conveyancing has become more efficient over time with conveyancers able to afford a higher referral fee due to cost efficiencies arising from new technology and more efficient business models.

The combined effect of these two elements has meant that consumers have paid the same level of total conveyancing fees while conveyancers themselves have kept less of the money and estate agents have gained through higher referral fees. Whether higher referral fees have resulted in greater profitability for estate agents or whether competition in estate agent services has resulted lower estate agent fees or better service is unclear.

It should be noted that interviewees were consistent in stating that conveyancing fees had remained broadly flat throughout the period in which referral fees have been allowed for solicitors. As such this result does not appear to be linked to the credit crisis and associated impact on the housing market although the latter has clearly led to substantial changes in the quantity of conveyancing undertaken.

Although the price for consumers has not increased, it is possible that conveyancing fees could have fallen but that the increase in referral fees has prevented a reduction in conveyancing fees. In order to consider this we examine the typical conveyancing charge for those who do pay referral fees and the typical conveyancing charge for those who do not pay referral fees which is shown in Figure 10 below.

**Figure 10: Typical conveyancing fee for a property valued at £200,000**



Source: CRA Estate agents survey

Figure 10 above shows that the conveyancing fee paid by customers of estate agents who do not take referral fees is actually higher than the conveyancing fee paid by customers of estate agents who do take referral fees.

This is also consistent with our survey finding that estate agents believed that one of the advantages for customers of using the conveyancer that the estate agent referred them to

was the cost. Indeed around 50% of estate agents who believed that there were advantages to using national conveyancers stated that cost was the advantage.

Interview evidence has indicated that one of the key advantages of referral fees is that this facilitated investment in technology. Through being on panels and paying referral fees conveyancers could be confident that they would receive large volumes of business which in turn gave them sufficient certainty to be willing to make investment in technology. These investments in technology then led to cost efficiencies as the conveyancing process could be conducted more efficiently. One of the implications of this is that it is not clear that conveyancing fees that have remained roughly constant over time would have resulted in the absence of referral fees. That is, in the absence of referral fees (or arrangements which replicate referral fees) we might not have observed increased the increased technology which has reduced the cost of conveyancing over time.

A small number of conveyancers who paid referral fees did state that they would charge customers who came direct a lower price than those who came via a referral although they broadly supported the contention that national firms who paid referral fees, because they had invested in technology, were able to charge lower prices for conveyancing than other firms.

There is therefore no evidence that referral fees lead to consumers paying more for conveyancing than would otherwise be the case.

As well as reducing costs through encouraging investment in technology, referral fees have also led to a transfer of money to estate agents. The effect of this could be passed onto consumers through lower prices or higher quality services in the estate agent market.<sup>36</sup>

### 2.5.2. The impact of referral fees on quality

The existence of referral fees introduces potential concerns that competition occurs in a way that gives rise to a reduction in the quality of the conveyancing service that the consumer receives.

Regulation is in place for both solicitors and licensed conveyancers regarding their conduct and requiring them both to act in the interests of their clients. For example:

- One of the core duties of solicitors is to act in the best interests of their client as noted in Rule 1.04 of the Solicitors' Code of Conduct;<sup>37</sup> and
- Under the CLC's Conduct Rules, licensed conveyancers must "at all times keep paramount the interests of the Client except as required by law or by the Council's Rules".<sup>38</sup>

We also note that conveyancers would be legally liable for any wrong advice and that this would be expected to act as a constraint on their actions. However, despite these

---

<sup>36</sup> We note that the OFT has stated that price competition between estate agents is weak but that new business models may put pressure on the traditional estate agent model. OFT, Home Buying and Selling Market Study – Survey of estate agents, February 2010.

<sup>37</sup> Rule 1.04, Solicitors' Code of Conduct 2007.

<sup>38</sup> CLC, Conduct Rules 2009, Rules 5.1.1.

regulatory requirements, some interviewees have nonetheless raised potential concerns about the impact of referral fees on quality.

First, it is possible that the conveyancer acts in a way that is in the interests of the estate agent rather than in the interests of the consumer. For example, estate agents may be keen for transactions to go through to completion (since that is when they will get paid) while those purchasing a property may have a greater interest in investigating any potential concerns which arise during the conveyancing process such as the risk of flooding or any concerns about the title of the land.<sup>39</sup> It is worth noting that the incentive for the conveyancer to act in this way is created by the long-term relationship between the estate agent and the conveyancer rather than by referral fees i.e. this incentive would exist even if the conveyancer received referrals where no referral fee was paid.

Second, some interviewees who were opposed to the use of referral fees argued that referral fees have the effect of reducing the quality of the conveyancing service. They argue that higher referral fees leave less money for the conveyancer.<sup>40</sup> In turn it is argued that this leads the conveyancer to seek to obtain more cases and spend less time per case in order to maintain the same level of income. It is then argued that spending less time per case leads to a reduction in quality.

Third, it is possible that referral fees may lead estate agents to recommend that the seller accept an offer from a purchaser who intends to use the referred conveyancer rather than an offer from a purchaser who does not intend to use the referred conveyancer. We note that the OFT has considered this issue in their recent report and the OFT found no evidence that this was occurring in practice.<sup>41</sup> During the course of our research we have not found evidence that this occurs in practice and we therefore we do not consider this issue further.

#### *Dimensions of quality*

It is important to understand the dimensions of quality which are of importance in respect of the conveyancing process and there appear to be three main areas:

- Issues to do with the title of the property including the searches that need to be undertaken;
- Ability to co-ordinate the exchange and completion of the transaction including the use of non-qualified staff and the time taken to complete the transaction; and
- Issues to do with the service levels offered by suppliers including complaints and overall service levels.

We consider each of these in turn in order to establish the details of the issue, the seriousness in terms of the level of consumer detriment that could be suffered if the particular dimension of quality is eroded and finally whether or not there is evidence to

---

39 We note that there will be a range of other areas where the interests of the estate agent and the interests of the consumer will be the same such as preferring a faster conveyancing process to a shorter process. It is also the case that conflicts of interest related to conveyancing are likely to arise between the estate agent and the purchaser rather than between the estate agent and the seller of the property.

40 It is notable that implicit in this statement is the fact that the price for conveyancing has remained constant and therefore any increase in referral fee means a reduction in the fees kept by conveyancers.

41 The OFT does recommend that this situation is monitored over time.

suggest that referral fees are having the effect of reducing quality. Since national conveyancing firms are more likely to pay referral fees than other firms we give particular consideration to whether there is evidence that national conveyancers are offering a lower quality service compared to local conveyancers who are less likely to pay referral fees. We also note whether other participants in the mortgage process play any role in ensuring that quality is maintained.

#### *Title of the property*

When purchasing a property it is important that the purchaser is paying for what they think they are buying. In particular it is important that the purchaser receives “marketable title” which involves checking that the person selling the property is the current owner of it and has the right to sell the property, as well as checking that there is nothing that would prevent the right to sell the property at a later date. For example, this would include:

- ensure that the buyer actually secures title to the land;
- checking that the buyer has rights of way to access the land; and
- making certain that the purchaser is aware of any restrictive covenants that would limit the use of the property.

Since the title of the property is what individuals are actually purchasing, and given that property purchases often represent one of the most significant purchasing decisions that individuals make, ensuring that individuals have the correct title is considered to be the most important element of the conveyancing process. If this part of the conveyancing service is of poor quality, the detriment to the consumer could be very substantial.

Consumers are in a weak position to assess the quality of conveyancing in respect of assessing whether they are receiving marketable title. It is likely therefore that consumers will only find out whether the work has been done properly when they later try to sell the property. Since this is likely to be some years later, the reputational risk for the estate agent from recommending the conveyancer is likely to be limited.

If the existence of referral fees were to affect quality in this way, this would be a potential significant cause of concern. However, in practice this does not appear to arise:

- It was noted by most interviewees that conveyancing was facilitated through the presence of the Land Registry. Most properties are already registered and difficulties associated with title are thought likely to have been sorted out at the time that the land was registered. In addition, the presence of the Land Registry enables relatively straightforward checking of the ownership of the land.
- Although concerns were expressed in interviews regarding the qualification of the staff used in national firms (discussed further below) this was not thought to affect the ultimate assessment. Interviewees suggested this could lead to a slower process (also discussed further below), but there was general agreement that ultimately the regulated conveyancer would “sign-off” the transaction thereby limiting concerns.
- The professional standards of the regulated conveyancer and ultimately the financial liability arising due to the seriousness of wrong advice related to the title were seen as a constraint on detriment arising from quality in this fashion.
- There is no evidence from complaints data that concerns of this kind are common or in any way associated to the use of referral fees (discussed again below).

### *Conduct of searches*

A number of conveyancers argued that there was a qualitative advantage to customers from their conveyancer being local to the area in which the property was located rather than being located elsewhere when considering the searches that need to be undertaken for a particular property.<sup>42</sup> Since referral fees were identified as leading estate agents to use national firms which have operations centralised in a small number of locations around the country, this trend could lead to a reduction in quality due to the searches which are conducted.

Some of the areas mentioned by interviewees where local knowledge was considered important, included flood risk, complex “local” leasehold terms and issues such as whether the area was used for coal-mining.

It should be noted that although these examples were highlighted, interviewees did not provide any actual evidence that national conveyancers had failed to identify these as concerns when operating from a distance. Furthermore, national conveyancers indicated that they would conduct searches by postcode that would identify whether an area was likely to suffer from some of these risks. The existence of search companies with databases containing this information supported their ability to do this without physically being in the locality of the property.

It was suggested by a small number of local conveyancers that being local may mean that they know about issues which are common to a particular estate or particular block of flats. However, where these examples were given this seemed to relate to repeat business of a very specific nature (rather than a local firm advantage per se). This may enable a local conveyancer to conduct subsequent business faster but there was no evidence that any benefit of this was passed on to consumers in the form of lower prices.

Finally, it should be noted that a number of conveyancers who consider themselves to be local conveyancers stated that they would commonly conduct conveyancing services for long-term clients who were moving to different parts of the country. They stated that clients who were satisfied with the service that they had provided in the past would use them again for any conveyancing needs regardless of the location of the property. No interviewee in this position indicated that the quality of their service in these cases was reduced due to not being local to the property which was being purchased or that they would have concerns undertaking the work.

We therefore conclude that there is no evidence that national conveyancers who pay referral fees conduct lower quality searches compared to local conveyancers.

### *Non-qualified staff and co-ordination of exchange and completion*

A number of interviewees noted that national conveyancers tend to be staffed with a large number of non-qualified staff and a small number of licensed conveyancers or solicitors. Data does not appear to exist on the typical ratios of qualified to unqualified staff hence it is not possible to monitor whether there has been a change in this over time although no interviewee disagreed with the statement. Further, since the use of national conveyancers has increased over time (which is linked to referral fees), the use of non-qualified staff is believed to have also increased.

---

<sup>42</sup> No interviewee suggested that it was important to visit properties for the purpose of conveyancing.

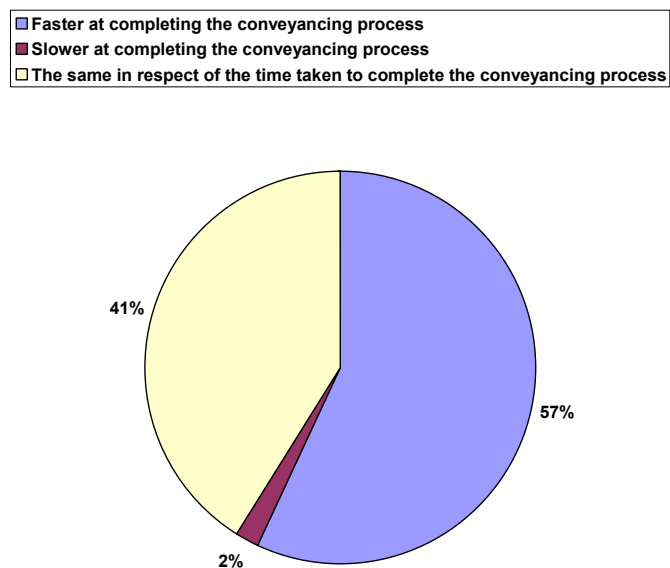
One concern that flowed from this related to the ability to co-ordinate the exchange and completion of contracts. It was noted by some interviewees (and not contradicted by any interviewees) that these elements of the process are not about the actual technicalities of legal advice but rather relate more to process requirements and the ability to administer and co-ordinate activities. As such it was acknowledged that these elements did not require particular legal training in order for them to be conducted to a high standard. Nonetheless, the speed and efficiency of this process was considered to be an important element impacting the quality of the process.

Interview evidence provided conflicting view on whether national conveyancers (who are more likely to use referral fees) offer a different level of service to local conveyancers:

- National conveyancers have a team of staff enabling them to offer continuity of service independent of individuals being away from the office or required for other activities. The system used to monitor the process allows managers to identify where a delay is taking place and the process itself makes the requirements of the conveyancer more predictable.
- Local conveyancers use a less process driven approach to conveyancing which enables them to undertake activities in parallel rather than in series. They also note that repeated interaction with other local conveyancers in the area (who may be working for the other party in the transaction) aids communication and efficiency.

It seems likely that arguments from both national and local conveyancers have merit and to assess the relative impact we asked estate agents who received referral fees to compare the time to complete transactions of those firms that paid them a referral fee compared to those who did not pay them a referral fee. Figure 11 below shows that only 2% of estate agents who accept referral fees believed conveyancers paying referral fees were slower than conveyancers who did not pay referral fees.

**Figure 11: The average time to complete for conveyancers who pay a referral fee compared to those who do not pay a referral fee**



Source: CRA Estate agents survey

It should be noted that this is considered only a weak measure of the efficiency of firms who do or do not pay referral fees. For example, different conveyancers will be advising both parties to the transaction and it is not always clear which firm is responsible for any delays. In addition, there is often a chain of property transactions and hence completion will depend on the slowest link in the chain. Despite the relatively weak measure, Figure 11 above does not provide evidence to support the allegation that conveyancers paying referral fees are usually slower than those who do not pay referral fees (indeed quite the opposite). This is consistent with other results from our estate agent survey which identified that key advantages of referral arrangements for the estate agent were improved communication and faster completion.

#### *Non qualified staff and dealing with complexities*

Conveyancers who object to the use of referral fees suggested that national conveyancers who use technology-driven processes and less qualified staff were capable of dealing with straightforward cases but were less equipped at dealing with more complex cases.

It should first be noted that those making this argument acknowledge that around 90-95% of cases would be categorised as straightforward. This alone indicates that any detriment from this source will be limited.

As already indicated, national conveyancers use process driven systems that allow unqualified conveyancers to conduct a significant amount of the process. The process itself is designed to ensure that all of the necessary steps that are required are conducted and will highlight if there are problems or complexities. Firms using a large amount of technology are also understood to have systems in place that make sure that any complexities are escalated to be dealt with by more qualified members of staff. Further, interviewees who raised this concern usually concluded that the main implication of complexity was to delay the process (presumably as other members of staff became involved).<sup>43</sup> Finally, we note that ultimately a regulated conveyancer will provide the sign-off of the work, taking responsibility for the process and the quality of the service.

#### *Face to face service*

Conveyancers who object to referral fees argue that local conveyancers can provide a higher quality face to face service than national conveyancers who deal remotely with their clients. There were three elements which were raised in this regard.

First, money laundering and identity checks were noted as easy to perform in a face to face environment since individuals can bring proof of identity such as their passport to a local conveyancer's office. We note that there is no evidence that money laundering checks being conducted in an inappropriate manner by national conveyancers.

Second, local conveyancers argued that being local meant that customers had the option of meeting the conveyancer in person which was not an option to those customers who used national conveyancers. Interviewees broadly agreed that there might be a group of customers for whom this would be important – especially those from an older generation who were used to face to face communication. However, interviewees also acknowledged

---

<sup>43</sup> We note that this is possible that national conveyancers are faster on straightforward cases compared to local conveyancers as indicated in Figure 11, but slower on complex cases. Data is not available at this level of detail.

that many customers were happy to communicate by phone or email and that this group of customers was likely to increase over time.

Third, it was suggested that national conveyancers did not always maintain continuity of staffing for a particular case so that clients may end up speaking to multiple different people rather than always speaking with the same individual. Those who object to referral fees state that this represents a worse service for customers. As discussed above, national conveyancers argue that this enables them to ensure that customers always have someone that they can speak with about their case and that communication with the client can be undertaken more rapidly than would occur when dealing with smaller firms who inevitably could not guarantee always having someone available to answer phone calls or emails. They also note that this enables them to have longer opening hours than smaller firms.

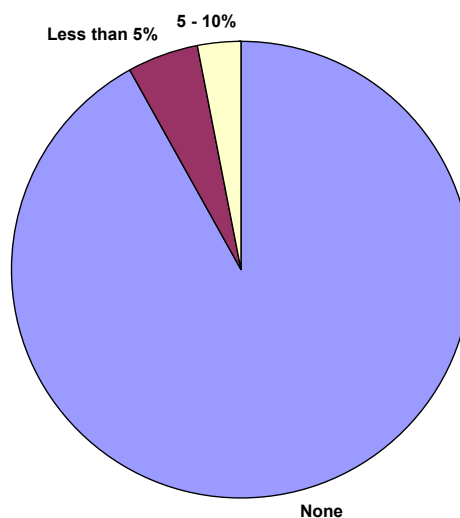
It is clear that national conveyancers and local conveyancers offer a slightly different service to their respective customers in terms of the mode of communication with them and the continuity of dealing with a particular individual. Based on the interviews conducted, it does not seem correct to state that services that are provided remotely are of lower quality than those provided face to face. However, there is likely to be a group of consumers who prefer face to face services to those provided remotely and these consumers are likely to prefer the option to use a local conveyancer.

### *Complaints*

Complaints are another potential measure of quality. If conveyancers paying referral fees offered lower quality to customers we would expect them to receive a higher proportion of complaints.

First, we consider the number of estate agents who have received queries or complaints regarding referral fees. The chart only relates to estate agents who receive referral fees.

**Figure 12: Queries or complaints regarding referral fees**



Source: CRA Estate agents survey

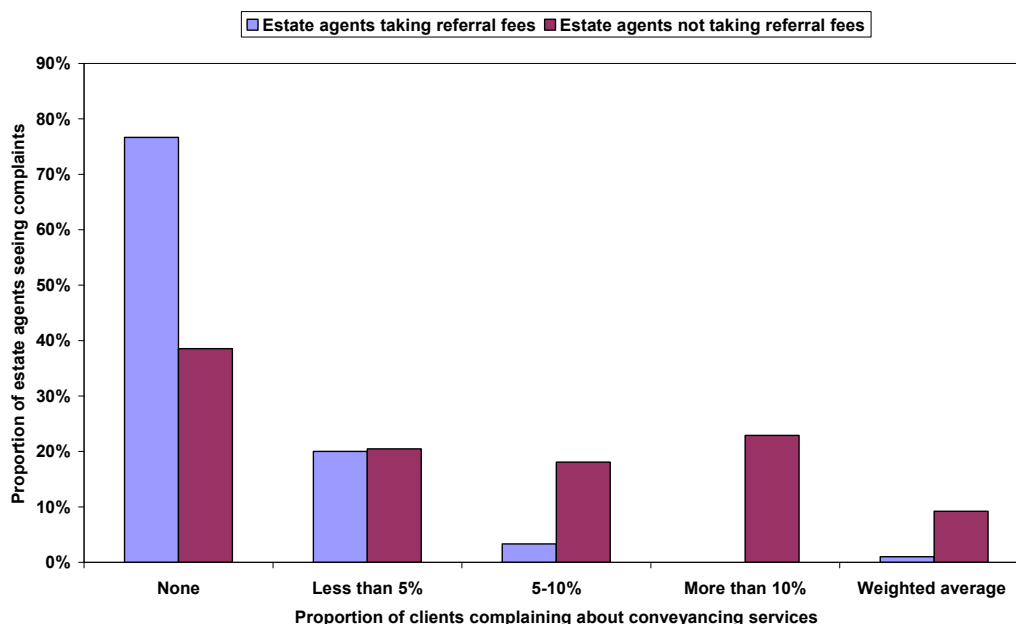


Of those who receive referral fees we find that 92% of estate agents had not received any complaints or queries directly about referral fees in the last year indicating that only a small number of estate agents had received queries or complaints.<sup>44</sup>

Evidence from the Legal Complaints Service also finds that there are few complaints regarding referral fees or fee sharing with only 12 such complaints over a ten year period.<sup>45</sup>

Second, we consider complaints regarding the conveyancing service itself. This is more likely to focus on service measures (such as communication and responsiveness) than the quality of the title (where issues may only be uncovered at a much later date). Figure 13 shows the proportion of customers making complaints regarding conveyancers for estate agents taking referral fees compared to estate agents who do not take referral fees.

**Figure 13: Complaints regarding the quality of the conveyancing service**



Source: CRA Estate agents survey

As shown in Figure 13, estate agents who are paid referral fees from conveyancers are receiving fewer complaints than those who do not receive referral fees.<sup>46</sup> This does not provide evidence of a concern about quality.

---

<sup>44</sup> Although small, this appears to be higher than for personal injury cases although we do not have directly comparable data on this. It is not clear whether the relatively higher figure results from including queries in the question (which may be resolved and not turn into concerns about referral fees), whether it results from greater transparency in disclosure for referral fees in conveyancing compared to personal injury cases or whether it reflects greater interest in referral arrangements where customers pay a conveyancing fee set through market forces in contrast to set legal costs in personal injury which claimants do not need to pay under no-win-no-fee.

<sup>45</sup> Data provided by the Legal Complaints Service to CRA.

### *Service level agreements*

As noted in section 2.2.1, panels of conveyancers are commonly used by estate agents. Alongside some of these panels are service level agreements or standards which are set out. These agreements will typically cover a range of requirements, especially those focused on communication standards, speed of response and monitoring customer feedback. For example, conveyancers may be required to meet particular time commitments, such as being able to “package the deal within 48 hours” after the deal is agreed.

The use of formal service level agreements is relatively rare with only 12% of estate agents stating that they have them in place, although this figure increases to 39% among those who receive referral fees. Interview evidence suggests that national estate agent firms that will commonly have these agreements in place with national conveyancing firms (where referral fees are used). It is less common to have formal service level agreements in place between local firms (where formal panel arrangements are also less common).

### *Overall service levels*

Finally, there are direct measures of customer satisfaction regarding the conveyancing services they receive. Evidence from interviews has identified that large estate agents require their national conveyancers to provide feedback on customers satisfaction as part of the service level agreement. Confidential evidence from a major estate agent provided to CRA for the purposes of this project shows very high level of satisfaction of well over 90% (based on internal survey evidence). These satisfaction levels have been maintained at high levels over the years when referral fees have been increasing.

This survey evidence has also finds that over the last three years:

- over 90% of customers stated that their performance was better than different legal representatives they have used before;
- over 90% of customers would use them again; and
- over 90% stated that they were value for money.

It is also interesting to note that estate agents require the conveyancer to undertake surveys of this kind. Conducting such surveys is inconsistent with the accusation that estate agents are only interested in referral fees. Instead it supports the views that estate agents are choosing conveyancers on the basis of quality, as well as issues to do with fees (both the conveyancing fee and the referral fee).

Small conveyancers are less likely to undertake surveys of this kind. It is therefore not possible to directly compare satisfaction levels across different types of conveyancer.

Evidence from the OFT also finds that there is a high level of customer satisfaction regarding conveyancing. They find that 92% of consumers describing themselves as

---

46 It is possible that estate agents responding to the survey have sought to “game” the survey with those taking referral fees suggesting that the conveyancing service is better than it actually is. It should be noted that there were relatively few questions which made direct reference to referral fees in the question itself and instead a number of charts have shown comparisons between responses based on a tabulation of responses to different questions.

either very (68%) or fairly (24%) satisfied with their conveyancer with only 8% describing themselves as dissatisfied.<sup>47</sup>

Overall there is therefore no evidence that national conveyancers who use referral fees offer a lower quality of service than local conveyancers or that there have been concerning reductions in the customer's view of overall level of services due to referral fees.

#### *Quality assurance by mortgage providers*

Even if quality was a concern, it is important to consider whether the lender (involved in the provision of a mortgage to the purchaser) provides any quality assurance of the conveyancing process. This is plausible since, if the borrower has difficulties repaying the mortgage then the lender might be expected to be concerned about whether they will be able to recover their money through the repossession and sale of the property. In practice, mortgage providers have made it clear that they offer little quality assurance of the conveyancing process.

While their incentives are broadly aligned with the customer, it is clear that mortgage providers consider that the frequency with which they are likely to face detriment from poor conveyancing is sufficiently small for it not to be worthwhile investing in a process of checking of the quality of the service. Their primary concern is to ensure that their mortgage charge is appropriately registered on the property such that if there is a repossession they will be protected. Mortgage providers agree that 95% of cases are straightforward and the likelihood of any problems is small.

Even at present during poor economic conditions, the number of repossessions is still very small at around 43,000 a year compared to typical mortgage approvals of over 3 million.<sup>48</sup> In addition, if the property is repossessed, mortgage providers only suffer if the value of the property is insufficient to repay the outstanding mortgage. Furthermore, in the event of there being a problem, lenders would be able to make a claim on the conveyancer. Hence the infrequency with which mortgage providers suffer detriment means that they do not consider it worthwhile to undertake any quality assurance role.

It should be noted that mortgage providers do generally maintain a list which conveyancers need to be on if the mortgage provider is to be willing to offer transfer funds through them. In practice this list is very wide and reflects the vast majority of conveyancers active in a given market, although some lenders are reluctant to work with sole practitioners because of concerns about fraud.

Fraud may arise when conveyancers receive the money from the purchaser's lender but do not then pass it on to the seller's conveyancer and instead "disappear" with the proceeds. Some conveyancers may seek to arrange a number of completions at the same time in order to maximise the amount of money that they steal.

