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Regulation of legal and medical professions in the Us and Europe: A comparative analysis [*]

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Abstract

This paper analyzes the regulation of access to, and activity of, the legal and medical professions. A critical assessment is offered of the economic theory of the regulation of professions in relation to the key issues of: (a) Why regulate, (b) How to regulate, and (c) What to regulate. We suggest a set of indicators to measure the quality of regulatory restrictions, and thereby expose comparative inefficiencies, in the medical and legal professional activities. We conclude that generally speaking the USA followed by Norway, the UK [England and Wales] and Belgium perform better in terms of efficient regulation, whereas Germany, Austria and Portugal perform badly for both legal and medical professionals. Other countries (including the Netherlands, Spain, France) vary. Our results are partly, but not entirely, consistent with previous findings.

Keywords: Regulation, Rent-Seeking, Lawyers, Physicians.

[*1] See Ogus, A., 1994, Regulation: Legal Form and Economic Theory, Oxford, Oxford University Press, page 216.

1. Introduction

A profession can be defined as an occupation with the following general characteristics: it requires specialized skills partially or fully acquired by intellectual training; it provides a service calling for a high degree of integrity, and it involves direct or fiduciary relations with clients.[1] This paper analyzes the regulation of access to, and pursuit of, certain professions, namely medicine and the law. The legal and medical professions (also notaries, pharmacists, and accountancy, less so architects and engineers, and even less economists and journalists) appear to be relatively highly regulated according to the European Commission. However, there are important disparities in levels of regulation across European countries. Austria, Germany, Greece, Italy, Luxembourg, and Portugal appear to be quite rigid whereas France, Spain, and Belgium have a relatively less strict approach to the regulation of a significant number of professions. By contrast, Denmark, Finland, Sweden, Ireland, the Netherlands, and the United Kingdom have developed a more flexible regulatory framework for the professions.[2] The United States could be included in this last group of countries if the analysis were to be extended outside of the European Union, though there are important differences at state level.

Even though many commentators think that professional regulatory activities are mostly explained by rent-seeking motivation, we find very different institutional arrangements across countries. Whilst ultimately governed by law and oversight by public officials (judge, bureaucrat or legislator), these regulations are somehow delimited and enforced by the profession itself. Thus, it is of importance to assess which arrangements are more prone to private capture and to suggest ways of reforming regulatory institutions.

One obvious motivation is the fact that professional regulatory activities have been included in the current public policy agenda. The European Commission, in particular the Directorate-General for Competition, has shown interest in promoting competition in the market for professional services, thus opening a general discussion concerning regulatory frameworks.[3] The British Government has started a review process of the regulatory setup for legal services in order to foster competition, innovation, as well as consumer protection and accountable regulatory enforcement.[4]

[2] Stocktaking Exercise on Regulation of Professional Services, Overview of Regulation in the EU Member States, 2003.
[3] Stocktaking Exercise, 2003, *op. cit.* 3.
[4] Review of the Regulatory Framework for Legal Services in England and Wales, Consultation Paper and

The present paper has two major parts. In the first part, we present a critical assessment of the economic theory of the regulation of the professions, reviewing in particular: (a) Why regulate, (b) How to regulate, and (c) What to regulate. In the second part, an application to the regulation of professions in the United States and Europe is developed. We suggest a set of indicators to measure the quality of regulatory restrictions and thereby to expose comparative inefficiencies in legal and medical activities. The choice of countries to be included in the analysis has been solely determined by information made available.

2. Theories of regulation of professions -- why

The different theories can be classified in three groups: market failure (including asymmetry of information); public interest (apart from market failure); private interest (rent-seeking).

2.1 Market failure

The view that regulation promotes the public interest by correcting for market failure relies on the inefficiency of the market equilibrium.[5] The main market failure that applies to professional markets is information asymmetry.[6] For most clients and consumers, professional services are credence goods.[7] The consumer is less informed about the nature and quality of the service, and often relies on the expertise of the professional in order to assess (agency function) and implement the aprropriate strategy (service function). There is a potentially severe problem arising from some kind of supplier-induced demand. Under these conditions the market usually fails to produce the socially optimal quantity and quality of the professional service. Some protection for the consumer of professional services is necessary to guarantee quality and mitigate inefficiencies. Protection of consumers frequently takes the form of regulation of the profession and the respective market.

Final Paper by Sir David Clementi, 2004.

[5] Posner, R. A., 1975, The Social Costs of Monopoly and Regulation, Journal of Political Economy 83, 807-827; Noll, R., 1989, Economic Perspectives on the Politics of Regulation, in Handbook of Industrial Organization II, Amsterdam, North-Holland, 1253-1287.

[6] Stephen, F. and Love, J., 1999, Regulation of the Legal Profession, in Encyclopedia of Law and Economics, Ghent, University of Ghent, 987-1017.

[7] Darby, M. R. and Karni, E., 1973, Free Competition and the Optimal Amount of Fraud, Journal of Law and Economics 16, 111-126.

Nevertheless we should have in mind that the costs generated by asymmetry of information must be balanced against the benefits of labour specialization. A reduction in information asymmetry might not be efficient if it also implies a substantial loss of benefits from labour specialization. For example, it is important to emphasize that the information asymmetry does not apply to all consumers. Repeat purchasers in the market for professional services are able to acquire experience and knowledge of the market which reduces the asymmetry of information (e.g., corporate clients in the market for legal services). Professionals must also take note of reputational effects which may arise from social networks even when most consumers are not repeat purchasers. Furthermore, when the service function is provided separately from the agency function, there is scope for revelation of information that limits opportunism (e.g., medical diagnosis and treatment by different medical doctors).[8]

Besides the moral hazard problem we have so far described, there is the possibility of adverse selection insofar as consumers cannot judge the quality of professionals. The "lemons problem" may arise, prompting the need for some kind of licensing or an equivalent mechanism.[9] Competition among professionals does not solve the problem due to the fact that good professionals may be driven out of the market by bad professionals given the inability of the market to discern and pay for quality.

Another information problem may occur in the market for professional services, namely bounded rationality or rational ignorance. Consumers use simplified rules to process information rather than complex rational analysis. They also usually lack the education level, or even the intellectual ability, to be able to understand all available information on services. Regulation is justified if the regulatory body has more information and expertise at its disposal than average consumers.[10]

Legal professionals usually stress the need for self-regulation, arguing that severe losses would occur if poorly trained lawyers were allowed to perform services. This loss is particularly significant in the health sector, where injuries to the body and life represent substantial and eventually under-compensated damages. The consequences of medical maltreatment and legal misrepresentation go beyond

[8] Emons, W., 1997, Credence Goods and Fraudulent Experts, RAND Journal of Economics 28, 107-119.
[9] Leland, H. E., 1979, Quack, Lemons, and Licensing: A Theory of Minimum Quality Standards, Journal of Political Economy 87, 1325-1346.
[10] Maks, J. A. H. and Philipsen, N. J., 2002, An Economic Analysis of the Regulation of Professions, in The Regulation of Architects, Antwerpen, Intersentia.

the direct customer and generate serious negative externalities for the general public. Good health standards and the quality of the legal system are positively related to the quality of physicians and lawyers.[11]

Finally a fifth form of market failure that justifies regulation is the existence of public goods. Information concerning the quality of professional services satisfies the conditions of non-rivalness and non-exclusivity in consumption. Therefore, there is the possibility that private provision (by professionals) of information is not efficient. This may well justify mandatory information disclosure with respect to professional quality.[12]

Regulation of professional services can improve the market equilibrium. Asymmetric information causes moral hazard and adverse selection and eventually negative externalities for the general public thus precluding an efficient level of health and legal safety from being achieved by the market. The benefits of regulation include a decrease of search costs, improvements in service quality and more adequate supply of information concerning quality of professional services. Also, and very important, a reduction in risk is to be expected. In fact, due to the asymmetry of information, regulation could be the most adequate substitute for insurance.[13]

Notice that, although the case for regulation under a public interest perspective might not be controversial among economists, it remains unclear which form of regulation should be used. If there are severe limitations to entry, it is an open question whether prohibition of advertising and regulation of fees might be justified under a theory of public interest. What seems clear is that in a market for professional services, where quality is uncertain, confidence and trust in the professionals is important for efficiency. After a couple of visits to a doctor a patient whose health problems have been solved may start trusting the doctor. An attorney who handles cases with care and arranges affairs with success may create a trust relationship with his clients. The problem is of course that most customers are not repeat purchasers, and even if they were, the costs of mistakes in the initial rounds could be very high.

