COMPLIANCE-BASED ENTITY REGULATION

LSUC TASK FORCE CONSULTATION

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Submitted by: The Ontario Bar Association

ONTARIO BAR ASSOCIATION
A Branch of the Canadian Bar Association

L'ASSOCIATION DU BARREAU DE L'ONTARIO
Une division de l'Association du Barreau canadien

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Introduction

The Ontario Bar Association ("OBA") is pleased to provide this submission to the Law Society of Upper Canada Task Force on Compliance-Based Entity Regulation in response to its Consultation Paper: "Promoting Better Legal Practices" ("the Consultation Paper").

As the largest voluntary association of lawyers in the province, we are ever seeking to improve the ability of our members to innovate and adapt now and for the future. Engaging on issues about the ability of lawyers to deliver high quality, cost-effective legal services is one way we are bringing the broad experiences of our membership to improve the profession and assisting lawyers to best serve our clients and the public.

The OBA

Established in 1907, the OBA is the largest voluntary legal association in Ontario and represents 16,000 lawyers, judges, law professors and law students. OBA members are on the frontlines of our justice system in every area of law and every type of practice, and provide legal services to a broad range of clients in every region of the province. In addition to providing legal education for its members, the OBA is pleased to assist government, the Law Society, and other decision-makers with dozens of policy initiatives each year – in the interests of the public, the profession, and the administration of justice.

The proposal for compliance and entity regulation has the potential to impact every lawyer in the province. On a daily basis, OBA members across the province interact directly with members of the public seeking assistance with virtually every kind of legal issue where lawyers are engaged. The ethical and professional issues that compliance-based regulation seeks to address are of significant interest to lawyers because they are fundamental to the delivery of high quality, cost-effective legal services to the public.

In order to garner input for this submission within the Law Society's consultation period, the OBA has consulted our elected council members in all eight judicial regions of the province for their views on the issues outlined in the Consultation Paper. We have also received input from members of a number of OBA practice sections, including Sole, Small Firm, and General Practice; Canadian Corporate Counsel Association – Ontario Chapter; SOGIC and the Equality Committee. Collectively, these members provide a critical cross-section of the bar, including senior and junior lawyers from managing partners to new calls, who practice across Ontario as solicitors and barristers in solo, small, medium and large firms.

Background

The Law Society Consultation Paper

In June 2015, Convocation of the Law Society of Upper Canada established a Task Force (the "LSUC Task Force") to study and make recommendations on compliance-based regulation and entity regulation to establish a proactive approach to regulation intended to help lawyers and paralegals to improve their practice standards and client service.

In January 2016, the LSUC Task Force issued the Consultation Paper setting out context and background on compliance-based regulation and entity regulation ("CBR/ER") for the purpose of seeking input from lawyers about the appropriateness of such regulation in Ontario.

As noted in the Consultation Paper, the LSUC Task Force believes that a focus on proactive regulation is appropriate, particularly given that the majority of complaints about lawyers relate to practice management issues. The Law Society's research suggests that lawyers achieve greater success in their professional practices when they focus on how their practices are best managed and establish policies and procedures to achieve the professional goals set out in the Law Society's rules and requirements.

The LSUC Task Force believes that encouraging all practitioners to reflect on and improve the systems they have in place could improve practice management overall for the benefit of clients and practitioners, and may have the effect of increasing client satisfaction and reducing the incidence of complaints and claims.[1]

The Consultation Paper suggests that CBR/ER might be an effective solution to these challenges because:[2]

1. Practitioners would have access to Law Society resources identifying and explaining principles of effective practice management. The implementation of proactive regulation would benefit the management and culture of the firm as a whole, which would promote and improve ethical best practices of both the firm and the lawyers associated with it.