There is no evidence that firms which pay referral fees (typically larger firms) are more likely to conduct fraud than others. Instead, the increased concern regarding fraud is

---

<sup>47</sup> Source: OFT, Home buying and selling Market Study, Quantitative Consumer Survey Report, Prepared for the OFT by GfK NOP Social Research, November 2009, OFT 1140.

<sup>48</sup> Council of Mortgage Lenders, "Mortgage arrears and possessions declined in fourth quarter of 2009", 11 February 2010. Source for mortgage approvals: Bank of England, based on an average for 2000-2007. 2008 was around 2 million and for 2009 around 1.3 million.

linked to more general economic conditions (fraud also increased during the previous recession).

During interviews mortgage providers stated that their internal evidence indicates that fraud is more likely to be conducted by sole practitioners because they have fewer controls in place regarding their activities and have no need to co-ordinate with colleagues in order to perpetrate the crime. Given that most concerns regarding referral fees have related to national conveyancers, there is no evidence that quality is being reduced, or indeed fraud introduced, due to the presence of referral fees.

The only example given of quality assurance activities being undertaken by mortgage providers was where conveyancers failed to register the mortgage charge on the property. Where this continued despite reminders from the lender, some lenders would put the firm on a blacklist and would not be willing to transfer funds through that conveyancer in the future. However, it is clear that this is more about the service in respect of the mortgage provider than the service with respect to the customer.

Overall we do not find that mortgage providers protect consumers in terms of ensuring high quality conveyancing (although neither is there evidence that they introduce any concerns regarding referral fees).

**Table 3: Summary of the role of referral fees in competition for legal services in conveyancing**

Issue	Evidence and causation	Potential detriment
Competition leading to an increase in referral fees	Strong evidence that referral fees on panels have increased over time.  Willingness to pay referral fees is part of panel selection.	Conveyancing fees have remained broadly constant over time hence no evidence that referral fees are increasing conveyancing fees.  Evidence suggests conveyancing fee for those paying referral fees is lower than those who do not pay referral fees in reflection of formal arrangements facilitating investment in technology.
Choice of conveyancer determined by estate agents based on referral fees	Competition on referral fees have contributed to trend towards panels and nationals, and away from local firms.  Evidence of a movement towards panels before 2004 with changes in 2004 making arrangements more explicit and less complex.  Conveyancers who do not pay referral fees often have other arrangements in place.	No evidence of problems with the title of property which could have created most significant detriment.  Referral fees have facilitated significant automation of the conveyancing process and the use of non-qualified staff. While national conveyancers offer a different service to local conveyancer there is no evidence it is of lower quality.  Evidence on the number of complaints or the speed of transaction does not indicate that nationals offer a lower quality service to consumers.
Referral fees impacting quantity of conveyancing	Conveyancing is a derived demand in the context of property transactions and re-mortgages. No evidence that referral fees impact the decision to conduct own conveyancing compared to	N/A

---

seeking professional advice.

---

Source: CRA

## **2.6. Changes impacting future competition**

The major change that might impact the conveyancing market is that of Alternative Business Structures (ABS) which allow for the potential of non-legal firms combining with legal firms and offering an integrated service to clients. In the conveyancing area that could involve estate agents to combine with firms of licensed conveyancers or solicitors. We note that it is already the case that some estate agents have in-house licensed conveyancers and therefore it is not clear whether ABS is necessary from the perspective of estate agents as they already exploit commercial advantages from having in-house conveyancers.

However, ABS does allow for the potential integration between estate agents and solicitors. We note that at present licensed conveyancers can act for both buyer and seller as long as this is disclosed, there are no apparent conflicts of interest and there are different individuals working for different parties, whereas solicitors would not be able to do this. A small number of interviewees have raised concerns that solicitor-controlled ABSs may be regulated in a different manner to non-lawyer-controlled ABSs (whether they are licensed conveyancers or estate agents). We note that having differential regulation for entities operating in the same market is not usually a desirable outcome.

The ability to have ABS potentially effects some of the policy options which we consider below.

## **2.7. Policy options**

In this section, we discuss the policy options proposed by the LSB including:

- Banning referral fees;
- Capping referral fees;
- Standardised disclosure to clients; and
- Greater disclosure to the approved regulator.

It is important to recognise that since we find no evidence that referral fees are currently causing consumer detriment in the conveyancing market, policy options which are focused on referral fees do not bring benefits.

### **2.7.1. Banning referral fees**

As we have discussed above, referral fees were already effectively being paid in the conveyancing market before they were permitted for solicitors in 2004. Licensed conveyancers could pay referral fees prior to 2004, but it is clear that de facto referral fees were also in place across the market at this time. For some firms this arose through other means such as paying for hospitality, however there was already a trend to centralise this through more formal arrangements between large firms by using marketing fees or other payments.

Banning referral fees would not change the fact that introducers such as estate agents have direct contact with clients and are therefore in a position to direct the business flow regarding conveyancing. They would still be incentivised to recommend a conveyancer to the customer and achieve economic benefits from this. If there was a ban, most our

interviewees (particularly those involved in paying or receiving referral fees) agreed that this would lead to a similar situation as that seen prior to 2004 where “creative schemes” were used to pay referral fees.

We would not expect that the market would go back to the early stage pre 2004 where individuals working for estate agents received hospitality. Since referral fees are already formalised and constitute an important income source for some estate agents, we believe that these firms would opt for more systematic arrangements with conveyancers in which estate agents received monetary income, e.g. in the form of marketing fees.

Some firms have also indicated that the role of HIPs adds complexity to the payment of referral fees with some conveyancers offering to conduct the HIP for free for the estate agent where they receive the conveyancing business. The introduction of this may provide another way in which firms could “get around” any ban on referral fees through providing other services at low cost.

For those (usually smaller) firms who do not have referral fees but have reciprocal referral arrangements in place or do currently ensure referrals through offering hospitality, we would expect this to continue.

However, even if it was possible to regulate different schemes by which referral fees could be paid, the cost of doing this would outweigh any benefits since we have not found any evidence of detriment to consumers resulting from referral fees.

Instead, we find that referral fees have encouraged greater investment in processes and automation and offered the consumer a different service proposition to that of the local conveyancer. There is no evidence that this has diminished quality and there is some evidence that these investments (facilitated by referral fees) have helped to drive cost efficiencies in the conveyancing process potentially keeping conveyancing fees down.

It is also possible that some large firms may choose to enter into ABS as a way of internalising the payment of referral fees (when they would not otherwise choose to integrate the conveyancing service with the estate agency). Few interviewees suggested this would arise although this may reflect some uncertainty regarding whether regulation would permit such firms to advise buyers on the conveyancing process at the same time as advising sellers on the sales process.

### **2.7.2. Capping referral fees**

Currently, the level of both conveyancing fees and referral fees are based on market forces. As noted, we find no evidence that increases in referral fees have generally led to increases in conveyancing fees and therefore capping referral fees would not be expected to lead to lower conveyancing fees. In theory a cap on referral fees could be attractive if there were a group of consumers who were facing very high conveyancing fees caused by very high referral fees. No interviewees have suggested that this is occurring.

If a cap was to be used, the impact of this would depend on the level of the cap and potentially the structure of the cap. If the level of the cap was above the current level of referral fees there would be no impact. If it was set below current levels, this would be likely to affect national conveyancers where we find higher referral fees are paid rather than firms who tend to operate more locally where we found that lower referral fees were common. Interviewees are clear that, in the same way that a ban would lead to other

arrangements being put in place, we would also see these arise where firms wanted to have referral fees above the cap.

As noted in section 2.4.2, there is some evidence that in a small number of cases referral fees vary according to the value of the property (in the same way that conveyancing fees themselves typically vary according to the value of the property). Having a flat cap of referral fees cross the market may therefore introduce distortions in comparison to today where some referral fees vary.

Additional costs would also be imposed regarding determining how such a cap would be set and how it would be reviewed over time. As such, a cap is likely to be administratively more complex than simply banning referral fees but would have largely the same economic effect.

### 2.7.3. Standardised disclosure to consumers

Before considering the impact of this, it is useful to examine how disclosure is currently working in the conveyancing market. Solicitors and licensed conveyancers are required to disclose to consumers that they pay referral fees, and where the payment is calculated with reference to the particular referral, solicitors must disclose the amount of the referral fee.<sup>49</sup> In addition, solicitors are required to ensure that the estate agents themselves disclose this information to the client. Licensed conveyancers must also disclose the existence and amount of any sum payable by the licensed conveyancer arising from the client's instructions.<sup>50</sup>

However, it is clear that information is not always disclosed properly. For example, the Professional Standards Unit (PSU) conducted themed visits on the subject of referral fees and of 135 visits found that "about 55% of visited firms had minor weaknesses/breaches...and about 39% of the firms had significant weaknesses/breaches".<sup>51</sup> Many of these weaknesses related to solicitors failing to ensure that introducers made sufficient disclosure regarding referral fees.

Figure 14 below sets out whether estate agents disclose information to their clients.<sup>52</sup>

---

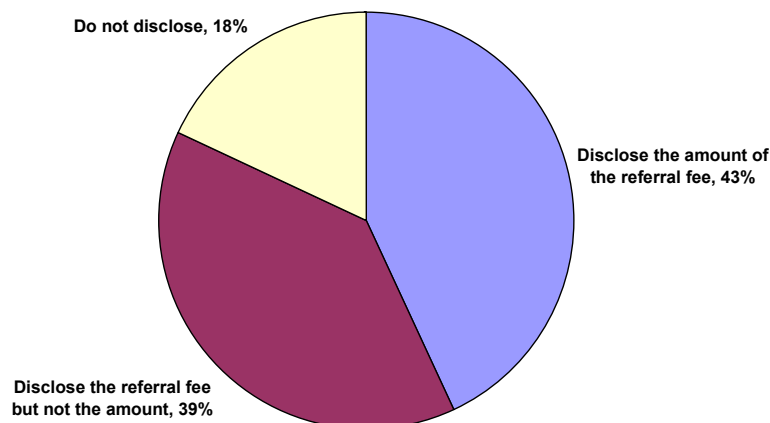
49 Solicitors Code of Conduct, Rule 9.02 e(ii).

50 CLC, Conduct Rules 2009, 5.2.8.

51 Referral arrangements – final report to the SRA Board, Solicitors Regulatory Authority, 10 December 2007. It should be noted that the sample which was chosen for the visits was focused on those where there was intelligence regarding potential regulatory problems although there remained a high level of non-compliance even among firms that had been chosen at random.

52 The results from our survey are similar to those found by the OFT that 53% of estate agents informed their clients of the size of fees received from conveyancers, while a further 28% of estate agents informed their client about the existence of the fee, but not the amount. Source: OFT, Home buying and selling: A Market Study, February 2010 OFT 1186.

**Figure 14: Disclosure of the referral fee to the client**



Source: CRA Estate agents survey

We note that these results do not necessarily imply that estate agents are failing to comply with existing rules if the 18% of estate agents who do not disclose information are all introducing clients to licensed conveyancers where there is no obligation to ensure that introducers disclose this. Similarly, the current regulations only require the amount to be disclosed if this is calculated with reference to the particular client.

Our interviewees noted that the SRA has already been stepping up its enforcement efforts regarding the disclosure of referral fees. This enforcement effort appears to be currently focused on larger firms. During interviews, large estate agents also stated that their panel conveyancers were increasingly checking that the estate agent made the appropriate disclosure suggesting that enforcement efforts are bringing improvements.

In particular, it appears that many firms are in ongoing discussions regarding how marketing fees or fixed admission to a panel should be presented in disclosure documents given to customers. In addition, as noted in section 2.7.1, the introduction of arrangements where conveyancers offer to conduct HIPs for free makes disclosure of referral fees more complex.

Evidence from the LSB's Consumer Panel finds that consumers are very strongly in favour of transparency.<sup>53</sup> Indeed transparency was seen to allay many of the concerns that consumers otherwise expressed about the role of referral fees. For example, this was seen as ensuring that consumers know that there is a commercial relationship in place between the estate agent and the conveyancer.

However, although there may be some problems regarding the disclosure of information, the current evidence shows that there is little response from customers on the disclosure of referral fees. This could be because the disclosure is hidden in the small print or

---

53 Referral Arrangements Research, Report prepared by Vanilla Research, March 2010.



because conveyancing is simply a secondary service alongside the property transaction which has the customer's main focus of attention. Interview evidence indicated that few consumers were concerned about referral fees because they focused on the overall conveyancing fee that they needed to pay rather than how this was shared between the estate agent and the conveyancer.

It is interesting to note that one interviewee also suggested that requiring disclosure related to referral fees led to improved disclosure of the actual conveyancing fee itself.

One major firm has provided its disclosure document to CRA. This gives monetary amounts related to the fees which are passed to the conveyancer and those which are retained by the estate agent. Although the information is in slightly smaller print than other parts of the document, the information is contained within one page form which customers complete and which also sets out the conveyancing fee. This firm has informed CRA that of around 25,000 conveyancing transactions each year, they are only aware of around 10 cases where customers had raised any issues on the referral fee.

Thus while consumers may like greater transparency of information, there is no evidence that having this information makes a substantial difference to consumer behaviour. Indeed this is consistent with research in other areas where introducers are common such as in financial services. For example:

- There was no evidence that the introduction of the "menu" which disclosed commission information related to financial advice (including the market average commission rates) led to a reduction in commission or to a reduction in the dispersion of commission;<sup>54</sup>
- When considering disclosure of commission to commercial companies, 81% of companies who received this information did not use it;<sup>55</sup> and
- Less than 20% of consumers believed that charges were important and shopped around on the basis of charges when considering investment products.<sup>56</sup>

Overall this evidence indicates that consumers have a relatively poor response to information that is similar to that disclosed in the conveyancing market suggesting that policy options focused on changing consumer behaviour through information disclosure would be expected to have a relatively modest impact.

#### **2.7.4. Disclosure to approved regulator**

The final policy option is that information on referral fees is provided to the Approved Regulator. This would, it is argued, allow the regulator to review the terms of the referral arrangements and the fees that are paid and to assess whether specific arrangements result in consumer detriment.

---

<sup>54</sup> Charles River Associates (previously CRA International), An Empirical Investigation into the Effects of the Menu, for the Financial Services Authority, May 2007.

<sup>55</sup> Charles River Associates (previously CRA International), Commercial insurance commission disclosure: Market Failure Analysis and high level Cost Benefit Analysis, for the Financial Services Authority, December 2007.

<sup>56</sup> Charles River Associates (previously CRA International), Benefits of Regulation: Effect of Charges Table and Reduction in Yield, for the Financial Services Authority, March 2008.

While most interviewees did not have any objection to providing additional information to Approved Regulators, most did not believe that this would cause any change in behaviour and were unsure as to what the Approved Regulator would do with the information. As such interviewees did not generally support this as a regulatory intervention.

In particular, it is unclear how consumer detriment would be measured on the basis of gathering information on referral fees. Instead it appears as though Approved Regulators would also need to collect a broad set of performance measures on customer satisfaction, pricing and speed on a company-by-company basis. However, the cost of this would be likely to be significant. Instead it would seem to be more appropriate to collect information on how the market develops (rather than on individual companies). This information could be based on the metrics discussed through this chapter rather than collect detailed information on individual conveyancers.

We also note that there was no evidence from interviews of cases where there were outliers regarding particularly high referral fees being paid and the associated service being of very low quality which again reduces the value from gathering information on referral fees in this manner.

Approved Regulators could also choose to disclose information related to referral fees from across the market if there are concerns that some firms might be paying “too much” to estate agents for the referrals because they do not have information on the referral fees that others are paying. It should be noted that the evidence gathered for this research suggests that national conveyancers in arrangements with national estate agents are paying higher referral fees than local conveyancers who have arrangements with local estate agents. In as far as concerns exist regarding high referral fees, since these appear to be linked to national conveyancers, it seems unlikely that these firms would suffer from a lack of information regarding referral fees. Instead it appears as though they have to pay these fees as a result of a competitive process.

In addition, we note that given the large number of solicitors and licensed conveyancers who provide conveyancing services, there would be considerable costs on these firms associated to gathering this information. Similarly there would be costs imposed on Approved Regulators in examining this information.

Given the lack of consumer detriment that has been identified the costs associated to this scenario would outweigh any benefits.

### 3. CRIMINAL ADVOCACY

In this chapter we consider the role of referral fees and other referral arrangements in the area of legally aided criminal advocacy. This area was raised as an area of potential concern in correspondence with the LSB and during the LSB Consumer Panel's roundtable discussion and subsequent interviews.<sup>57</sup> As explained below referral fees (as defined in Chapter 1) are not used in provision of legal services involving criminal advocacy, however, fee-sharing is common and can have similar effects. It was therefore decided in consultation with the LSB that this would be one of the areas which would be considered in detail during the research.

Sections 3.1 and 3.2 consider details of the demand and supply conditions regarding legal services in the criminal area. The concerns that have been raised arise in the publicly funded criminal advocacy market hence we limit the scope of this section to this area and section 3.3 provides details of the legal aid scheme.

Sections 3.4 to 3.6 consider how the market currently operates in terms of competition, quality and quantity of legal services provided. Section 3.7 considers the impacts of the various different policy options on this market.

#### 3.1. Demand for legal services

The criminal legal market is currently structured around:

- Litigation work where lawyers engage with clients, gather evidence and prepare a case for trial – this work is usually conducted by solicitors; and
- Advocacy work where lawyers argue the case for the client during formal legal proceedings – this work is conducted by both barristers and also solicitor advocates who have obtained the necessary rights to conduct advocacy in particular courts.

It is common for the litigator to instruct the advocate and therefore we consider separately the issues of how the litigator is chosen and how the advocate is chosen.

##### 3.1.1. Choice of litigator

Criminal clients may obtain a solicitor through the “duty solicitor” who is at the police station that they are taken to or they may choose their own solicitor. If they choose their own solicitor this is likely to be because they are a repeat offender who has used the solicitor before, part of a “criminal family” who have experience of a particular solicitor or are told about a particular solicitor by other individuals who are in custody or in prison. It is also possible that individuals have a solicitor which they have used for other types of work and simply use the same solicitor should they find themselves facing criminal proceedings. Based on interviews with solicitors operating in the criminal area it is estimated that there is a roughly even split between those clients who come through the duty solicitor route and those who come because of repeat business or the connections of

---

<sup>57</sup> No concerns were raised during interviews or the LSB Consumer Panel roundtable regarding criminal advocacy outside the legal aid system and therefore we focus on legally aided criminal advocacy alone.

family and friends. This is consistent with information in the Carter Review which found that clients choose their own solicitor in approximately half of all cases.<sup>58</sup>

Having chosen a solicitor it is most common that individual clients would continue to use that solicitor throughout the progress of their case. Interviewees have indicated that there is limited subsequent switching of clients between solicitors. However, this may happen for a number of reasons including that an alternative solicitor may give a more optimistic view (possibly a less realistic view) on the likelihood of success or the length of the sentence.<sup>59</sup> Interviewees have not suggested that the choice of the litigator or switching litigators has been linked to referral fees or other referral arrangements and therefore we do not consider further any issues regarding how the solicitor is chosen.

### 3.1.2. Choice of advocate

In terms of choosing the advocate, the client might name a specific advocate (if they have used one before), but it is much more likely that the solicitors would instruct the advocate on the client's behalf. Even those with existing experience (repeat offenders) are likely to rely on the litigator for this decision because the solicitor would typically be the person with whom the client has the most contact. All interviewees agreed that clients were in a very weak position to be able to assess the quality of advocacy services.

Advocates in the Crown Court can be either solicitor advocates or barristers.<sup>60</sup> Where a member of the independent bar is chosen either because of a request of the client or because of the selection by the solicitor, they would be instructed by the litigator as barristers do not have direct access to clients in criminal cases. Hence barristers are dependent on solicitors to provide them with clients and therefore compete with each other primarily to secure referrals from solicitors rather than through competing directly for the clients. This choice of barrister by a solicitor may involve choosing a specific individual advocate but commonly involves contacting a clerk within particular chambers who then allocates the case to a particular barrister within the chambers.<sup>61</sup>

Self-employed barristers are usually subject to the "cab-rank" rule which broadly requires barristers to accept any case in a field he is competent to practise (subject to availability).<sup>62</sup> Barristers are not obliged to accept instructions "other than at a fee which is proper" and in November 2003, the Bar Council issued guidance indicating that it was open to barristers to decline cases under the Advocate Graduated Fee Scheme (AGFS) if they did not consider the fee for the case to be a proper fee (see section 3.3.1 on the AGFS).<sup>63</sup> Hence the cab-rank rule does not necessarily apply for legally aided cases which are the subject of this chapter.

---

58 Legal Aid: A market-based approach to reform, Lord Carter's Review of Legal Aid Procurement, July 2006 – we refer to this as the Carter Review.

59 Some interviewees have indicated that this may be imposing costs on the legal aid system as it may mean that a second solicitor has to be paid to undertake the same preparation work that the original solicitor conducted.

60 All solicitors can undertake advocacy in other, lower, courts.

61 That the clerk plays this allocating role is noted in the Carter Review as well as being noted during interviews.

62 The Bar Council Code of Conduct, paragraph 602.

63 The Bar Council, Guidance from the Criminal Bar Association, Acceptance of Instructions in Criminal Cases.

Since the litigator has an important role in choosing the advocate it is clear that there is potential for referral fees and referral arrangements to arise in this market. Indeed a number of issues have been raised by multiple interviewees regarding referral arrangements in respect of the choice of advocate for work conducted at the Crown Court under legal aid.

We consider the selection criteria for choosing an advocate in section 3.4 below but first consider the supply of legal services involving criminal advocacy and also the price of these services in the context of legal aid work.

### 3.2. Supply of legal services

The LSC is responsible for delivering legal aid and in 2008/09 spent approximately £78 million on the litigator graduated fee scheme and £275 million on the advocate graduated fee scheme (see sections 3.3.1 and 3.3.2 below).<sup>64</sup> Table 4 below shows that there are a large number of firms operating in the legal aid market and the great majority of these firms (77%) have revenues from the Legal Services Commission (LSC) of less than £0.5 million.

**Table 4: Number of firms by size of claim from the LSC, 2008-2009**

Less than £0.5m	£0.5-1m	£1-2m	£2-3m	£3-4m	More than £4m
1,785	378	122	19	2	2

Source: National Audit Office, The Procurement of Criminal Legal Aid in England and Wales by the Legal Services Commission, 27 November 2009.<sup>65</sup>

Information does not appear to be available on the split of the number of firms for advocacy work compared to litigation work.

#### 3.2.1. Solicitor advocates

Historically, advocacy services in the Crown Court could only be conducted by barristers and could not be conducted by solicitors. However, changes in 1990 and 1999 allowed solicitors to act as advocates in the Crown Court by obtaining their “higher rights of audience”. These solicitors are known interchangeably as “Higher Court Advocates” (HCAs) or “solicitor advocates”. We use the latter terminology throughout the rest of the report. The number of solicitors with higher rights has increased over time as shown in Table 5 below.

---

<sup>64</sup> These figures are expected to increase somewhat as legacy cases are completed and new cases come under these schemes. Remaining expenditure within the £700 million related to crime in higher courts included £112 million on the complex crime unit (dealing with very high cost cases), £11 million on the court of appeal and supreme court and £224 million on “legacy” work reflecting work before revisions to the Advocate and Litigator Graduated Fee Schemes. Due to changes in these schemes and changes in the recording of claims for payment, it does not appear possible to compare figures over time for the Graduated Fee Schemes. Source: Legal Services Commission, Statistical information 2008/09, CDS 4 – Crime higher: Legal aid schemes.

<sup>65</sup> Information published by the Ministry of Justice identifies 6 firms that received more than £4 million rather than the 2 firms noted by the NAO. Source: Ministry of Justice, Highest paid solicitors firms and barristers from Legal Aid in 2008/09, 22 March 2010. The reason for the difference between the NAO and MoJ figures is unclear, but both sources indicate the small number of large firms operating in this market.

**Table 5: Number of solicitors with higher rights of audience**

	Number of solicitors with higher rights of audience
2004	1,160
2008	2,582
2009 (September)	2,593

Source: 2004 and 2008 from The Law Society as quoted in National Audit Office, The Procurement of Criminal Legal Aid in England and Wales by the Legal Services Commission, 27 November 2009. 2009 figures provided to CRA by The Law Society.

Information was not available from The Law Society on figures for 2005-2007. However, evidence from interviews has indicated that more solicitors have sought to obtain their higher rights in the light of changes to the AGFS in 2007 which increased the price paid for advocacy services.

It is also interesting to note that larger solicitor firms tend to both be more likely to have solicitor advocates in-house and also to be more likely to have seen the usage of solicitor advocates increase over time as shown in Table 6 below.

**Table 6: Use of solicitor advocates by size of solicitor firm**

	Number of solicitors in the firm			
	1	2-5	6-12	13-40
Proportion employing solicitor advocates	33%	39%	54%	73%
Proportion stating use of solicitor advocates has increased in the last five years	17%	34%	45%	50%

Source: GFK for the NAO, Solicitor Survey for criminal legal aid, Results summary, 2009, p7.

Overall, 45% of solicitor firms employ solicitor advocates. The proportion who stated that their use of solicitor advocates had increased over time was 37% (with 57% stating that this had stayed the same, 5% stating that this had decreased and a further 1% did not know).

In addition, firms that considered themselves “very likely” to be working in criminal legal aid in the next five years were more likely to have solicitor advocates than those firms who considered themselves “very unlikely” to conduct criminal legal aid in the next five years (53% compared to 34%) suggesting that the use of solicitor advocates in criminal advocacy would be expected to increase still further in the next few years.

