

THE EMERGENCE OF GROUP AND PREPAID LEGAL SERVICES: EMBRACING A NEW REALITY

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I. INTRODUCTION

Group and prepaid legal service plans have grown from humble beginnings to now having a strong foothold in “voluntary benefits packages in the country’s largest companies and some of [its] smallest local employers.”¹ Although estimates vary, it appears that as many as twenty to forty percent of Americans are covered by some form of legal services plan.² Group and prepaid legal services have emerged as a viable alternative for a vastly underserved and unserved segment of Americans. However, this emergence came with significant obstacles, and the burdens that squelched group and prepaid legal services in the beginning still exist in today’s legal marketplace, albeit in a less restrictive form. The continued success of group and prepaid legal service plans will require embracing a new reality that incentivizes innovation in the incorporation of non-lawyers in the legal marketplace and the manner in which legal services can be delivered.

As new legal service providers with disruptive business models, such as web-based providers of legal services and group and prepaid legal services, enter the legal landscape, legal consumers and investors are beginning to take notice and advantage. With multiple million-dollar acquisition deals and capital investments, these new methods of legal service delivery are primed to make a disruptive entrance.³ With the legal market in a state of flux, the time for new and

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¹ Nathan Solheim, *A Positive Verdict on Group Legal Plans*, BENEFITSPRO (Mar. 05, 2012), <http://www.benefitspro.com/2012/03/05/a-positive-verdict-on-group-legal-plans>.

² Judith L. Maute, *Pre-Paid and Group Legal Services: Thirty Years After the Storm*, 70 FORDHAM L. REV. 915, 916 (2001).

³ John Wallbillich, *LegalZoom: Substance Over Forms?*, WIREDGC, (May 4, 2011), *archived at* www.webcitation.org/6EBdp6sDX (announcing two venture capitalists' investment in

innovative legal service delivery methods seems to have arrived. However, as these new innovators attempt to enter the legal landscape, the tension between the new kids on the block and the old guard appears to be escalating. As a profession that has historically proven resistant to change, and as a profession with over \$200 billion in revenue at stake, it will be interesting to watch the development of the ethical and legal issues that are now arising.⁴

This essay will analyze the group and prepaid legal services industry and how regulatory mechanisms must change in order to create a conducive environment that will foster the necessary innovation to allow this industry to continue to thrive. Part II will examine the tortured history of group and prepaid legal services, with a particular focus on early regulatory obstacles. Part III will discuss the rapid growth of the group and prepaid legal services industry through the employee benefit plan vehicle, positive tax treatment, and the commercialization of prepaid legal plans to the general public. Part IV will describe how modern group and prepaid legal service plans operate, focusing primarily on the financial details of particular plans offered, services that are generally covered under the plans, and how legal service providers provide their services and receive payment for the services provided. Part V will analyze the current state of regulations and rules governing group and prepaid legal services plans, with a particular focus on state commerce, insurance regulations, and state supreme court governance. Part VI will describe how evolving regulatory schemes can have a positive effect on the group and prepaid legal services industry in order to foster an environment that incentivizes innovation and that will aid in the continued growth of the group and prepaid legal services industry. Part VII concludes the essay.

II. HISTORY OF GROUP AND PREPAID LEGAL PLANS

Throughout history, ethical rules governing advertising, solicitation, and volunteering legal advice have cast lawyers in a “passive and reactive [role].”⁵ Although this system worked relatively efficiently for sophisticated, repeat users, it made finding a competent legal representative for occasional users a much more arduous task.⁶ Moreover, it was an even more burdensome task to find a

LegalZoom); Gerald J. Clark, *Internet Wars: The Bar Against the Websites*, 13 HIGH TECH. L.J. 247, 248 (2013).

⁴ See Daniel Fisher, *Silicon Valley Sees Gold in Internet Legal Services*, FORBES (Oct. 5, 2011), archived at www.webcitation.org/6EC1CrAiP (reporting fee billings by 160,000 law firms in a year).

⁵ Maute, *supra* note 2, at 917.

⁶ *Id.* (“The model worked reasonably well for some sophisticated consumers of legal services, particularly repeat users, who had established contacts with the legal community and access to reliable information about lawyers competent in their area of need.”).

competent lawyer to provide representation for an affordable price.⁷ This environment made access to justice more difficult for both poor and middle-income Americans.

