



Theory and Evidence on the Regulation of the Latin Notary Profession

A Law and Economics Approach

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Prof. Dr. Roger Van den Bergh
Corresponding author: r.vandenbergh@frg.eur.nl

Prof. Dr. Yves Montangie

Erasmus Competition and Regulation institute (ECRi)
Erasmus University Rotterdam
Room H7-25
P.O. Box 1738
3000 DR Rotterdam
The Netherlands
Tel.: +31 (0)10 408 2220
Website: www.ecri.nl

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GLOSSARY

Credence good

A good the quality of which cannot be assessed by the consumer thereof, neither before, nor after purchase or consumption. Since the consumer does not possess the necessary information, he has to rely on the assurance by the seller of the good that its quality is sufficient. Professional services often are credence goods. For example, the quality of heart surgery by a certain surgeon cannot be assessed by his patient. He has to rely on the surgeon's assurance that the surgery was well performed.

Experience good

A good the quality of which cannot be assessed by the consumer beforehand, but only after purchase and consumption of the good. For example, a consumer can only assess the quality of canned food after he has purchased and opened the can.

Externalities

A cost (negative externality) or benefit (positive externality) that is enjoyed by certain persons and that is caused by a transaction in which they were not involved. The parties to the transaction may not take these externalities into account. Therefore, their transaction may cause undesirable negative externalities (for example, setting up a factory without regard for the consequences for third parties may cause environmental damage to the detriment of others). Conversely, a certain transaction between parties may, while this is not immediately the intention of the parties, cause certain benefits to third parties (for example, an education offered by a school to individual students will not only benefit these parties but will also benefit future employers who can hire well-educated and productive employees).

Market for lemons

A market in which, due to certain information problems, only lower quality goods threaten to be sold. The concept was developed by Akerlof (1970) who illustrated this by a model of the market for used cars. Some used cars are of good quality, while some other cars are of low quality ('lemons'). While the sellers of used cars have perfect information on their products, consumers do not have the necessary information to assess the quality of used cars and will base their decision to purchase mainly on prices. Therefore, it is likely that only cheap, low quality cars will be sold while sellers of higher quality cars with a higher price will be driven out of the market. This process is also known as adverse selection.

Moral hazard

Moral hazard is a problem common in principal-agent relationships characterised by information problems. The provider of a certain good (agent) is supposed to act in the best interests of his client (principal). However, when the principal lacks perfect information, he may not be able to indicate the desired price-quality level of the service he desires. This may incite the agent to display opportunistic behaviour. He may be inclined to over-supply quality in order to charge higher prices, even if his client would be better served with a lower quality at a more reasonable price. He may even supply services his client does not need (supplier induced demand).

Multi-disciplinary practice (MDP)

Any partnership, professional corporation, other association or entity in which members of different professions work together on a regular basis. For example, an MDP may consist of lawyers and accountants who decide to operate a common practice, in which they jointly purchase an office space, organise a library and hire supporting staff.

Profession, liberal profession

There exists no clear definition of the term 'profession' or 'liberal profession'. In this report, the term is used to indicate occupations that involve specialised skills that are partially or fully acquired by intellectual training. They are often characterised by information problems causing the consumers thereof to have difficulties in assessing the quality of the services provided. The services provided by professionals therefore call for a high degree of integrity and are characterised by direct or fiduciary relations with clients. This is guaranteed by government regulation, self-regulation or self-regulation under government control.

Public good

A good that can be consumed by everyone, even those who do not ask and pay for it, and for which the producer of the good cannot exclude non-paying beneficiaries. A classical example is national defence: some may not be willing to contribute to the organisation of the army, but will benefit from it since the national forces contribute to maintaining peace and order on the national territory and defend it against attacks from outside to the benefit of all citizens.

Regulatory capture

The influence exercised by a regulated industry or profession on the regulatory agency it is supposed to be regulated by. Regulated professions or industries will normally try to influence their regulators to their own benefit. Under certain circumstances, such influence may cause the regulatory agency to act wholly or partially in the interest of the regulated sector, rather than in the interest general public interest as it is supposed to.

Rent seeking

A situation in which a professional body is supposed to control the members of a profession and to regulate this profession to the benefit of consumers and society a whole, but where resources are instead allocated to promote the economic interests of the members of that profession. In doing so, rent seeking may lead to a loss of social welfare.

Specification standards

Standards that impose certain production methods or materials onto suppliers. For example: a government may decide to regulate which safety devices have to be built into a lawn mower to prevent accidents.

Target standards

A standard by which the quality of a certain good is not regulated beforehand, but by which ex post liability is imposed onto the producer of the good in case its poor quality causes harm to the consumer thereof. For example: a liability rule which does not specify what result a certain medical treatment should have, but does impose liability onto the physician involved when it seems that he has acted in negligence of common medical standards or not taken the necessary steps or precautions to prevent any harm to his patient.

INTRODUCTION

1. The need for regulation of professional services markets

There are a number of differences between professions and other occupations. The profession is an occupation that involves specialised skills, which are partially or fully acquired by intellectual training. Buyers of professional services often face difficulties to assess the quality of the services provided. In addition, the service provided by a profession calls for a high degree of integrity, characterised by direct or fiduciary relations with clients. This description of a profession is different from the one used in the IHS report¹, which does not provide any definition of professions but merely states very generally that “professional services are distinguishable from the general category of services in the economy” and that “the distinction rests primarily on the historical development of the occupations at the heart of these services” (p. 7). This formulation gives the impression that professional services primarily differ from other goods/services due to their historical development. Such reasoning would also make it possible to argue in favour of regulation of traditional crafts and trades, such as jewellery. This is methodologically false; one cannot logically jump from the historical development of these markets to the suggestion that their existence is solely justified by this historical process, as if it were some kind of historical anomaly that created and supports the existence of these markets.

The definition of a professional service demonstrates some characteristics of the market on which these services are offered and acquired. Since it involves specialised skills, it is safe to say that the information of the consumer concerning the particular service will be at best sketchy. There exists an unbalance in information between the provider of the service – who may assess the quality of his service – and the consumer, who has no information about the quality of the service he is about to acquire, and only in the case of experience goods can access information of the service he bought. This is a far cry from the ideal of perfect information, necessary for perfect competition and its blessings for social welfare. In relation to this specialisation, one has to realise that the services offered by professions have so called credence qualities, or – at best – experience qualities. Credence goods are goods the quality

¹ IHS (2003).

of which can neither be assessed before, nor after the consumption of the said good. This assessment requires specialised skills or knowledge, which the consumer in the market of some professional services typically lacks. Experience goods exhibit less serious information problems: consumers cannot assess the quality of the provided service *ex ante*, but can appreciate the quality *ex post*.

Economic theory has shown that this information asymmetry between provider and consumer can culminate in a so called 'market for lemons'. Since the consumer cannot judge the quality of the service he will acquire, he will not be willing to pay a high price for high quality. As a result, providers of higher quality (with a higher price) are driven out of the market, which results in a market with sub-optimal quality services. This process is also known as adverse selection.

Another problem resulting from the information asymmetry is moral hazard. The moral hazard concept signifies that there is a discrepancy between the goals of the agent and the objectives of the principal. The provider of the service (agent) is supposed to act in the best interests of his customer (principal). However, since this principal cannot express the price-quality relationship he desires, the agent has every incentive to over-supply quality in order to charge higher prices, even if his client would be better served with a lower quality at a more reasonable price. The same goes for supplying services the client does not need (supplier induced demand).

Apart from the information problem, one has to take into account that professional services generate externalities, i.e. effects (positive or negative) on third parties. This is a feature not normally associated with perfect competition – in a perfectly competitive market, all externalities are internalised, i.e. the price at which a good is offered incorporates the negative (or positive) effects on possible third parties. When a professional service of sub-optimal quality is offered, the negative effects will not only harm the consumer of the service, but also other individuals, not involved in the transaction. Again social welfare is decreased.

Lastly, it is important to notice that the services offered by professions often consist of providing information. This has two, seemingly opposite, effects. First, this information is often tailored to the need of the specific consumer. Thus, one could argue that the service provided is not homogeneous (a prerequisite for perfectly competitive markets), but

heterogeneous. Second, information has a tendency to be a public good, i.e. a good that can be consumed simultaneously by everyone, even by persons who do not pay for it. The drawback of public goods is that they tend to be under-produced, since a lot of consumers will not pay to acquire the good in question, effectively reducing demand to a sub-optimal level.

These market-failures (information-asymmetry leading to moral hazard and adverse selection, externalities and public goods) are to be cured in order for the market of professional services to be a more efficient market.

2. The specific need for regulation of the Latin notary profession

An analysis of the function of Latin notaries reveals additional arguments in favour of regulation. The Latin notaries provide two categories of services: on the one hand, they provide certain public services and on the other hand they provide legal services in a broad sense. The provision of the public services is solely entrusted to Latin notaries – the group as such has a monopoly right to exercise certain activities. The legal services in the broad sense, on the other hand, may well be provided by other legal professions, such as barristers, lawyers, tax advisers and sometimes even accountants. The latter aspect of the Latin notary function is sensitive to competition by other professions.

The public service of the Latin notary has been enacted in the law. In several countries, governments have made the mediation of the Latin notary mandatory for certain transactions. The common denominator of these transactions is that they tend to have a substantial influence not only on the parties involved, but also for third parties (and society in general). Examples include the acquisition of real estate, marriage contracts, and the creation of legal persons.

Through the mandatory mediation of a Latin notary, the government aims at minimising the risk that transactions cause legal uncertainty, and thus attempts to minimise the negative effects on welfare. The Latin notary acts as a compliance officer who will exert an *ex ante* control of the quality of the transactions. In this way *ex post* transaction costs, such as litigation costs are reduced or even totally eliminated. Obviously, this creates benefits for the

parties involved, but the mediation of the Latin notary transcends this micro-level, which is why it is classified as a public function. There are positive externalities for the community as a whole: the government saves resources, otherwise engaged in a more extensive judicial apparatus, and third parties have more and correct information concerning a certain transaction. The importance of well-defined and enforceable property rights for the development of market economies has been demonstrated by studies investigating the causes of under-development in third world countries (see Hernando de Soto's *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else*). Authenticating legal documents on transfer of property is crucially important for the well-functioning of the economy as they determine ownership of valuable assets and connected liabilities. Hernando de Soto has argued that the real cause of poverty in Eastern Europe and Latin America is not lack of money, but the absence of a reliable registration system for landed property which impedes financing of real estate transactions².

The Latin notary also, as part of his public function, acts as a registrar of official documents; he carries the obligation to undertake the necessary steps for the recording and registration of the documents he authenticates in a wide variety of legal matters. Above that, Latin notaries commonly have (and are forced by law to have) own large archives, in which official documents are stored and made available to certain individuals. In addition, they provide information for archives held by public authorities.

The key characteristic of this public function is the impartiality of the Latin notary. In order to guarantee the reduction of transaction costs by the *ex ante* control exerted by Latin notaries, the Latin notary must be free of bounds and independent of the respective parties.

3. Criticisms of (self-)regulation

By imposing quality standards to suppliers of professional services, in addition to liability rules, the regulator can minimise effectively the negative effects of the information asymmetry (moral hazard and adverse selection). By imposing the obligation to use certain professional services under specific circumstances, the regulator can ensure that negative

² de Soto (2000)

externalities are avoided and positive externalities are created and the public good of information is produced.

However, regulation is not without its critics. First, it is argued that anti-competitive measures may lead to a loss of welfare. Some regulatory measures are, strictly speaking, anti-competitive measures:

- imposing quality standards is in fact the creation of an entry barrier, thus lowering the number of potential providers of legal services,
- forcing consumers to use professional services under certain circumstances – even if in fact, they prefer not to acquire those services – can be qualified as a measure to artificially raise demand.

This suggests that regulation is a dangerous thing: on the one hand it is necessary for the market of professional services to work at all but, on the other hand, it obstructs competition. Establishing a workable level of competition requires, in short, striking a balance between these two opposite effects of regulation.

Second, because of the entry barriers created to achieve a high quality standard, it may be possible for the members of the profession to raise prices for their services and achieve higher economic rents. They are not restricted by the threat of entry of new producers as a result of the higher prices, since access is effectively blocked by the entry barrier.

This can be enhanced by the creation of a professional body, composed of members of the profession, which controls entry requirements. Although there may be good reasons to let such a professional body monitor the members of the profession and regulate the profession (i.e. self-regulation of the profession), it is quite possible that these professional bodies will promote their members' interests beyond the level required to ensure high quality, thus effectively creating extra economic rents for their members. The process of allocating scarce resources to the pursuit of economic rents is called 'rent seeking'. Needless to say, rent seeking activity should be avoided at all costs, since it decreases social welfare.

Moreover, the professional body is in a position to lobby with the government in order to influence the outcomes of regulation. This is called 'regulatory capture' and constitutes a form of rent seeking. It cannot be excluded that the professional body will try to influence the

government to the main benefit of its members, instead of society as a whole. This is more likely to succeed if the professional body represents a relatively small number of members, who agree on a finite number of goals to achieve, with relatively low costs of professional organisation and where the costs of their actions are spread over a large population (thus ensuring that no organised opposition will arise to block their efforts in getting the favourable legislation).

However, the above criticisms do not justify the conclusion that self-regulation should be avoided³. Self-regulation has a number of definite advantages over regulation by the government. First of all, the relation government-profession suffers from the same information asymmetry as the relation consumer-producer. It is difficult – i.e. costly – for the government to acquire the information, necessary to regulate efficiently. Second, in the case of government regulation, the costs of monitoring, controlling and regulating will be spread among the general public. In the case of self-regulation, these costs are borne by the professions themselves. And finally, self-regulation is more flexible than government regulation, which cannot react as quickly to changing conditions and may therefore hamper innovation. These disadvantages of government regulation do not exist for professional organisations: they have easy access to the necessary information, can spread the costs of regulation among their members and can quickly react upon changing conditions. Thus, self-regulation is generally more efficient and less costly than regulation by the government or the creation of an independent controlling body.

Furthermore, it is important to stress that there is little empirical material to corroborate the rent-seeking hypothesis. The IHS report itself admits this and is plagued by methodological and logical flaws when interpreting the sketchy data the researchers were able to gather. For example, in the report, the ‘volume’ of legal services is used as a proxy for profits earned and on that basis conclusions are drawn with respect to the success of rent-seeking efforts in certain professional services. It is all too easy – and scientifically false – to draw the conclusion that where there is a high volume and a relatively small number of professionals, they must be overcharging. It is, for example, possible that the smaller number of professionals in a given member state works harder than their counterparts in other member

³ Moreover, some of the disadvantages of ‘pure’ self-regulation may be alleviated by organising self-regulation under government control.

states, thus reaching a higher volume, regardless of a lower price per service. An overview of the major criticisms of the IHS Report is provided in chapter 2.

The strongest opponents of self-regulation argue that the public function of a Latin notary could be organised in a different way. In their view, it is feasible to organize a mandatory registration by a government agency when certain transactions occur. However, one can ask if this would be as cost-efficient as the present mediation by Latin notaries. First of all, the Latin notary costs are primarily borne by the parties in the transaction; if a government agency would intervene, it is possible that (some of) the costs will be spread over society (taxes and government wages). Another argument is related to the incentives to work efficiently. A Latin notary may be seen as an individual enterprise, which is more likely to operate efficiently than a government agency. Latin notaries have more incentives to do so: the more efficient a particular notary office operates, the better its competitive situation towards other notary offices. Of course, another option would be to entrust other legal professionals with these public functions, e.g. lawyers who could be given the authority to control the legality of certain documents, just as Latin notaries have now. This has the disadvantage that monitoring costs may substantially increase. Latin notaries are a defined, identifiable group, since they are specially appointed by the government. Lawyers are not such a well-defined group and, moreover, lack the necessary impartiality-characteristics engrained in the Latin notary function. The risk that a lawyer would take sides in the control on the legality of documents, is more prominent than is the case with Latin notaries, since the function of a lawyer is primarily to take (and defend) a certain viewpoint of a certain party. The need for impartiality is the main reason why Latin notaries as a group have – with the exemption of other legal professionals – the authority to verify and certify the legality of certain legal documents.

