REGULATING LAW FIRMS IN CANADA*

Adam M Dodek**

Law societies should regulate law firms. This article identifies the regulatory anomaly of law firms being ever present in the practice of law in Canada but peripheral in the regulation of lawyers in this country. Law societies should regulate law firms primarily on the basis of ensuring public confidence in self-regulation and respect for the rule of law and only secondarily out of concerns for public protection. The author conducts a "regulatory audit" of how law societies in Canada currently regulate law firms and also examines how law firms are regulated in comparable jurisdictions. The author then presents a suggested template for law firm regulation.

Les barreaux devraient assurer la réglementation des cabinets juridiques. Cet article vise à identifier les lacunes réglementaires qui découlent du fait que si les cabinets juridiques sont omniprésents dans la pratique du droit au Canada, ils sont aux abords de la réglementation des juristes au pays. Les barreaux devraient se charger de la réglementation des cabinets, dans un premier temps, afin d'assurer la confiance du public quant à l'autoréglementation et le

* This article is dedicated to Harry Arthurs who paved the way. We walk in your shadow every day.

** Associate Professor, Faculty of Law, Common Law Section, University of Ottawa. Thanks to Joanne St Lewis for her inspiration, collaboration and facilitation of this project. Thanks to Brent Cotter, Richard Devlin, Trevor Farrow, Allan Fineblit, Stephen Goudge, Rand Graham, Allan Hutchinson, John M Law, Paul Paton, Darrel Pink, Stephen Pitel, Lorne Sossin, Alan Treleaven, Alice Woolley and two anonymous reviewers for reading earlier drafts of this article and providing helpful comments. This project could not have been completed without the contributions of several outstanding JD students at the University of Ottawa's Faculty of Law. Lars Brusven and Katelyn Wiley were the lead researchers on this project and they immersed themselves in the subject and did fabulous work. Niklas Holmberg, Jarrod Olson and Flora Stikker also contributed to the work of this paper. Thanks to Christine Parker for helpful discussions about the regulation of law firms in Australia and to Noah Dodek and Kevin Cohen for educating me about securities compliance issues. In addition, numerous officials at various regulators across the country and abroad were very responsive in providing information about their work. I am especially grateful to Darrel Pink, Executive Director of the Nova Scotia Barristers' Society, for sharing his time and the work of the Barristers' Society on the regulation of law firms. The author extends his appreciation to Malcolm Mercer, General Counsel and Partner, McCarthy Tétrault, for convening a meeting of law firm general counsel in Toronto in 2011 which greatly assisted the author in understanding some of the issues faced by large law firms. Support for this project was provided by the Law Foundation of Ontario for which the author expresses his gratitude.

respect de la primauté du droit, et dans un deuxième temps, en vue d'assurer subsidiairement la protection du public. L'auteur effectue une analyse des règlements relatifs à la pratique courante des barreaux canadiens quant à la réglementation des cabinets juridiques, ainsi qu'un examen de la réglementation des cabinets dans des juridictions semblables. Enfin, l'auteur présente un modèle de réglementation des cabinets juridiques.

> The Law Society regulates lawyers, not lawyers and firms, even though there are roughly 3,400 firms of lawyers in the province. As others here have pointed out, there may be a public interest in regulating firms, because firms have cultures and ways of doing things that firm members are expected to respect, and the firms, therefore, can influence lawyer conduct. We are exploring means by which firms can be drawn under the regulatory umbrella.
>
> Gordon Turriff, QC, Past President, Law Society of British Columbia (2009)[1]

> The Law Society of Upper Canada exists to govern the legal profession in the public interest by ensuring that the people of Ontario are served by lawyers who meet high standards of learning, competence and professional conduct, and upholding the independence, integrity and honour of the legal profession, for the purpose of advancing the cause of justice and the rule of law.
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> Law Society of Upper Canada, Role Statement (1994)[2]

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[1] Gordon Turriff, QC, President Law Society of British Columbia, "Self-Governance as a Necessary Condition of Constitutionally Mandated Lawyer Independence in British Columbia," Speech delivered at the Conference of Regulatory Officers in Perth, Australia, October 2009, PDF of speech updated December 2009 and available online at: <http://www.lawsociety.bc.ca/publications_forms/report-committees/docs/turriff-speech.pdf>.

[2] Law Society of Upper Canada, Minutes of Convocation, Research and Planning Committee report to Convocation, 27 October 1994. This Role Statement is now incorporated somewhat less elegantly into ss 4.1 and 4.2 of the *Law Society Act*, RSO 1990, c L-8. Section 4.1 provides, *inter alia,* that "It is the function of the Society to ensure that (a) all persons who practise law in Ontario or provide legal services in Ontario meet standards of learning, professional competence and professional conduct that are appropriate for the legal services they provide …." Section 4.2 provides in relevant part,

> In carrying out its functions, duties and powers under this Act, the Society shall have regard to the following principles:
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> 1. The Society has a duty to maintain and advance the cause of justice and the rule of law.
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> 2. The Society has a duty to act so as to facilitate access to justice for the people of Ontario.
>
> 3. The Society has a duty to protect the public interest.

1. Introduction: The Centrality of Law Firm Practice and the Absence of Law Firm Regulation

In Canada, provincial legislatures have entrusted law societies to regulate the practice of law in the public interest.[3] In attempting to fulfill this mandate, the statutory provisions and the regulatory focus of law societies have always focused on the people who provide legal services rather than on the vehicles through which legal services may be provided. This approach dates back to the origins of self-regulation of the legal profession in Canada with the creation of the Law Society of Upper Canada in 1797 when ten lawyers, representing fully two-thirds of the practicing lawyers in the colony of Upper Canada, gathered in what is now Niagara-on-the-Lake to found the Law Society of Upper Canada.[4] The traditional model of the delivery of legal services then was the sole lawyer in private practice. This model has survived for over two centuries. However, over the last thirty years significant changes have occurred in the structure of the Canadian legal profession.

Law firms of all sizes are now omnipresent in the Canadian legal profession. By 1990, David Stager and Harry Arthurs observed that the dominant model of the sole practitioner had "been replaced … by partnerships of diverse size, structure and location."[5] The same year the Supreme Court of Canada wrote rather prematurely of "the virtual disappearance of the sole practitioner" in large urban centres.[6] However, like Mark Twain, reports of the death of the sole practitioner have been greatly exaggerated.[7] The Law Society of Upper Canada's *2009 Annual Report* records that twenty-three per cent of all lawyers in Ontario are sole practitioners and over half of Ontario lawyers are "smalls and soles" –

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4. The Society has a duty to act in a timely, open and efficient manner.

5. Standards of learning, professional competence and professional conduct for licensees and restrictions on who may provide particular legal services should be proportionate to the significance of the regulatory objectives sought to be realized."

3 The regulation of the professions is a matter of provincial competence under constitutional division of powers; see generally *Law Society of British Columbia v Mangat*, 2001 SCC 67 at para 38, 3 SCR 113; *Attorney General of Canada v Law Society of British Columbia*, [1982] 2 SCR 307; and *Lafferty v Lincoln* (1907), 38 SCR 620.

4 See Christopher Moore, *The Law Society of Upper Canada and Ontario's Lawyers, 1797-1997* (Toronto: University of Toronto Press, 1997) at 13.

5 *Lawyers in Canada* (Toronto: University of Toronto Press, 1990) at 166.

6 *MacDonald Estate v Martin,* [1990] 3 SCR 1235, SCJ No 41 (QL) at para 14 *per* Sopinka J [*Martin v Gray*].

7 *Ibid* at para 68. In *Martin v Gray,* Cory J, concurring in the result, rightly took Sopinka J to task for his fixation on the "large firm," noting that the then-latest statistics of the Law Society of Upper Canada showed that 64% of all lawyers worked in firms of 1-10 lawyers (noting that outside metropolitan Toronto the figure was 82%).

lawyers working in small firms with ten or fewer lawyers or sole practitioners.[8]

Without denying the continued importance of sole and small firm practitioners, it is important to recognize that close to half of all Canadian lawyers practice in law firms with more than ten lawyers.[9] Moreover, the rise of the large law firm, variously defined as larger than 50 or 75 lawyers,[10] is an important feature of the Canadian legal profession. In 2009, one in four Ontario lawyers in private practice worked in a firm with more than 25 lawyers.[11] The trend across the country is similar: more and more lawyers are practicing in medium and large law firms.[12]

While law firms are ever present in the practice of law, they are peripheral in the regulation of lawyers in Canada. At the very least, this discrepancy presents a question that should be addressed: should law firms be regulated?[13] This question has not escaped the notice of law societies,

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8 Law Society of Upper Canada, *2009 Annual Report* (Toronto: Law Society of Upper Canada, 2010) at 6, online: http://www.lsuc.on.ca/media/ar_perf_2009_en_web.pdf [Law Society of Upper Canada, *2009 Annual Report*]. Statistics in other provinces are similar. See Federation of Law Societies of Canada, *2007 Law Societies' Statistics* at 7, online: http://www.flsc.ca/en/pdf/statistics2007.pdf [Federation of Law Societies, *2007 Statistics*]. Law societies have rightly focused on issues concerning sole practitioners and small firm practitioners through such measures as the creation of the Sole Practitioner and Small Firms Task Force (Ontario). Statistics from 2009 are used because the Law Society of Upper Canada's 2010 statistics includes combined numbers for both lawyers and regulated paralegals; see Law Society of Upper Canada, *2010 Annual Report* (Toronto: Law Society of Upper Canada, 2011) 8, online: <http://www.lsuc.on.ca/WorkArea/DownloadAsset.aspx?id=2147485006>.

9 See Federation of Law Societies, *2007 Statistics*, *ibid*.

10 In 1990, Stager and Arthurs described firms of 21-75 as "large" and those with more than 75 lawyers as "mega-firms;" see Stager and Arthurs, *supra* note 5 at 169. While the Federation of Law Societies of Canada does not classify law firms in descriptive terms, it divided them into sole practitioners, firms of 2-10 lawyers, 11-25 lawyers, 26-50 lawyers, and 51+ lawyers; see Federation of Law Societies, *2007 Statistics*, *supra* note 8.

11 See Law Society of Upper Canada, *2009 Annual Report*, *supra* note 8 at 7. Most of these lawyers worked in firms of more than fifty lawyers. Of 22,613 lawyers in private practice, 1,314 (5.8%) worked in firms of 26 to 50 lawyers and 4,476 (19.84%) worked in firms of more than fifty lawyers; see *ibid.*

12 *C.f.* Federation of Law Societies, *2007 Statistics*, *supra* note 8.

13 A related but separate question is the question of the regulation of commercial firms that provide legal services known variously as "multi-disciplinary partnerships" (MDPs) or "alternative business structures" (ABSs). See Paul D Paton, "Multidisciplinary Practice Redux: Globalization, Core Values, and Reviving the MDP Debate in America" (2010) 78 Fordham L Rev 2193; Michael Trebilcock and Lilla Csorgo, "Multidisciplinary Professional Practices: A Consumer Welfare Perspective"

as evident from the comment of the former president of the Law Society of British Columbia excerpted at the beginning of this article. As described below, the Barreau du Québec, the Nova Scotia Barristers' Society and most recently the Law Society of British Columbia have begun to regulate law firms in different ways.

Law societies should regulate law firms. They should do so primarily on the basis of ensuring public confidence in self-regulation and respect for the rule of law and only secondarily out of concerns regarding public protection. The proper question is not, "Why should law firms be regulated?" but "Why do they largely escape law society regulation?" It is widely recognized that law firms have their own culture. It is contested whether this culture strengthens or weakens ethical conduct of the firm's constituent lawyers. Resolution of this issue is not necessary for the purposes of my argument. Once it is acknowledged that the law firm is an independent actor exerting significant influence on the practice of law, the burden of justifying why it should be regulated necessarily shifts.

The absence of law firm regulation creates a problem of legitimacy for law societies mandated to regulate the practice of law in the public interest. This regulatory gap also raises rule of law concerns and may threaten public confidence if the public believes that the most powerful groups of lawyers escape regulation.[14] Bar leaders in Canada have ratcheted up the expectations of self-regulation through the strength of their rhetoric and their actions against perceived incursions of self-regulation. As a result, lawyers in Canada have set the bar for what self-regulation is supposed to accomplish at a very high level. Consequently, the failure to regulate law firms may threaten self-regulation of the legal profession in Canada.

This paper presents an argument and a blueprint for law firm regulation. It has five parts in addition to this introduction. In Part 2, I detail why Canadian law societies should regulate law firms. Part 3 undertakes a "regulatory audit"[15] of how law societies in Canada currently

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(2001) 24 Dal LJ 1; Kent Roach and Edward Iacobucci, "Multidisciplinary Law Partnerships and Practices: Problems, Prospects and Policy Options" (2000) 79 Can Bar Rev 1.

[14] I raise similar concerns respecting the regulation of government lawyers in Adam M Dodek, "Lawyering at the Intersection of Public Law and Legal Ethics: Government Lawyers as Custodians of the Rule of Law" (2010) 33 Dal LJ 1. The difference is that government lawyers exercise public power whereas law firms exercise private power. On the exercise of power by lawyers see Adam M Dodek, "Lawyers, Guns and Money: Lawyers and Power in Canadian Society" in David L Blaikie, Thomas A Cromwell and Darrel Pink, eds, *Why Good Lawyers Matter* (Toronto: Irwin Law, 2012).

[15] I take the idea of a "regulatory audit" from Richard Devlin and Albert Cheng, "Re-calibrating, Re-visioning and Re-thinking Self-regulation in Canada" (2010) 17(3)

regulate law firms. In this section and in this paper I focus mainly on the Law Society of Upper Canada as the regulator of the largest number of lawyers in Canada as well as the jurisdiction with which I am most familiar. Then I turn to comparative experience in Part 4 by examining how law firms are regulated in three comparable jurisdictions: the United States, Australia and the United Kingdom. Then in Part 5, I present a suggested template for law firm regulation.[16] Finally, Part 6 provides a brief conclusion.

2. The Core Case for Regulating Law Firms

Why should law societies regulate law firms? As stated above, the number of lawyers practicing in firms is significant. However, numbers alone do not warrant a shift in the inquiry from individuals to entities. There are substantive reasons as well. It is widely recognized that "the firm" is a significant entity for understanding the practice of law.[17] As lawyers have increasingly grouped together in firms to provide legal services, collective firm cultures are created. There are no doubt firm cultures that are created by small associations or partnerships, but the smaller the organization, the more that culture can be traced to the constituent parts. When extended beyond a few lawyers, firms are likely to develop a separate and distinct

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Int'l J of the Legal Profession 233 at 234. I was also inspired by the Auditing Canadian Democracy series edited by William Cross; see William Cross, ed, *Auditing Canadian Democracy* (Vancouver: UBC Press, 2010).

[16] I am indebted to Richard Devlin and Porter Hefferman, "The End(s) of Self-Regulation" (2008) 45 Alta L Rev 169 for inspiration for the structure of this article.

[17] Most of the literature is American. See Marc Galanter and Thomas Palay, *Tournament of Lawyers: The Transformation of the Big Law Firm* (Chicago: University of Chicago Press, 1991) [Galanter and Palay, *Tournament of Lawyers*]; Mark Stevens, *Power of Attorney: The Rise of the Giant Law Firms* (New York: McGraw-Hill, 1987); Marc Galanter and Thomas M Palay, "Why the Big Get Bigger: The Promotion-to-Partner Tournament and the Growth of Large Law Firms" (1990) 76 Va L Rev 747; Richard H Sander and E Douglas Williams, "A Little Theorizing About The Big Law Firm: Galanter, Palay, and the Economics of Growth" (1992) 17 Law & Soc Inquiry 391; Robert L Nelson, *Partners with Powers: Social Transformation of the Large Law Firm* (Berkeley: University of California Press, 1988); Robert L Nelson, "Ideology, Practice, and Professional Autonomy: Social Values and client Relationships in the Large Law Firm" (1985) 37 Stan L Rev 503; Ronald Gilson and Robert Mnookin, "Sharing among the Human Capitalists: An Inquiry into the Corporate Law Firm and How Partners Split Profits" (1985) 37 Stan L Rev 313. In the Canadian context see Ronald J Daniels, "Growing Pains: The Why and How of Canadian Law Firm Expansion" (1993) 42 UTLJ 147 and Ronald J Daniels, "The Law Firm as an Efficient Community" (1993) 37 McGill LJ 801 [Daniels, "Efficient Community"].

organizational culture.[18] This is most notable for large law firms but also exists for medium-size and possibly for smaller firms as well.

Law firms are front and center in the lawyer-client relationship. As Lucie Lauzière has written, "[t]he law firm is now the intermediary between client and lawyer."[19] This is certainly true in terms of advertising, solicitation, client intake, conflicts of interest, retainer agreements, billings and many other interactions that clients and potential clients have with the delivery of legal services via "the firm." With larger law firms, the influence of a collective culture may be even stronger.

On large law firms, the American scholars Marc Galanter and Thomas Palay have written that "[t]he big law firm is … a social form for organizing the delivery of comprehensive, continuous, high-quality legal services. Like the hospital as a way to practice medicine, the big firm provides the standard format for the delivering complex services."[20] While law firms south of the border may be bigger and the profits (and therefore the stakes) higher, Canadian law firms chiefly parallel their American counterparts. This should not be surprising given that Canadian law firms have molded themselves in the image of their American models.