### 3.2.2. Barristers

Precise figures are not available on the number of barristers conducting legal aid work in the criminal area. The number of barristers who, in their annual return to the Bar Council, denoted themselves as criminal barristers is set out in Table 7.

**Table 7: Criminal barristers**

<b>Year</b>	<b>Number of barristers at the independent bar</b>	<b>Members of Criminal Bar Association</b>
2009	4,303	3,885

Source: Provided to CRA by the Bar Council 26 March 2010.

The Bar Council and the Criminal Bar Association do not hold information on the number of barristers practising criminal law over time. Quantitative evidence therefore does not appear to exist on how the number of barristers conducting legal aid work has changed over time.

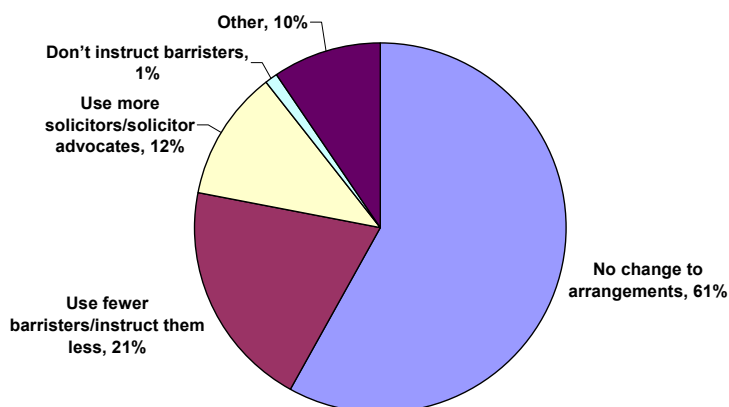
However, interview evidence suggests that the number of barristers practising criminal law has remained roughly constant or declined slightly over time. The Bar Council undertakes a survey examining the reasons for leaving the independent bar. Criminal barristers represent just under one-third of all barristers, but represent around half of those who left the independent bar in 2008.<sup>66</sup> Of these, 45% transferred to the employed bar (slightly more than the average across all areas of law).

The widening of the providers of advocacy services to include solicitor advocates as well as barristers is having an effect on this part of the market. All interviewees in this area agreed that barristers were facing a decline in the amount of criminal work that was being referred to them whereas that conducted by solicitor advocates was increasing. As shown in Figure 15 below, survey evidence also supports this view.

---

<sup>66</sup> Electoral Reform Services, Survey of Barristers Changing Practice Status 2001-08, prepared for General Council of the Bar, December 2009. This is based on a based of 12,136 barristers quoted in the exit survey and the number of criminal barristers quoted in Table 7.

**Figure 15: How, if at all, have the arrangements under which your firm instructs barristers changed in the past 5 years?**



Source: GFK for the NAO, Solicitor Survey for criminal legal aid, Results summary, 2009, p22.

It is clear from Figure 15 that there has been a reduction in the use of barristers and an increase in the use of solicitor advocates over the past 5 years. Larger firms were more likely to have used fewer barristers and more solicitor advocates. For example, firms employing between 13 and 40 solicitors stated that 33% used fewer barristers and 24% used more solicitor advocates.<sup>67</sup>

One of the other effects that interviewees have highlighted is that a movement away from using barristers and towards using solicitor advocates has led to a reduction in the number of criminal pupillages available.<sup>68</sup> The Bar Council does not hold information on the number of criminal pupillages over time. In part this is because pupillages may cover a number of different areas of law.

### 3.2.3. In-house and external advocates

As well as the split between barristers and solicitor advocates, for a particular client the solicitor instructing an advocate may choose between an in-house advocate or an external advocate:

- An in-house advocate may be either an employed barrister or a solicitor advocate; and

---

<sup>67</sup> It should be noted that there are differences in the responses to this question compared to the question set out in Table 6 regarding the increase use of solicitor advocates. This is likely to reflect the phrasing of the question. For example, it is possible that the arrangements with barristers themselves had not changed hence respondents answered the question by stating that the arrangements had not changed, but that solicitors used barristers on fewer occasions.

<sup>68</sup> A pupillage is effectively a training programme before individuals are accepted as barristers.



- An external advocate could be an independent barrister, an independent solicitor advocate or another solicitor firm with in-house advocates.

It is not possible to identify the extent to which in-house advocates are being used compared to external advocates or how this has changed over time. Information is not currently available from the LSC directly on this and neither is information available from the Bar Council on the number of employed barristers active in the criminal area. This would be useful information to collect in the future.

### 3.3. Price of legal services

Prices for publicly funded criminal advocacy services are set through the legal aid system.<sup>69</sup>

With the exception of very high cost cases (VHCCs - see section 3.3.3), the LSC does not currently influence the choice of advocate for a particular case. For VHCCs, advocates must be on an approved list which was formed following a competitive tendering process whereby advocates were assessed against experience and price based criteria. There are currently 221 advocates who are on this list.

#### 3.3.1. Advocate Graduated Fee Scheme

The Advocate Graduated Fee Scheme (AGFS) for Crown Court advocacy was introduced in January 1997 and revisions to the scheme came into force on 30<sup>th</sup> April 2007.<sup>70</sup> The AGFS sets out fees for:

- specific activities – such as standard appearances, different types of hearing, volume of pages of prosecution evidence, number of days of the trial, numbers of witnesses;
- specific types of advocate – Queen’s Counsel (QC), Leading Junior, Led Junior, Junior alone; and
- specific types of cases – such as homicide, burglary, drugs offences etc.<sup>71</sup>

Changes in 2007 increased the “basic fee” to include a number of items which previously had individual costs associated to them. In particular the basic fee now includes the Plea and Case Management Hearing (PCMH) and up to four “standard appearances”.<sup>72</sup> The PCMH is considered to be an important step in the case as, in addition to determining the plea, the case management elements set out what evidence to accept without challenge in written form, which witnesses will be called and whether they need special protection, whether previous convictions will be taken into account, and other factors which are likely to be influential in the outcome of the case.

---

<sup>69</sup> Means testing will require some defendants to make contributions to the costs of legal services. However, at present it appears as though this will not affect the prices for legal services which will remain set by the LSC. Source: Ministry of Justice, Crown Court Means Testing: Draft Regulations, Consultation Paper CP11/09, 14 July 2009.

<sup>70</sup> See Criminal Bar Association Guidance Notes, The Revised Advocates Graduated Fee Scheme 2007.

<sup>71</sup> In addition, fees vary according to the case outcome such as whether, and when, the defendant pleads guilty. In general, the fees are based on verifiable outputs which are used as a proxy for complexity of cases. It is also the case that an overall comparisons of the scheme compared to the previous scheme is only really possible for a basket of cases.

<sup>72</sup> See Criminal Bar Association Guidance Notes, The Revised Advocates Graduated Fee Scheme 2007.

The revisions to the AGFS suggested by the Carter Review specifically sought to increase fees for cases conducted by junior advocates.<sup>73</sup> It was estimated that advocates with less than 5 years' experience would see fees increase by around 18% and those with 5-10 years' experience by around 20%. By contrast, those with 15 years' experience were estimated to see an increase of only 5% and QCs a slight reduction. Overall, the revisions led to an increase in fees of around 16% (in some cases this was the first time that fees had been changed since 1997).<sup>74</sup>

One of the important concepts brought in by the revised AGFS was the "Instructed Advocate". This is the advocate who has primary responsibility for the case.<sup>75</sup> If an Instructed Advocate has not been nominated in advance, the advocate attending the PCMH will be named as the Instructed Advocate. The revised AGFS meant that the case fee is paid to the Instructed Advocate and if a "Substitute Advocate" is used (perhaps because the Instructed Advocate is unable to attend a particular hearing) the Instructed Advocate is responsible for paying the appropriate fee to the Substitute Advocate. By contrast, the previous scheme involved all of the different advocates who might be involved in a case making separate claims for their activities. Interviewees indicated that one of the major aims of introducing the concept of the Instructed Advocate was to reduce the administrative cost for the LSC as they only need make payments to the Instructed Advocate rather than multiple advocates for any particular case.

The other major aim of having an Instructed Advocate was to have case ownership and improve early and effective preparation of cases. As such it was intended that the Instructed Advocate would be the advocate that attends hearings and the trial. For example, the Funding Order notes that,

*"An instructed advocate must remain as instructed advocate at all times, except where-*

*(a) a date for trial is fixed at or before the plea and case management hearing and the instructed advocate is unable to conduct the trial due to his other pre-existing commitments;*

*(b) he is dismissed by the assisted person or the litigator; or*

*(c) he is required to withdraw because of his professional code of conduct."*<sup>76</sup>

In addition, the Consolidated Criminal Practice Direction 2007 states,

*"Active case management at the PCMH is essential to reduce the number of ineffective and cracked trials and delays during the trial to resolve legal issues. The effectiveness of a PCMH hearing in a contested case depends in large measure upon preparation by all concerned and upon the presence of the trial advocate or an advocate who is able to make decisions and give the court the assistance which the trial advocate could be expected to give. Resident Judges in*

---

73 Lord Carter's Review of Legal Aid Procurement, Legal Aid: A market-based approach to reform, July 2006.

74 Ministry of Justice, Legal Aid: Reforming Advocates Graduated Fees, 16 December 2009.

75 In some cases there can be two appointed advocates – the "leading instructed advocate" and the "led instructed advocate".

76 The Criminal Defence service (Funding) Order 2007, Schedule 1 Advocates' Graduated Fee Scheme, Part 5, Paragraph 20, (9).

*setting the listing policy should ensure that list officers fix cases as far as possible to enable the trial advocate to conduct the PCMH and the trial.”<sup>77</sup>*

Furthermore, that the intention was for the Instructed Advocate to be the trial advocate is also clear from the Carter Review which stated that,

*“This trial advocate must be identified at the commencement of the case. The graduated case payment will be made directly to that trial advocate”<sup>78</sup>*

Since all of the fees paid to the Instructed Advocate are based on prescribed levels set out in the AGFS, price competition does not arise in terms of the level of fees which are paid by the LSC.

### 3.3.2. Litigator Graduated Fee Scheme

As with the AGFS, the Litigator Graduated Fee Scheme (LGFS) sets out fees for litigators undertaking Crown Court work and was implemented in January 2008.<sup>79</sup> Payments for litigators are only made to the litigator named on the representation order.

Again the fees are based on the nature of the alleged offence, the length of trial, pages of evidence, number of defendants etc. One of the intentions of the changes was to bring savings to the LSC.<sup>80</sup> Interview evidence also indicated that the impact of the LGFS was to reduce the level of fees which are paid to solicitors with both barristers and solicitors highlighting this. This is also supported by survey evidence of solicitor firms which found that profit rates had fallen in criminal aided work over the last three years.<sup>81</sup> The Carter Review noted that profitability was considered a concern in 2006 (before changes to the LGFS).<sup>82</sup>

As well as a reduction in fees per se, the fact that revisions to fees led the litigator fee to fall and the advocate fee to increase has also changed the relativity between these fees with advocacy becoming relatively more attractive compared with litigation. As noted below in section 3.4, this has had implications for advocacy services.

---

77 Ministry of Justice, Consolidated Criminal Practice Direction 2007, Section IV.41.8.

78 Legal Aid: A market-based approach to reform, Lord Carter’s Review of Legal Aid Procurement, July 2006.

79 Legal Services Commission, The Litigator Graduated Fee Scheme Guidance, 30 September 2009.

80 National Audit Office, The Procurement of Criminal Legal Aid in England and Wales by the Legal Services Commission, 27 November 2009. Legal Services Commission, The Litigator Graduated Fee Scheme; A Response to Consultation, October 2007.

81 For example, 28% of firms stated that they were unlikely or very unlikely to be still conducting criminal legal aid work in the next five years and of these firms, 39% stated it was due to a lack of profitability within the present system and 38% stated it was due to lack of profitability without specifying further. Source: GFK for the NAO, Solicitor Survey for criminal legal aid, Results summary, 2009, p30.

82 Legal aid firms “consistently report that they are at the edge of profitability”. Legal Aid: A market-based approach to reform, Lord Carter’s Review of Legal Aid Procurement, July 2006.

### 3.3.3. Very high cost cases

Since 2000, there has been a contract based scheme for VHCCs. At present VHCCs are Crown Court cases where a trial would be expected to last for 41 days or longer.<sup>83</sup> In 2009, there were only around 100 VHCCs conducted.<sup>84</sup> The work conducted on a VHCC is agreed in advance with the Complex Crime Unit of the LSC with contract managers assessing proposed work and comparing proposals with other contracts on the same case.<sup>85</sup> No concerns have been raised during interviews regarding the role of referral fees or fee sharing arrangements in the context of the VHCC scheme and therefore we do not consider these cases further.<sup>86</sup>

### 3.3.4. Fee-sharing arrangements

Following the changes to the AGFS, the Instructed Advocate makes claims for all advocacy services including those conducted by a Substitute Advocate. This, along with the combining together of certain tasks within the basic fee, means that fee sharing arrangements may now be necessary in order to establish the fees that the Substitute Advocate receives. This contrasts with the previous AGFS where individual advocates submitted claims to the LSC for the components of work that they conducted. Interviewees have highlighted numbers of concerns relating to fee sharing arrangements. Guidance has been produced relating to these fee sharing arrangements as noted below.

#### *LSC guidance*

The LSC, as the body responsible for paying legal aid, has set out guidance regarding fee sharing and referral fees in respect of LSC crime contracts.<sup>87</sup> The LSC has stated that,

*"The level of remuneration payable to any SA [Substitute Advocate] is for agreement between the IA [Instructed Advocate] and the SA. This is a contractor/sub-contractor arrangement. The LSC, through the Funding Order, stipulates the total case fee payable (to the IA) in any given case but it does not set out how individual, substitute, advocates should be paid for work that they have done on a case.*

*... Where both the IA and any SA are independent members of the Bar, the remuneration that should be paid to a SA has been set out in the Bar Council's Remuneration Protocol.*

---

83 Other cases include trials expected to last between 25 and 40 days which relate to terrorism or serious fraud office prosecutions or where which have at least two of: at least 10,000 pages of prosecution evidence; at least 10,000 pages of unused or third party material; more than five defendants; and fraud or serious drugs cases where the value of the fraud or drugs exceeds £1 million. Source: Legal Services Commission website available at [www.legalservices.gov.uk/criminal/very\\_high\\_cost\\_criminal\\_cases.asp](http://www.legalservices.gov.uk/criminal/very_high_cost_criminal_cases.asp).

84 Ministry of Justice, Legal Aid: Reforming Advocates Graduated Fees and Very High Cost (Crime) Cases 2010, April 2010.

85 Legal Aid: A market-based approach to reform, Lord Carter's Review of Legal Aid Procurement, July 2006.

86 Given the greater involvement of the LSC in overseeing the work and the individuals involved in advocacy for VHCCs, there is likely to be less concern regarding any potential detriment arising from a reduction in the quality of advocacy services as has been raised in other areas.

87 Legal Services Commission, Fee Sharing/Referral Fees, Important guidance for holders of LSC Crime Contracts, November 2009.

*... However, in cases where the IA is an in-house advocate – either HCA or employed barrister– the Bar Council protocol is not binding and the remuneration payable to a barrister acting as a SA is for negotiation between the parties on a case by case basis.*

***Negotiation on this basis, between the respective defence team, is anticipated and permitted under the regulations.”<sup>88</sup> [emphasis in original]***

### ***Bar Protocol***

The Bar Council has adopted the Graduated Fee Payment Protocol.<sup>89</sup> The Protocol is available from Her Majesty’s Court Service (HMCS) webpage dealing with the AGFS and the LSC’s guidance indicates that fee sharing arrangements between members of the independent bar *should* be as set out in the Protocol although as noted in the quote above, the Protocol is not binding on other advocates.

The Protocol sets out details of fee-sharing arrangements to be used when more than one advocate is involved in a particular case. This includes setting out a large number of examples of the payments to be made in different circumstances and for different activities. As with the AGFS itself, the fees vary by type of case, experience of the advocate and specific activities. We understand from interviews that the Protocol seeks to set out fee sharing arrangements which are “fair” to all advocates involved in a case.

## **3.4. Role of referral fees and fee sharing arrangements in competition for advocacy services**

As noted in section 3.1.2, while some clients will request a particular advocate this is rare and in the main, clients will rely on the choice of advocate suggested by their solicitor. The LSC, while it pays for the advocacy service, does not choose the advocate for a particular case. It is important therefore to consider the criteria which are used for the selection of advocates by solicitors and how referral fees or fee sharing arrangements impact this process. It is also worth recalling that currently barristers do not have direct access to clients and therefore are dependent on referrals from solicitors which affects the way that competition occurs.

There are a number of issues that have been raised throughout the research process and during interviews regarding how competition is being influenced by various aspects of the way that fees are paid in the market. In this section we assess each of the issues that have been raised in turn to establish both the cause and also the extent of any issue. We focus here on whether there is evidence available to substantiate the particular issue raised, but we do not consider whether this is detrimental in this section. Instead, section 3.5 considers whether these issues are having any detrimental impact on the market.

### **3.4.1. Use of pure referral fees**

The LSC’s contractual terms prevent firms from making or receiving any payment for the referral or introduction of a client and the LSC states that it has observed little evidence of

---

<sup>88</sup> Legal Services Commission, Fee Sharing/Referral Fees, Important guidance for holders of LSC Crime Contracts, November 2009.

<sup>89</sup> The General Council of the Bar of England and Wales, Graduated Fee Payment Protocol, April 2007.

referral fees.<sup>90</sup> It notes that some cases reported as referral fees could be negotiations of fee sharing arrangements where the Substitute Advocate is not satisfied with the remuneration because it is lower than that set out in the Bar Council's Protocol.

Although interviewees may loosely refer to concerns related to referral fees, in practice, they were concerned about fee sharing arrangements and other referral arrangements rather than pure referral fees as defined in this report. As such there was no evidence that referral fees are currently being paid or received i.e. no payments were being made directly from advocates to litigators or other advocates in order to secure work.

In addition, no evidence was identified that there had been any change in advocacy services following changes in 2004 when solicitors were allowed to pay or receive referral fees. This further supports the evidence that referral fees are not currently being paid in respect of criminal advocacy. (Although as noted in Chapter 1, fee sharing arrangements and referral fees can lead to the same outcome in terms of the value of money which each party receives.)

#### **3.4.2. Increased use of solicitor advocates**

It was clear from Table 5 that there has been an increase in the number of solicitor advocates over time. In part this simply represents a trend which started during the 1990s when solicitors were able to obtain their higher rights and which has continued since then.

The number of solicitor advocates increased substantially between 2004 and 2008. Unfortunately data was not available for this research on the number of solicitor advocates in the intervening years and therefore it is not possible to be conclusive about the timing of the increases. Nonetheless, interview evidence did not attribute any of the growth in the number of solicitor advocates to the 2004 changes related to referral fees.<sup>91</sup> Instead, interviewees indicated that more solicitors sought to obtain their higher rights in the light of the changes to the AGFS which increased the price paid for advocacy services in 2007. Subsequent changes to reduce the price paid under the LGFS in 2008 had a similar effect as advocacy became relatively more profitable than litigation. Thus it appears to be the case that the increase in the number of solicitor advocates reflects changes to the total price paid for advocacy compared to litigation in recent years.

Further we note that the increase in the number of solicitor advocates would have been expected even in the absence of fee sharing arrangements. That is, if revisions to the AGFS had maintained the previous system where individual advocates were paid for the work that they did (hence fee sharing arrangements would not have been necessary), we would still have expected an increase in the number of solicitor advocates simply because the price for advocacy increased. We consider any potential impact from fee-sharing arrangements themselves in section 3.4.5 below.

---

<sup>90</sup> Legal Services Commission, Fee Sharing/Referral Fees, Important guidance for holders of LSC Crime Contracts, November 2009.

<sup>91</sup> There is no mention in the Carter Review of any changes arising in criminal advocacy due to referral fees. Instead it appears to Legal Aid: A market-based approach to reform, Lord Carter's Review of Legal Aid Procurement, July 2006.

### 3.4.3. Use of in-house rather than external advocates

Based on evidence from interviews, solicitor firms with in-house advocates will typically refer cases to their in-house advocate and use external advocates only for any surplus cases (when they face capacity constraints) or those cases which are beyond the abilities of their in-house staff.

Allowing solicitors to obtain their higher rights means that we would have expected an increase in the use of (in-house) solicitor advocates compared to the (external) independent bar. However, interviewees (both representatives from the independent bar and firms with in-house advocates) have stated that the increased use of in-house advocates in recent years is due to issues of profitability following the changes in the AGFS and LGFS.<sup>92</sup> This is also supported by other evidence where comments made by solicitors included:<sup>93</sup>

*“Our use [of barristers] depends on the court [the case is] being heard in, depends on type of cases, the longer the case; the more serious the case the more likely we were to use barristers. [We] use more in-house (solicitor advocates) because it is more profitable and provides continuity with the client, like in the USA where teams of lawyers work for the client and continuity is maintained.”*

*“I haven’t instructed outside counsel in the last 2 years. ... with the changes in the funding arrangements, it isn’t cost effective to instruct outside counsel and our success rate is as high if not higher than the Bar.”*

Information on the advocates used for different cases is collected through HMCS. However, we understand that information is not currently available to (or from) the LSC which would enable an assessment of the extent to which in-house rather than external advocates are being used.

Again we note that the incentive to use in-house rather than external advocates is due to the relative profitability of the AGFS and LGFS. It is not linked to referral fees (which are not paid) and does not depend on issues to do with fee sharing arrangements (which we consider further in section 3.4.5).

### 3.4.4. In-house Instructed Advocates conducting part of, but not all, advocacy services

The creation of the Instructed Advocate role places this advocate in control of the case and the associated fees. Some interviewees have argued that this has caused an increase in the appointment of in-house advocates to conduct early parts of the case, especially the PCMH, when they do not intend to conduct the trial (the implication of this for quality is examined in section 3.5.3).

---

<sup>92</sup> In general, the ability to appoint in-house advocates would also be expected to lead to cherry picking where the most profitable cases are conducted in-house and less profitable cases use external advocates. Over time we might expect to see greater competition focused around obtaining the Instructed Advocate position. This may involve greater competition on attracting clients although we note at present that independent barristers do not currently have direct client access which means that they will not be able to compete for this role in the same way that solicitors can.

<sup>93</sup> GFK for the NAO, Solicitor Survey for criminal legal aid, Results summary, 2009.

One of the changes to the revised AGFS was to increase the fees associated to early stages of the case in order to encourage effective preparation of the case. This therefore creates greater incentive for firms to keep these stages of the case in-house, but then to seek a Substitute Advocate for the trial.

It was also noted that if the client pleads guilty at an early stage, the advocacy role is thought to be relatively straightforward and also well paid. This gives a clear incentive for solicitor firms to hold on to the case where they expect the client will plead guilty.<sup>94</sup> If the client then decides not to plead guilty and the Instructed Advocate is not capable of conducting the advocacy, solicitor firms may then need to identify a Substitute Advocate at short notice.

During the course of the research we have sought to identify evidence on whether there have been any changes in the extent to which Instructed Advocates conduct early parts of a case but do not conduct the trial. Despite the fact that the information required to assess this issue is captured through HMCS, at present this information is not available to (or from) the LSC in a form that can easily be examined. We understand that such information may become available in the future and as such suggest that in future data is captured which considers the extent to which:

- the Instructed Advocate is also the trial advocate;
- the Instructed Advocate conducts the PCMH; and
- the trial advocate conducts the PCMH.

In each case it will be useful to consider how this changes over time and whether the trends vary according to whether the advocate is in-house or part of the independent bar. Information on the extent to which these trends occur will then need to be combined with issues set out in section 3.5.3 regarding any detriment associated to these trends.

Despite the lack of quantitative evidence, interviews with the independent bar and Judiciary have noted that there has been an increase in the extent to which the PCMH is conducted by an advocate who is not the trial advocate (the implications of this are considered in section 3.5.3).

It should be noted that the incentive to act as Instructed Advocate and conduct early parts of cases is driven by the relative profitability of the AGFS and the LGFS, and by the relative profitability of particular stages of the advocacy process or particular cases. As such the incentives in respect of keeping *part* of the case in-house are similar to those in respect of the trend to use in-house advocates for the *whole* case identified in section 3.4.3. For the same reason, we note that the incentive to keep work in-house remains even if solicitors were obliged to follow the Bar Protocol. However, it is the case that the extent of this incentive is affected by fee sharing arrangements and we consider this in section 3.4.5 below.

---

<sup>94</sup> Representatives of the Judiciary have noted that a similar trend has been observed in the Crown Prosecution Service (CPS). The CPS has increased its use of in-house prosecutors and believed to be less likely to appoint an external prosecutor where they believe the client will plead guilty. It is understood that budgetary concerns are a motivating factor for this as this approach reduces the (relatively expensive) fees associated with external prosecutors.



### 3.4.5. Appointment of external advocates based on fee sharing arrangements

In addition to the general incentive for solicitor firms to seek to retain work in-house, being the Instructed Advocate gives control of the fees which are paid to any Substitute Advocate. The Instructed Advocate is then in a position where they can use negotiations on fee sharing as the basis for the selection of the Substitute Advocate. There are two (linked) implications of how this impacts competition.

First, solicitor firms may appoint (external) solicitor advocates in preference to (external) barristers because solicitors are not constrained by the Bar Protocol. There is mixed evidence from interviews regarding the extent to which this arises:

- Barristers report that they are suffering from a reduction in work (although it is difficult to distinguish this from the pressure caused by the increased use of in-house advocates and solicitor advocates more generally);
- Some solicitor firms have explicitly stated that they would prefer to use solicitor advocates rather than barristers in order to avoid the Bar Protocol; and
- Some solicitor firms have stated that currently they would prefer to refer work to the independent bar because barristers will not compete with them for the litigation work whereas they face the danger that referring to solicitor advocates could lead to poaching of clients for the whole case.<sup>95</sup>

Although the evidence is mixed, at least some solicitor firms are seeking to refer to solicitors rather than barristers because of fee sharing arrangements. Information identifying advocates is captured through HMCS but is not currently available in a form that allows us to assess the extent to which external advocates are solicitors or barristers.

