

Spring 2004

## Lawyers as Lawmakers: A Theory of Lawyer Licensing

Larry E. Ribstein

Follow this and additional works at: <https://scholarship.law.missouri.edu/mlr>



Part of the [Law Commons](#)

---

### Recommended Citation

Larry E. Ribstein, *Lawyers as Lawmakers: A Theory of Lawyer Licensing*, 69 Mo. L. REV. (2004)  
Available at: <https://scholarship.law.missouri.edu/mlr/vol69/iss2/1>

This Article is brought to you for free and open access by the Law Journals at University of Missouri School of Law Scholarship Repository. It has been accepted for inclusion in Missouri Law Review by an authorized editor of University of Missouri School of Law Scholarship Repository. For more information, please contact [bassettcw@missouri.edu](mailto:bassettcw@missouri.edu).

# MISSOURI LAW REVIEW

---

VOLUME 69

SPRING 2004

NUMBER 2

---

## Lawyers As Lawmakers: A Theory of Lawyer Licensing

*Larry E. Ribstein\**

### ABSTRACT

Existing explanations of lawyer licensing focusing on the need to ensure lawyer quality are unconvincing. A license to practice is a dubious signal of quality, the licensing requirement restricts the availability of legal services, and state licensing is subject to political capture by lawyers. These criticisms of lawyer licensing laws are increasingly important as the current system is threatened by changes in the legal services market and increased federal regulation of the legal profession. It is, therefore, time to reexamine the theory underlying the state licensing system.

This Article provides an alternative rationale for state licensing requirements. Lawyer licensing encourages lawyers to participate in lawmaking by capitalizing the benefits of their law-improvement efforts in the value of the law license. In other words, the license gives lawyers a kind of property right in state law. State competition gives lawyers an incentive to favor welfare-maximizing state laws that make the state attractive as a location for businesses and as a forum for litigation. This theory has important implications for both federalism and the scope and nature of lawyer licensing requirements.

---

\* Richard W. and Marie L. Corman Professor of Law, University of Illinois College of Law. I owe a particular debt to Bruce Kobayashi. Thanks for comments by Tom Ginsburg, Klaus Heine, Bruce Johnsen, Dean Lueck, Geoffrey Miller, Erin O'Hara, Richard Painter, Eric Rasmussen, Roberta Romano and participants at workshops at the American Law & Economics Association Annual Meeting, George Mason University Law School, University of Illinois College of Law and Kelley School of Business, Indiana University. Valuable research assistance was provided by Sheila Hathi and Brett Pyrdek.

## TABLE OF CONTENTS

INTRODUCTION .....	301
I. THE TRADITIONAL CASE FOR STATE LICENSING .....	303
<i>A. The Information Asymmetry Argument</i> .....	304
<i>B. Costs of State Licensing</i> .....	309
1. Licensing as a Poor Signal of Quality .....	309
2. Distorting the Supply of Legal Services .....	310
3. Effect of Ethics Rules on Lawyer Competition .....	313
<i>C. The Politics of Licensing</i> .....	314
<i>D. Alternatives to State Licensing of Law Practice</i> .....	315
1. Certification and Related Devices .....	316
2. Alternative Rules for Selecting State Licensing Regime .....	317
3. Permitting Practice Outside of Licensing State .....	319
4. Federal Licensing and Regulation .....	319
5. Alternative Methods of Lawyer Discipline .....	321
<i>E. Current Challenges to State-of-Practice Licensing</i> .....	321
1. Multi-State Law Practice .....	322
2. The Technological Threat to Traditional Law Practice ...	324
3. Inadequacy of State Regulation of Lawyers .....	325
4. Attack on Unauthorized Practice Laws .....	326
II. AN ALTERNATIVE ARGUMENT: LAWYERS AND STATE LAWMAKING .....	327
<i>A. Evidence of Lawyers' Participation</i> .....	327
<i>B. Lawyers' Incentive to Participate</i> .....	330
1. An Overview of the Theory .....	331
2. Licensing the Practice of Law .....	332
3. Tying Lawyers to States .....	333
4. Tying Practice of a State's Law to the Enacting State ...	335
<i>C. A Direct Intellectual Property Approach</i> .....	337
III. THE STATE COMPETITION DEBATE .....	339
<i>A. The Efficiency of Jurisdictional Competition</i> .....	339
<i>B. Effect of Lawyers' Influence</i> .....	345
1. Benefits of Lawyer Participation .....	345
2. Costs of Lawyer Participation .....	347
3. The Effect of Jurisdictional Competition and Type of Practice .....	349
4. Type of Law .....	352
<i>C. Implications for Federalism</i> .....	355
IV. THE NATURE AND SCOPE OF LICENSING REQUIREMENTS .....	355
<i>A. Licensing Requirements</i> .....	356
<i>B. Defining Law Practice</i> .....	356
<i>C. Licensing Specialists</i> .....	361

D. State Variations .....	361
E. Other Professions .....	361
V. CAVEATS AND CONCLUSIONS .....	362

## INTRODUCTION

Many commentators believe that state licensing of lawyers, like professional licensing generally, accomplishes little other than keeping the price of legal services and lawyers' wages high by restricting entry into the profession.<sup>1</sup> These doubts about lawyer licensing are especially acute in light of rapid changes in the legal services market. The increasingly interstate nature of legal services, the growth of nationwide professional firms, and the provision of legal information over the Internet call into question traditional rules requiring a state license for the practice of law.

Powerful forces are moving for changes in the traditional approach to lawyer licensing. Among other recent events, several states and the American Bar Association have endorsed clarifying rules on multi-jurisdictional practice;<sup>2</sup> the Justice Department and the Federal Trade Commission have challenged state bar restrictions on unauthorized practice of law;<sup>3</sup> and Congress has enacted a provision for a federal code of ethics for securities lawyers, a significant step toward federalization of law practice.<sup>4</sup> This is, therefore, a good time to consider the fundamental issues regarding the current system of regulating lawyers, particularly including what types of activities should require a law license and whether lawyer regulation should continue to be based on licensing by individual states.

This Article presents a new rationale for state licensing of lawyers—specifically, that state licensing gives lawyers an incentive to participate in the lawmaking process. Lawyers contribute much valuable time to state law reform not merely to enhance their own reputations, but to attract litigation or clients to their states. State licensing, operating in conjunction with

---

1. See generally MILTON FRIEDMAN, *Occupational Licensure*, in CAPITALISM AND FREEDOM 137 (1962); Morris M. Kleiner, *Occupational Licensing*, 14 J. ECON. PERSP. 189 (2000); Simon Rottenberg, *Introduction*, in OCCUPATIONAL LICENSURE AND REGULATION I (Simon Rottenberg ed., 1980); George J. Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. MGMT. SCI. 3 (1971).

2. State positions are summarized at <http://www.crossingthebar.com> (last modified Mar. 15, 2004). The ABA has recommended amending Model Rule 5.5 to specifically permit practice other than in a state in which a lawyer is licensed in certain circumstances. See American Bar Association, *Report of the Commission on Multijurisdictional Practice* (Aug. 2002), available at <http://www.abanet.org/cpr/mjp-home.html> [hereinafter, *MJP Commission*].

3. See *infra* note 129.

4. See Sarbanes-Oxley Act of 2002 § 307, 15 U.S.C. § 7245 (Supp. 2003).

conflict of laws rules, plays a role in this process by protecting lawyers' lawmaking efforts from free-riding by those who are not licensed locally. A state law license confers an exclusive right to represent clients based in the state and to practice in the state's courts. Moreover, the law applicable to a case or transaction often depends on the forum and where parties reside. Parties therefore will choose to reside or litigate in a state based to some extent on the quality of the state's law.<sup>5</sup> It follows that the value of a licensed lawyer's special rights to represent clients residing in a state or to appear in a state's court will depend on the licensing state's law. This encourages lawyers to participate in making that law.

This analysis has two important implications. First, the analysis is significant to the debate over the efficiency of federalism and state competition. A federal system makes it easy for individuals and firms to choose laws that suit their needs. It is not clear, however, why state lawmakers should have an incentive to provide suitable laws. Corporate franchise fees can give lawmakers in a small state like Delaware significant incentives to encourage local incorporations.<sup>6</sup> But prior literature has not clarified states' incentives to compete outside of this narrow context. This Article shows that lawyers' participation in state lawmaking in order to attract clients is the engine that drives jurisdictional competition.<sup>7</sup> It also shows that, by encouraging lawyers to engage in these activities, lawyer licensing is the fuel that runs the engine. Indeed,

5. See F.H. Buckley & Larry E. Ribstein, *Calling a Truce in the Marriage Wars*, 2001 U. ILL. L. REV. 561; Bruce H. Kobayashi & Larry E. Ribstein, *Contract and Jurisdictional Freedom*, in THE FALL AND RISE OF FREEDOM OF CONTRACT 325 (F.H. Buckley ed., 1999) [hereinafter Kobayashi & Ribstein, *Contract*]; Erin Ann O'Hara & Larry E. Ribstein, *Conflict of Laws and Choice of Law*, in 5 ENCYCLOPEDIA OF LAW AND ECONOMICS 631 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000); Erin A. O'Hara & Larry E. Ribstein, *From Politics to Efficiency in Choice of Law*, 67 U. CHI. L. REV. 1151 (2000) [hereinafter O'Hara & Ribstein, *From Politics to Efficiency*]; Larry E. Ribstein, *Choosing Law By Contract*, 18 J. CORP. L. 245 (1993) [hereinafter Ribstein, *Choosing*]; Larry E. Ribstein, *From Efficiency to Politics in Contractual Choice of Law*, 37 GA. L. REV. 363 (2003) [hereinafter Ribstein, *From Efficiency to Politics*]; Larry E. Ribstein & Bruce H. Kobayashi, *State Regulation of Electronic Commerce*, 51 EMORY L.J. 1 (2002) [hereinafter Ribstein & Kobayashi, *State Regulation*].

6. See Roberta Romano, *Law as a Product: Some Pieces of the Incorporation Puzzle*, 1 J.L. ECON. & ORG. 225 (1985) [hereinafter Romano, *Law as a Product*]; see also Roberta Romano, *The State Competition Debate in Corporate Law*, 8 CARDOZO L. REV. 709 (1987) (arguing that reincorporation costs limit state competition, so that firms reincorporate mainly when they are contemplating a transaction that is facilitated in the new jurisdiction).

7. For an earlier article noting this point, focusing on state choice of law statutes, see Larry E. Ribstein, *Delaware, Lawyers, and Contractual Choice of Law*, 19 DEL. J. CORP. L. 999 (1994).

states' ability to encourage lawyer participation in lawmaking by licensing lawyers helps support a federal rather than a unified system of laws.

Second, this Article's analysis has implications for the nature and scope of lawyer licensing. The lawmaking-incentive argument provides better support than traditional arguments for requiring broad training and education of lawyers. But it does so only where lawyers' participation in lawmaking is likely to lead to more efficient laws. This may be the case only as to types of practice where state laws are subject to viable competition that can weed out laws that unduly favor lawyers' interests.

This Article proceeds as follows. Part I evaluates the traditional argument for lawyer licensing based on ensuring lawyer quality. Part II presents this Article's alternative justification based on lawyers' participation in state lawmaking. Parts III and IV discuss the implications of this theory for, respectively, state competition and the extent and scope of licensing requirements. Part V concludes, highlighting the potential limitations of this Article's analysis.

## I. THE TRADITIONAL CASE FOR STATE LICENSING

This Article focuses on the system whereby lawyers are licensed to practice law in particular states.<sup>8</sup> Under the current system, one who does not have a license may not practice law. The need for a license restricts entry into the legal profession and mobility among the states by, among other things, requiring an extensive legal education; requiring lawyers to incur the costs and risks of the bar examination in each state where they wish to practice (depending on reciprocity rules); and imposing costs of maintaining the license, such as mandatory continuing legal education ("CLE").

It is important to emphasize that licensing is required not only for those who call themselves "lawyers," as would be the case for a less binding certification requirement,<sup>9</sup> but, by virtue of unauthorized practice rules, for anyone who wants to perform legal services. Unauthorized practice laws and the definition of law

---

8. In most states, supreme courts control the rules for bar admission. See Benjamin Hoom Barton, *Why Do We Regulate Lawyers?: An Economic Analysis of the Justifications for Entry and Conduct Regulation*, 33 ARIZ. ST. L.J. 429, 434 n.16 (2001). Courts and legislatures often delegate lawyer regulation to the state bar association. For analyses of compulsory bar membership, also referred to as "integrated" or "unified" bars, see Theodore J. Schneyer, *The Incoherence of the Unified Bar Concept: Generalizing from the Wisconsin Case*, 1983 AM. B. FOUND. RES. J. 1, and Bradley A. Smith, *The Limits of Compulsory Professionalism: How the Unified Bar Harms the Legal Profession*, 22 FLA. ST. U. L. REV. 35 (1994). Part I.D discusses possible alternative systems of regulating lawyers.

9. See *infra* Part I.D.1.

practice are discussed in more detail below.<sup>10</sup> For present purposes it is enough to note that a non-lawyer not only may not participate in legal proceedings on behalf of another, but also may not be able to advise others on the law. Given the pervasiveness of legal issues in modern life, this prohibition applies to a potentially wide range of conduct.

Another important feature of the current system is that lawyers who practice outside the state where they are licensed risk fines in both the licensing and non-licensing states.<sup>11</sup> Careful lawyers must particularly beware the borderline cases, such as where the lawyer must spend a substantial amount of time on behalf of a single client in a non-licensing state.<sup>12</sup> While lawyers can be licensed in several states, this involves potentially high costs of taking a bar exam or being admitted on motion in each state, as well as maintaining bar memberships through continuing legal education, dues, pro bono work and the like.<sup>13</sup>

This Part discusses the traditional case for state licensing of professionals, including lawyers. It shows that conventional arguments emphasizing information asymmetries are too weak to support the current system. This suggests that this Article's alternative theory that state licensing gives lawyers incentives to participate in lawmaking may provide critical support for retaining some form of state licensing. Subparts A and B discuss the questionable benefits and significant costs of state licensing. Subpart C provides a political perspective that casts further doubt on the traditional arguments for state licensing by showing how licensing promotes lawyers' interests. Subpart D shows how licensing's benefits can be obtained through alternative, arguably less costly, means. Subpart E discusses the market and political attacks on the current system that make it vulnerable in the absence of a new and stronger rationale such as the one this Article proposes.

### *A. The Information Asymmetry Argument*

Arguments for mandatory licensing of lawyers often are based on information asymmetry between lawyers and clients. A client can most reliably judge a lawyer based on experience with the lawyer and the results the lawyer produces. Legal services therefore are a kind of "credence" good that the client

---

10. See *infra* Part IV.

11. For discussions of the penalties for unlicensed practice focusing on the specific context of multi-state law practice, see William T. Barker, *Extrajurisdictional Practice by Lawyers*, 56 BUS. LAW. 1501 (2001), Jeffrey L. Rensberger, *Jurisdiction, Choice of Law, and the Multistate Attorney*, 36 S. TEX. L. REV. 799 (1995), and Charles W. Wolfram, *Sneaking Around in the Legal Profession: Interjurisdictional Unauthorized Practice by Transactional Lawyers*, 36 S. TEX. L. REV. 665 (1995).

12. See *supra* note 11.

13. For discussion of licensing requirements, see *infra* Part IV.A.

initially takes on trust.<sup>14</sup> Clients' difficulties in evaluating lawyers arguably make an unregulated lawyer market one for "lemons" in which low-quality lawyers ultimately will predominate.<sup>15</sup>

This argument is based on consumers' high costs of acquiring information about the quality of professional services.<sup>16</sup> The argument therefore assumes that government can provide information through licensing at a lower cost than individual consumers would incur through self-help.<sup>17</sup> A lawyer's license tells clients that the lawyer meets certain minimum qualifications. This information may be particularly helpful for clients who deal rarely with the legal system, lack independent resources for checking qualifications, or have relatively small or routine matters that do not justify substantial investigation.

Licensing laws not only provide a screening mechanism, but also back rules governing professional conduct. Legal representation can give rise to agency costs—that is, the costs of a property owner's delegating management power to a non-owner agent whose interests may conflict with the principal's.<sup>18</sup> For example, a lawyer may spend insufficient time on a client's work, misuse client funds, spend more time than necessary on a client's work, or misrepresent her qualifications.<sup>19</sup> The state's power to withdraw a professional license enforces

14. As to credence goods generally, see Michael R. Darby & Edi Karni, *Free Competition and the Optimal Amount of Fraud*, 16 J.L. & ECON. 67, 69 (1973), and Ellen R. Jordan & Paul H. Rubin, *An Economic Analysis of the Law of False Advertising*, 8 J. LEGAL STUD. 527, 530-31 (1979).

15. See generally George A. Akerlof, *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*, 84 Q.J. ECON. 488 (1970). For applications to professionals, see Hayne E. Leland, *Minimum-Quality Standards and Licensing in Markets with Asymmetric Information*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 265, Hayne E. Leland, *Quacks, Lemons, and Licensing: A Theory of Minimum Quality Standards*, 87 J. POL. ECON. 1328 (1979), Thomas G. Moore, *The Purpose of Licensing*, 4 J.L. & ECON. 93, 104-05 (1961), and Carl Shapiro, *Investment, Moral Hazard, and Occupational Licensing*, 53 REV. ECON. STUD. 843 (1986). For an article examining market solutions to the credence good problem, see Thomas N. Hubbard, *How Do Consumers Motivate Experts? Reputational Incentives in an Auto Repair Market*, 45 J.L. & ECON. 437 (2002).

16. See generally George J. Stigler, *The Economics of Information*, 69 J. POL. ECON. 213 (1961).

17. For commentary making the information cost argument in the context of professional licensing, see CHARLES L. SCHULTZE, *THE PUBLIC USE OF PRIVATE INTEREST* 35-42 (1977), and Keith B. Leffler, *Physician Licensure: Competition and Monopoly in American Medicine*, 21 J.L. & ECON. 165, 172-74 (1978).

18. See generally Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976).

19. See Larry E. Ribstein, *Ethical Rules, Agency Costs, and Law Firm Structure*, 84 VA. L. REV. 1707 (1998).



conduct regulation by causing forfeiture of the professional's substantial investment in the training and other costs necessary to obtain the license.<sup>20</sup>

These arguments require two important qualifications. First, private markets or alternative methods of protecting consumers, including malpractice liability and certification,<sup>21</sup> may produce comparable benefits at the same or lower cost. Clients have low-cost methods of obtaining reliable information about lawyers without any regulation, including reputation information from friends and their own past dealings with lawyers.<sup>22</sup> Lawyers can address the information problem by signaling quality through advertising and other ways.<sup>23</sup>

Second, regulation must be appropriately designed to provide quality assurances. Some barriers to entry are less effective than others in ameliorating information asymmetry regarding professional services.<sup>24</sup> Poorly designed licensing laws may injure consumers by providing a false assurance of quality.<sup>25</sup>

Even apart from these qualifications, the benefit to clients is unclear. Clients are unlikely to assume without any information that a lawyer will be completely honest and trustworthy. Indeed, the "lemons" theory assumes that buyers understand the quality problem and therefore pay less for both high and low-quality products than they would if there were no such problem to compensate for the risk of being cheated or for the cost of self-protecting by monitoring, obtaining a bond, or getting more information.

Under the traditional information-asymmetry rationale, lawyer licensing arguably has four types of benefits. First, by providing quality assurances,

20. See Alan D. Wolfson et al., *Regulating the Professions: A Theoretical Framework*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 206.

21. See *infra* Part I.D.

22. See Barton, *supra* note 8, at 439; George C. Leef, *The Case for a Free Market in Legal Services*, CATO POL'Y ANALYSIS, Oct. 9, 1998, at 1; Keith B. Leffler, *Commentary*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 290.

23. See Fred S. McChesney & Timothy I. Muris, *The Effect of Advertising on the Quality of Legal Services*, 65 A.B.A. J. 1503 (1979) (showing that legal clinic using advertising in high-volume legal practice reduced costs without compromising quality); Timothy J. Muris & Fred S. McChesney, *Advertising and the Price and Quality of Legal Services: The Case for Legal Clinics*, 1979 AM. B. FOUND. RES. J. 179 (same). For general theoretical discussions of the role of advertising in providing quality assurances, see Benjamin Klein & Keith B. Leffler, *The Role of Market Forces in Assuring Contractual Performance*, 89 J. POL. ECON. 615 (1981), Benjamin Klein et al., *Vertical Integration, Appropriable Rents, and the Competitive Contracting Process*, 21 J.L. & ECON. 297 (1978), and Leffler, *supra* note 22. Indeed, a practitioner's incurring the opportunity costs of choosing to make a living out of law itself signals that at least the lawyer genuinely believes in her ability.

24. See *infra* Part I.B.1. But note that any entry barrier arguably provides at least some information, if only in permitting the professional to signal her confidence that she has enough skill to warrant the opportunity cost of obtaining the license.