[11] Rubin, P. H. and Bailey, M. J., 1994, The Role of Lawyers in Changing the Law, Journal of Legal Studies 23, 807-831.
[12] Maks and Philipsen, *op. cit.* 10.
[13] Zerbe, R. and Urban, N., 1988, Including Public Interest in Theories of Regulation, Research in Law and Economics 8, 4-5.

Regulation and legal rules should aim at enhancing the trust relationship by economizing on information costs. There are three reasons why regulation can be expected to create a confidence premium (thus rewarding professionals above marginal productivity): (a) The cost of obtaining information is lower for the professional than for the client, (b) The information involved is productive, (c) The provision of true information must be rewarded in order to avoid strategic behavior or opportunism. At first glance, these reasons explain the need for minimum quality standards and even some regulation of fees, but do not seem to justify severe restrictions on entry and on advertising.

2.2 Other public goals

Regulation of professionals may also pursue public goals other than economic efficiency (i.e., correcting for information asymmetries and externalities). These goals may be explained by a paternalistic view of the role of government or community values, and usually are related to redistribution.[14]

Confidence, honesty and trust might be values pursued by the government which in turn may actually promote greater social welfare and foster growth. The social willingness to pay for these values may be above its market or economic value, thus justifying government's intervention. A doctor or a lawyer in a small town may have a socially valuable role or function that goes beyond the professional service s/he provides. Redistribution in favour of the professional against the consumer is just a form of paying for these alleged social services.

2.3 Private interest

The final theory of regulation relates to private interest and relies on capture and collusion.[15] From this perspective the regulation of markets for professional services is seen to arise and be sustained because it is in the interests of the members of the profession. It essentially allows for their cartel-like behavior.[16] As a result, the capture theory predicts that professional licensure should decrease the supply of professionals below the social optimum, increase the prices charged by

[14] Ogus, 1994, *op. cit.* 1, pages 218-219.
[15] Posner, R. A., 1974, Theories of Economic Regulation, Bell Journal of Economics and Management Science 5, 335-358.
[16] Benham, L. and Benham, A., 1975, Regulating Through the Professions: A Perspective on Information Control, Journal of Law and Economics 18, 421-447.

professionals, and increase existing professionals' incomes beyond marginal productivity, thus generating rents and quasi-rents.[17]

The most successful groups in obtaining wealth transfers are likely to be small, usually single issue oriented and extremely well organized. On the other side, those who bear the cost of paying rents are large fractions of the population, difficult to organize and with information problems. When these conditions are met, wealth transfers are expected to take place from the public as a whole to the very well-organized interest groups.

The government should protect the public from these interest groups but incentives to provide public interest legislation can be overcome by pressure from those benefiting from wealth transfers. Moreover, wealth transfers may not be recognized by the public in general and comparisons with other jobs and occupations can be difficult.[18] Just take the case of a confidence premium. Comparing figures about the income situation of professionals and other occupations may provide some evidence about how much better paid they are, but we can hardly distinguish the confidence premium from pure rents. Unemployment within the profession below the average rate of unemployment could be an indication of rent-seeking but also that the population requires more professional services than other goods and services on average. Less regional variance with respect to payments could help to identify rent-seeking (payments less subject to local market and business conditions indicate some degree of market power), but at the same time it could be that the willingness to pay for health and legal professional services varies less across regions than for other goods and services. Market concentration indices for professional services can be constructed but are of course subject to the appropriate delimitation of the market (e.g., most large law firms are specialized in certain areas of the law) and also distortions in the public sector (e.g., a national health service is the major provider of medical services in many European countries).

[17] Stigler, G., 1971, The Theory of Economic Regulation, Bell Journal of Economics and Management Science 2, 3-21; McChesney, F., 1987, Rent Extraction and Rent creation in the Economic Theory of Regulation, Journal of Legal Studies 26, 101-118; Olsen, R. N., 1999, The Regulation of Medical Professions, in Encyclopedia of Law and Economics, Ghent, University of Ghent, 1018-1053; Hadfield, G., 2000, The Price of Law: How the Market for Lawyers Distorts the Justice System, Michigan Law Review 98, 953-1006; Kleiner, M. and Kudrle, R. T., 2000, Does Regulation Affect Economic Outcomes? The Case of Dentistry, Journal of Law and Economics 43, 547-582.

[18] Van den Bergh, R., 1993, Self-Regulation in the Medical and Legal Professions and the European Internal Market in Progress, in Regulation of Professions, Antwerpen, Maklu.

The fact that rent-seeking behavior is intrinsically difficult to identify[19], even more when there are sound public interest arguments for regulation to be made, makes regulatory capture more likely. Nevertheless, it is possible to develop legal and political instruments to limit it. Promoting competition, in particular by making use of the internal European and US markets (which should promote a free flow of professional services), auditing professional bodies (including comparative institutional analysis) or forcing the separation of the service function from the agency function (e.g., medical diagnosis and treatment by different medical doctors) certainly helps to mitigate the problem.

2.4 A compromise between theories

In contrast to both pure private and public interest theories, the public and the professionals both have an influence on the form and content of professional regulation. Thus, professionals will sometimes, but not always, be able to use regulations to limit supply and generate rents. On the other hand, the public interest will be pursued sometimes, but not always.[20] In fact, public and private interest theories mirror two distinct historical phases in economic research, emphasizing the corrective and the redistributive roles of regulation.[21] Different institutional arrangements and regulations are consistent with each theory. In particular, self-regulation is not necessarily an indicator of rent-seeking. Professional regulatory bodies are consistent with public interest theory. Identifying rent-seeking requires a more detailed analysis of the legal substance than just the legal form.

[19] But not impossible, see Olsen, R. N., Lueck, D., and Plank, T. E., 1991, Why do States Regulate Admission to the Bar? Economic Theories and Empirical Evidence, George Mason University Law Review 14, 253-286.
[20] Peltzman, S., 1976, Toward a More General Theory of Regulation, Journal of Law and Economics 19, 211-244.
[21] Hägg, G. T., 1997, Theories on the Economics of Regulation: A Survey of the Literature from a European Perspective, European Journal of Law and Economics 4, 337-370.

3. Institutional arrangements -- how

There are several possible institutional arrangements to correct for market failure in the market for professionals as well as to avoid private capture. We identify three types of solution: regulation by the government; self-regulation; and regulation by third parties.

3.1 Regulation by the government

Regulation by the government usually includes quality regulation, certification and licensing. The government could subsidize high quality suppliers to ensure that they remain in the market even if adverse selection persists. Unfortunately this does not guarantee that the higher quality service will actually be supplied due to moral hazard. Second, penalties can be imposed on low quality suppliers and entry to the market could be restricted to some minimum standard.[22] These regulations however require a regulatory agency that must avoid capture and be able to do what consumers cannot: assess quality and signal it to potential clients.[23] Apart from simple mandatory disclosure measures (e.g., professional specialty, professional education) and prohibiting what seems obvious misleading advertising (e.g., professional misrepresentation, that is, saying one is a lawyer or a doctor when one is not), effective quality regulation by the government seems difficult to imagine.

Under certification or licensing, a document (certificate or licence) is awarded to an individual who satisfies certain conditions. These conditions may be education or training. The government as well as a private agency may certificate or license professionals, and regulate professional education, compulsory periods of training, and performance requirements.

The difference between licensing and self-regulation is that while rules are issued by public authorities in both settings (since the professional body is entrusted with public authority), entry and performance are regulated by the state in the first case (eventually delegated to a private agency independent from the profession) and by the profession in the second case. The consequence is that self-regulation promotes strong professional association (as we know with lawyers and doctors) whereas licensing does not. A profession becomes only a real profession if

[22] Dingwall, R. and Fenn, P. T., 1987, A Respectable Profession? Sociological and Economic Perspectives on the Regulation of Professional Services, International Review of Law and Economics 7, 51-64.
[23] Stephen and Love, 1999, *op. cit.* 6.

it has the decisive power to fix remuneration; otherwise it is just a form of licensing (just like economists and journalists almost everywhere).