Second, solicitor firms may be choosing (solicitor) Substitute Advocates on the basis of the most preferential fee sharing arrangements i.e. firms instruct the advocate who is willing to conduct advocacy services for the lowest price. Since the overall fees are set by the LSC, this would leave the remainder of the fee to the Instructed Advocate. Barristers and their representatives often refer to this as “improper fee sharing arrangements” since the arrangements do not conform to the Bar Protocol. (It should be noted that there is no compulsion for advocates other than the independent bar to conform to the Bar Protocol.)

No quantitative evidence is available on the proportion of fee sharing arrangements which do and do not conform to the Bar Protocol. Those participating in these arrangements are clear that the primary motivation for the selection of a particular advocate is the willingness of the advocate to accept 80% of fees that might otherwise have been accepted therefore increasing profitability for the solicitor making the referral. Advocates willing to accept non-Protocol fees will therefore be chosen in preference to those who are not willing to accept non-Protocol fees. Those participating in arrangements stress that this choice is dependent on the advocate being capable of conducting the work although those who do not participate in these arrangements dispute this (this is considered further in section 3.5.3).

It is also interesting to note that the figure of 80% was consistently cited during interviews by those who were aware of fee sharing arrangements in place (including by those who used fee sharing arrangements). It appears to be the case that a small number of solicitor

---

<sup>95</sup> We note that if such poaching of clients arose, solicitor firms would be unlikely to continue to refer work to those particular solicitor advocates suggesting that this effect would be limited.

firms may have “market-tested” the level of fees that advocates would be willing to accept and had settled on the 80%. Information about the 80% figure then appears to have been disseminated throughout the market such that other solicitor firms seeking to select advocates on the basis of fee sharing arrangements have simply used this figure.

#### **3.4.6. Use of in-house juniors**

A further method by which the selection of advocates occurs is through solicitor firms requiring that an in-house junior advocate be used as the “led junior” on a case rather than leaving the leading advocate to appoint the junior. From the solicitor firm’s perspective one of the key drivers for this is that it means that more work (and therefore more revenue) is kept in-house. Some interviewees have suggested that the using an in-house junior advocate may be a condition of the work being referred to a particular external advocate.

That this practice arises has been confirmed by barristers, solicitors and representatives of the Judiciary although the extent of it is not possible to quantify as data on this is not currently available.

CRA has been provided with examples relating to the use of in-house juniors and some of these examples date from before April 2007 when the revised AGFS took effect. Representatives of the Judiciary suggest that these arrangements have been in place for more than a decade. Hence the practice of requiring in-house juniors to be used has not been caused by changes in the AGFS or associated fee sharing arrangements although the increased price for advocacy may have increased the extent to which in-house juniors are used.

#### **3.4.7. Alternative referral arrangements**

In addition to arrangements that are made for a specific case, it has also been identified that referral arrangements are in place that extend beyond the particular Crown Court case at hand. An example of this is where arrangements are made between chambers and solicitor firms in which the solicitors provide the senior barristers with Crown Court work in return for agreements that junior barristers will conduct work in the Magistrates Court for low prices.<sup>96</sup> It is unclear whether the junior barrister would also gain through being appointed the led junior on the Crown Court work that chambers receive as a result of these arrangements.

No evidence currently exists on the extent to which solicitor firms appoint the same set of chambers on Crown Court and Magistrates Court cases. It has also been noted by interviewees that arrangements such as these have been in place for a considerable length of time and date to before the AGFS revisions and are therefore not linked to fee sharing arrangements. However, it is possible that the pressure to enter into these arrangements has been increased in the light of the increased competition for advocacy more generally.

Indeed, the Bar Council has identified that this practice has been arising and issued guidance in November 2008 which is aimed at preventing junior barristers from suffering

---

<sup>96</sup> In broad terms, pricing for the Magistrates Court is based on “one case one fee” enabling solicitors and advocates to negotiate agreements on the payment for any advocacy required. We also note that this suggests that to some degree chambers are acting as economic entities.

from lower fees in this manner.<sup>97</sup> The fact that the Bar Council issued guidance is indicative of this not being limited to a small number of examples.

Furthermore, evidence from interviews has indicated that price competition for advocacy work in the Magistrates Court has increased over time. This appears to reflect the fact that, as a lower court, the Magistrates Court is the entry level location for advocacy hence there are more advocates that attempt to conduct work in the Magistrates Court than in the Crown Court (where greater experience is required). The advent of solicitor advocates has increased the number of advocates seeking to undertake advocacy services in the Magistrates Court and therefore it is no surprise that this market is considered to be more competitive. One of the implications of this is that even if evidence existed on the prices which are charged for advocacy in the Magistrates Court, it is likely to be very difficult to identify the cases where prices of junior barristers are low because of arrangements within chambers to ensure senior barristers receive Crown Court cases compared to those cases where prices of junior barristers are low because of competition for the Magistrates Court work more generally.

In addition to arrangements related to junior advocates, interview evidence, which is described during interviews as “anecdotal” has identified that a range of other referral arrangements are in place. For example, examples have been given where chambers or individual external advocates would provide training for solicitors, mentoring schemes and secondments. These services are provided for free to solicitor firms in the expectation that the external advocate would receive referrals on Crown Court work. No evidence is available on the extent to which these arrangements are in place.<sup>98</sup>

#### 3.4.8. Summary on the role of referral fees in advocacy

Table 8 below sets out a summary of the extent to which various arrangements are affecting competition for advocacy services. We summarise both the evidence related to any trends identified as well as the causation for the trends observed in order to assess whether any of these issues are driven by fee sharing arrangements equivalent to referral fees or whether they are driven by other factors.

**Table 8: Summary of the role of fee sharing arrangements in competition for advocacy**

<b>Issue</b>	<b>Evidence and causation</b>
Increased use of solicitor advocates over time	Quantitative evidence of an increase in the number of solicitor advocates over time. Interview evidence supports increase in solicitor advocates because advocacy became more profitable under the AGFS.
Use of in-house rather than external advocates	Quantitative evidence not available on the extent of this trend, but supported by interview evidence. Survey and interview evidence finds that it is driven by changes to the AGFS and LGFS which made advocacy relatively more profitable.
In-house advocates conducting part but not all of the advocacy	Quantitative evidence not available but interview evidence identifies that cases are kept in-house where pleading guilty is expected as this is profitable. If the client then decides not to plead guilty,

---

<sup>97</sup> The Bar Council, Improper fee arrangements, 18 November 2008.

<sup>98</sup> It is also noteworthy that representatives of the Judiciary consider that it is not possible to police these arrangements.

services	<p>substitute advocates may be required at short notice. Primary driver is profitability of AGFS especially for guilty pleas.</p> <p>Quantitative evidence not available on the extent to which the Instructed Advocate is the trial advocate or which advocate conducts the PCMH. Interview evidence (including with Judiciary) that there has been increased use of non-trial-advocate at PCMH. Primary driver is profitability of AGFS especially in early stages.</p>
Appointment of external advocates based on fee sharing arrangements	<p>Quantitative evidence not available on the extent of a preference for external solicitors advocates rather than barristers. Interview evidence supports some firms having a preference for solicitors to avoid the Bar Protocol on fee sharing.</p> <p>Quantitative evidence not available on the proportion of fee sharing arrangements which conform to the Bar Protocol. Interview evidence identifies that advocates willing to accept non-Protocol fees will be chosen in preference to those who are not willing to accept non-Protocol fees.</p>
Use of junior in-house advocates	<p>Quantitative evidence not available on the extent of using in-house junior advocates. Evidence of these arrangements pre-date changes to the AGFS in 2007 but some evidence that it has increased over time.</p>
Alternative referral arrangements	<p>Qualitative evidence of senior barristers receiving Crown Court work in return for low priced junior barristers for Magistrates Court work. Evidence that this has occurred for some time but that the Bar Council issued guidance in 2008 suggests it has increased. Low prices linked to referral arrangements unlikely to be distinguishable from those linked to increased competition in Magistrates Courts.</p> <p>Anecdotal evidence of training, mentoring schemes and secondments in anticipation of receiving referrals with no evidence of the extent to which such arrangements are in place.</p>

---

Source: CRA

### 3.5. Market failure and potential detriment arising from fee sharing arrangements

Many of the potential concerns regarding fee sharing arrangements relate to the quality of advocacy services. For this reason in section 3.5.1 below we first set out the requirements that are currently in place which aim to ensure that high quality advocacy services are maintained. Section 3.5.2 then sets out some of the current issues surrounding assessing the level of quality of advocacy. Section 3.5.3 then examines whether the issues noted in Table 8 above lead to market failure or consumer detriment.

#### 3.5.1. Current restrictions to ensure quality

The Solicitors Regulation Authority and the Bar Standards Board are the Approved Regulators responsible for ensuring that appropriate standards are set and upheld in the services which are offered by solicitors and barristers respectively. Codes of Conduct are in place for both solicitors and barristers which seek to ensure high quality legal services are provided. For example:

- One of the core duties of solicitors is to act in the best interests of their client as noted in Rule 1.04 of the Solicitors' Code of Conduct;<sup>99</sup> and

---

<sup>99</sup> Rule 1.04, Solicitors' Code of Conduct 2007.

- A barrister must promote and protect a lay client's best interests under paragraph 303 of Bar's Code of Conduct.<sup>100</sup> This also requires that an advocate should not take on a case for which they are not competent.

We might therefore expect these duties to ensure that advocates do indeed act in the best interests of their clients and provide a high quality service.

In addition to this, the fact that advocates are observed in court by litigators who may appoint them in future gives an incentive to ensure that they perform well. Furthermore, the concern of the litigator for their own reputation should also act as a mitigating factor against any reduction in quality by the advocate. For example, if the litigator does not select a high quality advocate they may lose future repeat business from that client (or their family and friends).<sup>101</sup>

However, despite these factors, interviewees of all types have indicated concerns about the quality of advocacy services suggesting that relying on the Codes of Conduct and the instructing solicitor is insufficient to ensure quality is maintained. Indeed, during the course of the development of the Quality Assurance for Advocates (QAA) scheme, 90% of advocates interviewed after the research pilot believed that quality could not be adequately determined by the market. The LSC also stated that,

*"there remain advocates at all levels who appear in cases (from the simplest to the most complex) that are beyond their competence".<sup>102</sup>*

Concerns about quality in criminal advocacy were identified in the Carter Review in 2006. It was noted that introducing price competition in criminal legal aid would bring a significant risk to quality as high quality efficient suppliers could be undermined by low quality unsustainable suppliers. For this reason the Carter Review stated that,

*"A swift move towards a proactive quality assurance process for advocates is required as a **precondition** of the new advocacy procurement system."<sup>103</sup>  
[Emphasis added]"*

It is clear from this that the intention of the Carter Review was that a quality assurance scheme would be in place *before* any movement towards a more market based pricing system. In practice this has not arisen and the QAA scheme remains under development at the time of writing (see section 3.6.1 below).

Finally, we note that consumers are thought to be in a weak position to assess the quality of advocacy services that they receive indicating that the role of the consumer in selecting or the advocate or switching advocates is likely to be very limited in ensuring that quality standards are maintained.

---

100 Paragraph 303(a) of the Bar's Code of Conduct.

101 Although consumers are thought to be in a weak position to assess the quality of advocacy services that they receive which limits the extent to which the reputational concern is effective.

102 Legal Services Commission, Quality Assurance for Advocates, Working with the professions to deliver a framework for better advocacy, A Discussion Paper, February 2010.

103 Legal Aid: A market-based approach to reform, Lord Carter's Review of Legal Aid Procurement, July 2006.

### 3.5.2. Current methods of assessing quality

#### *Quality assessment*

All interviewees acknowledged that the assessment of quality in criminal advocacy is challenging. There is currently no method of measuring or monitoring quality in place and therefore no evidence that can be directly examined to assess whether there has been any change in quality over time. In particular, the LSC does not directly monitor the quality of advocacy.

#### *Pilot QAA scheme*

There is tentative evidence from the pilot scheme of the QAA which finds that for Level 2 (reflecting straightforward Crown Court cases), solicitors had a higher failure rate (42%) than barristers (25%).<sup>104</sup> This is based on a voluntary pilot scheme and the LSC notes that individuals may have sought to test themselves at a higher level than that at which they commonly operated. However, the LSB notes that,

*“there is no evidence to show that merely having the right to appear and conduct trials in the Crown Court means that an advocate can exercise their skills at the requisite entry level for that court”*<sup>105</sup>

#### *Complaints by clients*

Information is available on the level of complaints related to legal services in the criminal area:

- The Bar Standards Board reports that 136 complaints were made in 2008 relating to the criminal area which represented 16% of all complaints made;<sup>106</sup> and
- The number of complaints in the criminal area recorded by the Legal Complaints Service has increased over time from 364 in 2000 to 774 in 2009 although complaints in most areas of law have also increased.<sup>107</sup> Criminal complaints have remained at around 5% of all complaints over this period. Data provided to CRA does not enable us to determine whether these complaints relate to advocacy as opposed to other parts of the legal service provided.

Complaints data is currently of insufficient detail to enable it to be used to establish whether clients have observed any change in the quality of advocacy services. However, it should be noted that all interviewees highlighted that clients have very limited ability to assess the quality of advocacy suggesting that even if complaints data was available at a sufficient level of detail, it would be a weak method of assessing quality.

#### *Concerns from Judiciary*

Interviews, including with representatives of the Judiciary, have indicated that there has been an increase in Judicial concern regarding the quality of advocacy in recent years.

---

104 Legal Services Commission, Quality Assurance for Advocates, Working with the professions to deliver a framework for better advocacy, A Discussion Paper, February 2010.

105 Legal Services Commission, Quality Assurance for Advocates, Working with the professions to deliver a framework for better advocacy, A Discussion Paper, February 2010.

106 Bar Standards Board, Annual Report 2009.

107 Data provided by the Legal Complaints Service to CRA.

The LSC reports that the lack of pre-defined levels at which advocates are allowed to operate means,

*“the judiciary is clear that this is leading to too many advocates accepting instructions that are beyond their level of competence”<sup>108</sup>*

Indeed, interviewees indicated that increased Judicial concern was one of the reasons that the development of the QAA scheme had received greater focus in recent times.

#### *Examples from interviewees*

During the course of interviews, examples were provided of poor quality advocacy arising in specific cases. However, it was acknowledged by interviewees that there were examples of high and low quality advocacy being conducted by both barristers and solicitor advocates. It is not possible to conclude from these examples that there is a difference in quality between barristers and solicitors for particular types of cases. Therefore it can not be concluded from this information that changes in the use of solicitor advocates compared to barristers impacts the quality of advocacy.

It is, however, worth noting that interviewees (including solicitors expressing a preference for using in-house solicitor advocates) generally acknowledged that the more complex cases were likely to remain the preserve of experienced barristers. Further, most of the interview evidence suggested that concerns about quality were primarily raised in relation to choosing internal advocates in preference to external *junior* barristers rather than more experienced barristers. This suggests that in-house advocates are primarily being used on cases at the lower level of complexity.

### **3.5.3. Areas of potential detriment**

#### *Using in-house advocates*

As noted in section 3.4.3, interview evidence has identified an increased use of in-house advocates in preference to external advocates. It was noted that this trend strengthened following changes to the AGFS. Concerns have been expressed, including from the Judiciary, that an increased use of in-house advocates is leading to a reduction of quality as firms appoint advocates on the basis of profitability causing advocates to be appointed for cases beyond their competence.<sup>109</sup> In the absence of a quality assurance scheme it is not possible to assess the effect of this in detail.

#### *Using in-house advocates for part of the case – guilty pleas expected*

It was noted in section 3.4.4 that cases where clients plead guilty are relatively profitable hence solicitors appoint in-house advocates for these. One of the effects of this was thought to be that where clients do not in fact want to plead guilty, solicitors will seek a substitute advocate at short notice (such as the night before the PCMH).

While this last minute preparation appears detrimental, in practice it appears common that advocates undertake preparation the night before they are in court because, for small cases, timetables for court are only published in the late afternoon the day before. Since

---

108 Legal Services Commission, Quality Assurance for Advocates, Working with the professions to deliver a framework for better advocacy, A Discussion Paper, February 2010.

109 It may also lead to the appointment of an advocate who, while competent, may not be the best quality advocate that could be appointed. For convenience, in the main text we refer only to the issue of competence.

last minute preparation by advocates is not out of the ordinary, that it occurs in these cases where in-house advocates are replaced by external advocates because the client decides not to plead guilty does not bring additional detriment compared to normal practice.

*Using in-house advocates for part of the case - trial advocates not attending or directing the PCMH*

Interview evidence has identified an increase in the extent to which the PCMH is conducted by an advocate who is not the trial advocate. All interviewees agreed that it was not always possible for the trial advocate to attend the PCMH because of difficulties surrounding the timetabling of cases and therefore that seeking substitute advocates for the PCMH was common for both barristers and solicitor advocates.

Given that PCMHs are commonly undertaken by advocates who will not be the trial advocate it is important to consider why any increase in the use of in-house advocates for this stage might be detrimental. There are two areas of concern regarding this.

First, an inexperienced advocate (such as those who do not conduct many trials) may not have “the trial advocate’s eye” by which it is meant that they will not always know what to look for when considering issues of case management. This was the concern that was most frequently identified by interviewees including by the Judiciary and is consistent with the evidence of concerns set out in section 3.5.1.

Second, if in-house advocates conduct the PCMH (for financial reasons) without any intention of being the trial advocate, then the trial advocate would not have had the opportunity to influence the PCMH. As such this is a worse outcome compared to when the Instructed Advocate does intend to conduct the trial but is unable to attend the PCMH for valid reason. Representatives of barristers have suggested that the appointed trial advocate would expect to give instructions to the substitute advocate regarding the PCMH. It should be noted that this is dependent on:

- a specific advocate being appointed as the Instructed Advocate in advance of the PCMH; and
- the advocate having undertaken preparation in advance such that they can direct the substitute advocate.

Given that interview evidence has indicated that preparation for small cases arises the night before court appearances, the extent to which these conditions will be met in practice is unclear.

It is also worth noting that any increase in the extent to which the trial advocate is not attending or directing the PCMH goes against some of the intentions of the revisions to the AGFS. For example, increasing the basic fee was aimed at encouraging increased preparation at early stages of the case so as to improve efficiency and the creation of the Instructed Advocate was partly to encourage case ownership. Based on the evidence of interviews, the revisions may be having the opposite effect, which may itself be reducing the quality of advocacy.<sup>110</sup>

---

110 Issues to do with case ownership and early preparation of the case were considered to be beyond the scope of this research.



Having an insufficiently experienced advocate conduct the PCMH could result in decisions which adversely affect the client's defence. At present the lack of a quality assurance scheme means that there is little to prevent this from arising. However, the lack of a quality assurance scheme also means that it is not possible to assess the extent to which this is, or is not, causing detriment to clients.

#### *Selecting advocates on the basis of fee sharing arrangements*

As noted earlier, interview evidence has suggested that some solicitors are selecting advocates on the basis of fee sharing arrangements.

The first concern raised is that advocates who conduct work under fee sharing arrangements may not receive sufficient fees – arrangements where they receive 80% of the fees they would otherwise have expected have been consistently mentioned in interviews. It is argued that these advocates may therefore need to conduct more work in order to receive the same level of income and would therefore spend less time conducting the case than they otherwise would have done. There are two important observations:

- For cases typically conducted by junior barristers, the Carter Review estimated that the AGFS revisions would lead to an increase in fees of around 20%. A subsequent reduction of 20% due to fee sharing arrangements therefore places the fees roughly in line with where they were before the AGFS revisions in nominal terms; and
- The operation of the Bar Protocol means that in some cases substitute advocates would be conducting a particular role for 80% (or less) of the fee that they might expect in other cases.<sup>111</sup> There have been no concerns expressed that the operation of the Bar Protocol is leading to a reduction in the quality of services undertaken.

These observations indicate that there is not strong evidence that the impact of the fee sharing arrangements would be to significantly reduce the level of quality simply because the fees are "insufficient". Furthermore, we note that if advocates have an incentive to reduce the quality of work under fee sharing arrangements because quality is not monitored, then they would have the incentive to reduce the quality of work without fee sharing arrangements simply because quality is not monitored.

The second concern that is expressed is that fee sharing arrangements are "improper". By this, it is meant (usually by representatives of barristers) that the fees which have been set out by the LSC as appropriate to different tasks are not being received by those who conduct those tasks but some (improper) proportion of them is being retained by the Instructed Advocate. Examples of this might include:

- Where an individual is named as the Instructed Advocate but does not conduct any of the appearances or the trial but still receives 20% of the fees; or
- Where an individual is named as the Instructed Advocate but does not conduct the trial yet still receives 20% of the fees which are specifically set out as payments for the trial.

---

<sup>111</sup> For example, this arises where there are three standard appearances in addition to the PCMH and trial. This is because the sum of the individual components under the previous pricing approach would be greater than the basic fee under the revised AGFS, hence the Bar Protocol sets out the way to reduce all fees by the same proportion. See examples 4, 5, 6 and 7 of the Bar Protocol.

The advantage of a non-Protocol fee sharing arrangement therefore accrues to the individual or firm who, as the Instructed Advocate, has a position of bargaining power in comparison to other advocates. We note that negotiations on fee sharing arrangements bring no immediate benefits to either the client or the LSC compared to following the Bar Protocol since the overall level of fees is fixed.<sup>112</sup> Although there appear to be no benefits from this, for the same reasons as those cited above, at present there is no clear detriment arising from this.

The third concern raised is that the fee sharing arrangements lead to the selection of an advocate who is insufficiently qualified for the case at hand but is willing to conduct the case for a lower fee than others. In the absence of a method of assessing quality it is not possible to establish the extent to which this is arising or to assess the detriment that occurs because of it. However, as noted above the judiciary is concerned about advocates conducting work that they are not qualified to do and this is the very issue that was highlighted in the Carter Review as explained in section 3.5.1, hence it does appear to be a valid concern.

The current lack of a QAA scheme means that the clients have little protection against incentives which are increasingly focussed on profitability rather than the quality. These concerns are likely to remain in place until a robust QAA scheme is in place. Indeed, this also explains why the Carter Review stated that a QAA scheme was a *pre-condition* for introducing a more market based pricing system.

Evidence from interviews suggests that it is junior barristers who are facing most of the pressure from these fee sharing arrangements. This indicates that current pressures are being faced in respect of less complex cases. Concerns about the detriment caused by a reduction in quality are likely to be lower for less complex cases compared to more complex cases.

The fourth concern that arises relates to the long-term implications for the independent bar. Relative to the past, the revised AGFS and fee sharing arrangements are combining to favour in-house and solicitor advocates compared to the independent bar. This has the effect of reducing the attractiveness of joining the independent bar (and increasing the attractiveness of becoming an in-house advocate). If junior barristers are not able to conduct a sufficient number of more straightforward cases (because these are conducted by in-house advocates) then they may not be able to build up a practice or to learn and improve their advocacy skills over time.

It is possible that this leads to a reduction in the number of experienced barristers in years to come. In turn this may have detrimental effects for the most complex cases which nearly all interviewees believe will remain the preserve of the independent bar. Alternatively it may simply lead to a change in the career path of advocates in which individuals increasingly obtain initial experience as in-house advocates and then either move to the independent bar when they are more experienced or the more complex cases may instead be conducted in-house.

---

<sup>112</sup> We consider in section 3.7 whether information relating to fee sharing arrangements could be useful to those setting prices for Legal Aid.

### *Use of in-house juniors*

One of the concerns of external advocates having to use an in-house junior advocate is that the in-house junior may not be performing the role of the junior to a sufficiently high standard. As such interviewees referred to this practice as using “straw juniors”.

Representatives of the Judiciary have stated that the use of straw juniors has been identified as a concern. Indeed in 2008 the Judiciary took steps to reduce the use of multiple advocates.<sup>113</sup> However, it should also be noted that this did not appear to lead to a reduction in particular straw juniors after they had been identified but rather to a reduction in granting permission for a led advocate more generally. (Although this would affect the number of straw juniors since they can only be appointed as led advocates.)

If a led advocate is appointed in a case this is because the case is sufficiently complex to require a second advocate. In addition one of the roles of a led advocate is to ensure that a trial could continue if the leading advocate could not attend the court temporarily.

Where examples were provided in which leading advocates had a straw junior, the evidence suggested that this was overcome through the leading advocate conducting the work that the led advocate would have done. This leads to greater pressure on the leading advocate who under the AGFS would not be rewarded to the same degree as if they had been the only advocate. This suggests that quality may be maintained through the action of the leading advocate but that resources are being wasted through payments to led advocates who are not performing a useful role.

### *Referral arrangements*

The allocation of work on the basis of other referral arrangements (primarily between chambers and solicitor firms) was identified as a minor issue in comparison to the other issues highlighted above. As such interviewees did not identify particular implications for quality from these arrangements.

## **3.5.4. Summary**

Table 9 below sets out a summary of the impact of fee-sharing arrangements (similar to referral fees) in criminal advocacy. We highlight in bold those areas where there is potential concern regarding consumer detriment which is linked to fee sharing arrangements.

**Table 9: Summary of the impact of fee sharing arrangements in criminal advocacy**

<b>Issue</b>	<b>Evidence and causation</b>	<b>Detriment</b>
Increased use of solicitor advocates over time	Quantitative evidence of an increase in the number of solicitor advocates over time. Interview evidence supports increase in solicitor advocates because advocacy became more profitable under the AGFS.	No systematic evidence that solicitor advocates of different quality to barristers for particular cases.