25. See *infra* Part I.B.2.

licensing encourages people to use licensed professional advisors rather than other ways of dealing with the law, including self-representation.<sup>26</sup> The question, then, is whether society is better off if people get their legal advice from professional advisors. Professionalizing legal advice arguably serves social justice, the rule of law, and the reliability of contracts.<sup>27</sup> On the other hand, legal professionals may promote socially wasteful litigation. Also, licensing, by increasing the price of legal advice, may reduce low-income clients' access to legal services.<sup>28</sup> This might be ameliorated by requiring lawyers to render services to the poor as part of the cost of the license.<sup>29</sup> But this requirement could have its own negative consequences, including encouraging more inefficient litigation.<sup>30</sup>

Second, licensing may benefit lawyers by reducing their costs of signaling quality. But this benefit accrues mainly to lawyers who practice alone or in small firms and who have difficulty signaling quality in other ways. By contrast, large law firms can signal quality by posting substantial and long-lived reputation bonds.<sup>31</sup> It is not clear how society gains by subsidizing small firms. Licensing

26. However, as discussed *infra* Part I.B.2, licensing may actually encourage those people who do use substitutes to use substitutes that are inferior to those they would use if licensing and unauthorized practice laws did not drive the superior goods from the market.

27. See Barton, *supra* note 8; Frank B. Cross, *The First Thing We Do, Let's Kill All the Economists: An Empirical Evaluation of the Effect of Lawyers on the United States Economy and Political System*, 70 TEX. L. REV. 645, 678-79 (1992) (arguing that "[t]he uncertain and relatively insignificant monetary costs of lawyering are more than justified by the nonmarketed social goods (including human rights and democracy) that lawyers help supply"); Malcolm Getz et al., *Competition at the Bar: The Correlation Between the Bar Examination Pass Rate and the Profitability of Practice*, 67 VA. L. REV. 863, 864 (1981) (noting importance of lawyers in ensuring access to justice and reliability of contracts).

28. See *infra* text accompanying note 59.

29. Current rules do not include such a requirement. See Barton, *supra* note 8. Model Rules of Professional Conduct, Rule 6.1, recommends that "[a] lawyer should aspire to render at least (50) hours of pro bono publico legal services per year." However, Comment 12 to the Rule states that "[t]he responsibility set forth in this Rule is not intended to be enforced through disciplinary process." MODEL RULES OF PROF'L CONDUCT R. 6.1 cmt. 12 (2003).

30. See RICHARD A. POSNER, *OVERCOMING LAW* 61 (1995). This is an old argument. See ROBERT BURTON, *THE ANATOMY OF MELANCHOLY: VOLUME ONE* 84 (Holbrook Jackson ed., 1932) (noting that lawyers "plead for poor men gratis, but they are but as a stale to catch others"). Pro bono rules also may have anti-competitive effects. See Jonathan R. Macey, *Mandatory Pro Bono: Comfort for the Poor or Welfare for the Rich?*, 77 CORNELL L. REV. 1115 (1992) (noting that pressures to do pro bono work help large firms by reducing competition from smaller firms).

31. With respect to this function of large law firms, see Ribstein, *supra* note 19 (showing how ethical rules backed by mandatory licensing may discourage the growth

may reduce concentration in the market for legal services,<sup>32</sup> but the cost of such concentration is not clear.<sup>33</sup> Also, even if licensing reduces concentration in the market for lawyers, it may increase concentration and reduce availability of legal services overall by blocking entry of low-end non-lawyer providers.<sup>34</sup>

Third, lawyer licensing arguably protects third parties who would be injured by unregulated legal advisors who enable others to break the law. But the costs and benefits of licensing must be compared to those of liability rules. One who hires a lawyer to harm third parties may be held liable as a principal, or the lawyer may be held liable for aiding and abetting the client's wrong. Focusing on lawyers' qualifications to practice would seem to be an ineffective way to prevent lawyers from engaging in misconduct.<sup>35</sup>

Fourth, lawyer licensing might be said to increase social welfare by backing lawyer regulation that improves the administration of justice.<sup>36</sup> In particular, licensing law practice may help ensure good lawyer conduct in court by bringing the power of license revocation to bear on violations of conduct rules.<sup>37</sup> But it is not clear whether this additional sanction is necessary to ensure compliance with conduct rules or that licensing contributes significantly to regulating lawyer conduct in court.<sup>38</sup>

Even if these arguments support licensing of lawyers, they do not necessarily support the current system of requiring lawyers to obtain a license in each state in which they practice, as distinguished from the alternative approaches to licensing discussed below.<sup>39</sup>

---

of large firms).

32. See Wolfson et al., *supra* note 20, at 207.

33. Indeed, from the standpoint of the theory emphasized in this Article, the emphasis on small firms may impose social costs by discouraging investments in efficient lawmaking. See *infra* Part II.B.3.

34. See *infra* text accompanying note 59.

35. This is illustrated by the apparently extensive failings of licensed professionals to protect the public from damage in connection with the Enron bankruptcy. It is not clear that either licensing or mandatory lawyer disclosure of client dishonesty is better than relying on private ordering, since clients have an incentive to signal that they have nothing to hide by hiring lawyers who pledge to disclose client wrongdoing. See Richard W. Painter, *Toward a Market for Lawyer Disclosure Services: In Search of Optimal Whistleblowing Rules*, 63 GEO. WASH. L. REV. 221 (1995).

36. See Barton, *supra* note 8, at 477-81.

37. See *supra* text accompanying note 20.

38. See Barton, *supra* note 8; Leef, *supra* note 22.

39. See *infra* Part I.E.

### B. Costs of State Licensing

Any benefits of lawyer licensing should be balanced against its potential costs. The following Sections show how licensing may cause several potential types of market distortions compared to an unrestricted market for legal services.<sup>40</sup> A review of these costs shows that state licensing of lawyers requires stronger justifications than those based on information asymmetry discussed in Subpart A.

#### 1. Licensing as a Poor Signal of Quality

Professional licensing standards are not well designed to ensure quality of professional services<sup>41</sup> and there is little evidence that they have done so.<sup>42</sup> Specifically, it has been argued that law school,<sup>43</sup> bar exam,<sup>44</sup> and continuing legal education requirements<sup>45</sup> provide little assurance of attorney competence.<sup>46</sup>

40. See generally Christopher Curran, *Regulation of the Professions*, in 3 THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 247-55 (Peter Newman ed., 1998) (discussing market distortions caused by licensing).

41. Milton Friedman long ago pointed out the irrationality of education requirements for professionals. See FRIEDMAN, *supra* note 1, at 158. For other criticisms of professional licensing standards, see S. DAVID YOUNG, *THE RULE OF EXPERTS: OCCUPATIONAL LICENSING IN AMERICA* (1987), Robert G. Evans, *Professionals and the Production Function: Can Competition Policy Improve Efficiency in the Licensed Professions?*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 225, and Alan D. Wolfson et al., *supra* note 20, at 180.

42. See Deborah Haas-Wilson, *The Effect of Commercial Practice Restrictions: The Case of Optometry*, 29 J.L. & ECON. 165 (1986) (showing that quality of optometry is not affected by commercial practice restrictions); Morris M. Kleiner & Robert T. Kudrle, *Does Regulation Affect Economic Outcomes? The Case of Dentistry*, 43 J.L. & ECON. 547 (2000) (study showing that increased licensing restrictiveness did not improve dental health); Kleiner, *supra* note 1, at 198 (summarizing studies).

43. See Leef, *supra* note 22.

44. See Barton, *supra* note 8; Daniel R. Hansen, Note, *Do We Need the Bar Examination? A Critical Evaluation of the Justifications for the Bar Examination and Proposed Alternatives*, 45 CASE W. RES. L. REV. 1191 (1995). For other criticisms of the bar exam, see Andrea A. Curcio, *A Better Bar: Why and How the Existing Bar Exam Should Change*, 81 NEB. L. REV. 363 (2002); Kristin Booth Glen, *When and Where We Enter: Rethinking Admission to the Legal Profession*, 102 COLUM. L. REV. 1696 (2002).

45. See Walter Gellhorn, *The Abuse of Occupational Licensing*, 44 U. CHI. L. REV. 6 (1976).

46. Analogously, a study showed that consumers' complaints against contractors rose as contractors learned to pass the entrance exam without becoming more competent. See Alex R. Maurizi, *The Impact of Regulation on Quality: The Case of California Contractors*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 26.

Even if licensing requirements screen out less skilled practitioners, they may not measure the skills that matter to most clients. Many routine tasks such as preparing wills for small estates and handling no-fault divorces call for attention to detail rather than an understanding of the complex legal theories law schools teach or mastery of the legal rules bar exams measure. Thus, a study found little evidence of risk to the public from lay providers of real estate settlement services.<sup>47</sup>

These criticisms have two important implications. First, if licensing requirements do not exclude unfit practitioners, it follows that the costs involved in distorting the supply of legal services discussed below outweigh the benefits of such distortions. Second, irrational licensing requirements may mislead clients about lawyers' competence. If, as mandatory licensing laws assume, clients mistakenly rely on a professional's shingle, bolstering the shingle with a license based on the wrong criteria encourages even more mistaken reliance.<sup>48</sup>

## 2. Distorting the Supply of Legal Services

Lawyer licensing restricts the total supply of lawyers or the supply in particular locations or market segments. State licensing laws that prevent lawyers from practicing outside the licensing state or discourage them from obtaining licenses in multiple states insulate each state sub-market from competition.<sup>49</sup> The price of legal services may rise in a jurisdiction when demand for lawyers increases relative to supply because licensing restricts entry of new lawyers.<sup>50</sup> Though lawyer supply ultimately may increase with the

---

47. See Joyce Palomar, *The War Between Attorneys and Lay Conveyancers—Empirical Evidence Says “Cease Fire!”*, 31 CONN. L. REV. 423 (1999).

48. See Barton, *supra* note 8, at 445 (noting that bar examinations and continuing legal education requirements send false signals of lawyer competence). For similar criticisms of professional licensing outside of law, see generally YOUNG, *supra* note 41, and Curran, *supra* note 40, at 250.

49. See RICHARD L. ABEL, AMERICAN LAWYERS 116-17 (1989).

50. With respect to the effect of professional licensing on mobility, see Bryan L. Boulier, *An Empirical Examination of the Influence of Licensure and Licensure Reform on the Geographical Distribution of Dentists*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 73 (showing how permitting reciprocity of licensing affects distribution of professionals and consumer surplus among states); and Kleiner, *supra* note 1 (showing that less reciprocity is correlated with less mobility of professionals and misallocation of labor across states).

demand for lawyers, other things equal,<sup>51</sup> licensing laws may cause at least short-term market disequilibrium.<sup>52</sup>

Important variations on bar requirements include admission on motion without having to meet other qualifications; maintaining a local office; a written exam that may or may not differ from that required for new lawyers;<sup>53</sup> a minimum period of practice in another state;<sup>54</sup> reciprocity, or whether the applicant's state admits lawyers from the entry state on similar terms; special rules for "emeritus" lawyers or lawyers who will serve the poor; and special rules for in-house lawyers.<sup>55</sup> Bar requirements also may make it costly for lawyers to maintain multiple bar memberships after they are admitted. For example, lawyers in the dozen or so states that do not have a mandatory continuing legal education requirement must incur additional costs in order to maintain bar membership in another state that does require CLE.

It is not clear whether or how much professional licensing affects the price or availability of professional services.<sup>56</sup> Lueck, Olsen and Ransom attempted to isolate the supposed cartel effect of lawyer licensing by correlating lawyers'

51. See B. Peter Pashigian, *The Market for Lawyers: The Determinants of the Demand for and Supply of Lawyers*, 20 J.L. & ECON. 53 (1977) (showing that the supply of lawyers is determined mainly by business activity and earnings outside the legal profession).

52. This effect may be exacerbated by the requirement that law schools be nonprofit, which limits their incentives to respond to increases in the demand for lawyers. See *id.*; see also Sherwin Rosen, *The Market for Lawyers*, 35 J.L. & ECON. 215 (1992) (presenting data as to number of and enrollment in law schools).

53. Many states also require the objective MPRE exam. However, since this exam need be taken only once and its scores used in many states, it does not constrain multiple licenses as much as a written exam.

54. The District of Columbia is the only jurisdiction that does not require prior legal experience for admission on motion. The states vary slightly regarding what is defined as "practice." Only Virginia requires the actual practice of law as distinguished from law teaching or working as in-house counsel or a government lawyer. The California requirement that lawyers admitted elsewhere take the California bar is discussed *infra* note 158 and accompanying text.

55. These requirements are summarized at <http://www.crossingthebar.com/admissionchart.htm> (last edited Apr. 9, 2004).

56. For studies purporting to show that licensing increases price, see Haas-Wilson, *supra* note 42 (showing effect of restrictions on the price of optometry services); Kleiner & Kudrle, *supra* note 42 (showing that increased licensing restrictiveness raised prices of dental services); Kleiner, *supra* note 1 (showing effect of licensing on earnings); and Lawrence Shepard, *Licensing Restrictions and the Cost of Dental Care*, 21 J.L. & ECON. 187 (1978) (showing higher fees for dentists in states without reciprocity). *But see* Edward Shinnick & Frank H. Stephen, *Professional Cartels and Scale Fees: Chiselling on the Celtic Fringe?*, 20 INT'L REV. L. & ECON. 407 (2000) (finding no evidence of cartel pricing in Scotland and Ireland).

income and the price of legal services with barriers to entry as indicated by such factors as bar passage rates and residency requirements for admission.<sup>57</sup> They concluded that lawyers' income and prices correlated less with barriers to entry than with market variables such as population density, growth, per capita income and employment, with human capital variables such as lawyers' experience and schooling, and with specific factors reflecting demand for legal services such as the divorce rate. Also, the percentage of lawyers in the state population did not depend on barriers to entry, but rather on the demand for lawyers as indicated by employment in industries that tend to generate law business. On the other hand, the study provided some support for the cartel theory by showing that regulatory variables testing state restrictions on admission to the bar were jointly important to lawyer earnings.<sup>58</sup>

The important question is whether any distortions in the market for lawyers caused by lawyer licensing increase or decrease social welfare. If lawyer licensing fails to exclude unskilled lawyers but excludes some skilled lawyers, it prevents the efficient production and utilization of legal advice. Alternatively, licensing may have little effect beyond that of private ordering and markets, so that its costs outweigh its benefits.

Licensing may reduce social welfare even if it functions as intended in screening less qualified practitioners. For example, licensing may leave lower-income clients without legal help because they cannot afford licensed practitioners,<sup>59</sup> or at least may reduce competition and raise prices for low-end customers.<sup>60</sup> To the extent that income levels correlate with race or ethnicity, licensing requirements may hurt members of racial minority groups.<sup>61</sup>

---

57. See Dean Lueck et al., *Market and Regulatory Forces in the Pricing of Legal Services*, 7 J. REG. ECON. 63 (1995).

58. See *id.* Although the study showed no significant correlation with the price of legal services to clients and the hourly rates firms charged for individual lawyers' services, lawyer earnings arguably measure the cartel effect more accurately than prices because the latter depend partly on the cost of living in each locale. There was also no significant correlation between some individual regulatory variables and lawyer earnings. But in assessing whether state regulation restricts entry the rules should be viewed as a package, with harsher restrictions in some areas substituting for laxer restrictions in others.

59. See YOUNG, *supra* note 41, at 20-21. For criticisms of the bar exam requirement as promoting this result, see Curcio, *supra* note 44, and Glen, *supra* note 44.

60. See J. Howard Beales, III, *The Economics of Regulating the Professions*, in REGULATING THE PROFESSIONS: A PUBLIC POLICY SYMPOSIUM 125, 137-38 (Roger D. Blair & Stephen Rubin eds., 1980); see also John R. Lott, Jr., *Licensing and Nontransferable Rents*, 77 AM. ECON. REV. 453 (1987) (showing how non-transferable professional licenses discourage some low-cost producers).

61. For discussions of the discriminatory effects of professional licensing laws, see, for example, FRIEDMAN, *supra* note 1, at 150-51, YOUNG, *supra* note 41, at 75-80, Barton, *supra* note 8, at 444, Curran, *supra* note 40, at 251, Richard B. Freeman, *The*

Professional school accreditation requirements similarly may affect the cost of legal services.<sup>62</sup>

Licensing laws also may reduce the quality of services clients of all types actually receive by forcing them to substitute self-help or unqualified practitioners for the lower-level but adequate practitioners licensing laws drive out of the market.<sup>63</sup> As Milton Friedman observed, requiring people to hire licensed practitioners is like requiring them to have either Cadillacs or no automobiles at all.<sup>64</sup> This problem is graphically illustrated by a study showing that licensing increased electrical shock cases as people substituted self-help for licensed electricians.<sup>65</sup>

Ironically, the foregoing arguments suggest that licensing hurts the ones who need it most, and helps those who need it least. Licensing is most important in ensuring quality where clients are least able to self-protect, as in small transactions where the costs of obtaining information outweigh the benefits,<sup>66</sup> or where clients are relatively uneducated and unsophisticated. Yet at the lower end of the market licensing laws most restrict the supply of services. Licensing more accurately signals quality at the upper end of the market, but here large law firms provide the same protection, and clients are more sophisticated.

### 3. Effect of Ethics Rules on Lawyer Competition

The state licensing system has important implications for the promulgation and enforcement of ethical rules. Ethical rules have been characterized as standard form contracts between lawyers and clients.<sup>67</sup> But the contractual

*Effect of Occupational Licensure on Black Occupational Attainment, in OCCUPATIONAL LICENSURE, supra note 1, at 165, Gellhorn, supra note 45, at 18, and Hansen, supra note 44, at 1219-20 (discussing the discriminatory effects of the bar exam requirement).*

62. See John S. Elson, *The Governmental Maintenance of the Privileges of Legal Academia: A Case Study in Classic Rent-Seeking and a Challenge to our Democratic Ideology*, 15 ST. JOHN'S J. LEGAL COMMENT 269 (2001); George B. Shepherd & William G. Shepherd, *Scholarly Restraints? ABA Accreditation and Legal Education*, 19 CARDOZO L. REV. 2091 (1998); George B. Shepherd, *No African-American Lawyers Allowed: The Inefficient Racism of the ABA's Accreditation of Law Schools*, 53 J. LEGAL EDUC. 103 (2003). For a discussion of the analogous effect of medical school accreditation, see RICHARD HARRISON SHRYOCK, *MEDICAL LICENSING IN AMERICA 1650-1965* (1967).

63. See FRIEDMAN, *supra* note 1, at 153, 156; YOUNG, *supra* note 41, at 78-79; Leef, *supra* note 22, at 25-26.

64. See FRIEDMAN, *supra* note 1, at 153.

65. See Sidney L. Carroll & Robert J. Gaston, *Occupational Restrictions and the Quality of Service Received: Some Evidence*, 47 S. ECON. J. 959 (1981).

66. See *supra* text accompanying notes 16-17.

67. See Jonathan R. Macey & Geoffrey P. Miller, *An Economic Analysis of Conflict*



characterization is misleading because licensed lawyers are subject to the disciplinary authority of the state in which they are licensed to practice, and to the rules of the tribunal where their conduct or its predominant effect occurred.<sup>68</sup> Ethical rules help support the price of legal services by maintaining lawyers' status as a learned profession rather than merely purveyors of a commodity.<sup>69</sup> Ethical rules constrain competition in several ways, including by preventing lawyers from working for non-lawyer owned firms,<sup>70</sup> and impeding protection of firms' investments in business development by restricting non-competition agreements.<sup>71</sup> Perhaps most importantly, uniform ethical rules constrain efficient forms of law firm organization, including multidisciplinary practice.<sup>72</sup>

### C. *The Politics of Licensing*

The politics of state licensing give reason to doubt that the social benefits of the system outweigh the costs. Winning interest groups typically are those who can most effectively organize to raise and spend political resources.<sup>73</sup> They tend to be relatively homogeneous groups that can cheaply and effectively constrain members from free-riding off of co-members' expenditures and efforts.<sup>74</sup> Lawyers would seem to fit this description, particularly because of their regular professional contacts and ability to utilize preexisting bar associations. They will, therefore, be able to out-lobby larger but more fragmented groups of consumers and business clients.<sup>75</sup>

*of Interest Regulation*, 82 IOWA L. REV. 965 (1997).

68. See MODEL RULES OF PROF'L CONDUCT R. 8.5 (2001) (amended 2003).

69. See POSNER, *supra* note 30, at 56; Ronald D. Rotunda, *Professionalism, Legal Advertising, and Free Speech in the Wake of Florida Bar v. Went For It, Inc.*, 49 ARK. L. REV. 703 (1997). Gillian K. Hadfield, *The Price of Law: How the Market for Lawyers Distorts the Justice System*, 98 MICH. L. REV. 953, 992 (2000), also notes how lawyers gain from the professional nature of law practice, but views this as resulting largely from the "natural" barrier of the scarce availability of the cognitive skills necessary to engage in complex legal reasoning rather than from lawyers' rent-seeking. Both effects may be at work.