The importance of firm culture has also been recognized in Canada. In the Canadian context, Ronald Daniels argued that "… in the setting of the modern corporate law firm, firm culture constitutes an important, indeed, essential component of the theory of the firm. By taking culture seriously, the behaviour and structure of the corporate law firm can be much more

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[18] See Lynn Mather, "How and Why Do Lawyers Misbehave? Lawyers, Discipline and Collegial Control" in Scott L Cummings, *The Paradox of Professionalism: Lawyers and the Possibility of Justice* (Cambridge: Cambridge University Press, 2011) 109 at 116: "There is also a growing empirical literature describing the shared expectations and professional values of particular legal cultures and subcultures." On law firms, see Kimberly Kirkland, "Ethics in Large Law Firms: The Principle of Pragmatism" (2005) 35 U Mem L Rev 631; Mark C Suchman, "Working Without a Net: The Sociology of Legal Ethics in Corporate Litigation" (1998) 67 Fordham L Rev 837; Michael J Kelly, *Lives of Lawyers* (Ann Arbor: University of Michigan Press, 1994); Michael J Kelly, *Lives of Lawyers Revisited: Transformation and Resilience in the Organizations of Practice* (Ann Arbor: University of Michigan, 2007); Emmanuel Lazega, *The Collegial Phenomenon: The Social Mechanisms of Cooperation Among Peers in a Corporate Law Partnership* (Oxford: Oxford University Press, 2001).

[19] Lucie Lauzière, "Dependence and Interdependence in the Lawyer-Client Relationship" in Law Commission of Canada, ed, *Personal Relationships of Dependence and Interdependence in Law* (Vancouver: UBC Press, 2002) 40 at 41.

[20] Galanter and Palay, *Tournament of Lawyers*, *supra* note 17 at 2.

easily explained."[21] In larger firms, the whole may be larger than the sum of its parts. Law firms are increasingly recognized as an important arena and agent of professional conduct.[22] The American Bar Association's *Model Rules* regarding law firms recognize that "the ethical atmosphere of a firm can influence the conduct of all its members …"[23] This necessitates a separate focus on firm regulation.

Moreover, both American and Canadian commentators have expressed concerns about the ethics of large law firm practice. The American literature is voluminous[24] and the tales of ethical malfeasance at large law firms are legion.[25] Galanter and Palay observed that "… there is

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21 Daniels, "Efficient Community," *supra* note 17 at 804. For a discussion on the role of culture in "elite" law firms, see Harry W Arthurs, "The Dead Parrot: Does Professional Self-Regulation Exhibit Vital Signs?" (1995) 33 Alta L Rev 800 at 805-07 [Arthurs, "Dead Parrot"].

22 See Robert L Nelson and DM Trubek, "Arenas of Professionalism: The Professional Ideologies of Lawyers in Context" in RL Nelson, DM Trubek and RL Solomon, eds, *Lawyers' Ideals/Lawyers Practices: Transformation in the American Legal Profession* (Ithaca: Cornell University Press, 1991)177; Milton C Regan, "Taking Law Firms Seriously" (2002) 16 Geo J Legal Ethics 155; Milton C Regan, "Moral Intuitions and Organizational Culture" (2007) 51 St Louis U LJ 941; Kirkland, *supra* note 18; Elizabeth Chambliss, "The Professionalization of Law Firm In-House Counsel" (2006) 84 NC L Rev 1515; Elizabeth Chambliss, "New Sources of Managerial Authority in Large Law Firms" (2009) 22 Geo J Legal Ethics 63; LC Levin, "The Ethical World of Solo and Small Law Firm Practitioners" (2004) 41 Hous L Rev 305; DN Frenkel, R L Nelson and A Sarat, "Bringing Legal Realism to the Study of Ethics and Professionalism" (1998) 67 Fordham L Rev 697.

23 American Bar Association, *Model Rules of Professional Conduct*, Rule 5.1, Commentary 2, online: http://www.abanet.org/cpr/mrpc/rule_5_1_comm.html.

24 See e.g. Mary Ann Glendon, *A Nation Under Lawyers* (Cambridge: Harvard University Press, 1994) at 17-39; Anthony T Kronman, *The Lost Lawyer: Failing Ideals of the Legal Profession* (Cambridge: Belknap Press, 1991) at 291-300 (critical of internal culture of large law firms and preoccupation with making money); Deborah L Rhode, "Ethical Perspectives on Legal Practice" (1985) 37 Stan L Rev 589 at 626; Ralph Nader and Wesley J Smith, *No Contest: Corporate Lawyers and the Perversion of Justice in America* (New York: Random House, 1996); Sol M Linowitz with Martin Mayer, *The Betrayed Profession: Lawyering at the End of the Twentieth Century* (New York: Charles' Scribner's Sons, 1994) at 91-112; Cameron Stracher, *Double Billing: A Young Lawyer's Tale of Greed, Sex, Lies, and the Pursuit of a Swivel Chair* (New York: William Morrow, 1998); and Michael H Trotter, *Profit and the Practice of Law* (Athens and London: University of Georgia Press, 1997).

25 See e.g. Milton C Regan, Jr, *Eat What You Kill: The Fall of a Wall Street Lawyer* (Ann Arbor: University of Michigan Press, 2006); Steven J Kumble and Kevin J Lahart, *Conduct Unbecoming: The Rise and Ruin of Finley, Kumble* (New York: Carroll & Graf Publishers, Inc 1990); and Patrick Dillon and Carl M Cannon, *Circle of Greed: The Spectacular Rise and Fall of the Lawyer Who Brought Corporate America to its Knees* (New York: Broadway Books, 2010). Conversely, tales of ethical conduct – especially *pro*

a palpable anxiety and dismay within the legal profession concerning commercialization and the concomitant decline of professionalism in the setting of the big law firm."[26] Similar concerns about the impact of the growing commercialization of large law firm practice on the practice of law have been raised in Canada.

In his Goodman Lecture at the University of Toronto, Justice Stephen T Goudge of the Court of Appeal of Ontario lamented the imposition of business structures and techniques onto the practice of law in large law firms. Goudge, a former law firm managing partner and bencher, asked whether lawyers will "increasingly see anything but the narrowest aspects of professionalism – such as the most minimal compliance with the rules of professional conduct required to escape the discipline process – as a luxury they can no longer afford in the frantic scramble to do law as business?"[27] The fear raised by Justice Goudge is that the culture of the law firm can create the danger of what Deborah Rhode has described as

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bono work – at large law firms are also on the rise. Most notably, large law firm lawyers represented many of the Guantanamo Bay detainees; see Mike Scarcella and David Ingram, "Big Law Defends Guantanamo Lawyers" *The National Law Journal* (8 March 2010), online: http://www.law.com/jsp/article.jsp?id=1202445796111. On pro bono activity in large law firms generally see Ronit Dinovitzer and Bryant G Garth, "Pro Bono as Elite Strategy in Early Lawyer Careers" in Robert Granfield and Lynn Mather, eds, *Private Lawyers & the Public Interest* (New York: Oxford University Press, 2009) 115; Steven A Boutcher, "The Institutionalization of Pro Bono in Large Law Firms: Trends and Variation across the AmLaw 200" in Granfield and Mather, *ibid* at 135.

26 Galanter and Palay, *Tournament of Lawyers*, *supra* note 17 at 2. For a contrary view see Scott Cawood, "Law Firms as Great Places to Work" in Lawrence J Fox, ed, *Raise the Bar: Real World Solutions for a Troubled Profession* (Chicago: ABA, 2007) 67.

27 The Honourable Justice Stephen T Goudge, "Looking Back and Looking Forward on Learning in Professionalism" (2010) Can Legal Ed Ann Rev 109 at 114 (The 2008-09 David B Goodman Lecture, Faculty of Law, University of Toronto, 20 February 2009):

> These [national mega-firms] tend to spread their business ways well beyond the upper reaches of the profession that they are seen to inhabit. The measure of success becomes profitability. Income expectations become the primary driver of legal activity. Billable hours come to reflect the lawyer's ability to serve the needs of the client and the justice system. Business techniques are imported which previously would have been regarded as anathema – notions of corporate governance, firm branding, and marketing techniques are now simply a part of everyday life in law in the urban setting. While this paradigm is far from universal, it sets a powerful example that others seek to emulate. The challenge this presents is clear. Will lawyers increasingly see anything but the narrowest aspects of professionalism – such as the most minimal compliance with the rules of professional conduct required to escape the discipline process – as a luxury they can no longer afford in the frantic scramble to do law as business?

"ethical tunnel vision."[28] Canadian historian Christopher Moore has questioned the extent to which "professional ethics and the professional independence of the lawyer can endure in the [Profits-Per-Partner] legal environment in which law firms become businesses like any business."[29]

The negative view of law firm culture is not universally shared. Others like Daniels argue that law firms have a "shared commitment to professional excellence and integrity" such that the partners will monitor the behaviour of their peers in order to preserve and protect the firm's reputation.[30] Arthurs, Weisman and Zemans wrote that the conditions at "elite" law firms produce "an extreme commitment to meeting deadlines, covering all eventualities, and avoiding technical errors."[31] For the purposes of this paper, it is neither necessary nor desirable to resolve the question of whether law firms are a positive or negative force on the ethical conduct of the lawyers who practice therein.[32] It is sufficient only to

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28 Rhode, *supra* note 24 at 627.

29 Christopher Moore, "Megafirm: A Chronology for the Large Law Firm in Canada" in Constance Backhouse and W Wesley Pue, eds, *The Promise and Perils of Law: Lawyers in Canadian History* (Toronto: Irwin Law, 2009) 103 at 125.

30 Daniels, "Efficient Community," *supra* note 17 at 827 (describing the shared commitments to professional excellence and integrity within law firms and the impact of reputational bonds and partner monitoring on ethical behaviour of lawyers within law firms).

31 Harry W Arthurs, Richard Weisman and Frederick H Zemans, "Canadian Lawyers: A Peculiar Professionalism" in Richard L Abel and Philip S C Lewis, eds, *Lawyers in Society: The Common Law World* (Berkeley: University of California Press, 1988) 123 at 154.

32 For my part, I see aspects of the structure of law firms that shield lawyers from numerous forms of ethical malfeasance. Large law firm lawyers do not personally handle trust accounts. Law firms have systems to track correspondence, court dates and conflicts. By taking care of the business of the practice of law, law firms shield their lawyers from many areas which can be source of ethical problems for sole practitioners or small firm lawyers. Moreover, as Harry Arthurs so aptly observed, the "ethical economy" of the legal profession is such that in practice only certain types of ethical misconduct is likely to attract law society attention. According to Arthurs, there are essentially only four reasons why lawyers in Canada are subject to serious discipline "because they have been guilty of theft, fraud, forgery or some other criminal offence; because they have violated a fiduciary duty imposed on them by law; because they are unable to carry on their practices due to physical or mental disability or serious addiction; or because they have failed to respond to inquiries from their governing body;" see Arthurs, "Dead Parrot," *supra* note 21at 802. The existence of structures within firms makes it difficult for lawyers working within them to fall into the latter two categories. Similarly, it is difficult, although not impossible, for lawyers at larger law firms to steal from their clients' trust accounts. There are therefore structural reasons why large law firm lawyers are less likely to attract the attention of their governing bodies. Whether law societies are focusing on the right issues is another matter entirely.

establish that law firms are relevant actors in terms of their impact on regulation. As set out above, this is supported by the literature. However, in terms of law societies' statutory mandate to regulate the practice of law in the public interest, the perception of ethical misconduct within large law firms is more important than the reality. This perception fuels the need for law society regulation of law firms.

Allegations of ethical misconduct within law firms demonstrate the existence of a regulatory gap. In recent years, there has been a demonstrable increase in reports of ethical malfeasance within Canadian law firms. I have previously described Philip Slayton's *Lawyers Gone Bad*[33] as an "anecdotal collection of lawyer malfeasance."[34] Many of the tales in that book involve large law firm lawyers.[35] My point is not that law firms are dens of ethical malfeasance, but rather that some of these cases clearly demonstrate a gap in the regulation of lawyers because they may be characterized as a collective failure within the law firm rather than simply the act or acts of individual lawyers. For example, the Pilzmaker-Lang Michener affair from the 1980s involved a collective decision by the firm management not to report Pilzmaker to the Law Society.[36] That decision was not simply an individual one or a group of individual choices. It was a collective decision by leaders of the firm that either reflected existing firm policy or an ad hoc policy determination by the firm. The best interpretation is that the decision reflected a lack of firm policy is this respect. Treating the Lang Michener decision as one of multiple individual malfeasance mischaracterized what transpired. The ethical problem was a collective or systemic one, hence the continued reference within the bar to "the Lang Michener Affair." Other than Pilzmaker – the lawyer at the firm whose actions precipitated the crisis – the names of the Lang Michener partners are not generally referenced in discussions about the affair.

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33 Philip Slayton, *Lawyers Gone Bad* (Toronto: Viking, 2007).

34 See Adam M Dodek, "Canadian Legal Ethics: Ready for the Twenty-First Century at Last" (2008) 44 Osgoode Hall LJ 1 at 19.

35 Slayton, *supra* note 33 at 25-30 (Martin Pilzmaker at Lang Michener in Toronto); 30-38 (Bob Donaldson at Blake Cassels Graydon in Toronto); 39-49 (Dan Cooper at McCarthy Tétrault in Toronto); 84-100 (Robert Strother at Davis & Company in Vancouver); 101-114 (George Hunter at Borden Ladner Gervais LLP in Ottawa); 162-177 (Richard Shead at Buchwald Asper Henteleff in Winnipeg).

36 See Law Society of Upper Canada, *Report and Decision of the Discipline Committee In the Matter of the Law Society Act and in the Matter of Albert Knat, Bruce Carr McDonald, Bruce Andrew McKenna, Donald Neville Plumley, and Donald John Wright*, 8 January 1990 [unpublished] (available from the Tribunals office of the Law Society of Upper Canada and on file with author) [Lang Michener discipline decision].

Similarly, discipline cases involving law firm lawyers for conflicts of interest likely implicate not only the decisions of individual lawyers but firm policies. The current Law Society of Upper Canada discipline hearings against Torys LLP lawyers Beth DeMerchant and Darren Sukonick are a case in point.[37] DeMerchant and Sukonick stand accused by the Law Society of Upper Canada of violating the *Rules of Professional Conduct* by acting in a conflict of interest in relation to high profile transactions involving Conrad Black, Hollinger Inc and the sale of certain Hollinger assets to Canwest Global Communications. It is inaccurate to state that the decisions whether to represent multiple interests were made by DeMerchant and Sukonick alone. They would have been made in accordance with policies at their firms regarding conflicts. During the key period where DeMerchant and Sukonick are alleged to have acted in a conflict of interest – May 2000 to December 2003 – Sukonick was a fourth to sixth year associate.[38] It strains credibility to believe that a mid-level or senior associate or even a junior partner at a large corporate law firm would be in a position to make decisions on his own regarding retaining a client or disclosing potential conflicts of interest. While DeMerchant and Sukonick should surely be held accountable for their actions, focusing solely on these individuals misses part of the story of how the practice of law operates and how it should be regulated.

Another example that demonstrates the existence of such a regulatory gap involves the actions of the Winnipeg law firm of Thompson Dorfman Sweatman (TDS) in connection with Jack King, the husband of Associate Chief Justice of the Manitoba Court of Queen's Bench, Lori Douglas.[39]

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[37] See Law Society of Upper Canada, "Regulatory Proceedings, Current Hearings," online: <http://www.lsuc.on.ca/WorkArea/DownloadAsset.aspx?id=2147486413> (DeMerchant) and <http://www.lsuc.on.ca/WorkArea/DownloadAsset.aspx?id=2147486419> (Sukonick). See also Editorial, "The Torys fiasco: who was double-checking?" *The Law Times* (3 May 2010) 6 ("Torys, too, has questions to answer given the public interest in timely and efficient regulation by the LSUC.") and Jim Middlemiss, "Conflicts case a circus" *Canadian Lawyer* (January 2012), online: <http://www.canadianlawyermag.com/3986/conflict-case-a-circus.html>.

[38] Sukonick was called to the bar in Ontario in 1996; see his profile on the Torys website at <http://www.torys.com/OurTeam/Pages/SukonickDarrenE.aspx>. Full disclosure: Sukonick is an acquaintance; we attended summer camp together in 1986 and we attended McGill together. I last saw him at a dinner with mutual friends 7-8 years ago. We have never discussed these matters.

[39] This case quickly became notorious and was widely reported in the press. The Canadian Judicial Council has ordered that a public inquiry be held into the conduct of Justice Douglas. See Canadian Judicial Council, "Canadian Judicial announces it will proceed with a public inquiry in the case of Associate Chief Justice Lori Douglas" (6 July 2011), online: <http://www.cjc-ccm.gc.ca/english/news_en.asp?selMenu=news_2011_0706_en.asp>. For my report of the ethical issues involves in this matter see Adam

Both King and Douglas were partners at TDS when it is alleged that King attempted to lure a client into entering into a sexual relationship with Douglas by providing the client with salacious photos of Douglas. The client apparently complained to the partners at TDS and soon after King left the firm. King reportedly paid his former client $25,000 as part of a settlement agreement. At the time, the Law Society of Manitoba took no disciplinary action against King or against other lawyers at TDS. When the former client launched a complaint in 2010, the Law Society reopened its investigation and retained an independent prosecutor. King reached a consent agreement with the Law Society and received a reprimand.[40] Questions have been raised as to how the law firm handled the matter in 2003 and the extent to which it reported the actions of its partner, King, to the Law Society. The Law Society of Manitoba was rightly criticized for its failure to take more action in 2003 and for its lenient sanction against King in 2011. The law firm here is clearly on the hotseat but it escapes direct regulatory accountability because of the absence of law firm regulation in Manitoba.

Such cases challenge the legitimacy of self-regulation itself. In 1995, Harry Arthurs wrote a seminal article on self-regulation in Canada.[41] Arthurs offered two hypotheses for what he described as increased revelations of ethical misconduct in large firms: either the lack of structural or informal understandings with which to control lawyers working in the firm, or the inability to conceal any longer misconduct which may have always been common.[42] In describing the Law Society of Upper Canada's handling of misconduct in large law firms in the early 1990s, Arthurs stated that "[t]he Law Society's handling of misbehaviour in elite firms came to be seen as the ultimate test of the profession's moral right to regulate

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Dodek, "Sex on the Internet and Fitness for Judicial Office: Correspondent's Report from Canada" (2011) 13:2 Legal Ethics 215.