The two arguments against licensing and thus making the case for self-regulation are the following: (a) It still does not solve the problem of asymmetric information because neither the government nor a private agency independent from the profession have better knowledge of the quality of the service the profession provides than the profession itself (though they might have better knowledge than the average consumer), (b) It is less flexible (in dynamic markets where innovation is important agencies should be able to change quickly) and generates costs to be borne by the government rather than by the profession itself.[24] The second argument nevertheless has serious limitations. First, the profession can regulate fees to cover these costs (hence they will be borne by taxpayers or consumers in both cases). Second, rents created by the exercise of regulatory powers by the professional body can undermine flexibility. For example, rents may be used to successfully resist competition from other regulatory bodies offering more efficient rules.[25]

3.2 Self-regulation

Professional regulators have the necessary information to extract signals in markets for credence goods[26] but can hardly avoid the ultimate form of regulatory capture. Yet this type of body persists in most jurisdictions. One view is that there is a social contract between the profession and the community in order to reduce moral hazard. Naturally safeguards are required in order to ensure the profession does not operate a cartel. Also various watchdogs (e.g., the legal services ombudsman in England and Wales and in Scotland or the medical care independent review program in California and other states) are necessary.[27] Another view is that the reduction in costs of extracting information by professionals more than compensates for potential losses due to cartel-like behavior.[28] These potential losses can be mitigated if there is more than one professional body in competition with each other (nevertheless in most jurisdictions professional bodies have national or local monopoly), a large

[24] Miller, J., 1985, The FTC and Voluntary Standards: Maximizing the Net Benefits of Self-Regulation, The Cato Journal 4, 897-903.
[25] Curran, C., 1993, The American Experience with Self-Regulation in the Medical and Legal Professions, in Regulation of Professions, Antwerpen, Maklu.
[26] That is the well-known specific knowledge argument by Miller, 1985, *op. cit.* 24.
[27] Dingwall and Fenn, 1987, *op. cit.* 22.
[28] Ogus, A., 1995, Rethinking Self-regulation, Oxford Journal of Legal Studies 15, 97-108.

heterogeneous profession[29], and adequate legal instruments (e.g., efficient tort law).[30]

Though self-regulation solves the information problem we have discussed before, it is difficult not to expect that professional bodies use their regulatory powers to restrict competition somehow. Such rent-seeking behavior, alongside other significant costs of administering the regulatory system, causes a significant deadweight loss. In order to tackle this problem, we should have in mind four specific dilemmas: (a) It will be easier for professionals not to pass their better information and expertise to the users unless of course they have an interest in doing so (this will increase search costs for the consumers since asymmetric information will not be reduced), (b) Professionals will induce demand for services that clients, if fully informed, would not require (inefficient allocation of resources), (c) Control and enforcement of quality standards will not be very effective due to collusion (hence we should investigate the application of sanctions for malpractice), (d) Fees will be set above the confidence premium.[31]

3.3 Regulation by private parties

Alternatives to professional regulation have been proposed, most of them never implemented. One solution could be independent rating agencies informed by repeat purchasers to perform the agency function on behalf of infrequent consumers.[32] Others suggest deregulation via competition that will generate quality signals with adequate liability rules and removal of informational barriers.[33]

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[29] Shaked, A. and Sutton, J., 1982, Imperfect Information, Perceived Quality, and the Formation of Professional Groups, Journal of Economic Theory 27, 170-181.

[30] Danzon, P. M., 1985, Liability and Liability Insurance for Medical Malpractice, Journal of Health Economics 4, 309-331; Danzon, P. M., 1991, Liability for Medical Malpractice, Journal of Economic Perspectives 5, 51-69; Gravelle, H., 1990, Medical Negligence: Evaluating Alternative Regimes, Geneva Papers on Risk and Insurance 15, 22-26.

[31] We should note here a recent paper by Ribstein, L. E., 2004, Lawyers As Lawmakers: A Theory of Lawyer Licensing, Missouri Law Review 69, 299-366, who provides an alternative rationale for licensing requirements in the legal profession. His argument relies on the observation that lawyer licensing encourages lawyers to participate in lawmaking by capitalizing the benefits of their law-improvement efforts in the value of the law license. State competition gives lawyers an incentive to favour welfare-maximizing state laws that make the state attractive as a location for businesses and as a forum for litigation.

[32] Stephen, F. and Love, J., 1996, Deregulation of Legal Services in the UK: Evidence from Conveyancing, Hume Papers on Public Policy 4, 53-66.

[33] Leffler, K. B., 1978, Physician Licensure: Competition and Monopoly in American Medicine, Journal of Law and Economics 21, 165-186; Klein, B. and Leffler, K. B., 1981, The Role of Market Forces in Assuring Contractual Performance, Journal of Political Economy 89, 615-641; Carr, J. and Mathewson, G. F., 1988, Unlimited Liability as a Barrier to Entry, Journal of Political Economy 96, 766-784; Van den Bergh, R. and Faure, M., 1991, Self-Regulation of the Professions in Belgium, International Review of Law and Economics 11, 165-182; Miller, G. and Macey, J. R., 1995, Reflections on Professional Responsibility in a Regulatory State, George Washington Law Review 63, 1105-1120.

There has been a recent trend to relate effective regulation of professional services to the use of litigation. The large scale of litigation in the USA allows litigants to use their financial leverage to force changes of a regulatory nature and limit professional opportunism. If appropriate regulation does not exist for professional services, litigation can provide an effective substitute when it generates a transfer of wealth from the profession (the injurers) to the consumers (the injured).[34] Even so, there are important objections to the use of litigation as a way to stimulate effective regulation: (a) Consumers do not have the appropriate information to make a comprehensive analysis as to whether or not negligent behavior, reckless attitudes, or professional malpractices were exercised (thus, litigation will usually be an inferior substitute for regulation), (b) Consumers may be opportunistic when making decisions with respect to filing lawsuits and settling out of court (e.g., nuisance litigation), thus generating too much litigation, (c) Litigation may not create adequate incentives for efficient levels of professional services since it usually aims at providing compensation, (d) Litigation may fail in achieving efficient risk-sharing (restoring pre-accident levels of utility may not be possible, specially in the context of health).

In the context of medical malpractice there is some further controversy concerning the effectiveness of litigation.[35] Doctors in areas with greater malpractice pressure tend to use more defensive medicine: better treatment and medical high productivity seems to be positively related to the willingness of patients to litigate.[36] However, once the incentives for hospitals and managed care organizations are explicitly taken into account, the empirical results are less striking. In fact, there is some debate among economists over optimal liability rules for physicians and health organizations, though most agree that tort reform and managed care function are substitutes in achieving incentives for adequate performance.[37]

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[34] Viscusi, W. K., 2002, Overview, in Regulation through Litigation, Washington, DC, AEI-Brookings Joint Center for Regulatory Studies.

[35] Kessler, D., and McClellan, M., 1996, Do Doctors Practice Defensive Medicine?, Quarterly Journal of Economics 111, 353-390; Kessler, D., and McClellan, M., 1997, The Effects of Malpractice Pressure and Liability Reforms on Physicians' Perceptions of Medical Care, Law and Contemporary Problems 60, 81-106; Kessler, D. and McClellan, M., 2002, Malpractice Pressure, Managed Care, and Physician Behavior, in Regulation through Litigation, Washington, DC, AEI-Brookings Joint Center for Regulatory Studies; Kessler, D. and McClellan, M., 2002, Malpractice Law and Health Care Reform: Optimal Liability Policy in an Era of Managed Care, Journal of Public Economics 84, 175-197, have shown that malpractice liability provides important incentives for medical care.

[36] Olsen, R. N., 2000, The Efficiency of Medical Malpractice Law: A New Appraisal, Research in Law and Economics 19, 247-273.

[37] Danzon, P. M., 1997, Tort Liability: A Minefield for Managed Care?, Journal of Legal Studies 27, 491-519; Kessler, D. and McClellan, M., 2002, How Liability Law Affects Medical Productivity, Journal of Health Economics 21, 931-955; Agrawal, G. B. and Hall, M. A., 2003, What if You Could Sue Your HMO? Managed Care Liability Beyond the ERISA Shield, St. Louis University Law Journal 47, 235-312; Arlen, J. and MacLeod, B.,

4. Regulatory instruments – what

Currently, the literature has been focusing on regulatory instruments for control and reflecting the private interest nature of their use. These instruments are: entry restrictions with consequent professional monopoly rights; restrictions on advertising and other means of promoting competition within the profession; restrictions on fees and on fee contracts; restrictions on organizational forms; and restrictions on conduct and procedures .