70. See MODEL RULES OF PROF'L CONDUCT R. 5.4 (2003).

71. See *id.* R. 5.6. For a discussion of the professional self-interest basis of these rules, see Ribstein, *supra* note 19.

72. See Ribstein, *supra* note 19; Larry E. Ribstein, *Ethical Rules, Law Firm Structure and Choice of Law*, 69 U. CIN. L. REV. 1161 (2001); *infra* Part I.D.2.

73. See generally MANCUR OLSON, *THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS* (1971).

74. See generally ROBERT E. MCCORMICK & ROBERT D. TOLLISON, *POLITICIANS, LEGISLATION, AND THE ECONOMY: AN INQUIRY INTO THE INTEREST-GROUP THEORY OF GOVERNMENT* (1981); Robert D. Tollison, *Public Choice and Legislation*, 74 VA. L. REV. 339, 361-62 (1988).

75. For similar concerns about professional regulation generally, see FRIEDMAN,

Lawyers can promote licensing laws not only by lobbying to pass and enforce these laws, but also by directly participating in their enforcement. An influential study showed that unauthorized practice laws were enforced mostly by state bar unauthorized practice committees.<sup>76</sup> The bar thereby avoids having to get public prosecutors to take action in the face of public indifference to unauthorized practice.<sup>77</sup>

One might wonder whether lawyers gain on balance from licensing laws, since although they confer monopoly protection they also impose burdens on lawyers. The answer is that existing lawyers, who exert political pressure in favor of licensing, are “grandfathered” in under new licensing laws or increased requirements and therefore need not pay for any monopoly benefits the license confers.<sup>78</sup> Evidence that licensing standards rise with the supply of professionals<sup>79</sup> suggests that these standards are designed to help politically influential professionals protect their income from erosion by new entrants. It follows that licensing regulation will tend to persist irrespective of any social welfare benefits because existing practitioners, who have paid the costs of the license, would lose from deregulation.<sup>80</sup>

#### D. Alternatives to State Licensing of Law Practice

Complete evaluation of the state licensing system requires comparisons with other methods of regulating lawyers. The current system requires those who wish to perform certain types of services in a particular state to obtain a license from that state. The alternatives to state licensing discussed below are variations on these three features. Section 1 discusses certification as distinguished from mandatory licensing. Sections 2 and 3 discuss state regulation other than by the state in which the attorney practices. Section 4 discusses federal licensing. Section 5 discusses methods of attorney discipline other than licensing. The

---

*supra* note 1, at 143, and Gellhorn, *supra* note 45, at 16-17.

76. Deborah L. Rhode, *Policing the Professional Monopoly: A Constitutional and Empirical Analysis of Unauthorized Practice Prohibitions*, 34 STAN. L. REV. 1, 15-16 (1981).

77. *Id.* at 16.

78. See YOUNG, *supra* note 41, at 27.

79. See Alex Maurizi, *Occupational Licensing and the Public Interest*, 82 J. POL. ECON. 399 (1974) (showing that pass rates for professional examinations for various professions including law correlate with excess demand).

80. See YOUNG, *supra* note 41, at 27 (noting the “ratchet” and “escalator” effects of professional regulation that tend toward increasing and against decreasing regulation due to effects on existing practitioners); Barton, *supra* note 8, at 444; Curran, *supra* note 40, at 252; Leffler, *supra* note 22; B. Peter Pashigian, *Has Occupational Licensing Reduced Geographical Mobility and Raised Earnings?*, in OCCUPATIONAL LICENSURE, *supra* note 1, at 299; Wolfson et al., *supra* note 20.

availability of these plausible alternatives to the current system puts additional pressure on existing explanations for state licensing, and provides further need for an alternative explanation for such licensing, such as that offered in this Article.

### 1. Certification and Related Devices

Lawyers might be certified rather than licensed—that is, they could agree to comply with certain standards, but be permitted to perform the identical services without certification.<sup>81</sup> For the same reason that lawyers seek to allay clients' concerns about lawyer quality through licensing requirements, lawyers would have incentives to use nongovernmental bodies such as private associations to signal their quality to clients.<sup>82</sup> These associations could require members to conform to their rules, backed by the power to expel members or sue for fines.<sup>83</sup> Similarly, large law firms offer reputation bonds that secure the performance of their members.<sup>84</sup> Lawyers might be certified in particular specialties even if they are also licensed. In general, eliminating licensing requirements would permit practitioners to offer various levels of legal services

81. For comparisons between certification and licensing, see FRIEDMAN, *supra* note 1, at 144; YOUNG, *supra* note 41, at 18-19; Beales, *supra* note 60, at 133; Kleiner, *supra* note 1, at 192, 200; Leef, *supra* note 22, at 35-36.

82. See FRIEDMAN, *supra* note 1, at 146; Gellhorn, *supra* note 45, at 23; Leffler, *supra* note 22, at 290. Analogously, firms have been shown to subject themselves voluntarily to high-quality securities disclosure regimes in order to bond their disclosures. See John C. Coffee, Jr., *Racing Towards the Top?: The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance*, 102 COLUM. L. REV. 1757 (2002); Howell E. Jackson & Eric J. Pan, *Regulatory Competition in International Securities Markets: Evidence from Europe in 1999—Part I*, 56 BUS. LAW. 653, 691 (2001) (finding that the market demanded more securities disclosures than required by the minimum standards in E.U. directives, and noting that “market developments in European capital markets to date do not offer support to critics of regulatory competition who claim that the issuer choice proposals would prompt a race to the bottom in international securities regulation”); Larry E. Ribstein, *International Implications of Sarbanes-Oxley: Raising the Rent on US Law*, 3 J. CORP. L. STUD. 299 (2003); Edward B. Rock, *Coming to America? Venture Capital, Corporate Identity and U.S. Securities Law* (April 2002), in GLOBAL MARKETS, DOMESTIC INSTITUTIONS: CORPORATE LAW AND GOVERNANCE IN A NEW ERA OF CROSS-BORDER DEALS (Curtis J. Milhaupt ed., forthcoming 2003), available at <http://www.ssrn.com/abstractid=313419> (discussing Israeli firms' incorporation in Delaware).

83. See Paul V. Dunmore & Haim Falk, *Economic Competition Between Professional Bodies: The Case of Auditing*, 3 AM. L. & ECON. REV. 302 (2001) (showing that competition between professional auditing associations can effectively replace most government regulation of auditors).

84. See *infra* text accompanying notes 108-09.

at different prices<sup>85</sup> and enable competition between certified and uncertified lawyers.<sup>86</sup>

Many arguments for licensing do not adequately distinguish between licensing and certification. The relevant question is not whether there is an information asymmetry between clients and lawyers, but whether licensing, with all its costs, more efficiently addresses this asymmetry than certification. Private certifiers do not necessarily offer less protection than state regulators, who rarely use their powers to fine and jail noncomplying lawyers. Although consumers would have to evaluate certifiers, information about large law firms and certifying organizations is likely to be more cheaply available than that about individual lawyers.

One possible objection to relying on certification is that private alternatives to state licensing may not address social interests affected by law practice, such as service to the poor, the general community or the interests of justice. State laws emerge from a political process that arguably provides some accountability to non-lawyer interests. But non-lawyer groups have little clout in state licensing.<sup>87</sup> Conversely, private associations have an incentive to improve members' image through rules requiring public service as a condition of certification.

## 2. Alternative Rules for Selecting State Licensing Regime

Lawyers might be regulated under state law but, as with corporations, allowed to choose the applicable licensing and regulatory state without regard to where they reside.<sup>88</sup> This approach is similar to the private ordering model except that lawyers would be subject to some state enforcement mechanism and the choice would be among fifty-one regulatory bodies rather than a potentially much larger number of private organizations.<sup>89</sup>

85. See Beales, *supra* note 60, at 133; *supra* text accompanying note 64 (discussing the problem with licensing of forcing consumers to buy high-priced/high-quality legal services).

86. See FRIEDMAN, *supra* note 1, at 149.

87. See *supra* Part I.C.

88. This approach is discussed in more detail in Ribstein, *supra* note 72. See also Chesterfield Smith, *Time for a National Practice of Law Act*, 64 A.B.A. J. 557 (1978) (advocating a national practice system in which states fully recognize lawyers' admission in other states). A pure version of the choice of domicile approach that lets lawyers practice in any court under their chosen rules probably would be unworkable because a court needs to be able to apply a single set of rules to all those who appear before it. Accordingly, courts should be able to enforce their own rules of court administration.

89. State regulators could choose to defer in some respects to rules of local bar associations or lawyers and their clients contract for the licensing and ethical rules that apply to particular representations. Cf. Task Force on Conflicts of Interest, *Conflicts of*

There are three main differences between this “corporate” model of lawyer regulation and the current approach to determining the applicable regulatory regime.<sup>90</sup> First, it facilitates competition among regulatory regimes. If lawyers need not tie their choice of regulation to their place of practice, they can shop among all states for their preferred ethical rule. States would charge lawyers bar admission fees for using their regulation and the states with the regulations lawyers find most attractive would earn the most fees.

Second, the corporate model would facilitate adapting ethical rules to varying types of practice. Lawyers could choose, for example, an urban state’s rules suited to large firms, or a more rural state’s small-firm-type rules. Or states could cater to particular types of law practice, such as multidisciplinary or Internet-based.

Third, the corporate model allows each lawyer or firm to be governed by a single set of rules regardless of where they practice. This reduces lawyers’ costs of learning and complying with the rules if they practice in many states. Fourth, jurisdictional choice would facilitate state experimentation with various tradeoffs between more client protection and lower cost of legal services.

A variation on the corporate system would be permitting limited choice in particular circumstances. I have proposed letting multi-state law firms choose a single regulatory regime that governs all lawyers in the firm as to rules that have structural implications for law firms, including rules on who may own equity in the firm, non-competition agreements and members’ vicarious liability for the firm’s debts.<sup>91</sup> The costs of subjecting law firms’ lawyers to different structural rules in different states make applying some variation of a corporate-type rule necessary to sustain nonuniform professional regulation.<sup>92</sup>

A system that lets lawyers choose from among state licensing regimes may not be clearly more efficient than one in which lawyers can choose non-state regulators such as firms or private associations. Once the law permits *ex ante*

*Interest Issues*, 50 BUS. LAW. 1381, 1426 (1995) (suggesting that firms include choice of law clauses in engagement letters to deal with client conflict issues). This regime would make it harder for states to discipline lawyers and to design or apply rules as coherent bundles. As to the latter problem, see O’Hara & Ribstein, *From Politics to Efficiency*, *supra* note 5, at 1192-94. Also, clients might find it harder to analyze individual rules rather than simply making judgments about entire jurisdictions.

90. These differences between a conflict of laws regime in which states impose their rules based on physical location and a contractual choice regime in which parties choose the applicable law by contract at the time of the relevant conduct also exist in other contexts. For an application to the Internet, see Ribstein & Kobayashi, *State Regulation*, *supra* note 5.

91. See Ribstein, *supra* note 72.

92. The jurisdictional choice system proposed in Ribstein, *supra* note 72, can be reconciled with the present Article because it would mostly preserve individual lawyers’ incentives regarding investments in local state law.

choice, why limit the choice to state regulatory bodies? One reason is that clients face lower information costs in evaluating a limited number of state licensing regimes than a potentially much larger number of private associations. But perhaps for this reason only a few private organizations would emerge as prominent and have signaling value for lawyers. Accordingly, there may be little practical difference between the two regimes.

### 3. Permitting Practice Outside of Licensing State

A choice of state approach might preserve the basic outline of the current system of licensing lawyers in their principal state of practice but loosen the rules regarding practice outside the licensing state. The ABA and some states have clarified the legality of current practices of permitting practice outside the licensing state on a temporary basis, multi-state activities of in-house counsel, and admission on motion of lawyers who are in good standing and have practiced a certain number of years in another state.<sup>93</sup> Alternatively, the rules might permit lawyers licensed in a given state to practice anywhere else under a uniform registration system.

### 4. Federal Licensing and Regulation

General arguments for licensing do not relate to whether the states or the federal government will be doing the licensing. Congress can license lawyers through its power to regulate such areas as tax, bankruptcy, patent, antitrust and securities law.<sup>94</sup> Or Congress might broadly regulate law practice under its Commerce Clause power.<sup>95</sup> Federal courts have the power to license lawyers and to regulate at least some of their conduct.<sup>96</sup> In particular, federal regulation has

---

93. See MODEL RULES OF PROF'L CONDUCT R. 5.5 (2003); *MJP Commission, supra* note 2.

94. See *Sperry v. Florida*, 373 U.S. 379, 384-85 (1963) (holding that under Supremacy Clause federal and not state law controlled non-lawyers' right to practice before Patent Office).

95. For recommendations and predictions concerning federalizing regulation of the legal profession, see Stephen B. Burbank, *State Ethical Codes and Federal Practice: Emerging Conflicts and Suggestions for Reform*, 19 FORDHAM URB. L.J. 969, 974 (1992); Ted Schneyer, *Professional Discipline in 2050: A Look Back*, 60 FORDHAM L. REV. 125, 129 (1991) (foreseeing creation of a federal commission to regulate professional service providers); and Fred C. Zacharias, *Federalizing Legal Ethics*, 73 TEX. L. REV. 335 (1994).

96. See generally Fred C. Zacharias & Bruce A. Green, *Federal Court Authority to Regulate Lawyers: A Practice in Search of a Theory*, 56 VAND. L. REV. 1303 (2003) (discussing potential sources of and recent cases on federal court power to regulate lawyers).

been recommended as a way to resolve the controversy over multidisciplinary practice.<sup>97</sup> The federal regulation of securities lawyers is an important step toward federal licensing of lawyers.<sup>98</sup>

A federal licensing system has two potential advantages over a state system. First, lawyers exert significant control over state licensing. While lawyers probably also would influence federal licensing, national consumer and business groups may be better able to exert significant counter-pressure at that level. Second, the rise of interstate law practice<sup>99</sup> threatens the workability of a state-based system of lawyer regulation.

The federal government's role in lawyer regulation is not necessarily limited to licensing. Congress could enact minimum standards for lawyer licensing and let states regulate subject to those standards. Alternatively, lawyers' efforts to manipulate the supply and price of legal services through professional licensing and ethical rules could be addressed through antitrust laws.<sup>100</sup>

Federal regulation, however, is a dubious solution to problems with state licensing. First, because federal regulation empowers consumer and other interest groups instead of lawyers, it may just change the identity of the winners rather than producing more efficient results.<sup>101</sup> Second, federal regulation would substitute one-size-fits-all rules for variety among and competition between licensing and ethical regimes.<sup>102</sup> For example, states may vary as to whether they

97. See John S. Dzienkowski & Robert J. Peroni, *Multidisciplinary Practice and the American Legal Profession: A Market Approach to Regulating the Delivery of Legal Services in the Twenty-First Century*, 69 *FORDHAM L. REV.* 83, 150 n.356 (2000) (but noting that congressional action probably not feasible); James P. Holden, Written Remarks to the ABA Commission on Multidisciplinary Practice (Nov. 12, 1999), available at <http://www.abanet.org/cpr/holden.html>; see also Ted Schneyer, *Multidisciplinary Practice, Professional Regulation, and the Anti-Interference Principle in Legal Ethics*, 84 *MINN. L. REV.* 1469, 1477 n.37 (2000) (noting that "Congress could become a major player in the fight over MDP legalization").

98. See *infra* Part I.E.3.

99. See *infra* Part I.E.1.

100. See *infra* text accompanying note 129 (discussing federal antitrust concerns regarding state unauthorized practice enforcement).

101. See Wolfram, *supra* note 11, at 706-07. An indication of the political power of lawyers under federal licensing is the role the national bankruptcy bar has played in the expansion of bankruptcy law and blocking procedural bankruptcy reforms. See DAVID A. SKEEL, JR., *DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA* 86-100 (2001).

102. See H. Geoffrey Moulton, Jr., *Federalism and Choice of Law in the Regulation of Legal Ethics*, 82 *MINN. L. REV.* 73 (1997).

license lawyers at all.<sup>103</sup> Third, significant federal encroachment into a traditionally state-dominated area may not be politically feasible.<sup>104</sup>

Despite these problems, federal licensing might come to be seen as a plausible alternative if state regulators continue to refuse to accommodate the needs of modern law practice. Consumers and others may conclude that it is the only way both to regulate lawyers and to weaken the lawyer cartel. While lawyers might see federal regulation as the solution to the problems of state regulation of multi-state practice, it is important to assess the full consequences of abandoning state regulation, including the potential costs and benefits of giving lawyers a stake in the law of the licensing state.

## 5. Alternative Methods of Lawyer Discipline

The discussion so far has focused on regulation that attempts to screen out less qualified lawyers who would otherwise be able to compete for less informed consumers. This amounts to regulating the inputs that determine the quality of legal advice, including education and knowledge of the law. However, licensing provides little assurance of quality.<sup>105</sup> Accordingly, it may be better to dispense with licensing and regulate outputs to ensure lawyer quality, including through malpractice liability and disciplinary proceedings.<sup>106</sup> Also, the law could facilitate monitoring of lawyers' output by providing a readily accessible database of lawsuits or disciplinary proceedings. The existence of such alternatives casts further doubt on whether ensuring lawyer quality is a convincing justification for lawyer licensing.

### *E. Current Challenges to State-of-Practice Licensing*

Fundamental changes in the scope and nature of law practice increase the pressure to change or abandon the current system of state licensing of lawyers, and therefore the need for a new public interest rationale for this system. Section 1 discusses the increasingly interstate nature of law practice, including practice through multi-state law firms. Interstate law practice makes state-based law licensing more costly as well as politically suspect because lawmaking

---

103. This sort of variation is more defensible under the lawmaking-incentive argument presented in this Article than under a client-protection theory. *See infra* Part IV.D.

104. *See generally* Jonathan R. Macey, *Federal Deference to Local Regulators and the Economic Theory of Regulation: Toward a Public-Choice Explanation of Federalism*, 76 VA. L. REV. 265 (1990).

105. *See supra* Part I.B.1.

106. *See* YOUNG, *supra* note 41, at 18-19, 53; Barton, *supra* note 8, at 462.



jurisdictions do not internalize regulatory costs.<sup>107</sup> Section 2 discusses new technologies that blur the line between information and legal advice. Section 3 discusses perceived inadequacies of state regulation of lawyers that provide a public interest argument for federalizing licensing and regulation of lawyers. Section 4 discusses increasing judicial and federal regulatory scrutiny of enforcement of unauthorized practice laws, which may force regulators to clarify the scope of such laws and the policy basis of licensing lawyers.

### 1. Multi-State Law Practice

Law practice is becoming increasingly nationalized and internationalized. A licensing system designed when law practice was confined within state borders therefore seems anachronistic. In particular, the growth of multi-state law firms and in-house corporate legal practice causes significant strains in the current approach.

The growth of multi-state firms reflects both the increasing size and reach of firms' clients and the increasing recognition of the governance advantages of large law firms. Large law firms can provide client protection comparable to that provided by ethical rules. A law firm can back its members' promises of high-quality and honest performance by posting its reputation as a kind of bond that transcends the reputations of its individual members.<sup>108</sup> When law firms breach their implicit promises of performance, the market exacts a penalty scaled to the level of wrongdoing by devaluing the firm's reputation, and therefore reducing the price it can charge for its services.<sup>109</sup>

Reputation bonding has implications for law firms' structure and size.<sup>110</sup> The firm needs, among other things, a compensation mechanism that gives partners an incentive to develop the firm's goodwill and not just their own reputations. Non-competition clauses bind the partners to this sharing deal. Also, larger firms can offer larger reputation bonds. In order to grow to its optimal size, a law firm may need to leverage its reputation and expertise by spreading across regions, specialties and disciplines.

Given large firms' potential for reducing lawyer-client agency costs, lawyer regulation may be inefficient to the extent that it keeps these firms below their

---

107. In other words, the regulation involves "spillover" of regulatory costs on parties outside the state. See generally RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 699-700 (5th ed. 1998); Saul Levmore, *Interstate Exploitation and Judicial Intervention*, 69 VA. L. REV. 563, 568 (1983).