In conclusion, the market for professional services needs regulation to a certain extent, in order to overcome the problems of information asymmetry leading to adverse selection and moral hazard, externalities and public goods characteristics. However, regulation can also encourage monopolistic behaviour, rent seeking, and regulatory capture by the professional body. The main question is not whether there is competition between providers of legal services (there is), but how much (and if there is enough).

4. The European Commission's policy on professional services and the IHS report.

In March 2000, the Lisbon European Council adopted an economic reform programme with the aim of making the EU the most competitive and dynamic knowledge-based economy in the world by 2010. The European authorities acknowledge that professional services, such as those provided by lawyers, Latin notaries, accountants, architects, engineers and pharmacists, can deliver an important contribution in achieving this aim.

However, in most EU countries those professions are subject to regulations regarding entry into the profession, fees, advertising, monopoly (exclusive) rights and rules on business organisation (such as restrictions on multi-disciplinary co-operation). Such measures can under certain circumstances be in breach of the EU's competition rules. Self-regulatory measures can under some circumstances be qualified as agreements between undertakings or decisions by associations or undertakings that distort competition on the common market or a substantial part thereof. These are prohibited by Article 81(1) of the EC Treaty. Regulatory measures that have been adopted and/or imposed by the government of a member state can be in breach of the said Article 81(1) combined with other Treaty provisions (Art. 3(1) (g) and Art. 10(2)).

Therefore, the regulation of liberal professions has since long been under fire from the European competition authority, the European Commission and its Directorate-General Competition. The Commission has already undertaken individual actions against certain types of regulations (fee and advertising restrictions, bans on multi-disciplinary practices) in certain professions⁴. Several national competition authorities have followed the Commission's example.

In a speech on 21 March 2003⁵, Competition Commissioner Mario Monti announced that the Commission would launch a stocktaking exercise for professional services. The aim of this exercise would be to gain insight in the potential (negative) impact of professional regulations and their possible justification. As a part of this exercise, DG Competition published an independent study by the Institut für Höhere Studien (Institute for Advanced Studies - IHS) of

⁴ For references to most of these cases, see the Commission report at p. 18 and further (European Commission, (2004).

⁵ Monti (2003).

Vienna, Austria on the regulation in the professions. At the same time, all interested parties were invited to comment on these initiatives.

In October 2003, DG Competition published a summary of the responses and an overview of regulations in the EU Member States and hosted a Conference on this issue in Brussels. At that occasion, Competition Commissioner Monti announced that the Commission would produce a Communication on this subject by early 2004. This Communication was published on 9 February 2004⁶.

In its Communication, the Commission acknowledges that the existence of asymmetry of information, externalities and public goods in professional services may necessitate some level of regulation. The Commission therefore argues that some exceptions to the competition rules should be allowed⁷. It explicitly refers to the decision of the Court of Justice in the *Wouters* case⁸. In that decision, the Court stated that certain types of regulation, even when they restrict competition, may be necessary for the proper functioning of certain professional services and should therefore be permitted.

On the other hand, the Commission stresses that professional regulation may indeed eliminate or limit competition between professionals. In the Commission's view, this may lead to lower efficiency and innovation and reduce the incentives to lower prices and to increase quality. The Commission claims that "a significant body of empirical research shows the negative effects that excessive or outdated restrictive regulations may have for consumers".

⁶ European Commission (2004).

⁷ On p. 18 of its Communication, the Commission also refers to the case law of the Court of Justice that excludes the exercise of public authority from the scope of the competition rules. The landmark case in this regard is the decision of the Court of Justice of 19 January 1994, case C-364/92, *Eurocontrol*, ECR 1994, 43. Certain professions may engage partially in an economic activity and partially exercise public authority. The competition rules will then not be applicable to the activities related to the exercise of public authority. This may be of particular relevance to the profession of the Latin notary. However, an analysis of the relevance of the 'Eurocontrol' doctrine to the notary profession requires a strictly legal analysis which falls outside the scope of this report. The same goes for the analysis of the impact of free movement rules on activities related to the exercise of public authority. It is noteworthy however that the rules on the free establishment in the EC Treaty also provide an exception for 'activities which [...] are connected, even occasionally, with the exercise of official authority' (Art. 45 EC Treaty). Being an exception to the fundamental principles of free movement, this provision is interpreted narrowly in the ECJ's jurisprudence. It only allows an escape route for those services that are directly and specifically connected with the exercise of public authority.

⁸ European Court of Justice, Decision of 19 February 2002, case C-309/99, *Wouters et al.*, ECR 2002, I-1577, rec. 97.

Therefore, while the Commission acknowledges that some regulation of the professional services markets will remain necessary and justified, it urges for any restrictions on competition in these regulations to be reviewed and, where they are not objectively justified, removed or replaced by less restrictive rules. According to the Commission, a proportionality test should be used to identify which regulatory measures are objectively necessary to attain clearly articulated and legitimate public interest objectives, without imposing restrictions on competition that go further than strictly necessary.

The Commission also announced that it would report in 2005 on progress in the elimination of anti-competitive and unjustified regulatory measures. A second Communication on competition in the liberal professions was published on 5 September 2005⁹.

5. Aim of this report.

We applaud any scientific discussion on the benefits and disadvantages of professional regulation. In our view, only thorough scientific research based on sound theory and supported by empirical evidence can be a solid basis for any policy change in this regard. Therefore, the Commission's initiative is most welcome as it may urge both the community of professionals and scientists to shed light on some issues of regulation that have not been (thoroughly) researched so far.

We believe that the regulation of the Latin notary profession and its effects is most certainly a topic that needs further research. The activities of Latin notaries do not fully correspond to the common definition of a profession. From the above, it is clear that the activities of Latin notaries can generate certain specific positive externalities that are not inherent in other professions. It should be investigated whether this difference might explain why only the Latin notaries (and not the remainder of the legal profession) act as public officials. Nevertheless, there have only been a few scientific studies on the benefits and/or disadvantages of the Latin notary profession. The large majority of these studies are mainly theoretical and do not offer empirical evidence on the actual costs and benefits of the Latin

⁹ COM (2005) 405 final

notary profession and the regulation thereof in its current status. In our view, any additional research into this subject will therefore be most useful.

We feel that such research should meet a number of conditions in order to form a solid basis for policy changes. First of all, such research should take account of all theoretical arguments in favour of and against regulation, also keeping in mind the specificity of different types of regulation and their consequences. Secondly, such research should – obviously - also take account of the specific characteristics of the Latin notary profession. Thirdly, such research would have to establish to what extent the theoretical arguments have been confirmed by empirical evidence. In short: any policy changes should be based on a well-balanced and well-founded scientific approach.

In its Communication, the Commission at first glance seems to adopt such an approach. While it criticises certain types of regulation for certain professions for their anti-competitive effect, it also admits, referring to the *Wouters* case, that certain types of regulation may be necessary to guarantee the good functioning of certain professions. The Commission also acknowledges that certain regulatory measures may be in the public interest.

Nevertheless, some elements in the Commission's Communication seem to suggest that its approach to the issue of professional regulation, specifically in the Latin notary profession, may threaten to present some shortcomings. Firstly, the Commission seems to rely quite heavily on a limited amount of existing empirical evidence on the effects of professional regulation to support the view that professional regulation mainly has negative effects. In that regard, in its Communication, the Commission often refers to the results of the IHS study. While one could admit that the IHS study offers interesting food for thought, one also has to take account of the fact that this study has already been criticised on a number of grounds, both conceptual and methodological. Further, the Commission's conclusion that "a significant body of empirical research shows the negative effects that excessive or outdated restrictive regulations may have for consumers" seems too general. It does not take into account a number of empirical surveys that either cast doubt on this conclusion or - conversely – show that regulation can also have positive effects.

Secondly, neither the IHS study nor the Commission's Communications seem to take sufficient account of the specificity of the Latin notary profession. While the IHS study

acknowledges that Latin notaries partly perform a public task, it does not offer any specific evidence on the possible advantages of the Latin notary profession but mainly groups Latin notaries together with lawyers to form the broader category of 'legal services'. The Commission distinguishes Latin notaries from lawyers but does not pay sufficient attention to the specific benefits that may be created by the Latin notary profession and the regulation thereof in its current status.

In the light of the foregoing, this report aims at sketching the 'broader picture' for a scientific approach of the regulation of the Latin notary profession. To that end, it will try to put the findings of the IHS report and the Commission's Communication into this broader perspective.

The first chapter of this report will give an overview of the main tasks of the Latin notary. This will allow us to further elaborate on the reasons why regulation of the Latin notary profession is needed. Both the need to cope with information asymmetry in markets for professional services and the provision of public goods may justify restrictions of competition. In particular, Latin notaries provide certain services that not only benefit the parties to a certain transaction, but also a wide variety of third persons and society as a whole. In this way, the Latin notary profession generates substantial positive externalities and thus increases legal certainty.

The second chapter will present theoretical arguments and empirical evidence on the effects of professional regulation. This chapter will first summarise the criticisms to the IHS study that have been forwarded. Further, this chapter will discuss the main arguments in favour and against the most common forms of professional regulation (regulation granting monopoly rights, restrictions on entry, fees, advertising and forms of business) to highlight the necessity of a well-balanced approach. This chapter will also offer an account of a number of empirical studies which either confirm or rebut these theoretical arguments. It is submitted that this overview will show that empirical evidence on the effect of professional regulation is, in its current status, at best sketchy and fragmentary and does not allow drawing general conclusions on its positive or negative effects, especially not in relation to the Latin notary profession. Finally, an overview will be given of the empirical work conducted so far on the liberalisation of the Dutch notary profession. The Netherlands are a rare example in having been able to reform its notary profession. An evaluation of the effects of the Dutch

deregulation program is therefore highly informative for policy makers in other countries that may consider reforms along the lines suggested by the European Commission. However, in the view of the authors of this report, also the empirical work on the Dutch experiment does not allow any definite conclusion on the desirability of (specific forms of) the regulation of the notary profession.

Finally, the conclusions will summarise the main findings of this report. This final part will also contain an outlook, which will indicate along which lines future empirical work could be carried out. The goal of such studies (in particular analyses of the social benefits and costs of the mandatory intervention by a Latin notary) should be to provide better evidence allowing informed policy decisions on the reform of the Latin notary profession.

CHAPTER I - Tasks of the Latin notary and the need for regulation

In this chapter we will describe the tasks of Latin notaries. By closely analysing the specific characteristics of the Latin notary profession, the reasons of potential market failures and the ensuing need for regulation will become clear. First, regulation is needed to overcome problems of asymmetric information. Second, Latin notaries provide certain services the consequences of which exceed the interests of the parties involved in these services and benefit society as a whole. The most important positive externality generated by the Latin notary profession is legal certainty. In a competitive market, positive externalities may not be provided, since none of the parties involved in a transaction can appropriate these benefits and will therefore feel no incentive to guarantee the production thereof. Therefore, regulation is needed to make sure that an optimal level of legal certainty is provided.

1. Tasks of Latin notaries

Latin notaries provide a varied and complex number of services. The exact scope of Latin notary activities may vary from one country to another. However, these services can generally be grouped into two main categories of services. On the one hand, the Latin notary is entrusted by the government with the task of drafting and authenticating documents, of undertaking certain steps to ensure the recording and registration of these documents, and of keeping archives of all the documents that were authenticated by him. This is the notary's main task. Apart from that, the Latin notary in subsidiary order offers legal advice on a wide variety of legal issues.

The Latin notary's main task in relation to authentic documents can be divided further in three categories and will most commonly include the following services:

Services relating to the transfer of real estate property

- Drafting and authenticating contracts relating to the transfer of real estate property (conveyancing)
- Drafting, authenticating and registering mortgages
- Organising public sales (by auction) of real estate
- Dividing property rights (for example dividing the property rights to a certain estate into apartment rights)
- Drafting and authenticating lease contracts
- Providing advice on these issues

Services relating to family practice

- Drafting or modifying marriage contracts and partnership contracts
- Drafting or modifying and authenticating wills
- Acting as a mediator in family law matters (e.g. divorces with mutual consent)
- Settlement of inheritances
- Drafting and authenticating acts of gift
- Ensuring that the rights of minors or legally incapacitated persons are guaranteed in transactions effectuated with his assistance

Services provided for enterprises and businesses

- Establishing and modifying the articles for corporations
- Establishing and modifying the articles for foundations, trusts and associations
- Offering guidance for the transfer and creation of shares
- Offering guidance for mergers and scissions of corporations
- Providing advice on shareholders' agreements

As said, next to these three main areas of activity, a Latin notary can also provide legal advice on a wide variety of legal issues, including:

- Providing advice on taxation issues
- Providing advice on estate planning
- Providing advice on different types of contracts

- General legal advice, both on national and international law issues

2. Regulation of Latin notary services

There exist some general regulatory measures that regulate the entry into the Latin notary profession. Only persons who have complied with these requirements are allowed to become a member of the professions and are then entitled to use the reserved title of ‘notary’. For example, in most countries, Latin notaries will have to have undergone a specific training and obtain certain diploma’s (a law degree and possibly a postgraduate degree in notary studies). Further, in most countries, the Latin notary profession is only open to persons who have gained a specific professional experience and/or taken specific examinations. In most countries, the number of Latin notaries is also limited and may be distributed alongside certain geographical delimitations. Latin notaries are in all cases nominated by the government.

Furthermore, Latin notaries are subject to a number of general deontological rules such as the obligation to act neutrally and impartially, the duty of professional secrecy save certain legal exceptions, and the obligation not to take part in transactions in which they have a conflict of interest.

It is important to stress that this regulation is relevant for all of the Latin notary’s fields of activity, including the provision of legal advice where his mediation is not mandatory. However, the ‘hard core’ of the services provided by Latin notaries, i.e. the public services, are the subject of additional specific regulation that can be summarised as follows.

First of all, for some services a monopoly right has been granted to Latin notaries. This is, for example, the case for conveyancing services in most countries and, in many countries, for the mediation in the incorporation of businesses, drafting and authenticating marriage or partnership contracts and wills and settling inheritances. For these services, a mandatory mediation of a Latin notary is provided; demand for these services is therefore compulsory.

Secondly, however, this monopoly right is in most cases coupled with the duty of the Latin

notary to provide these services to whoever requests them. In principle, a Latin notary cannot refuse to provide these services, except in certain extraordinary circumstances. Furthermore, Latin notaries are presumed to be able to offer all of these services and are not allowed to limit themselves to a certain specialisation.

Thirdly, in many countries, the fees for the services for which a mandatory mediation by a Latin notary exists, have been regulated (fixed, minimum, maximum or advised fee).

Lastly, and most importantly, the acts that have been authenticated by Latin notaries and the circumstances under which this takes place possess certain specific characteristics:

- The Latin notary is obliged to check the legality of the acts he authenticates and has to advise the parties thereto of the implications and consequences to which they submit themselves. He has to refuse his cooperation in drafting and authenticating acts of an illegal nature.
- Secondly, acts that have been authenticated by a Latin notary possess specific evidentiary power and deliver proof of what has been declared by the Latin notary. Since they also have an official character, they can be registered in certain public registers. They can often also serve as an execution instrument, meaning that they can form the basis of (forced) execution of contractual obligations without any further intervention of a judicial body being needed.
- Thirdly, Latin notaries will be obliged to keep archives of the acts that have been authenticated by them. That way, they act, to a certain extent, as a registrar of official documents.

In some countries, Latin notaries are also obliged to co-operate with or provide certain services for the tax authorities to ensure an efficient collection of taxes on certain transactions. For example, in some countries Latin notaries will be obliged to collect the registration taxes payable at the occasion of a real estate transaction. They may even be obliged to check whether the seller has no unpaid tax debts and, if so, withhold the amount of these taxes from the selling price to transfer this amount to the tax authorities. Further, Latin notaries will also have to provide the tax authorities with information on the value of inheritances with a view

to the efficient collection of inheritance taxes.