40 See Law Society of Manitoba Discipline Digest, <http://www.lawsociety.mb.ca/lawyer-regulation/discipline-case-digests/documents/2010/case_digest_10_13.pdf>. See also Carol Sanders and Gabrielle Giraday, "Disgraced lawyer gets reprimand; Law Society raps knuckles for soliciting sex with wife" *Winnipeg Free Press* (29 March 2011), online: <http://www.winnipegfreepress.com/local/disgraced-lawyer-gets-reprimand-118826224.html>; Editorial, 'No surprise that King got love tap' *Winnipeg Sun* (29 March 2011), online: <http://www.winnipegsun.com/comment/editorial/2011/03/29/17790611.html>.

41 Arthurs, "Dead Parrot," *supra* note 21 .

42 *Ibid* at 806; see also Harry Arthurs, "Lawyering in Canada in the 21st Century" (1996) 15 Windsor YB Access Just 202 at 222.

itself."[43] Arthurs concluded that "the Law Society came near to failing this test, at least from a public point of view."[44]

In addition, it appears that law firms are attracting more attention in the courts and in the press. Over the past few years, there has been an increased propensity for law firms to be named as defendants in actions either as a result of the individual actions of their partners or what could be considered firm policies or decisions.[45] While there is a difference between professional liability and professional misconduct, often the relevant factual matrix overlaps.[46] Again, the issue for me is not whether there is an increase in ethical malfeasance at law firms but rather that there is a notable increase in questions being raised about conduct within law firms.

Law societies should regulate law firms because the perception exists that members of large law firms receive favourable treatment from regulators. This perception undermines the claims of self-regulation being in the public interest. On the existence of the perception that law societies favour the professional elite over less well-connected lawyers, Wes Pue has written that "[w]hether this perception is attributable primarily to an over-suspicious turn of mind (fed by failures of communications from law societies, perhaps) or reflects a systemic bias is, to some extent, moot.

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43 *Ibid* at 807. Arthurs attributes this near failure to "bad judgments by the firms themselves, delays in the discipline process, obfuscatory explanations and light penalties."

44 *Ibid.*

45 See Tim Naumetz, "Cassels case reads like a blockbuster script" *Law Times* (1 February 2010) (quoting Simon Chester of Heenan Blaikie that "[i]t is the largest conflict of interest case in Canadian history"); Jeff Gray, "GM suit reignites conflict argument" *Globe and Mail* (6 April 2010), online: <http://www.theglobeandmail.com/report-on-business/industry-news/the-law-page/gm-suit-reignites-conflict-argument/article1525335/>; *Trillium Motor World Inc v General Motors of Canada Limited*, 2011 ONSC 1300 (alleging that law firm was in a conflict of interest); Michelle Henry, "Woman alleges sexual discrimination in lawsuit against Toronto-based firm" *The Star* (15 February 2011), online: <http://www.thestar.com/news/article/938888—woman-alleges-sexual-discrimination-in-lawsuit-against-toronto-based-firm> (*Jaime Laskis v Osler, Hoskin & Harcourt LLP*, US District Court SDNY Court File No 11 Civ 0585); *Bruno Appliance v Cassels Brock & Blackwell LLP*, 2010 ONSC 5490, OJ No 4661 (QL) (allegations of vicarious liability against the firm as well as alleging a systemic failure against the firm); *Allen v Aspen Group Resources* (2009), 81 CPC (6th) 298 (ONSC) (certifying class action against, *inter alia*, law firm that acted in connection with a take-over bid); *Robinson v Rochester Financial Limited*, 2010 ONSC 46, 89 CPC (6th) 91 (certifying class action against parties involved in charity investment, including major law firm).

46 For example, a conflict of interest may be the subject of a motion for disqualification in court, a cause of action in tort for breach of fiduciary duty and law society discipline for breach of ethical rules. See *R v Neil*, 2002 SCC 70 at para 37, 3 SCR 631.

Perceptions take on lives of their own."[47] These perceptions and questions about the ethical conduct within law firms raise rule of law concerns.

Ultimately, law societies should regulate law firms because of the fundamental rule of law idea that no one is above the law and that the law applies equally to the most powerful as well as to the weakest in society.[48] Law firms exercise significant power within the Canadian legal profession and within Canadian society. The perception that the most powerful within the legal profession lie outside of regulation has the potential to seriously undermine public confidence in self-regulation of the legal profession.[49] It is not enough to simply regulate the individuals who make up law firms because law firms have an independent existence and identity. Individual lawyers promote their practices to the public through the vehicle of the law firm. The public sees law firms but does not see law firms being regulated.

This failure to regulate law firms threatens the profession's claim to the right to self-regulation. As leading American scholars have stated, "the profession's failure to promulgate ethical standards for firms constitutes a significant breach of its duty of self-regulation. This breach threatens not only the quality of modern private practice, but also the credibility of the entire disciplinary system."[50]

Regulating law firms will complement rather than undermine the personal accountability of lawyers. I am arguing for law firm regulation that would supplement not supplant the existing system of lawyer regulation. Two strong arguments against law firm regulation are that (1) it is not necessary because the existing system of individual accountability works well; and (2) it would actually be detrimental because it would weaken individual accountability.[51] The first argument is purely speculative and is frequently criticized because of the lack of systematic

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47 W Wesley Pue, "Death Squads and 'Directions over Lunch': A Comparative Review of the Independence of the Bar" in Law Society of Upper Canada, *In the Public Interest: The Report and Research Papers of the Law Society of Upper Canada's Task Force on the Rule of Law and the Independence of the Bar* (Toronto: Law Society of Upper Canada, 2007) 83 at 107 [Law Society of Upper Canada, *In the Public Interest*].

48 See *British Columbia v Imperial Tobacco Canada Ltd*, 2005 SCC 49 at para 58, 2 SCR 473; and *Reference re Secession of Quebec*, [1998] 2 SCR 217 at para 71.

49 See Elizabeth Chambliss and David B Wilkins, "A New Framework for Law Firm Discipline" (2002) 16 Geo J Legal Ethics 335 at 345. In the American context, Chambliss and Wilkins have written that "… the profession's failure to engage in effective regulation of its most powerful entities may result in the loss of self-regulation altogether."

50 *Ibid* at 344-45.

51 Most notably see Julie Rose O'Sullivan, "Professional Discipline for Law Firms? A Response to Professor Schneyer's Proposal" (2002) 16 Geo J Legal Ethics 1.

analysis to support such a claim.[52] In Canada at least, such assertions are contradicted by the experience of regulation of lawyers at large firms who are rarely subject to regulatory scrutiny.[53] Moreover, even if one believes that the existing regulation of individual lawyers works just fine, that does not license inaction. Regulators must always seek to improve and to optimize regulation and must adapt to changing perceptions and conceptions of the public interest. Regulators have no good response to the question posed by members of the public who see law firms everywhere in the practice of law but nowhere on the regulatory radar. To members of the public and their elected representatives, it would certainly appear as if law firms are receiving a blanket exemption from regulatory scrutiny. This point is supported by the anomaly of the failure of law firm regulation in comparison with entity regulation for all other comparable professions in Canada as set out below.

Similarly, law firm regulation as I propose it would not weaken individual accountability, but would complement it.[54] A system of law firm regulation along the lines that I propose in Part 5 herein would enhance individual accountability by creating an ethical infrastructure for lawyers within a law firm. Individual lawyers would become ethically accountable both to their firms and to their law society. Again, as I explain in Part 5, I propose a system of regulation of law firms which includes the possibility of disciplining firms, but that is not the central feature of my proposal. Rather, the central feature is the creation of compliance requirements that will increase transparency and accountability for the actions of the lawyers

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52 See Elizabeth Chambliss, "The Nirvana Fallacy in Law Firm Regulation Debates" (2005) 33 Fordham Urb L J 119. See generally Anthony E Davis, "Legal Ethics and Risk Management: Complimentary Visions of Lawyers Regulation" (2008) 21 Geo J Legal Ethics 95.

53 See Harry W Arthurs, "Why Canadian Law Schools Do not Teach Legal Ethics" in Kim Economides *et al*, *Ethical Challenges to Legal Education and Conduct* (Oxford: Hart Publishing, 1998) 105 at 115; Alice Woolley, "Regulation in Practice" online: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1976090 at 43: "The ethical economy of Canadian legal regulation is alive and well. Law societies focus regulatory attention on lawyers in small firms or solo practice who have engaged in obvious moral misconduct or flouted the societies' regulatory requirements."

54 Some have argued that the dominant law firm legal structure of the limited liability partnership (LLP) itself undermines individual lawyer accountability. In the notorious *Lawyers Gone Bad, supra* note 33, Philip Slayton asserts that in a traditional partnership, lawyers were liable for the misdeeds of their partners and this created an incentive to ensure that one's partners were trustworthy. However, with an LLP, only the assets of the partnership (i.e. the law firm) are at risk, rather than the individual assets of the partners. According to Slayton, the LLP structure thus shifts risk away from the law firm to clients and insurers and takes away "a powerful incentive to adopt systems that prevent negligence and malfeasance;"see Slayton, *supra* note 33.

in a firm and therefore for the firm as an entity as well. The possibility of discipline of a law firm as an entity should not lessen the accountability of individual lawyers for their ethical violations. It may, however, counsel the imposition of discipline sanctions against a firm in addition to any levied against the individual lawyers.

In the two decades since Arthurs and Daniels provided contrasting perspectives on law firms, the case for their regulation in Canada has strengthened. Law firms have increased in size and influence. Many regulators are aware of the external pressures on self-regulation in Canada arising from the loss of self-regulation in other jurisdictions.[55] As Alice Woolley has written, "Canada is, arguably, the last bastion of unfettered self-regulation of the legal profession in the common law world."[56] Leaders in the legal profession are also, however, generating pressures internally that did not exist two decades ago. Increasingly, legal leaders have been making claims about the moral, legal and indeed the constitutional right to self-regulation. The title of a speech by the former President of the Law Society of British Columbia is self-explanatory: "Self-Governance as a Necessary Condition of Constitutionally Mandated Lawyer Independence in British Columbia."[57]

Moreover, the case for regulation of law firms is buttressed by the regulation of firms in other professions. For many other professionals in Canada, firm regulation is an established part of the regulatory system. Medicine, pharmacy, accounting, engineering, architecture, real estate and securities are all characterized by significant entity regulation. I pause to highlight several relevant examples from accounting, engineering and securities.

The regulation of public accounting firms is commonplace and extensive across Canada. It involves both direct and indirect regulation, compliance and discipline. In Ontario, firm regulation is authorized by legislation and undertaken by each of the three designated public accounting bodies that regulate chartered accountants (CAs), chartered

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55 See generally Paul D Paton, "Between a Rock and a Hard Place: The Future of Self-Regulation—Canada between the United States and the English/Australian Experience" (2008) J Prof Law Symp Issues 87.

56 Alice Woolley, *Understanding Lawyers' Ethics in Canada* (Toronto: Lexis Nexis, 2011) at 4.

57 *Supra* note 1. Others distinguish between lawyer independence and self-regulation. See Patrick J Monahan, "The Independence of the Bar as a Constitutional Principle in Canada" in Law Society of Upper Canada, *In the Public Interest*, *supra* note 47 at11; Roy Millen, "The Independence of the Bar: An Unwritten Constitutional Principle" (2005) 84 Can Bar Rev 107; Roy Millen, "Unwritten Constitutional Principles and the Enforceability of the Independence of the Bar" (2005) 30 Sup Ct L Rev (2d) 463.

general accountants (CGAs) and chartered management accountants (CMAs).[58] In the majority of jurisdictions, public accounting firms are clearly subject to ethical rules and disciplinary procedures. In Ontario, for example, CA firms may be the subject of complaints and may also be found guilty of professional misconduct.[59] Each CA institute, with the exception of Quebec, has adopted a similar version of professional rules.[60]

Every province regulates engineering firms to some degree. Under these systems, there is significant intertwining of individual and firm responsibility and in most provinces it is possible for a firm to be subject to discipline. In Ontario, every engineering firm must hold a certificate of authorization which is essentially a business licence for engineering. In addition to providing basic information about the employees and partners of the firm, every holder of a certificate of authorization must have a supervising engineer who is an employee or partner of the firm.[61] Many

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58 Under the standards created by the Public Accountants Council of Ontario that designated bodies must meet in order to become and remain authorized, each designated body have a process for complaints and discipline against individuals and firms; see Public Accountants Council of Ontario, *Standards for the Public Accountants Council of Ontario* (Approved June 20, 2006), para 12(1), 13(8)(c), online: Public Accountants Council of Ontario, <http://www.pacont.org/docs/Final%20Standards%20-%20June%2020-06.pdf>. The source legislation for each of three designated bodies contains provisions relating to the registration, regulation and discipline of firms. See *Chartered Accountants Act*, SO 2010, c 6, Sched C, ss 21 (registration), 33 (complaints), 35 (discipline); *Certified General Accountants Act*, SO 2010, c 6, Sched A, ss 19-20 (registration), 32 (complaints), 36 (discipline); *Certified Management Accountants Act*, SO 2010, c 6, Sched B, s 21-22 (registration), 32 (complaints), 35 (discipline). For example, in the CA Act, firms are expressly included in the definition of "registrants" and are therefore governed by all provisions regulating registrants; see *Chartered Accountants Act*, *ibid*, Sched C, s 2(d).

59 *Ibid*, s 35(3).

60 The texts of all the rules are more or less identical, with some major exceptions. The most important discrepancy for our purposes is found in the forewords of the documents. Four provinces – Ontario, Alberta, British Columbia and Prince Edward Island – have included a section explaining the extent to which entities must obey the rules of conduct; see "ICAO Rules of Professional Conduct" (2010), online: ICAO, at 501 <http://www.icao.on.ca/Resources/Membershandbook/1011page2635.pdf>. The remaining five provinces have apparently and deliberately left that section out of their rules documents. See "Rules of Professional Conduct" (2009), online: ICAM, at F-6 <http://www.icam.mb.ca/PDF/rules.pdf>

61 *Professional Engineers Act*, RSO 1990, c P 28, s 17. The supervising engineer must have at least five years of professional engineering experience and assumes professional responsibility for the services provided; see Regulation 941, RRO 1990, s 47. Generally, certificate of authorization holders are required to carry professional liability insurance. The registrar must maintain a register of every holder of a certificate of authorization which is available for public inspection and searchable online. See

jurisdictions have mechanisms for maintaining regulatory oversight over firms after licensing or registration. Sometimes this mechanism is an express provision whereby entities are explicitly included in a particular regulatory section. Entities might also be brought under the regulatory authority of the association implicitly by holding a certificate of authorization or permit. That is, a discipline provision might apply to a "holder of a certificate of authorization," meaning an entity that is so authorized.[62] The certificate or permit enables the regulation of entities in these cases. In most provinces both types of regulation are found in the legislation,[63] meaning that the two methods are not necessarily mutually exclusive. Many provincial regulators have disciplinary jurisdiction over entities.[64] Similar systems are in place for the related profession of architecture.[65]

Professional Engineers of Ontario, online: PEO, <http://www.peo.on.ca/CofARegistry/CofACheck.cgi>.

62 See *Engineering Profession Act*, SPEI 1990, c 12, s 6(7).

63 See *Professional Engineers Act*, *supra* note 61, ss 20, 28(2))

64 These include enforcing the association's ethics code (see *Engineering and Geoscience Professions Act*, SNB 1999, c 50, s 17(6)(a)); the jurisdiction of complaints or discipline committees over entities (*The Engineering and Geoscientific Professions Act*, CCSM 1998, c E120, ss 30(3), 33(1)); and punishment for "conduct unbecoming" (*Engineers and Geoscientists Act, 2008*, SNL 2008, c E-12.1, s 20(c)(iii)). Other jurisdictions do not discipline firms. In Nova Scotia, entities are expressly excluded from being licensed or becoming association members, and the ethics provisions apply only members and licensees; see *Engineering Profession Act*, RSNS 1989, c 148, s 11(1), 17(1) and Bylaws, s 24.

65 As with the regulation of engineering, architectural firms are regulated. However, in architecture, discipline focuses on the individual architect and not the firm. The primary means of regulating architectural firms is through the certificate of practice. All architectural firms – whether they are a sole proprietorship or a large firm partnership must hold a certificate of practice. The Ontario Association of Architects attempts to regulate firms by placing responsibilities on individual architects in positions of authority. Each firm must designate one licensed architect to serve as Personally Supervising and Directing (PSD) the practice of the firm overall and one for each office. The *Architects Act* places personal ethical responsibility on the PSD architect for all the actions of the firm; see *Architects Act,* RSO 1990, c A-26, s 22. Information about firms is available and searchable on the Ontario Association of Architects website. Ontario Association of Architects, "Search-OAA Practices", online: OAA <http://www.oaa.on.ca/client/oaa/OAAMembers.nsf/msearch!openform. The Ontario Association of Architects has the regulatory powers to discipline architectural firms but in practice only individual architects are sanctioned. The Complaints and Discipline Committee has jurisdiction over both individuals and all holders of certificates of practice; see *Architects Act*, *ibid*, ss 30(1), 38(1). It is possible for an entity to commit professional misconduct and to be found incompetent, and the Discipline Committee has the authority to sanction the entity for these infractions; see *ibid*, ss 34(2), 34(3), 34(4). Also note that "professional misconduct" is defined in Regulation s 42. However, the latest annual reports from the Ontario Association of Architects reveal that the Discipline Committee has only

Firm regulation in the Canadian securities industry is extensive, active and wide-ranging. The Ontario Securities Commission (OSC) exercises both direct and indirect regulatory powers over entities involved in securities trading. The available administrative penalties are also wide-ranging, and include the ability to levy fines, intervene in personnel choices and business operations, and to revoke registration and with it, the right to practice in the securities trade. The OSC regulates "market participants" which includes not only those entities registered with the OSC as "registrants," but also a host of other entities which are not registered thereunder.[66] The OSC has powers of compliance and discipline against all market participants. It has the power to compel the cooperation of any market participant with an OSC compliance review "for the purpose of determining whether Ontario securities law is being complied with."[67] One of the fundamental principles of the OSC's regulatory mandate is that the creation of "requirements for the maintenance of high standards of fitness and business conduct to ensure honest and responsible conduct by market participants" is one of "the primary means of achieving the purposes of this Act."[68] Thus, one of the core principles of the OSC's regulatory mandate is to develop compliance systems. The OSC is entrusted with the development of standards which are, in turn, to be used to prevent fraud and facilitate ethical behaviour. The OSC has the power to investigate entities which are included in the statutory language through the use of the term "person or company."[69] The most relevant sanctions, from a regulatory perspective, are the administrative penalties which the OSC may apply to entities or individuals under its jurisdiction. There are other sanctions available, namely civil and criminal penalties.[70]

The OSC has delegated some of its regulatory powers to various self-regulatory organizations (SROs) such as the Investment Industry Regulatory Organization of Canada (IIROC) which is the national SRO which oversees all investment dealers and trading activity on debt and

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considered complaints against individual architects; see Ontario Association of Architects, *Annual Report 09* (2009), online: <http://www.oaa.on.ca/client/oaa/OAAHome.nsf/object/Annual+Report+2009/$file/Annual+09+FINAL+F.pdf> at 23. Firms were investigated for the improper use of the term "architect" in their company name, however; see *ibid* at 24.