108. See *supra* note 31 and accompanying text.

109. See Daniel R. Fischel, *Multidisciplinary Practice*, 55 BUS. LAW. 951 (2000); Ribstein, *supra* note 19.

110. Ribstein, *supra* note 19.

optimal size.<sup>111</sup> The current approach to regulating lawyers based on where they practice promotes inefficient regulation of law firms. Since the lawyers based in each office of a multi-state firm are practicing law in that state,<sup>112</sup> they are subject to that state's licensing requirements and regulation. Thus, a multi-state firm's internal structure must comply with the rules of every state in which lawyers affiliated with the firm are based, including every state in which the firm has a branch or headquarters office.<sup>113</sup> For example, if some state ethical rules do not allow enforcement of strong non-competition clauses, a nationwide firm might have to choose between providing for the most efficient firm-wide incentive structure and maintaining a branch in the regulating state. This virtually compels uniformity of legal rules regarding law firm structure and inhibits evolution of and competition among these rules.<sup>114</sup>

Ethical restrictions on non-lawyer ownership of law firms<sup>115</sup> represent the most important constraint on law firm size and structure. Regulating law firm capital structure has important structural consequences.<sup>116</sup> Among other things, requiring all law firm owners to be lawyers makes law firms less hospitable for non-lawyers than if non-lawyers could share ownership and control.<sup>117</sup> Although law firms might affiliate with multidisciplinary offices in jurisdictions that allow them, this structure can entail significant costs. The firm may find it difficult to provide for the monitoring and incentives it needs to maintain its reputation bond where professionals in one state's office have no financial interest in another state's office. Moreover, it may be hard to determine what types of affiliations constitute sufficient integration to subject the firm's lawyers to rules against multidisciplinary practice in states where they are licensed.<sup>118</sup> Accordingly, to be safe, law firms must comply with the most restrictive state rules on multidisciplinary practice.

111. *Id.* at 1719-20.

112. *See supra* text accompanying note 11.

113. *See* ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 91-360 (1991). Indeed, a lawyer working for a multi-state firm may be subject to the rules of his licensing state even if he practices in a permissive state if his firm handles legal matters related to the licensing state. *See* Michigan State Bar, Standing Comm. on Prof'l and Judicial Ethics, Op. RI-225, 1995 WL 68958 (Feb. 1, 1995) (holding that a Michigan lawyer does not violate Michigan rules by having an ownership interest in a D.C. law firm that has non-lawyer partners permitted by D.C., but not Michigan, rules, *and* does not handle "Michigan legal matters"); Ribstein, *supra* note 72 (discussing regulation of multi-jurisdictional law firms).

114. Ribstein, *supra* note 72.

115. *See* MODEL RULES OF PROF'L CONDUCT R. 5.4 (2003).

116. *See generally* Ribstein, *supra* note 19; Ribstein, *supra* note 72.

117. *See* Ribstein, *supra* note 19, at 1725.

118. *See* Ribstein, *supra* note 72, at 1172-73.

The rise of multidisciplinary practice puts pressure on the state-based system for regulating lawyers. Although states can block entry of multidisciplinary firms under the current system, the status quo nevertheless might break down in the face of the developments described above. Clients may seek more efficient delivery of legal and other professional service, large U.S. law firms may face competition from accounting and European-based law firms, and even smaller boutique firms could gain by engaging in multidisciplinary practice.<sup>119</sup> With lawyers and clients clamoring for change, a stronger rationale must be found for the current system.

## 2. The Technological Threat to Traditional Law Practice

New technologies, particularly including computer software and the Internet, could fundamentally change the provision of legal advice. First, websites can convey large quantities of legal information directly to consumers. This reduces not only the need for legal advice, but also the information asymmetry between lawyer and client that provides the current rationale for state licensing.

Second, Internet services and computer software blur the line between information provision and legal advice. This is partly because of the potential for interactivity, where information is provided based on the user's particular need or question, just as in a traditional lawyer-client setting.<sup>120</sup>

These new technologies force more precise delineation of the activities that require a law license. They also challenge state-by-state licensing by permitting lawyers to interact with clients in states in which the lawyers are not licensed. Firms and individuals exploiting the new technologies may try to reduce legal impediments to lucrative business opportunities. Moreover, the fact that Internet law practice can provide effective legal assistance on routine matters to a low-income clientele makes opposition by the ABA politically unattractive. In general, these new business methods demand a clearer theory of the appropriate scope of regulation than is provided by the existing analytical framework.

---

119. See Fischel, *supra* note 109, at 972.

120. Examples of Internet-based document preparation services include <http://www.mylawyer.org/> (last visited Mar. 16, 2004) (promoting automated legal documents "powered by our easy-to-use Rapidocs software. . . . Our smart forms include complete and detailed instructions on how to create/use the documents and how to file them in court if necessary."); and <http://www.completecase.com> (last visited Mar. 16, 2004) (stating that "[o]ur simple and inexpensive process will enable you to complete your divorce documents from the comfort of your home, without incurring the cost of an attorney, or dealing with lengthy completion and delivery periods. . . . You will receive completed documents, explanations and instructions. The documents are customized to the state or province you live in, your children, your income, your assets and other factors in your case.").

### 3. Inadequacy of State Regulation of Lawyers

State licensing not only may impose extra burdens on law practice, but also may result in a suboptimal amount of regulation. Since lawyers essentially determine the substance and application of state licensing requirements and regulation,<sup>121</sup> licensing requirements are more likely to protect the lawyers' monopoly than to impose restrictions that reduce the profitability of law practice.

An important example of this phenomenon is imposing duties on corporate lawyers to report client fraud. While firms may be willing to pay lawyers to perform this reporting function in order to signal their honesty,<sup>122</sup> markets alone may not produce the socially optimal amount of reporting. Regulation that imposes this obligation on lawyers may reduce lawyers' profits if they cannot fully recoup costs by increasing prices. Lawyers therefore may resist imposing these obligations under state law, increasing political pressure to impose the obligations under federal law, where non-lawyer interest groups are more powerful.

This is, indeed, the way the issue of lawyers' reporting obligations played out in Enron and other recent corporate frauds. States had resisted imposing broad reporting obligations as recently as the 2000 revision of the ABA Model Rules.<sup>123</sup> The political pressure to do something about corporate fraud resulted in the imposition on securities lawyers of a broad federal reporting obligation.<sup>124</sup> This law could intensify debate on whether lawyers are more appropriately regulated at the federal or the state level, particularly in areas significantly affected by federal law.<sup>125</sup> The answer should depend on a full analysis of the justifications for state licensing and regulation of lawyers, including the lawyers-as-lawmakers explanation offered in this Article.

121. *See supra* Part I.C.

122. *See Painter, supra* note 35.

123. *See* MODEL RULES OF PROF'L CONDUCT R. 1.13 (2001) (amended 2003); Ethics 2000 Commission Revision to Model Rule of Professional Conduct 1.13, available at <http://www.abanet.org/cpr/e2k-rule113.html> (last visited Oct. 16, 2002).

124. *See* Sarbanes-Oxley Act of 2002, 15 U.S.C. § 7245 (Supp. 2003); 17 C.F.R. § 205.1-7 (2003) (SEC rules adopted under Section 307 providing, among other things, for attorney reporting obligations).

125. *See, e.g.,* John C. Coffee, Jr., *The Attorney as Gatekeeper: An Agenda for the SEC*, 103 COLUM. L. REV. 1293, 1316 (2003) (concluding that "private self-regulation of attorneys through bar associations means the continued government of the guild, by the guild, and for the guild. . . . SEC rules thus offer the best prospect for a relevant, precise response that avoids pointless disparity while clearly notifying securities attorneys that—like it or not—they are gatekeepers. To paraphrase Clemenceau, professions are too important to be left to the professionals.").

#### 4. Attack on Unauthorized Practice Laws

State licensing laws are enforced primarily through prosecutions under state unauthorized practice statutes.<sup>126</sup> The vague definition of the practice of law under these statutes potentially reaches many different types of information, including title searches, and filling in forms to obtain uncontested divorces, probate estates or enter bankruptcy, as well as books, software and websites containing discussions of law, legal forms or advice on particular legal issues.<sup>127</sup>

There are significant policy issues concerning the appropriate breadth of unauthorized practice laws, particularly where they bar performance of services that do not require skills learned in law school or tested on the bar exam. The justifications for prohibiting unlicensed practitioners from engaging in borderline law practice are particularly relevant in determining whether restricting such activities is contrary to the First Amendment or, to the extent done by professional associations, the antitrust laws.<sup>128</sup> Issues concerning the borderline practice of law are likely to intensify with the rise of the new technologies discussed above in Section 2. Indeed, the Federal Trade Commission and the Department of Justice recently expressed concern over bar prosecutions and the vagueness of unauthorized practice provisions.<sup>129</sup>

---

126. See Center For Prof'l Responsibility, American Bar Association, *1999 Survey of Unauthorized Practice of Law Committees* (1999), available at [http://www.abanet.org/cpr/model-def/model\\_def\\_statutes.pdf](http://www.abanet.org/cpr/model-def/model_def_statutes.pdf) (comprehensively summarizing these statutes).

127. See generally Rhode, *supra* note 76 (comprehensively analyzing the law and presenting data on unauthorized practice enforcement).

128. See *id.* at 53-55, 62-96 (analyzing First Amendment and antitrust issues).

129. See Letter from Federal Trade Commission and Department of Justice to Standing Committee on Unauthorized Practice of Law, State Bar of Georgia (Mar. 20, 2003), available at <http://www.ftc.gov/be/v030007.htm> (Re: Comments on Potential Unlicensed Practice of Law Opinion Regarding Real Estate Closing Activity); Letter from Federal Trade Commission and Department of Justice to Task Force on the Model Definition of the Practice of Law, American Bar Association (Dec. 20, 2002), available at <http://www.ftc.gov/opa/2002/12/lettertoaba.htm> (Re: Comments on the American Bar Association's Proposed Model Definition of the Practice of Law); Letter from Federal Trade Commission and Department of Justice to Ethics Committee, North Carolina State Bar (Dec. 14, 2001), available at <http://www.ftc.gov/be/v020006.htm> (Re: North Carolina State Bar Opinions, 2001-4 and 2001-8 Restricting Involvement of Non-Attorneys in Real Estate Closings and Refinancing Transactions). It is at least potentially significant that the current chair of the FTC, Timothy J. Muris, has expressed support for applying the antitrust laws to professionals. See Timothy J. Muris, *California Dental Association vs. Federal Trade Commission: The Revenge of Footnote 17*, 8 SUP. CT. ECON. REV. 265 (2000). McChesney & Muris, *supra* note 23, also presents evidence inconsistent with the efficiency of professional regulation, specifically of price advertising by lawyers.

## II. AN ALTERNATIVE ARGUMENT: LAWYERS AND STATE LAWMAKING

Based on the foregoing discussion, there would seem to be little reason to maintain the current system of state licensing of lawyers. Information asymmetries between lawyers and clients do not clearly justify lawyer regulation. Moreover, state licensing of lawyers seems an inappropriate way of responding to this problem, particularly compared with alternative solutions such as certification. Nor does lawyer licensing help ensure that lawyers will serve the public good. Indeed, lawyer licensing would seem to hurt the very people who most need protection—the poor and disadvantaged who cannot pay the highly trained lawyers the system requires. And even if some licensing system were justified, it is not clear that states, rather than the federal government, should administer this system, particularly given the increasingly interstate nature of law practice.

However, the existing theory misses a principal benefit of this system. Specifically, lawyer licensing, by giving lawyers exclusive rights to practice the law of a particular state, also gives them incentives to maintain the efficiency of the law of that state. In other words, what would seem to be the main drawback of lawyer licensing—that it restricts competition in the legal services market—emerges as an important argument for maintaining the system. This rationale justifies not only the basic concept of state licensing of lawyers, but also licensing requirements that demand qualifications beyond those needed to protect clients. To the extent that lawyers are expected to be lawmakers, they should be trained and screened to perform their lawmaking function.

Subpart A introduces the analysis by discussing the role lawyers actually play in state lawmaking. Subpart B discusses how lawyer licensing combines with other legal rules, including those governing choice of law, to give lawyers incentives to engage in lawmaking activities. Subpart C discusses alternative means of promoting lawyers' participation in lawmaking.

### *A. Evidence of Lawyers' Participation*

The lawmaking incentive argument for state licensing depends on whether lawyers can and do actually play a role in state lawmaking. It is important in this regard to distinguish between lawyers' roles as advocates or representatives of others and lawyers' work on their own behalf. Lawyers may be public servants in acting as legislators and judges. They also may act on behalf of specific clients as advocates, lobbyists and drafters of private codes.<sup>130</sup> The important

---

130. With respect to the latter activity, see *infra* Part II.C. For an analysis focusing on lawyers' participation in lawmaking as advocates in litigation, see Bruce H. Kobayashi and Larry E. Ribstein, *Class Action Lawyers as Lawmakers*, U. Ill. Public Law Research

incentives in these contexts are those of the public or clients, with the lawyers' personal interests mattering only in determining how well lawyers further their principals' objectives. By contrast, the important question for present purposes is lawyers' role as lawmakers on their own behalf, and how licensing affects this role.

Lawyers clearly see their individual, nonrepresentative participation in lawmaking as part of their self-identification as a profession. Lawyers' participation in furthering the rule of law has been cited as a justification for licensing lawyers<sup>131</sup> and for requiring lawyers to reside in the licensing state.<sup>132</sup> The Model Rules of Professional Conduct provide that lawyers should spend part of their time in "participation in activities for improving the law, the legal system or the legal profession."<sup>133</sup> Comment 8 to the Rule explains that this provision "recognizes the value of lawyers engaging in activities that improve the law, the legal system or the legal profession" and includes "legislative lobbying to improve the law, the legal system or the profession."

There is evidence that lawyers do spend substantial time in lawmaking activities.<sup>134</sup> Lawyers' role in writing Delaware corporate laws has been documented and discussed.<sup>135</sup> Moreover, an extensive study of the adoption of limited liability company laws demonstrated lawyers' major role in writing and

Paper No. 4-03 (Feb. 2004), available at [http://papers.ssm.com/sol3/papers.cfm?abstract\\_id=501548](http://papers.ssm.com/sol3/papers.cfm?abstract_id=501548).

131. See Barton, *supra* note 8, at 479-81; see also *MJP Commission*, *supra* note 2 (noting that state licensing helps maintain a locally active bar, but without specific reference to lawmaking activities).

132. Chief Justice Rehnquist cited lawyers' role in lawmaking as a justification for state residency requirements for lawyers notwithstanding the Privileges and Immunities Clause, U.S. CONST. art. IV, § 2. See *Supreme Court of N.H. v. Piper*, 470 U.S. 274, 290-94 (1985) (Rehnquist, C.J., dissenting). Justice Rehnquist said that a

State has a substantial interest in creating its own set of laws responsive to its own local interests, and it is reasonable for a State to decide that those people who have been trained to analyze law and policy are better equipped to write those state laws and adjudicate cases arising under them.

*Id.* at 292 (Rehnquist, C.J., dissenting). Since this Article's theory focuses on incentives to participate in lawmaking rather than the lawmakers' information, it does not directly provide an argument for residency requirements. Requiring residency may be a way of binding lawyers to particular states, but this also can be accomplished by the other barriers to multi-state bar membership discussed *infra* Part II.B.3.

133. MODEL RULES OF PROF'L CONDUCT R. 6.1(b)(3) (2003).

134. Given lawyers' direct participation in law reform discussed in the text, it follows that amounts spent by state bar associations for lobbying would not accurately reflect the extent of lawyers' role in lawmaking.

135. See S. Samuel Arsht, *A History of Delaware Corporation Law*, 1 DEL. J. CORP. L. 1, 17-21 (1976); Jonathan R. Macey & Geoffrey P. Miller, *Toward an Interest-Group Theory of Delaware Corporate Law*, 65 TEX. L. REV. 469 (1987).

promoting these statutes.<sup>136</sup> Discussing the history of adoption of such laws in forty-five of the fifty-one U.S. jurisdictions, the study showed that lawyers, acting on their own behalf, usually through their local state bar, appeared to be the major impetus for adoption in thirty-two of these jurisdictions, and significant participants in an additional six states.<sup>137</sup>

Lawyers, like other professionals, may be better able than nonprofessional groups to overcome collective action or free-rider problems inherent in political activity.<sup>138</sup> One way for a group to overcome collective action problems is by undertaking political activity as a byproduct of its other functions, thereby incurring no marginal cost for political organization.<sup>139</sup> This applies to professional associations, including bar associations, which are organized primarily to facilitate information exchange and networking among members.<sup>140</sup>

Lawyers, however, play a special role in the lawmaking process as compared with other interest groups, including business and accounting groups that also influence state business legislation.<sup>141</sup> First, lawyers already have expertise about the law that their rivals must acquire or hire in order to be able to lobby successfully.<sup>142</sup> Thus, lawyers need not rely on third parties to translate the issues they care about into specific laws and lawmaking strategies.

Second, lawyers have incentives to participate in law reform benefits beyond any advantages they might gain from enacting specific laws. Lawyers as a group acquire an aura of professionalism from these activities.<sup>143</sup> Individual

136. Carol R. Goforth, *The Rise of the Limited Liability Company: Evidence of a Race Between the States, but Heading Where?*, 45 SYRACUSE L. REV. 1193 (1995).

137. A possible problem with this example is that lawyers would have a special interest in LLC legislation that may not apply to other legislation—that is, an incentive to push a new form of limited liability entity for their own practices. On the other hand, it is arguably relevant that the LLC form can be used in all states by nonprofessional firms. Also, lawyers obtained only marginal advantages from LLC legislation, since they had access to other limited liability vehicles that afford lawyers the same liability protection. See generally ALAN R. BROMBERG & LARRY E. RIBSTEIN, BROMBERG AND RIBSTEIN ON LIMITED LIABILITY PARTNERSHIPS, THE REVISED UNIFORM PARTNERSHIP ACT AND THE UNIFORM LIMITED PARTNERSHIP ACT § 7.04 (2003); LARRY E. RIBSTEIN & ROBERT R. KEATINGE, RIBSTEIN AND KEATINGE ON LIMITED LIABILITY COMPANIES ch. 15 (2003). The point for present purposes is only to show that lawyers can play a substantial role in law reform, not that they will do so in all situations in which it is efficient. This broader issue is discussed below in Part II.C.

138. As to these problems, see *supra* text accompanying note 74.

139. See OLSON, *supra* note 73.

140. See Paul H. Rubin & Martin J. Bailey, *The Role of Lawyers in Changing the Law*, 23 J. LEGAL STUD. 807 (1994).

141. These groups played significant roles in the enactment of LLC statutes in several states. See Goforth, *supra* note 136.

142. See Macey & Miller, *supra* note 135, at 508-09.

143. See POSNER, *supra* note 30, at 56. This may explain the Model Rule discussed



lawyers can enhance their personal reputations for expertise by drafting legislative proposals and by advertising their efforts through such activities as continuing legal education lectures.<sup>144</sup>

Third, lawyers can influence their state's law other than by directly participating in lawmaking. For example, they can earn money and reputation benefits by writing forms, manuals, and treatises. These materials have been characterized as part of a "network" that increases the value of a state's law.<sup>145</sup>

Fourth, large law firms can help lawyers act collectively. These firms can allocate members' efforts to political and law-reform activities, and can internalize the reputation benefits of members' participation.<sup>146</sup> Lawyers who practice alone or in small firms may have less flexibility in allocating their time to activities that cannot be billed to specific clients.

### B. Lawyers' Incentive to Participate

This Subpart shows how licensing lawyers to practice in a particular state gives lawyers an incentive to participate in law reform by ensuring that the value inherent in a state's body of law will be shared by a particular group of practitioners. This puts the welfare effects of lawyer licensing discussed above in Part I in a different light. The barriers lawyer licensing places on entry and movement may increase social welfare as compared to a regime without licensing if lawyers contribute to the efficiency of state law. At the same time, data showing that lawyers gain from barriers to entry might reflect the value of the law of the licensing state. This theory therefore provides a potential argument in favor of lawyer licensing to the extent that lawyers have incentives to make state law more efficient.<sup>147</sup>

Section 1 provides an overview of the theory. The remainder of this Subpart discusses the conditions for the creation of lawyers' rights in state law and how these conditions relate to licensing and other laws. As discussed in Section 2, the law-creation argument supports requiring a license to practice at least some types of law. Section 3 shows how the law-creation argument further

*supra* text accompanying note 133.

144. Although these reputation benefits may not depend on lawyers' having a special interest in a particular state's law, they arguably enhance any incentives to work on a particular state's law that state licensing creates. See *infra* text accompanying note 154.

145. See Michael Klausner, *Corporations, Corporate Law, and Networks of Contracts*, 81 VA. L. REV. 757 (1995).

146. Firms will play this role only if they can protect the reputation capital they create in the process, as through enforceable non-competition agreements that encourage lawyers to contribute to the firm's reputation rather than their own client-building activities. See Ribstein, *supra* note 19; *supra* Part I.B.3.

147. Lawyers' incentives to favor efficient laws are discussed *infra* Part III.B.1.

implies that lawyers must be tied to courts and clients located in particular states by being required to obtain costly licenses to practice law in those states. Section 4 shows how lawyers' incentives depend on choice of law, jurisdiction and forum rules that tie application of a state's law to the enacting state's residents and courts.