The compliance by Latin notaries with the foregoing regulations is ensured by the possibility of disciplinary sanctions and personal liability for all damages resulting from any disregard for these rules.

3. Market imperfections alleviated by the regulation of the Latin notary profession

We believe that the regulation of the Latin notary profession can be a tool to overcome a number of market imperfections, just as is the case for other professionals in the legal sector (lawyers) or in other sectors.

3.1 Asymmetric information, adverse selection and moral hazard problems

First of all, the Latin notary profession and the regulation thereof may be an instrument to tackle the problem of asymmetric information for legal services and the negative consequences this may present (adverse selection, moral hazard). It may also cure the problems arising out of legal services presenting certain characteristics of public goods. These problems are basically the same for all professional legal services, i.e. also those provided by lawyers.

There can be little doubt that the market for the legal services provided by Latin notaries is characterised by asymmetric information. Consumers of these services do not possess the same information about the nature and quality of legal services as the providers thereof. This will especially be the case for certain complex legal transactions like the creation of a corporate structure with legal personality that will be affected by or be party to an unforeseeable number of transactions with others.

Legal services provided by Latin notaries can therefore be qualified as credence goods (consumers will not be able to judge the quality of the services that are provided) or at least as experience goods (consumers will only be able to judge the quality of the services after they

have been purchased). A report by SEO¹⁰ estimates, for example, that real estate is being sold on average every seven years. This indicates that any mistakes that would have been made when selling the good are likely to remain hidden until the next sales transaction, i.e. on average only seven years later. Another example of such good may be a marriage or partnership contract: a consumer will normally only be able to judge the quality of this contract when the marriage or partnership is ended, if ever.

We already indicated in the Introduction how such a situation may lead to problems of

- adverse selection, meaning that consumers will focus their decision to purchase services mainly on price. Providers of higher quality services (with a higher price) can then be driven out of the market, which results in a market with sub-optimal quality services;
- moral hazard, meaning that, since the consumer cannot decide on the optimal price-quality relationship he desires, the professional has an incentive to over-supply quality in order to charge higher prices, even if his client would be better off with lower quality services at a lower price or even no services at all.

These problems could be aggravated by the possibility of ‘free rider’ behaviour of providers of legal services such as Latin notaries. They may be inclined to offer services of a lower quality, knowing that they can profit from the reputation of the profession as a whole. Since consumers cannot judge the quality of these services, free rider behaviour by individual Latin notaries may then go unpunished.

The extent to which these problems may actually occur depends on the type of consumer. ‘Repeat players’, i.e. consumers who purchase these services on a regular basis, may build up certain knowledge and experience that reduces the asymmetry of information between themselves and the service provider. As far as Latin notary services are concerned, this may be the case for larger commercial clients (such as real estate agents and banks)¹¹.

On the other hand, most consumers will be ‘one time shoppers’ and purchase a certain service

¹⁰ SEO (2004), at p. 4.

¹¹ Love and Stephen (1999), at p. 989.

only once or at least on an irregular basis. This will be the case for individual consumers who purchase legal services provided by Latin notaries: buying real estate, getting married, entering into a registered partnership or drafting a will are quite probably legal transactions that average consumers only enter into once or a limited number of times in their life. They will not build up any experience and the asymmetry of information between these consumers and the service provider will basically remain unchanged over time.

Further, a number of Latin notary services come down to selling information, mainly where the Latin notary provides advice on legal issues. This information has a tendency to be a public good, i.e. a good that can be consumed simultaneously by the consumer thereof and by other persons who do not actually pay for the service. Such public goods tend to be under-produced, since consumers will not be prepared to pay the total price for a good that will benefit a larger group of persons.

3.2. Positive externalities generated by Latin notary services.

Informational asymmetries and public goods problems, as discussed above, are market imperfections that are relevant for the services provided by Latin notaries but are common to all providers of legal services. In our view, what distinguishes Latin notaries from these other providers is the fact that the Latin notary, for some aspects of his activity, can be regarded as executing a public task. We remind that the Latin notary, when drafting and authenticating acts,

- has to check the legality of these acts, advise the parties involved of the consequences thereof and refuse to co-operate in drafting and authenticating illegal acts,
- grants an official character to these acts which gives them a specific evidentiary power and the character of an execution instrument ,
- acts as a registrar of official documents and has to keep archives of the acts that have been authenticated by him,
- in some cases has the duty to provide certain services on behalf of the tax authorities.

These obligations are services that are provided not only on demand of and for the benefit of the parties to a transaction, but also on behalf of other parties, including the government.

From an economic point of view, it is clear that these public services can generate substantial positive externalities: they can have a substantial positive influence not only on the parties involved, but also on third parties and on society in general. We remind that in a normal competitive market, these externalities may not be provided, since none of the parties involved in a transaction can appropriate these benefits and will therefore feel no incentive to guarantee the production thereof.

3.2.1. Which positive externalities are generated by Latin notary services?

The most important positive externality is that the Latin notary, through his mediation, can contribute to **greater legal certainty**.

Firstly, this flows from the fact that he has to advise the parties to a transaction of the possible consequences thereof. This effect is enhanced by his duty to act as a neutral, impartial advisor to all parties appearing before him and to avoid any conflict of interest. Through his advice, the Latin notary will ensure that all parties are well aware of the contents and effects of the transaction they are planning. This will not only save these parties the burden of trying to gather this information themselves or obtain similar advice through their own advisors, and thus save transaction costs. It may also prevent any misunderstandings that could later lead to conflicts.

Secondly, legal certainty is enhanced by the duty of the Latin notary to check the legality of the acts he authenticates and to refuse any co-operation to illegal acts. In doing so, he acts as a 'gatekeeper' who contributes to the enforcement of the law. Through this *ex ante* control on transactions, the risk of litigation on the validity of certain acts at a later stage is eliminated or at least reduced.

Thirdly, legal certainty is enhanced by the particular evidentiary power of Latin notary acts and the fact that the Latin notary is obliged to keep archives of all acts authenticated by him. These official documents will be easily available when any discussion arises on a transaction

that was guided by him and will, because they deliver evidence of what has been said and agreed before him, diminish the risk of contradictory views and interpretations.

Fourthly, enhanced legal certainty will result from the role of the Latin notary act as an execution instrument. This allows for an execution without the intervention of any judicial body and thus leads to a quicker enforcement at a lower cost of certain contractual obligations in case of a dispute. This means that the existence and contents of rights will be established sooner and legal 'peace' will be restored in a more efficient manner than through the course of sometimes lengthy and cumbersome judicial procedures.

These advantages of the mediation of Latin notaries will in the first place obviously benefit the parties involved in a transaction. They will be better informed and protected against the consequences of illegal transactions or the non-compliance with any obligations by one of them. All this can lead to substantial cost savings.

However, the mediation of the Latin notary clearly transcends this 'micro-level' and can create certain benefits for society as a whole. Through his mediation, the Latin notary also serves the interests of a number of third parties, i.e. parties who are not involved in the transaction itself but who do have an interest in the transaction being valid and of a high legal quality. This will especially be the case for the government and, by extension, for the whole society. Through acting as a 'filter' to prevent illegal transactions being concluded and through ensuring that consumers are well-informed when entering certain transactions, the mediation of a Latin notary will reduce the risk that this transaction will, at a later stage, be the object of litigation. Hence, Latin notary mediation is likely to reduce the number of legal procedures that will be initiated. This seems to be confirmed by a Spanish empirical analysis by Pastor Prieto, whose work suggests that the degree of litigation seems higher in those areas of the law where the mediation of a Latin notary is not provided¹².

That way, Latin notary mediation can clearly lead to a substantial reduction of costs for the functioning of the judicial apparatus that are normally born by society as a whole. It has to be pointed out that these beneficial effects would quite probably not be realised without the mediation of a Latin notary as a neutral and impartial actor. By lack of information, the parties to a transaction themselves will not only be unable to grasp the full legal consequences

¹² Cited by Arruñada (1996), footnote 8.

of their acts, they will also not internalise the potential costs of litigation, since a large part of these costs will not be borne by themselves but by society as a whole¹³.

Another important positive externality is the fact that, through some aspects of his activity, the Latin notary contributes to a **more effective and efficient collection of taxes**.

It is obvious that this will only to a limited extent benefit the parties to a transaction. However, under the assumption that an effective and efficient tax collection is seen as desirable, it is clear that this benefits the government and, by extension, society as a whole.

An *effective* tax collection is characterised by the fact that all due taxes are paid and that tax evasion is eliminated. A Latin notary may contribute to this through his obligation, in some countries, to check whether the seller of real estate has tax debts and, if so, to withhold the amount of these taxes from the selling price and transfer this amount to the tax authorities. His obligation to gather and transfer certain information on taxable transactions will also contribute to this. This is even enhanced by the fact that, as Mackaay¹⁴ rightly points out, in many countries disciplinary sanctions can be imposed onto Latin notaries who co-operate in fraudulent manoeuvres to evade taxes (for example by providing false information on the actual selling price of property subject to registration duties).

Tax collection could be considered *efficient* when it is cost-efficient, i.e. when the collection takes place at the lowest possible cost. One can imagine that the collection of taxes will probably be cost-efficient when it takes place ‘at the source’, i.e. through the person who is closely involved in the taxable transaction. As far as the gathering of information on taxable transactions is concerned, it can be argued that the Latin notary, as a close witness to the transaction, will be able to gather this information at a much lower cost than the tax authorities who, as third persons, are not themselves involved in it.

3.2.2. These externalities are generated in all areas where Latin notary mediation is mandatory

¹³ See also Mackaay (2002).

¹⁴ Mackaay (2002), at p. 540.

The mediation of a Latin notary is mandatory for certain transactions in each one of his main areas of activity: the transfer of real estate, family practice and certain services for enterprises and businesses. It is submitted that the Latin notary's mediation can generate positive externalities in all of these areas.

REAL ESTATE TRANSACTIONS

When guiding the transfer of property rights to real estate and authenticating the acts relating to this, the Latin notary will be obliged to control whether the seller is actually the rightful proprietor. He will further have to establish what other rights can be exercised in relation to the sold property and which persons are the beneficiaries of these rights. In doing so, he will have to retrace any transactions relating to the sold property that have been executed during a substantial period in the past.

Apart from that, the Latin notary will, as a part of his duty to offer impartial advice, also inform the parties to the transaction of any obligations that may be based on a variety of laws and regulations, for example certain mandatory requirements imposed by environmental laws or urbanisation laws.

It is clear that, in doing so, the Latin notary contributes to legal certainty concerning the property rights to real estate and the existence of other rights and obligations. His mediation will therefore reduce the number of potential disputes on these rights. This will in the first place be to the benefit of the parties to the transaction.

However, it is clear that the Latin notary's mediation can also benefit a number of third parties and society as a whole. As indicated above, this will alleviate the burden on the judicial system and thus benefit the whole of society.

Furthermore, certainty on the existence and exact scope of property rights is crucial in ensuring the good functioning of the real estate market. Since uncertainty surrounding these property rights could destabilise this market, it is obvious that a wide range of actors involved in this market benefit from the Latin notary system. This is particularly true for financial institutions who provide mortgage loans. A house will often be the largest and most valuable

asset of families; many of them will take out a loan covered by a mortgage to be able to purchase this house. For the mortgage bank, it is then crucial to have certainty on any other rights that may be resting on the property, as the execution of its mortgage rights could be hindered by the existence of other conflicting rights. Above that, the function of the Latin notary act as an execution instrument may simplify and thus lower the costs of an execution procedure¹⁵.

It seems clear that a system such as the mandatory mediation of a Latin notary, that ensures legal certainty on property rights, has far-reaching positive consequences, not only for the parties to sales transactions, but also for a wide number of third parties and the government. It is therefore not surprising that the existence of an effective legal framework, guaranteeing well-defined, enforceable and transferable property rights has been described by Hernando de Soto¹⁶, a respected economist at the Peruvian Institute for Liberty and Democracy, as a prerequisite for capital generation and for the development of market economies.

Some have argued that there may be alternatives to the Latin notary system in developing a stable system of property rights. For example, Arruñada¹⁷ argues that the mediation of Latin notaries may be unnecessary and that their role in creating legal certainty may be replaced by a recording and/or a registration system. Organising these records and executing these registrations could in his view be done by other persons at a lower cost. Arruñada's views offer interesting food for thought and are surely worth further research. One will have to establish, for example, in how far some of his conclusions that are based on studies of title insurance systems in the US, can be translated to a civil law context.

In our view, Arruñada's analysis departs from a too narrow view on the activities of a Latin notary. The Latin notary does not merely record or register official documents but, as indicated above, also controls the validity of the property title and informs the parties of all other relevant legal issues. Furthermore, Arruñada's analysis does not take account of the other positive externalities generated by the Latin notary system. In the foregoing, we have already indicated how the Latin notary can also contribute to an effective and efficient collection of taxes to the benefit of the government and society as a whole. We can but repeat

¹⁵ Mackaay (2002), at p. 540.

¹⁶ de Soto (2000).

¹⁷ Arruñada (2004).

what was already indicated there: in many countries, the Latin notary has to co-operate in collecting registration duties and other tax debts at the occasion of sales of real estate. That way, the Latin notary operates ‘at the source’ and can probably function in a more effective and efficient manner than the tax authorities. It remains to be seen whether alternative systems could generate the same positive effects at a lower cost.

FAMILY PRACTICE

When advising on marriage contracts and partnership agreements, wills and acts of gift, the Latin notary, as an impartial advisor, will inform the party or parties thereto of all possible legal implications. The same will be true when he acts as a mediator in family law matters, for example at the occasion of a divorce with mutual consent. Contrary to other advisors (e.g. lawyers), he acts for both parties which may not only lead to reductions in direct costs but may also speed up procedures. Above that, through his role as a ‘gatekeeper’, he will ensure the conformity of all acts he authenticates with all binding laws and regulations. Through his role in inheritance matters, his mediation will also warrant a correct settlement of inheritances. Here too, the Latin notary will through his mediation contribute to legal certainty concerning the rights and duties of the parties involved and will therefore reduce the number of potential disputes.

While at first glance all this would seem to work to the exclusive benefit of these parties, we feel that here too, this legal certainty on rights and duties can benefit certain third parties and society as a whole¹⁸.

First of all, the Latin notary is often entrusted with the task of *ensuring that the rights of minors or other legally incapacitated persons are guaranteed* in transactions effectuated with his assistance. This means that, when someone appears before him to effectuate a transaction on behalf of a minor or another legally incapacitated person and claims to be his legal representative, the Latin notary will at all times be obliged to check whether this person indeed possesses the required authorisation.

¹⁸ We do therefore not adhere to the view in the SEO-report (2004) that the Latin notary’s mediation does not generate substantial externalities in family practice.

Marriage contracts and partnership agreements will obviously not only affect the interests of the partners to the agreement, but will also affect the legal position of family members that are dependent on them and, in the first place, the children of both or either one of the partners. Further, such agreements may also affect the interests of the creditors of one or both partners. For example, when one of the partners is a merchant, he will vouch for his commercial debts with his private assets. When he marries under a system of separation of goods, it is in the interest of his creditors that this separation of goods is not effectuated in breach of the law and that they are informed of this agreement. These interests may then be protected by the mediation of the Latin notary as a gatekeeper.

Wills and the settlement of inheritances can also affect a wide number of persons. First of all, it is necessary that an impartial authority establishes which persons are entitled to the whole or parts of an inheritance, taking account of any existing wills. Some of these persons may never have been involved in any transactions relating to the planning of the inheritance and have no knowledge thereof. Furthermore, it is important that the beneficiaries of a will or inheritance can obtain an official declaration from an impartial authority on their rights to be able to claim their part. This declaration is particularly important when some of the assets of the testator are under control of third parties (e.g. accounts with financial institutions), since they will only be able to transfer these assets when they are assured that the person claiming any rights thereto can prove this on the basis of such official declaration. Lastly, for obvious reasons, a correct settlement of inheritances and obtaining knowledge thereof can also benefit creditors of the testator or the beneficiaries of his estate.

