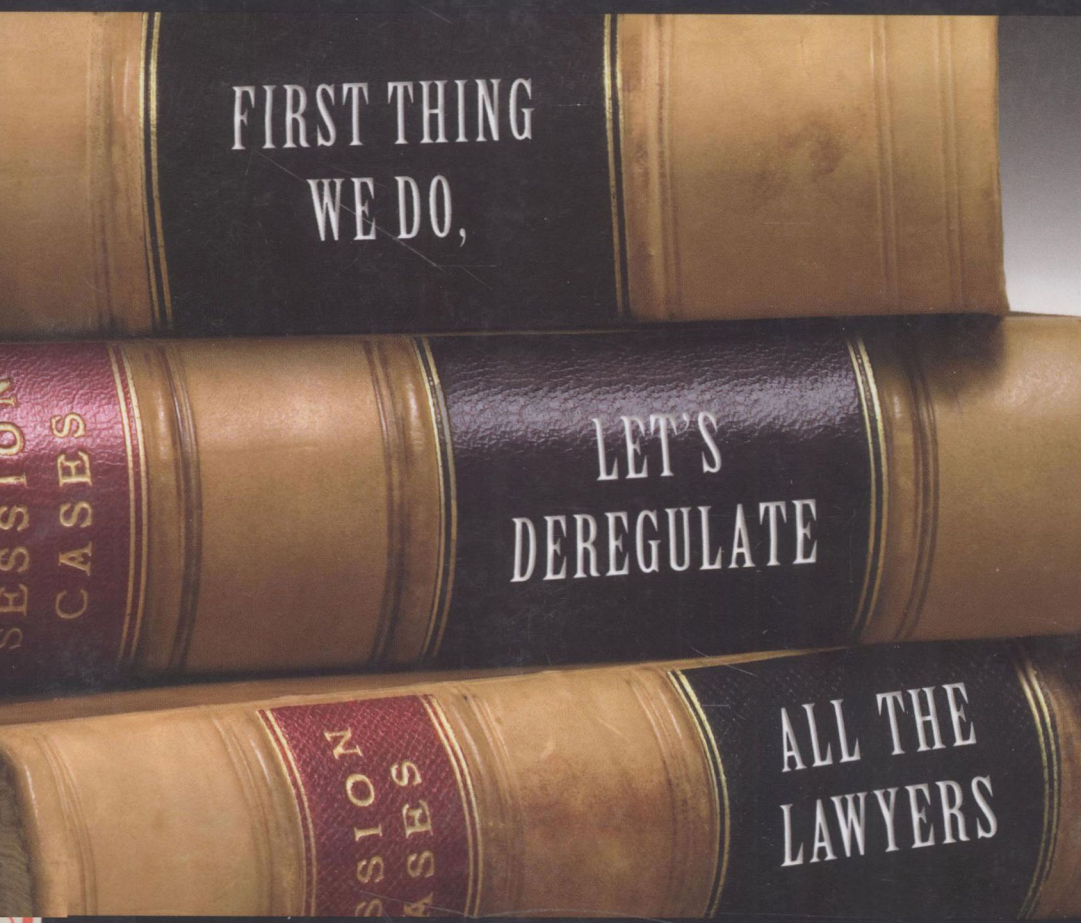

CLIFFORD WINSTON
ROBERT W. CRANDALL
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FIRST THING WE DO, LET'S DEREGULATE ALL THE LAWYERS

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Contents

CHAPTER ONE

Introduction

In late 2000 Justin Anthony Wyrick Jr. became the most requested legal expert on the website AskMeHelpDesk.com. To the great surprise of many bloggers and their followers, "Justin" was actually a fifteen-year-old high school student named Markus Arnold who apparently had never read a law book. The American Bar Association (ABA) was not impressed. In its view, Arnold had committed a serious ethical violation by misrepresenting himself as a lawyer.

Arnold was never prosecuted, but in an earlier episode Rosemary Furman nearly went to prison for trying to help people solve their legal problems without having a license to practice law. As recounted by Leef (1998), Furman was a legal secretary in Florida who decided to go into business for herself in 1972 by preparing and filing the necessary legal papers for people seeking a divorce. Her customers sought out her services and willingly paid for them; no one ever complained about her work. Despite this problem-free track record, the Florida Supreme Court in 1984 ordered her jailed for practicing law without a license. As it turned out, Furman never served any jail time, but only because Governor Bob Graham intervened.