### 1. An Overview of the Theory

Whether lawyers will invest resources in developing state law depends on the extent to which others will free-ride off these investments. Licensing gives lawyers a kind of property right in their state's law in the form of exclusive rights to represent clients in the licensing state and to practice in that state's courts.<sup>148</sup> Thus, to the extent that the quality of a state's law induces people to locate in a state and litigate in the state's courts, licensing helps lawyers capture these advantages to the exclusion of non-lawyers and out-of-state lawyers. A state's law therefore comprises part of the value of that state's law licenses. The monopoly profits that lawyers earn because of licensing are, in effect, the price consumers of law (i.e., clients) pay to lawyers for participating in lawmaking. These incentive effects are an important function of lawyer licensing apart from protecting individual clients or maintaining a lawyer cartel.<sup>149</sup>

This argument does not mean that lawyer licensing, to be efficient, must give lawyers perfect incentives to participate in lawmaking in the sense of eliminating free-riders. Rather, the argument is that lawyer licensing may be preferable to a system in which there are no barriers to the practice of law. To be sure, stricter barriers would increase lawyers' property rights in law. But the costs of more stringent lawyer licensing may outweigh its benefits in terms of incentives to produce law, particularly since lawyers have reputation and other

---

148. This property right in state law created by the license should be distinguished from the property right in the license itself. See *supra* note 20 and accompanying text. Lawyers' rights in law deal with the non-excludability aspect of the public good nature of law. Law would still have the public good quality of non-rivalrousness in the sense that the use of law by some does not reduce its value to others. These two aspects of public goods are distinguished in J.G. Head, *Public Goods and Public Policy*, 17 PUB. FIN. 197 (1962). With respect to general property rights of excludability, use and alienability, see Harold Demsetz, *Property Rights*, in 3 NEW PALGRAVE DICTIONARY, *supra* note 40, at 144-45. Law licenses differ from the standard definition of property because the licenses themselves (as distinguished from other components of firm goodwill) are inalienable. Inalienability may reduce lawyers' incentive to improve state law by reducing their ability to capitalize on the improvement. However, it is not critical to my analysis whether lawyers' exclusive rights in their state's laws are technically "property" rights or, as discussed in the text, provide perfect incentives.

149. See *supra* text accompanying note 1 (discussing cartel effects of lawyer licensing).

incentives to produce law even without protection from free-riders.<sup>150</sup> These costs include not only licensing's effect on the supply and mobility of lawyers,<sup>151</sup> but also the negative effects of restricting access to efficient laws.<sup>152</sup>

Licensing might seem to be unnecessary for incentive purposes because lawyers earn individual reputation benefits from participating in state lawmaking even if they do not share in the value of the law they create.<sup>153</sup> But licensing explains why lawyers would seek reputation benefits through state lawmaking efforts rather than from other activities. In the absence of exclusive benefits from the local state law, lawyers might seek to enhance their reputations by participating in uniform and federal lawmaking and engaging in forms of service other than participation in lawmaking.<sup>154</sup>

It is important to consider the lawmaking-incentive theory of lawyer licensing in the context of the overall welfare effects of lawyer licensing. Without licensing there would be more competition to provide advice about the law. This may reduce the price and increase the quality of legal advice, depending on the validity of the traditional consumer-protection arguments for licensing. While lawyer licensing may reduce the overall quality and increase overall price of *legal advice*, it also may increase the quality of *law*. This effect on the quality of law should be balanced against, or added to, the other effects of lawyer licensing.

## 2. Licensing the Practice of Law

Lawyers' incentive to participate in making the law of the state in which they practice depends on whether new entrants can free-ride off of lawyers' investment in lawmaking. Requiring a license to practice under a state's law helps serve this function by giving licensees exclusive rights to practice under a particular law, and thereby in effect permitting licensees to charge clients for use of this law. This includes licensing at least some types of trial and transactional work that involve applications of legal expertise. In other words, any law-creation benefits of law licensing would undercut arguments for deregulating law practice. It would also justify requiring a law license as

---

150. See *infra* text accompanying note 220.

151. See *supra* Part I.B.2.

152. This is analogous to the defense of incomplete protection by trade secret law. See David D. Friedman et al., *Some Economics of Trade Secret Law*, 5 J. ECON. PERSP. 61 (1991).

153. See *supra* text accompanying note 144.

154. This is subject to the qualification that state licensing may operate to deter investments lawyers otherwise would make in laws other than those of the licensing state. See *infra* text accompanying note 288.

distinguished from simply enabling practitioners to earn a certificate if they choose to do so.<sup>155</sup>

### 3. Tying Lawyers to States

Limiting free-riding off lawyers' investment in state law requires barriers not only to the practice of law generally, but also to the practice of law in a particular state. Although such licensing may not prevent all free-riding, in this case by other licensed lawyers in the state, it at least prevents free-riding by lawyers from other states.

Perhaps the most important barrier to entry to law practice in a state is the requirement to take a bar exam. The bar exam usually requires months of study and the risk of embarrassing failure.<sup>156</sup> That states pass a very high percentage of applicants if they take the exam enough times<sup>157</sup> suggests that the bar exam is more a price of admission than an effective screen. On the other hand, the bar exam probably deters some people from attempting to obtain a license. Only four jurisdictions pass fewer than sixty percent of those taking a particular test. These include Louisiana, where the low rate may reflect the state's idiosyncratic civil law system; the District of Columbia, which is unique in admitting lawyers on motion without prior experience elsewhere; and California, which uses its bar exam to screen graduates of unaccredited California schools.<sup>158</sup> The fourth state is Delaware, whose low passage rate may be particularly significant for present purposes. Since Delaware is the most prominent example of a state where lawyers have played an important role in maintaining the state's law, this provides some anecdotal evidence of the role of state licensing in encouraging lawyers' participation in lawmaking.

An additional entry barrier is rules that effectively discourage lawyers from obtaining and maintaining licenses in several states, including annual fees,

155. See *supra* Part I.D.1 (distinguishing licensing and certification systems); *infra* Part IV.B (discussing appropriate scope of licensing requirements under lawmaking-incentive theory).

156. See Kleiner, *supra* note 1, at 193.

157. See George M. Crow, *So You Passed the Bar. Big Deal*, THE RECORDER, May 1, 2000, at 4. The first-time pass rate has, however, been shrinking in recent years. See Deborah J. Merritt et al., *Raising the Bar: A Social Science Critique of Recent Increases to Passing Scores on the Bar Exam*, 69 U. CIN. L. REV. 929 (2001).

158. This affects California's granting of reciprocity to lawyers from other states, since admitting graduates of non-California schools who have not taken the California bar would discriminate against similarly situated graduates of California schools. A California task force recently studied the issue but declined to change the rule requiring lawyers to take the bar exam. See CALIFORNIA SUPREME COURT ADVISORY TASK FORCE ON MULTIJURISDICTIONAL PRACTICE, FINAL REPORT AND RECOMMENDATIONS 39 (Jan. 7, 2002), available at <http://www.courtinfo.ca.gov/reference/documents/finalmjprept.pdf>.

mandatory continuing legal education, examination requirements for licensed lawyers as well as new applicants, and requirements for maintaining an office in the licensing state.<sup>159</sup>

Bar admission buys at least two important privileges. First, lawyers may appear in the courts of the states in which they are licensed. This may be significant even if their clients reside elsewhere because clients may want to have the same lawyers or firms handle both their litigation and planning work in order to reduce search costs and realize economies of scope, particularly from sharing information among lawyers and across cases.

Second, a state license confers the exclusive right to practice on behalf of clients located in the state. Lawyers gain a competitive advantage from physical proximity to their clients. Even if lawyers can conduct some activities in a state without being licensed there, a license allows lawyers to meet regularly with clients under circumstances that clearly would constitute practicing law in that state.<sup>160</sup> A client would want to hire legal advisors and planners whose offices are near the firm's headquarters or other major location. A licensing requirement therefore protects lawyers from competition for transactional work by out-of-state lawyers.

The effect on lawyers' incentives of the privileges conferred by licensing is clarified by comparing the current system of lawyer regulation with the alternative approaches discussed above.<sup>161</sup> If legal advisors need not obtain any license to practice law, they would have to compete with everyone, regardless of location, who chooses to give legal advice. Anyone who sought to invest in a state's law therefore would face a world of free-riders. A federal licensing system would limit who could give legal advice but would not address free-riding on investments in the law of a particular state. Lawyers might invest in federal rather than state law, but would then face potential free-riding by the entire national bar.<sup>162</sup> Finally, under a system that lets lawyers contract for the applicable regulatory system irrespective of their place of practice, lawyers could represent clients and practice anywhere, regardless of whether they have invested

---

159. See *supra* text accompanying note 49. As to residency requirements, see Supreme Court of Va. v. Friedman, 487 U.S. 59, 68-70 (1988) (noting Virginia's requirement that lawyers admitted on motion maintain an office in the state as a reason why residency requirements were unnecessary to ensure a link between the state and its licensed lawyers).

160. See articles cited *supra* note 11.

161. See *supra* Part I.D.

162. The federal government could license legal specialties, which could then internalize the benefits of lawmaking efforts at the federal level. An important advantage of state licensing of specialties is facilitating variation in licensing requirements. See *infra* text accompanying notes 285.

in the state's law, thereby increasing potential free-riders and deterring investments in lawmaking.<sup>163</sup>

State variations may provide evidence supporting the law-creation argument. For example, one might expect to see higher barriers to enter a Sunbelt state where lawyers are seeking to retire or practice part of the year.<sup>164</sup> States' exclusion of "snowbirds" may have an efficiency rationale under the theory proposed in this Article. Retirees are likely to have higher discount rates than younger lawyers, and therefore are less likely to invest in development of a state's law that has long-term payoffs, and more likely to free-ride off of other lawyers' investments.

#### 4. Tying Practice of a State's Law to the Enacting State

Tying lawyers to particular states gives them an interest in the *courts* and *clients* of that state, but not necessarily in that state's *law* because any lawyer can advise on the law of any state. Indeed, as between the lawyer licensed to practice in state A and the lawyer in state B who has regular contact with a client who seeks advice under state A's law, the state B lawyer may be better able to get the client's business because the client values regular contact with the lawyer.<sup>165</sup> It seems to follow that a lawyer licensed in state B would have no more reason to invest in state B than in state A law. Thus, in order to create rights in law, a lawyer's license to practice in a particular state must give the lawyer preferred access to that state's law. This requires tying the law to the courts and clients of the enacting state.

This is done in several ways. First, judges applying modern approaches to choice of law tend to apply their own state's law.<sup>166</sup> Thus, while an Idaho lawyer can become expert in Delaware law, the lawyer still may have to litigate in Delaware courts, and therefore get admitted in Delaware or affiliate with a Delaware lawyer, to be able to count on litigating cases under Delaware law.<sup>167</sup>

163. However, this Article's justification for lawyer licensing does not necessarily depend on the absence of free-riding, but only on licensing's reducing free-riding enough to give lawyers some incentive to participate in lawmaking. See *supra* text accompanying note 150.

164. See Kleiner, *supra* note 1.

165. See Macey & Miller, *supra* note 135, at 493-94.

166. For studies showing pro-plaintiff, pro-resident and pro-forum biases see Patrick J. Borchers, *The Choice of Law Revolution: An Empirical Study*, 49 WASH. & LEE L. REV. 357 (1992), Michael E. Solimine, *An Economic and Empirical Analysis of Choice of Law*, 24 GA. L. REV. 49, 81-89 (1989), and Stuart E. Thiel, *Choice of Law and the Home-Court Advantage: Evidence*, 2 AM. L. & ECON. REV. 291 (2000).

167. The courts of Delaware (or some other state) may offer advantages regardless of which state's law they apply, such as speedy and expert resolution of cases. See Romano, *Law as Product*, *supra* note 6. However, this relates to the state government's

It follows that an Idaho lawyer might prefer that her clients choose to be governed by Idaho law, and therefore would have an incentive to invest in Idaho rather than in Delaware law.

Second, under the *forum non conveniens* doctrine, courts may refuse to hear cases that are more conveniently heard elsewhere, including because they require application of another state's law.<sup>168</sup> Judges might apply *forum non conveniens* because they hope that other courts will reciprocate, so the courts of each state retain control over that state's law, or because they gain little reward from the effort expended in deciding precedents under another state's law.<sup>169</sup>

Third, whether a state's law applies to a particular party depends to some extent on the party's contacts with the state. Default choice of law rules for contract actions look to the location of the parties and the relevant transaction.<sup>170</sup> If the parties contract for the application of a particular state's law, enforcement of that contract may depend on whether the chosen state has a "substantial relationship" to the parties or transaction or on the chosen state's "interest" in the issue.<sup>171</sup> Parties' contacts with the designated jurisdiction are a significant factor in enforcing choice of law clauses.<sup>172</sup> Thus, interstate companies can expect the

investments in the court system rather than lawyers' investments in the law.

168. See, e.g., *Rogers v. Guaranty Trust Co.*, 288 U.S. 123, 130 (1933). For a discussion of the relevance of *forum non conveniens* to Delaware lawyers' interest in Delaware law, see *Macey & Miller, supra* note 135, at 497-98. Note that the applicable law is only one factor considered in *forum non conveniens*. See *Koster v. Am. Lumbermens Mut. Cas. Co.*, 330 U.S. 518, 527-28 (1947); RUSSELL J. WEINTRAUB, COMMENTARY ON THE CONFLICT OF LAWS 262-78 (4th ed. 2001); 15 C. WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 3828 (2d ed. 1986).

169. For this reason, even if a court is willing to apply the law of another state, its opinions on that law may be less clear or elaborate than opinions on its own law.

170. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 188(2) (1971) (listing factors for determining law applicable to breach of contract, including place of contracting, negotiation, performance, subject matter, and location of the parties).

171. *Id.* § 187(2).

172. In a study of seven hundred cases involving application and enforcement of contractual choice of law clauses, in 429 of the 590 cases in which the clauses were enforced, one or both of the parties resided in the designated state, while in 143 cases the opinion did not clearly identify contacts with the designated state, and in only eighteen cases parties clearly did not reside in the designated state. See Ribstein, *From Efficiency to Politics, supra* note 5, at 376-77. Delaware Code Annotated 6 Section 18-109(d) (1999) seems explicitly to make litigation in the state's courts a condition of enforcement by authorizing limited liability company agreements that provide that a manager or member may consent to be subject to the *nonexclusive* jurisdiction of the courts of a specified jurisdiction or the *exclusive* jurisdiction of the Delaware courts. However, *Elf Atochem North America, Inc. v. Jaffari*, 727 A.2d 286 (Del. 1999), interpreted the statute as not precluding agreements vesting exclusive jurisdiction in a non-Delaware court. This holding in effect elevates Delaware's policy of enforcing contracts over its policy

law of their headquarters state to be particularly important. Moreover, a firm that seeks to avoid a particular state's law needs to avoid "minimum contacts" with that state that would suffice under the Due Process Clause to bring the firm into court there.<sup>173</sup> It follows that states with business-friendly laws will attract firms and that states with anti-business laws will repel them.<sup>174</sup> As discussed above, firms tied to particular states will tend to seek legal advice from lawyers who are licensed in those states. Thus, the advantage a law license confers in representing clients based in the licensing state depends on the attractiveness of that state's law. This gives lawyers an incentive to participate in lawmaking in the states in which they are licensed.

### C. A Direct Intellectual Property Approach

This Article characterizes lawyer licensing as a method of creating intellectual property rights in law. This raises the question whether a more direct approach of explicitly creating such property rights might be preferable.<sup>175</sup> Under such a direct approach, lawmakers would be given property rights in specific laws. This would eliminate the need to license lawyers in order to accomplish this result, with all of the market distortions licensing entails. The property rights might be given to the state itself, which could then license or hire law drafters, or to specific law writers, who could sell their creations to the state.

The legal problem with such property rights is that public law may not be entitled to federal copyright protection on the ground that the public is entitled to unimpeded access to law.<sup>176</sup> Although one may write a model code that is

---

of localizing jurisdiction.

173. See generally *Asahi Metal Industry Co. v Superior Court*, 480 U.S. 102 (1987); *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980); *Int'l Shoe Co. v. Washington*, 326 U.S. 310 (1945).

174. For discussions of this point in the context of pressures leading states toward efficiency, see Kobayashi & Ribstein, *Contract*, *supra* note 5, and Ribstein & Kobayashi, *State Regulation*, *supra* note 5. Note that the discussion in the text implies that there may be a tension between efficient choice of law rules and efficient lawyer licensing rules since, apart from lawyer licensing, there are strong arguments for enforcing contractual choice of law even without establishing a particular relationship with the chosen state. See generally Ribstein, *Choosing*, *supra* note 5.

175. For discussion of various ideas along these lines, see Michael Abramowicz, *Speeding up the Crawl to the Top*, 20 YALE J. ON REG. 139 (2003).

176. See *Veeck v. S. Bldg. Code Cong. Int'l*, 293 F.3d 791, 798-800 (5th Cir. 2002) (denying protection to building code adopted into law in violation of license); Irina Y. Dmitrieva, *State Ownership of Copyrights in Primary Law Materials*, 23 HASTINGS COMM. & ENT. L.J. 81 (2000).



protected under copyright law, the author lacks copyright protection in enacted law based on the code.<sup>177</sup>

Private lawmaking thus provides a way to encourage lawmaking efforts in the absence of formal property rights. Various groups contractually create the rules by which they are governed.<sup>178</sup> Private parties can create rules for such groups and obtain copyright protection for the rules without running afoul of the public access concerns that apply to public law. Strong legal rights might be replaced by competition among legal regimes.<sup>179</sup>

Private lawmaking cannot, however, completely replace public law. Rather, it exists only in certain circumstances in which private groups can internalize lawmaking costs. The rest of society's legal needs must be satisfied by government-supplied laws, as to which the need for public access is likely to continue to preclude creation of intellectual property rights. In this setting, state licensing of lawyers may be the best way to encourage lawmaking efforts.

---

177. See *Veeck*, 293 F.3d at 800. But see *Practice Mgmt. Info. Corp. v. Am. Med. Ass'n*, 121 F.3d 516 (9th Cir. 1997) (holding that codes that identified medical procedures produced by the American Medical Association had intellectual property protection despite adoption by a federal agency). A possible compromise that accommodates public access would be to grant a broad fair use privilege but protect laws from copying by commercial interests or other jurisdictions that seek to use the laws to encourage use of their courts and lawyers. Due process concerns are satisfied by giving those who choose to be subject to the innovating state's law full access to that law.

178. See generally Lisa Bernstein, *Opting out of the Legal System: Extralegal Contractual Relations in the Diamond Industry*, 21 J. LEGAL STUD. 115 (1992) (describing private remedies in a merchant's association); Gillian K. Hadfield, *Privatizing Commercial Law: Lessons from the Middle and the Digital Ages*, Stanford Law School, John M. Olin Program in Law and Economics, Working Paper No. 195 (March 2000), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=220252](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=220252) (discussing private merchants' remedies); David R. Johnson & David Post, *Law and Borders—The Rise of Law in Cyberspace*, 48 STAN. L. REV. 1367, 1380, 1383, 1390-91 (1996) (discussing private remedies as a way of resolving Internet disputes); David V. Snyder, *Private Lawmaking*, 64 OHIO ST. L.J. 371 (2003) (discussing broad range of private lawmaking and comparisons with public lawmaking).

179. These alternatives to law might also address the standard public interest arguments for lawyer licensing by eliminating the need to rely on legal experts. See Hadfield, *supra* note 69 (discussing problems in connection with law's excessive complexity). There are, however, important benefits to formal law, including a developed network of case law and forms, and the ability to offer a coherent set of complex terms. See generally Larry E. Ribstein, *Statutory Forms for Closely Held Firms: Theories and Evidence from LLCs*, 73 WASH. U. L.Q. 369 (1995). Even without such law, alternative dispute resolution systems might call for participation of lawyers or those with skills comparable to lawyers, and therefore might raise policy issues similar to those relating to professional licensing.

### III. THE STATE COMPETITION DEBATE

Lawyers' role in lawmaking is most significant in the context of the state competition debate. Although this debate has centered on corporate law, and specifically the success of Delaware corporate law, it raises issues that relate broadly to state law. This Part shows that many of the arguments commentators have made for the proposition that state competition leads to inefficient outcomes do not fully take account of lawyers' role in this competition. Subpart A discusses commentators' arguments for imperfections in jurisdictional competition, focusing on corporate law. Subpart B discusses the likely impact of lawyers and lawyer licensing on the efficiency of state law.

#### A. *The Efficiency of Jurisdictional Competition*

State law can be viewed as a kind of "product" that state legislatures manufacture and that competes in a market for laws.<sup>180</sup> Analogously to other product markets, there are potential benefits from competing state laws as compared with uniform state laws or federal laws. This is especially clear regarding corporate law, where firms' ability freely to choose the applicable state law by selecting the state of organization seems to encourage competition.

The debate concerns whether state competition is likely to lead to efficient outcomes. State competition may not operate efficiently where litigants cannot easily exit a particular state's law, as where they are sued in a court that applies unfavorable local law.

State competition regarding corporate law is particularly controversial. Some commentators argue that the corporate law competition is a "race to the bottom" because managers disregard shareholder interests in choosing the incorporation state.<sup>181</sup> Others argue that corporate law is a "race to the top" because capital markets discipline managers' jurisdictional choice,<sup>182</sup> and there

180. See Romano, *Law as a Product*, *supra* note 6.

181. See William L. Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663 (1974). For more recent commentary consistent with this view, see Lucian Arye Bebchuk & Allen Ferrell, *Federalism and Corporate Law: The Race to Protect Managers from Takeovers*, 99 COLUM. L. REV. 1168 (1999), and Lucian Arye Bebchuk, *Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 HARV. L. REV. 1435 (1992).