Acts of gifts likewise generate certain effects for third parties that are not involved. For example, a gift may affect the rights of legal heirs that have not been involved in the act. It is therefore crucial that there exists some legal control as to the validity of gifts and that these gifts can be recorded in an official document to create certainty on the existence and exact contents of it for future use.

Apart from the fact that a wide range of third parties are affected by these transactions in the area of family law, society as a whole may also benefit from the mediation of a Latin notary. As indicated, through his gatekeeper function and the fact that, as an impartial advisor, he informs all parties of the legal consequences of the transactions they are engaging into, the Latin notary will reduce the number of disputes and thus alleviate the burden on the judicial

apparatus.

One could also argue, although it has to be admitted that this effect will be difficult to quantify, that this may serve the broader goal of maintaining stable family relations in society. In most countries where the Latin notary profession is recognised, there exists a consensus that family relations, no matter between which persons they are established and what legal form they may assume, are still the cornerstone of society. Through his role as an impartial advisor and gatekeeper, the Latin notary substantially prevents the number of disputes on these matters and thus contributes to a stable society.

Finally, in inheritance, wills and gifts matters the Latin notary has the duty to inform the tax authorities of the existence and value of the transactions he is settling. That way, for the same reasons as described in the previous sections, he can contribute to an effective and efficient collection of taxes and duties on successions and gifts.

SERVICES TOWARDS BUSINESSES AND CORPORATIONS

Mediation by a Latin notary is mandatory for certain business transactions in several countries. Most of these relate to the establishment of corporations, foundations, trusts and associations or any structural changes thereof, like issuing shares, capital increases, mergers and scissions. These transactions require a document which is authenticated by a Latin notary. Here too, the Latin notary will have to exercise control over the legality of the acts he authenticates and thus function as a gatekeeper. In some countries, the establishment of a limited liability company requires providing a financial plan which the Latin notary has to keep in his archives. This financial plan may play a role in assessing the liability of the founders of the company in future disputes.

Such transactions will obviously not only generate effects on the parties involved, but also on third parties. When a new legal person is created or its characteristics are modified, it is necessary that third parties are informed of this and also obtain certain basic information on the identity and characteristics of this legal person. Shareholders, directors, clients and suppliers and all other creditors and, finally, the tax authorities all have a clear interest in this. The financial plan, kept under the custody of the Latin notary, will not only affect the position

of the founders of the company, but also future creditors.

Through his role as a gatekeeper, the Latin notary further ensures that legal persons are being established in line with all legal provisions. The same goes for mergers and scissions or all other structural transactions for which his mediation is mandatory. That way, his mediation is likely to reduce the number of potential disputes.

Thus, the Latin notary's activities may benefit a large number of persons and society as a whole and hence, from an economic point of view, be considered to generate substantial positive externalities. The enhanced legal certainty flowing from his mediation surely may be in the interest of the good functioning of the economy¹⁹.

¹⁹ Compare Nguyen-Hong (2000), at p. 3 § 4.

CHAPTER II - Theory and evidence on the effects of professional regulation

As indicated above, this chapter will first briefly summarise the criticisms to the IHS study. Thereafter, the second section of this chapter will give an overview of the main arguments in favour and against the most common forms of professional regulation (regulation granting monopoly rights, restrictions on entry, fees, advertising and forms of business). This section will also offer an overview of empirical studies which either confirm or rebut the theoretical arguments. Finally, the third section will describe the recent experiences with the deregulation of the notary profession in the Netherlands.

1. Criticisms relating to the IHS report

1.1 Contents of the IHS report

The IHS report can be very briefly summarised as follows. The IHS study departs from the insight that, while a lot of research on the regulation of professions has been undertaken, most studies have focused on the professions in the US. The study therefore aims at making a comparative analysis of the regulation of a number of professions in EU member states. The study focuses on the regulation of legal services (lawyers and Latin notaries), accountancy services (accountants, auditors and tax advisers), technical services (architects and consulting engineers) and pharmacy services (community pharmacists).

Firstly, the study tries to compare the level of regulation for these professions across the different member states. The study thereby distinguishes between entry regulation and conduct regulation. Data on the existence and contents of different types of regulation in the various professions were mainly collected through a questionnaire that was sent to the relevant professional organisations and governmental bodies.

The study then tries to make these data comparable. To do so, it develops so-called 'regulation indices', i.e. scores that are given to the level of entry and conduct regulation for the different professions across the member states. The indices for entry and conduct

regulation are also added to form one general regulation index for the different professions in each state, thus allowing an objective comparison. This comparison shows that there are large differences in the level of regulation for several professions.

The study then goes on to try and find out whether these different levels of regulation also have an impact on market outcomes. To that end, the study undertakes a number of case studies. In these case studies, for each profession subsets are formed of member states where the level of regulation for the professions, as indicated by the regulation indices, differs substantially. The regulation indices for those countries are then linked to data on the volume of services that are being provided and on the number of professionals active in each country.

In the researchers' view, these case studies allow to draw interesting conclusions. One clear tendency seems to be that in professions in countries with a high level of regulation, a relatively high volume of services is being provided compared to the number of practising professionals. Conversely, the same professions in member states with a lower level of regulation seem to produce a relatively smaller volume of services in relation to the number of professionals. The researchers claim that, while specific data on profit were not available, "a connection may be surmised between volume of business per professional and excess profit".

While the authors acknowledge that these results are not necessarily the result of regulation, they argue that the case studies seem to offer some support for the view that regulation primarily leads to higher profits for the professionals but leads to suboptimal outcomes from the point of view of the whole economy and consumers in particular.

1.2 Criticisms to the IHS report.

It can be applauded that the IHS study aims at gaining useful insights into the nature and level of regulation of the professions throughout the EU. Furthermore, the attempt to shed some light on the potential effects of regulation through the case studies is to be welcomed. The IHS study therefore undoubtedly offers some interesting food for thought.

Nevertheless, a number of criticisms can be raised against the study. These criticisms have been thoroughly developed in a report by RBB Economics²⁰. The main criticisms are the following:

- *the theoretical framework of the IHS study shows some shortcomings*

First of all, the study presents only a very broad outline of the theoretical arguments on regulation. It does not sufficiently take account of the different effects of different types of regulation. Further, it does not pay sufficient attention to the specific characteristics of each profession and the specific types of regulation they may necessitate.

Secondly, it can be argued that the study shows a certain bias in favour of contra-regulation theories. The study seems to depart from the view that there may possibly be too much regulation and does not ask the more general and neutral question what the optimal level of regulation should be.

Thirdly, the theoretical analysis in the report offers no solid ground for the empirical analysis that is undertaken in the case studies, as it does not clearly show what the relevant questions are and, particularly, how one can research whether there is too much or too little regulation within a certain profession.

- *The methodology used in the report shows certain flaws.*

The construction of the regulation indices that are being used in the study is subject to a certain level of subjective judgement. Also, while the questionnaires were the main source of information in constructing the indices, in some professions the rate of response was rather low. This could compromise the reliability of the information used. Further, it cannot be determined to what extent the results obtained have been influenced by the assumptions made.

²⁰ RBB Economics (2003).

Further, the study uses the 'volume' variable in the case studies. Volume is calculated as turnover adjusted for differences in price levels and gross domestic product. This is somewhat misleading since, that way, one does not measure the actual output.

RBB further points out that the study also shows certain shortcomings as far as the economic technicalities of the analysis are concerned. They argue, for example, that the correlation analysis (i.e. an analysis where the correlation between two variables is measured) used by the researchers is not the appropriate instrument and that alternative statistical analyses may have been more fit for the purposes of this study. Also, valuable information may have been lost due to the use of gap adjustment (i.e. adjusting the economic variables to try to control the differences between each member state).

- *The interpretation of the results in the study is questionable.*

The conclusions of the researchers rest on certain highly questionable assumptions. For example, the crucial conclusion that the case studies seem to offer some support for the view that regulation mainly leads to excess profits for the professionals to the detriment of consumers and the economy as a whole, is entirely dependent on the assumption that higher volume (i.e. turnover) equals higher profit. This assumption is far fetched. It is perfectly conceivable that turnover in a severely regulated profession may be higher because the bureaucratic costs are higher - and hence the prices charged. Another possible explanation for higher turnover might also be that a smaller number of professionals in these states works harder than in other member states and thus reaches a higher turnover, in spite of a lower price per service. A third explanation may be that the turnover is higher because the prices are higher since the quality of the services provided is superior, not because of the existence of excess profits.

This last example illustrates the most crucial shortcoming of the IHS report: it focuses mainly on volume and price of the services provided by professionals, but does not take account of the potential effect of regulation on the quality of these services. The researchers explain this by stating that it proved difficult to obtain reliable data on

quality. However, this does not prevent them from suggesting that regulation may be unnecessary to guarantee quality, stating that “there have been no apparent signs of market breakdown in those member states which we have shown to be less regulated”. This is a false argument: the absence of a total market failure does not necessarily imply that the quality in a less regulated market reaches an optimal level.

1.3 The IHS study and the Latin notary profession: an interesting starting point, not a policy tool

The foregoing brief overview of the main arguments raised against the IHS study by RBB economics shows that, while the study offers an interesting starting point for further research, its methodology and results are fragmentary and disputable. We therefore strongly believe that it should not be relied on too heavily in formulating concrete policy conclusions.

This is especially the case for the Latin notary profession. The researchers themselves acknowledge in their report (p. 57) that they lacked information on several aspects of the Latin notaries’ professional regulation, particularly on matters for which the consultation of a Latin notary is mandatory in the respective countries. As already indicated in the previous chapter, the main reason for the organisation and regulation of the advantages of the Latin notary profession in its current status is that the services provided by Latin notaries may generate substantial positive externalities. Since the researchers did not possess all necessary information, their study could obviously not take account of these potential benefits of the Latin notary profession.

We therefore feel that, if the European Commission should undertake a policy review on the regulation of the Latin notary profession, it should not base any policy decisions on the IHS report but rather engage in further discussions and research into the actual effects of the relevant regulation.

2. Overview of theoretical arguments and empirical evidence about the main types of professional regulation

This part of the report will discuss the main arguments in favour and against the most commonly used forms of professional regulation. As a preliminary remark, it can be pointed out that it is generally agreed that certain types of professional regulation offer no or very little problems from a competition law and policy point of view. For example, certain professional obligations such as maintaining the dignity of the profession and respecting the confidentiality or secrecy of the information obtained about clients, will not by themselves have a noteworthy negative impact on competition between professionals.

Conversely, certain aspects of professional regulation are often deemed to have a substantial negative impact on competition and thus to lead to disadvantages for consumers: the existence of monopoly rights, entry restrictions, restrictions on fees, on advertising and on business organisation. Still, these restrictions may be justified if there are wider public policy benefits. It is those restrictions that stand at the centre of attention of research on professional regulation and of the competition authorities – particularly the European Commission. Therefore, these will be the focus of the following part of this report. For each type of restriction, a brief overview of theoretical arguments against and in favour of these restrictions will be given. Thereafter, the report will attempt to summarise existing empirical evidence on the effects of these aspects of regulation.

2.1 Monopoly rights

In some professions, exclusive rights are granted to the members of the profession to perform certain services. Such an exclusive right granted to a certain group of professionals is commonly called a monopoly right. Such monopoly rights and their potential positive or negative effects have been the object of numerous theoretical comments.

2.1.1. Theoretical arguments on monopoly rights

The classical argument *against* monopolies is that they tend to lead to welfare losses due to a less efficient functioning of the market. Service providers benefiting from a monopoly right are not restricted by the threat of competition by providers from outside the protected profession. That way, they can restrict output, i.e. provide less services, while at the same time raising prices for their services and thus achieve higher economic rents to the disadvantage of consumers. They become ‘price makers’ with the only limit to their pricing behaviour being the maximum price that consumers are willing to pay.

At this point it should be noted that the classical theoretical argument against monopolies may be irrelevant to the Latin notary profession if the applicable state regulation obliges the notary to provide the services he obtains exclusive rights for. In such a case, the Latin notary does not have the possibility of lowering his output. Furthermore, the fees for these services may be imposed by the government, leaving no room for price increases by the professionals. For the same reasons, the arguments raised against the introduction of (quantitative) entry restrictions may be irrelevant as far as the notary profession is concerned.

Some arguments can be forwarded *in favour of* certain monopoly rights.

Granting monopoly rights may prove necessary to guarantee the provision of so-called universal services. These are services which are deemed to be that important that every person should be able to purchase them at a reasonable price. Some of these services may prove not to be profitable to service providers for certain geographic areas or for certain types of consumers. In the absence of regulation, it may in that case very well be possible that certain consumers will not be able to purchase these services at a reasonable price. Granting a monopoly right to professionals may overcome this problem by ensuring that service providers can serve enough clients to make the provision of these services worthwhile.

Another argument states that conferring monopoly rights for certain services may lead to an enhanced degree of specialisation which, in turn, may guarantee a higher quality of services being provided to consumers. For example, as far as the legal profession is concerned, Bishop²¹ argues that consumers of legal services may be better off when a division is made –

²¹ Bishop (1989)..

and other professionals would be occupied with – the preparation of a case and the pleading of a case before court. However, as Stephen and Love²² point out, one also has to take into account the possibility that such division may lead to higher transaction costs. Moreover, one would have to ascertain that a monopoly right is not being granted for services that can be provided at a lower cost by other (para-)professionals, since this would lead to a welfare loss for consumers. Finally, it may prove very difficult to deliver empirical evidence of such assumptions.

2.1.2. Empirical evidence on the effects of monopoly rights

In spite of the fact that several pertinent arguments against or in favour of monopoly rights have been forwarded, empirical evidence on the effects of monopoly rights and their abolishment, possibly through the introduction of a para-profession, are strikingly scarce.

There are no convincing general empirical studies into the possible positive effects of monopoly rights. As to the negative effects of monopolies, only a limited number of studies attempt to grasp the possible disadvantages of monopoly rights. This may be explained by the fact that there exist no or little data which allow for solid conclusions on the effects of the variations of monopoly rights over time or in different locations.

However, there is at least one example from recent times of the abolishment of a monopoly right on which a number of empirical analyses have been undertaken. The year 1987 saw the end of a long held monopoly right for conveyancing services in England and Wales. Conveyancing services can be defined as a bundle of professional legal services related to buying and selling real estate property: Conveyancing includes the investigation and transfer of title as well as fulfilling certain legal formalities related to mortgage finance. Ever since 1804, solicitors had held a monopoly right over conveyancing services in England and Wales. In the 1970ies, this monopoly right came under the attack of consumer organisations and home owners' associations, especially against the background of the steadily growing level of home ownership. They argued that the solicitor fees for conveyancing services were too high and that the average time to complete a typical transaction was too long. The Mergers and

²² Stephen and Love (1999).

Monopolies Commission²³ also published a number of reports, suggesting that the existing regulation of the solicitor profession limited the competitiveness and efficiency of the profession.

When this general disagreement continued during the early 1980ies, the government in 1984 decided to introduce legislation to abolish the existing monopoly right and to partially liberalise the market for conveyancing services. In 1985, the Administration of Justice Act was passed which created a para-profession called 'licensed conveyancers' the members of which would be allowed to offer conveyancing services in competition with solicitors. Actual entry of these licensed conveyancers took place as of 1st May 1987.

This abolishment of a former monopoly right and the introduction of - at least some level of - competition offered a unique opportunity to measure the effects of such liberalisation. This partial liberalisation has indeed been the focus of a number of studies between 1985 and 1992. These studies provide limited, though interesting, insights on the effects of the relaxation of a profession's monopoly rights and the impact of the entry of paraprofessionals.