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[1] Consultation Paper, p. 5-6. The paper notes that, "more than half of the complaints involved client services (52 per cent) and other issues relating to practice management infrastructure, including financial matters. This could include a variety of issues, including a lack of effective communication by the practitioner with the client. Law Society data also indicate that the majority of complaints concern sole practitioners (53 per cent in 2014) and firms of between two and five lawyers (26 per cent of complaints during that year). Fifteen per cent of complaints were made against lawyers in medium-sized firms of between six and 20 lawyers. Six per cent were made against lawyers in firms of more than 20 lawyers."
[2] Consultation Paper, p. 6-7.

2. Compliance-based entity regulation recognizes that a firm has a role to play in ensuring that the ethical behaviour of lawyers and paralegals is promoted and that a firm may be accountable for system failures that resulted in the lawyer's conduct.

3. A focus on compliance could lead to reduced complaints, by encouraging practitioners to consider how practice management problems might be avoided, rather than reacting to problems after the fact. Responding to complaints can be time-consuming and stressful.

4. Compliance-based entity regulation provides practitioners the flexibility and autonomy to develop internal systems and processes that take into consideration risk, size, practice type, and client base.

5. A renewed focus on effective practice management will better protect the public and increase public confidence in the legal profession.

6. Compliance-based entity regulation allows the regulator to respond to new issues as they arise without having to create new rules.

The Consultation Paper includes the following key definitions relevant to this submission:[3]

"**Compliance-based regulation**" emphasizes a proactive approach in which the regulator identifies practice management principles and establishes goals, expectations and tools to assist lawyers and paralegals in demonstrating compliance with these principles in practice. This approach recognizes the increased importance of the practice environment in influencing professional conduct and how practice systems can help to guide and direct conduct to meet appropriate professional standards. Lawyers would report on their compliance with these expectations, and would have autonomy in deciding how to meet them. Practitioners would also have flexibility in deciding which policies and procedures should be adopted in order to achieve effective and compliant practice management.[4]

"**Entity regulation**" refers to regulation of the business entity through which lawyers provide services, and may include sole proprietors. For example, a law firm would be an entity. Entity regulation recognizes that many professional decisions that were once made by an individual lawyer or partner are increasingly determined by law firm policies and procedures and firm decision-making processes. The environment in which a lawyer works plays an increasingly significant role.

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[3] Consultation Paper, p. 4-5.

[4] Some members have expressed the view that the phrase "outcomes-based regulation" better reflects the stated objective of the Law Society in establishing a principles based regime that permits flexibility in meeting the desired outcomes. That phrase also avoids the potential that "compliance-based regulation" implies a prescriptive approach that focuses on regulating the processes by which outcomes are achieved, contrary to the stated intent of the Task Force and the view expressed later in our submission. For the purposes of this submission we have simply used compliance-based regulation for consistency with the Law Society's Consultation Paper.

The Consultation Paper notes that compliance-based regulation and entity regulation "do not necessarily have to be implemented together, but proactive regulation may be more effective if the business entity is also involved. To ensure compliance with these principles by the entity as a whole, the LSUC Task Force believes there is merit to considering the regulation of the practice itself, in addition to the individual practitioner."[5]

In our consultations and for the purposes of this submission we have addressed compliance-based regulation and entity regulation separately so as to appropriately focus on the merits of each.

Comments

The Law Society has indicated it has not yet made any decisions about the implementation of CBR/ER. The Consultation Paper provides elements of context and background on CBR/ER and presents questions that may be relevant to different options that could be pursued.

In the following sections we address the questions by way of the critical principles that our members believe should inform the development of such initiatives. For some of the questions, our members expressed the view that it is difficult to provide meaningful feedback without more details about a specific option in question. Once the LSUC Task Force reaches a conclusion on some of the fundamental issues, the context will provide an opportunity to provide additional input on some of the follow-up questions.