---

113 Data provided by the Judiciary indicates that the total number of applications for multiple advocates reduced in 2009 compared to 2008 although the proportion of applications granted remained roughly constant. Evidence was not available from earlier years to assess whether previous years had higher numbers of applications. A significant driver of the desire to reduce the use of multiple advocates in 2008 was believed to be the need to save money in this area in order to fund a particular VHCC scheme.

Use of in-house rather than external advocates	Quantitative evidence not available on the extent of this trend, but supported by interview evidence. Survey and interview evidence finds that it is driven by changes to the AGFS and LGFS which made advocacy relatively more profitable.	Concerns that a focus on profitability causes advocates to be appointed for cases beyond their competency.
In-house advocates conducting part but not all of the advocacy services	<p>Quantitative evidence not available but interview evidence identifies that cases are kept in-house where pleading guilty is expected as this is profitable. If the client then decides not to plead guilty, substitute advocates may be required at short notice. Primary driver is profitability of AGFS especially for guilty pleas.</p> <p>Quantitative evidence not available on the extent to which the Instructed Advocate is the trial advocate or which advocate conducts the PCMH. Interview evidence (including with Judiciary) that there has been increased use of non-trial-advocate at PCMH. Primary driver is profitability of AGFS especially in early stages.</p>	<p>Last minute preparation is common for PCMH hence no additional detriment arises compared to normal practice.</p> <p>Concerns that inexperienced advocates adversely impact defence. Lack of quality assurance scheme means little prevents this from arising, but also means it is not possible to assess detriment.</p>
<b>Appointment of external advocates based on fee sharing arrangements</b>	<p><b>Quantitative evidence not available on the extent of a preference for external solicitors advocates rather than barristers. Interview evidence supports some firms having a preference for solicitors to avoid the Bar Protocol on fee sharing.</b></p> <p><b>Quantitative evidence not available on the proportion of fee sharing arrangements which conform to the Bar Protocol. Interview evidence identifies that advocates willing to accept non-Protocol fees will be chosen in preference to those who are not willing to accept non-Protocol fees.</b></p>	<p><b>No evidence that 80% fee sharing is reducing quality; furthermore, this can arise under Bar Protocol.</b></p> <p><b>No immediate benefits for either clients or LSC from non-Protocol arrangements.</b></p> <p><b>Concerns that a focus on profitability causes solicitor advocates to be appointed for cases beyond their competency. Greatest impact observed where quality is of less concern on less complex cases.</b></p> <p><b>Potential reduction of experienced barristers in future or change in career path for advocacy with more in-house advocates and fewer independent barristers.</b></p>
Use of junior in-house advocates	Quantitative evidence not available on the extent of using in-house junior advocates. Evidence of these arrangements pre-date changes to the AGFS in 2007 but some evidence that it has increased over time.	Judicial concern resulted in action against led advocates generally rather than in-house "straw" juniors. Impact on clients mitigated by leading advocate although resources are wasted.
Alternative referral arrangements	Qualitative evidence of senior barristers receiving Crown Court work in return for low priced junior barristers for Magistrates Court work. Evidence that this has occurred for some time but that the Bar Council issued guidance in 2008 suggests it has increased. Low prices linked to	Interviewees did not identify particular quality implications from these arrangements.

referral arrangements unlikely to be distinguishable from those linked to increased competition in Magistrates Courts.

Anecdotal evidence of training, mentoring schemes and secondments in anticipation of receiving referrals with no evidence of the extent to which such arrangements are in place.

---

Source: CRA

It is worth noting that throughout the research and interviews there has been no suggestion that referral fees or referral arrangements have any impact on the quantity of criminal advocacy which instead is determined by external events related to crime. It is possible that that functioning (and profitability) of the legal aid scheme itself impacts the extent to which advocates are willing to operate in this market although this is not an issue which is directly related to referral arrangements so we do not consider it further.

### **3.6. Changes impacting future competition**

In addition to considering the current state of competition and the manner in which competitive forces are affecting the market, it is also important to consider the effects of changes which are expected in the market.

#### **3.6.1. Quality assurance for advocates**

As noted above, the Carter Review indicated that there was a need to have a quality assurance scheme in place for criminal advocacy. It was intended that this scheme would be in place in advance of the revisions to the AGFS in 2007 but in practice the Quality Assurance for Advocates (QAA) scheme is still under development.

The LSC has been developing aspects of the QAA since the Carter Review including through setting out and testing various competencies that would be required of advocates, consideration of different levels of complexity of cases such that different advocates could be competent at levels applicable to different cases, and piloting various different assessment mechanisms to demonstrate competency.<sup>114</sup> Responsibility for the continuing development of the QAA scheme has now moved to the Joint Advocacy Group consisting of the professions' regulatory bodies.

We note that there are concerns that a focus on profitability causes advocates to be appointed for cases beyond their competency either in the case of using in-house advocates or through fee sharing arrangements. That is, advocates may be selected on the basis of profit rather than on the basis of quality.

The development of the QAA is positive and can only improve the assessment of quality in comparison to today where there are no mechanisms which are used for the direct assessment of quality of advocacy. We assume that the intention of the QAA will be to ensure that advocacy services are maintained at a suitable level of quality.

---

<sup>114</sup> Legal Services Commission, Quality Assurance for Advocates, Working with the professions to deliver a framework for better advocacy, A Discussion Paper, February 2010.

### 3.6.2. Best value tendering

Proposals for piloting “best value tendering” were put on hold at the end of 2009. Outline proposals were subsequently put forward by the MoJ in March 2010 with detailed options expected over the summer of 2010. Given that detailed proposals are not currently available it is not possible to assess how they will impact the conclusions of this report. It was also announced in March 2010 that the LSC would be moved to an Executive Agency under the MoJ.<sup>115</sup> The Government has stated that this will lead to tighter financial control over the LSC budget.

In the light of these announcements it may be necessary for the LSB to consider the impact of any revised proposals for best value tendering once they are available and to assess and how they may interact with the competitive dynamics which have been examined in this report.

### 3.6.3. Revisions to the advocate graduated fee scheme

The MoJ has indicated that it intends to reduce the fees payable through the AGFS through.<sup>116</sup>

- A staged reduction in fees of 4.5% each year for three years (a total reduction of 13.5% by year three); and
- An extension of the AGFS to cover cases lasting up to 60 days thereby removing cases of 41-60 days from the VHCC and bringing them under the AGFS.

If these changes are applied, they would (over time) broadly reverse the changes in 2007 which increased advocacy fees by around 16%.

The revisions to the AGFS and LGFS led to advocacy becoming relatively more profitable compared to litigation especially for cases conducted by junior advocates.<sup>117</sup> This led to an increase in the number of solicitor advocates obtaining their higher rights and an increase in the extent to which they conducted advocacy work. It is unclear whether any reduction in the AGFS will reverse the trend for solicitor advocates to conduct advocacy or whether, having obtained their higher rights, such individuals will continue to seek to conduct advocacy. Solicitor firms have indicated that, much as they do today, they will assess the relative profitability of conducting advocacy in-house compared to instructing external advocates.

However, it seems likely that the scale of reductions in fees will impact the scale of fee sharing arrangements that are in place i.e. substitute advocates may no longer be

---

115 Legal Services Commission, Review of legal aid delivery and governance published, 3 March 2010.

116 Ministry of Justice, Legal Aid: Reforming Advocates Graduated Fees, 16 December 2009 and Ministry of Justice, Legal Aid: Reforming Advocates Graduated Fees and Very High Cost (Crime) Cases 2010, April 2010.

117 One of the reasons that the MoJ has chosen to seek savings for longer cases (rather than cut the AGFS by a greater level) is to reduce the impact on junior advocates. Source: Ministry of Justice, Legal Aid: Reforming Advocates Graduated Fees, 16 December 2009.

prepared to enter into arrangements where they receive 80% of the fees that they otherwise would have done.<sup>118</sup>

#### 3.6.4. One-case-one-fee

The Carter Review anticipated a move towards “one-case-one-fee” for Crown Court cases in which there would be a single fee paid to a firm (presumed at present to be a solicitor firm due to the limitation on barristers from having direct access to clients) out of which that firm would be responsible for paying any other service providers. We understand that there are two primary drivers for this:

- Reduction in administrative costs – in the same way that the AGFS was aimed at reducing the administrative costs for the LSC in processing fee claims by having a single point of contact for advocacy services, one-case-one-fee would take this a step further. The LSC would move from paying a single advocate and a single litigator for each case to paying a single firm, presumably therefore reducing the number of payments by half.<sup>119</sup>
- Increase in efficiency – it seems possible that there could be efficiency gains from either the same firm conducting both litigation and advocacy services, or improving the interface between the litigator and the advocate. At present we understand that advocates express concern that the case notes which they are given are not always provided by the litigator to a sufficient standard, similarly litigators indicate concern that advocates may not always be sufficiently prepared for court appearances. Moving to a situation where one firm is responsible for all aspects of the activities and where they can profit from organising things in a more efficient manner would be expected to lead to efficiency gains being made.

We note that the Carter Review indicated that decisions regarding moving to a single graduated fee for all defence services would be best decided after suppliers had time to adjust to the revised graduated fee schemes and had “new opportunities to structure their services following implementation of wider legal services reforms”. This suggests that the intention of a movement to a single graduated fee scheme was that it should arise after alternative business structures (see below) have been implemented rather than before.<sup>120</sup>

As yet there are no concrete proposals related to one-case-one-fee, but once proposals become clear it will be important to consider the following:

- Whether a single fee scheme removes the incentive for firms to appoint in-house advocates as the Instructed Advocate where there is no intention to conduct significant parts of the advocacy work. Movement to a single fee could place all of the fees in the control of the firm with the initial client contact, hence firms may not need to seek to be the Instructed Advocate in order to have this control;

---

118 Certain cases under the Bar Protocol may also become less attractive for advocates. For example, cases where large numbers of appearances mean that substitute advocates who conduct one appearance receive less than they would receive in cases where there are only a small number of total appearances.

119 Although it would need to be assessed whether the administrative costs associated to this were significant or whether any costs associated to checking the claims differed.

120 Legal Aid: A market-based approach to reform, Lord Carter’s Review of Legal Aid Procurement, July 2006.

- Whether a single fee scheme places additional bargaining power in the control of the firm receiving the single fee or whether the bargaining power can already be fully exploited through fee sharing arrangements related to the AGFS; and
- Whether a single fee scheme would continue to specify fees for different components of criminal defence work and whether the current Bar Protocol would be of relevance under a single fee regime. Currently there is no evidence that fee sharing arrangements under the Bar Protocol give rise to concerns about quality. A movement away from this position could lead to an increase in the number of cases in which there might be concerns regarding quality although this will be highly dependent on whether a QAA scheme is in place in advance of one-case-one-fee.

As yet, proposals regarding any single fee are not clear and therefore it is not possible to assess the impact and how it would affect fee sharing arrangements and the issues described within this report.

### 3.6.5. Alternative business structures

Moving to a situation in which barrister-run firms (or chambers) are able to directly access clients (or have agency arrangements with solicitors who access these clients specifically on behalf of the chambers) clearly changes the balance between barristers and solicitors as barristers would have similar access to clients as litigators. As such barristers operating in these models would not be dependent on referrals from external solicitor firms as they are now.

From an economic perspective this represents a similar structure as is currently observed today with solicitor firms that employ barristers. Interviewees agreed that barrister-led firms employing solicitors would broadly operate in the same way as solicitor-led firms employing barristers.<sup>121</sup>

The integration of the litigator role and the advocacy role within the same organisation reduces the extent to which fee sharing arrangements are used and increases the extent to which in-house advocates are used. In as far as concerns are raised about fee sharing arrangements, integration would have the effect of removing such concerns because arrangements would be internalised within the same organisation. However, we note that the potential detriment regarding fee sharing arrangements, namely that a focus on profitability causes advocates to be appointed for cases beyond their competence is the same potential detriment that arises through the use of in-house advocates.<sup>122</sup>

---

121 It is possible that if barristers seek to maintain their self-employed status through chambers (which enables them to work on cases against other barristers in the same chambers), any arrangements between barristers and any centralised litigator activity may be more complex than those seen within firms in which advocates are employed (rather than self-employed). This may require agency arrangements or other arrangements that set out fee sharing arrangements within this structure.

122 It is unclear whether the desire to protect a firm's reputation would be relatively more successful in maintaining quality for in-house advocates compared to external advocates, but as noted earlier, concerns are raised about quality in both circumstances and there is currently no QAA scheme in place to be able to draw conclusions on this.



### **3.7. Policy options**

#### **3.7.1. Allowing referral fees for barristers**

One potential policy option for consideration is that referral fees could be allowed for barristers in order that they are not disadvantaged in comparison to solicitors in competing for work on the basis of referral fees.

In criminal advocacy we note that referral fees are not paid as they are currently banned under the LSC's contract, hence there would be no impact in this area from allowing referral fees. Furthermore, interviews with barristers and their representatives have shown no support for allowing barristers to receive or pay referral fees.

#### **3.7.2. Banning referral fees**

##### *Banning referral fees*

Referral fees are not currently paid in the area of criminal advocacy, hence banning referral fees would not have any impact in this area. As noted in section 1.2, fee sharing arrangements can replicate the effects of referral fees hence even if referral fees were in place, a ban of referral fees while allowing fee sharing arrangements would not be effective in altering market dynamics.

##### *Banning fee sharing arrangements*

Fee sharing arrangements are in place which can replicate the economic effect of referral fees. Concerns have been identified regarding the operation of fee sharing arrangements in criminal advocacy as a focus on profitability may cause advocates to be appointed for cases beyond their competency. Banning such arrangements could therefore reduce the extent to which this is a concern.

However, despite this, there is no support among any interviews for banning fee sharing arrangements altogether. Interviewees have indicated that the current approach to scheduling in the Crown Court in which timetables for court are only published in the late afternoon the day before along with uncertainty regarding the length of time that cases will take mean that flexibility is required to use Substitute Advocates. Under the current AGFS, banning fee sharing arrangements would imply banning the use of Substitute Advocates. Removing the ability to use Substitute Advocates is considered to be disproportionate to the potential detriment arising from the use of fee sharing arrangements.

##### *Banning non-Protocol fee sharing arrangements*

As noted above, no concerns have been expressed that the operation of the Bar Protocol is leading to a reduction in the quality of services undertaken. We therefore also consider whether banning all non-Protocol fee sharing arrangements would address the concerns raised regarding quality.

First, we consider the implications for using in-house advocates where concerns were identified that a focus on profitability was causing advocates to be appointed for cases beyond their competency. If the AGFS causes an incentive to conduct the whole case in-

house, then this occurs irrespective of fee sharing arrangements and therefore banning non-Protocol arrangements has no effect on these incentives.<sup>123</sup>

Second, we consider the implications for the trade-off between using in-house advocates and using an external advocate. Some firms who currently instruct external advocates under non-Protocol arrangements may instead choose to employ additional in-house advocates. Given the lack of evidence currently available on the quality of advocacy it is not possible to assess whether quality would:

- increase because of the removal of incentives to choose one external advocate over another on the basis of fee sharing arrangements; or
- decrease because of the incentive to employ additional in-house advocates.

Third, we consider the implications for using external advocates where concerns were identified that fee sharing arrangements caused a focus on profitability which meant that advocates were appointed for cases beyond their competency. Banning non-Protocol arrangements would have two effects here:

- It would place solicitors and barristers on a level playing field (although this could also be achieved through removing the Bar Protocol); and
- It would remove price from the selection process leaving the choice to be made primarily on the basis of quality.<sup>124</sup>

In the absence of a QAA scheme, banning non-Protocol fee sharing arrangements would therefore be expected to bring benefits from an increase in quality compared to today. It would reduce the risk that high quality efficient advocates are undermined by low quality advocates.

It should be noted that this position holds while there is no alternative method of assessing quality. Once a robust QAA scheme is in place that enables quality to be assessed, it is assumed that such a scheme would ensure quality is maintained. At this stage, allowing price competition to arise would be beneficial. Indeed this would drive efficiency enabling efficient advocates to gain at the expense of inefficient advocates with the QAA scheme protecting the level of quality. We note that this is also the premise behind many of the changes proposed in the Carter Review.

Finally, we note that one disadvantage from forcing all firms to follow the Bar Protocol relates to the potential for information on fee sharing to be used as an indicator of appropriate market prices, although the value of this information is mixed since fee sharing arrangements may be adversely impacting quality. In addition, the value of this information may be limited if future prices will be set with reference to best value tendering rather than through administrative price setting.

---

123 If the AGFS causes an incentive to keep in-house the cases where clients are expected to plead guilty, then this also occurs irrespective of fee sharing arrangements and therefore banning non-Protocol arrangements has no effect. (It should be recalled that there was no detriment identified from this since last minute preparation is common for PCMHs.)

124 It remains possible that the choice is made on the basis of "other referral arrangements" considered in section 3.4.7, but broadly returns the decision making-process to the same factors as that before the revised AGFS where fewer concerns about quality were raised. Hence the removal of price from the decision process implies that quality would be expected to play a greater role in the selection process.

### 3.7.3. Capping referral fees

Since referral fees are not currently paid, capping referral fees is not a relevant policy option in the area of criminal advocacy.

### 3.7.4. Disclosure to clients

There was no support from any quarter regarding the suggestion that information on fee sharing arrangements should be disclosed to the end client in the case of criminal advocacy. It was noted that the accused are not commonly not paying for either the litigation or the advocacy service and therefore revealing information regarding the sharing of fees would not be an aid in terms of seeking to reduce the level of fees as might arise in cases where the end client was paying for services.

It was also noted by some interviewees that if some clients attempted to negotiate with the solicitor to receive some of the fees then, if the client was found guilty, this could be considered to be gaining from the proceeds of crime and was not a desirable outcome.

### 3.7.5. Disclosure to approved regulators

Disclosure of information related to fee sharing arrangements could be made to the BSB or SRA and, in common with other markets, this could enable them to identify outliers in these arrangements. However, given the position of the LSC both pays for criminal advocacy and also sets the prices for different activities within the legal aid system we focus on whether disclosure of information to the LSC would be of use.

In theory, the primary advantage of requiring disclosure of information on fee sharing arrangements would be that the LSC would be able to identify whether there were activities where prices were set “too high” and others where they are set “too low” in order to take this information into account when revising fees in the future. However we note that:

- Information on fee-sharing alone would be insufficient to assess whether relative prices are appropriate without additional information on the work that had been conducted by different advocates. For example even though a Substitute Advocate may conduct the PCMH or trial, the Instructed Advocate may have provided direction on this;
- Given the concerns that fee sharing arrangements are leading to a reduction in the quality of advocacy, disclosure of information related to fee sharing is of more value once the QAA scheme is in place and quality standards are maintained. Before the QAA, and in the absence of alternative methods to assess quality, it will be unclear whether variation in fee sharing arrangements reflects issues of efficiency and price competition or variation in quality;
- As with many regulated markets, once it is known that a particular indicator will be used as a method of setting prices in future this changes the incentives for firms to reveal accurate information where this might lead to pressure for prices to fall; and
- Disclosure of this information to the LSC operates in the opposite direction to recent moves by the LSC which have been to reduce the level of administrative costs associated to the operation of the AGFS.

Overall it does not appear as though disclosure of information to the LSC would be of immediate benefit. Furthermore, given the number of Crown Court cases (120,000) and

the complexity in the number of different elements which affect fees under the AGFS, this would entail gathering substantial volumes of information and considerable costs. We also note that if future prices will be set with reference to best value tendering rather than through administrative price setting by the LSC then the value of gathering this information will also be reduced.

The large number of cases and the complexity of the different elements which affect fees under the AGFS also limits the extent to which it would be feasible, or useful, to publish information on fee sharing arrangements to allow for more informed negotiation between parties.

## 4. PERSONAL INJURY

In this chapter we consider the role of referral fees and referral arrangements in the area of personal injury cases. Personal injury is an area of law where referral fees are commonly paid. Indeed, The Law Society's Practice Standards Unit (PSU) identified that personal injury was the area in which more firms disclosed to The Law Society the presence of referral arrangements than any other area of law.<sup>125</sup> It was therefore agreed with the LSB that this would be one of the markets that we examined during the research.

There are a variety of different types of personal injury that can arise although it is estimated that around three-quarters of personal injury claims relate to the motor area in respect of Road Traffic Accidents (RTAs).<sup>126</sup> We therefore mainly focus on this area of personal injury claims although we also consider employer liability which is the second largest area of claims in the personal injury market.

**Table 10: Personal injury market 2008**

Market	Number of claims registered	Value of claims paid
Motor	625,000	£3-4 billion
Employer Liability	87,000	£1.3 billion

Source: Datamonitor, "UK Personal Injury Litigation 2009", December 2009, p10. Data for new claims refers to period April 2008 – March 2009. Estimates of claims by Datamonitor are based on information from CRU, ABI, IUA.

### 4.1. Demand for legal services

#### 4.1.1. Number of accidents

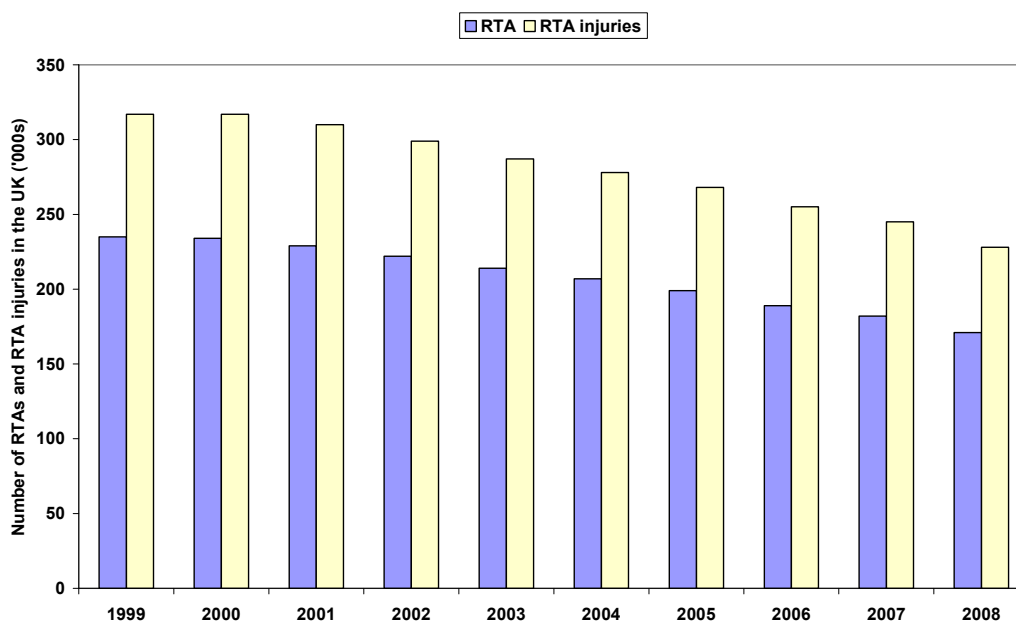
One of the key elements that drives the demand for legal services in the personal injury market is the number of RTAs that occurs. Figure 16 below is based on accidents which are reported to the police. This shows that the number of RTAs and associated injuries has fallen over time.

---

<sup>125</sup> The Law Society, Practice Standard Unit, Report on Themed Visits – Referral Fees, July 2006.

<sup>126</sup> Based on the number of claims in 2008-2009 for motor, employers' liability, public and product liability and clinical negligence as cited in Datamonitor, UK Personal Injury Litigation 2009, December 2009.

**Figure 16: RTAs and RTA injuries**



Source: Department for Transport, "Transport Statistics Great Britain 2009 Edition", November 2009, p145. RTA injuries is the sum of "seriously" and "slightly" injured.

The police data, on which Figure 16 is based, is considered by the Department for Transport (DfT) to be the most reliable source of information on road casualties for monitoring trends over time. However, the DfT has also stated that the number of RTAs reported to the police significantly understates the number of accidents. While the downward trend in the number of RTAs is considered a true reflection of trends, the DfT has estimated that the actual number of RTAs in 2008 was around 800,000.<sup>127</sup>

In contrast to the decline of RTAs and RTA injuries, motor personal injury claims have been increasing from 400,000 in 2000-01 to 625,000 in 2008-09. We will discuss this trend in more detail in Section 4.5.

#### 4.1.2. Choice of provider

Unusually for most markets, the price of legal services does not play a strong role in the selection of legal services provider by consumers because of the prevalence of "no-win-no-fee" agreements. This is discussed in more detail in section 4.3 below.

Instead of selecting on the basis of price, evidence from interviews indicates that most consumers selected their provider on the basis of marketing by different providers (including introducers). In addition to marketing, interviewees stated that the role of recommendations from family and friends was also thought to be an important method of selecting a legal provider for personal injury claims.

This is consistent with evidence found in research for the LSB's Consumer Panel.<sup>128</sup> This research also found that, for personal injury claims, consumers searched online to

---

127 Department for Transport, "Reported Road Casualties Great Britain: 2008 Annual Report", September 2009, p58.

128 Referral Arrangements Research, Report prepared by Vanilla Research, March 2010.

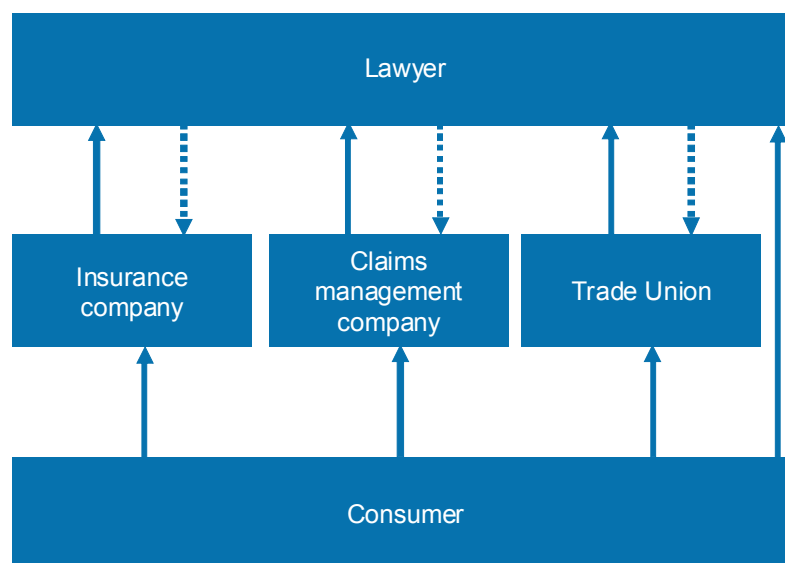
find a lawyer with relevant expertise. Some individuals were found to shop around for a lawyer although for personal injury this tended to be to ensure that they found someone they were comfortable with. This research also found that there were low levels of price comparison for personal injury claimants because consumers using no-win-no-fee arrangements did not care about costs as they would be passed onto the other party.