182. See Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977). For other commentary consistent with this view, see FRANK H. EASTERBROOK & DANIEL R. FISCHEL, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* (1991), Daniel R. Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law*, 76 NW. U. L. REV. 913 (1982), and Romano, *Law as a Product*, *supra* note 6.

is evidence supporting this view.<sup>183</sup> Specifically, Delaware has been said to have won the competition by offering advantages other states cannot readily duplicate, including a sophisticated bar and judiciary, well-developed case law, a convenient location and ability to credibly commit to continuing to supply high-quality law.<sup>184</sup>

More recent theories of state law inefficiency attempt to show how, despite market competition and efficient pricing of state laws in capital markets, a state such as Delaware can retain its dominance in corporate law while preventing the emergence of the optimal legal rules that would prevail in a perfectly competitive market. These theories do not, like the “race to the bottom” theory, assert that the winner of the state competition is the worst law, but only that the winner is not as efficient as the law that would emerge under better competitive conditions.

These theories come in several varieties, some of which focus on the demand for law, while others focus on the supply. First, it has been argued that other states cannot readily duplicate Delaware’s “network” advantages, thereby “locking in” Delaware law as against the emergence of more efficient legal standards.<sup>185</sup> This “network externalities” theory is based on the idea that buyers

---

183. See Peter Dodd & Richard Leftwich, *The Market for Corporate Charters: “Unhealthy Competition” Versus Federal Regulation*, 53 J. BUS. 259 (1980); Roberta Romano, *The Need for Competition in International Securities Regulation*, 2 THEORETICAL INQUIRIES IN L. 387, 495-97 (2001) (reviewing eight studies finding positive abnormal stock returns from changing incorporation state); Romano, *Law as a Product*, *supra* note 6. This evidence has been challenged, primarily on the ground that it does not take adequate account of the fact that reincorporations are not random events, so that their effects may be determined by the characteristics of particular corporations and transactions. See Lucian Bebchuk et al., *Does the Evidence Favor State Competition in Corporate Law?*, 90 CAL. L. REV. 1775, 1784-85 (2002). There is also evidence that Delaware firms had higher Tobin’s Q’s than non-Delaware firms in a study covering the period 1981-1996. See Robert Daines, *Does Delaware Law Improve Firm Value?*, 62 J. FIN. ECON. 559 (2001). This is obviously significant given Delaware’s victory in the charter competition. However, a later recent study casts doubt on the extent and implications of this “Delaware effect.” See Guhan Subramanian, *The Disappearing Delaware Effect*, 20 J.L. ECON. & ORG. (forthcoming 2004) (finding that the effect disappears during the post 1996 period, possibly because of changes in Delaware takeover law and in managerial compensation that offset any Delaware law takeover law advantage).

184. See Romano, *Law as a Product*, *supra* note 6.

185. See Klausner, *supra* note 145. For other discussions of the network externalities and related theories in the context of business associations, see Lucian Arye Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127 (1999), Marcel Kahan & Michael Klausner, *Antitakeover Provisions in Bonds: Bondholder Protection or Management Entrenchment?*, 40 UCLA L. REV. 931 (1993), Marcel Kahan & Michael Klausner, *Path Dependence in Corporate Contracting: Increasing Returns, Herd Behavior and Cognitive Biases*, 74 WASH. U. L.Q. 347 (1996), Marcel Kahan & Michael Klausner,

or users add value to a product.<sup>186</sup> In the case of business associations, as more firms join the network of users, more cases are decided interpreting ambiguous terms in similar contracts, common practices such as investment banker fairness opinions emerge, legal services become standardized and therefore less costly, and books and continuing legal education materials explain contractual terms, all reducing errors of ambiguity, inconsistency and incompleteness in contract terms.<sup>187</sup> Also, widespread use of corporate terms helps capital markets value corporate terms. These benefits might be viewed as “externalities” because new users do not consider benefits they would confer on other users when adopting the product or standard. Thus, firms may continue to use Delaware law even if this law is less efficient than that of other states because the firms do not internalize the network benefits from adopting that other law. States may concede the most lucrative portion of the market to Delaware and follow a relatively passive strategy of adopting the Model Business Corporation Act, which provides sophisticated drafting and a network of case law that enables states other than Delaware to retain the incorporation business of small and medium-sized firms. Variations on this network externalities theory are that Delaware’s legal indeterminacy enables it to increase network effects and thereby to hold onto its dominant position,<sup>188</sup> and that it uses its market power to

---

*Standardization and Innovation in Corporate Contracting (or “The Economics of Boilerplate”)*, 83 VA. L. REV. 713 (1997), Brett H. McDonnell, *Getting Stuck Between Bottom and Top: State Competition for Corporate Charters in the Presence of Network Effects*, 31 HOFSTRA L. REV. 681 (2003), and Tara J. Wortman, Note, *Unlocking Lock-In: Limited Liability Companies and the Key to Underutilization of Close Corporation Statutes*, 70 N.Y.U. L. REV. 1362 (1995). For criticisms of this application of network externalities theory, see Clayton P. Gillette, *Lock-in Effects in Law and Norms*, 78 B.U. L. REV. 813 (1998), Mark A. Lemley & David McGowan, *Legal Implications of Network Economic Effects*, 86 CAL. L. REV. 479, 562-86 (1998), and Larry E. Ribstein & Bruce H. Kobayashi, *Choice of Form and Network Externalities*, 43 WM. & MARY L. REV. 79 (2001) (presenting evidence contrary to the operation of network externalities in the development of business associations laws).

186. See Paul A. David, *Clio and the Economics of QWERTY*, 75 AM. ECON. REV. 332 (1985). For criticisms of the network externalities theory, see S. J. Liebowitz & Stephen E. Margolis, *The Fable of the Keys*, 33 J.L. & ECON. 1 (1990), and S. J. Liebowitz & Stephen E. Margolis, *Network Externality: An Uncommon Tragedy*, 8 J. ECON. PERSP. 133 (1994).

187. See Charles J. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interactions Between Express and Implied Contract Terms*, 73 CAL. L. REV. 261, 286-89 (1985) (discussing the role of these errors in the tradeoffs between express and implied terms).

188. See Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 COLUM. L. REV. 1908 (1998).

charge firms franchise taxes and litigation costs according to the benefits firms gain from using Delaware's law.<sup>189</sup>

A second "demand-side" explanation of state law inefficiency is that, because managers rather than shareholders initiate re-incorporations, state competition may not weed out laws that favor managers.<sup>190</sup> This argument resembles the traditional "race to the bottom" story, except that the argument is that Delaware wins not because it is the worst but rather because it is the least bad. Specifically, Delaware may compete to provide the best law in some respects, but not for provisions such as anti-takeover rules that attract management-initiated re-incorporations by redistributing corporate wealth from shareholders to managers. This theory attempts to reconcile its inefficiency story with evidence of positive stock price effects from re-incorporations.<sup>191</sup> There is also evidence that firms are attracted to or do not avoid states other than Delaware that have apparently pro-management provisions.<sup>192</sup> Although the agency problem on which this theory is based is specific to business associations, it is analogous to any contractual relationship in which one party seems to have leverage in choosing the applicable law, including franchiser and franchisee, and lender and borrower.

A third type of state law inefficiency theory focuses on parties' incentives to supply law rather than on the demand for such law. Legislators seemingly do not gain enough from making their state's law competitive to justify engaging proactively in law reform,<sup>193</sup> particularly since other jurisdictions can copy successful innovations.<sup>194</sup> Although the state's residents may gain from the state's being a leader in the competition, their gains probably are not large enough to overcome the significant costs they would incur in organizing to secure such gains.<sup>195</sup> Accordingly, they may prefer simply to exit to a state with better law. This is particularly the case for state competition outside of Delaware

189. See Marcel Kahan & Ehud Kamar, *Price Discrimination in the Market for Corporate Law*, 86 CORNELL L. REV. 1205 (2001).

190. Lucian Arye Bebchuk, *Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 HARV. L. REV. 1435 (1992).

191. See *supra* note 183 and accompanying text.

192. See Lucian Bebchuk et al., *Does the Evidence Favor State Competition in Corporate Law?*, 90 CAL. L. REV. 1775 (2002).

193. See Douglas J. Cumming & Jeffrey G. MacIntosh, *The Role of Interjurisdictional Competition in Shaping Canadian Corporate Law*, 20 INT'L REV. L. & ECON. 141, 144-46 (2000).

194. See Susan Rose-Ackerman, *Risk Taking and Reelection: Does Federalism Promote Innovation?*, 9 J. LEGAL STUD. 593 (1980).

195. By contrast, particular taxpayer groups may be able effectively to organize to oppose state regulation that drives industry away. See Kobayashi & Ribstein, *Contract*, *supra* note 5.

and not involving publicly held corporations, where incentives to compete for franchise fees are less obvious.<sup>196</sup>

It is unclear that state competition is flawed for any of the reasons discussed above.<sup>197</sup> For example, with respect to the argument that Delaware corporate law is entrenched against competition even from more efficient state laws, there is evidence that states other than Delaware respond defensively to changes in Delaware law, that these responses are positively related to franchise revenue, and that nationwide competition for corporate law is reflected in the interstate pattern of adoptions of corporate statutory innovations<sup>198</sup> and revisions to the Model Business Corporation Act.<sup>199</sup> Moreover, there is a basic theoretical question why contracts and markets cannot deal with the problem. For example, the parties in the corporate setting could contract to permit shareholders rather than managers to initiate a re-incorporation.<sup>200</sup> The evidence that corporations tend to gravitate toward anti-takeover states<sup>201</sup> does not necessarily establish the inefficiency of state competition. Instead, in the absence of direct evidence of inefficient competition, firms' choice of these states could indicate that the suspect provisions, or the overall statutes in which they are included, are wealth-maximizing. The main importance of this evidence therefore may be to show that states other than Delaware *are* competing in the charter market both to retain and proactively to capture incorporations.

The state competition debate has focused on publicly held corporations. Competition might differ in the market for unincorporated firms on the theory that Delaware does not dominate this market to the same extent as it does the market for publicly held firms.<sup>202</sup> Smaller firms' costs of operating outside the

196. See *supra* text accompanying note 6 (discussing Delaware's franchise fee incentive).

197. For an exhaustive rebuttal to arguments concerning imperfections in state corporate law competition, see Romano, *supra* note 183.

198. See *id.*

199. See William J. Carney, *The Production of Corporate Law*, 71 S. CAL. L. REV. 715 (1998).

200. It has been argued that firms should be permitted to opt into a federal takeover regime, and required to allow shareholders rather than managers to exercise the opt-in right. See Bebchuk & Ferrell, *supra* note 181. This proposal assumes that federal lawmakers have incentives to adopt socially optimal laws that state lawmakers lack. The proposed mandatory opt-in procedure lets shareholders avoid managers' exclusive right to initiate re-incorporations. For criticism of this proposal, see Stephen J. Choi & Andrew T. Guzman, *Choice and Federal Intervention in Corporate Law*, 87 VA. L. REV. 961 (2001). For a rebuttal, see Lucian Arye Bebchuk & Allen Ferrell, *Federal Intervention to Enhance Shareholder Choice*, 87 VA. L. REV. 993 (2001).

201. See Bebchuk, *supra* note 190.

202. Note that Delaware is second only to California in LLC formations. See Kobayashi & Ribstein, *supra* note 185 (presenting state-by-state data on organization of unincorporated firms). This indicates that Delaware may be competing for

formation state and paying foreign corporation fees may be high relative to total capitalization.<sup>203</sup> Also, the lower fees these firms generate would seem to translate into weaker state incentives to compete. On the other hand, these firms also are more mobile than corporations in terms of the low decision-making costs of changing their state of organization in response to inefficient legal rules. There is evidence of welfare-enhancing competition regarding the law of closely held firms.<sup>204</sup>

State competition for corporate law, as well as for other law, may work better than inefficiency theories would predict because these theories overlook lawyers' role in promoting state competition.<sup>205</sup> For reasons discussed above in this Subpart and more fully below,<sup>206</sup> lawyers can internalize the benefits of creating new networks of legal materials and of innovations even if new members of the network and legislators cannot. This responds to the "supply-side" problems discussed above.<sup>207</sup> Lawyers' interests in efficient law, discussed in the next Subpart, also may offset the power of other groups, such as managers, who pay less attention to overall efficiency.<sup>208</sup> Lawyers' role in state competition may explain data showing that states other than Delaware retain a significant percentage of companies located in the state, and even proactively compete for some out-of-state incorporation business, despite the lack of a Delaware-type franchise fee incentive.<sup>209</sup> This data is consistent with lawyers' efforts to make

unincorporated firms just as it does for corporations.

203. See Bebhuk, *supra* note 190 (showing evidence that larger firms are more likely than smaller firms to incorporate outside home state); Roberta Romano, *State Competition for Close Corporation Charters: A Commentary*, 70 WASH. U. L.Q. 409, 413 (1992) (arguing that there is relatively little competition for such firms because the transaction cost benefits of closely held firm statutes are relatively low).

204. See Ribstein, *supra* note 179, at 392-94; see also Goforth, *supra* note 136 (showing evidence of competition regarding LLC laws); Bruce H. Kobayashi & Larry E. Ribstein, *Evolution and Spontaneous Uniformity: Evidence from the Evolution of the Limited Liability Company*, 34 ECON. INQUIRY 464 (1996) (showing evidence of evolution of state statutes toward efficient level of uniformity).

205. For an examination of lawyers' role in non-corporate state competition, see Ribstein, *supra* note 7.

206. See *infra* text accompanying note 220.

207. See *supra* text accompanying notes 193-200. Lawyers' incentives in this regard would seem to be stronger than those of Congress to legislate regarding takeovers, the approach suggested by Bebhuk & Ferrell, *supra* note 200, at 1002. This conclusion is supported by Congress's spotty record regarding takeover legislation. See Romano, *supra* note 183, at 537-38.

208. See *infra* text accompanying note 231.

209. See Bebhuk, *supra* note 190. Bebhuk argues that states lack incentives to promulgate optimal law. Even if that is the case, the point in the text is the more limited one that state competition may be more efficient given lawyer licensing than it would be in the absence of such licensing.

their state's corporation law a viable choice. Also, firms may choose to locate and incorporate in particular states in order to maximize the chance that courts will apply that state's *non-corporate* law.<sup>210</sup> This, in turn, may be attributable to lawyers' efforts to maintain the law of the states in which they are licensed, as explained more fully below.<sup>211</sup>

### B. Effect of Lawyers' Influence

This Subpart considers the question whether lawyers' participation in lawmaking is likely to result in laws that are more, or less, efficient than would be the case with less lawyer involvement. It shows that lawyers' effects on state law depend on the incentives of both lawyers and of contracting parties. Even if lawyers want to use the law to extract benefits from clients, state competition may constrain them from doing so.

In evaluating lawyers' incentives, it is important to consider the alternatives and to avoid the Nirvana fallacy. If lawyers do not exercise influence, other interest groups may take their place. These groups may be more likely than lawyers to promote inefficient wealth transfers.<sup>212</sup> Also, lawyers' incentives might differ in the absence of state licensing.<sup>213</sup> Accordingly, enhancing lawyers' incentives to participate in state lawmaking might lead to more efficient laws than if lawyers do not have these incentives. Thus, even if lawyers can extract private gains from their state's laws, society still might be better off than if lawyers had less influence.

Sections 1 and 2 discuss the costs and benefits of lawyers' participation in lawmaking. Section 3 summarizes the general factors concerning state lawmaking and competition that help determine whether lawyers will make state law more, or less, efficient.

#### 1. Benefits of Lawyer Participation

Lawyers may play a beneficial role in state competition by solving "supply-side" problems that critics of state law have discussed.<sup>214</sup> First, lawyers may have an incentive that legislators lack to update their state's law in order to

210. See *supra* notes 5, 170-71 and accompanying text; *infra* note 238 and accompanying text.

211. See *infra* Part II.B.

212. An example is the effect of non-lawyer interest groups in diluting statutory enforcement of contractual choice of law in states other than Delaware. See *infra* text accompanying note 252.

213. See *supra* note 101 (noting the role of the national bankruptcy bar in lobbying for bankruptcy law as an indication of lawyers' incentives under federal licensing).

214. See *supra* text accompanying note 205.



attract clients from and avoid losing clients to lawyers in competing states. Lawyers can enhance their reputations by participating in state lawmaking. Indeed, other states' copying of lawyer-sponsored innovations may bring lawyers more public recognition,<sup>215</sup> in contrast to the potential erosion of benefits to originating states or legislators resulting from this spread.<sup>216</sup> Lawyers' gains, unlike those of legislators, do not depend on an interest group's being able to overcome organizational costs to lobby them. Moreover, unlike legislators, lawyers' gains are not offset by any potential loss of support of competing interest groups.

Second, lawyers may have incentives to resist changes in their state laws that cause one-time wealth-transfers, even if these transfers generate short-term increases in legal business.<sup>217</sup> Lawyers would hesitate to hurt their state's reputation as a favorable place to do business by sponsoring wealth-transferring law changes. This theory most clearly applies to Delaware corporate law where circumstances such as the small size of the state and its reliance on franchise taxes enable Delaware to post a kind of "bond" securing the maintenance of efficient corporate law.<sup>218</sup> But other states also have incentives to establish themselves as magnets for commercial transactions and litigation. This may affect the law of a commercial center like New York, which contracting parties frequently designate as the governing law.<sup>219</sup>

Third, lawyers can earn royalties, attract clients, and increase their reputations by supplying ancillary legal materials that increase the benefits of using a state's law. These include continuing legal education lectures and materials, treatises, legal forms, and law review articles. Since lawyers gain reputation and other benefits from producing these materials regardless of how many clients use their state's law, lawyers can help overcome supposed network externalities problems inherent in business association law.<sup>220</sup>

Fourth, lawyers may provide expertise that attracts clients to the state and its laws. For example, the state's lawyers might commit substantial resources to specializing in representing particular types of clients, such as high-tech companies. This commitment may, in effect, bond the bar to maintain the law relating to the needs of those industries.

215. Lawyers' reputations may be harmed by working on ill-conceived innovations. But this risk may do no more than offset lawyers' incentives to promote excessive innovation in order to generate additional legal fees.

216. See *supra* text accompanying note 194.

217. See Larry E. Ribstein, *Changing Statutory Forms*, 1 J. SMALL & EMERGING BUS. L. 11 (1997) (discussing the tradeoff between change and stability).

218. See Romano, *Law as a Product*, *supra* note 6.

219. See Ribstein, *From Efficiency to Politics*, *supra* note 5, at 433 n.301 (showing data indicating New York's prominence as a state that is contractually selected to supply the applicable law).

220. See *supra* text accompanying note 185.

## 2. Costs of Lawyer Participation

Lawyers' participation in lawmaking will not necessarily lead to more efficient laws because lawyers have incentives to seek legal rules that inefficiently increase the demand for lawyers.<sup>221</sup> Thus, it has been argued that Delaware lawyers seek to make Delaware law excessively lawyer-friendly.<sup>222</sup>

Lawyers use their influence to adversely affect the law in several ways. First, lawyers may seek rules that increase the need for and cost of litigation,<sup>223</sup> including fact-intensive standards that judges must apply in specific cases.<sup>224</sup>

Second, lawyers may advocate rules that increase the cost of or need for legal advice.<sup>225</sup> Most directly, lawyers may favor unauthorized practice laws requiring the use of lawyers for tasks that may not require extensive legal training, such as no-fault divorces and real estate work.<sup>226</sup> Also, laws that render certain types of agreements or terms unenforceable or impose formalities as a condition of enforceability may deter business people from writing agreements without legal assistance.

Third, lawyers may benefit from frequent changes in laws that force parties to seek legal advice in connection with rewriting their agreements to conform to the new law.<sup>227</sup>

Fourth, lawyers may seek to sponsor inefficient laws in order to attract litigants to the courts in which they are licensed. Lawyers thereby may be

221. See, e.g., Rubin & Bailey, *supra* note 140. Since licensing laws constrain the supply of lawyers, see *supra* Part I.B.2, increasing the demand for legal services would increase lawyers' income, other things being equal.

222. See Macey & Miller, *supra* note 135.

223. See Fischel, *supra* note 109, at 969 n.57; Macey & Miller, *supra* note 135, at 504.

224. See Kahan & Kamar, *supra* note 189 (noting these and other factors that increase Delaware corporate litigation).

225. It has been argued that government-supplied law is inherently complex and costly, and arguably disadvantages low-income clients with small transactions. See Hadfield, *supra* note 69. The point is that, even given a particular amount of government-supplied law, increasing lawyers' role might cause law to be more complex and costly than it otherwise would be.