66 See *Securities Act*, RSO 1990, c S 5, s 1(1).

67 *Ibid*, s 2.0(1).

68 *Ibid*, s 2.1(2).

69 *Ibid*, s 1.1.

70 For a discussion of these penalties, see e.g. Mark R Gillen, *Securities Regulation in Canada*, 3d ed (Toronto: Thomson Canada, 2007) at 567, 575. The *Securities Act* sets out sixteen specific administrative penalties available to the OSC, referred to as "orders."

equity marketplaces in Canada.[71] IIROC has direct regulatory powers over member firms, requiring them to register and firms may be sanctioned for rule breaches. Similarly, individuals must also be registered. IIROC exercises significant regulatory powers over firms both directly and indirectly through extensive compliance obligations imposed on firms and on persons in authority in firms. Legislation requires all firms to establish various internal controls and systems. Every registered firm has to "establish, maintain and apply" policies and procedures "to establish a system of controls and supervision sufficient to (a) provide reasonable assurance that the firm and each individual acting on its behalf complies with securities legislation, and (b) manage the risks associated with its business in accordance with prudent business practices."[72]

Medicine,[73] pharmacy[74] and real estate[75] are also characterized by significant entity regulation. In sum, the regulation of entities in these other

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[71] See IIROC, "About IIROC," online: <http://www.iiroc.ca/English/About /Pages/default.aspx>.

[72] National Instrument 31-103 Registration Requirements and Exemptions and Consequential Amendments to Related Instruments (2009), 32 OSCB (Supp-4), 11.1.

[73] Lawyers and doctors are often grouped together in discussions of professionals. However, the regulation of the practice of law and the regulation of the practice of medicine are very different. While doctors often practice together in groups in their offices or clinics, they are regulated as individuals. This is likely because in an office setting, doctors deal with patients on a one-to-one basis. However, in hospitals patients are treated by teams of physicians and health care workers in a manner that is somewhat analogous to how a group of lawyers work for a client. Yet separate bodies regulate doctors and hospitals. However, the Colleges of Physicians and Surgeons in Alberta, British Columbia and Ontario have been given limited regulatory authority over non-hospital medical facilities. See O Reg 114/94, s. 45(1); "New Premises Inspection Program Launched to Protect Patients" (2010), online: College of Physicians and Surgeons of Ontario http://www.cpso.on.ca/whatsnew/news/default.aspx?id=4046; "Non-Hospital Medical and Surgery Facilities Program," online: CPSBC <https://www.cpsbc.ca/node/74>; "CPSBC Bylaws," online: Part 5, Section A <https://www.cpsbc.ca/files/u6/HPA_Bylaws_-_June_1_2009.pdf>; and College of Physicians and Surgeons of Alberta, "Non-Hospital Surgical Facility: Standards and Guidelines," online: CPSA, <http://www.cpsa.ab.ca/Libraries/Pro_QofC_Non-Hospital /NHSF_Standards.sflb.ashx>.

[74] In pharmacy, unlike in medicine, there is a much stronger link between the regulation of individuals and entities. Most jurisdictions have some form of licensing mechanism used to grant permission for an entity to operate a pharmacy as well as provisions for discipline of pharmacies. In most cases, discipline of pharmacies and pharmacists occur together. See *Health Professions Act*, RSA 2000, c H-7, s 43; see also *The Pharmacy Act, 1996*, SS c P-9.1, s 19. In Ontario, for example, pharmacies must have a certificate of accreditation and holders of such a certificate fall under the jurisdiction of the Discipline Committee. *Drug and Pharmacies Regulation Act*, RSO 1990, c H-4, ss 139(1), 140(1). Discipline cases against pharmacies are not infrequent;

professions both support the case for law firm regulation and also provide various manners in which firms may be regulated which I draw upon in Part 5 of this paper.

The case for regulation of law firms is strong. Richard Devlin and Albert Cheng have written about "defensive self-regulation" in Canada.[76] According to them, regulatory reforms in Canada are attributable to a response to the experiences of former self-regulating legal professions in other jurisdictions. The case for law firm regulation may fit into Devlin and Cheng's paradigm or it may be an opportunity for "proactive self-regulation." Whichever the one, the need for regulating law firms in Canada is pressing. Thus, it is necessary to turn from the why to the how of law firm regulation.

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see <http://www.ocpinfo.com/Client/ocp/OCPHome.nsf/web/Discipline+Decisions and http://www.canlii.org/en/on/oncpdc/>.

75 Real estate entities are subject to a high degree of regulation from registration to discipline. In Ontario, both firms (brokerages) and individuals (brokers/salespersons) must register; see *Real Estate and Business Brokers Act, 2002*, SO 2002, c 30, Schedule C, s 1(1) [*REBBA*]. Most regulatory provisions apply generally to registrants, therefore imposing the same regulatory responsibilities on both firms and individuals. Similar provisions exist under the legislation of other provinces, such as Alberta and British Columbia. See *Real Estate Act*, RSA 2000, c R-5 and *Real Estate Services Act*, SBC 2004, c 42. Each province requires at least one real estate professional to take on a supervisory role with respect to his or her colleagues and brokerage. In Ontario this person is referred to as the "broker of record;" in Alberta the "registered broker" or "broker;" and in British Columbia, the "managing broker." The broker of record plays an important role in ethical oversight. He or she has a number of positive obligations to facilitate ethical compliance among his or her colleagues and the entity with which he or she is employed. Brokers may be responsible for the conduct that is occurring within the entity. In Ontario, "the broker of record shall ensure that the brokerage complies with this Act and the regulations." See also Real Estate Council of Alberta, *Real Estate Act Rules*, s 2(1), online: Real Estate Council of Alberta, <http://www.reca.ca/industry/content/legislationbulletins/PDF/Rules%20Oct%201%2008%20Amended%20Jan%2028%202010.pdf>. In practice, brokers of record as well as their firms may be sanctioned for ethical misconduct committed by others under their supervision. In Ontario, entities are also expected to facilitate ethical compliance. The Act provides that "a brokerage shall ensure that every salesperson and broker that the brokerage employs is carrying out their duties in compliance with this Act and the regulations;" see *REBBA*, *ibid*, Sched C, s 26. A corresponding duty is imposed on individuals to ensure that the brokerage does not do anything to contravene the *Code of Ethics*; see O Reg 580/05, s 2(1). Brokerages may be disciplined by the regulatory bodies and this occurs not infrequently. The sanctions that may be imposed include a maximum fine of $25,000 and requiring the brokerage to fund educational courses for brokers and salespersons employed by the brokerage or to arrange and fund such educational courses; see *REBBA, ibid*, Sched C, s 21(4).

76 Devlin and Cheng, *supra* note 15 at 257.

3. Modest Measures: A Regulatory Audit of Law Firm Regulation in Canada

In this section, I examine the existing forms of regulation of law firms in Canada. Outside of Nova Scotia and Quebec, and as of 2012, British Columbia, there is little explicit regulatory focus on law firms. However, across Canada there is significant regulation of law firms when it comes to Law Society regulation of trust accounts and audits of books and accounts. This is not articulated in terms of firm regulation but may be characterized as individual regulation through the auspices of the firm. Part A of this section discusses different models of firm regulation and Part B examines how law societies in Canada currently regulate firms.

A) Different Models of Firm Regulation

There are number of different ways to consider or classify the regulation of professionals like lawyers. Michael Trebilcock has frequently distinguished between "input measures" and "output measures."[77] Input measures are regulatory mechanisms that focus on entry to the profession. These include educational requirements, licensure, good character requirements, apprenticeship (articling). Output measures focus on actions of the professional in practice: complaints, continuing education requirements, insurance, and discipline.[78]

Another manner of approaching regulation is to consider the difference between a complaint-based system and a compliance-based system. Most law societies in Canada operate predominantly under a complaint-based system. Simply put, they act upon complaints received largely from clients rather than proactively based upon some other criteria. A Canadian lawyer who is not subject to a complaint is unlikely to attract the attention of his or her law society. Until recently, the minimal compliance requirements for most Canadian lawyers consisted of the filing of an annual report.

The recent introduction of mandatory continuing legal education (CLE) by Canadian law societies is a more significant example of a compliance-based regulatory initiative.[79] For example, since January 1,

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77 See Michael Trebilcock, "Regulating Legal Competence" (2001) 34 Can Bus LJ 444.

78 *Ibid* at 444.

79 The Law Society of British Columbia and the Barreau du Québec introduced mandatory CLE in 2009 and the Law Societies of New Brunswick and Saskatchewan in 2010. See generally Devlin and Cheng, *supra* note 15 at 240-41. Manitoba introduced mandatory CLE in 2011; see http://www.lawsociety.mb.ca/education/CPD-requirements

2011, all Ontario lawyers are now subject to an annual twelve-hour Continuing Professional Development (CPD) requirement, which must include a minimum of three hours in ethics, professionalism and/or practice management.[80] CLE functions as a compliance-based regulatory model. The hallmarks of such a model are the imposition of mandatory affirmative duties and reporting obligations on professionals and random checks (or audits) for compliance. Every lawyer in Ontario will be required to complete twelve hours of CLE annually and file a report to that effect. The Law Society of Upper Canada will undertake random audits of a segment of that population.[81]

Another example of compliance-based regulation that is directly relevant to this paper is found in Rule 5.1 of the American Bar Association's *Model Rules of Professional Conduct*. This rule is entitled "Responsibilities of Partners, Managers, and Supervisory Lawyers." It provides:

> A partner in a law firm, and a lawyer who individually or together with other lawyers possesses comparable managerial authority in a law firm, shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the Rules of Professional Conduct.[82]

The Commentary to Rule 5.1(a) states that the rule requires lawyers with managerial authority with the firm to create policies and procedures including those related to conflicts of interest, dates by which actions must be taken in pending matters, accounting for client funds and property and proper supervision of inexperienced lawyers.[83]

As discussed herein, Australia has been at the forefront of developing compliance-based regulatory initiatives. These have been developed in response to perceived inadequacies of the complaint-based system. Australian commentators John Briton and Scott McLean have argued that there are four main limitations to traditional complaints-based regulation when relied on in an era of increasing size and complexity of law firms.

/2012-requirements. Nova Scotia is introducing mandatory CLE July 1, 2012.; see http://www.nsbs.org/for_lawyers/professional_development. Lawyers in Alberta must make a CPD plan; see http://www.lawsociety.ab.ca/lawyers/cpd.aspx.

80 Law Society of Upper Canada, "Continuing Professional Development Requirement," online: http://www.lsuc.on.ca/latest-news/a/continuing-professional-development-requirement/

81 *Ibid.*

82 American Bar Association, *Model Rules of Professional Conduct*, Rule 5.1(a) [ABA *Model Rules*].

83 *Ibid,* Rule 5.1(a), cmt.

First, complaint-based systems focus exclusively on the conduct of individual lawyers. Such systems ignore the reality of law firm organizational cultures that tend to develop contextual ethical standards and practices.[84] Second, complaint-driven processes are highly selective in their application. The refrain that law societies target certain practice areas and practice settings is one as familiar in Canada as it is apparently in Australia.[85] Third, Briton and McLean argue that complaint-driven processes focus exclusively on minimum standards of behaviour. The point of concern – and intervention – occurs when a lawyer's conduct falls below a minimum threshold. Thus, lawyers internalize the idea that they only need to act in a manner that is just above the line of acceptability. Such a system is counterproductive to the goals of cultivating high, and continually improving, professional ethical standards. Fourth, complaints-driven processes are entirely reactive. Intervention occurs after a consumer, or the legal system itself, has suffered a wrong. While an ethical violation must be punished, any legal ethics system should strive to achieve pro-active measures that prevent or reduce the occurrence of such behaviour. If a goal of the legal profession is to ensure consumer confidence, professional regulation should incorporate prevention measures in addition to those focused on deterrence.[86] How a law society oversees compliance initiatives is a question for additional investigation.

Another way to conceive of the regulation of firms is to contrast direct and indirect forms of regulation. Direct regulation involves methods of regulation that regulate the firm itself such as strict trust accounting rules and conflicts rules where lawyers switch firms.[87] Indirect forms of regulation attempt to regulate the conduct of firms through regulating individuals who hold positions of responsibility within a firm. Examples include the ABA's Model Rule 5.1 for partners and supervising lawyers, Australia's legal practitioner director, the Ontario Association of Architects' personally supervising and directing (PSD) architect, and the supervising broker for real estate in Ontario.[88] In terms of direct regulation, there are numerous ways to directly regulate the activities of a firm.

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84 John Briton and Scott McLean, "Incorporated Legal Practices: Dragging the Regulation of the Legal Profession into the Modern Era" (2008) 11 Legal Ethics 242.

85 *Ibid.*

86 *Ibid*.

87 Thanks to Alan Treleaven for providing these examples to me.

88 See discussion of PSD architect requirement, *supra* note 65. See also discussion of the role of the "broker of record" in real estate in Ontario under *REBBA*, *supra* note 75, Sched. C, s 12(2).

1) Registration

Registration is essentially an information-gathering exercise. For example, the Law Society of Upper Canada requires that all professional corporations register with it.[89] The information contained in registration materials may be minimal (as in the case of professional corporations) or it can be more extensive (as in the case of certificates of authorization for engineers in Ontario[90]). Registration may be coupled with public disclosure which has the benefit of providing information to members of the public.

2) Licencing

In licensing a firm, there must be some requirements and a vetting process by the regulator. The requirements may be minimal or they may be more onerous. There is usually some method for imposing restrictions or conditions on a licence and for its revocation.

3) Information

Firms may be required to provide information to the regulator. For example, in Nova Scotia LLPs must file an annual report with the Barristers' Society.[91] The provision of information may have multiple purposes. It may assist the Society to compile information about the practice of law. It may be used for compliance purposes in that the disclosure of certain information could trigger an audit or an investigation. Finally, the process of providing information may lead a firm to make changes to its systems or policies as the self-auditing experience in New South Wales discussed below demonstrates.

4) Compliance

Various compliance tools may be used to regulate firms. Canadian law societies conduct practice reviews or audits of firms. Firms may be required to undergo a self-audit as in the case of Incorporated Legal Practices (ILPs) in New South Wales. Firms may be obliged to establish

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89 See Law Society of Upper Canada, Bylaw 7 Business Entities, Part II Professional Corporations, paras 3-14, online: http://www.lsuc.on.ca/media/bylaw7.pdf.

90 See *Professional Engineers Act*, *supra* note 61, ss 12(2), 15, 17; Regulation 941, RRO 1990, s 47; and http://www.peo.on.ca/offering/CofA.html.

91 See Nova Scotia Barristers' Society, Regulations made pursuant to the *Legal Profession Act*, SNS 2004, c 28, Reg 7.4.

particular compliance systems as required for certain firms under the *Legal Services Act* in the UK[92]

5) Discipline

A final form of regulation is the imposition of sanctions against a firm. The most frequent forms of firm sanctions are reprimands and fines. Other sanctions include suspension of license, revocation, the imposition of conditions and requiring a firm to establish certain systems or policies. Often discipline is combined with a licensing scheme in order to be able to place conditions on a license or suspend a license.

With this framework in mind, I now turn to the current means of regulating law firms in Canada.

B) The Current Regulatory Structure in Canada

Canadian law societies regulate the legal profession primarily through two mechanisms: licensure and discipline. Over the past decade, law societies have introduced practice reviews which are remedial and focus on competency rather than conduct issues.[93] Importantly, the dominant feature of regulation of lawyers in Canada has been its operation as a complaints-based system, that is, one that is reactive to complaints received about the conduct or competency of a lawyer. This may be changing with the introduction of mandatory CLE which operates on a compliance model.

As a general matter, law societies regulate individual lawyers.[94] They impose regulatory obligations on them, investigate complaints against individuals and sanction them. In certain circumstances, law societies are empowered to regulate groups of lawyers who work together. A significant exception to the general rule of individual-focused regulation is law society financial regulation. For example, in the case of financial audits, Ontario's *Law Society Act* empowers the Society to conduct an audit of the financial records "of a licensee or group of licensees" and the Society is empowered to enter the business premises of the licensee or group of licensees and require the production of their records and provide

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92 See Solicitors' Regulation Authority, "Outcome-focused regulation at a glance" updated October 10, 2011, online: http://www.sra.org.uk/solicitors/freedom-in-practice/OFR/ofr-quick-guide.page.

93 For a discussion of practice reviews in Ontario see Gavin MacKenzie, "Regulating Lawyer Competence and Quality of Service" (2008) 45 Alta L Rev 143.