Charitable societies, such as legal aid offices, were the first attempts at introducing lay intermediaries into the legal service profession to aid those who were recognized as not possessing the requisite financial means to procure competent legal representation.⁸ This liberal approach was viewed as “symbolic” by commentators during the early twentieth century, since the organized bar still stressed that “[a] lawyer’s responsibilities and qualifications [were] individual.”⁹ This was particularly evident to organizations that wished to assist their members with personal legal matters, because “[a] lawyer could accept employment from an organization regarding its own legal matters, but could not render legal services to its members regarding their individual affairs.”¹⁰

Until the mid-1960’s, ethics rules governing the prohibition of lawyers’ involvement with group legal services were viewed as overly strict.¹¹ Then, beginning in 1963, the first of three groundbreaking Supreme Court cases all but required the organized bar to relax its strict rules governing group legal services.¹² In *NAACP v. Button*, the Supreme Court held “that the [NAACP] had a constitutionally-protected right of political association to make available attorneys willing to bring civil rights and desegregation cases on behalf of its members. The Commonwealth of Virginia had no compelling state interest sufficient to justify its strict antisolicitation statutes.”¹³ Until that time, the Supreme Court had never found “a fundamental and potentially absolute constitutional restriction upon the power of the states to regulate the practice of law.”¹⁴ However, although the *NAACP* case was groundbreaking, most lawyers were not alarmed by its holding and “pigeonholed it as a special case involving civil rights.”¹⁵

⁷ *Id.*

⁸ *Id.* at 918; *See also* CANONS OF PROF’L ETHICS, Canon 35 (1908) (excluding “charitable societies” from the rule prohibiting interference by lay intermediaries).

⁹ *Id.*; *see* Maute, *supra* note 2, at 918.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.* (“A trilogy of Supreme Court decisions in the mid-1960’s forced the organized bar to relax strict ethics rules prohibiting lawyers’ involvement with group legal services.”).

¹³ *Id.*; *NAACP v. Button*, 371 U.S. 415, 415 (1963).

¹⁴ Barlow F. Christensen, *Regulating Group Legal Services: Who is Being Protected--Against What--and Why?*, 11 ARIZ. L. REV. 229, 231 (1969).

¹⁵ Maute, *Pre-Paid and Group Legal Services: Thirty Years After the Storm*, at 918.

The truly earth-shaking consequences of the *NAACP* case were not recognized until the following year with the Supreme Court's ruling in *Brotherhood of Railroad Trainmen v. Virginia ex rel Virginia State Bar*. In order to assist its members, the Brotherhood of Railroad Trainmen ("BRT") "recommend[ed] to Brotherhood members and their families the names of lawyers whom the Brotherhood believe[d] to be honest and competent."¹⁶ Virginia attempted to file an injunction, "claiming [BRT] violated antisolicitation rules" and was engaging in the unauthorized practice of law.¹⁷ Again, this time to the surprise and dismay of the organized bar, the Supreme Court disagreed with the Commonwealth of Virginia and held that the state's regulatory effort violated protected rights of "free speech, petition and assembly."¹⁸ Immediately after the Supreme Court's ruling, the American Bar Association ("ABA") and forty state bars joined in opposition and filed an application to appear as *amicus curiae*, seeking a rehearing of the issue.¹⁹

Railroad Trainmen introduced the organized bar to a new reality and forced them to embrace the evolution of the legal marketplace and change in the delivery of legal services.²⁰ After *Railroad Trainmen*, ABA President Lewis F. Powell, Jr., in order to appease reformers, made a commitment to overhaul the Canons of Professional Ethics and create a new set of rules and standards that would be appropriate for the changing legal landscape.²¹ Under President Powell's leadership, two committees were created to oversee the revision of the ethics rules, study the needs of the middle class, and create viable mechanisms to address the needs of the middle class.²² The first committee, the Special Committee on Evaluation of Ethical Standards, or the "Wright Committee" (named for its chair, Edward L. Wright), undertook the task of revising the ethics rules.²³ The second committee, the Special Committee of Availability of Legal Services, or the "Availability Committee," was tasked with studying the unmet

¹⁶ *Brotherhood of Railroad Trainmen v. Virginia ex rel Virginia State Bar*, 377 U.S. 1, 1 (1964).