4.1 Entry restrictions

Entry restrictions are justified in order to assure quality of professional services but on the other hand they undermine competition by creating professional monopoly rights.[38] These restrictions require candidates to have specialized skills acquired by university[39] education and by training (for a mandatory period). These requirements of education (a specific diploma) and traineeship may be determined both by the government and the professional body.

Controls over these requirements can be exercised at three levels: (a) By defining the content of intellectual and training requirements, (b) By exercising influence over the organizations that educate and perform training of professionals[40], (c) By evaluating candidates after education and training at an exam or other type of screening device (eventually subjecting admission to some kind of *numerus clausus*). From a public interest perspective, we would expect some control over entry requirements but no strong influence over organizations that educate and perform training as well as a strict examination of candidates. Some level of education and training is indeed necessary since the relationship between human capital and high quality services is expected to be positive. Moreover, reliance on self-regulation may increase the specificity of human capital investment and individual commitment to the profession.[41]

2003, Torts, Expertise and Authority: Liability of Physicians and Managed Care Organizations, New York University Law Review 78, 1929-2006.

[38] Shaked, A. and Sutton, J., 1981, The Self-Regulating Profession, Review of Economic Studies 47, 217-234; Van den Bergh, R., 1999, Self-Regulation of the Medical and Legal Professions: Remaining Barriers to Competition and EC Law, in Organized Interests and Self-Regulation: An Economic Approach, Oxford, Oxford University Press.

[39] In Europe, after obtaining a university degree; in the United States, after completing studies in a professional graduate school; for an overview of the evolution of legal education from college to professional graduate schools in the United States, see Stevens, R., 1983, Law School: Legal Education in America from the 1850s to the 1980s, The University of North Carolina Press: Chapel Hill and London.

[40] Shepherd, G. B., 2000, Cartels and Controls in Legal Training, Antitrust Bulletin 45, 437-466.

[41] Donabedian, B., 1995, Self-Regulation and the Enforcement of Professional Codes, Public Choice 85, 107-118.

Educational requirements do vary for lawyers. A law degree used to be enough for practising law in Spain, but not in most countries. Quite extensive mandatory training periods exist followed up by examination. Making licences dependent on requirements of continuing education is not practised, but professional associations run courses and seminars in joint ventures with law schools and law firms to help updating knowledge. It should be noted, nevertheless, that in Sweden and Finland there are no restrictions on who can provide legal advice and representation. Entry regulations are not very different across our sample of countries with respect to the medical profession.[42]

Entry restrictions can also apply to para-professionals (e.g., para-medicals or other legal professionals) under the argument that they supply an inferior quality service. However, they also do it at lower prices. It turns out that the entry of low quality para-professionals could be welfare enhancing.[43] In other words, restrictions on para-professionals are expected to be undesirable unless the profits of the profession are given a sufficiently high weight in the social welfare.[44]

From our discussion it is clear that entry restrictions should be more similar to certification rather than a very comprehensive and strict examination of candidates before, during, and after education and training takes place. Notwithstanding the absence of severe restrictions on entry - this does not necessarily imply competition. Professional markets tend to be spatially localized.[45] Hence mobility might be seriously undercut and thus promote local monopolies.[46] For example, in many jurisdictions lawyers may only appear before courts in the local area corresponding to the bar to which they have been admitted. In general, in Europe, lawyers can plead before any court. There are however important limitations in the United Kingdom, Germany, and the United States.

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[42] According to Faure, M., Finsinger, J., Siegers, J., and Van den Bergh, R., 1993, Regulation of Professions, Antwerpen, Maklu, chapter on the Dutch medical profession, the Netherlands were an exception since registration was not required. As a consequence, a complex insurance system has been developed in the Netherlands to protect consumers. At that point in the book, it is argued that one of the consequences is that it was actually easier for a doctor registered in a professional body in another country of the European Union to practice medicine there than a Dutch doctor (because the insurance premium was much lower for the former). Niels Philipsen has kindly called my attention that such information is not accurate because the Individual Health Care Professions Act is from 1993, but before other regulations applied such that a license and registration system has existed in the Netherlands for a long time.

[43] Shaked and Sutton, 1981, *op. cit.* 38.

[44] Gehrig, T. and Jost, P., 1995, Quacks, Lemons, and Self Regulation: A Welfare Analysis, Journal of Regulatory Economics 7, 309-325.

[45] Stephen and Love, 1999, *op. cit.* 6.

[46] Pashigian, B. P., 1979, Occupational Licensing and the Interstate Mobility of Professionals, Journal of Law and Economics 22, 1-25.

In Europe, many of the entry restrictions are in the process of being removed. The implementation of the Establishment Directive means that it is possible for lawyers and doctors qualified in one member state to become full members of the profession in another member state without further examinations, though for example it does not apply to mobility for the legal profession within the different jurisdictions of the United Kingdom.[47] In the United States, the lack of reciprocity between state bar associations seems to lead to lower number of practising lawyers and higher incomes, though not to higher prices of legal services.[48]

European directives (namely Directive 77/249, Directive 89/48, and Directive 98/5) have been implemented in most countries for the legal profession. Entry restrictions can collide with competition law in Europe and anti-trust in the United States. For many years, entry regulations issued by professional bodies were not subject to competition authorities. In Europe, the European Court of Justice (ECJ) explicitly recognizes that professionals may be subject to higher standards of conduct, and therefore accepts some restrictions. However, whether or not competition rules apply will depend on whether the professional body could reasonably have considered the restriction essential for the proper functioning of the profession. Hence simply showing that the restriction itself is not necessary for proper functioning does not suffice for enforcing competition law.[49] As follows from the Wouters case (309/99), the ECJ precludes two ways to regulate professions. Either the government has empowered the professional body to regulate the profession without the government being fully involved, or the government retains the power to adopt professional rules. Regarding the latter, these professional rules will be considered state measures and excluded from the scope of EU competition law. The United States case law however seems to point in a different and more competitive direction by not tolerating outright collusion, for instance on prices, simply because it is the market for a professional service.

European directives (namely Directive 93/16) have been increasingly implemented for the medical profession. The medical diplomas and certificates obtained in any state of the European Union are recognized by each member state (Directive 93/16 complemented in details by Directive 97/50, Directive 98/21,

[47] Stephen, F., 2003, An Economic Perspective on the Regulation of Legal Service Markets, Evidence submitted to the Justice 1 Committee's Inquiry into the Regulation of the Legal Profession.
[48] Lueck, D., Olsen, R. and Ransom, M., 1995, Market and Regulatory Forces in the Pricing of Legal Services, Journal of Regulatory Economics 7, 63-83.
[49] Andrews, P., 2002, Self-Regulation by Professions - The Approach Under EU and US Competition Rules, European Competition Law Review 23, 281-285.

Directive 98/63 and Directive 99/46). After registration with the professional body, a physician can practice under the rules of the country (given the recognition by the ECJ of the so-called principle of double deontology). For example, given the shortage of physicians in Portugal and the high number of doctors in Spain, many Spanish doctors have made use of this European legislation to establish themselves in Portugal.

Even though entry restrictions are important and significant, entry to legal and medical professions has continued to grow in most jurisdictions. Obviously what is important is the growth in supply relative to demand.[50] Nevertheless, we should notice that some empirical evidence suggests that economic growth is negatively affected by more lawyers, the explanation being that their professional services do more redistribution than production.[51]

4.2 Restrictions on advertising

Restrictions on advertising can be justified under a public interest perspective inasmuch as they apply to other markets for goods and services. Advertising is a common method of providing information and, from a social welfare perspective, advertising should be allowed when it is productive, that is, it conveys important and relevant information to consumers concerning professional services. There is no reason to suppose that advertising of professional services should be subject to very different regulations than those applied generally to other experience and credence goods and services. This argument conflicts with the claim used by professional bodies that advertising should be prohibited because it threatens the integrity and ethical responsibility of the profession by commercializing it. According to most professional associations, competition would be contrary to the dignity of the profession.[52]

[50] Stephen, 2003, *op. cit.* 47. A quick overview of statistical data concerning professions confirms substantial differences across countries. Jurisdictions with less restrictive entry rules (Spain as well as the United States and the United Kingdom) have a substantially higher number of lawyers per capita, Greece being an exception (severe entry restrictions but high number). France, Austria and the Netherlands have a low figure, Japan having the lowest. Italy, Spain, Greece, and Belgium have the highest relative number of physicians. The United States and Norway, Switzerland and Japan have a low figure, the United Kingdom has the lowest. For details, see the full descriptive statistics available at the webpage of the author, http://docentes.fe.unl.pt/~ngaroupa/survey.doc.