94 In the case of Ontario, the Law Society of Upper Canada regulates individual lawyers and paralegals.

information.[95] In practice, the Law Society of Upper Canada conducts spot audits of firms not of individual lawyers or paralegals within the firm. Law firms have client identification requirements[96]

Most law societies now extensively regulate professional corporations but do little in the way of regulating the preferred business entity for larger law firms, the limited liability partnership. For example, the Law Society of Upper Canada has detailed regulations regarding professional corporations[97] but very little on LLPs,[98] despite having the regulatory authority to do so.[99] In practice, the Law Society of Upper Canada regulates professional corporations but not LLPs (other than requiring them to hold professional liability insurance[100]). In contrast, professional corporations are required to apply for and maintain a certificate of authorization and may have that certificate revoked.[101] Most provisions of the Act and of other by-laws that refer to individual licensees also apply, with necessary modifications, to a professional corporation.[102] Most law societies in Canada operate under a similar manner of entity regulation as the Law Society of Upper Canada: they may regulate professional corporations but regulation of LLPs is minimal. There are a number of exceptions to this general rule, most notably Quebec, Alberta, Nova Scotia and, as of May 2012, British Columbia.[103]

The Barreau du Québec regulates law firms through compliance measures but not discipline. Every firm must provide the Barreau with a detailed undertaking under which it promises to facilitate the ethical

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95 *Law Society Act*, *supra* note 2, s 49.2.

96 See Law Society of Alberta, *Law Society Rules*, rule 118.1 et seq.

97 *Law Society Act*, *supra* note 2, ss 61.0.1-61.0.9.

98 *Ibid,* s 61.1.

99 Importantly for the consideration of regulatory changes with respect to business entities such as LLPs, the *Law Society Act* empowers the Society to make by-laws governing the practice of law and the provision of legal services by LLPs, including "requiring that those partnerships hold a permit to practice law or provide legal services, governing the issuance, renewal, suspension and revocation of such permits and governing the terms and conditions that may be imposed on such permits; see *ibid,* s 62 (0.1) (28). An analogous provision exists for professional corporations; see *ibid,* s 62(0.1)(29).

100 Law Society of Upper Canada, By-Law 7, para 1.

101 Law Society of Upper Canada, *ibid*, paras 4-6.

102 *Law Society Act*, *supra* note 2, ss 61.0.4 – 61.0.9; Bylaw 7, para 13.

103 In May 2012, the Legislature of BC enacted the *Legal Profession Amendment Act, 2012*, which, *inter alia*, provides for the legislation of law firms. Much of the regulation will come by way of regulations yet to be enacted.

behaviour of the advocates working in the firm.[104] In particular, the firm must sign a form which lists all of the members of the firm and stipulates the following:

> (a) It [the entity] shall ensure that the members who engage in their professional activities within the Firm have a working environment allowing them to comply with any law applicable to the carrying on of their professional activities.[105]
>
> (b) It shall ensure that the partnership or company as well as all persons comprising same or working therein comply, to the fullest extent applicable, with the *Professional Code* and *An Act respecting the Barreau du Québec* (RSQ, c B-1) as well as with the regulations adopted thereunder.[106]

The firm also undertakes to provide each member of the firm with a working environment allowing the advocate to comply with the rules of law applicable to the carrying on of one's professional activities, particularly as regards the following:

> professional secrecy, the confidentiality of information contained in client files and the preservation thereof ; professional independence; the prevention of situations of conflict of interests; activities reserved for advocates; liability insurance; professional inspections; advertising; billing and trust accounts; and access by the syndic of the Barreau to this undertaking and, if applicable, to every contract or agreement regarding a member;[107]

The firm must also designate a member of the firm to act as a representative with the Barreau.[108] This regulation establishes the strongest compliance requirements for law firms in Canada. The Barreau also has the power to discipline law firms, but in practice it does not.

Nova Scotia has the most extensive regulatory powers regarding law firms. These powers cover the spectrum from licensing to discipline and include some less intrusive compliance powers. Many of these powers, including the power to discipline law firms, were adopted during the wholesale overhaul of the Nova Scotia Barristers' Society's legislation

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104 *Regulation respecting the practice of the profession of advocate within a limited liability partnership or joint-stock company and in multidisciplinarity*, RRQ, c C-26, r 19.1.2, Schedule B, s 3.

105 *Ibid,* s 3(a)

106 *Ibid*, s 3(d).

107 *Ibid,* Sch B.

108 *Ibid*, ss 2-3.

when Nova Scotia enacted a new *Legal Profession Act* in 2005.[109] The inclusion of the power to discipline law firms was not and has not been controversial in Nova Scotia. However, the Barristers' Society considered expanding the discipline provisions and adopting compliance requirements but abandoned these proposals in the face of opposition. In a discussion paper on the regulation of law firms, the Society considered and rejected the following: (1) obligating a firm to appoint an in-house specialist to act as ethics adviser and encourage compliance (a "compliance specialist"); (2) regulating development of specific benchmarks and accountability measures including but not limited to conflict of interest checking systems; handling client property; billing practices; and file opening, monitoring and closing; (3) mandatory continuing legal education; and (4) mandatory and regular law firm practice reviews.[110]

Nova Scotia has notable information requirements for firms. Firms must file an annual "law firm report" which includes the names of all members of the Barristers' Society associated with the firm, and the nature of their association; the location and particulars of all trust accounts and firm bank accounts maintained by the firm; the names and responsibilities of employees of the firm, or others, who maintain the accounting record of the firm; and such other information as may be required by the Council of the Barristers' Society. Firms must also file an annual trust report.[111] Alberta has a similar requirement.

Nova Scotia and Alberta require registration of LLPs.[112] Firms must apply to the Barristers' Society to register as a Nova Scotia LLP. The requirements are not onerous: the executive director of the Barristers' Society must verify that (i) the partnership and its partners meet all of the applicable eligibility requirements for practice as an LLP imposed under the *Legal Profession Act*; (ii) the partners of the partnership have liability insurance in the form and amount required; and (iii) all of the Nova Scotia partners of the applicant partnership are entitled to carry on the practice of law in Nova Scotia.[113] Alberta LLPs must apply each year to renew their registration and provide information akin to the annual report requirements in Nova Scotia.[114]

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109 *Legal Profession Act*, *supra* note 91.

110 Nova Scotia Barristers' Society, *Discussion Paper on the Regulation of Law Firms* (2006) [unpublished] [on file with author and cited with permission].

111 Regulations made pursuant to the *Legal Profession Act*, *supra* note 91, Reg 7.2.1.

112 *Law Society of Alberta Rules*, rr 159.1-159.2.

113 Regulations made pursuant to the *Legal Profession Act*, *supra* note 91, Reg 7.4.

114 *Law Society of Alberta Rules*, r 159.7.

Beyond these forms of regulation, Nova Scotia and Alberta have a number of provisions that recognize the firm as a relevant party in regulation of lawyers. In Alberta, duties respecting client identification and verification are considered duties of law firms,[115] recognizing the reality that client intake will often be the responsibility of a designated lawyer or firm employee. Further, every law firm in Alberta must designate a "Responsible Lawyer" who is accountable for the operation of all law firm trust accounts and general accounts.[116] In Nova Scotia, every law firm must designate an official representative in communications with the Barristers' Society. Second, a law firm is entitled to receive a copy of each complaint against a lawyer associated with the firm and of each determination or decision.[117] The unstated but apparent purpose of this provision is both to put the law firm on notice regarding a complaint about one of its lawyers and to ensure that a lawyer is unable to hide a complaint from the firm. Even if the lawyer changes firms, the old firm is still entitled to receive information if the subject matter of the complaint took place while the lawyer was practicing at the old firm.[118]

Finally, Nova Scotia is the only jurisdiction in Canada with the clear statutory authority to discipline law firms. This change was introduced in 2005 when the legislature enacted a new *Legal Profession Act.* There does not appear to have been any precipitating event that triggered this regulatory change, which proceeded without controversy. The Act now contains an interpretive clause which stipulates that all references to "members of the Society" includes law firms unless otherwise indicated.[119] Consequently, the Barristers' Society now has the mandate to regulate and discipline law firms for violations of the code of conduct. Two sanctions are available against law firms. First, a firm found guilty of professional misconduct may be ordered to pay a penalty of up to $50,000. Second, a disciplinary panel may order "any other action the panel thinks is appropriate in the circumstances including an order to retain jurisdiction to monitor the enforcement of its order."[120]

The specific procedural framework for complaints against law firms is set out in new regulations. When a complaint is filed against a law firm for professional misconduct, that firm is required to designate one of its practicing lawyers to receive official communications from the Society

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115 *Ibid*, r 118.1-118.10.

116 *Ibid*, r 119.3.

117 Regulations made pursuant to the *Legal Profession Act*, *supra* note 91, Reg 7.2.2.

118 *Ibid*, Reg 7.2.3.

119 *Legal Profession Act*, *supra* note 91, s 27.

120 *Ibid* at s 45(5).

and to assist in the investigation of the complaint.[121] To date, while there apparently have been some complaints against law firms in Nova Scotia, none have resulted in any formal disciplinary action that has been published.

Although the Nova Scotia Barristers' Society appears to be the only law society with an expressed intent to regulate law firms as entities, statutes delegating regulatory authority to the Law Society of Alberta and the Law Society of Newfoundland and Labrador contain language that would appear to provide for law firm regulation. Alberta's *Legal Profession Act* explicitly grants the Society's benchers the ability to "make rules respecting the rights and duties of law firms."[122] In practice, neither Law Society appears to exercise the available statutory powers to discipline law firms at this time.

Thus, the regulatory landscape in Canada is one of limited regulation of law firms, outside the notable area of financial regulation. We now examine how three comparable jurisdictions regulate law firms.

4. The Regulation of Law Firms in Other Jurisdictions

This section analyzes the regulation of law firms in three countries. In discussions about regulation of the legal profession in Canada and the independence of the bar, these three jurisdictions are the most frequently invoked, often as a cautionary tale or warning about the threats to self-regulation. Thus, this section examines law firm discipline in the United States, the emergence of a new compliance-based model for law firm regulation in Australia and elements of compliance and discipline in the United Kingdom. The point of this section is to demonstrate that firm regulation is very much on the radar in other jurisdictions. In the United States, it was mooted two decades ago and has never really caught on. In contrast, in Australia and the United Kingdom firm regulation is very much on the rise.

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121 Regulations made pursuant to the *Legal Profession Act*, *supra* note 91, s 7.2.1

122 *Legal Profession Act*, SA 1990, c L-9.1, s 7(2)(r). Prior to November 1, 2011, Alberta's *Code of Conduct* contained a "Principle of Co-Responsibility" in the interpretation section which stipulated that: "[t]he term 'lawyer' is defined in this Code to include the lawyer's firm and each firm member except where expressly stated otherwise or excluded by the context." (s 3(d)). This Code was replaced on November 1, 2011 by a version of the Federation of Law Societies *Model Code of Conduct* which lacks any like provision. A similar provision to that contained in the old Alberta Code exists under legislation in Newfoundland and Labrador; see *Law Society Act*, SN 1999, c L-9 s 41(f).

A) Never Really Achieving Liftoff: Firm Regulation in the United States

In the 1990s, there was much debate in American regulatory and academic circles over the issue of disciplining law firms. This was triggered by notable high-profile scandals involving large law firms. The ABA considered amending its *Model Rules* to allow for law firm discipline but a proposal was narrowly defeated. To date, only New York and New Jersey engage in law firm discipline. The experience of both jurisdictions reveals that such powers have been exercised sparingly. As a result, interest in law firm discipline has waned in the US and does not appear to be on the regulatory agenda. There is greater interest in adopting some of the compliance regulation that has been established in Australia and that has now been enacted under the *Legal Services Act* in England and Wales. Two states that have formal powers to discipline firms are New York and New Jersey.

In New York, the Appellate Division of the Supreme Court metes out discipline for violation of the New York State *Rules of Professional Conduct*.[123] Provisions extending liability to law firms has been a part of the state's governing ethical code since 1996.[124] The language of the provisions concerning firm regulation is quite expansive. Rules under section 5 concern responsibilities of law firms, partners, managers and supervisory lawyers. They include:

> 5.1(a) A law firm shall make reasonable efforts to ensure that all lawyers in the firm conform to these Rules.
> 5.1(c) A law firm shall ensure that the work of partners and associates is adequately supervised, as appropriate. A lawyer with direct supervisory authority over another lawyer shall adequately supervise the work of the other lawyer, as appropriate. In either case, the degree of supervision required is that which is reasonable under the circumstances, taking into account factors such as the experience of the person whose work is being supervised, the amount of work involved in a particular matter, and the likelihood that ethical problems might arise in the course of working on the matter.[125]

Rule 5.1(a) may be viewed as creating a duty of facilitating compliance with the Rules and Rule 5.1(c) as establishing a duty of supervision. The general rule prohibiting misconduct applies to both individuals and law

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[123] New York followed a version of the ABA's *Model Code of Professional Conduct* until 2009 when it adopted *Rules of Professional Conduct* based on the ABA's *Model Rules*.

[124] O'Sullivan, *supra* note 51 at 2.

[125] New York Unified Court System, *Rules of Professional Conduct*, online: <http://www.courts.state.ny.us/rules/jointappellate/index.shtml>.

firms. The language of the Rule is quite broad and includes discriminatory conduct and conduct unbecoming.[126]

Ultimately, a firm can be sanctioned if it fails to meet these responsibilities. Although a firm will not be held strictly liable in every case of lawyer misconduct, commentators have pointed out that the wording could lead to a violation of the provision even in cases where there has been no lawyer misconduct, simply due to a firm failing to meet an affirmative duty.[127] However, a review of disciplinary cases against law firms in New York reveals a conservative approach to firm regulation and discipline. There are no instances where a firm has been sanctioned for failing to meet the compliance and supervision provisions outlined above.[128]

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[126] *Ibid*, Rule 8.4. provides:

A lawyer *or law firm* shall not:

(a) violate or attempt to violate the Rules of Professional Conduct, knowingly assist or induce another to do so, or do so through the acts of another;

(b) engage in illegal conduct that adversely reflects on the lawyer's honesty, trustworthiness or fitness as a lawyer;

(c) engage in conduct involving dishonesty, fraud, deceit or misrepresentation;

(d) engage in conduct that is prejudicial to the administration of justice;

(e) state or imply an ability:

(1) to influence improperly or upon irrelevant grounds any tribunal, legislative body or public official; or

(2) to achieve results using means that violate these Rules or other law;

(f) knowingly assist a judge or judicial officer in conduct that is a violation of applicable rules of judicial conduct or other law;

(g) unlawfully discriminate in the practice of law, including in hiring, promoting or otherwise determining conditions of employment on the basis of age, race, creed, color, national origin, sex, disability, marital status or sexual orientation. Where there is a tribunal with jurisdiction to hear a complaint, if timely brought, other than a Departmental Disciplinary Committee, a complaint based on unlawful discrimination shall be brought before such tribunal in the first instance. A certified copy of a determination by such a tribunal, which has become final and enforceable and as to which the right to judicial or appellate review has been exhausted, finding that the lawyer has engaged in an unlawful discriminatory practice shall constitute prima facie evidence of professional misconduct in a disciplinary proceeding; or

(h) engage in any other conduct that adversely reflects on the lawyer's fitness as a lawyer [emphasis added].

[127] See Rachel Reiland, "The Duty to Supervise and Vicarious Liability: Why Law Firms, Supervising Attorneys and Associates Might Want to Take A Closer Look at Model Rules 5.1, 5.2 and 5.3" (2001) 14 Geo J Legal Ethics 1161. See also New York State Bar Association, *New York Rules of Professional Conduct with Comments*, online: <http://www.nysba.org/Content/NavigationMenu/ForAttorneys/ProfessionalStandardsforAttorneys/RulesofProfessionalConduct.pdf>.

[128] This statement is accurate as of July 1, 2011. Law firms have been sanctioned and disciplined under provisions with language applying to lawyers rather than entities. In *re Wilens and Baker,* NYS 2d 116 (NY App Div 2004), a disciplinary investigation was

A possible reason for the dearth of case law concerning the regulation and discipline of law firms under the Rule 5 provisions could be due to the disciplinary committee opting to investigate and settle complaints privately. According to a 2001 report, the disciplinary committee had issued only two private admonitions against two small private law firms for professional misconduct.[129] However, the report also notes that in a 2001 interview a disciplinary prosecutor with the committee declared that scrutiny of violations by law firms was increasing and firm misconduct has become a more significant part of the committee's focus.[130] A decade later, it is not clear that much has changed. Ultimately, law firm discipline is rare in New York. The story in New Jersey is similar.

New Jersey became the first state to incorporate law firm regulation into its *Rules of Professional Conduct*.[131] Similar to New York's Rules, New Jersey's firm responsibility provisions are located within the general supervisory duties pertaining to partners and supervisors. New Jersey's Rule 5.1 is similar to New York's in imposing a duty to facilitate compliance with the Rules but goes a little further in requiring the firm to make reasonable efforts to ensure that their lawyers "undertake measures giving reasonable assurance that all lawyers conform to the *Rules of*

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undertaken after complaints by clients of a firm which dealt with immigration issues. The Court found that when clients or family members indicated that they could not pay all of the requested fee or persisted in inquiring about their case, they were treated in a rude and demeaning manner and ordered to leave the firm's office. In addition, the firm neglected several of the client matters entrusted to them. Finally, the firm's practice was not to release copies of a client's file after the firm had been discharged unless the former client agreed in writing that no funds previously paid to the firm should be reimbursed to the client. The respondent firm was found guilty for nineteen violations of the Code – seventeen of which were provisions with language referring strictly to lawyers. The firm was also sanctioned for two violations of the misconduct rule which expressly includes law firms, stating that "A lawyer or law firm shall not engage in any other conduct that adversely reflects on the lawyer's fitness as a lawyer." New York Unified Court System, *New York Lawyer's Code of Professional Responsibility*, online: <http://www.nysba.org/Content/NavigationMenu/ForAttorneys/ProfessionalStandardsforAttorneys/LawyersCodeDec2807.pdf>. The Court imposed a public censure on the firm. This case demonstrates the use of law firm discipline either for cumulative ethics infractions or for activity that could be considered collective firm behaviour rather than just an amalgam of individual misconduct.]