¹⁷ *Id.*; Maute, *supra* note 2, at 918.

¹⁸ *Brotherhood of Railroad Trainmen*, 377 U.S. at 5.

¹⁹ Maute, *supra* note 2, at 918.

²⁰ *Id.* at 919.

²¹ *Id.* (discussing the ABA President's commitment to "revamp the outdated Canons in order to avert reformers' efforts to create a government-subsidized legal service program that would undermine traditional professional concerns, and to improve access to services by the middle class"); see also Lewis F. Powell, Jr., *The President's Page*, 51 A.B.A. J. 3, 20 (1965).

²² Maute, *supra* note 2, at 919.

²³ *Id.*

needs of the middle class and creating viable mechanisms to address those needs.²⁴

Although the ABA's focus was on revamping and improving the delivery of legal services to the middle class, its approach was still considered conservative.²⁵ This was particularly true concerning group and prepaid legal services.²⁶ Canon 2 of the Canons of Professional Conduct, which dealt with the professional duty to increase the availability of legal services, consumed about half of the Wright Committee's time during committee meetings.²⁷ However, while the ABA committees dealt with revamping the Canons of Professional Ethics, the Supreme Court gave its final say on the issue of group legal service plans.

In *United Mine Workers v. Illinois State Bar Association*, the Supreme Court held that a closed-panel plan in which the union referred injured members' compensation claims to a private lawyer salaried by the union was constitutional.²⁸ In that case, the Illinois State Bar Association sought to enjoin the United Mine Workers of America (the "Union") from certain practices it considered to be the unauthorized practice of law.²⁹ The Union argued that it established its legal department "in the interests of [its] members" and to deem that as the unauthorized practice of law was tantamount to infringing upon its "freedom of speech, assembly, and petition."³⁰ The Court agreed with the Union, and, citing both *NAACP* and *Railroad Trainmen*, added that although those two prior cases were "characterized as a form of political expression," those decisions should not "be so narrowly limited."³¹ The Court held that "the First and Fourteenth Amendments [gave] [the Union] the right to hire attorneys on a salary basis to assist its members in the assertion of their legal rights."³²

²⁴ *Id.*

²⁵ *Id.* at 920 (discussing the organized bar's conservative resistance to group legal services).

²⁶ *Id.*

²⁷ *Id.* at 919-20; Interview by Olavi Maru with Edward L. Wright, Chair of the ABA Special Committee on Evaluation of Ethical Standards (the "Wright Committee") (Oct. 28, 1976), <http://www.abf-sociolegal.org/oralhistory/wright.html>.

²⁸ *United Mine Workers of Am. v. Ill. State Bar Ass'n*, 389 U.S. 217, 217 (1967).

²⁹ *Id.* at 218 (explaining that the "Union employ[ed] one attorney on a salary basis to represent members and their dependents in connection with claims for personal injury and death under the Illinois Workmen's Compensation Act").

³⁰ *Id.* at 220-23.

³¹ *Id.* at 221.

³² *Id.* at 221-22.

After the Supreme Court's ruling in *United Mine Workers*, the ABA realized that it had considerable work to do to bring its rules within compliance.³³ However, although some voices within the bar called for the abandonment of "traditional restraints on advertising and solicitation as applied to group legal services," the majority of ABA members strongly opposed any proposal that called for the expansion of group legal services.³⁴ The main concerns voiced were "[l]oss of the independence of the bar, loss of the traditional client-lawyer relationship, the encroachment of advertising, solicitation and the morals of the marketplace, [and] a reduction in the quality of legal services."³⁵

Although cloaked in seemingly good intentions and healthy debate, tones of economic protectionism abound in the ABA's revision of the Canons of Professional Conduct.³⁶ The organized bar found itself trying to simultaneously accept the new reality of constitutionally-protected group legal services, while, as the former ABA President Chesterfield Smith put it, "intelligently regulat[ing] [group legal services] by pointing out the evils which [were] legitimate and proper . . . to protect."³⁷ To ensure this proper regulation, in January 1969, the Wright Committee circulated proposed rule DR 2-103(D)(5).³⁸ The rule stated, in pertinent part:

[A]ny other non-profit organization that recommends, furnishes, or pays for legal services to its members or beneficiaries, but only in those instances and to the extent that *controlling constitutional interpretation at the time of the rendition of the services requires the allowance of such legal service activities*, and [subject to specified restrictive conditions] only if the following conditions, unless prohibited by such interpretation, are met: (a) The primary purposes of such organization do not include the rendition of legal services; (b) The recommending, furnishing, or paying for legal services to its members is incidental and reasonably related to the primary purposes of such organization; (c) Such organization does not derive a financial benefit from the rendition of legal services by

³³ See Maute, *supra* note 2, at 920 (discussing the ABA committees' clear understanding that the Canons would require considerable revision to bring them into compliance with the Supreme Court rulings).