226. See *supra* Part I.C. These laws, in turn, may be opposed by powerful non-lawyer groups that also seek this business. See Lueck et al., *supra* note 57, at 80. For a discussion of the appropriate scope of unauthorized practice laws under the lawyers-as-lawmakers model, see *infra* Part IV.B.

227. See Ribstein, *supra* note 217 (discussing the need to balance the benefits of legal evolution against the costs of change). However, these incentives are counterbalanced by other incentives that favor stability. Lawyers may want to ensure the stability of their state's law in order to attract clients. See *supra* text accompanying note 217. They may also be concerned about the increasing risk of malpractice liability for not keeping abreast of changing law.

serving their states' as well as their own interests even if they are reducing overall social welfare. By contrast, in the three situations discussed above, lawyers may be serving their own interests at the expense not only of social welfare, but also of their own states to the extent that pro-lawyer rules make the states less desirable places to live and do business. Lawyers' objective in advocating such rules is to extract enough gains from those who remain to compensate for the loss of business from those who leave.

Lawyers' direct influence on legal rules differs from their influence as clients' agents. Lawyers may, for example, exploit their relationships with corporate managers to encourage firms to incorporate in states where lawyers are licensed or that are otherwise favorable to the lawyers whether or not they serve the interests of firms or their managers.<sup>228</sup> But it does not necessarily follow that lawyers perversely influence state law in their role as lawmakers. Instead, lawyers may try to improve their states' laws when they cannot easily induce firms to make bad choices.

In any event, the theory that lawyers act as perverse agents in the incorporation decision is questionable for several reasons. First, incorporation choices are reviewed by in-house counsel whose interests are strongly aligned with those of their firms. Second, lawyers in multi-state law firms may not care in which of the states a client chooses to incorporate, at least to the extent that the lawyers' and law firms' interests are aligned.<sup>229</sup> These law firms, in turn, handle many of the large transactions in which firms contractually designate the applicable state law.<sup>230</sup> Third, any lawyer self-interest in promoting choice of law may simply offset the self-interest of other corporate agents. For example, corporate lawyers may favor takeovers that would leave them representing the acquired company, thereby balancing managers' interests in anti-takeover laws.<sup>231</sup>

---

228. See Bebchuk, *supra* note 192, at 1790-91; cf. John C. Coates IV, *Explaining Variation in Takeover Defenses*, 89 CAL. L. REV. 1301 (2001) (showing that the identity and location of law firms representing companies affect the anti-takeover charter provisions these companies choose in going public).

229. The individual lawyer may care to the extent that a client's incorporation decision determines which of the firm's offices will service the client. But, for example, a lawyer in the non-Delaware office of a multi-state firm may lose less from the client's decision to incorporate in Delaware, where the firm also has an office, than would a lawyer based outside of Delaware in a firm that does not have a Delaware office. Similar considerations apply to advising clients on the contractual choice of non-corporate law.

230. See *infra* text accompanying note 241.

231. See Romano, *supra* note 183, at 534.

### 3. The Effect of Jurisdictional Competition and Type of Practice

Jurisdictional competition determines whether lawyers can benefit from promoting inefficient laws without causing clients to seek coverage of less lawyer-friendly law or extralegal dispute resolution.<sup>232</sup> Whether law is excessively lawyer-friendly therefore depends on whether it is insulated from the effects of state competition.

Lawyers' ability to attract litigation business to their home jurisdictions through their lawmaking efforts depends significantly on the rules for determining the applicable law. Parties' ability to effectively contract for the applicable law and forum is likely to maximize the joint welfare of contracting parties.<sup>233</sup> Even in consumer settings, where selling firms may seem to have an advantage over buyers, markets arguably constrain firms from using one-sided choice of law and choice of forum clauses.<sup>234</sup> It follows that, to the extent such legal rules apply, lawyers could attract litigants to their forum only by drafting and promoting efficient laws rather than those that favor any particular party or group. On the other hand, to the extent that plaintiffs can decide where to sue at the time of litigation and the courts do not enforce choice of law and choice of forum clauses, as in many tort cases, lawyers have an incentive to secure plaintiff-friendly laws to maximize litigation in their jurisdictions. These laws are often inefficient because they take account only of the interests of one party to the suit.

These general observations suggest that the following factors, among others, determine whether lawyers will have incentives to advocate efficient laws:

---

232. *See id.* at 525-26 (noting that "Delaware's commanding position in the charter market no doubt may enable the corporate bar to siphon off a share of Delaware's rents by fashioning a legal regime that increases its income at the expense of share value. But the trade-off will not reach the point at which a firm will be indifferent to staying in Delaware or changing domicile."). Romano also notes, *id.* at 526, that lawyers do not gain abnormal returns because of competition in the market for legal services, citing Rosen, *supra* note 52, consistent with data showing that lawyers' income is attributable to the value of their human capital. *See supra* note 57 and accompanying text. However, Delaware lawyers might gain from adoption of pro-lawyer rules because licensing laws constrain competition to provide the additional services these rules require.

233. *See O'Hara & Ribstein, From Politics to Efficiency, supra* note 5. The effectiveness of the choice of law clause can be enhanced by a choice of forum clause because courts are likely to apply local law. *See Kobayashi & Ribstein, Contract, supra* note 5.

234. *See Kobayashi & Ribstein, Contract, supra* note 5; O'Hara and Ribstein, *From Politics to Efficiency, supra* note 5; Ribstein, *Choosing, supra* note 5.

1. Lawyers' gains from enacting lawyer-friendly rules may depend on whether the rule enables the lawyer to extract significant profits from each client that outweigh losses caused by clients leaving the lawyers' jurisdiction to avoid the rule. Thus, litigation-promoting rules may help trial lawyers but hurt transactional lawyers.
2. Tort litigators may have an incentive to favor inefficient plaintiff tort laws in their home jurisdictions because defendants cannot easily avoid being sued in pro-plaintiff states.<sup>235</sup>
3. Trial lawyers who specialize in contract disputes have an incentive to favor efficient laws in their home jurisdictions because, to the extent that courts enforce contractual choice of law, they can increase local litigation only if the parties agree in advance of a dispute to be governed by local law and to have the dispute decided in the local court.
4. Transactional lawyers have an incentive to increase the efficiency of their state's law in order to encourage potential clients to locate in their states. Location in a state exposes a firm to the jurisdiction of local courts, which in turn are likely to apply local law,<sup>236</sup> and makes application of that state's law more likely even in other states' courts under conflict of laws rules.<sup>237</sup> Even incorporating in a jurisdiction may enhance the likelihood that courts will enforce the choice of the law of that jurisdiction.<sup>238</sup> Although firms that benefit from wealth transfers might gain from locating in a state with inefficient laws, this effect is likely to be offset by causing wealth-transferors to avoid the state. Moreover, since firms cannot easily determine the effects of many commercial and business laws at the time of making their location decisions, they would tend to locate in states based on the state's reputation for overall efficiency and stability of their laws rather than on the wealth-transferring effects of specific laws.
5. Lawyers specializing in some types of law practice may have incentives to promote inefficient laws in their home states. For

---

235. Tort defense lawyers might also gain from more litigation rather than from defendant-favoring laws. Thus, their incentives may be similar to those of plaintiffs' lawyers, although they may be less tied to a particular jurisdiction.

236. See *supra* note 166 and accompanying text. For discussions of the effect of location decisions as an offset to plaintiff forum-shopping, see Kobayashi & Ribstein, *Contract*, *supra* note 5, and Ribstein & Kobayashi, *State Regulation*, *supra* note 5.

237. See *supra* text accompanying notes 170-71.

238. For cases holding that the place of incorporation was a significant factor in enforcing contractual choice of law, see *Nedlloyd Lines B.V. v. Superior Ct.*, 834 P.2d 1148, 1153 (Cal. 1992), *Guardian Sav. & Loan Ass'n v. MD Assocs.*, 75 Cal. Rptr. 2d 151, 156 (Cal. Ct. App. 1998), and *Al Baraka Bancorp (Chicago), Inc. v. Hilweh*, 656 A.2d 197, 200 (Vt. 1994). *But see* *Curtis 1000, Inc. v. Suess*, 24 F.3d 941, 948-49 (7th Cir. 1994).

example, divorce lawyers may have an incentive to lobby for laws that force people to use lawyers in divorces because this may be the only way the lawyers can retain business, even if some people leave the jurisdiction to get cheaper divorces.<sup>239</sup>

6. Large law firms' incentives regarding state law may differ from those of smaller firms. Large firms' clients are likely to be relatively large companies that need the sort of diverse services only large law firms can provide.<sup>240</sup> These clients, in turn, are relatively likely to employ contractual choice of law clauses<sup>241</sup> and to consider the choice of law ramifications of location decisions. Thus, lawyers in large law firms have an incentive to make their state's law attractive to parties that choose law by contract, rather than *ex post* at the time of litigation.<sup>242</sup> By contrast, smaller firms' clients are more likely to be local and not particularly sensitive to choice of law, or tort plaintiffs who seek advantage from choosing the law and forum at the time of suit.

The efficiency of lawyers' involvement in lawmaking may not, however, depend as much on the nature of their practice as the above categories suggest. Lawyers' political influence depends on their ability to subordinate their individual interests to those of lawyers as a whole. Thus, lawyer lobbying may depend on the overall balance of lawyers' interests rather than reflecting the differing interests of various subgroups of lawyers. Moreover, since lawyers share earnings through firms, lawyers in firms that engage in a range of transactional and litigation work have an incentive to promote the overall efficiency of state law rather than the interests of any department of the firm.<sup>243</sup> In short, transactional lawyers' overall interest in efficient laws may determine lawyers' lobbying goals.

On the other hand, lawyers' overall interest may be in reducing competition among legal systems and increasing uniformity and harmonization of law. This may explain lawyers' support for uniform laws in the U.S. and the opposition of

---

239. See *supra* Part I.E.3; *infra* Part IV.B (discussing unauthorized practice laws).

240. See Ribstein, *supra* note 19, at 1716.

241. See Ribstein, *Choosing*, *supra* note 5, at 288 (noting that, since choice of law clauses generally are included in elaborate form contracts, they are cost-justified mainly if used on a large scale by big national firms).

242. Lawyers in multi-state law firms also may have less parochial incentives when advising clients in that they have less of an interest in their clients' choosing the law of a particular state, at least to the extent that the interests of the individual lawyers in the firm are aligned with those of the firm. See *supra* text accompanying note 228.

243. This suggests that a move toward larger law firms may have implications for the efficiency of state law.

many lawyers to Delaware-type jurisdictional competition in Europe.<sup>244</sup> To the extent that lawyers' gain from the types of inefficient rules discussed in Section 2 is constrained by jurisdictional competition, lawyers may use their political power to restrict jurisdictional competition and thereby to loosen market constraints on their self-interested conduct.

Lawyers' incentives regarding jurisdictional competition may depend on the extent to which they stand to gain clients from more competition even as competition limits lawyers' ability to extract gains from each client. Lawyers may gain if the states in which they practice are net winners in interstate competition. Lawyers' choice of states in which to practice may depend on where they need to live. Also, licensing laws themselves constrain lawyer mobility.<sup>245</sup> Lawyers who must or want to live in states that could be expected to lose from free competition might favor uniform laws.

#### 4. Type of Law

The efficiency of lawyers' influence on law may vary not only from one type of lawyer or firm to another but also from one type of law to another. This may have significant policy implications for lawyer licensing. For example, because firms in effect contract for the application of business association statutes in advance of any dispute, the analysis in Section 3 predicts that lawyers' involvement in this type of lawmaking will produce more efficient laws. Prior studies have examined state-by-state adoption of corporate innovations in the Model Business Corporation Act<sup>246</sup> and of limited liability company statutes.<sup>247</sup> LLC statutes remove barriers to limited liability that add planning and litigation costs with little corresponding benefit.<sup>248</sup> There is, in fact, significant evidence that lawyers pushed for changes in and adoption of the statutes.<sup>249</sup> This provides at least anecdotal support for the efficiency of lawyers' lawmaking efforts.

244. The implications of this Article's analysis for other federal systems, including Europe, are discussed *infra* Part III.C.

245. See *supra* Part I.B.2.

246. See Carney, *supra* note 199.

247. See Larry E. Ribstein & Bruce H. Kobayashi, *Uniform Laws, Model Laws and Limited Liability Companies*, 66 COLO. L. REV. 947 (1995).

248. See Ribstein, *supra* note 179; Larry E. Ribstein, *The Deregulation of Limited Liability and the Death of Partnership*, 70 WASH. U. L.Q. 417 (1992).

249. See *supra* note 136 and accompanying text. It would be interesting to see if states where lawyers have the most influence in lawmaking are those that reacted most quickly to this development. Note that lawyers may have pushed for these laws not simply to help their clients or improve the law, but also for the more selfish benefit of widening the scope of limited liability for their own firms. See *supra* note 137. This may imply that lawyers would not be so proactive with respect to laws that did not affect lawyers in this way.

Another example of efficient lawmaking is statutes providing for enforcement of contractual choice of law clauses.<sup>250</sup> These statutes arguably are efficient because they enhance parties' ability to select the law when transacting rather than when litigating, thereby helping to ensure that the applicable law will maximize the welfare of all contracting parties.<sup>251</sup> Comparing the versions of these statutes adopted in Delaware, where lawyers seem to have significant influence,<sup>252</sup> with those adopted in states where lawyers are less influential, provides some anecdotal evidence of the efficiency of lawyers' role in state lawmaking.

Conversely, lawyers' impact on the efficiency of state law may appear from a positive or negative correlation between states' adoptions of inefficient statutes and lawyers' power in each state. For example, there is evidence that statutes that impose constraints on franchise contracts reduce social welfare.<sup>253</sup> Transactional lawyers could be expected to oppose these statutes because they deter potential franchiser clients from locating in enacting states.<sup>254</sup> This suggests that a state's failure to adopt such a statute might be partly attributable to lawyers' opposition. More directly, it may be possible to measure lawyers' impact by examining states' overall regulatory environments.

Differences among types of laws might appear not only in states' tendency to enact them, but also in their tendency to enact uniform versions of the laws. A state's willingness to adopt a uniform law proposal may reflect the state's lawyers' reluctance to invest in customized drafting or their inability to promote a customized law. This, in turn, may be attributable to the lawyers' lack of political power or incentives to invest in lawmaking. On the other hand, a state's tendency to adopt uniform law proposals may not clearly test the efficiency of lawyers' involvement because uniformity is efficient in some circumstances and inefficient in others. In particular, the benefits of uniformity are relatively low for laws relating to long-term contracts because parties can solve most problems of state-to-state variation by contracting for the application of a particular law. Uniformity's benefits in this situation therefore probably do not outweigh its costs in terms of reduced variation and competition.<sup>255</sup> Although states have tended toward uniformity where it is efficient, they have not clearly avoided uniformity as to rules for long-term-contracts where uniformity is least

---

250. See generally Ribstein, *supra* note 7 (discussing these statutes).

251. See *supra* text accompanying note 233.

252. See Macey & Miller, *supra* note 135.

253. See James A. Brickley et al., *The Economic Effects of Franchise Termination Laws*, 34 J.L. & ECON. 101, 115-16 (1991); Richard L. Smith II, *Franchise Regulation: An Economic Analysis of State Restrictions on Automobile Distribution*, 25 J.L. & ECON. 125 (1982).

254. See Ribstein & Kobayashi, *Contract*, *supra* note 5.

255. See Larry E. Ribstein & Bruce H. Kobayashi, *An Economic Analysis of Uniform State Laws*, 25 J. LEGAL STUD. 131 (1996).



efficient.<sup>256</sup> The states that have moved toward inefficient uniformity may be those in which lawyers are weakest.

States also vary widely in the extent to which they copy the uniform law proposals promulgated by the National Conference of Commissioners on Uniform State Laws. Some states adopt proposals in name, but only after making significant variations. A state's enactment of a modified version of a uniform law may indicate active lawyer involvement rather than passivity. Moreover, a state's decision to modify a uniform provision may or may not be efficient. For example, uniformity may be efficient in provisions concerning third-party creditors, such as restrictions on dividends, because firms cannot effectively contract for the application of a particular provision without their creditors' consent. On the other hand, uniformity is less efficient with respect to provisions applying solely between the firm's owners because customized contracting is practicable in this context.<sup>257</sup> Variations in the degree of adoption of a given proposal across the states might correlate with lawyers' role in lawmaking, although many variables regarding different types of laws may be significant.

The above discussion suggests that one can test the nature of lawyers' influence on law by observing both the types of laws a jurisdiction enacts and lawyers' power in that state. However, it may be difficult to determine the precise extent of lawyers' political power. Neither the number of lawyers in a state,<sup>258</sup> nor the amount lawyers spend on lobbying,<sup>259</sup> is likely accurately to measure lawyers' power. Indeed, large relative numbers of lawyers might negatively correlate with lawyers' political power because it indicates that the lawyers have been unable effectively to control entry into the profession. More promising tests, therefore, would reflect factors that relate to lawyers' political coordination costs. For example, lawyers in a state dominated by a few large law firms may be more politically powerful than in one consisting of many sole practitioners or small firms. Also, the heterogeneity of law practice may be important. A mix of tort, business and other types of lawyers may be less effective in enacting a particular legislative program than a bar dominated by corporate or tort lawyers. This could account for differences in the law between, say, Delaware, where the corporate bar is strong, and Mississippi, where the tort lawyers appear to be strong.

---

256. *See id.*

257. *See Kobayashi & Ribstein, supra* note 204.

258. *See supra* text accompanying notes 73-75 (discussing the role of coordination costs).

259. *See supra* note 134 (noting the significance of lawyers' direct participation in lobbying).

### C. Implications for Federalism

This Article sheds possible light on the allocation of political power between federal and state governments. Given a U.S.-style federal system, licensing lawyers encourages their participation in state lawmaking by reducing free-riding on their lawmaking efforts. This implies that, given lawyers and lawyer licensing, a U.S.-style federal system, or allocating more power to the states within such a system, may be more efficient than a unitary system or a strong federal government.<sup>260</sup> By analogy to this Article's argument for lawyer licensing, the costs of impeding nation-wide competition by having fifty-one legal systems may be outweighed by the incentives a federal system creates to enact better laws.

A variation on this argument is that the quality of competition among the states in a federal system may depend on lawyers' incentives to participate in lawmaking. For example, lawyers may have less influence on lawmaking in Europe than in the U.S. Also, significant legal, cultural and language differences between regimes inherently limit lawyers' practice outside their home jurisdictions. If European lawyers get little business from outside their home countries, they may have an incentive to oppose all jurisdictional competition and favor harmonization of laws rather than to accept competition and make their jurisdictions more competitive.<sup>261</sup> Also, the advent of multinational law firms may change European lawyers' incentives regarding jurisdictional competition since law firms can compete for international business even if individual lawyers cannot.<sup>262</sup>

## IV. THE NATURE AND SCOPE OF LICENSING REQUIREMENTS

This Part discusses implications of the lawmaking-incentive theory for the nature and scope of licensing requirements and for licensing of professions other than law. Subpart A discusses how this Article's theory bears on what should

---

260. This is analogous to one commentator's argument that federalism promotes social relationships that allow citizens to overcome collective action problems. See Jason Mazzone, *The Social Capital Argument for Federalism*, 11 S. CAL. INTERDISC. L.J. 27 (2001).

261. The absence of a history of jurisdictional competition in Europe may have affected the structure of legal institutions and lawyers' incentives. All this may change in the wake of *Case C-212/97, Centros Ltd. v. Erhvervs-og Selskabsstyrelsen*, 1999 E.C.R. I-1459, [1999] 2 C.M.L.R. 551 (1999), which applied the law of the incorporating jurisdiction, and therefore introduces an important predicate of U.S.-style jurisdictional competition. For a discussion of implications of *Centros* for European business association law, see Larry E. Ribstein, *The Evolving Partnership*, 26 J. CORP. L. 819 (2001).

262. I am indebted to Klaus Heine for this point.

be required in order to obtain a license. Subpart B deals with the definition of law practice for purposes of determining what constitutes unauthorized practice of law. Subpart C outlines an alternative approach to addressing the free-rider problem—licensing specialists rather than, or in addition to, state-by-state. Subpart D discusses the potential for state variation and competition in licensing requirements. Subpart E discusses this Article’s implications for state licensing of professions other than law.

### A. Licensing Requirements

The lawmaking-incentive argument for lawyer licensing may provide a basis for determining the requirements for obtaining a law license. If licensing is solely a way to ensure lawyer quality, it is not clear that three years of broad law school training in law and policy, or even a college degree, should be required for a license. Law schools do not teach the skills that are important to representing many clients,<sup>263</sup> while teaching skills that are irrelevant to what most lawyers do.