129 Sarah McShea, "Revisiting Law Firm Discipline: Does it Really Work?" *New York Professional Responsibility Report* (February 2001), online: <http://lazar-emanuel.com/Revisiting%20Law%20Firm%20Discipline%20%E2%80%93%20Does%20It%20Really%20Work.pdf>.

130 *Ibid*.

131 New Jersey Supreme Court Office of Attorney Ethics, *Rules of Professional Conduct*, online: <http://www.judiciary.state.nj.us/rules/apprpc.htm#x5dot1>. New Jersey operates a similar system of court-annexed discipline as New York.

Professional Conduct."[132] Rule 5.1 is also notable in that it imparts responsibility to the firm as an entity but not to the individual partners themselves. The commentary to this rule states that responsibility is not imputed to a law partner unless the attorney has *direct* supervisory authority over the transgressor.[133] Rule 5.3(a) creates a duty for law firms "to adopt and maintain reasonable efforts" to ensure that the conduct of all lawyers working within their firm or organization is compatible with the professional obligations of the lawyer.[134] This Rule is considered significant because it essentially requires law firms to establish ethical infrastructures.

New Jersey regulators have been perceived to be more aggressive than their New York counterparts in enforcing firm liability provisions. However, given the longer time period that firm regulation has been operating in New Jersey, it appears that ethics committee officials have been similarly reluctant to publicly pursue law firms for ethics violations. There are only six reported cases of disciplinary action taken against law firms.[135]

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[132] Rule 5.1 is entitled "Responsibilities of Partners, Supervisory Lawyers, and Law Firms" and provides:

> (a) Every law firm, government entity, and organization authorized by the Court Rules to practice law in this jurisdiction shall make reasonable efforts to ensure that member lawyers or lawyers otherwise participating in the organization's work undertake measures giving reasonable assurance that all lawyers conform to the Rules of Professional Conduct.
>
> (b) A lawyer having direct supervisory authority over another lawyer shall make reasonable efforts to ensure that the other lawyer conforms to the Rules of Professional Conduct.
>
> (c) A lawyer shall be responsible for another lawyer's violation of the Rules of Professional Conduct if:
>
> (1) the lawyer orders or ratifies the conduct involved; or
>
> (2) the lawyer having direct supervisory authority over the other lawyer knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.

[133] See Reiland, *supra* note 127 at 1161.

[134] New Jersey Supreme Court Office of Attorney Ethics, *Rules of Professional Conduct*, online: <http://www.judiciary.state.nj.us/rules/apprpc.htm#x5dot1>.

[135] In five of the six cases, the firm was sanctioned for violating provisions found elsewhere in the Code that contain language referring to lawyers. For example, a firm was publicly reprimanded and fined $10,000 for violating a lawyer's duty regarding the safekeeping of property; see *In re Jacoby & Meyers,* 687 A 2d 1007 (NJ 1997). In another case, the firm had parked a vehicle covered with advertisements outside of a building that had been recently burned down by a gas pipe explosion; see *In re Ravich, Koster, Tobin, Oleckna, Reitman & Greenstein,* 715 A 2d 216 (NJ 1998). The culpable attorneys and the law firm were publicly reprimanded for violating the Code by soliciting disaster victims. Finally, in the last case, the firm was found to have mishandled two client matters due to gross neglect, lack of diligence and failure to communicate with the clients; see *In re*

In only one of these was the law firm disciplined under the compliance and supervision provisions.[136]

The experience in New York and New Jersey has impacted the national debate in the US on law firm discipline. In 1997, the ABA established the Ethics 2000 Commission with a mandate to review the *Model Rules* and made recommendations for its modernization.[137] In response to events in the 1980s and 1990s, the Commission proposed to amend Model Rules 5.1 and 5.3 to extend duties to law firms as entities, as per New York and New Jersey.[138] During deliberations, the main argument in favour of the proposed amendment was that it would be an effective tool in cases where one of the *Model Rules* was violated from within a firm, but where no particular lawyer could be identified as personally responsible or, alternatively, that all partners were co-equally responsible for the problem.[139]

Rovner, Allen, Seiken and Rovner, 754 A 2d 554 (NJ 2000). The law firm also failed to supervise junior attorneys assigned to these matters. It was publicly reprimanded for violating negligence provisions and Rule 5.1(b), which requires a lawyer with direct supervisory authority to ensure that the supervised lawyer conforms to the *Rules of Professional Conduct*. These violations committed by the firm were in addition to lack of diligence and failure to communicate. An analysis of the full Disciplinary Review Board decision in this case suggests that when an entire firm is heavily implicated in a Code violation, or all of the firm's partners are found to be culpable, the courts have been willing to extend the bounds of firm liability; see *In the Matter of Rovner, Allen, Seiken and Rovner*, Supreme Court of New Jersey Disciplinary Review Board (1999), online: <http://lawlibrary.rutgers.edu/drb/decisions/99-068.pdf>.

136 See *Re Sills, Cummis, Zuckerman, Radin, Tischman, Epstein & Gross*, 927 A 2d 1249 (NJ 2007). The firm was investigated for a lack of supervision which led to a lawyer employed by the firm engaging in the practice of law before he had been admitted to the state bar; see New Jersey State Judiciary, *2008 Disciplinary Summaries*, online: <http://www.judiciary.state.nj.us/oae/DisciplinarySummaries1984-2008.pdf>. In the decision, the Office of Attorney Discipline and the respondent firm signed a statement of consent wherein it was agreed that the firm violated Rule 5.1(a) in failing to take reasonable efforts that give reasonable assurance that all lawyers conform to the *Rules of Professional Conduct*. The sanction against the firm included a public reprimand and an order to reimburse the Disciplinary Oversight Committee for the appropriate administrative costs and expenses incurred in the prosecution of the matter.

137 American Bar Association Center for Professional Responsibility, *Ethics 2000 Commission*, online: <http://www.abanet.org/cpr/e2k/home.html>.

138 There was also material presented that mentioned the possibility of extending the misconduct rule under 8.4, which appears to not have come to a vote; see American Bar Association Center for Professional Responsibility, *Ethics 2000 Commission*, Meeting Minutes Friday, March 24, and Saturday, March 25, 2000 Chicago, Illinois, online: <http://www.abanet.org/cpr/e2k/032400mtg.html>.

139 American Bar Association Center for Professional Responsibility, *Ethics 2000 Commission*, testimony of Attorneys' Liability Assurance Society Inc, A Risk Retention

The Commission narrowly rejected the proposed amendment. It was persuaded by two chief arguments. First, "[a]ny possible benefit from being able to extend disciplinary liability firm-wide was small when compared to the potential cost of de-emphasizing the personal accountability of partners and supervisors."[140] Second, the Commission acknowledged that discipline of law firms might provide additional incentive to them and increased visibility of the disciplinary system to the public, it was not convinced that law firm discipline was necessary since all partners and those with managerial authority were already responsible for making sure the firm has in effect reasonable measures to assure compliance with the Rules.[141] I addressed these criticisms in Part 2 above.

The defeat of the proposal for law firm discipline in 2001 effectively ended the debate over law firm discipline in the US. The ABA has now established an Ethics 2020 Commission with a similar mandate as Ethics 2000. Law firm discipline is not on the agenda. In discussions at ABA meetings, there is greater interest in regulation of firms through compliance, along the lines of the Australian model.[142]

Group (15 February 2001), online: <http://www.abanet.org/cpr/e2k/e2k-witness_lundy.html>.

However, testimony from Robert Creamer of the Attorneys' Liability Assurance Society Inc offered strong arguments against extending liability to firms. First, he argued that it was unnecessary because in both small and large firms it is always more practical and effective to discipline firm partners for a firm's ethical violations. Second, Creamer argued that firm discipline was unnecessary because at that time the two jurisdictions that had adopted similar provisions – New York and New Jersey – had disciplined only three firms for violations. Third, he argued that the amendment was unwise because, in his experience dealing with lawyer misconduct, it was always the case that individual lawyers, rather than the firm, were the fundamental source of the problem. Finally, he argued that the amendment was unfair, as it would be imposing "collective guilt" in a contemporary system of legal ethics with a paradigm centred on individual accountability.

[140] See Margaret Colgate Love, "The Revised ABA Model Rules of Professional Conduct: Summary of the Work of Ethics 2000" (2002) 15 Geo J Legal Ethics 470 at 471.

[141] ABA Center for Professional Responsibility, Comm'n on Evaluation of the Rules of Prof'l Conduct, Minutes 3 (March 16-17, 2001), online: <http://www.abanet.org/cpr/e2k/e2k-03-16mtg.html>.

[142] Even Ted Schneyer whose 1991 article, "Professional Discipline for Law Firms," (1991) 77 Cornell L Rev 1, served as a catalyst for debate on firm regulation, has turned his attention to compliance initiatives in Australia and the UK; see Ted Schneyer, "Thoughts on the Compatibility of Recent UK and Australian Reforms with US Traditions in Regulating Law Practice" 2009 J Professional Lawyer 13 [Schneyer, "Thoughts"].

B) Australia: New Directions in Compliance-Based Regulation

Regulatory reforms in Australia were motivated in part because of perceived inadequacies with the law societies' handling of scandals involving large firms.[143] Australian reforms have targeted law firms chiefly through the creation of compliance obligations rather than law firm discipline. In this section, I provide a brief overview of the structure of regulation of the legal profession in Australia and then proceed to analyze the regulatory tools created to regulate law firms and the issues that have arisen in the process.

1) Regulation and Reform

Australia is a federal state and like Canada the constitutional authority to govern legal services lies within the jurisdiction of state governments. However, state legislation and ethical rules have been adopted, in varying degrees, based upon national "Model Laws" and "Model Rules" which have been developed in collaboration between the Standing Committee of Attorneys-General and the Law Council of Australia.[144] Recent reforms have led to greater variation in regulation of lawyers across Australia which can be placed along a spectrum from self-regulation at one end to independent regulation at the other end and co-regulation in between.

The three most populous states in terms of legal service providers – New South Wales (NSW), Queensland, and Victoria – all utilize a system of co-regulation. Queensland has a single Legal Service Commissioner appointed by the government who has authority to refer investigations to the Law Society or the Bar Association.[145] In Victoria, reforms in 2006

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[143] I am indebted to Christine Parker both for her scholarship on this issue and her collegiality in taking the time to explain the context of law firm regulation in Australia to me.

[144] Christine Parker and Adrian Evans, *Inside Lawyers Ethics* (Port Melbourne, Australia: Cambridge University Press, 2007) at 46.

[145] *Legal Profession Act 2007* (Qld) at s 584(1-2). However, circumstances preceding the reforms that created the office in Queensland had the practical consequence of the leaving power of investigation and discipline much more centralized in the hands of the individual Commissioner. In 2004, Queensland witnessed a high-profile scandal involving a large Brisbane firm. The Baker and Johnson firm faced wide-ranging accusations of unprofessional, unethical, and fraudulent conduct, including one case where the firm won a case for a client and subsequently diverted the entire compensation payout while attempting to sue the client for extra fees; see *Baker Johnson v Jorgensen* [2002] QDC 205 discussed in Parker and Evans, *ibid* at 56. Despite wide public outcry, the Queensland Law Society failed to investigate the law firm and was later sharply criticized by the Attorney General for maintaining inadequate complaints handling procedures; see Parker and Evans, *ibid* at 56. One of the results of this situation was the creation of the Legal Service Commissioner who, in practice, is far less likely to refer

replaced a complicated system of co-regulation with a seven-member Legal Services Board headed by a Legal Services Commissioner.[146] Tasmania, the Northern Territory and the Australia Capitol Territory (ACT) follow a system of self-regulation, along lines that we are familiar with in Canada. Finally, South Australia and Western Australia utilize a system of independent regulation where government-appointed bodies oversee regulatory duties and complaints investigations.[147]

2) The Emergence of Compliance-Based Regulation Regimes

In the 1990s, the legal profession in Australia pushed for deregulation and the implementation of more competitive business models through which to offer legal services. There was a corresponding worry among regulators that traditional regulatory regimes would prove inadequate for ensuring that high ethical standards would be adhered to by lawyers, especially in law firms. A number of high-profile cases involving lawyers at firms helped spur the move to a compliance-based model.[148] In comments that parallel the Canadian context, one leading Australian commentator noted that the commercial mentality existing at one of the firms caught in an ethical scandal created the type of situation where regulators were unable to address the root of the problem.[149]

With an eye to preventing these types of situations from occurring, legislators in all states committed to adopting a *Model Bill for the Legal*

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investigations to the Queensland Law Society than his New South Wales counterpart. Consequently, Queensland is now said to be the most independent of the three co-regulation jurisdictions in Australia; see *ibid* at 57.

146 *Legal Profession Act 2004* (Vic), s 6.2(8-9).

147 See Parker and Evans, *supra* note 144 at 46-48.

148 In *Law Society of New South Wales v Foreman* (1994) 34 NSWLR 408, discussed in Christine E Parker, "Law Firms Incorporated: How Incorporation Could and Should Make Firms More Ethically Responsible" (2004) 23 UQLJ 347 [Parker, "Law Firms Incorporated"]. An attorney was struck off the roll for forging a law firm time sheet in order to support her evidence that she had given the client a costs agreement at the beginning of the retainer. Her actions were attributed, at least in part, to pressures to meet billing targets. A second case involved the same firm and concerned the intentional destruction of thousands of documents in the course of tobacco litigation. See discussion of *McCabe v British American Tobacco Australia Services Ltd*, [2002] VSC 73 (Unreported, Eames J, 22 March 2002) in Parker, "Law Firms Incorporated," *ibid.* The lawyers were also found to have misled the plaintiff and the Court regarding the documents' destruction. The trial judge struck out the defendant's defence and ordered judgment for the plaintiff without a trial on the basis that the destruction of documents had unfairly prejudiced the plaintiff's chances of success.

149 *Ibid.* Such concerns echo those raised by Justice Stephen Goudge in the Canadian context; see *supra* note 29 and accompanying text.

Profession which in 2011 was still under consideration.[150] The Bill strived for a new paradigm for regulating firms and other types of business structures that provide legal services. All Australian states and territories have now enacted a version of the Model Bill that relates to the regulation of legal practices and alternative business structures.

From a Canadian perspective, there are two critical points for understanding the regulation of law firms in Australia. First, Australian law did not and does not permit LLPs. Therefore, by allowing firms to incorporate into ILPs, the reforms presented an attractive new practice structure for lawyers. Second, the compliance measures enacted by the reforms currently only apply to ILPs. Lawyers practicing in traditional partnerships or alone are not subject to these regulations. Thus, the Australian reforms effectively established a new separate regulatory regime for ILPs, leaving the traditional complaints and discipline process in place for lawyers practicing in all other settings.

All states have maintained their traditional complaints-based investigation systems; however, early successes of the new compliance-based systems have had a positive impact on the number of complaints that regulators need to deal with. Of all the states, New South Wales has been at the forefront of regulatory change and I therefore focus on this state.

New South Wales also has the largest number of incorporated practices, with more firms opting to incorporate every year.[151] New South Wales' legislation explicitly authorizes ILPs and Multi-Disciplinary Practices (MDPs). The primary means of regulating the activities of an ILP is through regulating the actions of its legal practitioner director. Every ILP must have a legal practitioner director who is responsible for the legal services offered by the ILP. The legal practitioner director must also ensure that "appropriate management systems" are implemented and maintained.[152]

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150 See Council of Australian Governments, National Legal Profession Reform, online: <http://www.ag.gov.au/legalprofession>.

151 As of August 2010, there were 945 ILPs in New South Wales accounting for approximately one fifth of all legal practices in New South Wales. Another 110 ILPs were awaiting approval. As these numbers suggest, the option to incorporate has proven popular for firms. The majority of ILPs are in suburban Sydney, followed by the city of Sydney, and there are over 200 ILPs in rural New South Wales. "The majority of ILPs are either sole practitioners or firms with 3-10 partners. Several large national firms have also incorporated. There are about 30 multidisciplinary practices in New South Wales;" see New South Wales, Office of the Legal Services Commissioner, *2009-10 Annual Report* (Sydney, 2010) 16, online: <http://www.lawlink.nsw.gov.au/lawlink/olsc/ll_olsc.nsf/vwFiles/OLSC_2009_2010_AnnRep.pdf/$file/OLSC_2009_2010_AnnRep.pdf>.

152 *Legal Profession Act 2004 (NSW),* s 140(2).

This provision relates to the compliance audits, which will be discussed below. If the director fails to meet the standards for maintaining an appropriate management system, he or she will be held liable for professional misconduct. Under the Act, the director is also held vicariously liable for the professional misconduct of any legal practitioner employed by the ILP. If a legal practitioner director is found guilty of misconduct or is removed from that position, an ILP is given seven days to install a new one.[153]

Australian regulators hope to ensure consumer protection and ethical conduct by ILPs through a compliance system which involves two types of audits. Unlike most of the other compliance requirements, these audits apply not just to ILPs and MDPs but to all entities including law firms and all other types of entities that provides legal services. They reflect the "education towards compliance" framework which New South Wales, Queensland and Victoria regulators have agreed on as a guiding principle. Essentially, regulators in these States "exercise [their] audit powers in such a way as to encourage the highest possible level of voluntary compliance."[154] It is understood that from time to time audits will discover findings that warrant disciplinary action; however, the primary purpose is to encourage practitioners and directors to implement and improve appropriate management systems.[155]

The first type of audit by the Legal Services Commissioner is essentially a practice review.[156] It can be conducted at any type of legal practice, and can be initiated regardless of whether an allegation has been made against a member of the practice.[157] The goals for this type of audit are to achieve compliance with the Act and with the *Professional Conduct and Practice Rules* of the NSW Law Society. When conducting an audit, the Legal Service Commissioner can compel a legal practice to turn over documents and information it requires, but the statute does not authorize the Commissioner to discipline the firm as an entity as a result of an audit. The corresponding provision in Victoria's *Legal Profession Act* appears to grant the Legal Services Commissioner the power to discipline a firm upon audit findings; however, when the Legal Service Commissioner procured a legal opinion, it was told disciplinary action would only be available against ILPs, not partnerships.[158]

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153 *Ibid* at s 142.