³⁴ Maute, *supra* note 2, at 921-23; see 1969 Reports of the ABA House of Delegates Meeting 65-66 (August 12, 1969). (hereinafter "ABA Hearings").

³⁵ Maute, *supra* note 2, at 921-23.

³⁶ *Id.* at 923-24 (discussing how economic protectionism resonated "in the comments by a representative of the Illinois State Bar Association" when discussing the possible ramifications of expanding the role of group legal services in the legal marketplace).

³⁷ *Id.* at 923.

³⁸ *Id.* at 921.

the lawyer; (d) The member or beneficiary for whom the legal services are rendered, and not such organization, is recognized as the client of the lawyer in that matter.³⁹

The Code of Professional Responsibility (the “Code”) was adopted without amending the provision governing group legal services.⁴⁰ Per usual, many jurisdictions adopted the Code as it was drafted by the Wright Committee.⁴¹ However, “a substantial number revised or omitted the controversial provisions on group legal services.”⁴² As amendments to the group legal services provision of the Code garnered further attention and criticism, it became clear to members of the ABA that an amendment was necessary.⁴³

Although the ABA was in agreement that an amendment to the group legal services provision of the Code was necessary, a division still remained among ABA members over the substance of the amendment.⁴⁴ Many ABA members campaigned for a more hostile approach to group legal services, while other members pushed for a more lenient approach.⁴⁵ In what are known as the “Houston Amendments,” the opposed members prevailed and “substituted the hopelessly uncertain reference to controlling constitutional interpretations with detailed and discriminatory restrictions on [group legal service] plans.”⁴⁶ However, due to vocal criticism, no state adopted the amendment, and it was later replaced by an amendment that eliminated the majority of discriminatory burdens that existed in its predecessor.⁴⁷

With the advent of the Model Rules of Professional Conduct (the “Model Rules”) in 1977, group legal services made a long-awaited step towards mainstream acceptance as a permissible delivery method of legal services. Although the Model Rules prohibit partnerships with non-lawyers where “any of the firm activities involve legal practice,” they did allow for “experimentation in

³⁹ *Id.* at 921-22; R.W. Nahstoll, *Limitations of Group Legal Services Arrangements Under the Code of Professional Responsibility, DR 2-103 (D)(5): Stale Wine in New Bottles*, 48 TEX. L. REV. 334, 344-45 (1970) (reproducing the text of the Proposed Final Draft) (emphasis added).

⁴⁰ Maute, *supra* note 2, at 924.

⁴¹ *Id.* at 925.

⁴² *Id.*

⁴³ See J. Robert Kramer II, *Note, Group Legal Services: From Houston to Chicago*, 79 DICK. L. REV. 621, 622-23 (1975).

⁴⁴ Maute, *supra* note 2, at 925.

⁴⁵ *Id.*

⁴⁶ *Id.*; see Kramer, *supra* note 43, at 623.

⁴⁷ Maute, *supra* note 2, at 926.

[new] methods” of delivering legal services.⁴⁸ Over time, the organized bar continued to relax its restrictions on group and prepaid legal services.⁴⁹

The organized bar’s shift from a closed approach to a more open approach in the treatment of group and prepaid legal services was made apparent by two ABA ethics opinions in the mid-1980’s. First, in 1985, ABA Informal Opinion 85-1510 “determined that the Model Rules permitted lawyer participation in a for-profit lawyer referral service, as long as the lawyer did not pay a fee or share legal fees with the service.”⁵⁰ Second, and more importantly, in 1987, ABA Formal Opinion 87-355 “allowed participation with any for-profit prepaid legal service plan that complied with other provisions of the Model Rules.”⁵¹