[51] Murphy, K. M., Shleifer, A., and Vishny, R., 1991, The Allocation of Talent: Implications for Growth, Quarterly Journal of Economics 106, 503-530.

[52] However, as we observe in Europe, lawyers seem to be increasingly aware that dignity has a price. When Belgian lawyers seemed to lose business to Dutch and British law firms, the professional association decided to relax constraints on advertising. See Faure, M., 1993, Regulation of Attorneys in Belgium, in Regulation of Professions, Antwerpen, Maklu.

Two kinds of advertising can be distinguished, price advertising being more controversial than quality advertising. When information about price is easier to obtain than information about quality (which is true for experience and credence goods but not for search goods), increasing the availability of price advertising might discourage quality competition and encourage price competition, leading to a degradation of the average quality in the market.[53] This argument may support some restrictions on price advertising, but not necessarily banning it.

The general conclusion from empirical evidence seems to be that restrictions on advertising increase the price of professional services and that the more advertising there is the lower the price is. However, there are several articles that contradict these findings.[54] There is no systematic evidence distinguishing between the effects of the two forms of advertising.[55] Nevertheless, quality advertising is much more common than price advertising.[56]

Medical advertising is regulated in most jurisdictions, the United States and the United Kingdom being less restrictive and Portugal and Germany being the most restrictive. With the exception of the announcement of opening or closing of a practice, listing in the phonebook and the nameplate (and even this is clearly regulated in dimension and content), advertising is banned. Competitive pressure and publicity on the internet have led the professional bodies to issue new documents on publicity, clarifying the strictness of the rules justified by the so-called principle of non-commercialization of medical services and alleged protection of consumers. Advertising is allowed in Spain or Belgium as long as it does not convey false information or bad publicity to the medical profession. More difficult to understand is why in some countries physicians are not allowed to advertise, but managed care organizations are.. They operate in the same market for professional services and there is no economic reason to justify why physicians cannot advertise about price and quality but managed care organizations can.

For legal professionals, price advertising is banned in most jurisdictions, except the United States (though regulated by each state bar), under the cover that comparative advertising is strictly prohibited. Quality advertising is usually

[53] Cave, M., 1985, Market Models and Consumer Protection, Journal of Consumer Policy, 335-351.
[54] Rizzo, J. A. and Zeckhauser, R. J., 1992, Advertising and the Price, Quantity and Quality of Primary Physician Services, Journal of Human Resources 28, 381-421; Love, J. and Stephen, F., 1996, Advertising, Price and Quality in Self-Regulating Professions: A Survey, International Journal of the Economics of Business 3, 227-247.
[55] Stephen, 2003, *op. cit.* 47.
[56] Stephen, F., Love, J., and Peterson, A., 1994, Deregulation of Conveyancing Markets in England and Wales, Fiscal Studies 15, 102-118.

allowed for partnerships but not for sole practitioners. Competition within the European Union has pushed bars to relax the constraints. Overall, the regulation of publicity for legal services is still more restrictive in Portugal and France and much less restrictive in the United Kingdom and the Netherlands, Germany, Spain and Belgium being intermediate cases with a trend for deregulation.

4.3 Restrictions on fees

Restrictions on fees can be seen as a way of assuring the confidence premium for professionals. Fees can be subject to control by the profession itself, by the courts or by the government (in the case of mandatory fee schedules). Over time, in most jurisdictions, mandatory scales have been transformed into recommendations. However, in Germany legal fees are still determined by the government. For a long time, in Belgium and the Netherlands, a recommended legal fee schedule was produced by the professional body and, in Belgium, there was a recommended minimum, until competition pushed for the abolition of such rules. Medical fees are set by the government in most public health services (e.g., NHS in the United Kingdom) or by managed healthcare organizations.

Price fixing is very restrictive and not very common. Moreover, it is unclear if it enforces high quality production (it seems it would if quality were either high or low and with homogeneous consumer preferences[57]). Recommended fees suggest a more sophisticated approach to cartel-like behavior.[58]

Limitations on fee contracts (e.g., the outlawing of contingent fee contracts in the market for lawyers in Europe) are more difficult to justify on the basis of quality assurance. Moreover, the enforcement of limitations on fee contracts is costly and generates incentives for bargaining on the shadow of the law (e.g., informal contingent fees in Europe). In fact contingent fees for both legal and medical professional services would solve the moral hazard problem. The fundamental argument put against contingent fee contracts in the legal and medical professions is that they conflict with the principle that professionals should not have a vested interest in the cases they take. For example, in the case of lawyers, there could be a conflict of interest between client and lawyer over if and when to

[57] Maks and Philipsen, 2002, *op. cit.* 10.

[58] Though we would expect recommended fees to be seen as mandatory by the profession, the evidence provided by Shinnick, E. and Stephen, F., 2000, Professional Cartels and Scale Fees: Chiselling on the Celtic Fringe?, International Review of Law and Economics 20, 407-423, for conveyancing markets in Scotland and Ireland goes in the opposite direction. The authors nevertheless recognize that these markets satisfy the necessary conditions for successful deviations from collusive agreements. Another possibility is that recommended fees provide a focal point against which professionals discount thus colluding at a lower level (Stephen, 2003, *op. cit.* 47).

settle. The determination of an appropriate fee if settlement takes place would of course solve the problem. Also, we would expect well-informed clients to prefer an hourly fee contract (and avoid conflict over settlement) whereas less experienced litigants would prefer contingent fee contracts.

With respect to legal fees, in most countries prices can be freely negotiated and usually more competent lawyers charge higher fees, except in Germany. Recommended fees existed at some point in Belgium, the Netherlands, Spain and Portugal. Fees are usually based on hours worked, litigation value (except in Belgium), and complexity of the case. Contingent fees are allowed in the United States but not in Europe (the introduction of contingent fees is apparently under consideration in the Netherlands following the Engeleer case and the ruling by the Dutch competition authority NMA). Usually legal fees take the form of hourly fees or flat fees. A first exception was developed in the United Kingdom (first in Scotland, and in the 90s in England and Wales) where a lawyer receives an up-rating on the normal fee if the case is won which is not related to the value of damages (conditional fees). Similar arrangements are now being considered in many European countries.[59]

As to medical fees Germany, along with Portugal and the Netherlands has the least competitive market. Nevertheless, European countries have a powerful national health service that effectively restrains fee competition. The same does not happen in the United States, where fees can be freely negotiated.

Professional bodies can also manage the subsidies the government supplies to consumers of professional services, usually the national health service for health services and legal aid for legal services. The costs of legal aid and national health services have been growing rapidly. Usually this is caused by the increasing number of cases, rather than by the fees paid to lawyers or physicians. Though these fees are usually much lower than normal fees, the profession can use them as a way of attracting consumers. Professionals have no clear incentive to avoid using government subsidies to generate oversupply of services.

Legal aid in particular is usually run by independent government funded bodies (e.g., the Netherlands, the United States, and England and Wales), legal aid boards (e.g., Scotland and Spain) or courts (e.g., Germany), the exceptions being

[59] For a summary, see Maurer, V., Thomas, R., and DeBooth, P. A., 1999, Attorney Fee Arrangements: The United States and Western European Perspectives, Northwestern Journal of International Law and Business 19, 272-329.

Belgium, Greece and the new system in Portugal where legal aid is funded by the Government but run by the professional body.

4.4 Restrictions on organizational forms

Special regulations apply to law and medical firms. Restrictions on organizational forms are difficult to justify by reference to the public interest. If some aspects of professional services may favour partnerships rather than incorporation, we should expect the market to solve that, not the professional body.