A first remarkable study is the research by Farmer, Love, Paterson and Stephen²⁴ on the market for conveyancing services towards the end of 1986, that is after the decision on abolishing the solicitors' monopoly was taken, but before the first licensed conveyancers actually entered the market. They conducted a survey among a representative sample of solicitors in England and Wales to check what their response to enhanced competition for conveyancing services would be. One of their findings is that at that time solicitors' fees showed a downward tendency. As Stephen and Love²⁵ seem to suggest, this could be explained by the fact that solicitors may already have been lowering their fees in anticipation of the entry of the licensed conveyancers

A later survey by Gillanders, Love, Paterson and Stephen²⁶ focused (among others) on fees charged by a representative sample of solicitors for a routine conveyancing transaction in November and December of 1989, i.e. after the entry of the licensed conveyancers as

²³ This is one of the UK authorities entrusted with the enforcement of competition law and currently goes under the name of 'Competition Commission'.

²⁴ Farmer, Love, Paterson, and Stephen (1988).

²⁵ Stephen and Love (1999).

²⁶ Gillanders, Love, Paterson, and Stephen (1992).

competitors for the solicitors in conveyancing services. Their research took account of data for 27 representative geographic areas. It was expected that, if the entry of licensed conveyancers would indeed enhance competition, conveyancing fees would be lower in areas where licensed conveyancers had been most active. This was indeed confirmed by the results of their inquiry, which suggests that the presence of licensed conveyancers as competitors exercises a downwards pressure on conveyancing fees. This seems to confirm the converse assumption that a monopoly right causes fees to be higher and thus works to the disadvantage of clients²⁷. However, the researchers themselves put this result into perspective. First of all, they stress that their research was based on fees quoted by the solicitors, not on the actual fees paid by their clients. Moreover, they point out that the fees in areas where the licensed conveyancers had entered the market (namely the larger markets), were already lower in 1986, i.e. before the solicitor's monopoly was abolished. This could mean that the lower fees may (partially) be declared by other factors than the entry of the licensed conveyors.

In 1992, Stephen, Love and Paterson undertook a similar research covering the same locations as the earlier 1989 survey and using similar data, i.e. quoted fees for conveyancing transactions²⁸. The results of this research are somewhat surprising. They found that the fees quoted by solicitors were on average higher than those quoted by licensed conveyancers. Furthermore, solicitor's fees had generally risen and even risen faster in markets where they did not face competition from licensed conveyancers. On the other hand, a striking result of their research is that licensed conveyancers' fees also had risen between 1989 and 1992. Furthermore, the fees of licensed conveyancers had risen faster than those of solicitors in markets where both professions were active. This seems to contradict the assumption that abolishing monopoly rights will lead to lower fees being charged to the benefit of consumers. The researchers admit that their research results can not *per se* assess the effect on fees of the change of the regulatory regime, but suggest that there seems to have been an accommodation between solicitors and licensed conveyancers after the entry of the latter. This is remarkable, especially since the licensed conveyancers were not subject to any competitive constraints comparable to those of the solicitor profession.

²⁷ A report by Indecon (2003) reports on another study revealing evidence on the introduction of the para-profession of licensed conveyors in New South Wales (Australia). This report seems to confirm that the introduction of some level of competition, coupled with relaxation of restrictions on fee advertising, may result in lower fees charged by solicitors for conveyancing services.

²⁸ Love, Paterson and Stephen (1994).

Looking back on these results, Stephen and Love²⁹ have sought explanations for these findings. They present several elements which could explain why the entry of licensed conveyancers has not, as expected, lead to lower fees as a consequence of the introduction of a certain level of competition in the market for conveyancing services. One element could be that the fees were to a large extent influenced by the level of solicitor concentration in local markets. Further, the overall level of entry of licensed conveyancers was rather low, especially in rural areas. Several factors may explain this, such as the slump in the housing market in those days and the fact that conveyancers have more limited opportunity for business development and risk spreading across different services, since they can only offer a limited range of services. The fact that licensed conveyancers carry a larger risk may explain why they charge higher fees than expected to compensate for this risk. The authors believe that positive effects may be realised when other multi-services providers (such as banks and building societies) would be allowed to enter the conveyancing market. Since there exists no evidence of such entry, this question remains open.

2.1.3. Conclusion on monopoly rights

Several pertinent arguments have been developed against and in favour of monopoly rights for certain professional services. However, empirical evidence on this topic remains scarce. Nevertheless, there have been a number of relatively recent studies on the effect of the abolishment of the monopoly for conveyancing services in England and Wales. In our view, these interesting studies and their puzzling results show that, currently, it is difficult to draw clear-cut general conclusions on the effect of monopoly rights. While some studies seem to confirm the widespread assumption that monopoly rights lead to higher fees to the detriment of consumers, other studies show that the introduction of – be it a limited level of – competition does not automatically guarantee lower fees. These studies and the comments thereto suggest that a number of other factors may be of relevance in studying the effects of monopoly rights. Therefore, it can be argued that, to establish the effects of a particular existing professional monopoly, a sophisticated approach, mapping and investigating these factors, will be required.

²⁹ Love and Stephen (1996).

2.2. Entry regulation

All professions are characterised by the existence of entry restrictions, i.e. one or more regulations restricting the entry into the profession. These entry restrictions may be of a qualitative or quantitative nature or relate to certain personal characteristics of the members of the profession

Qualitative entry restrictions may take the form of³⁰:

- requirements relating to the minimum level and period of education and training (e.g. the possession of certain degrees and diploma's),
- requirements relating to a minimum level or period of professional experience (for example having undergone an apprenticeship in an established practice),
- successful completion of certain professional examinations after a professional education (generally known as licensing³¹),
- other personal characteristics (such as citizenship and residence, language competence, absence of civil or criminal convictions).

Apart from these qualitative restrictions, some professions in certain jurisdictions are also subject to quantitative restrictions, i.e. limitations as to the number of entries into the profession. Such is, among others, the case for the pharmacy and Latin notary professions. In such cases, the restrictions may be based on demographic or geographic criteria or a combination of both. This means that the restrictions may limit the number of professionals in relation to the general population, allow a limited number of professionals for separate geographical areas or limit their number for each geographical areas whereby the number of professionals in each area is related to its population. In many cases, these entry restrictions are coupled with monopoly rights to provide certain services.

³⁰ See also Indecon (2003), at 19.

³¹ Maks and Philipsen (2002), at p. 18 § 2, distinguish 'licensing' from 'certification'. Licensing means that only professionals who have obtained the required license are allowed to render certain services. Certification means that the regulated services may be rendered by everyone, but that only those professionals who have obtained a certification are allowed to use a protected title. As such, a certification does not function as a direct entry requirement

2.2.1. Theoretical arguments on entry regulation

Entry restrictions are most commonly justified by the fact that they may cause certain *positive effects*.

Qualitative entry restrictions are said to serve the aim of guaranteeing a minimum level of quality of the services rendered and avoiding adverse selection problems. It is argued that, because of the existence of information asymmetries, a consumer cannot judge the quality of the service he will acquire. Therefore, he will base his choice mainly on price and will not be willing to pay a higher price for higher quality. As a result, providers of higher quality services (with a higher price) are driven out of the market, which results in a market with sub-optimal quality services. That way, the information asymmetry between the service provider and the consumer could culminate in a 'market for lemons'.

By introducing qualitative entry restrictions (possibly combined with monopoly rights), one can ensure that only professionals with appropriate qualifications and a minimum level of competence can render these services. The exclusion of low-quality suppliers will enhance the average level of quality in the market and alleviate the information asymmetry problem between the professionals and the consumers.

Some may argue that qualitative entry restrictions will only improve quality under certain conditions and, furthermore, that such restrictions will not necessarily be to the benefit of consumers when it appears that there are consumers who would also be willing to purchase lower quality services at a lower price. In such cases, information regulation might be sufficient. However, there seems to be a consensus that for some professional services, social welfare might decrease if untrained professionals are allowed to be active on the market. Simple information regulation will then not be enough to protect consumers³².

In economic literature, specific views have also been forwarded on criteria relating to nationality and citizenship or residence as a condition to professional practice. It is argued that such requirements may be justified when it is deemed necessary for professionals to be familiar with national laws and habits. This argument is of particular importance for legal professions. Residence requirements may be justified by the need to establish an efficient

³² Maks and Philipsen (2002), at p. 18 § 3.

relationship between professionals and consumers and the need to create an adequate possibility for the consumer to take legal recourse in cases of negligence and malpractice³³.

Quantitative restrictions are often justified by the consideration that they may increase overall profitability. They may prove necessary when there is a risk that providing services to certain consumers threatens to be unprofitable. In such case, a provider of services would only provide services to these consumers when his loss can be offset by the profit he gains in servicing other, profitable consumers. Limiting the number of professionals and enhancing their profitability may then take away this concern and ensure that the service in question can be purchased by all. This argument is of particular relevance in situations where, in absence of a specific regulation, certain sparsely populated areas are threatened not to be serviced because this would prove unprofitable. In such case, introducing a quantitative restriction of the number of professionals on the basis of geographical and/or demographic criteria may increase profitability and guarantee that consumers in these less profitable areas will be able to enjoy the services.

On the other hand, entry restrictions may also generate certain *negative effects*.

Professionals may want to maximise their income by providing a lower level of supply, thus increasing prices. They may reach this effect by setting the level of qualitative entry restrictions too high. This can have the effect of limiting the number of professionals and of the services that are provided³⁴. This may especially be the case when the entry restriction is combined with a monopoly right for the profession. The existence of a monopoly right prohibits any supply being created by other suppliers outside the profession. Therefore, qualitative entry restrictions may, possibly in combination with other restrictions, lead to socially undesirable results.

Quantitative entry restrictions obviously reduce the number of service providers and thus enhance the risk of reduced supply and increased prices. Furthermore, where the quantitative restriction has a geographical component, this may lead to the creation of local monopolies, the potential disadvantages of which have been described above. The existence of a numerical

³³ Indecon (2003), at p. 19-20.

³⁴ Leland (1979), at p. 1338.

limitation excludes any additional services being produced by new entrants to the profession³⁵.

As far as restrictions on the basis of nationality, citizenship or residence are concerned, it has been argued that these are difficult to justify since they mainly lead to preventing the cross-border provision of services and are more likely to be motivated “by the desire to maintain control over the professional’s standards, to allow governments and to assure collection of taxes and compliance with other laws”³⁶.

It is therefore clear that a cautious and sophisticated approach of entry restrictions is required. As far as qualitative restrictions are concerned, one could, for example, investigate whether there are no other, less restrictive means to guarantee the level of quality of the service rendered. Maks and Philipsen distinguish three mechanisms to do so³⁷.

One of these mechanisms are so-called ‘specification standards’. These are standards developed by the government that impose certain production methods or materials onto the suppliers. Maks and Philipsen argue that such standards seem unsuitable for professional services, since the government does not have at its disposal the specific knowledge required to set an appropriate specification standard.

Another mechanism could be introducing so-called ‘target standards’. This implies that the quality of the service is not regulated beforehand, but that liability is imposed for possible harmful consequences flowing from poor quality services being rendered by a professional (*ex post* control). Mak and Philipsen submit³⁸ that a liability rule may be sufficient when the rendering of a low quality service involves only small risks for third parties. However, a liability rule would not offer adequate protection when the damage resulting from low quality service is of a substantial magnitude. In our view, this can arguably be the case for (at least some) professions.

When adequate protection of the desired level of quality of professional services cannot be guaranteed through specification standards and liability rules, only a so-called ‘performance

³⁵ Compare Love and Stephen (1999), at p. 993.

³⁶ OECD (2000), at p. 32.

³⁷ Compare Maks and Philipsen (2002), at p. 15 § 1.

³⁸ Maks and Philipsen (2002), at p. 17 § 3.

standard' will offer a solution. A performance standard implies controlling the quality of the service before it comes onto the market. This is exactly what happens through introducing qualitative entry restrictions.

As far as quantitative restrictions are concerned, the possible justification seems to be valid only for sparsely populated areas but not for areas that are densely populated and thus do not present the risk of reduced supply. However, even in sparsely populated areas one would have to establish whether there are no less restrictive alternatives like offering special compensation for rendering public services.

In the light of the foregoing, it is clear that a careful case-by-case approach is required to establish whether or not the introduction of a certain entry restriction is necessary and/or justified in a certain profession.

Leland³⁹ has constructed a model which suggests which characteristics of a market would justify the introduction of qualitative entry restrictions. However, this model is a theoretical one which rests on a number of assumptions which may be difficult to test in a real life context.

It would therefore seem reasonable to argue that, to establish with certainty whether an entry restriction in a profession can be justified on the basis of the foregoing theoretical arguments, it would require a concrete empirical analysis of:

- whether this restriction would actually lead to a reduction in the number of professionals,
- whether this would lead to a reduction in supply and higher prices,
- whether the presence or absence of the entry restriction would have any effect on the quality of the services rendered.

2.2.2. Empirical evidence on the effect of entry regulation

EFFECT ON THE NUMBER OF PROFESSIONALS

³⁹ Leland (1979); for comments see Indecon (2003), at p. 19.

Quantitative restrictions will by their own nature have the effect of limiting the number of professionals.

However, there is little empirical evidence to support the view that qualitative entry restrictions will lead to a lower number of active professionals. While such restrictions exist in all professions, the number of practitioners in most professions is large, which suggests that qualitative entry restrictions do not by themselves restrict the number of professionals and thus limit competition⁴⁰.

As far as the legal profession is concerned, Stephen and Love⁴¹ indeed point out that entry to the legal profession in the United States has continually grown over the years, in spite of the existence of qualitative entry restrictions.

As a matter of fact, one study even seems to suggest an opposite effect. Stephen and Love quote an empirical analysis of the legal profession in different states of the US by Lueck, Olsen and Ransom⁴². They examined the relationship between state lawyer density, state bar exam pass rates and the requirement of an ABA recognised degree. Their research suggests that lawyer density is higher in states where the pass rate is lower and in states where an ABA recognised degree is required. This seems to suggest that more professionals are entering the legal profession in states where entry restrictions are higher.

Olsen⁴³ reports that a number of studies on the effect of entry restrictions in the medical professions have led to quite different results. The results of most of these studies (relating to dentists and physicians) seem to confirm the common view that qualitative entry restrictions lead to a lower number of professionals. However, a study on licensing restrictions for nurses showed that these restrictions had no or, for some years, even a positive effect on the number of entries into that profession.

Empirical evidence does, however, seem to support the view that combining qualitative entry restrictions with geographical restrictions may possibly have a negative effect on the number of professionals. This seems to be confirmed by a number of analyses focussing on the effect

⁴⁰ This is also acknowledged by the OECD (2000), at p. 24 § 3.

⁴¹ Stephen and Love (1999), at p. 994.

⁴² Stephen and Love (1999) quote Lueck, Olsen and Ransom.

⁴³ Olsen (1999), at p. 1026.

of restrictions of mobility between states for lawyers in the US. It is reported by Stephen and Love⁴⁴ that most of these studies show that such lack of reciprocity leads to a lower number of professionals and higher lawyer incomes.

EFFECT ON SUPPLY AND PRICES

As far as the effect of entry restrictions on supply and prices is concerned, there have been numerous studies focussing on the effect on prices or return and income of professionals as a proxy thereto. Most of these studies relate to the medical profession.

Critics of entry restrictions often refer to the somewhat older research of Friedman and Kuznets (1945). They compared the incomes of dentists and physicians, entry restrictions for the latter profession being more severe. They found that physicians' average income was substantially higher than that of dentists. This is seen as a confirmation of the hypothesis that more severe entry restrictions mainly lead to higher incomes for the professionals. Stephen and Love⁴⁵ put these findings into perspective, arguing that this difference would probably not be caused exclusively by the different level of entry regulation but rather by the "global effect of self-regulation".

The comprehensive overview of empirical evidence on the regulation of medical professions by Olsen⁴⁶ clearly shows that no hard general conclusions on this can be drawn. Olsen refers to a number of studies on the differential rates of return within the medical profession as a broad category. These studies focus on the different levels of entry restrictions and their effect on the return for certain medical specialisations. They show that different rates of return can often be explained by other factors than the level of entry restrictions, such as the number of hours worked weekly on average by certain specialised professions. As Olsen states, these studies 'seriously question the conclusions of earlier studies'. Olsen further mentions a large number of studies that focus on the impact that restrictions may have on income directly. These studies present different results, some of them even suggesting that entry restrictions may lead to a lower income for certain medical specialists.