Although ethics opinions purport to merely interpret existing rules and hold no actual force of law, ABA Formal Opinion 87-355 was viewed as a significant endorsement of group and prepaid legal service plans because it endorsed permissible lawyer participation in group legal service plans without imposing heavy restrictions on them.⁵² Furthermore, ABA Formal Opinion 87-355 went a step further by identifying five ethical concerns that the ABA deemed important when evaluating whether lawyer involvement was permissible under the Model Rules: independent judgment, confidences, conflicts, competence, and marketing.⁵³ Independent judgment reigned supreme as the most important concern to the ABA.⁵⁴

In recent years, the loosening of restrictions upon group and prepaid legal services has continued, albeit at a slow pace.⁵⁵ Group and prepaid legal plans are now a “fact of life” and, compared to the organized bar’s past hostility towards them, are mostly a “non-issue.”⁵⁶ The ABA has made attempts to embrace this

⁴⁸ *Id.* at 929.

⁴⁹ *Id.*

⁵⁰ *Id.* at 930; ABA Comm. on Ethics and Prof'l Responsibility, Informal Op. 85-1510 (1985).

⁵¹ Maute, *supra* note 2, at 930; ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 87-355 (1987).

⁵² Maute, *supra* note 2, at 930.

⁵³ *Id.* at 931.

⁵⁴ *Id.* (“The requirement of maintaining lawyers' independent professional judgment, embodied in Rule 5.4, was most important to the Committee. After referring a plan member to a lawyer, the plan sponsor should have no further dealings with the member on legal issues, the opinion cautioned. Thereafter, a traditional client-lawyer relationship would exist between the member and providing lawyer. . .”).

⁵⁵ *See Id.* at 932.

⁵⁶ *Id.* at 932-33.

new reality by creating the ABA Standing Committee on Group and Prepaid Legal Services⁵⁷ and affiliating itself with the American Prepaid Legal Services Institute, which is an organization committed to the continued development and success of group and prepaid legal services.⁵⁸

III. RAPID GROWTH OF THE GROUP AND PREPAID LEGAL SERVICES INDUSTRY

As of 1987, an estimated 13 million middle-income Americans were enrolled in some form of prepaid legal service plan and another 17 million were covered by some form of group legal services arrangement.⁵⁹ With the assistance of favorable tax treatment, mass commercialization of group and prepaid legal plans, lessened ethical restrictions, and innovative legal plan structures, the number of middle-income Americans covered by some form of group or prepaid legal services arrangement blossomed to an estimated 152 million in 2000.⁶⁰ Although this number can be deemed deceiving because it includes 86 million Americans that utilize “free” or “access” plans for routine benefits that are covered under umbrella organizations such as AARP, the number still signifies the substantial effect that group and legal prepaid service plans have had on the legal marketplace.⁶¹

In the late 1980’s, group and prepaid legal plans were beginning to emerge as a viable and sustainable method of legal service delivery, and also as a financially beneficial alternative for both attorney-service providers and consumers.⁶² Trade unions paved the way for subsequent group and prepaid legal

⁵⁷ Jennifer A. Rymell, *The Growing World of Legal Entrepreneurs*, 31 No. 1 GPSOLO 8, 8 (2014) (describing group and prepaid legal services as “efficient mechanism[s] for matching lawyers with clients in need of services,” and comparing legal service plans to “a PPO in the health insurance industry”).

⁵⁸ AM. PREPAID LEGAL SERV. INST., WHO’S WHO IN PREPAID LEGAL SERVICES: MEMBERSHIP DIRECTORY 2 (2000).

⁵⁹ Alec M. Schwartz, *A Lawyer’s Guide to Prepaid Legal Services*, 15 No. 5 LEGAL ECON. 43, 43 (1989).

⁶⁰ Maute, *supra* note 2, at 933; Brian Heid & Eitan Misulovin, *The Group Legal Plan Revolution: Bright Horizon or Dark Future?*, 18 HOFSTRA LAB. & EMP. L.J. 335, 337 (2000); *see* Wayne F. Foster, *Prepaid Legal Services Plans*, 93 A.L.R. 3d 199, 199 (1979) (describing the effect of federal legislation that granted legal service benefit plans preferential tax treatment, and made plans a permissible subject of bargaining).

⁶¹ Maute, *supra* note 2, at 934 (explaining that free plans are offered to active members at no additional cost and access plans are only accompanied with nominal charges).