Common organizational restrictions extend to incorporation (even where incorporation is permitted usually unlimited liability is maintained and the directors of the firm must be professionals) and multidisciplinary partnerships (i.e., involving members of more than one profession) as possible organizational forms. The usual justification for these restrictions is agency costs. Effort in production and quality are difficult to measure by others outside of the profession, thus making sole practitioners or professional partnerships the most likely form of organization where adequate incentives will be less costly to design.[60] The problem of course is that by banning other organizational forms, specialization of professionals beyond particular aspects of their service (thus lowering the cost of providing services) and economies of scope (by providing a "one stop shopping" service including lawyers, accountants, surveyors or medical doctors, dentists, and beauty consultants) are lost. For example, in the European countries where multidisciplinary partnerships are permitted, commercial law is increasingly dominated by the legal branch of the major international accounting firms.[61]

A second type of restriction on organizational form concerns the separation between the service function (assess or diagnosis the problem) and the agency function (implement the correct solution). This separation limits opportunism and creates incentives for the revelation of information.[62] However, it can be seen as a prohibition on vertical integration between different stages in production, thus generating costs in terms of technology (economies of scale) and agency costs (hold-up problem). The issue then is whether or not the benefits from formally separating the roles outweigh the costs.[63]

[60] Carr, J. and Mathewson, G. F., 1990, The Economics of Law Firms: A Study in the Legal Organization of Firms, Journal of Law and Economics 33, 307-330; Matthews, R., 1991, The Economics of Professional Ethics: Should the Professions be more like Businesses?, Economic Journal 101, 737-750.
[61] Stephen, F., 2002, The European Single Market and the Regulation of the Legal Profession: An Economic Analysis, Managerial and Decision Economics 23, 115-125.
[62] Emons, 1997, *op. cit.* 8.
[63] Stephen, 2003, *op. cit.* 47.

In the United Kingdom, as well as in Ireland and most of Australia, the legal profession has two branches: solicitors and barristers. Solicitors provide legal advice to the public and have rights of audience in the lower courts. Barristers have the rights of audience in higher courts and can be commissioned to advise solicitors, and they provide the majority of judges in the higher courts in the later stages of their career. A member of one profession cannot become a member of the other. The debate over the efficiency of separating the legal profession in the United Kingdom is inconclusive.[64]

The structure of legal firms in Europe has been changing rapidly since the 90s. Sole practitioners or small professional partnerships have been increasingly replaced by large professional partnerships, corporations (where they are allowed) and multidisciplinary organizations. The entry of foreign law firms or partnerships into the market for legal services is not helped by current regulations in some countries where the use of original denomination as well as original organizational form are only allowed under certain limited conditions.

4.5 Restrictions on conduct

The introduction of professional standards and ethics generates a number of costs, including administrative costs (defining, monitoring, and enforcing quality), compliance costs (from fulfilling professional obligations), and opportunity costs (since opportunistic behavior is restricted).[65]

Professionals are expected to pursue an agenda of minimizing these costs. They will lobby for their own quality level and standards.[66] A standard can be an effective mechanism to protect insiders from competitors by imposing their own quality standard thus reducing to zero compliance costs. On the other hand, a conflict between the government and the professions with respect to accepting and formally observing conduct rules is not likely, because professionals are usually involved in the actual formation of these rules.[67]

[64] Bishop, W., 1989, Regulating the Market for Legal Services in England: Enforced Separation of Function and Restrictions on Forms of Enterprise, Modern Law Review 52, 326-351; Ogus, A., 1993, Regulation of the Legal Profession in England and Wales, in Regulation of Professions, Antwerpen, Maklu; Bowles, R., 1994, The Structure of the Legal Profession in England and Wales, Oxford Review of Economic Policy 10, 18-33; Kerridge, R., and Davis, G., 1999, Reform of the Legal Profession: An Alternative "Way Ahead", Modern Law Review 62, 807-823.
[65] Ogus, 1994, *op. cit.* 1.
[66] Hau, H. and Thum, M., 2000, Lawyers, Legislation and Social Welfare, European Journal of Law and Economics 9, 231-254.
[67] Maks and Philipsen, 2002, *op. cit.* 10.

Administrative costs will depend on how the professional body regulates the conduct of professionals. Many forms of conduct regulation can be found in the professional rules. A code usually describes the tasks and duties of the profession and is often called professional ethics. The professional body also establishes disciplinary procedures for cases where the restrictions on conduct are violated. These rules usually define conditions under which professionals might be sanctioned and eventually expelled from the profession.

There are two reasons why the enforcement of restrictions on conduct is not expected to be high. First, it is not a problem of controlling entry, but rather of controlling exit. There are clear incentives to avoid conflicts within the profession and make exit too easy. Second, the alternative mechanisms (litigation in court) still rely too much on the profession. By controlling the production of expert witnesses (directly, by providing and managing expert witnesses; indirectly, by training them), the professional body may block any attempt to force physicians and lawyers to leave the profession for professional misconduct or gross malpractice. Naturally, in most countries, professionals are subject to contractual and extra-contractual liability, however it is difficult for judges to make a decision on medical malpractice or negligence in preparing a lawsuit if expert witnesses are not available.

Some limitations to the discretion professional bodies have in dealing with restrictions on conduct have been emerging out of international professional federations (though these are mostly recommendations) and to some extent by EU directives on professional services (not surprisingly usually perceived by professionals as intrusions into national legal and medical culture). However, the evidence is that most disciplinary actions are taken for lack of dignity or improper behavior towards other professionals rather than professional malpractice.[68]

In the United States, lawsuits for medical negligence are frequent nowadays (leading some people to talk about a medical malpractice crisis), but were very infrequent 50 years ago. Physician liability existing prior to 1960s might actually have been too low, resulting from capture and the consequent use of self-regulation to deny expert witnesses testimony in malpractice cases. However, after the 1960s, it became much easier to obtain expert witnesses due to the erosion of local medical societies in disciplining unethical practices and local rules.[69] The consequence was an explosion of litigation over medical malpractice and thus the

[68] Faure, 1993, *op. cit.* 52; Hellingman, K., 1993, An Economic Analysis of the Regulation of Lawyers in the Netherlands, in Regulation of Professions, Antwerpen, Maklu.
[69] Olsen, 2000, *op. cit.* 36.

current need for tort reform in medical negligence.[70] Liability for medical malpractice is also of growing importance in European tort litigation. Contrary to the United States experience, the medical malpractice explosion does not seem to have come to a peak yet.[71]

Liability for medical negligence is extremely complex in many European countries. First, it can be contractual (breach of contract in the private sector) or extra-contractual liability (negligence for doctors in the national health system). Whereas for contractual liability, the patient has a longer period to sue the physician after the wrongdoing, for extra-contractual liability, the same period is typically much shorter. Such liability dichotomy exists in England and Wales, but the development of expert witnessing and the structure of the legal system has not produced the chilling effect that is observed in other countries such as Portugal. The problem in some continental European countries is that whereas for doctors in the private sector, law enforcement is exercised by regular courts, doctors in the national health service are under the jurisdiction of administrative courts. Given that many physicians work for the national health service but practise privately part-time, conflicts and questions of court jurisdiction usually take place when patients want to sue doctors. Not surprisingly, lawsuits for medical negligence are rare and unlikely to succeed in such a context.

4.6 A guideline for research on rent-seeking

Table one summarizes most of the discussion we have presented. It also suggests some guidelines for identifying rent-seeking behavior on the part of the profession. We will use these results while presenting the methodology developed for comparative analysis of professions.

[70] Miller, F. H., 1997, Medical Discipline in the Twenty-First Century: Are Purchasers the Answer?, Law and Contemporary Problems 60, 31-58; Dauer, E. A. and Marcus, L. J., 1997, Adapting Mediation to Link Resolution of Medical Malpractice Dispute with Health Care Quality Improvement, Law and Contemporary Problems 60, 185-218; Sloan, F. A. and Hall, M. A., 2002, Market Failures and the Evolution of State Regulation of Managed Care, Law and Contemporary Problems 65, 169-208; Fine, D. K., 2003, Physician Liability and Managed Care: A Philosophical Perspective, Georgia State University Law Review 19, 641-685.

[71] Faure, M. and Koziol, H., 2001, Cases on Medical Malpractice in a Comparative Perspective, Tort and Insurance Law, Vienna, Springer-Verlag.