For the purposes of providing input at this stage, we set out the central themes and feedback received in our consultations to date reflecting the views from our broad-based decision making council and our most engaged members. In our view, these consensus views reflect some key considerations that should be relevant to any further CBR/ER development.[6]

We are aware that a number of law societies in Canada are currently considering compliance-based regulation and entity regulation. Our members have noted the importance of avoiding disparate reporting requirements in multiple jurisdictions where they practice and are required to report to different law societies. The Law Society should encourage other Canadian law societies to develop any additional regulatory requirements in a concerted and coordinated manner in keeping with the key criteria outlined in this submission. Seeking to harmonize the approach minimizes the burden

[5] Consultation Paper, p. 4-5.
[6] See "Innovating Regulation: A Collaboration of the Prairie Law Societies", Law Societies of Alberta, Saskatchewan and Manitoba (November 2015), which notes: "In doing this work, we are clear that this discussion paper is a first step. We have no illusions that simply opening the discussion to these issues will enable us to find all of the answers. This is a process and the intention of this paper is to set the groundwork and try to advance the discussion with a clear understanding that there will be more to come." (at p. 3)

of compliance on law firms operating in more than one jurisdiction compared to the situation if there is a patchwork of regulations.

The bar is also concerned about increasing time and cost involved with any additional regulatory action. At this time, we understand that the Law Society envisages that cost efficiencies may be found in the reduction of complaints or other high-cost Law Society activities. In any event, our membership believes it is important for the Law Society to minimize the costs both to the regulator and to the bar that will be associated with any CBR/ER initiatives.

Compliance-Based Regulation

Overview

The OBA is broadly supportive of the concept of compliance-based regulation as a potential avenue for encouraging improvements to practice management that would benefit the management and culture of the firm as a whole, and promote and improve ethical best practices of both the firm and the lawyers associated with it.

If designed and implemented appropriately, the outcomes outlined by the LSUC Task Force have the potential to benefit practitioners, the public, and the administration of justice. Arguably, a focus on proactive regulation – with the necessary flexibility and autonomy for innovation – could encourage practitioners to consider how practice management problems might be avoided, rather than reacting to problems after the fact. The LSUC Task Force also suggests the approach could lead to reduced complaints, which our members agreed are a significant burden on practitioners even when there has been no fault on the lawyer's part.

Our members have noted that many firms have already established formal or informal practice oversight committees and developed the practice management systems that might be part of a compliance-based regime. The type of existing proactive approach was reported throughout our consultation with the OBA membership across all practice types, from the largest firms to small or solo practices. That said, members recognized that it could be helpful to encourage all practitioners to more systematically consider the firm approach to such practices, and that a renewed focus on effective practice management could increase public confidence in the legal profession.

The Law Society discussion of CBR/ER initiatives references the experiences in other jurisdictions, most notably in New South Wales, Australia. The Consultation Paper notes that in that jurisdiction, there is a strong correlation between the implementation of proactive regulation and a reduction in

the number of complaints, with a 2008 article reporting that the complaints rate for practices required to report having gone down by two-thirds after self-assessment.[7]

The substantial decrease in complaints reported from the Australian experience is undoubtedly of interest to lawyers to increase client satisfaction and service to the public. However, our members are aware of the need to exercise caution in assessing the experiences from other jurisdictions with respect to their applicability to Ontario. Care is especially warranted where the implementation of proactive regulation in New South Wales was undertaken in an entirely different regulatory context and where the cause of the apparent success is a matter of some uncertainty.[8] While OBA members do not believe these differences militate against implementing compliance-based regulation, they counsel the need to carefully develop and monitor a scheme appropriate for the Ontario context.

The Need for a Manageable and Appropriate System

To the extent possible, adopting compliance-based regulation should alleviate rather than exacerbate the regulatory burden on the profession, increase engagement in ethical best practices, and potentially reduce client complaints significantly. Setting out prescriptive rules for compliance, however, would be contrary to the purpose and benefits of outcomes focused regulation, would impose a costly new burden on Canadian lawyers and law firms, and would render outcomes-focused regulation insufficiently flexible to apply across practice contexts. In order to be effective, the system must be manageable and appropriate to the practices that are required to comply. This avoids unnecessary burdens on licensees, but also facilitates the meaningful contemplation of practice management objectives that reflect the perceived drivers of success in the Australian experience.