⁴⁴ Love and Stephen (1999), at p. 994.

⁴⁵ Love and Stephen (1999), at p. 993.

⁴⁶ Olsen (1999).

Olsen finally mentions a number of studies on the effect of entry restrictions directly on prices. The majority of these studies seem to confirm the view that entry restrictions lead to higher prices. However, according to Olsen these studies show some methodological weaknesses. However, a more recent analysis by Kleiner and Kudrle⁴⁷ on dental services seems to confirm this effect. Their research into the effect of different levels of entry regulation across several US states showed that prices for dental services in states with severe restrictions were higher than in other states.

Similar research on entry restrictions in the legal profession is scarce. Stephen and Love quote an empirical analysis by Lueck, Olsen and Ransom (1995)⁴⁸ who find little support for the view that restrictions affect the price of legal services. Stephen and Love themselves also indicate that, conversely, the growing number of lawyers “has not necessarily coincided with greater competition in terms of reduced fees and a greater range of services”.

In the light of the foregoing, it is in our view clear that no hard conclusions can be drawn on the effect of entry restrictions on supply and prices.

EFFECT ON THE QUALITY OF THE SERVICES RENDERED

The studies on the effect of entry restrictions mainly focus on the potential negative effects of these restrictions, i.e. whether they limit the number of professionals and cause lower output and higher fees. Research into the potential positive effects on the quality of the services provided is rather scarce and mainly concentrated on studies on medical services. As a preliminary remark, it is appropriate to quote Olsen⁴⁹, who stresses that “studies of quality almost universally suffer from one overwhelming weakness; quality is difficult to measure.

Haas-Wilson (1986)⁵⁰ concluded that entry regulations in optometry had no significant impact on quality. In their study, quality was measured on the basis of the thoroughness of the eye exam. Conversely, the evidence on dentists presented by Carroll and Gaston (1981)⁵¹ seems to suggest that entry restrictions even lead to a lower quality. However, as Olsen⁵² points out,

⁴⁷ Kleiner and Kudrle (2000).

⁴⁸ Love and Stephen (1999), at p. 993.

⁴⁹ Olsen (1999), at p. 1027.

⁵⁰ Haas-Wilson, D. (1986).

⁵¹ Carroll, and Gaston. (1981).

⁵² Olsen (1999), at p. 1027.

their criterion used to measure the quality of the services, namely how long patients had to wait to obtain an appointment, is highly questionable since it says little about the actual quality of a dentist's services. Olsen quotes another research on optometrists by Feldman and Begun (1985) who used the length and thoroughness of the eye exam as an indication for quality. They found that regulation actually increased the quality of the services.

However, the research by Kleiner and Kudrle (2000)⁵³ seems to confirm the earlier study of Haas-Wilson. They studied the effects of entry restrictions across several US states on the quality of dental services. They based their findings on data on dental deterioration retrieved from the dental records of new enlistees into the US Air Force, combined with socio-economic characteristics. Their results show that overall dental health was not higher in states with more severe entry restrictions, which seems to deny the existence of any positive effect on quality.

From the foregoing, it is clear that empirical evidence shows very different results. We feel, therefore, that the European Commission's somewhat narrow view on this topic is not justified. In its Communication on professional services⁵⁴, the European Commission refers to a staff report of the US Federal Trade Commission by Cox and Foster (1990). In that report, the researchers assess a number of empirical studies on the effect of entry restrictions. They indeed conclude that a majority of these studies show little or no positive effect on the quality of the services provided. However, the authors also state that in "determining the best regulatory framework — if regulation is needed — the characteristics of a particular market must be examined". We feel that this more mitigated conclusion is the right one. The varying results of empirical research justify the view that general conclusions on the effect of entry restrictions are impossible and that a more sophisticated approach for different types of restrictions in individual professions is required.

2.2.3. Conclusion on entry restrictions

While there exist a number of studies into the effect of entry regulation on the number of professionals, output and prices of the regulated services and the impact of this regulation on

⁵³ Kleiner and Kudrle (2000).

⁵⁴ European Commission (2004), at p.16.

the quality provided, empirical evidence on this subject remains all in all limited and fragmentary. All studies focus on one or a limited number of professions and on certain types of entry regulation only.

Furthermore, the results of these studies show very different results. While some studies seem to confirm the expected negative effects of entry regulation on the number of professionals or their output and prices, other studies show no or even a positive effect. In addition, while some studies show that entry regulation enhances the quality of the services provided, other studies show no or a negative impact. However, research on the impact of entry restrictions on quality remains scarce. Also, since quality is difficult to measure, the validity of the conclusions of these studies can be questioned. We strongly feel that Olsen's conclusion on the medical profession is also valid for other professions. The current state of empirical research offers "no consistent picture of the impact that entry requirements [...] have on income, prices, supply or the quality [...]." General conclusions on the effect of entry restrictions therefore seem hard to justify.

2.3 Fee regulations

In some professions, the fees to be paid by the consumer of professional services are regulated to a certain extent. Such regulation can impose hourly rates, specific fees for certain services or fees calculated as a percentage of the value of a transaction. Fee regulation can take various forms. The most restrictive form of regulation is the imposition of mandatory fixed fees, which leaves no freedom whatsoever to negotiate fees between professionals and their clients. Mandatory maximum fees or minimum fees are less restrictive since they allow the professional to charge lower / higher fees.

Fee regulation in the form of mandatory fee schedules, imposed by a professional body or the government itself has long been widespread. However, in recent years these fee schedules have increasingly been challenged by competition authorities as being anti-competitive or against the public interest. Undoubtedly under the influence of the competition rules and their enhanced enforcement by the competition authorities, various professions in several jurisdictions have transformed their mandatory fee regulation into recommended fees. These

recommended fees are not binding to the providers of professional services but can function as a mere guideline in setting their fees.

Nevertheless, recommended fees can have a similar effect as a mandatory fee schedule when there is a possibility that setting a fee which deviates from the recommended fee, can be subject to disciplinary actions on the basis of other professional rules. For example, setting fees which are lower than the recommended fee can, in some professions, be considered as bringing the profession into disrepute⁵⁵ or generally being in breach of the profession's ethical rules⁵⁶. In such cases, chances that the professionals would readily deviate from the recommended fee schedule are reduced, and the practical consequence of the schedule could be akin to the effects of a mandatory fee schedule.

2.3.1. Theoretical arguments on fee restrictions

In defence of fee restrictions, it has been argued that such restrictions generate a number of *positive effects*.

First of all, fee regulations can be a useful tool to prevent the problem of 'adverse selection'. Consumers cannot judge the quality of services provided by professionals. Therefore, consumers will base their decision to purchase certain services mainly on the price and will not be willing to pay higher prices for higher quality. As a result, providers of higher quality services (with a higher price) may be driven out of the market, and entry of new high-quality service providers may be discouraged by the low income levels. This can result in a market with sub-optimal quality services. A fixed or minimum fee schedule may then overcome this problem and maintain the quality of services provided. Policy makers should be fully aware of the 'adverse selection' problem and refrain from introducing price competition as long as instruments to assess quality have not sufficiently been developed. In markets characterised by serious information asymmetries, where quality assessment does not (yet) reach the minimum level required to avoid adverse selection, fixed prices may be preferred to free tariffs.

⁵⁵ Love and Stephen (1999), at p. 1000.

⁵⁶ OECD (2000), at p. 25 § 1.

A maximum fee schedule may be helpful in dealing with the problem of ‘moral hazard’. Since a consumer of professional services, by lack of complete information, cannot estimate the desired price/quality level, a professional may be inclined to provide services of too high a quality and charge excessive fees, even if his client would be adequately served with a lower quality at a lower fee. A maximum fee schedule may protect consumers against such excessive charges.

Recommended fees can be a tool to inform consumers of the average fees to be paid for certain services. They can also alleviate the burden of drafting offers and/or negotiating individual fees. That way, recommended fees may reduce transaction costs and thus lead to lower fees. This is especially true in markets where search costs are high and where it may be useful for consumers to have information readily available.

On the other hand, fee restrictions may present a considerable *negative effect*.

A fee restriction reduces the level of uncertainty on the supply side and may limit or exclude competition between the professionals. This threatens to deprive the consumer of the advantages of a competitive market. These advantages not only include lower prices; it has also been argued that allowing competition on fees would stimulate efficiency and innovation in a profession. The removal of fee schedules and permitting competition on prices would therefore prove beneficial to consumers, especially for certain standardised services which are easily comparable⁵⁷. This is particularly true for fixed and minimum fees, which prevent any competition on prices and threaten to deprive consumers of the benefit of lower prices in a competitive market.

While maximum fees at first glance would seem to be solely in the benefit of consumers, they may have the effect of leading to a levelling of prices towards the maximum fee and thus have an effect equal to that of a fixed price. Recommended fees can have a similar effect: they can facilitate co-ordination of the competitive behaviour of professionals and thus lead to higher prices to the disadvantage of the consumer.

⁵⁷ OECD (2000), at p. 20 § 1, al. 2.

Thus, the removal of fee scales, whatever their nature, will not only improve price competition and efficiency, but may also lead to improvements in dynamic efficiency (in terms of, for example, new ways of providing services in the future). In addition, dynamic efficiency gains may occur through a low-cost incumbent undercutting competitors and forcing them to become more efficient.

While the critics of fee restrictions acknowledge that competition on fees may lead to adverse selection and moral hazard problems, they argue that rules on fees may not be the appropriate tool to address these problems. For example, setting minimum or fixed fees does not in itself guarantee that a desired level of quality level of the services will be offered. An alternative method, which is less restrictive of competition and would thus present less negative effects, is the mandatory publication of adequate information on quality and fees on behalf of the consumer.

From an economic point of view, these negative effects of fee regulation should be put into perspective and should not be overestimated. In spite of the existence of a fee regulation, some professionals may be inclined to disregard the regulation and offer services at lower prices than the mandatory/recommended fee. This behaviour has been described as ‘cheating’ or ‘chiselling’. It is generally agreed that it may not always be possible to prevent such cheating or chiselling, and that the ability to do so declines when the number of members of a certain profession is large.

2.3.2. Empirical evidence on the effect of fee regulation

While there have been some studies on the effect of fee schedules, empirical evidence on this topic remains overall limited and fragmentary. Moreover, most of the research is focused on the effect of recommended fees and on the existence of cheating or chiselling.

Button and Fleming⁵⁸ undertook a research into the consequences of the replacement of a mandatory fee schedule by a recommended fee schedule in 1982. Their research shows that, following this regulatory change, the fees charged by architects were slightly lower. However, the researchers point out that this effect may have been caused by circumstances presenting

⁵⁸ Button and Fleming (1992).

themselves before the regulatory change and may thus not have been caused thereby. This leads them to the conclusion that “with regard to fees and competition, self-regulation would appear to have been, in practice, marginally detrimental”.

As far as recommended fees are concerned, Arnauld and Friedland⁵⁹ have undertaken a limited research into the effects of a recommended fee in the lawyer profession in the US. They analysed the relationship between the existence of recommended fees and the income of lawyers for a standard transaction. Their conclusion was that the income of lawyers was positively related to the recommended fee in that the income rose with the recommended fee. However, this research does not allow to conclude that there is also a clear relationship between the existence of a recommended fee schedule and the actual fees that are being charged by lawyers. As Stephen and Love⁶⁰ point out, drawing this conclusion from Arnauld and Friedman’s research would only be possible if the demand for the standard transaction is inelastic.

Furthermore, research has been done into the existence of cheating or chiselling in the lawyers’ profession. The results thereof seem to suggest that cheating or chiselling on recommended fee schedules for lawyers does indeed exist. A report by Stephen⁶¹ into the effects of recommended fees for conveyancing services in Scotland showed that the fee schedule did not prevent a large number of the solicitors of charging a fee that was considerably lower than the fee recommended by the relevant professional association. Although only a limited number of professionals took part in this study, its results show that a cautious approach of the effects of fee regulation is justified. Later research by Shinnick⁶², as reported by Stephen and Love, confirmed these conclusions. He undertook research among Irish solicitors on the fees charged for conveyancing services and found that a large number of solicitors charged fees that were considerably lower than the recommended fee. His findings were once more confirmed by the research of Shinnick and Stephen⁶³ who also undertook a survey among Irish solicitors. They found that the recommended fee was disregarded at a large scale and that a large number of solicitors were charging fees considerably lower than the recommended fee.

⁵⁹ Arnauld and Friedland (1977).

⁶⁰ Love and Stephen (1999), at p. 1000

⁶¹ Stephen (1993).

⁶² Shinnick, Edward (1995), *The Market for Legal Services in Ireland*, paper presented at Irish Economic Association conference, quoted by Love and Stephen (1999), at p. 1001.

⁶³ Shinnick and Stephen (2000).

2.3.3. Conclusion on fee restrictions

While a number of arguments both in favour of and against fee schedules have been presented, there is only a limited amount of empirical evidence on this subject. The limited empirical evidence does not allow drawing hard conclusions on the positive or negative effects of fee regulation and certainly does not confirm the arguments claiming that such regulation mainly has negative effects. This is confirmed by the research on the possibility of cheating which suggests that the effect of fee regulation may be limited.

2.4 Advertising restrictions

Most professions have traditionally, to a certain extent, regulated the use of advertising. Such regulation could go from a total ban on advertising to the regulation of certain aspects of advertising. In recent times, these advertising restrictions have been put under great pressure by actions of consumer organisations and, particularly, competition authorities. For example, the European Commission has clearly stated that advertising should be allowed as a legitimate means of competition when it is based on verifiable and representative information⁶⁴.

Nevertheless, to some extent advertising restrictions remain in force in the majority of professions. Some professions in certain jurisdictions stick to a total ban on advertising; this is particularly the case in the medical professions in European countries. Other professions do allow the use of advertising in principle, but regulate the form or contents of advertising to a certain extent. Some professions may restrict the use of some forms of advertising such as television advertising or 'cold calling' or other specific types of advertising. Other professions may restrict the contents of the advertisement. For example, some professional organisations exclude or limit the possibility of advertising a specialised expertise that a member of the profession may possess. Furthermore, comparative advertising is generally not permitted in most professions.

⁶⁴ European Commission, Decision of 7 April 1999, case IV/36.147, EPI code of conduct, OJ L106/14 of 23 April 1999, rec. 41 and further.

2.4.1. Theoretical arguments on advertising restrictions

In spite of the fact that some regulatory bodies and competition authorities show a clear tendency in favour of advertising, several arguments *in defence of advertising restrictions* can be developed.

Advertising restrictions may prove to be a useful tool in overcoming some problems presented by the asymmetry of information between providers of professional services and their consumers. This asymmetry is caused by the fact that, by lack of information, consumers cannot assess the quality of professional services and the truthfulness of the information provided by the professionals on these services. Therefore, first of all, advertising restrictions prohibiting the use of potentially false and misleading advertising may be needed to protect the consumer.

Secondly, advertising restrictions may be a useful tool to prevent the problem of ‘adverse selection’ which could lead to excessive price competition among professionals and result in a reduction of the quality of the services provided in a market. Since consumers cannot judge the quality of services provided by professionals, they may base their decision to purchase certain services mainly on the price and will not be willing to pay higher prices for higher quality. As a result, providers of higher quality services who do not advertise or those who advertise higher prices may be driven out of the market. Since this may lead to lower income levels, this may also discourage entry of new high-quality service providers into the market, leading to a market with sub-optimal quality services. A restriction of advertising on fees may then cure this problem.

Thirdly, since consumers cannot assess the truthfulness of advertising by professionals, regulating advertising on non-price issues, e.g. on quality, may be necessary to prevent abuse. Professional services are so-called experience goods and an adequate assessment of their quality may only be possible in the long term, mainly by repeat buyers of these services. While this may guarantee a desired level of quality in the long term, this does not prevent certain professionals of using a so-called ‘fly-by-night’ strategy, i.e. offering services of a

lower quality than their reputation suggests⁶⁵. Therefore, regulation of the contents of advertising may be advisable.