⁶² *See* Schwartz, *supra* note 59, at 43 (describing the view that group and prepaid legal service arrangements were not only guaranteed income for legal practitioners, but were valuable to consumers as well).

service providers by focusing on the employee benefit model to benefit their constituents and their constituents' dependents. However, soon after trade unions began perfecting the employee benefit model, credit card companies, banks, credit unions, and associations began to enter the market with mass-commercialized marketing schemes.⁶³ Before long, companies that were not affiliated with any group began to market group and prepaid legal service plans to the general public.⁶⁴

Group and prepaid legal service plans offered via employee benefit programs deserve most of the credit for the growth of the industry.⁶⁵ During the late 1980's and early-1990's, as American financial markets grew, merged, and expanded their reach into new and emerging markets, a great need arose for skilled and affordable labor.⁶⁶ As prices for skilled labor increased, improving employee benefits packages became a priority for corporate human resource departments.⁶⁷ The affordability of group and prepaid legal plans made them a must-have for employee benefit packages of both large and small companies.⁶⁸ Group and prepaid legal service plans gave human resource managers the ability to improve their employee benefit packages by providing a simple, cost-effective method for employees to handle their legal needs.⁶⁹

Employees benefitted from the services provided by the legal service plans and from tax incentives since group and prepaid legal plans were given

⁶³ *Id.*

⁶⁴ *Id.*

⁶⁵ Heid & Misulovin, *supra* note 60, at 338 (stating that “[o]ne type of employee benefit program that [was] gaining favor in the American marketplace [was] the group legal plan”); see Maute, *supra* note 2, at 935.

⁶⁶ Heid & Misulovin, *supra* note 60, at 336.

⁶⁷ *Id.* at 337 (explaining that “in order to differentiate themselves from their competitors and attract the most qualified and dedicated employees,” firms began to provide improved benefit plans to their employees).

⁶⁸ *Id.* at 338 (stating that companies such as American Express, Microsoft, AT&T, and Tower Records became “became cognizant of group legal plans and began implementing this form of employee benefit program”); see also Jennifer Click, *The Ins and Outs of Prepaid Legal Plans*, HRMAGAZINE, Jan. 1, 1998, at 66, 67 (explaining the growing popularity of group and prepaid legal services in the employee benefit packages, an executive at Pre-Paid Legal Services, Inc. stated: “A lot of employers would love to give their employees a raise, but at the present time, their financial situation just doesn't warrant it. But they can afford \$3 or so a week. Now if you offered them that kind of raise, employees would probably be mad. But by providing a prepaid legal plan, employers can show concern for their employees and make them feel better”).

⁶⁹ Heid & Misulovin, *The Group Legal Plan Revolution: Bright Horizon or Dark Future?*, at 339.

“substantial impetus by federal legislation granting preferential tax treatment.”⁷⁰ Although preferential tax treatment of legal service plans ended, the expansion of group and prepaid legal services has not diminished.⁷¹ In fact, in the absence of explicit gross income exclusion, “many employees of companies enrolled in group legal plans can still enjoy some favorable tax relief by paying their monthly deductions with pre-tax income when enrolled in a flexible benefits plan.”⁷²

IV. HOW GROUP AND PREPAID LEGAL PLANS OPERATE

What does a group or prepaid legal service plan really do? This is the primary question that must be addressed before the internal operations of a group or prepaid legal service provider can be fully understood and appreciated. The function and underlying purpose of group and prepaid legal services can be divided into five distinct goals: (1) reduction of the perceived cost of legal services to the consumer; (2) increased buying power among a collective group of legal consumers; (3) encouragement of preventative legal care; (4) financial protection for consumers who encounter unexpected serious legal problems; and (5) creation of a financial and organizational platform to foster further innovation in the delivery of legal services.⁷³ Each goal is discussed in detail below.

Among many consumers, perception is considered reality. This is especially true when discussing the costs of legal services, which most consumers perceive as overly expensive.⁷⁴ However, with the advent of group and prepaid legal services, legal service consumers have experienced a reduction in the perceived cost of necessary legal services.⁷⁵ Rather than paying \$100 to \$200 per hour or a \$750 fee for representation in a bankruptcy proceeding, the consumer pays “\$50 to \$200 per year to a legal service plan, in return for which he or she is eligible to use a lawyer for services which otherwise might cost hundreds or thousands of dollars.”⁷⁶ The ability to access legal services at any time without

⁷⁰ Foster, *supra* note 60, at 199; see 26 U.S.C.A. § 120 (1976) (providing an exclusion from gross income of (1) amounts contributed by an employer on behalf of an employee and his dependents; or (2) the value of legal services provided under a qualified legal services plan). The exclusion ended on June 30, 1992.