## 4.2. Supply of legal services

According to The Law Society, there are currently 6,242 law firms in England and Wales conducting business in the field of personal injury.<sup>129</sup>

As highlighted in Figure 17, there are a number of different methods through which consumers can access lawyers and by which lawyers supply their services to consumers. This can include consumers going direct to lawyers or consumers going via an introducer in order to access a lawyer. The most common introducers which were consistently highlighted during the interviews were claims management companies (CMCs) and insurance companies as well as trade unions for employer liability cases. Some solicitor firms may be operating as introducers to other solicitors – these firms are sometimes referred to as “solicitor collectives”. We examine these firms alongside CMCs as the economic incentives facing these companies operate in similar ways to those of the CMCs.

**Figure 17: Supply of legal services in personal injury**



Source: CRA.

Where lawyers supply their services via an introducer, referral fees are commonly paid, as indicated by the dotted lines in Figure 17 above and introducers will typically have a panel of lawyers to whom they refer clients. From the supply side, lawyers will need to determine whether it is more effective to access clients directly (and thereby bear the costs of marketing and other associated costs) or through an introducer (and pay a referral fee).

---

129

Information taken from The Law Society database as of March 2010.  
<http://www.lawsociety.org.uk/choosingandusing/findasolicitor/action=lawfirmsearch.law>

Interview evidence has suggested that over the last ten to fifteen years, the proportion of personal injury business that comes through the direct channel has reduced with the vast majority of motor personal injury involving introducers and the payment of referral fees.

#### 4.2.1. Claims management companies

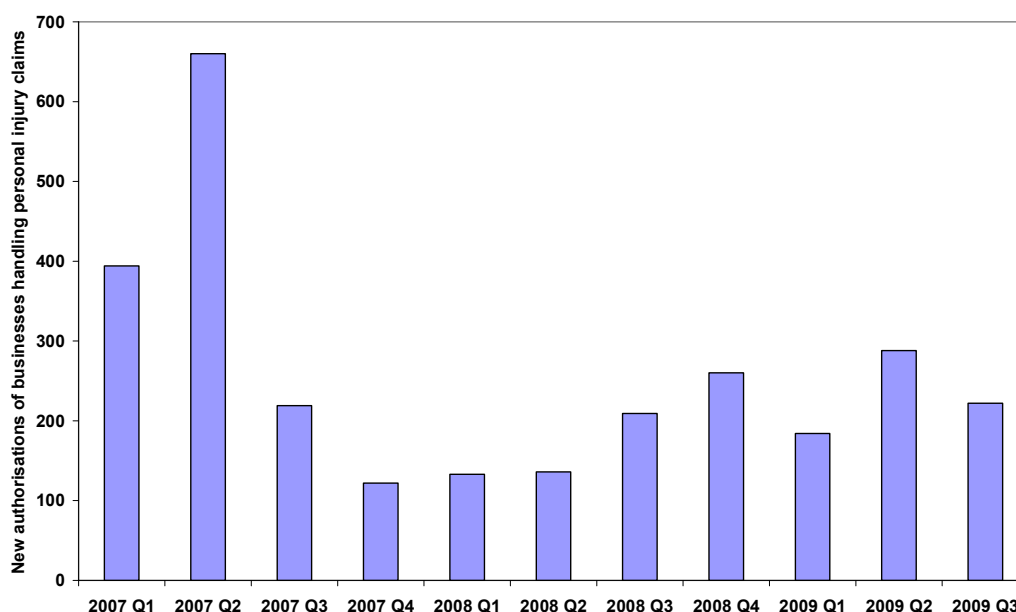
##### *Number of CMCs*

There are currently over 2,500 CMCs which are authorised by the Claims Management Regulation Unit of the Ministry of Justice (re refer to this as the Claims Management Regulator or CMR).<sup>130</sup> It is not possible to identify which of these are active in the motor market as opposed to other areas.

The number of CMCs has increased substantially from 1,128 authorised CMCs in 2007 when regulation of CMCs began.<sup>131</sup> Evidence from discussions at the workshop organised by the CMR have indicated that the high numbers of new entrants in early 2007 reflect firms coming under the regulation although the increase in the number of CMCs since 2007 is a genuine reflection of new entry to the sector rather than being driven by increased compliance with regulation.

The workshop discussion also indicated that new entrants were typically small CMCs who entered the market and spin-off companies who may be expanding the areas of claims in which they are active. Figure 18 below shows the number of new entrants over time.

**Figure 18: New authorisations of businesses handling personal injury claims**



Source: Information provided to CRA by CMR.

---

130 Based on information from the Claims Management Regulation Unit's database accessed on 26 March 2010. <https://www.claimsregulation.gov.uk/search.aspx>

131 Based on information for June 2007 provided to CRA by Claims Management Regulation Unit.



### *CMC business models*

Evidence from interviews has identified that there are a large number of different business models which operate in this area. Businesses vary according to:

- Ownership (and regulator) – some introducers are owned by and regulated as solicitors. (Since they act as introducers to other solicitor businesses and can act in similar ways to firms that are regulated as a CMC we include these in this section.) Other firms have non-solicitor ownership and are regulated by the CMR.
- Extent of service – some introducers provide a pure referral arrangement in which they simply take the contact details of the client and then pass this on to a solicitor, while other firms will conduct nearly all of the pre-litigation work themselves before passing on the case to a solicitor. Some CMCs will act as a “one stop shop” in offering services such as vehicle repair through credit hire/repair services, offering to arrange for medical experts, compiling accident reports etc.
- Business focus – as well as firms which focus purely on issues to do with claims management there is a vast array of other firms act as introducers including: car hire companies; accident recovery firms, vehicle repair firms etc (in some cases these firms will act as introducers to CMCs i.e. they are introducers to introducers).

Since firms that primarily focus on areas of business other than claims management typically represent reasonably low volumes of introductions we do not consider these other firms further.

### *Marketing and competition for customers*

All introducers (including solicitor collectives) have confirmed that the main method by which introducers compete for new customers is through marketing. CMCs believe that they have an advantage in marketing in comparison to lawyers which means they are able to attract customers more effectively than many law firms operating on their own.

There are fixed costs associated with conducting marketing and developing a brand which customers recognise. Hence it is primarily large firms who undertake large scale marketing efforts for this to be worthwhile. Some of the largest firms see the marketing role as their primary activity and spend significant resources examining the effectiveness of marketing spending and the response rate of different marketing channels.

The level of marketing expenditure by CMCs is estimated as being around £35-40 million per year between 2005 and 2008. The effect of economic conditions and the lack of a longer time series means that it is not possible to identify whether there has been a trend towards more marketing expenditure over time.<sup>132</sup>

Brand awareness and the availability of freephone numbers were thought to be important elements of competition. In addition, some firms seek to compete for customers through offering “100% compensation” guarantees. Law firms operating with introducers who advertise on this basis must agree to not charge the customer sums of money which would come out of the customer’s damages claim.

As explained further in section 4.4, referral fees were seen as the method by which this marketing was paid for.

---

132 Datamonitor, "UK Personal Injury Litigation 2009", December 2009, p47.

#### 4.2.2. Insurance companies

There are around 60 insurance companies who offer motor insurance in the UK although the top five companies are estimated to have a market share of around 70%.<sup>133</sup> These companies are primarily focused on providing motor insurance policies to their customers although they also act as introducers to law firms in the event of a claim.

It is important to note that the characteristics of the motor insurance market means that there are not thought to be any problems in terms of competition. In particular, consumers make repeat purchases each year, comparison websites are available which make shopping around straightforward, and no claims bonuses indicate that insurance companies are concerned to compete for existing customers who might otherwise switch to a different provider as well as for new customers.

During interviews insurance companies agreed that their role as introducer is purely dependant on their role as the provider of the motor insurance policy i.e. they are not seeking to directly attract personal injury customers. Clients will typically proactively contact their insurance company to tell them that they have been in an accident because of the insurance related to vehicle damage. In the course of this discussion, insurers will identify whether there are any potential personal injury claims and if so they will, with the client's consent, refer the case to a law firm. The income stream associated to these referrals plays an important role in encouraging insurers to pass customers on to law firms.

Under European law, consumers must be able to choose their own lawyer in any legal proceedings.<sup>134</sup> However, it seems to be the case that insurers who have provided legal expenses insurance (see section 4.3.3) typically interpret this as limiting the freedom of choice to after the issue of proceedings and that before this stage they may require consumers to use a solicitor from their own panel. Evidence from interviews has found that very few customers decide to choose an alternative solicitor at the point that proceedings are issued.

#### 4.2.3. Trade unions

There are just under 200 different trade unions in the UK with a total of 7.7 million members although the top 8 unions have a membership of some 5.6 million.<sup>135</sup> One of the key roles of a union is to offer services to their members in relation to employment conditions. For this reason, union members may well contact their union if they have an injury for which the employer may be liable and unions see it as one of their responsibilities to assist their members in these cases. Trade unions will also provide similar services on behalf of family members as well as in other types of personal injury cases such as motor insurance.

As part of this trade unions will refer their members to particular firms of solicitors. Some unions may have a variety of different solicitors that they refer members to some of which

---

133 ABI and SynThesis statistics.

134 European Commission, Council Directive 87/344/EEC of 22 June 1987 on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance.

135 Certification Office for Trade Unions and Employers' Associations, Annual Report of the Certification Officer 2008-2009, July 2009.

may be based locally to where the member is in order to enable the possibility of face to face meetings. Other unions primarily use one firm of solicitors.

### 4.3. Price of legal services

There are a number of different elements which affect the price of legal services in the personal injury market. We consider each of these in turn.

#### 4.3.1. Conditional fee agreements

Conditional fee agreements (CFAs) have been allowed since 1995 and are now common across the whole of the personal injury market in respect of claimants. The most common description of these arrangements is “no-win-no-fee”. Under these arrangements:

- If the case is lost, the consumer does not bear any of the costs of his own lawyer. The opponent’s legal costs and any disbursements would typically be covered through legal expense insurance (see section 4.3.3).
- If the case is won, the claimant’s lawyer will recover the cost of legal fees from the defendant. In the majority of motor claims the level of costs that can be recovered is regulated (see section 4.3.2). It is possible that other costs may be incurred by the consumer depending on the arrangements with lawyers or introducers – some, but not all, lawyers and introducers, will guarantee that the consumer keeps 100% of their compensation.

Other fees such as for disbursements could also be charged. It is possible that additional fees such as administrative fees will be payable although only one major CMC has been identified as doing this.

#### 4.3.2. Prescribed legal costs

Under the Civil Procedure Rules (CPR), the legal costs that can be recovered for motor cases are prescribed through the following:

- Predictable costs regime – this applies for low value motor claims which are settled outside court; and
- Fast track trial costs regime - this applies for low value motor claims which go to trial.<sup>136</sup>

It should be noted that the majority of motor claims are settled outside the court. The preliminary Jackson report finds that in about 90% of motor claims there is no dispute on liability.<sup>137</sup>

#### *Predictable costs in low value RTA claims settled outside court*

When the claim is settled before the issue of proceedings, the CPR sets out the costs that are recoverable where the total damages including personal injury and property damage resulted from a RTA do not exceed £10,000. The amount of recoverable “base costs” is

---

<sup>136</sup> In addition to these there is a small claims process for claims of no more than £1,000. The legal costs in the small claims track are not normally recoverable and the claimant has to fund the costs by, hence many claimants choose to pursue their claims as a litigant-in-person without legal assistance. Hence we do not consider this further.

<sup>137</sup> Rupert Jackson, “Review of Civil Litigation Costs: Preliminary Report”, May 2009, Volume one, p108.

prescribed by a formula which provides that the amount of fixed recoverable costs is the total of:

- (a) £800;
- (b) 20% of the damages agreed up to £5,000; and
- (c) 15% of the damages agreed between £5,000 and £10,000.<sup>138</sup>

In addition, where a CFA is in place, success fees of 12.5% of the base cost are applied. Disbursements (i.e. expenses incurred in the conduct of the case) can also be included in the recoverable costs.

#### ***Fast track trial costs***

Most claims which go to court are in the fast track where the trial can be concluded within one day. The upper limit of fast track claims was raised from £15,000 to £25,000 in April 2009.<sup>139</sup> Table 11 sets out the costs that can be awarded.

**Table 11: Amount of fast track trial costs**

<b>Value of the claim</b>	<b>Amount of fast track trial costs which the court may award</b>
No more than £3,000	£485
More than £3,000 but not more than £10,000	£690
More than £10,000 but not more than £15,000	£1,035
For proceedings issued on or after 6th April 2009, more than £15,000 but not more than £25,000	£1,650

Source: Part 46 of CPR. [http://www.justice.gov.uk/civil/procrules\\_fin/contents/parts/part46.htm](http://www.justice.gov.uk/civil/procrules_fin/contents/parts/part46.htm)

Success fees also apply in fast track trials where the allowable success fee is:

- (a) 100% where the claim concludes at trial; or
- (b) 12.5% where the claim concludes before trial.

Evidence provided by a substantial firm of claimant personal injury solicitors has indicated that 92% of all personal injury cases which they undertake fall within the bracket £1,000 to £25,000 with the majority below £5,000. The preliminary Jackson report estimates that at least 80% of all personal injury claims are below £5,000.<sup>140</sup>

#### **4.3.3. Guideline hourly rates**

Unlike motor claims most of which are settled under prescribed cost schemes, the legal costs for claims in employer liability are calculated on an hourly basis following the guideline hourly rates suggested by the Advisory Committee on Civil Costs (ACCC).

---

138 Civil Procedure Rules, Part 45. [http://www.justice.gov.uk/civil/procrules\\_fin/contents/parts/part45.htm#IDAKZI5B](http://www.justice.gov.uk/civil/procrules_fin/contents/parts/part45.htm#IDAKZI5B)

139 For claims above £25,000 the case will be operated through the "multi-track" process where there are no fixed or prescribed costs associated with legal services.

140 Rupert Jackson, "Review of Civil Litigation Costs: Preliminary Report", May 2009, Volume one, p108.

The rates are based on data collected by the ACCC through a survey of solicitors and other interested parties as well as through written and oral evidence provided by representatives of the main interest groups and others. Over time rates are often adjusted to reflect average earnings growth. The rates vary according to the level of experience of the lawyer and their location (with London having higher rates than other areas).

During the settlement of claims, defendants can negotiate with claimants over the number of hours to be included in the calculation of legal fees for the claimant's lawyer. If they can not reach an agreement on the amount of legal fees, they can refer the case to the court which would decide the amount of fees that was considered reasonable.

#### **4.3.4. Legal expense insurance**

One of the other factors impacting the price of legal services is the availability of legal expense insurance. There are two types of insurance policy which are relevant:

- Before-the-event (BTE) insurance. It is estimated that around 23 million adults have BTE insurance as an add-on to motor or household insurance and evidence from interviewees suggests that around 80% of motor insurance policyholders have BTE insurance.<sup>141</sup> The premium for BTE insurance as an add-on to motor insurance policies is in the region of £20; and
- After-the-event (ATE) insurance. Unlike BTE, ATE insurance is taken out by solicitors after an accident has already happened. It covers the policyholder against the possible legal costs from the opponent in the event of losing the case and sometimes covers the policyholder's own legal costs and disbursements if they are not recovered from the other side. It is important to note that changes since 2000 allowed ATE insurance premiums to be included as a disbursement and therefore to be recovered from the other side of the case is won. If the case is lost, the solicitor will receive no payment for their work and the insurer will pay the legal costs of the other side, any disbursements and will also forego the ATE premium. ATE insurance premiums are estimated as ranging from £250 to £600 depending on business model and the stages of legal process.<sup>142</sup>

There is evidence that the legal expense insurance market has been growing over the time with the value of premiums increasing from around £450 million in 2005 to £550 million in 2008.<sup>143</sup>

#### **4.4. Role of referral fees in competition for legal services**

In this section we examine some of the ways in which referral fees are impacting the way that competition arises in this market. Section 4.5 sets out whether any of these issues lead to consumer detriment.

Before setting out the role of referral fees in the competitive process it is useful to understand the situation before referral fees were allowed in 2004 which is considered in section 4.4.1.

---

141 Rupert Jackson, "Review of Civil Litigation Costs: Preliminary Report", May 2009, Volume one, p151-2.

142 Rupert Jackson, "Review of Civil Litigation Costs: Preliminary Report", May 2009, Volume one, p157.

143 Datamonitor, "UK Personal Injury Litigation 2009", December 2009.

#### 4.4.1. Pre-2004

Before 2004, lawyers were not allowed to either pay or receive referral fees. The evidence from interviews has been consistent in identifying that despite the ban on referral fees, referral arrangements were in place which had similar effects. There were a variety of approaches which were cited during interviews including:

- Charges for insurance policies (set at a level in excess of the true cost of providing any insurance arrangements);
- Marketing fees; and
- Administrative fees.

Rather than paying fees under a different guise, an alternative was for lawyers to reduce fees for legal services for other activities. This was particularly common for lawyers working with insurance companies and trade unions. For example, when working with insurance companies, lawyers may conduct defendant work at low prices or may be required to accept a number of “bent metal” cases (i.e. those in which there is only vehicle damage and no personal injury case to pursue) in return for referrals of personal injury claims.

Similarly when working with trade unions, in return for receiving referrals lawyers may undertake some of the trade union advice for free. Alternatively they may have provided services such as training and education for free or sponsored events put on by trade unions as another way of transferring funds to the union in return for referrals. In addition, some law firms will provide services directly for the trade union members such as having access to low price will writing services or obtaining free legal advice.

Overall the evidence from interviews was clear that before 2004, firms had “got around” previous restrictions relating to referral fees. No interviewee disputed this observation.<sup>144</sup>

#### 4.4.2. Choice of lawyer determined by introducers based on referral fees

The presence of introducers has the effect of leading competition among legal services providers to be focused around access to introducers. (Although all lawyers always retain the ability to seek to compete against introducers directly for the client.)

It should be noted that all introducers stressed the fact that referral fees were not the only part of the selection criteria for entry to their list or panel of lawyers. However, it is clear that introducers refer clients to particular law firms on the basis of referral fees. In simplest terms, law firms who are unwilling to provide some form of benefit (usually as referral fees although sometimes in the form of the provision of legal services for below market fees) will not be allowed to participate in any of the introducer models. There are a range of models through which this occurs:

---

<sup>144</sup> As we note later, this does not necessarily imply that alternative referral arrangements were able to perfectly replicate the effect of referral fees.

- Solicitor run firms are more likely than other CMCs to see themselves as a collective organisation in which marketing is undertaken centrally. Marketing budgets may be set in advance with individual law firms making contributions in proportion to the number of cases they receive. Without making a contribution to the marketing budget, firms would not be included in the collective. Firms operating through this type of arrangement consider that members of the collective are paying their share of marketing costs rather than paying a referral fee although we note that the economic effect of this is equivalent to the referral fees paid in other introducer models.
- Other CMCs are more likely to operate a pure referral fee model in which firms only enter an approved list or panel if they pay the required referral fee. Some of these firms have seen the number of firms on their panel grow as the CMCs themselves have expanded over time both numerically and in terms of the different types of claims that they handle.
- Insurance companies will typically have a (small) panel of large law firms to whom they refer claims. While there will be quality standards that need to be met (see section 4.5.1) the willingness to pay referral fees plays an important role in determining who will be on the panel.
- Trade unions have a mixture of arrangements in place. Some unions require referral fees to be paid. Other trade unions expect law firms to provide other services either below cost or for free in the same manner as was seen before 2004.

Although firms may seek to describe themselves in different ways, in all cases if referral fees (or their equivalent) are not paid, lawyers do not receive any work from these introducers. Hence only those lawyers who are willing to pay referral fees will receive referrals from introducers.

The prevalence of referral fees is also supported by evidence from a survey for APIL which finds that:

- 80% of firms who carry out personal injury work linked to legal expense insurance panels pay referral fees and/or have a fee sharing agreement; and
- 49% of firms not linked to legal expense insurance panels still pay referral fees or have fee sharing arrangements.<sup>145</sup>

It is likely that estimates on the basis of the number of firms are likely to understate the proportion of claims that involve referral fees or fee sharing arrangements. Interview evidence is clear that large solicitor firms operating in the personal injury market pay referral fees, whereas commonly it is smaller solicitors who are unwilling to pay such fees. This is also supported by research by The Law Society which finds that on average the number of personal injury cases conducted each year by firms paying referral fees was one hundred times that of those which do not pay referral fees.<sup>146</sup> Combined, this indicates that large firms conducting large volumes of work are more likely to pay referral fees than small firms conducting small volumes of personal injury work.

---

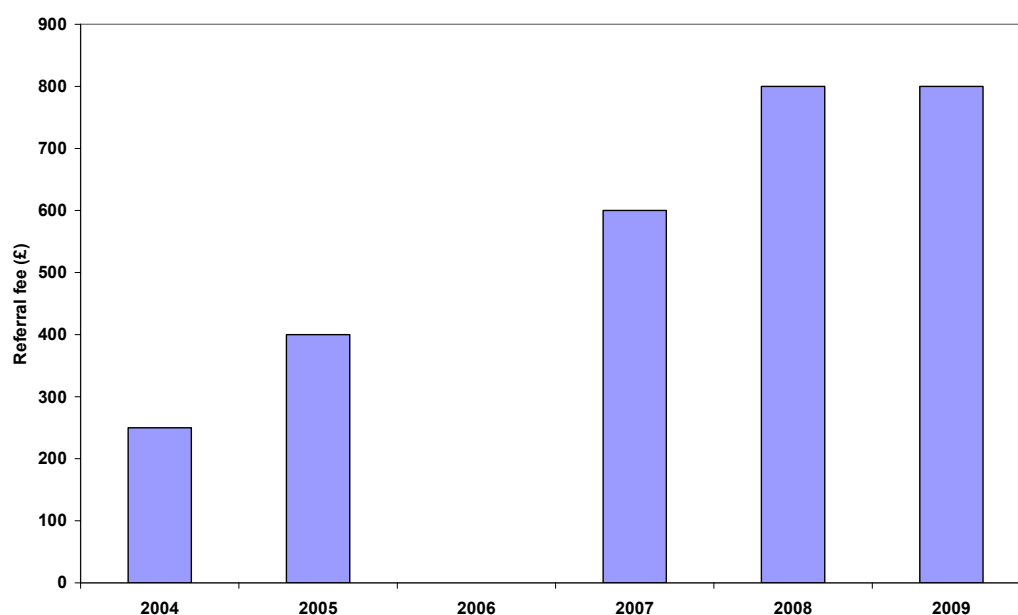
145 APIL, APIL members' views on LEI panels and payment for referrals, May 2007.

146 Moulton Hall, "Referral arrangements and legal services research report – Prepared for the Strategic Unit of the Law Society", June 2007, p3.

#### 4.4.3. Competition over introducers has led to an increase in referral fees

There is strong evidence that the overall level of referral fees in the market has increased over time as shown in Figure 19 below. The data on the level of fees has been compiled from a range of different reports as well as from interview evidence conducted for this project. Interview evidence has confirmed not only the level of referral fees being paid, but also the fact that referral fees have been increasing over time. This is also consistent with previous research which has also identified an increase in the level of referral fees over time.

**Figure 19: Level of referral fees from 2004 to 2009**



Source: CRA interviews for 2004, 2008, 2009. The Jackson Report also estimates that the bulk of referral fees for fast track RTA claims are around £800-880. Moulton Hall, "Referral arrangements and legal services research report – Prepared for the Strategic Unit of the Law Society", June 2007, p4 for 2007. ABI, "Marketing costs for personal injury claims – Evidence of market failure", Research paper No 15, 2009, p3 for 2005, 2007.

The primary reason that referral fees have increased in recent years is increased competitive pressures between lawyers and introducers whereby competition between law firms to gain access to introducer panels bids up the referral fees.

For firms on insurer panels, more rigorous tendering processes have been used which have been designed to increase the referral fees received by the insurance company. We understand that at least one insurance company has gone as far as using an auction process for this. It is thought that this enables them to capture as high referral fees as possible. In recent years insurers have also sought to reduce the number of law firms on their panel which is also likely to have increased the overall referral fee as the remaining law firms gain from economies of scale. Consolidation of insurer panels was confirmed by insurers and those working with insurers.

It is also clear from Figure 19 that the level of referral fees has stabilised in the last few years. Overall referral fees are constrained by the level of costs which are recoverable and this, combined with limits on the extent to which further efficiency gains might be possible, is believed to have led to the stabilisation of the level of referral fees in the last few years.