Lawyers are among the 20 percent of the U.S. labor force that is required to obtain a government license to practice a profession (Kleiner 2006)—a requirement that may not be justified, as suggested by the preceding anecdotes, because some legal services could be com-

petently provided by persons who have not had a formal legal education and who have not passed a state bar examination to obtain a license. Even people who do have a legal education are prevented from taking a bar examination and practicing law in all but a few states unless they graduated from an ABA-accredited law school. And ABA regulations prevent licensed lawyers who work for firms that are not owned and managed by lawyers from providing legal services to parties outside their firm. The ABA-imposed entry barriers are one important factor that we argue unnecessarily raises the cost of legal services. Before discussing the other important factor—that lawyers have become an effective interest group—we summarize how the ABA came to exert such a powerful influence on the practice of law.

The Evolution of the ABA's Influence

The association first attempted to include its accreditation of law schools as part of states' occupational licensing of lawyers in 1921, when, claiming concern over the quality of the legal education being administered, it adopted a statement of minimum standards of legal education and instituted a policy of publishing a list of law schools that complied with those standards. Whether this policy had beneficial effects and was justified is unclear: it is difficult not only to measure the quality of the legal education at the time but to verify that the ABA's accreditation standards improved it. Some commentators argue that the true motivation for the standards was to prevent minorities and the poor from joining the profession (Auerbach 1971). If true, that motivation would undermine an alleged benefit of occupational licensing: that it can increase the presence of minority workers by serving as an imprimatur of worker quality.[1]

1. Law and Marks (2009) test the effects of occupational licensing laws on minorities and find that they helped minorities in some occupations, but they do not report results for lawyers in their study. Lehmann (2010) finds that, compared with whites of similar credentials, blacks are much more likely to be hired by the best law firms. But they are assigned to worse tasks and less likely to be made partner because they are given less desirable work at the beginning of their careers.

Initially, state legislatures were not persuaded by the ABA's alleged justification for its standards, and four years after the standards were developed, not a single state required graduation from an ABA-accredited law school for admission to the bar. But by the 1950s the U.S. Department of Health, Education, and Welfare had recognized the Council of the ABA Section of Legal Education and Admissions to the Bar as the sole accrediting agency for degree-granting law schools, and about half the states had education requirements based on ABA standards. Friedman (1962, p. 153) suggested that the other states did not have such requirements because many state legislators themselves were graduates of unaccredited schools: "If they voted to restrict admission to the profession to graduates of approved schools, in effect they would be voting that they themselves were not qualified." Friedman later predicted that as more legislators were trained at accredited law schools, the ABA standards would be more broadly accepted (Fossum 1978). Indeed, Friedman's forecast has proved to be correct: today, all but a few states, notably California, require would-be lawyers to have graduated from an ABA-accredited law school, and every state except Wisconsin requires them to pass a bar exam.[2]

State governments also allow the ABA to enact regulations that govern the type of legal services that firms and individuals can offer. A firm is prohibited from offering legal services unless it is owned and managed by lawyers. The ABA defines the practice of law to prevent nonlawyers from providing what it deems to be legal products and services. Not surprisingly, its definition of the practice of law is expansive and includes nearly every conceivable legal service. The ABA has urged states to invigorate enforcement of practice restrictions on nonlawyers (Hadfield 2008a), even to restrict the sale of simple, standard-form wills as the unauthorized practice of law.

2. Wisconsin allows graduates of the University of Wisconsin Law School to practice law without passing a bar examination.

Lawyers as an Interest Group

With the help of the ABA, lawyers have developed into a powerful interest group that limits its membership. Unlike most other interest groups, lawyers benefit from government policies that increase the demand for their services.

The symbiotic relationship between policymakers and the legal profession has roots that can be traced to the formative years of the United States. In an 1816 letter to Benjamin Austin, Thomas Jefferson lamented that lawyers "by their numbers in the public councils, have wrested from the public hand the direction of the pruning knife."[3] Shepard (1981) documents the concern that lawyers may have been overrepresented in powerful state government positions during the nineteenth century, when, for instance, lawyers constituted 34 percent of the 1850 Virginia legislature despite making up less than 1 percent of the largely agrarian population. Between the Civil War and the 1950s, lawyers won approximately half of all gubernatorial elections (Schlesinger 1957).