Table 1 – Self-regulation of professions

	Entry restrictions	Fee restrictions	Advertising restrictions	Organization restrictions	Conduct restrictions
Public interest	Minor	Minor	Price	No	More on substance
Private interest	Severe	Severe	Price quality	Yes	More formal

5. Comparative institutional analysis

Given the very distinct institutional details, ranking the different institutional frameworks is a difficult and controversial task. Some comparative law scholars seem to be opposed to the idea of building indicators for law and legal institutions. Obviously, some institutional details are lost and legal complexity is reduced by providing comparable indicators. Nevertheless, a comparative institutional analysis cannot be reasonably influential without providing testable results.

We construct a comparative institutional ranking of the regulation of professional services. The interpretation of the indicators should be very careful having in mind that it depends crucially on the questions included in surveys (which do not cover all institutional details) and the relative importance we give to each set of questions (we try to correct somehow for this problem by presenting different weighted averages).

The twenty-two questions are divided across the five dimensions we have considered in previous sections: entry, organization, price, advertising, and conduct regulations.[72] The process by which we construct a market failure approach index is the following: A country gets a point if the answer to the question complies with the market failure approach and zero otherwise. Complying with the market failure approach means that the answer to the question is consistent with improving market performance (as summarized in Table one).[73]

[72] The questionnaire is a modified version of Faure et. al., 1993, *op. cit.* 42, where questions concerning professional schools, management of legal aid in the case of lawyers, malpractice litigation, and independent ombudsman have been included. We also eliminated some questions that in our view were mere duplications.

[73] The full questionnaire plus related information is available at the webpage of the author, http://docentes.fe.unl.pt/~ngaroupa/survey.doc.

5.1 Our Findings With Respect To Lawyers

Tables two and three present the results for each regulatory instrument. Besides a simple index constructed by adding up the points obtained in the twenty-two questions, we have considered two weighted averages, the first where the same weight is given to each regulatory intervention, and the second where entry restrictions get 50% and each of the other four gets 12.5%. The former is constructed to overcome the problem that the number of questions varies for different regulatory interventions, the latter aims at taking into account the fact that economists tend to judge entry restrictions to be more important for the purpose of market efficiency. The interpretation of total points is straightforward: a regulatory setup has 100% (twenty-two points in total) if fully compatible with the approach described by Table one; a lower percentage (less than twenty-two points in total) indicates a regulatory setup quite different from the market failure approach.

Table 2 – Comparative institutional analysis: Lawyers

	US	BEL	NET	SPAI	NOR	E&W	GER	FR	AUS	GREE	POR	MAXIMUM POINTS
Entry	4.5	4.75	3.75	4	3.25	3.25	2.75	2.75	3	2.5	2.75	6
Fees	4	2.75	3.75	3.42	3.5	3.75	1.58	3.75	2.25	2.5	2.42	4
Organ.	1.5	2	2.5	2	1.5	1.5	2.5	1.5	1	2.33	1	3
Advert.	2	1.67	1.16	1.67	1.5	1.16	1.34	1	1.34	0.67	1.16	2
Conduct	5	4	5	2.5	4.5	3.5	3	2.5	3	3.5	2	7
TOTAL	17	15.17	16.16	13.59	14.25	13.16	11.17	11.5	10.59	11.5	9.33	22
Sum over TOTAL	77.3% (1)	69.0% (3)	73.5% (2)	61.8% (5)	64.8% (4)	59.8% (6)	50.8% (9)	52.3% (7)	48.1% (10)	52.3% (7)	42.4% (11)	100%
Weighted average	79.3% (1)	71.0% (3)	73.8% (2)	67.6% (4)	66.2% (5)	61.1% (6)	55.7% (7)	55.1% (8)	49.9% (10)	53.4% (9)	45.2% (11)	100%
Entry weighted average	77.7% (1)	74.1% (2)	69.6% (3)	67.3% (4)	61.7% (5)	58.6% (6)	52.0% (7)	51.6% (8)	49.9% (9)	49.0% (10)	45.5% (11)	100%

Table 3 – Comparative institutional analysis: Physicians

	US	FRA	BEL	E&W	NOR	SWITZ	NET	SPAI	AUS	GER	POR	MAXIMUM POINTS
Entry	4	5	4.75	3.75	2	2.25	4.5	2.75	2.75	2.25	2.25	6
Fees	3	2.2	1.9	1.7	2.3	1.7	0.4	1.9	0.9	1.5	1.7	3
Organ.	3.5	2.5	2.5	4	4	3.5	3.5	2.5	2	2	1	4
Advert.	1.67	0.67	0.67	1	1.5	1.34	0.33	1	1	0.5	0.33	2
Conduct	6	3.5	3	3	4.5	5	1.5	3.5	4.5	3.5	3	7
TOTAL	18.17	13.87	12.82	13.45	14.3	13.79	9.98	11.65	11.15	9.75	8.28	22
Sum over TOTAL	82.6% (1)	63.0% (3)	58.3% (6)	61.1% (5)	65.0% (2)	62.7% (4)	45.4% (9)	53.0% (7)	50.7% (8)	44.3% (10)	37.6% (11)	100%
Weighted average	84.7% (1)	60.5% (5)	56.3% (6)	62.4% (4)	69.9% (2)	64.0% (3)	41.9% (10)	54.3% (7)	48.0% (8)	42.5% (9)	35.7% (11)	100%
Entry weighted average	77.9% (1)	69.1% (2)	64.9% (3)	62.4% (4)	56.2% (5)	54.1% (6)	52.8% (7)	51.1% (8)	47.2% (9)	40.6% (10)	36.4% (11)	100%

With respect to lawyers, we can immediately see that the United States regulatory framework seems closer to improving market performance for legal services than most European jurisdictions essentially due to the fact that the United States is not so much regulated and is more competitive. Within the EU we identify three groups: the Netherlands and Belgium that seem to have a regulatory framework producing a result similar to the United States, a second group of jurisdictions (Spain, Norway, and England and Wales) with a performance below the United States and the Benelux countries but clearly above the performance of the third group (Germany, France, Austria, Greece, and Portugal). Germany's result is justified by excessive regulation of fees. In the case of Austria, France, and Portugal, we should add excessive restrictions on organizational forms. In the case of Greece, excessive regulation of advertising is also observed.[74]

The overall result for the United States-Europe comparison is not surprising, though the variance across Europe is somehow surprising given the fact that European law bars subscribe to a professional code (the so-called Code of Conduct

[74] It should be noticed that there are no major ranking differences across the three indicators, with the Netherlands and Belgium one, Austria and Greece two, changing positions when more weight is given to entry restrictions.

for Lawyers in the European Union). It provides minimum common standards, though it is recognized (it says in its preamble that it is not possible nor desirable) that a general unified regulatory framework should not be developed. The Code also refers to the "corporate spirit of the profession" by which a relationship of trust and cooperation should be developed (a principle regulated under the name of duty of solidarity among lawyers).

More recently, the association of European law bars has emphasized that: (a) Personal advertising and publicity is forbidden unless explicitly allowed by the local bar; (b) Contingent fees (*pactum de quota litis*) are banned (a necessary rule of the profession); (c) Multidisciplinary partnerships are restricted since lawyers cannot share honorariums and fees with other professionals unless explicitly allowed by the local bar (a consequence of the duty of confidentiality and avoidance of conflicts); (d) Lawyers should not conflict with other lawyers, but if they do, the local bar should be asked to intervene before litigation; (e) A lawyer should not accept instructions to represent a client in substitution for another lawyer in relation to a certain matter if the client has not fully paid and reimbursed the first lawyer; (f) These restrictions cannot be considered a restriction of competition under EU competition law since they are applied in the specific context of a profession; (g) Comparative conclusions with respect to different regulations across Europe should be avoided because they follow from legal and cultural intrinsic differences, and are respected by the jurisprudence of the ECJ.[75]

5.2 Our findings with respect to physicians

With respect to physicians, we can see that the United States regulatory framework again seems closer to improving market performance for medical services than most European jurisdictions. Within the EU we identify two groups: the first group (Norway, France, England and Wales, Switzerland, Belgium, and Spain slightly below) with a performance below the United States but clearly above the performance of the second European group (the Netherlands, Austria, Germany and Portugal). Most of these results are consistent with previous evaluations, with the possible exception of the Netherlands due to different weighting of aspects concerning fees and conduct. Looking at the cases of Austria,

[75] CCBE Response to the European Commission Competition Questionnaire on Regulation in Liberal Professions and its Effects, May 2003, in relation to the report by Paterson, I., Fink, M., and Ogus, A., 2003, Economic Impact of Regulation in the Field of Liberal Professions in Different Member States, Study for the European Commission, DG Competition, Vienna, Institute for Advanced Studies.