First, any increased regulatory burden should be proportionate to the benefit to be achieved. In designing the approach, the LSUC Task Force should carefully assess the basis for the additional reporting requirements, which it has indicated would function as an additional layer of regulation on top of the current reporting requirements for all licensees. The Law Society has emphasized that

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[7] Tahlia Gordon, Steve Mark, and Christine Parker, "Regulating Law Firm Ethics Management: An Empirical Assessment of the Regulation of Incorporated Legal Practices in NSW", J.L. & Soc. (2010), Legal Studies Research Paper No. 453 [*Regulating Law Firm Ethics*].

[8] The Consultation Paper refers only to CBR/ER as implemented to date in jurisdictions that have alternative business structures ("ABS"), as in New South Wales, where the reporting obligation only applied to Incorporated Legal Practices that were already arguably in the process of significant change. According to "a preliminary empirical evaluation" noted in the LSUC Consultation Paper, "it appears to be the learning and changes prompted by the process of self-assessment that makes a difference, not the actual (self-assessed) level of implementation of management systems." The analysis notes that further research is necessary "to understand better exactly what it was about the NSW approach that achieved this effect. For example: Did the self-assessment exercise prompt changes to formal management systems at the firm level that made a difference? Or was the effect more one of consciousness-raising for individual lawyers who were reminded by the self-assessment exercise of the importance of being mindful to implement pre-existing ethical procedures and practices?" See *Regulating Law Firm Ethics*, note 7 above.

the compliance-based regulation would be tailored and not prescriptive, in order to facilitate the flexibility that supports innovation and avoids introducing a mere "box ticking" exercise.

Second, the implementation needs to be carefully structured to best encourage compliance. Many members said that any new reporting requirement should be included as part of the member annual report, or if that proves too cumbersome to incorporate, then at least coincidental in the reporting timeframe.[9] Particularly for smaller firms, this would facilitate the ability to review and report on the management systems. The need for appropriate guidance is discussed in the following section.

Appropriate Guidance

The OBA believes that the objectives of compliance-based regulation must be articulated in a way that is sufficiently high level and flexible to be adapted to different kinds of practice, with guidance that provides examples of how those responsible might comply. Forms of guidance need to be carefully developed, to elucidate reasonable interpretations of the requirements and avoid serving as complicated or prescriptive "box ticking" exercises that would frustrate the objectives of facilitating autonomy and innovation. Lawyers and law firms should be permitted to self-assess their compliance, reporting to the Law Society as required on their results, and on plans to address areas where they are not fully compliant.

CBR/ER has been described as an initiative in which the regulator can work more collaboratively with the bar, but it should also be an opportunity for lawyers to a encourage each other to improve professional and ethical practices. We note the *CBA Ethical Best Practices Self-Evaluation Tool* is designed to assist Canadian law firms and lawyers to systematically examine the ethical infrastructure that supports their legal practices, including competence, client communication, confidentiality, conflicts, preservation of client property/trust accounting/file transfers, fees and disbursements, hiring (including promoting diversity in the workplace), rule of law and administration of justice, and access to justice. The goal of the Self-Evaluation Tool is not to be prescriptive but rather to encourage exploration and discussion of firm practices.

In our consultations many OBA members related their own experiences with the Law Society's randomized Practice Management Review ("PMR"), which has been in place for nearly a decade. The Law Society states the PMR is intended as a proactive and preventive program to reflect the Society's emphasis on quality assurance in service of the public interest – designed to support the goals of its members to be efficient, effective and competent.

As noted in the Consultation Paper, "a PMR covers all aspects of practice, including file management, time, client and financial management. In the course of conducting the review, Law

[9] Regardless of the frequency of reporting required, it appears members favour coordinating the reporting obligation with the member annual report.