⁷¹ Heid & Misulovin, *supra* note 60, at 340.

⁷² *Id.*

⁷³ Schwartz, *supra* note 59, at 43-44.

⁷⁴ See Elliott E. Cheatham, *A Lawyer When Needed: Legal Services for the Middle Classes*, 63 COLUM. L. REV. 973, 975 (1963) (describing one of the reasons for the existence of a gap between legal needs and legal service as “fear of overcharging by the lawyer”).

⁷⁵ Schwartz, *supra* note 59, at 43.

⁷⁶ *Id.*

the large upfront cost has given many subscribers of group and prepaid legal services the impression that they are receiving legal services at a reduced cost.⁷⁷

Although consumers experience a perceived reduction in legal costs, many actually experience a true reduction in the cost of necessary legal services due to the increased buying power of service plan subscribers.⁷⁸ Generally, legal service providers are “willing to reduce fees in return for a high volume of those services provided for the group.”⁷⁹ Legal service providers have recognized that the benefit of guaranteed payment from a group of clients outweighs the risk of reducing their usual rates.⁸⁰

Because group and prepaid legal plans provide for ready access to a lawyer’s services, consumers are encouraged to partake in preventative legal care.⁸¹ Once a consumer has subscribed to a group or prepaid legal service arrangement, which can offer unlimited advice and consultation, “the marginal cost to the individual using that benefit may be the cost of a local phone call to a lawyer.”⁸² This small initial cost and the ease of use can allow the consumer to deal with a small legal problem before it blossoms into a larger issue with more significant ramifications.⁸³ Similar to medical treatment, early detection and resolution of a personal legal problem can prevent a legal catastrophe “and its attendant cost in time and money.”⁸⁴

Group and prepaid legal service plans are also extremely useful when serious legal problems cannot be avoided. Prepaid legal service plans “operate like any traditional insurance mechanism.”⁸⁵ Group and prepaid legal service plans create an efficient mechanism to match legal service providers with legal service consumers.⁸⁶ This is accomplished by establishing panels of lawyers “with expertise in various areas and match[ing] them with plan members.”⁸⁷ Again,

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ *Id.*

⁸⁰ See Cheatham, *supra* note 74, at 9 (explaining that many attorney service providers have established thriving legal practices exclusively from group and prepaid legal service clientele).

⁸¹ Schwartz, *supra* note 59, at 43.

⁸² *Id.* at 44.

⁸³ *Id.*

⁸⁴ *Id.*

⁸⁵ *Id.*; Rymell, *supra* note 57, at 9 (comparing the prepaid legal service model to a PPO in the health insurance industry).

⁸⁶ *Id.*

⁸⁷ *Id.*

similar to a traditional insurance mechanism, the plan can cover the anticipated legal service utilization by its members by “spread[ing] the risk that any one member would need to make any substantial claim on the plan’s assets among a large group of [members].”⁸⁸

To the extent allowable by the current regulatory framework, the organizational and financial structure of group and prepaid legal service plans foster innovation in the delivery of legal services to consumers.⁸⁹ Innovative organizational structures seek ways to deliver high quality, individualized legal services meeting the common legal needs of middle-class clientele.⁹⁰ By collecting funds from a group of legal consumers before the services are needed, legal service providers and plan administrators must discover and implement innovative measures “to predict the types and extent of service needed by plan members.”⁹¹ This need for further innovation requires legal service providers to develop systems that “make it easier for lawyers to produce standard documents such as wills and bankruptcy forms, telephone mechanisms [that] can be used to provide legal advice, and the availability of legal services [that] can be tailored to the needs of an identifiable group of people.”⁹²

A. Basic Formats of Group and Prepaid Legal Plans

Before exploring the inner-workings of group and prepaid legal plans, it is beneficial to briefly describe the basic formats in which legal plans are organized. The three basic forms of group and prepaid legal plans are as follows: the group plan, the prepaid access plan, and the comprehensive plan.⁹³

Group Plan. The group plan is less of a formal legal services plan and more of a group discount arrangement.⁹⁴ The group plan is simply a system “whereby an individual member of the group is referred to a lawyer or law firm recommended by the group leadership . . . [and], in return, the lawyer may provide free or low-cost advice and consultation, plus additional services

⁸⁸ Schwartz, *supra* note 59, at 44.