154 Parker and Evans, *supra* note 144 at 247.

155 *Ibid*.

156 *Legal Profession Act 2004* (NSW), s 670(1).

157 *Ibid* at 670(5). See Steven Mark and Tahlia Gordon, "Compliance Auditing of Law Firms: A Technological Journey to Prevention" (2009) 28 UQLJ 215.

158 Parker, "Law Firms Incorporated" *supra* note 148.

The second type of audit that is conducted is reserved exclusively for ILPs. It is, in part, related to the compliance self-assessment that legal directors are required to conduct soon after notifying the Legal Service Commissioner of the firm's intent to incorporate. The actual audit, which can be conducted in addition to the general audit, focuses on compliance with the implementation of "appropriate management systems." The Legal Service Commissioner has created ten general criteria for management systems that ILPs should work towards. Similar to a "practice review" audit, the ILP audits do not require a complaint to be filed before they are initiated. However, there are certain triggers that will automatically result in an audit occurring. They include an ILP failing to return a self-assessment form, the legal director submitting the self-assessment with a number of non-compliant ratings, or complaints being made against members of the ILP.[159]

In terms of action subsequent to an audit, New South Wales is confined to disciplining the legal director for any issues that arise. However, this constitutes an indirect means of regulating the ILP, as the entity may only offer legal services for seven days without a director being appointed. Queensland, on the other hand, explicitly authorizes the Legal Service Commissioner to discipline the ILP as an entity by making an application to the Supreme Court to disqualify the corporation from providing legal services or applying certain conditions on the way in which legal services are provided.[160]

In Victoria, incorporated law firms are subject to direct disciplinary action as well. In one case, a medium-sized Victorian ILP was fined $40,000 for late payment of barrister's fees. The money for the fees had been collected from clients and paid into the firm's office account instead of the trust account, and then only paid out to the barristers when it suited the firm's cash-flow.[161]

While audit statistics are not published, according to the NSW Commissioner between 2008-2009 his office conducted four formal audits of ILPs as well as a number of less formal reviews.[162] The formal reviews were initiated as a result of inadequate results on self-assessments, a trust account inspection report that raised issues with respect to supervision of employees, and as a result of numerous complaints files against particular ILPs. In each audit, the Legal Service Commissioner sent a copy of the

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159 *Supra* note 157.

160 *Ibid.*

161 *Mills Oakley Lawyer Pty Ltd*, (Unreported, Legal Profession Tribunal, Victoria, 31 October 2003), cited in Parker, "Law Firms Incorporated," *supra* note 148.

162 Mark and Gordon, *supra* note 157 at 218.

practice review workbook to the firms as well as questions that were to be asked during the audit. Each firm responded favourably to the audit and made the necessary adjustments to their policies to bring their practice in line with the "management system" standards.[163]

Finally, to enhance the efficiency and effect of the compliance self-assessments, regulators in both NSW and Queensland are implementing new technologically advanced methods into their regulatory efforts. For example, in both jurisdictions, online portals have been created to conduct self-assessments as well as create channels of communication between ILPs and regulators.[164] The NSW Commissioner believes that such systems will make the self-assessment process more responsive, educational, and importantly, the online portal will make best use of the limited resources of the Legal Services Commissioner. Plans are currently underway to create an online system for self-assessment for all law firms in NSW as a strategy for spreading the positive effects that such a process has had on ILPs.[165]

3) Results and Assessment of Compliance-Based Regulation

In addition to the positive experience reported by legal directors and legal services commissioners in various states, there have also been empirical assessments conducted that support the view that compliance-based approaches generate a significant drop in complaints by consumers. A wide-ranging study conducted by Christine Parker revealed that the legislative provisions regarding "appropriate management systems," combined with the mandatory self-assessment process upon notifying the Legal Services Commissioner of intent to incorporate, substantially decreased the number of complaints made against practitioners working for the ILP.[166] On average, the complaint rate for each ILP dropped by one third after the self-assessment process had taken place. The findings in this study would strongly support the NSW Commissioner's proposal of expanding mandatory self-assessment processes to all legal practices as a way of lowering overall complaint rates.

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163 *Ibid* at 219.

164 See New South Wales, Office of the Legal Services Commissioner, online: <http://www.lawlink.nsw.gov.au/olsc and Queensland, Legal Services Commission, online: http://www.lsc.qld.gov.au/>.

165 Mark and Gordon, *supra* note 157 at 220.

166 Christine E Parker, Tahlia Gordon and Steve Mark. "Regulating Law Firm Ethics Management: An Empirical Assessment of the Regulation of Incorporated Legal Practices in NSW" (2010) 37 JL & Soc'y 466.

Although regulators in Australia have responded relatively well to the changes brought on by deregulation in the legal profession, there are a number of criticisms about the current system. First, there is still concern that the current system does not go far enough in regulating law firms. Given the history of law firm malfeasance and a general consensus among Australian regulators that firm cultures play an important role in professional misconduct, there is still very little entity regulation. This is especially true in New South Wales where ILPs can only be regulated through the process of dismissing their legal director for misconduct. In all jurisdictions, unincorporated practices are entirely free of entity regulation. The NSW Commissioner has commented that although entity regulation would be ideal, it remains too difficult to implement in practice, as it is not clear when law firms should be responsible in disciplinary proceedings as entities. This problem is ultimately due to the poor fit between entity responsibility and the traditional disciplinary approach through the court system.[167]

It is worth noting, however, that the Queensland and Victorian statutes explicitly provide for discipline of ILPs. Further, under the Consultation Draft laws for the national legal profession reform project currently underway, both ILPs and unincorporated firms would be subject to discipline as entities. Various regulators around Australia appear committed to implementing these draft laws as a means to facilitate standardized regulation on a national level. If this occurs, this concern could be addressed.

The second concern that has been raised is the lack of resources and expertise to support the current compliance-based regulatory model.[168] Regulatory bodies in Australia have only recently begun to implement compliance measures and, while there has been success in lowering complaint rates, the types of pressures that exist in law firms regarding billing and client pressures still exist. It is not clear that a legal services commissioner has the capacity to deter these types of cases while, at the same time, monitoring firms through the new compliance measures. It is argued that a mere "appropriate management system" requirement without a robust system of deterrence against professional misconduct is seriously deficient.[169]

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167 Parker, "Law Firms Incorporated", *supra* note 148 at n 121.

168 *Ibid.*

169 *Ibid*.

C) Paradigm Shifts: Entity and Outcomes-Based Regulation in The United Kingdom

Canadian lawyers and regulators are familiar with the general loss of self-regulation in the UK. They are probably less familiar with the particulars of the sweeping reforms underway in that jurisdiction. For our purposes, the most notable aspects are the shift in regulatory focus from the individual to the firm, both through discipline and compliance. It is also notable that in England, large firms have lobbied strongly for a separate regulatory track for large corporate law firms but to date have only been partially successful in their efforts.

In 2007, the UK Parliament enacted the *Legal Services Act*[170] in response to the wide-ranging reforms proposed by Sir David Clementi in his 2004 report.[171] The Clementi Report and the *Legal Services Act* have been the subject of much discussion and analysis. They are reviewed here only as necessary for the issues in this paper. Some of the reforms proposed by Clementi and included in the *Legal Services Act* (collectively "the UK reforms") relate to the regulation of law firms but it is important to note that the desire to regulate law firms did not drive the reforms although it was one of the products of those reforms. Rather, the UK reforms were driven by a combination of chronic dissatisfaction with the Law Society of England and Wales' handling of consumer complaints, a desire for more competition in the delivery of legal services and the perceived conflict of interest between the Law Society's role as regulator and representative of the profession.[172]

Clementi recommended loosening the regulations concerning legal disciplinary practices (LDPs) and MDPs. An LDP is a practice structure where the owners and managers are not exclusively solicitors or registered foreign lawyers.[173] It is essentially a partnership between barristers and solicitors and a precursor to MDPs, which are scheduled to begin the licensing process in 2012. LDPs appear to be an intermediate step in the deregulation process. Clementi argued that it is necessary to allow alternative business structures, such as LDPs and MDPs, to exist. However, he noted that their existence raises important regulatory issues, such as the Solicitors Regulation Authority's jurisdiction being limited to

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170 *Legal Services Act 2007*, c 29 (UK).

171 Sir David Clementi, *Review of the Regulatory Framework for the Legal Services in England and Wales* (Department of Constitutional Affairs, 2004) 1-2 [Clementi Report].

172 *Ibid* at 1-4.

173 Law Society of England and Wales, *Legal Disciplinary Practices*, online: <http://www.lawsociety.org.uk/productsandservices/practicenotes/ldp/3540.article#ldp>.

the legal department of these operations. He recommended that the regulation of such entities "be based more on the economic unit, rather than the individual lawyer."[174] This specific concern instigated the subsequent reports undertaken by Lord Hunt and Nick Smedley which will be discussed below.

The UK reforms introduced full co-regulation in England and Wales. The *Legal Services Act* established the Legal Services Board which now serves as the independent oversight body of all regulators of the legal profession.[175] It approves regulators, the front-line regulatory bodies made up of practitioners. Though they maintain direct regulatory powers, they are now subject to the independent oversight by the Legal Services Board.[176]

The "reserved legal activities" component of the new Act arguably has the most significant implications for the legal services industry. The Act delineates the reserved or "inner-circle" activities. They are:

(a) the exercise of a right of audience;
(b) the conduct of litigation;
(c) reserved instrument activities;
(d) probate activities;
(e) notarial activities;
(f) the administration of oaths.[177]

Each reserved activity is overseen by an "approved regulator," which is a body that licenses and regulates individuals who undertake these activities. There is no regulation of "non-reserved" legal services.[178]

Entities that are licenced to provide "reserved" legal activities are regulated via (1) duties imposed on individuals within those bodies; (2) sanctions against such individuals; and (3) sanctions against the entity itself. Regulatory powers also extend to non-licensed managers or employees of entities that are authorized to provide reserved legal

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174 Clementi Report*, supra* note 171 at 10.

175 *Legal Services Act 2007*, *supra* note 170, s 2(2).

176 *Ibid,* ss 27-46.

177 *Ibid*, s 12.

178 This is a critical difference between the regulation of the profession in the UK and in Canada. It is the basis for understanding how legal services may be provided by commercial i.e. non-legal firms in the UK, also known as the "Tesco law" phenomenon. See Neil Rose, "'Tesco Law' – not the big bang, but it will change the face of legal services" guardian.co.uk (25 March 2011), online: <http://www.guardian.co.uk/law/2011/mar/25/tesco-law-alternative-business-structures>.

activities.[179] Under this provision, in a partnership between a solicitor and another type of professional service provider, all of the employees of the firm would be bound by the Solicitors Regulation Authority's *Code of Conduct*. Finally, the Act lays out an extensive array of sanctions that may be enforced against individuals or against entities themselves. The Act authorizes financial penalties against a firm for violating regulations.[180] A regulator may also disqualify an individual from associating with a licensed entity.[181] Regulators have the power to suspend or revoke licenses granted to entities to practice reserved areas of law.[182]

The Solicitors Regulation Authority thus now regulates solicitors and law firms according to a code of conduct and specific regulations passed by the Law Society. Its *Code of Conduct* refers to lawyers and law firms.[183] As a result of the Hunt[184] and Smedley[185] reports, the Solicitors Regulation Authority has explicitly made firm regulation a primary objective, as it explains in its new October 2011 *Solicitors Handbook*:

> Our approach to regulation has two elements: firm-based requirements and individual requirements. It focuses on the practices of regulated entities as well as the conduct and competence of regulated individuals. This approach allows us to take regulatory action against firms or individuals, or both, in appropriate cases.[186]

The most fundamental component of the Solicitors Regulation Authority's regulatory power comes from the requirement that before any type of entity can provide solicitor's legal services it must be recognized. There are specific criteria an entity must meet before gaining recognition, and all recognized bodies are required to renew their recognition with the Solicitors Regulation Authority on a yearly basis.[187] The Solicitors Regulation Authority may also revoke its recognition of an entity at any time for a breach of the *Code of Conduct*. Finally, in cases where there is a nonlawyer manager of a recognized body – as in the case of legal

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179 *Legal Services Act 2007*, *supra* note 170 s 176(2).

180 *Ibid*, s 95(1-7).

181 *Ibid*, s 99(1-3).

182 *Ibid* at s 101(1).

183 Solicitors Regulation Authority, *SRA Code of Conduct 2011*, Rule 23: Application of these Rules.

184 Lord Hunt of Wirral, *The Hunt Review of Regulation of Law Firms* (October 2009), online: <http://www.legalregulationreview.com/files/Legal%20Regulation%20Report%20FINAL.pdf>.

185 Nick Smedley, *Review of the Regulation of Corporate Legal Work* (March 2009), online: <http://www.legalregulationreview.org.uk/files/report_smedleyfinal.pdf>.

186 Solicitors Regulation Authority, *SRA Handbook* (6 October 2011) at 3.

187 Solicitors Regulation Authority, Definitions – Recognised Bodies, online: <http://www.sra.org.uk/consumers/problems/definitions.page#recbod>.

disciplinary partnerships – the Solicitors Regulation Authority maintains regulatory control over that individual as a manager. Nonlawyer managers must be approved by the Solicitors Regulation Authority by meeting specific criteria, must abide by the *Code of Conduct* and may have Solicitors Regulation Authority approval withdrawn at any time.[188]

The Solicitors Regulation Authority has also released a handbook to help prepare solicitors and firms for firm-based outcomes regulation, which was implemented in October 2011. It notes such things as the need for all firms to have a compliance officer to "oversee and embed adherence to the principles, rules and outcomes, and a compliance officer for finance and administration to ensure compliance with the Accounts Rules."[189] The Solicitors Regulation Authority notes that firms will need to undertake extensive measures to improve their management skills and processes to ensure compliance with the new outcomes based regime. However, it is offering firms risk management seminars in the lead up to the new regime being implemented. Further, the Solicitors Regulation Authority has stated that it will seek to be responsive to the needs of firms in meeting compliance goals rather than act as a heavy handed disciplinarian, especially as the initial changes take effect.[190]

If the Solicitors Regulation Authority decides to launch an investigation there are two types – one which could be considered a typical regulatory agency investigation, and one which is quite intrusive and has consequences for the entire entity.[191] The first type involves an onsite investigation of a legal practice and includes an initial meeting with senior or other available partners, directors, members or managers of a firm. This is followed by a request for information, documents and an explanation from the accused practitioner, if that is the case. Following an analysis of the relevant information the investigating team decides whether to prepare a breaches checklist, investigation report or both. The breaches checklist is a less-formal document and contains a summary of Solicitors Regulation Authority findings along with the corrective action the entity must take. An investigation report is for more serious cases and includes a findings summary which is referred to either the Crown Prosecution Service or the Solicitors Disciplinary Tribunal.

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188 *Ibid*.

189 Charles Plant, "Outcomes based regulation: what your firm needs to build" *Law Society Gazette* (8 July 2010), online: <http://www.lawgazette.co.uk/opinion/by-the-book/outcomes-focused-regulation-what-your-firm-needs-build>.

190 *Ibid*.

191 For a description of the entire investigation process, see: <http://www.sra.org.uk/solicitors/enforcement/we-are-investigating-you.page>.

Under the *Legal Services Act*, the Solicitors Regulation Authority investigating team also maintains the authority to impose the following sanctions: imposing a disciplinary sanction and award costs, controlling how a solicitor practises, closing a practice, or revoking recognition, if the case involves a recognised body. The Solicitors Regulation Authority may also levy a fine of £2000 on an individual solicitor or a law firm. The Solicitors Regulation Authority also maintains the right to publish information about the case and the penalty if it decides to do so is in the public interest.[192]

The second type of investigation is called an "intervention" and is more intrusive. The grounds are laid out in statute[193] and conduct that triggers this type of investigation is that of suspected dishonest conduct by a solicitor or an employee of a solicitor's firm.[194] Once an intervention commences, an individual's practice ceases to exist.[195] The practitioner's account monies immediately vest in the Solicitors Regulation Authority and it takes possession of all documents, which are given to an appointed agent who oversees the process. Notably, under the amended Statute, the Solicitors Regulation Authority maintains the authority to pre-emptively revoke the "recognized" status of a legal entity which undergoes an intervention.[196] According to the Solicitors Regulation Authority, an intervention into a solicitor's practice almost always results in a referral to the Solicitors Disciplinary Tribunal.[197]

Since the implementation of the new regulatory regime in England and Wales, the Solicitors Regulation Authority has followed a policy of publishing disciplinary decisions on their website in a database created to aid consumers.[198] The database contains regulatory decisions resulting from investigations starting after January 2008.[199] A consumer may search for a solicitor's disciplinary record, but there does not appear to be a way to view the disciplinary record of entities such as law firms or LDPs. The solicitor-focused nature of the database is likely because many firms face closure when their solicitors are investigated, whereas individual solicitors

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192 *Ibid*.

193 *Solicitors Act 1974* (UK), 1974, c 47, schedule 1.

194 *Ibid* at Schedule 1, s 1(a).

195 Solicitors Regulation Authority, *Intervention into a practice*, online: <http://www.sra.org.uk/solicitors/enforcement/intervention-tribunal/intervention-reasons-costs.page#grounds>.

196 *Ibid*.

197 *Ibid*.

198 See http://www.sra.org.uk/consumers/solicitor-check.page.

199 Solicitors Regulation Authority, *Policy statement on publication of regulatory and disciplinary decisions*, online: <http://www.sra.org.uk/documents/Solicitors Regulation Authority/consultations/1106.pdf>.

usually face a suspension and may later offer their legal services through a new entity.[200]

As seen from the above review, the shift from individual to firm-based regulation is a significant part of the dramatic changes in the regulation of the legal profession in the United Kingdom. It is also notable and perhaps surprising to some readers that large corporate firms in England have lobbied hard for a separate track of firm regulation. This review of the regulation of law firms in comparable jurisdictions provides a useful basis for thinking about how law firms should be regulated in Canada. I now turn to this issue.