Germany and Portugal, the reasons for performing so badly are very severe restrictions on fees, advertising, and organizational forms.[76]

5.3 Relationships between indicators

Our rankings are close but do not match exactly the rankings offered at Faure et. al. (1993)[77] for three reasons: (a) They offer three indices (libertarian, efficiency, and consumer protection) that in our view are less compelling, (b) We average out questions within the survey by relevant item while they simply add all questions with equal weight (therefore the issues covered with more questions carry more weight in their final ranking), and (c) We include other aspects of the regulatory setup (professional education, professional litigation, management of legal aid, and independent ombudsman in the sample countries).

In Tables four and five we present the rankings for libertarian (Faure a), consumer protection (Faure b), and efficiency (Faure c), for a sample of five countries (England and Wales, the United States, the Netherlands, Belgium and Germany). The libertarian index measures the absence of restrictive rules, the optimal framework being free competition without any limits. One point is assigned whenever a regulation is not used in a country and zero is assigned whenever the regulation is enforced. The efficient index looks for regulations only for market failures commonly accepted in economics (therefore, this is the index closer in spirit to ours). Finally, the consumer protection index accepts regulations that a country adopts in order to minimize losses of welfare for consumers thought at the expense of freedom of competition.

Paterson et. al. (2003)[78] also provide an index of regulation for different professions based on entry (IAS entry) and conduct (IAS conduct) restrictions. They measure how much a given profession is regulated, hence producing a result somehow similar to the libertarian index (Faure a). The entry and conduct indices

[76] Contrary to rankings for legal services, it should be noticed that there are important ranking differences across the three indicators, the only consistent results being the United States as first, and Portugal as last on all three indicators. Major changes are observed for Belgium and the Netherlands (get to the third and seventh positions when entry restrictions have more weight and fall to number six and ten otherwise), France (gets to the second position when entry restrictions have more weight, but falls up to number five in the weighted average indicator), Norway and Switzerland (number five and six respectively when entry restrictions have more weight, but number two and three in the weighted average indicator). Such observations indicate that while Belgium, the Netherlands, and France seem to have less restrictive entry regulations than Norway or Switzerland, the opposite happens with respect to other regulatory interventions (namely, fees, advertising, and conduct). Minor changes are noted for Germany, Spain, and Austria.

[77] Faure et. al., 1993, *op. cit.* 42.

[78] Paterson et. al., 2003, *op. cit.* 75.

are aggregated in a composite index which we do not present since it is just the sum of the points obtained in each of the previous indices.

In Table four we can see their ranking for the legal profession (the medical profession was excluded from their project though there was the intention of carrying on such study in the original proposal) for a sample of fifteen countries (all members of the European Union by 2004). We compare their indices with our entry indicator (first line of Table two) and a simple aggregation of the other four regulatory interventions (adding-up from second to fifth lines on Table two). Notice that the conduct index takes into account fewer aspects than ours. Their ranking does not always match ours because we look at improving market performance given the existence of a market failure. Hence we look at quantitative issues (e.g., number of restrictions), but also at quality and nature of regulatory instruments and constraints.

Table 4 – Comparative institutional ranking analysis: Lawyers

	NETH	*US*	*BEL*	*E&W*	*GER*	*SPAIN*	*NOR*	*FRA*	*AUS*	*GRE*	*POR*	*SAMPLE*
Faure a)	(1)	(2)	(3)	(4)	(5)	-	-	-	-	-	-	5
Faure b)	(2)	(1)	(5)	(3)	(4)	-	-	-	-	-	-	5
Faure c)	(1)	(2)	(3)	(4)	(5)	-	-	-	-	-	-	5
Garoupa Weighted	**(2)**	**(1)**	**(3)**	**(6)**	**(7)**	**(4)**	**(5)**	**(8)**	**(10)**	**(9)**	**(11)**	**11**
IAS Entry	(3)	-	(6)	(8)	(12)	(9)	-	(14)	(15)	(10)	(10)	15
Garoupa Entry	**(4)**	**(2)**	**(1)**	**(5)**	**(8)**	**(3)**	**(5)**	**(8)**	**(7)**	**(11)**	**(8)**	**11**
IAS Conduct	(5)	-	(6)	(4)	(10)	(12)	-	(9)	(13)	(15)	(8)	15
Garoupa Others	**(2)**	**(1)**	**(4)**	**(5)**	**(9)**	**(6)**	**(3)**	**(8)**	**(10)**	**(7)**	**(11)**	**11**

Notes: In brackets, the ranking position.
IAS also includes Finland (1 and 1), Sweden (2 and 2), Denmark (3 and 3), Ireland (5 and 6), Italy (7 and 14), and Luxemburg (13 and 10).

Notably, five countries have a different performance in our ranking than previous exercises. Spain, France and Greece perform considerably better in our assessment, while Portugal and England and Wales do less well. The reason relies on the different weighting of the aspects of the regulatory setup, in particular we pay more attention to structure of law firms, advertising, and conduct than Paterson

et. al. (2003)[79]. With respect to Belgium, the differences are essentially due to the recent changes operated in the regulatory setup for legal professional services in this country.

In Table five, we have the comparative institutional analysis for physicians. Our rankings are fairly consistent with previous research, with a minor exception of the Netherlands performing somehow less well in our ranking than in Faure et. al. (1993)[80] for reasons explained before (also notice that if we look at the entry indicator rather than the weighted average this problem disappears). US is consistently first in the different indicators.

Table 5 – Comparative institutional ranking analysis: Physicians

	US	*E&W*	*BEL*	*GER*	*NETH*	*NOR*	*SWI*	*FRA*	*SPAIN*	*AUS*	*POR*	*SAMPLE*
Faure a)	(1)	(1)	(4)	(5)	(3)	-	-	-	-	-	-	5
Faure b)	(1)	(2)	(3)	(5)	(4)	-	-	-	-	-	-	5
Faure c)	(1)	(1)	(3)	(5)	(4)	-	-	-	-	-	-	5
Garoupa Weighted	**(1)**	**(4)**	**(6)**	**(9)**	**(10)**	**(2)**	**(3)**	**(5)**	**(7)**	**(8)**	**(11)**	**11**

Note: In brackets, the ranking position

6. Conclusions

In this paper we have presented a systematized critical overview of the economic literature on regulation of professionals, with a special application to legal and medical services. A comparative analysis of medical and legal professional bodies has been developed for US and Europe. A set of indices to measure quality of the regulatory set-up has been constructed where aspects related to entry, fees, organizational forms, advertising, and conduct restrictions are included. A country getting a higher number of points is interpreted as having a professional regulatory framework more consistent with improving market performance (given the existence of a market failure).

The United States perform well in our study, closely followed by Norway, England and Wales, and then by Belgium, France, and Spain. Austria, Germany and Portugal perform less well, but evidence suggests that for legal services they are not too far away from the EU average whereas for medical services they are

[79] Paterson et. al., 2003, *op. cit.* 75.
[80] Faure et. al., 1993, *op. cit.* 42.

clearly below average. The Netherlands, for the medical profession, ranks more poorly whereas for the legal professions it performs quite well. Switzerland also performs fairly well for the medical profession (unfortunately no information was obtained for the legal profession) whereas Greece performs poorly for the legal professions (unfortunately no information was obtained for the medical profession).

Some policy conclusions can be extracted from the exercise with respect to the European Union. For the legal profession, the European Union should look at Belgium and the Netherlands as good examples of regulatory setups. With respect to the medical profession, Norway, Switzerland, and England and Wales[81] seem to be the examples to have in mind. Altogether, it should be noticed that the United States performs extremely well for both professions. Finally, in a quick comparison across professions (some care should be exerted in drawing policy conclusions from a direct comparison of indicators for the legal and medical professions), it seems that on average European countries have less efficient regulatory setups for the medical than for the legal profession.

[81] Although Davies, A. C. L., 2000, Don't Trust Me, I'm a Doctor: Medical Regulation and the 1999 NHS Reforms, Oxford Journal of Legal Studies 20, 437-456, raises important questions concerning the effects on the quality of the regulation of the medical profession by the 1999 NHS reforms.

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