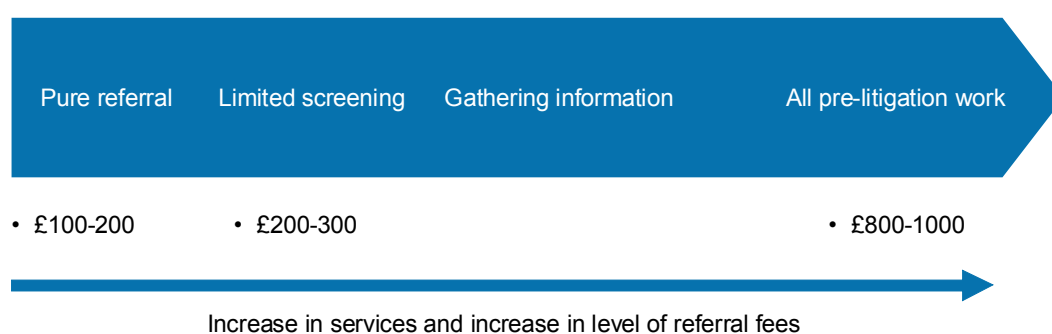


Since lawyers working with trade unions commonly use other arrangements to compensate the trade union for the referrals, it has not been possible to gather quantitative evidence on trends in referral fee equivalents over time. Figure 19 may therefore not be applicable to the trade union sector and other parts of this subsection may also not apply in the relationships between trade unions and the lawyers they refer members to.

#### *Link between services and referral fees*

As well as changes in the average referral fee over time, we have also identified that the current level of referral fees is linked to the level of services which are provided by introducers. This is set out in Figure 20 below.

**Figure 20: Services and referral fees**



Source: CRA

It was consistently identified from interviews with both introducers and also solicitors who pay referral fees to either CMCs or insurance companies that there was a link between the level of the referral fee and the extent to which the introducer conducted services for, or instead of, the solicitor. During the course of the study it was not possible to identify the proportion of introducer services which involve different levels of services being provided.<sup>147</sup>

For solicitors deciding where to operate in the market this makes sense since we would expect solicitors to be willing to pay more for cases where the validity of the claim had been screened or verified compared to where introducers had simply identified the contact details of a client. Put another way, if half of customers who call a CMC do not have a claim which is valid (such as because there was no one to claim from), we would expect solicitors to be willing to pay twice as much for claims where a screening process has eliminated these customers before they are referred to the lawyer compared to where all of these customers are referred to the lawyer. Similarly, we would expect solicitors to be willing to pay much more for cases where the CMC has undertaken certain activities such as collating details and photos of the accident or where the CMC has prepared all of the case such that the lawyer simply has to make the claim on the client's behalf and therefore incurs relatively limited cost itself.

---

147

If additional information on this was needed it may be possible for the CMR to identify the largest introducers and seek information on the services which they provided on behalf of lawyers. In addition, information would also need to be gathered from trade unions and insurance companies. Source: Lord Justice Jackson, Review of Civil Litigation Costs: Final Report, December 2009t

The referral fee may also vary depending on whether individual solicitors are required to take on all of the cases which are referred or whether they can decline cases which are initially referred to them (usually before any client contact occurs by the solicitor)

It is also the case that the level of fees is a function of the economies of scale and bargaining power of the introducer. For example, insurance companies which can refer very large numbers of claims to lawyers may be able to obtain higher referral fees from lawyers than other introducers which may be less likely to provide a steady flow of referrals to lawyers. This was also noted in the Jackson Report which highlighted that referral fees are lower where there are small numbers of referrals being made.<sup>148</sup>

#### *Structure of referral fees*

There are a variety of different models which are used in respect of how referral fees (or their equivalents) are paid. The models that are used by introducers include:

- Paying a fixed amount for every referral (common for many CMCs);
- Paying a monthly or annual membership fee (these may be the only fees paid or they may apply alongside other structures);
- Paying a fixed amount for a given proportion of all referrals (common with solicitor collectives where some introducers describe this as sharing the cost of marketing fairly across all members of the collective); and
- Paying a fixed amount for all referrals in a particular postcode area (common for insurance referrals).

The variety of methods of paying referral fees reflects the slightly different business models which are used and the ways in which client enquiries are referred to specific law firms by introducers.

#### **4.4.4. Referral fees facilitating growth of referrals**

As well as referral fees impacting competition between different lawyers, referral fees may also affect the overall level of claims that occurs. Referral fees represent the income stream for introducers and therefore we would expect introducers to want to increase this level of income. As the unit referral fee increases, introducers therefore have a greater incentive to increase the number of claims ("units").

#### *Motor claims*

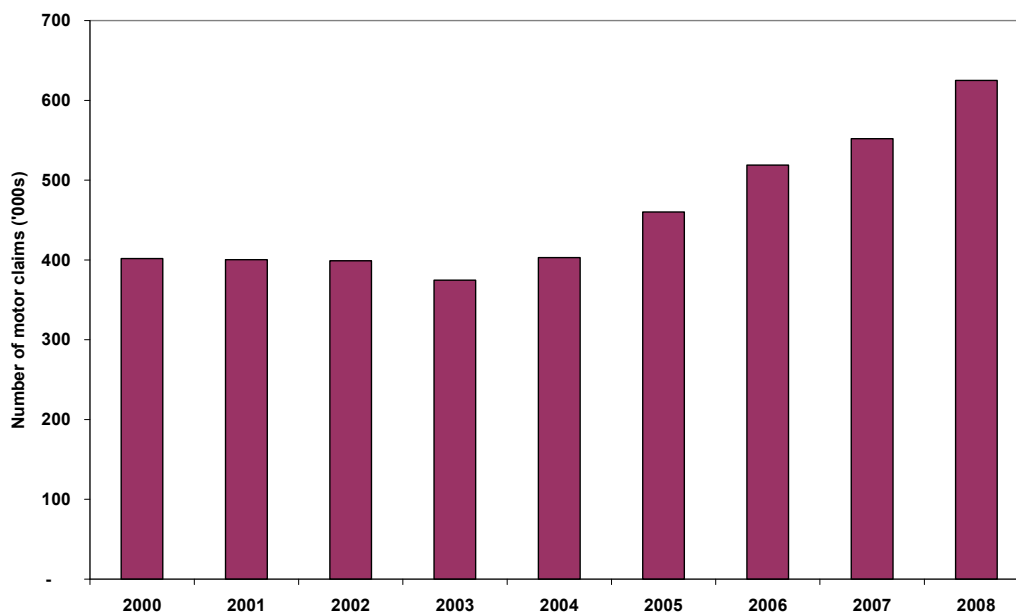
There is evidence that the total number of motor claims has been increasing over time as shown in Figure 21 below.

---

148

It was also noted that for claims outside the fast track scheme, referral fees may be more bespoke.

**Figure 21: Number of motor claims**



Source: CRU

It is notable that the timing of the increase in the number of motor claims coincides with the removal of the ban on referral fees in 2004. Potentially this could imply that the entire increase in the number of claims is a direct result of allowing referral fees. However, discussions held at the claims management workshop have indicated that referral fees were not the primary driver of the increase in the number of claims. Instead, some of the factors that were thought to be of importance in this regarding included:

- Changes to cost recovery in 2000 allowing a success fee and ATE premiums to be recovered from the losing side. The presence of ATE insurance provides protection for individual claimants against the cost of the other side should they lose hence consumers were able to make claims without incurring any costs;
- Court decisions made during 2000-2003 which increased the likelihood of success of future claims; and
- The Fixed Recoverable Costs Scheme bringing certainty to the market in 2003 regarding the costs which lawyers would receive thereby increasing the willingness of lawyers to take on a particular claim.

It is therefore not possible to attribute the whole increase in the number of cases to the role of referral fees. However, referral fees *do* fund introducers in marketing efforts and give insurers the incentive to encourage customers to bring cases and do appear to be facilitating the trend.<sup>149</sup> In addition, the ability to pay and receive referral fees in an “above board” manner may have encouraged some firms (both CMCs and solicitors) to invest in technology in order to deal with claims more efficiently. This may enable additional money to be spent on marketing to attract new customers. Since the number

---

149 We note that one major insurer does not accept referral fees and does not make referrals which is consistent with referral fees encouraging referrals since the absence of referral fees is seen alongside the absence of referrals.

of claims is continuing to increase (despite a fall in the number of RTAs), this does not suggest that marketing has yet reached the point where it is only leading to competition between firms rather than leading to an expansion of the market.

It was also noted by a number of interviewees that large introducers are able to match consumers to lawyers. Consumer research conducted on behalf of the LSB Consumer Panel identified that some consumers who directly approached lawyers were turned down by lawyers who either did not want to take on the work or did not feel competent to take on the work.<sup>150</sup> By contrast, consumers approaching an introducer whose brand is specifically linked to the conduct of personal injury work are much more likely to be matched to a lawyer who would be willing to accept the case. If consumers who are turned down by the initial lawyer are put off making a claim, then the branding of the introducers and the ability of them to find a lawyer who is willing to take on the case is also likely to increase the overall number of cases which are brought.

The importance of the role of marketing in personal injury claims (as distinct from other areas of legal services) was also noted by the LSB Consumer Panel's research.<sup>151</sup> Examples included:

- Response to television adverts where direct approaches to solicitors had been unsuccessful;
- Response to insurance companies when the individual might not have otherwise initiated a claim; and
- Response to radio adverts where the claimant was not aware of other firms specialising in personal injury claims.

It was noted that the claims where marketing was considered to have helped clients make a claim often involved less severe injuries whereas for those suffering major injuries marketing helped them to choose between firms having already decided to make a claim.

Overall therefore there is evidence that referral fees have facilitated a growth in the number of motor claims as individuals make claims that would not otherwise have arisen.

### *Employer liability*

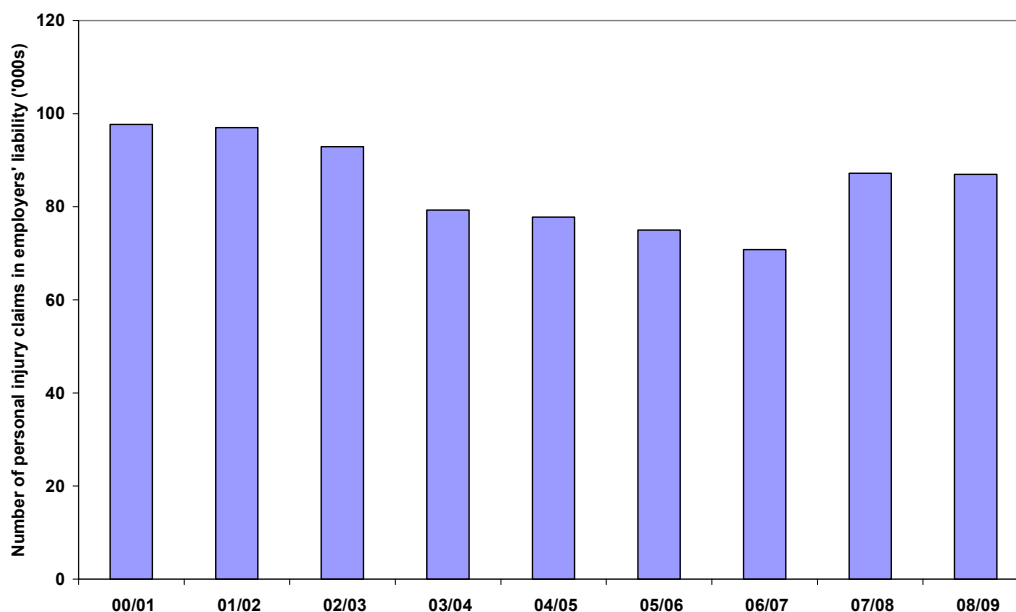
Unlike with the number of motor claims, the number of employer liability claims does not show an increasing trend in the number of claims made over time as seen in Figure 22 below.

---

150 An example of this was given during focus groups attended by CRA.

151 Referral Arrangements Research, Report prepared by Vanilla Research, March 2010.

**Figure 22: Number of personal injury claims in employers' liability**



Source: CRU

As noted in section 4.4.3, there is no evidence of a trend in the level of referral fees (or their equivalent) among trade unions, hence we would not necessarily expect to see an increase in the number of employer liability claims. Indeed, interviewees believed that the employer liability area was not facing a similar trend to the RTA sector because the employer liability sector had not seen as great an increase in marketing activity that had occurred in the RTA sector. Interviewees indicated that the increase in the number of claims in recent years was related to the economic cycle rather than referral fees.

#### **4.4.5. Choice of other experts determined by referral fees**

Suggestions have been made during the course of discussions that one of the other ways in which referral fees are affecting competition is not only the impact on the choice of lawyer for a case, but also the impact through the choice of other experts. In particular a number of interviewees have suggested that introducers will have a panel of medical experts who can opine on medical issues in dispute. It is argued that this panel of medical experts is determined by referral fees.

In the same way that introducers choose lawyers on the basis of referral fees as explained in section 4.4.2, we note that exactly the same incentives exist in respect of medical experts. Interviews with introducers have confirmed that they have panels of medical experts and that they receive referral fees from these experts. It has not been possible to identify the level of referral fees paid in these cases.

#### **4.4.6. Summary**

Table 12 below sets out a summary of the impact on competition from referral fees.

**Table 12: Summary of the role of referral fees in competition for legal services in personal injury**

Issue	Evidence and causation
Choice of lawyer determined by introducers on basis of referral fees	<p>Nearly all insurance companies and CMCs operate with lists or panels of lawyers in which referral fees are paid. Clear evidence that lawyers who pay referral fees receive more work than those who do not. Trade unions commonly use alternative referral arrangements with a similar economic effect to referral fees.</p> <p>Evidence of similar arrangements before 2004</p>
Competition to access panels has led referral fees to increase over time	<p>Strong evidence that referral fees on CMC and insurer panels have increased over time.</p> <p>No evidence regarding any trend in the value of alternative referral arrangements used by trade unions.</p>
Referral fees have facilitated growth of CMCs and insurer referrals	<p>Interview evidence supports growing role of CMCs in motor claims facilitated by referral fees. Interview evidence indicates that referral fee income has led to increased referrals by insurers. Consumer evidence supports the link between marketing by introducers and increasing claims.</p>
Choice of other experts constrained by introducers due to referral fees	<p>Interview evidence of approved lists of medical experts where referral fees are paid</p>

Source: CRA

#### **4.5. Market failure and potential detriment arising from referral fees**

In this section we assess whether the competitive effects of referral fees are causing any detriment to consumers.

##### **4.5.1. Referral fees and quality of service**

Some interviewees who have expressed concerns about the role of referral fees have suggested that increases in referral fees lead to a reduction in the quality of legal services because lawyers retain less fees to conduct the work. As such it is argued that they will spend less time on any given case and quality will fall.

It is noted that a potential reduction in the quality of service is only possible because customers are not able to assess the quality of service that lawyers are providing on their behalf. The quality of legal services relies on the professionalism of solicitors with or without referral fees – if lawyers are able to provide low quality services because customers can not judge this, then lawyers will be able to do this, indeed have the incentive to do this, with or without referral fees.

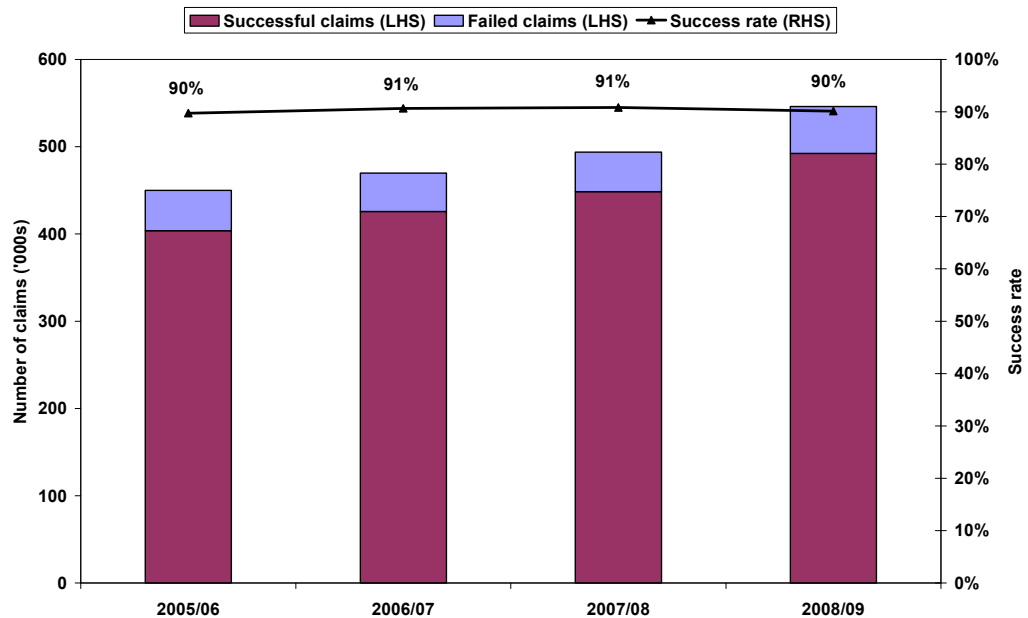
Nonetheless, we consider below the various different aspects of quality that have been highlighted during interviews which include:

- A reduction in the number of cases which are won;
- A reduction in the value of claims received by customers; and
- A reduction in the level of customer service.

*Proportion of cases won*

Figure 23 below shows the number of RTA claims that have been successful and those that have failed over time along with the implied success rate.

**Figure 23: RTA claims and success rate 2005-09**



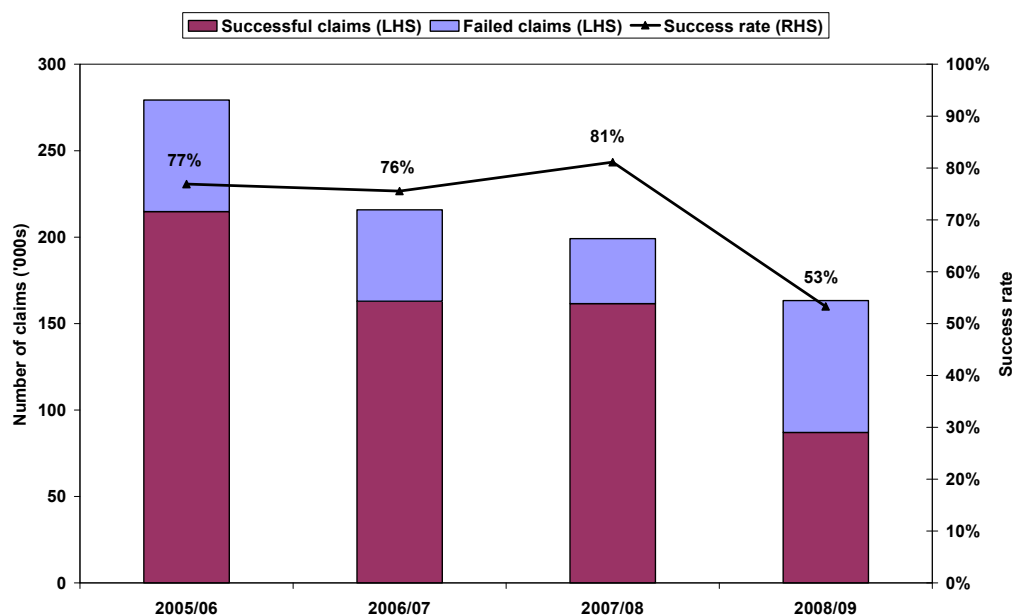
Source: Rupert Jackson, "Review of Civil Litigation Costs: Preliminary Report", May 2009, Appendix 25.

It is clear from Figure 23 that the success rate is very high at over 90% and this rate has been maintained over a period in which referral fees are estimated to have doubled. This therefore does not support the suggestion that referral fees are causing quality to fall.

However, it is clear from interviews that the assessment of liability is usually reasonably straightforward in RTAs (e.g. if the claimant's car was hit from behind). Hence the proportion of cases won can not fully reflect the quality of legal services in this sector.

Figure 24 below shows the proportion of claims which are settled successfully for employer liability cases.

Figure 24: Employer liability claims and success rate 2005-09



Source: Rupert Jackson, "Review of Civil Litigation Costs: Preliminary Report", May 2009, Appendix 25.

It should be noted that Figure 24 above is based on the number of settlements recorded by CRU whereas Figure 22 previously was based on the number of registered cases. The data in Figure 24 is the only available data which sets out then proportion of successful cases. We note that the success rate fluctuates at 76-81% level except for 2008-09 when it falls to 53%. The Jackson Report describes the final observation as anomalous, but there was no evidence given in the Jackson Report or in interviews suggesting that the 2008-09 reduction was caused by any changes to do with referral fees or referral arrangements.<sup>152</sup> Interviewees were also unable to explain the fall in the success rate.

#### *Value of claims received*

When considering the value of claims many interviewees stated that there were "standard" values of claims for different types of injuries and therefore lawyers who repeatedly operate in the personal injury arena would know the value of claims that clients should expect to receive. Indeed, there are a number of different resources available which assist lawyers in identifying the appropriate level of claims including:

- Reference books such as "The quantum of damages" by Kemp and Kemp provides details of what has been awarded in previous similar cases;
- Guidelines from the Judicial Studies Board; and
- Software tools such as Colossus or Claims Outcome Adviser (COA) which are commonly used by insurers to calculate damages.

Given the amount of information available on the level of claims that would be considered appropriate, and since many RTA cases are considered to be "standard" cases,

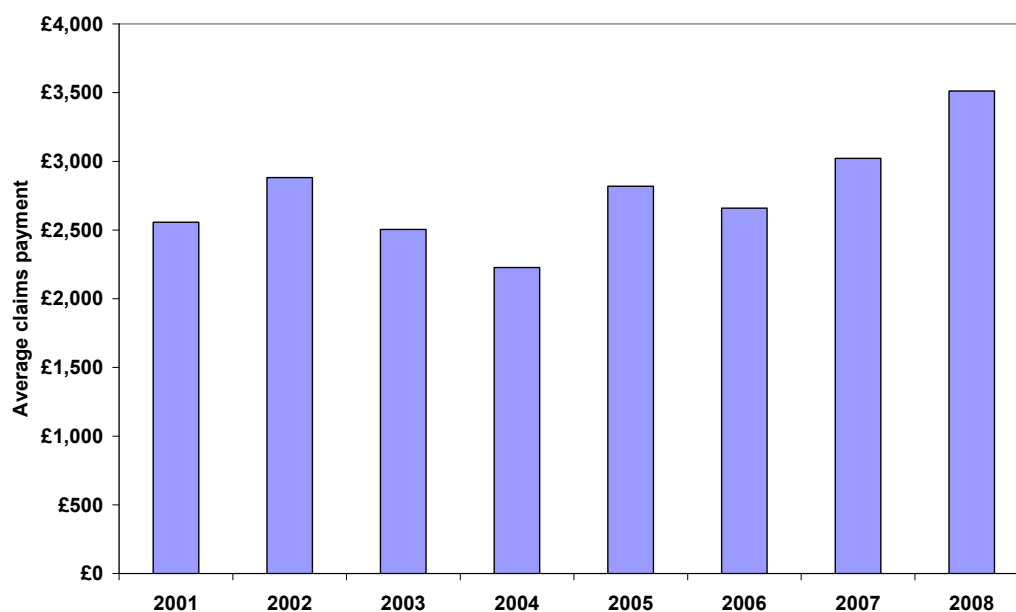
<sup>152</sup> The preliminary report of Jackson Review also identifies this anomaly. See Rupert Jackson, "Review of Civil Litigation Costs: Preliminary Report", May 2009, p139.



establishing the appropriate level of claims does not appear likely to take considerable effort. This alone suggests that accusations that referral fees lead to solicitors putting insufficient effort into obtaining the right level of damages and under-settling is likely to be incorrect.

If an increase in referral fees leads solicitors to under-settle so as to save themselves costs, we would expect to see a reduction in the average claims over time, especially after referral fees were permitted in 2004.

**Figure 25: Average claims payment for bodily injury in motor claims**



Source: Datamonitor, "UK Personal Injury Litigation 2009", December 2009.

As Figure 25 shows, the average claims payment of bodily injury in motor claims fluctuates over time. In particular, there is no evidence that there has been a reduction in the average claims over time as we would expect if increased referral fees were leading to a reduction in the quality of work by lawyers.

### *Service level agreements*

Acting against the potential for quality to deteriorate is the fact that many introducers play a role in ensuring the quality of legal services is at a sufficiently high level. This may involve quality screening at the beginning of the relationship. For example, some introducers will conduct in-depth discussions with law firms on its credibility, history, whether the applicant is a member of APIL or MASS, whether it has a case management system, number of staff, etc. Firms failing to meet these standards will not be accepted.

In addition, large introducers, particularly insurance companies, have service level agreements with lawyers to ensure that the quality of their service is acceptable. That introducers have such agreements in place is itself an indicator that they are concerned to

ensure that they refer to firms with an appropriate level of quality.<sup>153</sup> This is because they want to avoid poor quality legal services damaging their own reputation (whether that be as an insurance company or as a CMC more generally). Indeed this is supported by evidence from the LSB Consumer Panel's research which identified that consumers saw some introducers as having a "trusted brand".<sup>154</sup> Some of the factors in these agreements include:

- Requirements to respond to the initial enquiry from the customer within a particular period of time;
- Requirements related to the speed at which firms must respond to ongoing enquiries from customers; and
- Processes for handling and monitoring of complaints which are made against solicitors. We understand from CMCs that complaints most commonly relate to communication (hence the inclusion of communication standards in the service level agreements).

Insurers have indicated that there have been a small number of cases where lawyers have been removed from their panel because they were unable to meet the service level standards that were required.

Other introducers such as trade unions have indicated that they would monitor the service levels of any lawyers appointed and the selection of law firms would involve examining issues of quality. Trade unions have suggested that they face particular reputational concerns since they tend to have long term relationships with their members for whom they are offering a range of other services.