5. A Model for the Regulation of Law Firms in Canada

In Part 2 of this paper, I outlined my argument for law firm regulation in Canada. In this part, I set out the parameters for a proposed model for the regulation of law firms. It has been asserted that generally self-regulation promotes trust between professionals and their clients.[201] The normative ends of regulation of law firms should be public protection and promotion of public trust in self-regulation and in lawyers *qua* professionals. The essential "social contract" of self-regulation is that lawyers will regulate

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[200] There have been a number of firm closures by the Solicitors Regulation Authority, which turn up in searches of media reports. For example, in December 2009, a law firm was closed down by the Solicitors Regulation Authority as a result of suspected dishonesty, breaches of the Solicitors Accounts Rules, and breaches of the Solicitors Code of Conduct by five of its solicitors. See "Law firm closure in Stockport to affect 4,000 people" *BBC News* (8 January 2010), online: <http://news.bbc.co.uk/2/hi/uk_news/england/manchester/8448648.stm>. This was a significant closure, as 4000 customers were affected by the Solicitors Regulation Authority decision. However, a search for the law firm name on the Solicitors Regulation Authority database produces no results. Only when one searches for the name of one of the five suspended solicitors, does information about the law firm and misconduct turn up. A more recent law firm closure with wide ramification occurred in July 2010. The law firm was reported to be the UK's largest property conveyancing solicitor firm; see Dawn Murden, "Brokers warned to choose a conveyancing partner carefully as Solicitors Regulation Authority closes law firm" *Debt Management Today*, online: <http://www.debtmanagementtoday.co.uk/newsstory?id=862&type=newsfeature&title=brokers_warned_to_choose_a_conveyancing_partner_carefully_as_sra_closes_law_firm>. According to this report, solicitors of the firm were accused of overcharging customers for conveyancing services. Again, the decision can only be found on the Solicitors Regulation Authority website by searching for the names of the law firm's principals; however, once found, information about the firm name and closure details are available.

[201] Michael J Trebilcock, Carolyn J Tuohy and Alan D Watson, *Professional Regulation: A Staff Study of Accountancy, Architecture, Engineering and Law in Ontario prepared for The Professional Organizations Committee* (Toronto: Ontario Ministry of the Attorney General, 1979) 20.

themselves in the public interest.[202] An essential feature of this "social contract" of self-regulation is public accountability.[203] The regulation of law firms involves the creation of accountability mechanisms which are derivative of law societies' public accountability duties. This accountability imperative for law firms must be balanced against other regulatory principles of fairness, efficiency and effectiveness.[204] Thus, the model of law firm regulation that I propose below fosters accountability with the attempt at a "light" regulatory touch in recognizing concerns of fairness, efficiency and effectiveness.

A system of law firm regulation in Canada should include both compliance and discipline measures.[205] The experience of the regulation of other professions such as public accounting and real estate demonstrates the value of regulation through both compliance and discipline. Similarly,

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202 His Excellency The Rt Hon David Johnston, Governor General of Canada, "Canadian Bar Association's Canadian Legal Conference – The Legal Profession in a Smart and Caring Nation: A Vision for 2017" (Halifax, 14 October 2011), online: <http://www.gg.ca/document.aspx?id=14195>.

203 *Ibid.*

204 *C.f.* Alice Woolley, "Rhetoric and Realities: What Independence of the Bar Requires of Lawyer Regulation", University of Calgary, The School of Public Policy, Research Paper, vol 4, issue 8 (June 2011), online: <http://policyschool.ucalgary.ca/files/publicpolicy/A_Woolley_lawregulat_c.pdf>

205 In this section, I draw upon and attempt to respond to some of the following issues raised in the discussion paper prepared by the Barristers' Society of Nova Scotia:

- Should the focus be on regulation or on discipline or both?
- What will the emphasis be (i.e. make regulations but then reinforce with discipline referring to regulations)?
- If providing for law firm discipline, will the rules include a general supervisory duty of all disciplinary rules, or will there be select rules that attract a supervisory rule or will there be separate rules that are the focus of law firm activity exclusively?
- What liability standard should be set for firms – firm alone, firm and supervisory lawyer (ie partners), partners alone, or responsible subset of lawyers that caused the misconduct?
- Should a supervisory standard have an associated defence, such as "reasonable efforts"?
- What sanctions should accompany disciplinary misconduct of firms?
- Are there rules that could be better expressed as regulations, policies or procedures?
- Should there be policy and procedures relating to specific law firm activities?
- Should there be regulation made generally but allow firms to determine the nature or form of the regulation (ie regulate that each firm have in place policies and procedures relating to handing trust funds, or as is already the case, have the same policy regarding uniform trust fund accounts implemented by all firms)?
- Should there be included in regulations provision for an "ethics adviser" or "compliance specialist"? Should such a role be voluntary or mandatory? Should

the OSC and the IIROC operate on this basis. The Australian experience is also instructive. First, it has demonstrated the value of creating compliance requirements for law firms. Requiring law firms to engage in self-auditing and reporting has led to firms creating policies and procedures where they did not exist. Creating a compliance system involves an investment in time and money. Many law firms, however, have already created systems and policies in response to rules promulgated by law societies regarding client identification, cash transactions, conflicts, confidentiality, retention of client files, electronic data, etc. Moreover, insurers often require the creation of such systems and policies as part of "risk management" strategies.[206] Thus, in many ways, establishing a formal compliance regime would simply be operationalizing existing regulatory requirements and perhaps extending them across the profession.

Law societies should follow the model of the Nova Scotia Barristers Society and require all law firms to register and file annual reports. To be clear, I am not advocating a licensure system for law firms whereby law societies would set qualification standards and vet applications from law firms for licenses which could ultimately be subject to suspensions or revocation for disciplinary infractions. Such a system – as exists for securities regulation – would be expensive and require the creation of significant bureaucracies to administer. It is not clear to me that it is currently warranted in terms of a need for public protection or promotion of the public interest. I believe that both objectives can be adequately safeguarded through the creation of a system along the lines that I sketch out in this section.

The purpose of requiring law firms to register and file annual reports is to provide necessary information to law societies and to the public. Initial registration would also include information that must be contained in an annual report. Again, Nova Scotia's model is instructive. Firms should file an annual report which includes the names of all lawyers associated with the firm and the nature of their association; the location and particulars of all trust accounts and firm bank accounts maintained by the firm; the names and responsibilities of employees of the firm, or others,

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functions of an adviser or specialist be determined by regulation or left to the discretion of law firms?

See Barristers' Society of Nova Scotia, *Discussion Paper on Regulation of Law Firms* (2006) [unpublished] (on file with author).

206 Thank you to Malcolm Mercer and the group of large law firm counsel who deal with ethics and compliance issues for educating me and my colleagues about the role of insurance in creating ethical infrastructures within large law firms at a meeting in Toronto in 2011.

who maintain the accounting record of the firm.[207] The annual report should also designate an official representative for the purposes of communicating with the law society.[208] Finally, the annual report should also include the name of the firm "ethics counsel" whose responsibilities are described below.[209]

Law societies would create a public registry of law firms, searchable on law society websites. The purpose of such a registry would be to enable members of the public to view the above information on law firms.[210] It would also include any discipline history of law firms and their lawyer-members as well as information on pending discipline proceedings against the firm or its members. Such information should be presented in a manner that is clear and apparent to members of the public who are seeking information about a law firm or its members.

A strong compliance regime should be the core of a law firm regulation system. Compliance emphasizes prevention over punishment. Compliance aims to elevate the standard of practice rather than respond to complaints about professional misconduct. Again, the comparative experience of other professions in Canada and the legal profession in other jurisdictions shows that the regulation of the Canadian legal profession lags behind. It is somewhat ironic that Canadian lawyers are actively engaged in advising on and creating effective corporate governance compliance regimes but so little thought has gone into whether such regime would be beneficial for the legal profession. It is difficult to argue that the public interest does not require such measures.

Law societies should impose positive obligations on law firms to create systems and policies to ensure compliance with law society rules. The model here is a combination of ABA Model Rule 5.1(a) and IIROC's rule for registered firms. IIROC requires every registered firm to "establish, maintain and apply" policies and procedures "to establish a system of controls and supervision sufficient to (a) provide reasonable assurance that the firm and each individual acting on its behalf complies with securities legislation, and (b) manage the risks associated with its

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207 See Regulations made pursuant to the *Legal Profession Act*, *supra* note 91, Reg 7.2.1.

208 *Ibid* at Reg 7.2.2. See also *Regulation respecting the practice of the profession of advocate within a limited liability partnership or joint-stock company and in multidisciplinarity*, RRQ, c. C-26, r..

209 It is envisioned that in many if not most firms, the ethics counsel and the designated representative for communications with the law society would be the same person.

210 Banking and trust account information might need to be redacted for confidentiality or security reasons.

business in accordance with prudent business practices."[211] ABA Model Rule 5.1(a) requires law firm partners and managers to "make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the *Rules of Professional Conduct*."[212] Law societies should require law firms to "establish, maintain and apply" policies and procedures to establish a system of controls and supervision sufficient to provide reasonable assurance that the firm and each individual in the firm complies with applicable legislation, bylaws, rules and rules of professional conduct.[213]

In furtherance of these compliance obligations, law societies should require that every law firm designate one of its lawyers as "ethics counsel." This lawyer would serve as a law firm equivalent to the Chief Compliance Officer (CCO) in securities and other firms.[214] Such positions have become commonplace in American law firms. Some Canadian law firms already effectively have ethics counsel in place. Often denoted as "general counsel," these lawyers advise the firm on conflicts of interest and other ethics issues that arise within the firm.[215] Like the CCO under securities legislation, a designated ethics counsel would be responsible for ensuring, maintaining, supervising and applying the firm's policies and procedures to ensure compliance with law society regulatory and ethical responsibilities. It is hoped that the ethics counsel would also become an ethics counsellor to individual members of the firm: someone who other lawyers could come to when ethical issues arise.

Law societies should also provide for the discipline of law firms, both for compliance failures as well as entity misconduct. Creating compliance

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211 National Instrument 31-103 Registration Requirements and Exemptions and Consequential Amendments to Related Instruments (2009), 32 OSCB (Supp-4), 11.1.

212 ABA *Model Rules*, *supra* note 82, Rule 5.1(a).

213 Such policies would relate to matters such as retainer agreements, file opening and closing procedures, tickler systems, conflicts, confidentiality and billing. *C.f.* Schneyer, "Thoughts," *supra* note 142 at 14-15 (on the need to establish prophylactic ethics rules) and 17-20 (on the need for ethics rules on matters of law firm governance).

214 On such specialists see Elizabeth Chambliss and David B Wilkins, "The Emerging Role of Ethics Advisors, General Counsel, and other Compliance Specialists in Large Law Firms" (2002) 44 Ariz L Rev 559.

215 I prefer the term "ethics counsel" to both "general counsel" and "chief compliance officer." To me, "general counsel" connotes the legal adviser to the firm which may involve responsibilities beyond advising on ethics matters. In practice, many general counsel may be designated "ethics counsel" as well, if my proposal is adopted. Similarly, I prefer "ethics counsel" to "chief compliance officer" because the latter seems too narrow to me and connotes rule-following rather than a broader duty to foster an ethical environment and to serve as an advisor and counselor to lawyers within the firm who seek ethical advice.

requirements without having concomitant discipline powers over firms is problematic in two respects. First, the absence of discipline powers makes it difficult to enforce a compliance regime against recalcitrant law firms. Discipline is the necessary "stick" to ensure cooperation with compliance obligations. Law societies already use discipline powers to enforce compliance obligations against individual lawyers such as administrative suspension for failure to pay annual member fees or failure to complete required CLE/CPD. Second, there is a limit to the efficacy of even the strongest compliance measures. Discipline powers are necessary to deal with the most serious of violations, whether by individual lawyers or by law firms, that involve reckless or intentional conduct that violates law society rules or the rules of professional conduct.

The possibility of law firm discipline should also exist for entity misconduct. As explained in Part 2 above, I do not see law firm discipline as supplanting individual lawyer responsibility but rather as complementing it. Further, I do not see law firm discipline as something that is likely to be invoked frequently by law societies. Rather, discipline of law firms may be appropriate in two circumstances. First, lawyer malfeasance may be attributable to the lack of law firm policies and procedures or to flawed policies and procedures. For example, a lawyer may find herself in a conflict of interest because her firm lacked an appropriate conflicts screening procedure. Or the lawyer may have followed firm procedures regarding proceeding in the face of an arguable conflict of interest. In such cases, it is not accurate or fair to attribute an individual lawyer's breach of the rules of professional misconduct solely to the lawyer's actions if the lawyer was following the firm's procedures. The individual lawyer should be held accountable for her actions but so should the law firm as an entity. It is not that the firm policy should let the individual lawyer "off the hook" but that the existence of firm policy should place the firm squarely "on the hook" as well.

Second, law firm discipline may be appropriate where malfeasance is so wide-spread that it may be attributed to the organizational culture of a firm or to a firm systems failure. Whether one views law firms in negative ethical terms such as Slayton and many American critics or as positive ethical structures as Daniels does, collective sanction would be appropriate in such cases. The Pilzmaker-Lang Michener affair is case in point because it involved a collective decision made by the firm leadership not to report Pilzmaker to the Law Society of Upper Canada.[216] Similarly, if a lawyer or lawyers engage in sexual harassment of an employee or an associate, it may be appropriate to discipline the firm if it failed to have appropriate policies in place or failed to enforce them.

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216 See *supra* note 38.

Moreover, the response that the firm's management committee, managing partner or entire partnership could be sanctioned is both inaccurate and unrealistic. It is inaccurate because the larger the firm, the greater the fiction that the LLP is a partnership in the sense of an entity whose members share in the decision making and the management of the entity. It is much more akin to a corporation which operates through its management and executives. Indeed, the largest firms have now restructured themselves along such corporate lines. The partners in a firm of 50 lawyers are unlikely to create let alone monitor compliance with firm policies. Moreover, it is unrealistic to think that any law society would seek to sanction 50 let alone 200 or 500 partners. It is simply not feasible or efficient from a regulatory perspective. It makes far more sense to discipline the firm and the individual partners will be indirectly responsible for the sanction whether that be in monetary or reputational terms.

Given how I envision law firm discipline, I do not feel it would be appropriate to place the onus of responsibility almost entirely on a designated firm representative, such as the legal practitioner director for ILPs in New South Wales. A similar approach would see the managing partner or ethics counsel of a law firm disciplined for the actions of the firm. This approach is problematic because it imposes individual responsibility for collective malfeasance. The preferred approach is to maintain a system of predominantly individual responsibility but impose collective responsibility on law firms where warranted. Thus, where law firm discipline is appropriate, it should allow for law firms to be reprimanded and fined. Because discipline is tied to law firm policies and procedures, law societies should also be empowered to make other orders that are appropriate in the circumstances, such as ordering the creation of certain policies or systems, mandating training or continuing education, etc.

While various other issues would have to be addressed in grafting law firm regulation onto the existing regulatory framework,[217] I have attempted to lay out the foundation for such a regime in this section.

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[217] Many of these issues are addressed in the Nova Scotia Barristers' Society, *Discussion Paper on Regulation of Law Firms* (2006), *supra* note 205. For example: If providing for law firm discipline, will the rules include a general supervisory duty of all disciplinary rules, or will there be select rules that attract a supervisory rule or will there be separate rules that are the focus of law firm activity exclusively? What liability standard should be set for firms – firm alone, firm and supervisory lawyer (i.e. partners), partners alone, or responsible subset of lawyers that caused the misconduct? Should a supervisory standard have an associated defence, such as "reasonable efforts"? Are there rules that could be better expressed as regulations, policies or procedures? Should there be policy and procedures relating to specific law firm activities? Should there be regulation made generally but allow firms to determine the nature or form of the

6. Conclusion

Given the centrality of law firms to the practice of law in Canada, the growing trend to regulate law firms in other jurisdictions and the pervasiveness of firm regulation in other professions, the question for regulators in Canada should be rephrased from "why should law firms be regulated?" to "why aren't law firms being regulated?".

In Canada, this question is more acute than in other jurisdictions because of two factors. First, self-regulation of the legal profession is strongest in Canada among peer jurisdictions. This alone should shift the burden to the legal profession to ensure that self-regulation is in the public interest. However, the second factor is critical. This is the claim that has increasingly been made by members of the bar that self-regulation is not only in the public interest but is a superior public good, even a constitutionally mandated one. Given the importance of law firms, the need for law firm regulation is thus made more pressing. Indeed, the absence of firm regulation may be the Achilles heel of self-regulation in Canada. It is time for law societies to follow the path charted by Nova Scotia and ensure that when it comes to self-regulation, regulatory structures exceed regulatory rhetoric.

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regulation (i.e. regulate that each firm to have in place policies and procedures relating to handling trust funds or, as is already the case, have the same policy regarding uniform trust fund accounts implemented by all firms? An additional question that is sure to arise in a regime of law firm discipline is whether an individual lawyer have to disclose the discipline record of their former law firm if they were applying for a licence from the Society? This question would likely apply to an applicant transferring from another jurisdiction. This question may be relevant to the Society's statutory responsibility to determine the good character of applicants. An applicant for a licence should not be judged to lack good character simply because they worked at a law firm that was subject to discipline in another jurisdiction. However, the disclosure the discipline record of one's prior law may lead the Society to investigate the particulars of the case and determine whether the applicant was involved in any way that might affect licensing. One of the anonymous reviewers of this article raised the issue of how to deal with international law firms asking "[w]ho disciplines the global law firm?" This reviewer mused that "[p]erhaps there is another article to be written on this issue." I agree.