Society staff may speak with firm leadership, managing partners, and firm administrators if any issues are uncovered that relate to firm-wide matters. … Lawyers and paralegals have provided very positive feedback about these proactive initiatives. A 2015 report indicated that over 96 per cent of lawyers who underwent a PMR indicated that they found the process to be constructive and helpful to the management of their practice."[10]

Application to Sole and Small Firms

The response from our membership indicates a broad view that the above considerations are relevant to all lawyers to whom compliance regulation would apply. However, members were also aware that the practical burdens in assessing or developing effective reporting mechanisms for the regulations is likely to be most challenging for sole and small firms, who have limited resources to undertake these tasks.

The membership did not express a view that the sole and small firms should be excluded from the system, and were in fact supportive of the importance of including sole and small firms, given that proportion of complaints to the Law Society in those categories. Many members felt that it is critical for all lawyers to ultimately have the same professional reporting responsibilities, but they should be appropriately tailored to the specific firm size and practice.

Our members felt that if compliance-based regulation is adopted, it should be phased in for sole and small firms. Although there is not a bright line delineating the firms for whom this would be most important, the majority of members believed that firms of 5 or fewer lawyers met this criteria. An incremental approach for such firms would permit the Law Society first to review the experience with larger firms, and make any appropriate modifications before requiring compliance from those for whom the burden is most significant.

Application to Public Sector and In-house

The Consultation Paper states that private practices directly serving the public are most readily the starting point for compliance-based entity regulation. The LSUC Task Force notes it has met with other Canadian law societies, and suggests that if proactive regulation is implemented, there is also merit to exploring application through an incremental approach to government lawyers, corporate and other in-house counsel, practitioners in legal clinics, and other settings.

Public sector lawyers and in-house counsel are regulated by the Law Society and are held to high ethical standards, as are all other lawyers. However, the context in which they provide legal services is very different and the impacts on them may be very different than on lawyers practicing in the private bar. We agree with the LSUC Task Force's assessment that in-depth review and consultation must be undertaken before any decision to include public sector lawyers or in-house counsel in the scope of compliance-based or entity regulation.

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[10] Consultation Paper, p. 10-11.

Principles for a Practice Management System

The LSUC Task Force seeks input on the key components, or principles, for compliance and entity regulation, and has put forward 7 categories based on its Practice Review Basic Management Checklist and its review of the principles of compliance and entity regulation that have been developed in other jurisdictions.[11]

In general, OBA members viewed the proposed categories as a reasonable encapsulation of the elements of a law practice impacting how lawyers fulfil the duties owed to their clients, the public and the justice system more broadly.

The Consultation Paper notes that the LSUC Challenges Faced By Racialized Licensees Working Group has been considering equity, diversity and inclusion issues for Racialized Licensees in the legal professions, and we note and agree that the categories suggested by the Task Force for a practice management system properly include equity, diversity and inclusion and access to justice.

In the OBA's earlier submission to that LSUC Working Group, we referred to materials developed or promoted by the CBA offering research and key considerations to assist firms develop, assess and refine a diversity program that is best suited to their practice.[12] We also emphasized that "the guides avoid a 'one size fits all' approach and instead provide strategies to develop and refine effective solutions for firms of all sizes, practice types and locations."

Although it would be germane to any elements of a compliance-based regulatory scheme, our earlier submission noted that "it is essential to have the buy-in of firms for the ongoing development necessary to build a diverse and inclusive profession. ... The ongoing commitment of senior leadership and the communication of that commitment to firm members are also critical for earning the confidence of racialized lawyers within the firm. This in turn supports the firm's ability to consistently gather reliable information needed to assess and improve its initiatives, and is ultimately essential to the success of the firm's ability to build a culture of diversity and inclusion."

In our view, these should remain relevant and important considerations for guiding the objectives of the practice management system being considered as part of this consultation.