Lastly, advertising restrictions have also been defended as a means to preserve the 'dignity' of the profession and professional integrity and independence. It is argued that these can be undermined by excessive competition between professionals.

On the other hand, advertising restrictions may also have certain *negative effects*.

Advertising can inform consumers about different types of services and the conditions under which they are being provided. In doing so, it allows consumers to make better informed decisions. While it cannot be excluded that consumers could gather the relevant information themselves, Stigler⁶⁶ has argued that advertising by the providers of services can substitute a large amount of searching efforts by a large group of consumers. That way, advertising may lead to a considerable reduction in searching costs.

By better informing consumers at a reduced cost, advertising can contribute to enhancing competition in markets. Furthermore, advertising can also inform consumers of new services or the existence of new service providers and thus stimulate innovation and entry into the market. Advertising restrictions threaten to reduce or eliminate these potentially positive effects. By increasing the cost of information gathering by consumers, advertising restrictions can reduce consumer information and lead to less competition between service providers. This could lead to a reduction in output and higher fees being charged. Furthermore, by limiting information on new services or new providers, innovation and entry may become less effective or non-existent since there is no or only a limited possibility to inform the consumers thereof. By making it more difficult to quickly generate goodwill, restrictions on advertising can that way, as Stephen and Love indicate⁶⁷, raise the cost of entry in a market and thus constitute an entry barrier.

The adversaries of advertising restrictions also point out that the arguments in favour of such restrictions have to be put into perspective. First of all, these arguments offer no justification

⁶⁵ Shapiro(1983).

⁶⁶ Stigler (1961).

⁶⁷ Love and Stephen (1999), at p. 994.

for prohibiting advertising that is relevant, truthful and not misleading. Secondly, it is argued that one of the main arguments against fee advertising (the adverse selection problem) is only relevant when this type of advertising is mainly or exclusively used by the providers of low quality services. When advertising on fees is allowed and high-quality providers also advertise on fees, it cannot be excluded that consumers may interpret low fees as corresponding to low quality services and, inversely, higher advertised fees as a sign of high quality. This may then mitigate the effects of the adverse selection problem⁶⁸.

2.4.2. Empirical evidence on the effects of advertising restrictions

From the foregoing, it is clear that empirical research into the positive and negative effects of advertising and advertising restrictions can focus on their impact on

- quality, to support the adverse selection argument
- prices / fees, to support the argument that advertising enhances competition and would lead to lower fees.

There have been a large number of studies on this topic. As a preliminary remark, however, it has to be stressed that these studies always focus on one particular type of advertising (restriction), in one particular profession and in one well-defined jurisdiction. It has to be borne in mind, therefore, that general conclusions on the effect of advertising restrictions seem hard to defend on the basis of these studies. Furthermore, while there have been numerous studies into the effect of advertising (restrictions) on prices and most of these studies show the same tendencies, the number of studies focussing on the effect on quality is more limited and their conclusions are less unanimous. In the light of this, the statement of the European Commission, that there exists “an increasing body of empirical evidence highlighting the negative effects of advertising restrictions”⁶⁹ has to be put into perspective.

EFFECT ON PRICES/FEES

As said, a large number of empirical studies have been undertaken into the effect of advertising or advertising restrictions on prices/fees. It has to be highlighted once more that these studies, in our view, do not allow drawing general conclusions that are valid for all

⁶⁸ See on this topic Rogerson (1988) and Rizzo and Zeckhauser (1992).

⁶⁹ European Commission (2004), at p. 45.

advertising restrictions in all professions. Nevertheless, one cannot deny that an overwhelming majority of these studies lead to the conclusion that restrictions on fee advertising seem to present negative effects. These studies have shown that the removal of such advertising restrictions results in enhanced competition on fees and thus leads to lower fees. Some studies also show that this provokes an increased demand for certain professional services. An overview of these studies can be found in Stephen and Love⁷⁰ and in a report by Indecon⁷¹.

A notable exception to this is the study by Rizzo and Zeckhauser⁷², whose research on advertising in the medical profession remarkably results in a different conclusion. Their research dealt with the impact of increased advertising by physicians on the price, quantity and quality of primary care physician services. They find that physicians who advertise charge higher prices than those who do not, suggesting that advertising may lead to higher fees being charged for these services. However, their research also showed that the physicians who advertised engaged in a smaller number of patient visits but, on average, spent more time per patient, which was translated as a sign of higher quality. This may be explained by a so-called selection effect, meaning that physicians who advertise may aim at preferring patients who are less price sensitive and willing to pay more for a higher quality service.

Obviously, this study in itself does not allow to conclude that fee advertising will automatically lead to higher fees. However, what this study in our view does show is that one cannot simply focus on the potential effects of fee advertising (restrictions) to prices in order to assess the effects of these restrictions, but that one rather has to analyse the 'broader picture'.

EFFECT OF ADVERTISING ON QUALITY

While, with the exception of the study by Rizzo and Zeckhauser, the empirical evidence on the effect of advertising on fees seems to suggest that these mainly have negative effects, the same cannot be said of the evidence on the effect of advertising on quality. Indeed, as Stephen

⁷⁰ Love and Stephen (1999).

⁷¹ Indecon (2003).

⁷² Rizzo and Zeckhauser (1992).

and Love⁷³ put it in relation to the legal profession, “empirical work on the quality of legal services in the presence of lawyer advertising does not present such a clear-cut view as that on fees”.

A study of Murdock and White seems to confirm, to a certain extent, the adverse selection argument. They undertook a study into the quality of services provided by lawyers, based on the perception of that quality by their peers and by judges. The conclusion of their research seems to be that lawyers that do use advertising are more likely to offer a lower quality of services than non-advertising lawyers⁷⁴.

At first glance, the same result seems to flow from the research by Cox, Schroeter and Smith. Their investigation into the effect of advertising by lawyers in different regions shows that in regions where advertising is widespread, the quality seems to be lower. However, there conclusion is mitigated by the fact that they found no significant difference in quality between advertising and non-advertising lawyers within the same region. However, a similar tendency is shown in the research by Kwoka on the effect of advertising on the quality of optometric services, which suggests that restrictions on advertising do not lead to higher quality⁷⁵.

Domberger and Sherr⁷⁶ seem to come to the opposite conclusion in their research on the effects of the liberalisation of conveyancing services in England and Wales in the 1980ies. This liberalisation included, among others, a relaxation of advertising restrictions. While the main focus of their research was the evolution of fees after this liberalisation, they also tried to gain insight into consumer’s perception on the quality of the services rendered. In their research, quality was represented by the time the conveyancing of the transaction took, the quantity and quality of information provided by solicitors, the access to the solicitor and the overall perception of the fact whether the consumers obtained ‘value for money’. They found that there was a clear improvement of the perceived quality in later years, which seems to suggest that the liberalisation, including the lowering of the advertising restrictions, enhanced the quality of the services.

⁷³ Love and Stephen (1999), at p. 997.

⁷⁴ Murdock and White (1985).

⁷⁵ Kwoka (1984).

⁷⁶ Domberger and Sherr (1989).

Love and Stephen ⁷⁷ quote an older research by Muris and McChesney from 1979 who also seem to have found that high advertising lawyers provide better quality services than traditional non-advertising lawyers. Stephen and Love consider these results difficult to judge since the researchers only indirectly entered the effect of advertising into their analysis.

These different results show that, on the basis of existing evidence, it is not possible to ascertain whether or not advertising creates a risk of adverse selection and whether advertising restrictions can be an adequate means to solve this problem.

2.4.3. Conclusion on advertising restrictions

A number of arguments both in favour of and against advertising restrictions can be developed. There is a large number of empirical evidence on the effects of advertising restrictions on fees, showing that these restrictions in most cases lead to less competition and, correspondingly, higher fees being charged. It has to be borne in mind, however, that these studies only relate to certain restrictions in particular profession in a single jurisdiction. In our view, they cannot corroborate a general conclusion on the undesirability of advertising restrictions. Furthermore, the same unequivocal conclusion can certainly not be drawn for the effect of advertising restrictions on quality. Studies on this topic show different results. From all this, it seems clear that the existing studies do not immediately allow hard general conclusions on the effects of advertising restrictions and that a sophisticated case-by-case analysis is required.

2.5 Restrictions on business organisation

All professions impose certain regulations concerning the way in which professionals can organise their business. Most of these regulations deal with the conditions under which professionals can form partnerships.

⁷⁷ Love and Stephen (1999), at p. 998.

2.5.1. Theoretical arguments on restrictions on business organisation

In most professions, cooperation through unlimited liability partnerships is allowed, whereas the formation of limited liability partnerships is excluded. A prohibition on the formation of limited liability partnerships is most commonly justified by the argument that unlimited liability has a strong disciplinary function towards the professionals grouped in the partnership. By the fact that members in the partnership may potentially face unlimited personal liability claims, it is thought that they will be inclined to exercise control over the services provided by their partners. This mutual control mechanism would then help guaranteeing the quality of the services being provided. A possible argument against such restriction may be that this is an unnecessary restriction of the commercial freedom of professionals since the interest of consumers may be adequately protected by imposing a mandatory liability insurance or by measures that ensure an adequate capitalisation of the partnership.

Most professions also prohibit so-called multidisciplinary practices (MDP), in which members of different professions cooperate. There are some clear arguments against MDP. In some professions (e.g. in the legal profession), MDP may threaten professional secrecy, in as far one cooperates with other professionals who are not bound by a similar professional secrecy. Also, MDP may lead to conflicts of interest to the detriment of the consumers. It is useful to remind that the European Court of Justice therefore decided that, as an exception to the rules of European competition law, restrictions on MDP in the legal profession could be justified in the light of their “objectives, which are here connected with the need to make rules relating to organisation, qualifications, professional ethics, supervision and liability, in order to ensure that the ultimate consumers of legal services and the sound administration of justice are provided with the necessary guarantees in relation to integrity and experience”⁷⁸.

On the other hand, MDP may also prove beneficial to consumers for a number of reasons. When the know-how of members of different professions can be coupled within the same partnership structure, they can offer a ‘full service package’ to consumers (also referred to as ‘one stop shopping’). The exchange of information between these professionals on specific matters can then take place ‘internally’, which can lead to scale benefits and a reduction of

⁷⁸ European Court of Justice, Decision of 19 February 2002, case C-309/99, *Wouters et al.*, ECR 2002, I-1577, rec. 97.

transaction costs. Further, a MDP allows for internal risk spreading, since different professions may face different business cycles and fluctuations in income may be then be smoothed across the group⁷⁹. All this could lead to lower prices to the benefit of consumers. Furthermore, easing restrictions on MDP could open up the road to easier access to capital that may be needed to invest in equipment and infrastructure to improve consumer services.

One could therefore argue that the aims of guarding professional secrecy and preventing conflicts of interest may be realised by other, less restrictive means. For example, professional secrecy could be guaranteed by imposing similar obligations onto all partners in an MDP⁸⁰. One could also imagine creating certain measures which prevent a flow of information from professionals in the partnership who are bound by professional secrecy, to those members in the partnership who are not (so-called ‘Chinese walls’). One could also argue that there is no reason to prohibit minority participations in the MDP by other professionals. The ‘Legal Practice Plus’ – model presented by the English Law Society could serve as an example. This model means that “a limited form of multi-disciplinary practice [...] would supply all the range of services normally provided by solicitors in practice, and would be open to non-solicitor partners or directors. Solicitors would remain in majority control, although a partnership with one solicitor and one non-solicitor partner (NSP) would be allowed. The only limitation would be that ‘an accountant NSP could not audit statutory accounts’⁸¹.

2.5.2. Empirical evidence on the effect of restrictions on business organisation

There is very little empirical evidence confirming any of the arguments presented in favour or against the restrictions on business organisation as discussed.

The argument in favour of prohibiting limited liability partnerships is put into perspective by a study by Stephen and Gillanders (1993), referred to by Stephen and Love⁸². They present evidence on mutual control within UK law firms. They find that such control mainly takes place *ex ante*, i.e. when partners in the firm are screening prospective partners, rather than *ex*

⁷⁹ Love and Stephen (1999), at p. 1005.

⁸⁰ Deards (2002), at p. 625.

⁸¹ See Lord Chancellor's Department (2002).

⁸² Love and Stephen (1999), at p. 1009.

post, i.e. under the form of control on professionals already in the partnership. This seems to undermine the main argument in favour of the existing restrictions.

Carr and Matthewson (1990)⁸³ have undertaken a research in which they compare law firms in US states where limited liability is permitted with those in which it is not. They found that the average size of law firms was larger in states where limited liability partnerships were allowed. They see this as a possible indication of efficiency gains, which pleads against maintaining restrictions on the formation of limited liability partnerships. A similar conclusion was drawn from the study by Button and Fleming (1992)⁸⁴ into the effects of the partial liberalisation of the professions of architects in the UK in the 1980ies. They found that the abolition of the rule preventing practice under limited liability led to a considerable growth in this form of organisation. Furthermore, this change also influenced the average size of architectural practices in that it led to an increase of the number of large size architectural associations.

As far as a restriction of MDP is concerned, Indecon⁸⁵ reports a study by the US Federal Trade Commission on the effect of MDP between dentists and dental hygienists. This study focused on differences between states where such cooperation was allowed and states where this was prohibited. They found that, in states where cooperation was allowed, the costs of individual treatments was 6 to 30 percent lower than in other states. This seems to suggest that MDP can indeed lead to lower prices to the benefit of consumers.

2.5.3. Conclusion on restrictions on business organisation

On the basis of the scarceness of available empirical evidence, it is hard to draw general conclusions on the effect of restrictions on business organisation. This surely is a topic that requires additional research. The existing evidence surely does not present any solid justification for any policy conclusions.

⁸³ Carr and Matthewson (1990).

⁸⁴ Button and Fleming (1992).

⁸⁵ Indecon (2003), at p. 47.

3. Deregulation of the notary profession in the Netherlands

The 1999 Dutch Notary Act has been the most ambitious deregulation initiative in the sector of the notary profession. Its objectives are to increase competition and improve the quality of the notarial services. Whereas there was a *numerus clausus* under the old Act, in the new regime the total number of notaries in the Netherlands is no longer capped. Entry into the notary profession remains regulated, however, since junior notaries must submit a business plan to a supervisory committee for approval. The most innovative element of the new Notary Act is the change from fixed to unregulated notary fees. The fees for family services and corporate services became free immediately after the entry into force of the new Notary Act, whereas the fees for real property services were gradually liberalised. As of July 2003, all notary fees in the Netherlands are free⁸⁶. The liberalisation of the notary profession is regularly evaluated in order to check whether the new law reaches its goals.

3.1. Impact of liberalisation on quality

Early evaluations of the reform of the Dutch notary profession indicated that the new Act does not really foster entry into the profession and that compliance with ethical rules is diminishing⁸⁷. The new Notary Act was meant to speed up the appointment of junior notaries into notary positions, but the number of such appointments did not markedly increase. The decline in the number of junior notaries was due to a reduction in the number of students rather than to an inflow into notary posts. Junior notaries also preferred to join existing offices rather than to open a new independent practice. This trend increases the size of incumbent notary offices and runs counter to the goals of increasing competition⁸⁸. As to the diminishing obedience of ethical rules, a recent survey conducted among 310 notaries and 193 junior notaries reveals that a large majority (68 percent) is of the opinion that in practice profit making is preferred to the quality of the notarial deed. According to 64 percent of the respondents, the interests of clients dominate the public interest. The majority of notaries (59 percent) considers having good contacts with large clients more important than the protection

⁸⁶ There are two exceptions to this rule : (1) maximum fees apply in case of family services for low-income households; (2) the competent Minister may intervene whenever necessary to guarantee accessibility of notarial services.

⁸⁷ *Eindrapport Commissie Monitoring Notariaat, periode 1999-2003* (2003).