On the other hand, to the extent that licensing is justified as a way to encourage lawyers to participate in lawmaking, lawyers should be broadly trained in the legal system and public policy rather than just having the skills that matter to the specific work they choose to do.<sup>264</sup> This responds to the argument that law school accreditation requirements are excessively costly because they over-train lawyers for some tasks.<sup>265</sup>

### B. Defining Law Practice

Statutes enforce lawyer licensing requirements by imposing sanctions for the unauthorized practice of law.<sup>266</sup> The definitions in the statutes and developed

263. See Leef, *supra* note 22, at 35.

264. At the same time, if law school teaches skills that do not matter to most clients, this would suggest that law school should not be the exclusive requirement—that is, that there should be no “diploma privilege.” The bar exam may serve the purpose of ensuring that lawyers have the requisite basic legal knowledge.

265. See Elson, *supra* note 62.

266. For a summary of these provisions as of 1999, see Center for Professional Responsibility, American Bar Association, *1999 Survey of Unauthorized Practice of Law Committees* (1999), available at [http://www.abanet.org/cpr/model-def/model\\_def\\_statutes.pdf](http://www.abanet.org/cpr/model-def/model_def_statutes.pdf). For analyses of the law and policy of unauthorized practice of law, see Anthony Bertelli, *Should Social Workers Engage in the Unauthorized Practice of Law?*, 8 B.U. PUB. INT. L.J. 15 (1998), Barlow F. Christensen, *The Unauthorized Practice of Law: Do Good Fences Really Make Good Neighbors—Or Even Good Sense?*, 2 AM. B. FOUND. RES. J. 159 (1980), Derek A. Denckla, *Nonlawyers and the Unauthorized Practice of Law: An Overview of the Legal and Ethical Parameters*, 67 FORDHAM L. REV. 2581

in the cases are open-ended and circular.<sup>267</sup> In applying these definitions, courts have considered what lawyers customarily do, what requires legal skill, and what involves complexity.<sup>268</sup> The courts have characterized as unauthorized practice providing and filling in legal forms in ways that require discretion and legal knowledge.<sup>269</sup> Writing self-help books or drafting do-it-yourself legal kits is not

(1999), Paul D. Healey, *Pro Se Users, Reference Liability, and the Unauthorized Practice of Law: Twenty-Five Selected Readings*, 94 LAW LIBR. J. 133 (2002), and Rhode, *supra* note 76.

267. See Rhode, *supra* note 76, at 45-46.

268. See Bertelli, *supra* note 266, at 57; Rhode, *supra* note 76, at 81-83.

269. See, e.g., Colo. Bar Ass'n v. Miles, 557 P.2d 1202, 1203 (Colo. 1976) (enjoining "do-it-yourself" divorce businesses from services beyond those performed by scrivener or public stenographer, including preparation of pleadings, confidential consultations or appointments, and advising that obtaining a marriage dissolution can usually be done without a lawyer); Statewide Grievance Comm. v. Patton, 683 A.2d 1359, 1360 (Conn. 1996) (enjoining "Doc U Prep" service that completed forms for uncontested legal actions); Grievance Comm. of Bar v. Dacey, 222 A.2d 339, 346-47 (Conn. 1966) (estate planning advice by non-lawyer broker could be held to be unauthorized practice, including supplying a will and trust, filling in the blanks, supervising execution, advising as to tax consequences); Fla. Bar v. Brumbaugh, 355 So. 2d 1186, 1193-94 (Fla. 1978) (distinguishing secretarial services and assistance in filling in forms); *In re First Escrow, Inc.*, 840 S.W.2d 839, 848-49 (Mo. 1992) (escrow company may complete forms if no judgment or discretion, but may not draft or select legal documents or give advice concerning the effect of the document); *In re Thompson*, 574 S.W.2d 365, 369 (Mo. 1978) (sale of divorce kits was not unauthorized practice in the absence of personal advice); State v. Winder, 348 N.Y.S.2d 270, 272 (N.Y. App. Div. 1973) (giving advice on individuals' specific legal problems in connection with sale of divorce kit was unauthorized practice); Ohio State Bar Ass'n v. Martin, 642 N.E.2d 75, 78 (Ohio Bd. of Comm'rs on the Unauthorized Practice of Law 1994) (estate planning and trust service could not advise clients as to specific trust agreements or prepare and draft trust agreements). See generally Catherine J. Lanctot, *Scriveners in Cyberspace: Online Document Preparation and the Unauthorized Practice of Law*, 30 HOFSTRA L. REV. 811 (2002) (discussing application of unauthorized practice laws to on-line services that provide blank forms with instructions enabling consumers to prepare documents or complete forms based on information consumers provide); State Bar of Texas, *Task Force Recommendation of a New Statutory Definition for the Unauthorized Practice of Law*, 64 TEX. B.J. 860, 862 (2001) (recommending relaxation of regulation "where the legal service being provided can be readily determined to be of a simple nature and/or where others have skills, training, and ethical standards which provide adequate assurance of protection to the public"). A current example of a franchise form preparation service is "We the People," which prepares documents on "bankruptcy, divorce, incorporation, living trusts, wills and probate, guardianship, paternity, adoption, restraining orders, small claims, copyright and trademark, and quit claim deeds," and advertises "No Lawyers! Save Money!" See *Judge Denies Motions to Dismiss UPL Case Brought by State Bar*, ILL. ST. BAR ASS'N BAR NEWS, May 15, 2003 (discussing county court's denial of motion to dismiss consumer fraud complaint brought by the

unauthorized practice of law if it does not involve individualized assistance,<sup>270</sup> while legal computer software and Internet services may cross the line into unauthorized practice.<sup>271</sup>

The mechanistic definitions of law practice based on complexity or custom let self-interested bar committees foreclose competition by non-lawyers without regard to whether these practitioners can render the same quality service as lawyers, or whether clients or customers can accurately evaluate the service they are getting from the non-lawyer.<sup>272</sup> Even courts that take such public policy factors into account do not require any tangible evidence of harm to the public or consider whether regulatory goals could be met by less restrictive means.<sup>273</sup>

The arguments against state licensing of lawyers based on traditional theories of screening unqualified lawyers<sup>274</sup> are even stronger in the borderline unauthorized practice cases. Requiring broad-based legal training in three years of law school and an intensive bar exam makes less sense as the practitioner's

Illinois State Bar Association against "We the People" for engaging in unauthorized practice).

270. See, e.g., *N.Y. Lawyers' Ass'n v. Dacey*, 234 N.E.2d 459 (N.Y. 1967) (reversing unauthorized practice judgment against non-lawyer based on text and forms in book entitled "How To Avoid Probate!"); *Winder*, 348 N.Y.S.2d at 272 (distinguishing do-it-yourself kits for divorce and personal assistance in using the kits).

271. See *supra* Part I.E.2. For an important recent case on computerized legal advice, see *Unauthorized Practice of Law Comm. v. Parsons Tech., Inc.*, No. CIV. A 3:97-CV-2859-H, 1999 U.S. Dist. LEXIS 813 (N.D. Tex. Jan. 22, 1999), vacated by 179 F.3d 956 (5th Cir. 1999). The district court held that the CD-ROM "Quicken Family Lawyer," which enabled consumers to prepare their own wills or other simple legal documents by using the forms and instructions provided, violated the Texas unauthorized practice law because it "purports to select" the appropriate legal document, "customizes the documents," and "creates an air of reliability about the documents." *Id.* at \*18. In response, the Texas legislature amended the law to provide "that 'the 'practice of law' does not include the design, creation, publication, distribution, display, or sale . . . [of] computer software, or similar products if the products clearly and conspicuously state that the products are not a substitute for the advice of an attorney.'" *Unauthorized Practice of Law Comm. v. Parsons Tech., Inc.*, 179 F.3d 956, 956 (5th Cir. 1999) (quoting 1999 Tex. Gen. Laws ch. 799). Following enactment, the Fifth Circuit vacated and remanded. For discussions of *Parsons* and related law, see William H. Brown, Comment, *Legal Software and the Unauthorized Practice of Law: Protection or Protectionism*, 36 CAL. W. L. REV. 157 (1999), Steve French, Note and Comment, *When Public Policies Collide . . . Legal "Self-Help" Software and the Unauthorized Practice of Law*, 27 RUTGERS COMPUTER & TECH. L.J. 93 (2001), and Marie A. Vida, Comment, *Legality of Will-Creating Software: Is the Sale of Computer Software to Assist in Drafting Will Documents Considered the Unauthorized Practice of Law?*, 41 SANTA CLARA L. REV. 231 (2000).

272. See Rhode, *supra* note 76, at 85.

273. See *id.* at 85-86.

274. See *supra* Part I.

activities become narrower and more routine. Conversely, eliminating state licensing of lawyers as to such matters would facilitate the entry of national firms that routinize low-end practice without sacrificing quality.<sup>275</sup> To be sure, buyers of these low-end services may need more legal protection from unqualified lawyers than corporate clients with in-house lawyers who deal with the most reputable large law firms. But this protection is better provided by regulation or licensing for specific kinds of activities, such as real estate conveyances,<sup>276</sup> consumer bankruptcies<sup>277</sup> or no-fault divorces, than by requiring consumers to hire full-fledged lawyers even for marginal legal services.

Moreover, lawyer licensing has a greater effect on availability of legal services for low-income people or those involved in smaller transactions. Forcing these economically marginal clients to buy Cadillacs when they only need Chevrolets may cause them to rely on self-help, and thereby reduce the quality of services these clients actually receive.<sup>278</sup> The impact has been ameliorated somewhat by exempting legal assistance for the poor from unauthorized practice laws.<sup>279</sup> But since these exemptions leave the least sophisticated and therefore most vulnerable clients exposed to supposedly unqualified practitioners, they suggest that lawyer licensing is more concerned with protecting lawyers' profits than with protecting the public.

The analysis of unauthorized practice changes if the rationale for lawyer licensing is participation in lawmaking rather than ensuring quality of legal services. Under the lawmaking-incentive rationale, no license should be required for areas of practice where jurisdictional competition exerts little or no pressure toward efficient laws, including divorce, real estate conveyances and tort

275. See McChesney & Muris, *supra* note 23.

276. See Palomar, *supra* note 47, at 528 (discussing real estate conveyance specialist as a lower-cost alternative to lawyers).

277. There is special regulation under 11 U.S.C. Section 110 for preparers of bankruptcy petitions that requires the preparers to disclose certain information and provides for damages for preparer negligence or fraud. See *In re Boettcher*, 262 B.R. 94, 96 (Bankr. N.D. Cal. 2001) ("We the People" franchisee engaged in practice of law by filling in blanks in form drafted by attorney with 11 U.S.C. Section 110 regulating preparers of bankruptcy petitions); Russell A. Brown, *Bankruptcy and the Unauthorized Practice of Law*, 35 ARIZ. ATT'Y 30 (Feb. 1999) (discussing 11 U.S.C. § 110 (1994)). However, this provision does not authorize practice of law in violation of state statutes, and therefore does not replace lawyer licensing. See 11 U.S.C. § 110(k) (2000).

278. See *supra* text accompanying note 64.

279. See generally Bertelli, *supra* note 266, at 15. For cases applying such exceptions, see *Dixon v. Ga. Indigent Legal Servs., Inc.*, 388 F. Supp. 1156, 1165-66 (S.D. Ga. 1975), *In re N.H. Disabilities Rights Ctr., Inc.*, 541 A.2d 208, 209 (N.H. 1988), *In re Education Law Center, Inc.*, 429 A.2d 1051, 1058 (N.J. 1981), *Azzarello v. Legal Aid Soc'y*, 185 N.E.2d 566, 570 (Ohio Ct. App. 1962), and Wayne Moore, *Are Organizations that Provide Free Legal Services Engaged in the Unauthorized Practice of Law?*, 67 FORDHAM L. REV. 2397 (1999).

litigation.<sup>280</sup> State competition depends on the parties' ability to contract for the applicable law in advance of a dispute,<sup>281</sup> or on whether enforceability of contractual choice of law depends on contracting parties' contacts with the designated state, such as the location of real estate.<sup>282</sup> Without efficiency-enhancing state competition, lawyers may push for inefficient law, or simply benefit from the cartel effect of excluding non-legal practitioners without any side law-creation benefits. Moreover, removing the lawyer monopoly would have the law-creation benefit of encouraging the entry of legal service businesses that could lobby against competition-reducing regulation.

The law-creation argument may play a useful marginal role in unauthorized practice cases. The argument meshes with the quality-screening rationale in many typical unauthorized practice cases such as those involving real estate or divorce work. Where there is little quality-screening basis for licensing, the lack of efficient state competition, and therefore of a lawmaking-incentive rationale, should confirm the inapplicability of licensing laws. On the other hand, both arguments justify licensing transactional work. Licensing is arguably more important for quality screening in relatively low-end transactional work, such as routine corporation-formation, than in high-end work by reputable law firms for sophisticated clients. But as long as states efficiently compete, licensing might make sense even in low-end transactional cases that involve only minimal skill. Lawyers may gain some of the additional law business that would be generated by streamlining practice in these areas. Moreover, given jurisdictional competition, lawyers who attempt to raise costs for consumers stand to lose business to lawyers, or non-lawyers, in other jurisdictions.

In some practice areas the two rationales for licensing might lead to different results. For example, there is no law-creation justification for licensing tort lawyers because of the inefficiency of state competition in this area. But irrespective of the law-creation benefits of state licensing, states have strong incentives to retain the power to regulate lawyers' courtroom activities.<sup>283</sup>

---

280. See *supra* Part III.B.3.

281. It follows that changing the choice of law rule to permit such contracts could affect the analysis of lawyer licensing. For a defense of contractual choice regarding divorce law, see Buckley & Ribstein, *supra* note 5.

282. See *supra* text accompanying notes 170-74. Note that there may be a tension regarding the contacts rule between the efficiency of contractual choice and encouraging lawyer participation in lawmaking. See *supra* note 174.

283. See *supra* text accompanying notes 37-38.

### C. Licensing Specialists

The law-creation argument might justify licensing some legal specialties but not others. For example, separately licensing specialties such as intellectual property, bankruptcy, securities or tax would give lawyers in those areas extra incentives to participate in law reform by increasing their ability to capture the benefits of the reform.<sup>284</sup> To be sure, even without such licensing, lawyers can coordinate lawmaking efforts through voluntary specialty bar associations. But these associations do not provide entry restrictions comparable to those provided by unauthorized practice laws and therefore may not effectively prevent free-riding on the group's lawmaking efforts. Although there is some federal licensing of specialties,<sup>285</sup> state specialty licensing would have the added benefit of enabling both general state legal competition and state variations as to licensing requirements.

### D. State Variations

This Article's theory of state licensing does not necessarily justify licensing, or the same approach to licensing, in *all* states. As long as firms and parties are mobile or can contract for the law of any state, state law efficiency requires only that some states compete to provide efficient law. It follows that only some states need to provide incentives to produce efficient law, including lawyer licensing. Other states may decide that the perverse effects of licensing on the price and availability of legal services outweigh the benefits, particularly where incentives to participate in lawmaking are relatively unimportant. The potential for this sort of variation is another advantage of a state-based rather than federal system of licensing. By contrast, a client-protection theory of lawyer licensing implies that clients in all states need to be protected, and therefore that all states should license. This argument provides a stronger rationale for federal licensing.

### E. Other Professions

This Article's analysis applies only to *lawyer* licensing and not to licensing of other professions. Lawyers raise special considerations because of their interest in the overall quality of state law. Moreover, this rationale for state licensing may matter more to law than other professions such as medicine

---

284. Licensing also might encourage lawyers to develop specialized knowledge in order to better serve clients where lawyers otherwise might not capture sufficient benefits to produce a socially optimal amount of expertise. This rationale for licensing is related to the property rights theory in this Article but differs in that it focuses on the benefit to the lawyers' clients rather than to development of state law.

285. See *supra* text accompanying note 94.



because of the interstate nature of law practice. Given this interstate nature, requiring lawyers to be licensed in the law of a particular state may generate more costs than analogous requirements for other professions,<sup>286</sup> and therefore may require a stronger rationale than the standard asymmetric information theory that applies to professional licensing generally. By contrast, doctors usually see patients in the hospital or office where they are based, although as with law this may change with the development of Internet-based delivery of professional advice.

This Article's analysis may, however, relate indirectly to other professions. Just as licensing lawyers may give lawyers an incentive to maintain the law, licensing doctors and accountants may give those professionals incentives to maintain their chosen fields. For example, accountants have incentives to promulgate and maintain accounting standards, and doctors may have incentives to standardize medical procedures, at least in part because of the monopoly rights conferred by professional licensing.<sup>287</sup> A possible difference between lawyers and these other groups is that there is more need for uniform standards regarding activities of professionals outside law than there is for state laws. The particular value of lawyer licensing in promoting jurisdictional competition therefore may not apply to other professions.

## V. CAVEATS AND CONCLUSIONS

The increasingly national scope of the legal profession, new methods of delivering legal services, and doubts about the adequacy of state regulation in the wake of recent corporate frauds, strain already dubious existing rationales for state licensing of lawyers based on ensuring lawyer quality. But before abandoning this system, lawmakers should consider this Article's alternative rationale for state licensing—that it encourages lawyers' participation in state lawmaking. Eliminating or federalizing lawyer licensing might increase free-riding off of lawyers' lawmaking efforts, thereby reducing their incentives to engage in these efforts. This, in turn, could adversely affect the quality of state law.

This rationale for state licensing of lawyers is, to be sure, fragile at best. First, licensing has only a marginal effect on lawyers' incentives to participate in lawmaking because it gives lawyers only an incomplete property right in the law of the state where they are licensed. Each lawyer must share benefits of lawmaking efforts with lawyers from her own state and, to some extent, from other states. Indeed, lawyer licensing may actually *reduce* lawyers' participation in state lawmaking. If state-based licensing did not tie lawyers to particular

---

286. See *supra* Part I.D.

287. There may also be direct intellectual property protection in this situation. See *supra* note 177.

states, legal talent would be free to flow to its highest and best use. For example, without a licensing requirement, an expert corporate lawyer living and practicing in Pennsylvania would have more incentive to devote resources to developing an expertise in Delaware, federal or uniform law, and to protect the value of that expertise by investing in the creation and maintenance of those laws.<sup>288</sup> The effects of lawyer licensing in encouraging investments in home-state law therefore must be balanced against the effects of discouraging out-of-state investments.

Second, even if lawyer licensing does encourage lawyers to participate in lawmaking, this does not necessarily make state law more efficient than it would be without licensing. Lawyers have incentives to make law more lawyer-friendly, and thus to reduce the efficiency of state law.<sup>289</sup> At least as to some types of laws, state competition may not adequately constrain these incentives. Thus, the costs of giving lawyers a monopoly over legal services may outweigh any benefits of encouraging them to participate in lawmaking.

Third, the lawmaking incentive rationale may be attacked on fairness grounds. Low-income clients arguably bear the costs of lawyer licensing disproportionately to any benefits they receive from lawyers' participation in improving business and commercial laws.<sup>290</sup>

Fourth, licensing's benefits of encouraging lawyer participation in state lawmaking will be difficult to establish empirically. An empirical test would require correlating myriad factors, including type of practice, general background of jurisdictional competition and types of legal rules,<sup>291</sup> with necessarily imprecise evaluations of the efficiency of state law. There may be no reliable way to determine what state law would look like under a different approach to lawyer licensing.

Despite these caveats, the relationship between state licensing of lawyers and state law efficiency is sufficiently plausible that it should be considered along with other potential effects of lawyer licensing. First, lawyers clearly do actively participate in state lawmaking other than for clients, and would have less reason to do so if they had no special interest in the law of a particular state, other things being equal.

Second, any lawyer participation in state lawmaking is especially significant at a time when the increasing complexity and scope of regulation place greater burdens on state lawmakers, who operate with tiny budgets and often on a part-time basis. Without lawyers' assistance, the states may have to cede even more policymaking to the federal government, weakening further the laboratory of state law.

---

288. I am indebted to Jonathan Klick for this point.

289. See *supra* Part III.B.2.

290. See *supra* note 61 and accompanying text.

291. See Part III.B.3-4.

Third, even if lawyers' influence is not always positive, it is necessary to compare the current political dynamic with the situation that would exist in the absence of lawyer licensing. Eliminating lawyer licensing may shift power to non-lawyer, or trial lawyer, interest groups who seek wealth transfers and who lack transactional lawyers' stake in the efficiency of a state's overall legal system.

Fourth, even if the net benefits of the lawmaking-incentive rationale are unclear, the same is true of the existing lawyer-quality rationale. The lawmaking-incentive theory therefore may have an important marginal role in the overall policy analysis of lawyer licensing.

It follows that the best approach to reform of state licensing may be to tinker with the current system rather than eliminate it. For example, the states might allow more jurisdictional choice of ethical rules,<sup>292</sup> or deregulate areas of practice where licensing serves little purpose under either rationale.<sup>293</sup> But before eliminating or federalizing lawyer licensing, lawmakers should consider that, while more competition in providing legal services may be a good thing, this competition may come at the expense of lower quality state laws or a weakened federal system.

---

292. See Ribstein, *supra* note 72 (suggesting giving law firms some power to choose among state ethical rules that affect law firm structure).

293. See *supra* Part IV.B (discussing the scope of lawyer licensing under the lawmaking-incentive rationale).