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[11] They are: practice management, client management; file management; financial management and sustainability; professional management; equity, diversity and inclusion; and, access to justice.
[12] "Addressing Challenges Faced by Racialized Licensees", A submission by the Ontario Bar Association. (March 2015).

Entity Regulation

The Consultation Paper notes that regulation of lawyers and paralegals by the Law Society is currently based on the regulation of the individual practitioner, although some aspects of the Law Society's regulatory activity affects firms.[13]

As stated in the proposal to Convocation to establish a task force:

> "The firm generally sets the overall practice standards for those within the firm, and organizes the management of trust accounts, conflicts regimes and confidentiality standards. Firms often develop their own cultures, distinct from the culture of individual lawyers in the firm. Firm policies and practices including their management of trust accounts, their marketing and advertising, and services standards, are all currently the individual responsibility of all the licensees in a firm. However, the reality is that these practices are part of the firm's work and not necessarily under a single licensee's control. This means that, in effect, some of the responsibility for common firm practices is a matter for the firm directly. As such, it seems appropriate, and likely more efficient and fairer from the point of view of the individual licensees in the firm, to require the firm to manage and be accountable for these responsibilities."[14]

The Law Society does not currently require the designation of a "responsible lawyer" with respect to trust accounting. That said, the member annual report usually asks several questions regarding firm trust funds and trust property, which may be answered by a firm's managing partner.

In terms of sanctions, the Consultation Paper notes that if compliance or entity regulation were to be implemented, the Law Society would have a continuum of possible responses for non-compliance with professional standards, and the Law Society would consider remedial measures wherever possible. As an example, the Law Society might contact the entity to discuss the reasons for non-compliance and to discuss whether its policies and procedures might be improved if the entity has difficulty implementing or complying with practice management principles. Another possible response might be a compliance audit similar to the existing PMR program. The objective of a compliance audit, or review, would be to assist the entity to ensure that it has implemented the

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[13] Convocation also has by-law making authority with respect to the practice of law and the provision of legal services through professional corporations under s. 62(0.1)28.1 of the Law Society Act, RSO 1990, c L.8. Convocation has enacted by-law 7 (Business Entities) to provide a regulatory framework for limited liability partnerships and professional corporations. Section 61.0.4(2) currently permits audit, investigation and prosecution of a professional corporation, as well as of individuals. This authority has not been implemented through Law Society by-laws or policy.

[14] Treasurer's Report to Convocation, June 25, 2015, (Part 2), Proposed Task Force on Compliance-Based Entity Regulation, at paras. 40-41.

practice management principles. The question arises why this cannot just be done as it is now with respect to compliance-based regulation, without additional entity regulation.

There appears to be an assumption on the part of the LSUC Task Force that the addition of a new entity regulation regime is necessary in order to effectively implement compliance-based regulation. A number of our members indicated that the Law Society may possess the requisite authority to effectively implement a compliance-based regulatory scheme without the need for additional entity-based regulatory powers beyond those already available to the Law Society.

To the extent that the LSUC Society Task Force believes there are gaps or deficiencies, the OBA believes it is important for it to articulate those in the context of a proposed compliance-based regulatory scheme in order to facilitate a meaningful discussion on the merits of additional entity regulation. We believe this would help avoid unanticipated overlap with the Law Society's regulation of individual lawyers, and allow for a more informed discussion of whether a designated practitioner is required, and the roles and responsibilities of that person.

Until such time, the OBA is not in a position to support the implementation of entity regulation, as we believe there is an insufficient basis in which to appropriately consider its necessity, scope and particulars.

Conclusion

OBA members across Ontario share a keen interest in promoting a strong and relevant bar that allows lawyers to best serve the public. The OBA appreciates the Law Society's commitment to engaging the profession in a consultation to fully consider compliance and entity regulation, and looks forward to continuing to contribute to the Law Society's consideration of these issues as the Law Society further considers the issues raised in this Consultation Paper.