With the rapid growth of the federal government following the New Deal, federal legislative positions became substantially more powerful than their counterparts at the state level. During the past forty years, nearly 60 percent of the members of the U.S. Senate and 40 percent of the members of the U.S. House of Representatives held a JD (juris doctor).[4] In the same period, four of the eight presidents also studied and practiced law before embarking on their political careers. Generally, an interest group can more easily gain from the political process when it "speaks the same language" as the public officials whose policies it is trying to influence. Accordingly, it is not

3. The quote comes from *The Writings of Thomas Jefferson*, edited by H. A. Washington (New York: H. W. Derby Publishers, 1861).

4. The 91st Congress (1969–70) contained 58 senators and 219 representatives with a law degree. Lawyers' grip on legislative power has persisted; the 111th Congress (2009–10) contains 57 senators and 168 representatives with a JD. Those figures are taken from the Congressional Research Service's periodic publication "Membership of the Congress: A Profile."

surprising that members of the legal profession benefit when lawyers lobby former practitioners.

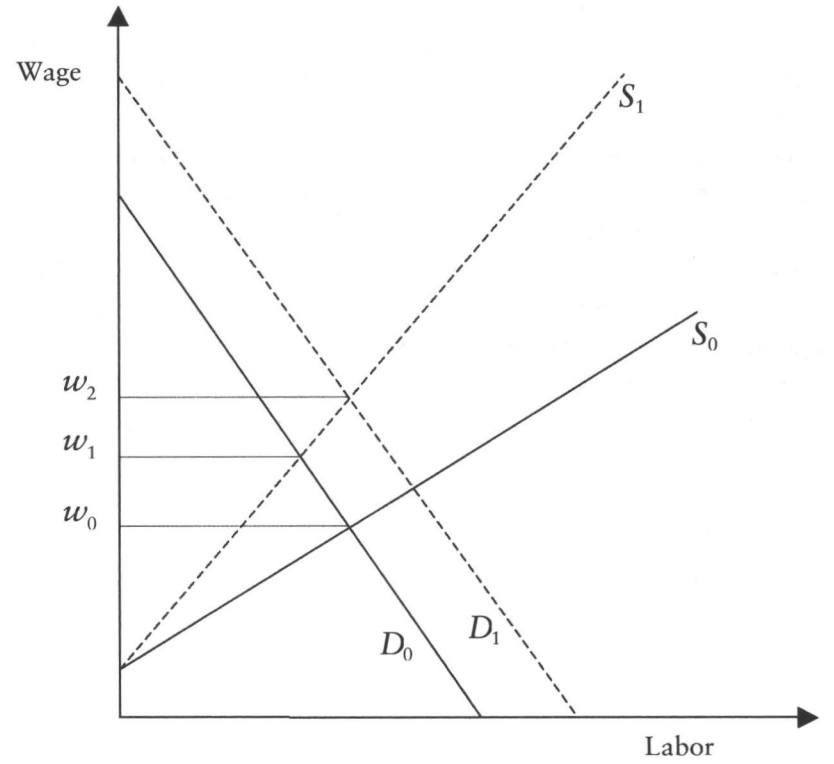
Basic economics suggests that entry barriers to the legal profession, regulations on the type of legal services that firms and individuals can provide, and government-induced demand for lawyers will raise the price of legal services. In this book, we argue that this higher price cannot be justified as the "cost" of ensuring that uninformed consumers of legal services are served by competent lawyers and that socially desirable policies are implemented and executed. Instead, the forces that reduce the supply of and increase the demand for lawyers create significant social costs including a sizable deadweight loss from higher legal fees, less innovation by law firms and lawyers, a misallocation of the nation's labor resources, and socially perverse incentives for attorneys in their collective behavior as an interest group to support inefficient regulatory, liability, patent, and other policies that preserve and enhance their wealth.

To address those costs and improve social welfare, we argue that deregulating entry by individuals and firms into the legal profession is desirable to force lawyers to compete more intensely with each other and to face competition from nonlawyers and firms that are not owned and managed by lawyers. Occupational licensing may be justified to protect consumers if they have imperfect information about the quality of a service being offered, but the theoretical and empirical evidence supporting occupational licensing for lawyers is weak. We do not oppose lawyers continuing to acquire credentials to signal their competence and quality, but allowing the ABA to enjoy a monopoly on law school accreditation and the states to require that lawyers pass a licensing exam is not necessary to facilitate informed decisions by consumers of legal services.