⁸⁸ Nahuis and Noailly (2005)

of weak parties, who may be economically inferior and lack sufficient legal knowledge⁸⁹. These results show that concerns on how to survive in the competitive struggle may dominate ethical considerations and jeopardise the quality of the notarial services.

The most recent assessments of the liberalisation show varying results: it is interesting to contrast the Report of the Commission on Evaluation of the 1999 Notary Act (Hammerstein Commission) and the Report of the Netherlands Bureau for Economic Policy Analysis (CPB), both published in September 2005. The Report of the Commission on Evaluation of the 1999 Notary Act⁹⁰ mentions a number of benefits resulting from competition between notaries: increased cost efficiency, innovation (increased use of ICT), cost-oriented fees and price differentiation. The Hammerstein Commission did not find hard evidence to support the claim that competition has led to a substantial loss of quality and reduction of professional integrity⁹¹, but nevertheless admits that there may be a reduced offer of services in particular market segments. After the liberalization of fees in the family practice, some notaries try to save on costs by spending less time on information and advice to clients. The Hammerstein Commission concludes that “The role of the notary in providing information is particularly at risk”.

It is also interesting to mention that the Hammerstein Commission asked the Research Bureau EIM to investigate whether the fear that price competition lowers quality is justified. To this end, information on the number of corrections in the Land Register for the year 2004 was collected in order to compare the measurable aspects of the legal quality (i.e. notaries’ craftsmanship) provided by so-called price fighters and notary offices charging higher prices. It was found that errors (lack of registration or mistakes requiring corrections) were made in 1.2 percent of all acts authenticating transfer of property and creating mortgages. Differences appeared to be great across notary offices and regions, but price fighters did not perform worse than other notaries. The EIM also conducted interviews with large commercial clients (real estate agents, mortgage agents and real estate project managers) and found that customer satisfaction has increased. Half of the respondents experienced an improvement of customer

⁸⁹ Laclé (2005)

⁹⁰ Commissie Evaluatie Wet op het notarisambt, *Het beste van twee werelden* (2005).

⁹¹ “There are no clear indications of an unacceptable reduction in the quality of services”, translation by the Koninklijke Notariële Beroepsorganisatie, *Evaluation of the Dutch Notaries Act*, (2005), p. 5

service. In the view of the large commercial clients, the prices of the notarial deeds have decreased and the quality has remained constant.⁹²

The Report by the Netherlands Bureau for Economic Policy Analysis⁹³ is more critical. This study casts serious doubts about the effectiveness and desirability of the reform. The authors of the CPB Report found no significant difference between the level of competition in 1996 (three years before the liberalisation) and 2002 (three years after the liberalisation) on local markets for family services and small scale real estate transactions⁹⁴. On the national market for professional consumers (market for corporate services and large scale real estate transactions), the results were more mixed and there is some evidence of increased competition. As to the effects on quality, the researchers found support for the fear that competition may deteriorate quality. Two different aspects of quality were investigated: service satisfaction as measured in consumer surveys and quality aspects that are not observable by consumers. Consumer surveys indicated that competition has a negative effect on quality, notably on the friendliness and the time spent to proceed the transaction. A comparison of the number of corrections in notarial deeds at the Land Register for the years 1995 and 2003 showed that in the latter year notaries' offices in oligopolistic markets provide lower quality than monopoly offices. This was not the case in 1995 and it suggests that competition leads to a deterioration of quality. This result seems different from the above mentioned study by the Research Bureau EIM, commissioned by the Hammerstein Commission, in which it was found that notaries charging very low tariffs do not make more mistakes than notaries charging higher prices. However, the different results may be explained by the fact that the EIM study compares quality across different regions in the liberalised market and not quality before and after the deregulation of the Dutch notary profession⁹⁵.

In sum, the evaluations of the 1999 Dutch Notary Act seem to call for a greater reluctance in introducing competition in the notaries' market, certainly as long as mechanisms to guarantee quality are not (yet) put in place. It also seems clear that competition tends to benefit above all

⁹² R. Vogels (2005).

⁹³ R. Nahuis and J. Noailly (2005).

⁹⁴ The report uses two different indicators for measuring the level of competition before and after the liberalization: a relative-profit indicator and a variation of the Bresnahan-Reiss indicator. The first method is based on the idea that an increase in firms' efficiency reflects an increase in competition. The second indicator measures by how much profit margins decrease as new competitors enter the local market.

⁹⁵ Also the variables to measure quality were not completely identical in both studies.

larger clients and may harm small consumers who suffer from information asymmetries in the market for notary services.

3.2. Impact of the liberalisation on prices and accessibility of services

The Dutch experience not only confirms the risk that competition in the markets for notary services may not work properly because of information asymmetries and jeopardise quality. It also shows that provision of public goods may be put at risk by increasing competitive pressures. In a regulated market, less profitable services may be cross-subsidised by gains in more lucrative market segments. Deregulation will cause prices to sink in the profitable market segments ('cream skimming') but lead to price increases for the previously cross-subsidised services. The deregulation of the market for notary services in the Netherlands corroborates this outcome.

In the Netherlands, services in family practice have long been subject to fixed tariffs. Following legislative changes in 1999, these tariffs were liberalised so that Latin notaries were henceforth free to establish their tariffs for these services (they only had to take account of certain price ceilings for low-income clients). On the basis of the classical anti-regulation arguments, one could have expected that tariffs would decrease following this liberalisation. Strikingly, however, this liberalisation caused a substantial increase in fees for services relating to wills, while the consumers' perception on the quality of services remained basically the same⁹⁶. Recent figures show that the price of a will almost doubled (increase of 97 percent) whereas the prices of a marriage contract and a partnership agreement increased by 60 percent and 39 percent, respectively.⁹⁷

Aalbers and Dykstra⁹⁸ have searched for possible explanations for this increase in prices. According to them, two possible explanations could be given:

- either Latin notaries started charging supra-competitive prices. This would mean that Latin notaries were using their market power to operate on a suboptimal efficiency level and realise excess profits for services in family practice.

⁹⁶ EIM (2002).

⁹⁷ Commissie Evaluatie Wet op het notarisambt (2005)

⁹⁸ Aalbers and Dykstra (2002).

- or the increased tariffs were nothing more than the reflection of the normal cost-based price level. This would mean that the previous fixed tariffs did not cover the cost of services in family practice and that family practice was unprofitable. Latin notaries then must have been cross-subsidizing, i.e. using the profits they earned in other areas of activity to cover the losses taken in family practice.

To assess which of these possible explanations is valid, Aalbers and Dykstra undertook a research to see whether Latin notaries were either operating inefficiently, or whether they had been cross-subsidising. Their analysis showed that Latin notaries' efficiency did not differ from the efficiency of other professions. While some Latin notaries had very high costs, this was not caused by inefficiency but rather by the fact that some Latin notaries, especially the ones established in the countryside, were not able, due to external circumstances, to operate on a larger scale. On the other hand, Aalbers and Dykstra did find that a substantial number of Latin notaries had indeed been cross-subsidising. This supports the view that family practice was unprofitable.

It can be assumed that all persons will, on a number of occasions in their life, be confronted with aspects of family law. As explained in the foregoing, these matters may also concern third parties and society as a whole. It is therefore likely that governments will consider it desirable that persons can use the assistance of well-informed professionals for these matters at a reasonable price. However, if family practice is unprofitable, this aim will not be realised under normal market conditions. Professional service providers will then either not provide these services or will have to charge extremely high fees, so that only a limited number of well-earning persons are able to purchase their services.

In order to ensure that fees remain low and that all citizens can afford to purchase these services, the government then has to design a mechanism by which, on the one side, professionals are obliged to offer these services at a reasonable price while, at the other hand, the losses they incur in offering family practice services can be compensated. This may be achieved when these professionals can obtain higher profits in other areas of activity, thereby allowing them to cross-subsidise. This can be organised through granting certain monopoly rights for these other areas, possibly coupled with quantitative restrictions. This monopoly right and the fact that there are only a limited number of professionals, can then guarantee sufficient profits to compensate for the losses they incur in family practice.

The Latin notary profession clearly corresponds to such system in which certain monopoly rights for profitable activities (real estate transactions and services for businesses) are granted in order to compensate for the losses that seem to be incurred in family practice. It can therefore be argued that the current organisation of the Latin notary profession is necessary to ensure that certain desirable services relating to family law can be provided to all at a reasonable cost.

CONCLUSIONS AND OUTLOOK

1. Summary of the main findings

This report departed from the view that the European Commission's initiative to evaluate the regulation of professions offers an interesting starting point for thorough scientific research. The European Commission acknowledges that professional regulation may have both positive and negative effects. On the one hand, certain aspects of regulation may have anti-competitive effects and lead to welfare losses. On the other hand, professional regulation may be needed to alleviate the effect of market imperfections, such as the existence of asymmetric information, externalities and public goods.

In the first chapter, we described the main tasks of the Latin notary and the regulation of this profession. Certain aspects of the current regulation have been criticised for their potentially anti-competitive and welfare reducing effects. We argued that these criticisms could be mitigated by the fact that the classical anti-regulation arguments may not be entirely valid when assessing the effects of the regulation of Latin notaries. Moreover, we stressed that the Latin notary profession and its regulation may generate certain substantial benefits. Regulation of the Latin notary profession may not only be needed to alleviate information problems; it may also be desirable to ensure the realisation of substantial positive externalities in the form of increased legal certainty.

Through his mediation as a neutral and impartial authority, the Latin notary will reduce the number of potential disputes on legal transactions. This will not only benefit the parties to these transactions, but also society as a whole. Furthermore, the Latin notary has to assume certain responsibilities relating to the gathering of tax information or the collection of taxes. That way, he contributes to an effective and efficient collection of taxes which is also in the benefit of society as a whole. We identified such positive externalities in each of the areas of activity of the Latin notary.

Unfortunately, the European Commission seems to rely too heavily on the results of the IHS study and other limited empirical evidence that suggests that regulation mainly has negative

effects. In the second chapter of the report, we showed that the IHS study has been criticised on a number of grounds and should not form the basis for specific policy conclusions. Furthermore, we gave an overview of theoretical arguments in favour and against the most common types of regulation and the existing empirical evidence in support thereof.

It is clear that for all these types of regulation a number of theoretical arguments both in favour and against these restrictions can be defended. However, while most of these arguments seem valid, none of them has been unequivocally confirmed by empirical evidence. As far as monopoly rights are concerned, some empirical evidence seems to confirm the common assumption that monopoly rights lead to higher fees to the detriment of consumers. However, some recent studies on the effect of the abolishment of the monopoly for conveyancing services in England and Wales show that competition does not automatically guarantee lower fees and suggest that a number of other factors may be of importance in studying the effects of monopoly rights.

Entry restrictions are often presumed to have a negative effect on the number of professionals, on output and on prices. Nevertheless, empirical evidence on this subject is limited and fragmentary and presents varying results. The main argument in favour of entry restrictions is that they may enhance the quality of the services that are being provided. Since quality is difficult to measure, here too empirical evidence is scarce and, on top of that, shows different results.

The same goes for fee restrictions. There are only a limited number of empirical studies on this subject; these do not allow to draw hard conclusions on the existence of positive or negative effects of fee regulation. Some of these studies indicate that the effect of certain fee restrictions may be limited by the possibility of cheating.

There is a large number of empirical evidence on the effects of advertising restrictions on fees. Most of these studies seem to confirm the view that advertising restrictions may reduce competition and lead to higher fees. However, there is little evidence on the effect of advertising restrictions on quality. Furthermore, here too, the existing evidence shows quite varying results.

Finally, the scarce empirical evidence on the effect of restrictions on business organisation does, in our view, not offer substantial support for any of the arguments for or against these restrictions.

In short, what little empirical evidence on the effect of professional regulation is available, shows varying results and does not allow to unequivocally confirm the arguments for or against regulation. Furthermore, as a general remark, it has to be stressed that all of these studies only relate to certain restrictions, for certain professions and in certain jurisdictions. In our view, they do not allow to draw general conclusions on the (un)desirability of these restrictions.

2. Outlook

This report does not contain a plea in favour or against specific forms of regulation of any profession. But in our view, it does show that there are no miracle formulas to decide if and to what extent regulation of a certain profession is necessary or justified. Such decisions can only be made on a case-by-case basis. We believe that this report shows that policy decisions regarding the regulation of professions should not focus on the limited amount of existing evidence but should be based on careful, well balanced and thorough theoretical and empirical analysis for each type of regulation and for each profession. This is particularly the case for the Latin notary profession, for which it should be established to what extent the substantial benefits it may generate may counterbalance any anti-competitive disadvantages.

To indicate the lines along which future empirical work could be carried out, we will give as an example a possible analysis of the social costs and benefits of a compulsory intervention by a Latin notary in a real estate transaction (sale of a house). In the Anglo-Saxon system, parties to real estate transactions wishing to obtain the necessary information and to be protected from mistakes and illegalities must seek assistance from their own lawyers and must assure their ownership by taking title insurance. Before it can be concluded that a registration system is cheaper than the intervention by the Latin notary, the costs of legal advice by (two) lawyers and the title insurance must be added to the costs of registration.

Economic theory predicts that the title insurance fee will be higher than the (part of the) notary fee for checking the legal validity of the transfer of property. Under a voluntary system, in which buyers are free to decide whether they take title insurance or not, insurance companies will ask a premium that corresponds to the expected costs of average legal problems. This fee may be too high for potential buyers who expect minor legal problems, so that only buyers who expect serious legal problems will find it interesting to buy title insurance. This may lead to a process of adverse selection, leaving insurance companies only with the high risks and causing further increases of the insurance premium. A mandatory intervention by a Latin notary can be seen as a compulsory insurance against legal problems with ownership. In this way, adverse selection in insurance markets may be overcome since both high risk and low risk buyers must obtain insurance coverage. Admittedly, empirical work is needed to confirm the predictions from economic theory but insights from the latter already warn against a too rapid and unconditional deregulation of the Latin notaries' monopoly.

Moreover, a registration system will not generate the same positive externalities as the Latin notary profession does. To conduct a full cost-benefit analysis, again not only the costs of registration and the notary fee for the transfer of real estate property can be compared. It is indispensable to quantify the positive externalities generated by the Latin notary profession. Besides higher title insurance fees, increased legal uncertainty may cause a lower willingness to invest in the improvements of houses and more expensive mortgages. Also on this point, empirical work should be conducted to see whether these detrimental effects do materialise in countries without a Latin notary system. The best way to assess the legal certainty generated by the Latin notary profession is to look at the ratio of law suits concerning real estate related to other law suits (thus correcting for country specific circumstances influencing the overall number of law suits). Latin notary mediation is likely to reduce the number of legal procedures that will be initiated. Data on the yearly expenses incurred by insurance companies on law suits (related to real estate and others) give an indication of the number of suits, provided that the average cost per suit is known. Another way to assess the legal certainty generated by the Latin notary profession is to compare the difference between the interest rate on mortgage loans and other loans in countries where the intervention of a notary is required and countries without a Latin notary system. If the difference is unequal, mandatory intervention of a Latin notary provides more legal certainty. Such information

seems crucial for assessing the desirability of reserved tasks for Latin notaries in the field of conveyancing.

Finally, under a registration system, a number of public tasks performed by Latin notaries (gathering and provision of information on real estate transactions, tax collection, archiving) must be performed by civil servants. Compared to Latin notaries who can act as individual enterprises willing to improve their competitive position towards other notaries, civil servants may have fewer incentives to operate efficiently. This may lead to more arrears in the collection of real estate taxes, and involve higher costs for the government budget.

In sum, empirical research could show that from a cost-benefit perspective, mandatory intervention by a Latin notary is superior to a registration system entrusted to civil servants. This could support the conclusion that the organisation of the Latin notary profession decreases transaction costs and ensures the provision of public goods without causing disproportionate restrictions of competition. Consequently, reserved tasks of notaries could be qualified as restrictions of competition that do not go further than necessary to guarantee the provision of public goods by increasing legal certainty. Again, as long as reliable empirical work is lacking, any policy conclusion on the desirability of reserved tasks in the field of conveyancing is premature.

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