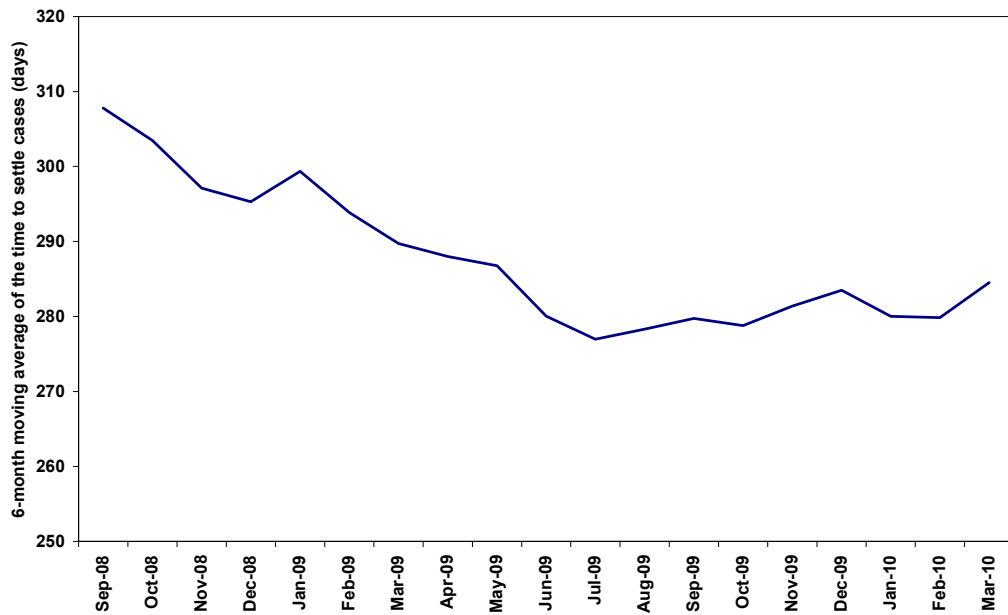
One of the aspects of customer service is the time taken to complete the claim. As noted in Figure 26 below a major solicitor firm has provided evidence of a reduction in the time to settle claims over the last few years.

---

153 As noted above some introducers will also require that firms comply with pricing restrictions such as giving 100% of the compensation from a successful claim to the client rather than lawyers receiving any fees from the claim.

154 Referral Arrangements Research, Report prepared by Vanilla Research, March 2010.

**Figure 26: Average time to settle a claim by a major solicitor firm**



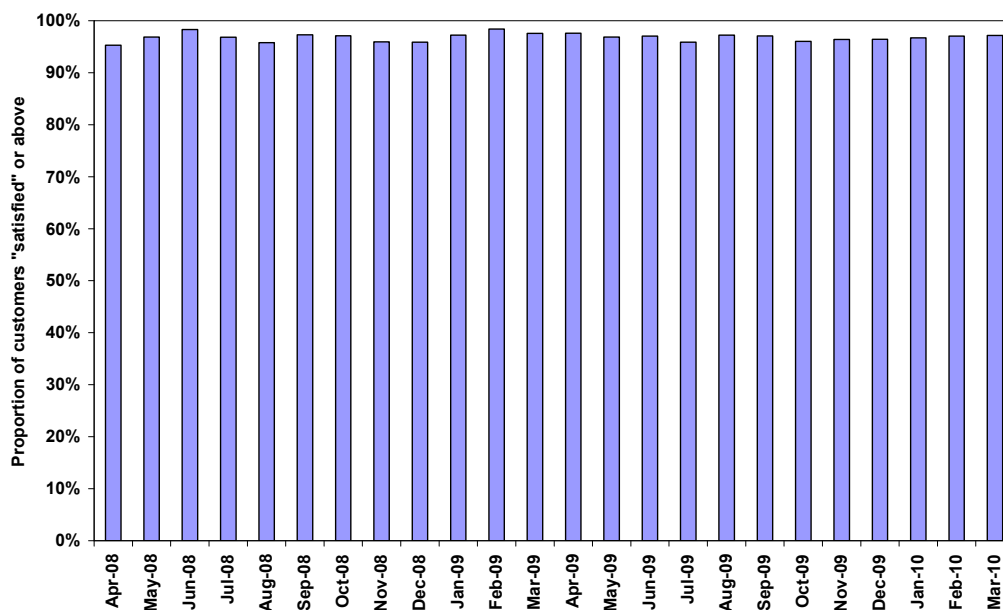
Source: Evidence from interviewee

The provider of this evidence has indicated that the reason for the reduction in the time taken to complete cases has been investment in technology (facilitated by revenues from referral fees) leading to improved processes and as such this reflects efficiency gains. (The suggestion that this is a reflection of “cutting corners” does not match with the evidence provided either in Figure 26 above or Figure 27 below.)

We also note that one of the drivers behind revisions to the fast track scheme as described in 4.6.1 below is to speed up the time taken for claims to be settled suggesting that the reduction in time demonstrated in Figure 26 should be interpreted as representing an improvement in customer service.

Finally, some large introducers and their panel solicitors operate customer satisfaction surveys at the conclusion of cases. Evidence from providers paying referral fees finds that customer satisfaction levels are very high. Figure 27 below shows that around 97% of customers rated their service levels as satisfactory or above over the last two years.

**Figure 27: Customer satisfaction for a major solicitor firm**



Source: Evidence from interviewee

Information was also available from a major trade union whose client care surveys revealed a similarly high level of customer satisfaction at over 95% during the last two years.

It is also useful to note that the arrangements between trade unions and law firms will often include requirements to provide other services to the trade union members such as free will writing or free legal advice - this has the effect of returning to consumers at least some of the benefits which accrue to trade unions from referral arrangements.

With very high levels of customer satisfaction there is therefore no evidence of any detrimental effect on the quality of service arising from the payment of referral fees.

#### *Complaints data*

Finally we note that the number of complaints related to referrals is minimal with only 14 complaints made about referral fees or fee sharing over the last 10 years.<sup>155</sup> We note that this is only weak evidence as if customers are concerned about their lawyer, the customer would be expected to complain about the specific issue they were concerned about rather than the referral fee per se.<sup>156</sup> In addition, this information is based on complaints to the Legal Complaints Service whereas customers may complain to the introducer regarding the quality of service of the lawyer. As noted above, dealing appropriately with complaints is one of the areas that is usually covered in service level agreements.

---

155 Based on information provided by the Legal Complaints Service to CRA.

156 Alternatively, the low level of complaints regarding referral fees could indicate that information on referral fees is not appropriately disclosed to customers. We consider this further in section 3.7.4.

#### 4.5.2. Referral fees facilitating growth of referrals

As noted in section 4.4.4, there is evidence that referral fees are facilitating a growth in the number of claims over time (although it is not possible to determine the extent of this due to other drivers of the same trend).

Some commentators have suggested that this is evidence that referral fees lead to “too much” marketing and low quality claims being introduced. We note that the evidence does not support this suggestion. In particular, the increase in the number of claims over time (alongside an increase in referral fees) has been accompanied by a constant success rate at over 90% which does not suggest that low quality claims are being brought. It is possible that introducers or lawyers are having to spend more time and effort screening out cases which have no merit. We would expect this to affect the level of the referral fee that lawyers are willing to pay (depending on whether the lawyer or the introducer conducts this additional screening) and for introducers this is simply a further part of the overall effectiveness of marketing in attracting clients.

Some interviewees have suggested that referral fees encourage fraudulent claims particularly related to whiplash claims. It is noted that such claims are a function of the verifiable nature of the claims i.e. if it is not possible to verify whether someone has whiplash then this is what provides the opportunity for fraudulent claims – this would arise irrespective of the presence of referral fees.

#### 4.5.3. Referral fees and other experts

Introducers have acknowledged that they have panels of medical experts for which they receive a referral fee. All introducers have stated that individual lawyers are free to choose not to use the medical experts that are on the introducer’s approved panel. The freedom for lawyers to choose their own medical expert, as well as reputational concerns of the introducer both act to prevent the quality of the medical expert being reduced. All introducers have stressed during the course of interviews that they do not interfere in the legal business of solicitors and respect the Code of Conduct that solicitors must act in the client’s best interest.

During the course of this research we have not focused on the quality of medical expertise as opposed to the quality of legal expertise and it has not been possible to gather information on quality indicators related to medical experts. However we note that no interviewee has provided any evidence of actual (as opposed to theoretical) problems in respect of the quality of medical expert services.

#### 4.5.4. Prices

We note that it is possible that increases in referral fees lead to an increase in prices. However, the vast majority of cases are conducted through the predictable costs scheme or the fast track scheme in which the level of legal costs are prescribed. Given these prices are fixed, referral fees do not affect the price of legal services.<sup>157</sup>

Alternatively it is possible that referral fees affect the price of insurance. Here we note that the cost of insurance will be partly driven by the cost of claims that insurance

---

<sup>157</sup> It is possible that there could be an impact if the price of legal services is partly determined by factors which include the cost of referral fees. Assessing the method by which the price of legal services is determined for the regulated schemes is beyond the scope of this report.

companies have to pay out. The more claims that are made (which section 4.5.2 indicates is partly a function of referral fees), the higher will be insurance prices.

Set against this it is important to recognise that referral fees constitute a source of income for insurance companies and therefore the income from insurer-introduced referral fees will have the effect of reducing the cost of insurance compared to in the absence of these fees (if the same level of claims were to be generated through other introducers). Since not all introductions arise through insurance companies and since claims are ultimately paid out, the combined effect of these two drivers seems likely to lead to higher insurance prices than otherwise.

However, it is not possible to conclude that this represents detriment to consumers as a whole as those customers who make a claim which they would otherwise not have done gain from this. Furthermore, we note that the main purpose of insurance is to make payments to those who have valid claims. Hence the insurance policy is being used for the purpose it was intended as payments are made to an increased number of people with valid claims.<sup>158</sup>

#### 4.5.5. Summary

Table 13 below sets out a summary of the impact on competition from referral fees and the evidence on whether this is causing any consumer detriment. Overall we conclude that there is no evidence of detriment arising from referral fees.

**Table 13: Summary of the role of referral fees in competition for legal services in personal injury**

Issue	Evidence and causation	Potential detriment
Choice of lawyer determined by introducers on basis of referral fees	Nearly all insurance companies and CMCs operate with lists or panels of lawyers in which referral fees are paid. Clear evidence that lawyers who pay referral fees receive more work than those who do not. Trade unions commonly use alternative referral arrangements with a similar economic effect to referral fees.  Evidence of similar arrangements before 2004	Success ratios for motor claims remained constant despite increase in referral fees  Information available on typical claims and value of claims remained constant despite increase in referral fees for motor claims.  No trends observed for employer liability claims.  Customer satisfaction levels found to be very high among panel lawyers.
Competition to access CMC and insurer panels has led referral fees to increase over time	Strong evidence that referral fees on CMC and insurer panels have increased over time.  No evidence regarding any trend in the value of alternative referral arrangements used by trade unions.	Service level agreements are in place and introducers are concerned about the impact of poor quality legal services on their own reputation  Increase in referral fees has not led to an increase in overall legal fees which are constrained by legislation

<sup>158</sup> Another example also helps to make this clear: If insurance companies made the claims process easier and therefore some consumers who previously did not complete the process because it was too complex were now able to complete the process, we would then expect this to lead to an increased number of claims and therefore an increase in insurance premiums. However, it is difficult to interpret having an easier claims process as leading to consumer detriment.

Referral fees have facilitated growth of CMCs and insurer referrals	Interview evidence supports growing role of CMCs in motor claims facilitated by referral fees. Interview evidence indicates that referral fee income has led to increased referrals by insurers. Consumer evidence supports the link between marketing by introducers and increasing claims.	No evidence of deterioration of cases. Fraudulent claims have causes other than referral fees.  Increased claims leading to higher insurance prices partly offset by referral fee income.
Choice of other experts constrained by introducers due to referral fees	Interview evidence of approved lists of medical experts where referral fees are paid	Interview evidence indicates that lawyers have freedom to use alternative experts. No evidence provided that experts on approved lists offer a low quality service.

Source: CRA

## 4.6. Changes impacting future competition

### 4.6.1. Revisions to the fast-track process

The Ministry of Justice has announced a new fast-track process that will apply to RTA personal injury claims valued between £1,000 and £10,000.<sup>159</sup> This came into effect on 30 April 2010. The scheme is intended to encourage early notification of claims, early admissions of liability and early settlements.

Where liability is admitted and the quantum of damages agreed before court proceedings are issued, the recoverable costs will fall for all but very small value claims (we would expect this to lead to a reduction in the value of referral fees that lawyers would be willing to pay for the introduction of work that goes through the revised fast track process). At the same time, however, revisions to the claims are aimed at reducing the costs incurred in making a claim (which might be expected to increase the level of referral fees that lawyers are willing to pay). It is therefore unclear what the overall impact will be on referral fees and it may be useful to continue to monitor these fees over time.<sup>160</sup>

However, the effect of the fast track scheme seems likely only to alter the *level* of referral fees rather than any of the other incentives and dynamics of competition associated with referral fees. As such we would not expect this to lead to substantial changes in competition related to referral fees. This is supported by evidence from interviews where no interviewee expected the revisions to lead to fundamental changes to the competitive process. Some interviewees did suggest that the revisions may have the effect of encouraging more cases to settle pre-trial rather than go to trial, but this was not thought likely to change the competitive dynamics of the market.<sup>161</sup>

<sup>159</sup> Ministry of Justice, "Quick and simple compensation scheme for road traffic accidents", 8 March 2010. <http://www.justice.gov.uk/news/newsrelease080310a.htm>

<sup>160</sup> Monitoring the level of referral fees could help to establish whether the improvements in the claims process outweigh the reduction in legal costs received.

<sup>161</sup> It is possible that this would be to the advantage of firms that are focused on "pre-litigation" cases compared to those that focus on cases which are litigated.

#### 4.6.2. Alternative business structures

As with the other areas considered in this report, the potential for firms to form alternative business structures could affect the way in which competition arises. We note that at present there does not appear to be very significant appetite for large scale change in the personal injury space in the light of potential alternative business structures (ABS). It is already the case that some law firms provide introducer services although the advent of ABS may encourage CMCs to purchase law firms.

Where firms enter into ABS and integrate the claims management activities with the legal services, this would imply that referral fees would no longer be required as both activities would be arising within the same entity. It is possible that increased integration would increase the frequency with which firms might be at risk from taking on both side of a case. Assuming that this was not allowed for contentious matters such as personal injury claims, we would expect firms to continue to have alternative lawyers who could be used for those cases much as they do today.

#### 4.6.3. Jackson Report

The Jackson Report was focused on addressing the costs of civil litigation and making recommendations that would promote access to justice at proportionate cost. The report makes a number of major recommendations including:

- Success fees and ATE insurance premiums should cease to be recoverable from the unsuccessful opponent;
- An increase in general damages of 10%;
- “Qualified” one way costs shifting i.e. that the claimant will not be required to pay the defendant’s costs if the claim is unsuccessful, but the defendant will be required to pay the claimant’s costs if it is successful;
- An extension of contingency fees to contentious work; and
- An extension of fixed costs for lower value litigation.

The Jackson Report also suggests banning referral fees. We consider this measure specifically in section 4.7.1 below, however, as noted in Table 13 above we find that there is no evidence that referral fees are causing consumer detriment. We note that the other recommendations made in the Jackson Report are not intended to encourage the use of referral fees. As such the introduction of other recommendations would not alter the conclusions of our report.

#### 4.7. Policy options

In this section, we discuss each of the policy options proposed by the LSB. It is worth noting that since Table 13 above concluded that there was not evidence that referral fees are causing consumer detriment, policy options focused on altering referral fees are unlikely to bring benefits.

##### 4.7.1. Banning referral fees

###### *Banning “pure” referral fees*

As discussed in section 4.4.1, referral arrangements were widely in place pre 2004. The immediate reaction of nearly all interviewees who currently use referral arrangements was



that a ban on referral fees would lead to a return to arrangements similar to those used before 2004.

It does not appear to be in dispute that one of the main functions that CMCs provide is that of marketing. If referral fees were banned we might expect to see fees described as marketing fees in future. If the payment of marketing fees would be acceptable we note that policing the difference between a referral fee and a marketing fee would be challenging.

Furthermore, different CMCs are operating different models with different types of service offered. The level of referral fees appears to vary according to these different levels of service indicating that in many cases the fee is paying for more than simply a referral. As such the opportunity to replace the current referral fee by charging higher prices for some of the other services provided appears to be an obvious route for firms to follow. For firms working on defendant cases for an insurance company, it seems entirely likely that lawyers would offer lower prices for those cases in order to receive referrals. Firms working with many trade unions already operate in this manner.

Despite the ability to get around the rules before 2004, there was some evidence that referral fees have facilitated a larger number of motor claims being made over time. This may simply be because designing fee structures to deliberately get around the rules introduces unnecessary costs into the process whereas after 2004 less transaction costs were required in using a referral fee system. Interviewees also noted that having referral fees brought increased certainty regarding income levels leading introducers to make investments through additional marketing or in technology in order to streamline the claims process. In turn this may have enabled an increase in referral fees and more money to be spent on advertising or other forms of encouraging customers to make claims.

In as far as there is evidence that referral fees have increased claims, banning them would be detrimental (since there is no evidence these are invalid claims). Even if referral fees have not significantly increased claims, then a ban appears likely to be broadly ineffective as firms have a number of ways that they could get around the rules where challenging the validity of arrangements is likely to be difficult.

We also note that the regulation of introducers and lawyers in relation to any concerns about referral fees may in fact be easier to police with referral fees in place as those firms which have more dubious arrangements can be easily identified compared to other firms which have simple referral fees in place. Identifying the more dubious arrangements is more difficult if the whole industry is focused on describing referral fees in other ways. This view was put forward by one of the regulatory bodies active in the personal injury market.

#### ***Banning all arrangements similar to referral fees***

As noted above banning referral fees is likely to lead firms to get around the rules. It is therefore important to consider whether it is possible to ban all arrangements which appear similar to referral fees.

We note that because of the different services provided by CMCs it would be difficult to identify whether the payment for a particular service was “fair” or whether it was unduly high because it included an element of referral fee in it. Assessing this would require exceptionally intrusive regulation through examining all flows of money between introducers and lawyers.

Alternatively, we might expect to find that lawyers and introducers enter into “agency arrangements” such that either the introducer was conducting outsourcing on behalf of the law firm, or the law firm was conducting outsourcing on behalf of the introducer.

If all flows of money from lawyers to introducers could be banned we note that this would be expected to distort the market by favouring some businesses over another and potentially by removing efficient business models from the market. For example this could:

- Imply that CMCs (including solicitor collectives) which are good at undertaking marketing are no longer able to do this;
- Unduly favour lawyer-introducer combinations where lawyers can conduct other work for the introducer (such as undertaking “bent metal” cases for insurance companies for free or advising trade unions for free) but where flows of money from the lawyer are not necessary; and
- Lead some firms to use ABS purely in order to get around referral fees through activities being integrated into the same firm when these firms would not otherwise have sought to integrate.

Once again, even banning arrangements which look similar to referral fees would either be ineffective or exceptionally difficult (and costly) to police especially since it is possible to circumvent any ban on flows of money. Furthermore, if it was possible to enforce a ban of some description it is likely that this would distort competition between different business models.

Finally, since no evidence was found of referral fees causing any consumer detriment, it is not apparent how the end clients would benefit from banning referral fees and arrangements which appear similar to referral fees.

#### **4.7.2. Capping referral fee**

Another policy option is to cap referral fees at a certain level e.g. the Jackson Report suggested £200. The rationale underlying the policy option is that high referral fees impose financial pressure on law firms which therefore reduce the quality of services they provide. It is argued that capping referral fees at a lower level would reduce the financial pressure and law firms would be able to provide services of high quality as they would have sufficient resources to do so.

We note that section 4.5.1 specifically focuses on whether high referral fees are leading to a reduction in the quality of legal services and we find that there is no evidence that they do. Since there is no detriment related to the quality of service, there is therefore no evidence that this policy option would bring benefits. However, we also note two difficulties with this policy option.

First, the same arguments set out in section 4.7.1 relating to banning referral fees also apply here.<sup>162</sup> Interviewees have stated that referral fees might be expected to be set at the cap but then additional arrangements would be used to “make up the difference” between the cap and previous ongoing referral fee levels. Therefore the same difficulty of policing the ban on referral fees also applies here and for the same reasons as set out

---

<sup>162</sup> We assume the situation in which the cap is lower than the current referral fee level. If the cap is above the current level then this would have no effect.

earlier, in as far as referral fees have facilitated claims over time, the cap would be detrimental.

If it was possible to enforce a cap then this could again distort competition as it would favour business models in which there was a “pure referral” (where referral fees are low) over those businesses in which introducers offer additional services (where higher referral fees were identified as being paid). For example, those CMC businesses on the left of Figure 20 which provided limited services would not be affected but those CMCs on the right of Figure 20 which provide more services would be affected.

Since lawyers can choose which introducers to use, they are in the position to trade off the costs of the pure referral model compared to the costs of using introducers who offer other services. That a multitude of business models survive in the market today at the very least suggests that some CMCs are more efficient at conducting these other services than lawyers are (as otherwise the lawyers would choose to use the pure referral fee model and conduct all the other services themselves).

Second, in addition to all of the difficulties set out relating to policing a ban which would also be faced under a scenario in which the fees were capped, the regulator would also need to set out:

- How the cap will be determined;
- Whether it would vary by different sectors such as for different types of claim; and
- How, if at all, such a cap would be reviewed over time.

This would impose additional regulatory costs beyond those required in section 4.7.1 to police any ban. Since there is no detriment from referral fees, this would bring no benefit.

#### **4.7.3. Standardised disclosure to clients**

The next policy option is to require greater disclosure of referral fees by providing information to clients in a standardised form including disclosing the monetary amount of the referral fee.

Solicitors and introducers are already required to disclose information to customers although as noted in section 2.7.3 there is evidence of poor compliance with these requirements in the past.

It should be noted that evidence from the LSB Consumer Panel’s research has identified that consumers value transparency of disclosing referral fees. It is therefore important to assess whether disclosing information to consumers is likely to change their behaviour.

Information is available on the extent to which clients respond to the existing disclosure information:

- One major insurer has stated that in 2009 only saw two customers commented on referral fee in around 50,000 cases;
- One top five CMC has never had any feedback from clients on any issues to do with referral fees; and
- One major solicitor firm working with insurers has not had any comments on referral fees out of 36,000 cases it deals with every year.

It should be noted that although disclosure of referral fee information was acknowledged as poor across the industry in the past, each of these firms highlighted the increased

enforcement focus on this area by the SRA and CMR. The large firms who provided the information in the bullets above indicated that they currently have standard processes and standard documents in place to disclose information to customers. This suggests that a lack of compliance is unlikely to be the cause of the lack of customer response.

It is possible that the lack of response to disclosure information by customers reflects the fact that information is provided in a descriptive manner rather than as a monetary amount. However, the lack of consumer response is consistent with evidence from other consumer markets where payments are made to intermediaries (see section 2.7.3 for further details on this). Instead it appears much more likely that since consumers know that they have a no-win-no-fee arrangement in place with the lawyer, they have limited interest in any financial arrangements between the lawyer and the introducer as these have no financial consequence for the consumer. This is also consistent with evidence from the LSB Consumer Panel's research as noted in section 4.1.

Requiring standardised disclosure would also impose costs on firms in both calculating the referral fee to be disclosed, redesigning any technology which provides the disclosure documents and then the cost of the actual disclosure.<sup>163</sup> Furthermore, providing this information would impose costs for regulators in designing a more standardised form and setting out the information that would need to be presented as well as policing compliance with the rules.

Existing evidence does not therefore give strong support that providing standardised information related to referral fees would affect consumer behaviour. In the absence of behavioural change, and given the lack of detriment caused by referral fees, there is no evidence that this policy option would bring benefits.

#### **4.7.4. Greater disclosure to regulators**

This policy option would require greater disclosure of referral fees or referral arrangements to Approved Regulators.

It is possible that revealing information on referral fees could lead regulators to identify outliers in the level of referral fees that are being paid. This information could then be used as an indicator when considering whether different companies should be investigated. However, it is unclear whether information on referral fees alone would be sufficient since regulators would also need to understand the business model which the firms are using to see whether referral fees are linked to the level of services provided.

Even though there is no information at the market level that the quality of legal services is being reduced because of referral fees, it is possible that individual arrangements between introducers and individual law firms may be leading to a deterioration of legal services. If this is the concern then it would appear as though the focus of regulatory

---

163 A number of firms using referral fees suggested that calculating referral fees on a standard basis would be challenging given the variety of different methods of paying referral fees such as monthly or annual payments, or membership fees. While it may be slightly more difficult for firms operating these models compared to those who have a fixed amount per referral, no interviewee was able to dispute their ability to use their previous last year's figures of total referral fees and total number of cases referred to provide an average referral fee per case. Furthermore, as indicated by the fact that it was possible to provide results for Figure 4 and Figure 5, firms operating more complex models of paying for referrals are nonetheless able to identify the average cost at present. (It is possible that this causes difficulties for new entrants, but they could use estimates from business plans in the first year of operation.)

attention should be focused on this potential for consumer detriment related to the quality of legal services rather than on referral fees.

Interviewees have agreed that the SRA has become increasingly vigilant and has already stepped up enforcement efforts in recent years. Given that this trend is already ongoing, and given that there is no evidence that referral fees are causing consumer detriment at the market level, this does not suggest that increasing disclosure to regulators beyond the existing levels is currently required.

It is also possible that information collected by regulators could be disclosed at an aggregate level so as to provide additional information for the market. We note, however, that referral fees are related to the different levels of services that are provided by introducers and that aggregating information across the market would therefore aggregate information across different business models. This makes the information less useful in comparison to markets where similar business models are used. Finally we note that no interviewee saw advantages for their business from publishing this information at the present time.