Characterizing the Empirical Debate

An overview of the empirical debate is provided in figure 1-1, where w_0 denotes lawyers' wages without the effects of occupational licensing and entry restrictions on supply, S_0, and of government policies on

Figure 1-1. *The Market for Lawyers*



Source: Authors.
Note: See text for explanation of terms.

demand, D_0. Occupational licensing and entry restrictions cause the supply of lawyers to shift inward and become more inelastic, as indicated by S_1, which causes lawyers' wages to rise to w_1. Public policies that induce firms and individuals to hire lawyers shift the demand for lawyers to D_1, causing lawyers' wages to rise even more to w_2. Our interest is in whether the increase in lawyers' wages caused by entry restrictions and government-induced demand for lawyers is unjustified on efficiency grounds or, alternatively, is justified because of lawyers' unobserved skills and abilities and their working environment, because consumers receive higher quality legal services than they would receive

without occupational licensing, and because lawyers contribute to implementing and executing beneficial public policies.

As regulatory economists, we find it natural to reason that occupational licensing, like other regulations that restrict entry, benefits existing suppliers by limiting competition. Thus its primary effect is to generate earnings premiums to practitioners in a particular profession such as law—earnings premiums that could be inefficient.

Labor economists are cautious about reaching the conclusion that workers in a particular profession such as law receive inefficient earnings premiums, noting the possibility that empirical estimates of wage premiums actually capture returns to unobserved skills, abilities, and working conditions, and that such returns are justified on efficiency grounds.[5] If this possibility is true, lawyers may receive earnings premiums that are unrelated to market inefficiencies caused by restrictions on entry and competition and that thus do not reflect social costs. We recognize this concern and therefore conduct a battery of tests to examine whether our estimates of earnings premiums can be explained by unobserved factors that reflect efficiencies, but we find no evidence that such efficiencies contribute to explaining lawyers' premiums.

Hadfield (2008b) summarizes the law literature that criticizes lawyers for being self-interested at the expense of consumers of legal services and the ABA for initiating regulations, including unauthorized-practice-of-law restrictions, which promote the interests of lawyers. This literature focuses on the costs to lawyers' reputations and to consumers who do not have access to legal services, but it does not discuss our concern about lawyers' potentially counterproductive role in maintaining inefficient public policies and how those policies benefit lawyers. If the demand for lawyers is increased by government policies that raise social welfare, then those benefits should be balanced against increases in lawyers' earnings. But we find that the policies that increase lawyers' earnings premiums have been assessed

5. Unobserved differences in skills refer to differences in skills among lawyers that we as empirical analysts are unable to observe. This does *not* imply that those differences in lawyers' skills are not observed by consumers of legal services.

empirically by scholars and found to have produced little improvement in economic welfare and are likely to have reduced it.

In this book, we recommend the deregulation of the legal profession, a recommendation that is justified even if entry restrictions do not generate inefficient earnings premiums. If lawyers' wages reflect only observed and unobserved differences in skills and ability, then consumers of legal services would continue to recognize those differences in the absence of occupational licensing requirements. Deregulation would also be justified even if the policies that increase lawyers' earnings premiums generate significant social benefits because lawyers would still be hired to implement those policies in a more competitive environment.

Finally, we do not minimize the vital role that lawyers in the United States play in supporting democratic institutions, protecting individual rights, and the like. But lawyers can also be judged on their effectiveness in contributing to economic activity and efficiency both within and outside their profession. We conclude that lawyers' performance on that score would improve greatly in a more competitive environment for legal services.

CHAPTER TWO

The Market for Lawyers

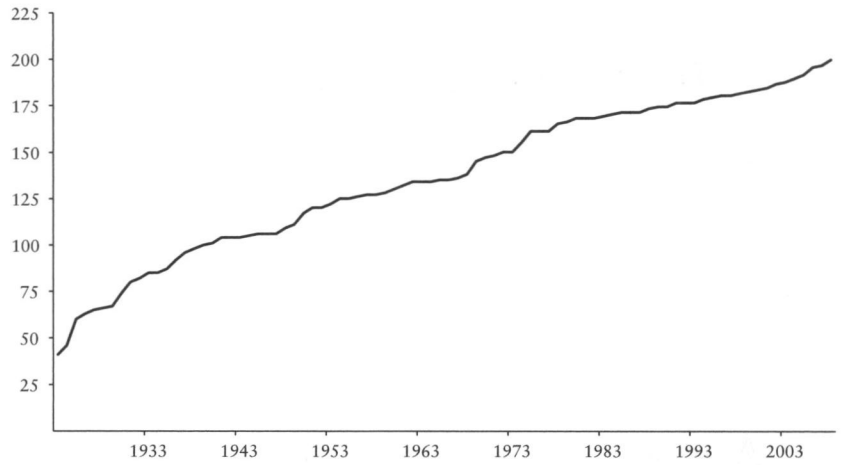
According to the Current Population Survey, approximately one million lawyers are currently working in the United States in law firms, government offices, and the legal departments of private corporations. This figure may comport with the conventional view that the United States has too many lawyers, but occupational licensing requirements have in fact constrained the supply of lawyers. In this chapter we provide an overview of the various policies that have affected the supply of and demand for lawyers and then estimate lawyers' aggregate annual earnings.

The Role of Law Schools in Limiting the Supply of Lawyers

As noted, to obtain a license to practice law, an individual must typically gain admission to a law school accredited by the American Bar Association and pass a state bar examination. The ABA's rigorous accreditation process takes a minimum of four years, including, for new law schools, an initial year during which the school must have been in operation before the ABA accreditation process can begin. The ABA has yet to consider online or foreign law schools for accreditation.[1]

1. The ABA has put off a decision on whether to accredit foreign law schools by saying it wishes to study the matter more fully. In June 2008 the Peking University of Transnational Law announced its intention to seek accreditation from

Figure 2-1. *Number of ABA-Approved Law Schools, 1923–2006*



Source: American Bar Association.

Figure 2-1 shows the growth in the number of law schools approved by the ABA to grant law degrees since it began accrediting schools during the 1920s. The growth in accredited schools has slowed in the past three decades—the ABA has accredited only about thirty new law schools since 1979 (and rejected the accreditation of an unknown number of other schools; the ABA does not disclose a list of schools it has been unwilling to accredit). The ABA has even put some accredited law schools, such as Golden Gate University and Whittier College, on probation because their students' first-time bar passage rate was too low, and it has refused to renew some other law schools' accreditation until those schools have satisfied certain conditions.

The ABA's actions may be justified as maintaining and signaling the quality of legal education in the United States. But the ABA has refused to provide further information about a law school's quality beyond its accreditation status and has continually issued disclaimers

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the ABA, so its graduates could potentially practice law in the United States. But the ABA said it would not consider the accreditation of any particular foreign law school until it completed its broader assessment.

of any law school rating system.[2] This policy is hardly consistent with the view that the ABA wants prospective law students and employers to be more informed about a law school's quality. As of 2010, 200 institutions in the United States were ABA-approved to confer law degrees, 7 of which had received only provisional accreditation. A few states, including California, have their own accreditation process and allow students who do not graduate from an ABA-accredited law school to sit for their bar examinations.[3]

Law school applicants are generally required to take the Law School Admissions Test (LSAT) and to report their scores. Thus, the number of distinct individuals who take the LSAT in any given year is a reasonable lower bound on the number of people in the United States interested in entering the legal profession. According to data from the Law School Admission Council, the number of unique first-time LSAT test takers has averaged nearly 100,000 a year from 1997 through 2004.[4] Only a very small percentage of people who take the test are discouraged from eventually applying to law school (although the expense and opportunity cost of three years in law school may discourage many from taking the test in the first place). The total number of law school applicants admitted to at least one law school averaged 53,300 a year during 1997–2004; thus, roughly half of the 800,000 law school applicants during the period were not admitted anywhere.[5] The Law School Admission Council has reported that the

2. The ABA recently passed Resolution 10A to "examine any efforts to publish national, state, territorial, and local rankings of law firms and law schools."

3. California's bar exam is considered to be among the most difficult in the country to pass, and it effectively serves as a screening device to limit the number of practicing attorneys in the state.

4. The Law School Admission Council is a nonprofit corporation that seeks to ease the admission process for law schools and their applicants. The council is best known for administering the Law School Admission Test.

5. John Nussbaumer, "The Door to Law School," Presentation at the University of Massachusetts School of Law, October 2010, presents data indicating that 60 percent of African American law school applicants from Fall 2000 to Fall 2009 did not receive an offer of admission from any law school. The "shut-out" rate was 45 percent for Hispanic applicants and 31 percent for Caucasian applicants.