⁸⁹ *Id.*; see generally Ray Worthy Campbell, *Rethinking Regulation and Innovation in the U.S. Legal Services Market*, 9 N.Y.U. J. L. & BUS. 1 (2012) (discussing the impact new innovations are having on the incumbent members of the legal profession and why further innovation is necessary).

⁹⁰ Maute, *supra* note 2, at 939.

⁹¹ Schwartz, *supra* note 59, at 44.

⁹² *Id.*

⁹³ *Id.*

⁹⁴ Click, *supra* note 68, at 68 (explaining that the average discount from these discount arrangement was twenty-five percent).

according to a plan fee schedule or at some discount from the lawyer's usual and customary charges."⁹⁵ This system does not involve any prepayment fees, administrators, insurance companies or other forms of third-party intermediaries.⁹⁶ Furthermore, there is no cost to the group, or member, for making the group plan available.⁹⁷

Comprehensive Plan. The most complex and comprehensive legal service plan format is the comprehensive plan.⁹⁸ The comprehensive plan is designed "to cover 80 to 90 percent of the average person's legal service needs in a given year."⁹⁹ Similar to an insurance plan, the plan depends heavily on risk-spreading principles and "assumes that only a certain proportion of the enrolled members actually will be using the benefits each year."¹⁰⁰ Due to the comprehensive plan's actuarial complexity, plan administration is generally handled by a trust fund, registered group, prepaid legal service organization, or an insurance company.¹⁰¹ Once a plan member pays the required fee, "benefits are available as stated in the plan at no additional charge, except for deductible and copayments which may apply to certain kinds of services."¹⁰²

All legal service plan formats share one common characteristic: they are either open-panel or closed-panel plans.¹⁰³ Under an open-panel plan, the plan member may choose between all local attorneys participating in the plan and, under certain circumstances, local attorneys who are not participating members in the plan.¹⁰⁴ Hence, within certain limitations, plan members choose the lawyer they desire.¹⁰⁵ The chosen lawyer may or may not be a member of the panel.¹⁰⁶

⁹⁵ Schwartz, *supra* note 59, at 44.

⁹⁶ *Id.*

⁹⁷ *Id.*

⁹⁸ *Id.*

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² *Id.* (explaining that benefits under a comprehensive plans can cover many legal necessities such as "legal advice and information by phone, plus other services related to specific kinds of legal matters, or may provide money which can be used by the plan member to pay lawyers for a wide variety of legal work").

¹⁰³ See Foster, *supra* note 60, at 199.

¹⁰⁴ *Id.*

¹⁰⁵ Schwartz, *supra* note 59, at 47.

¹⁰⁶ *Id.* Generally, any lawyer who wishes to be a member of the panel may do so. *Id.*

In contrast, under a closed-panel plan the participating member can only select from a small group of attorneys who are under contract to represent subscribers exclusively.¹⁰⁷ However, this distinction is less important in today's group and prepaid legal services industry due to innovative legal service delivery systems.¹⁰⁸ For instance, some plan designers find it far more economical to arrange for one law firm, or one group of lawyers, to set up a complex phone and record keeping system to handle the plan member's phone consultations, while utilizing an open-panel concept to handle the more complex legal issues plan members may have.¹⁰⁹ The same theory has been applied to plan members that reside in geographical areas that are not conducive to a closed-panel system, except for the phone consultation component of the plan.¹¹⁰

B. *Component Parts of a Legal Service Plan*

Group and prepaid legal service plans operate on an organizational platform that strives to make attorney access to middle-income consumers cheaper and more efficient. In order to achieve this goal, the component parts of the legal service plan must work as a cohesive unit. Generally, comprehensive legal service plans are made up of four component parts: consumers, lawyers, plan administrators, and underwriters.¹¹¹ Each component part is discussed below.

Consumer. The consumer or plan member is an important and vital component of the legal service plan. In the early years, due to the ABA's treatment of group and prepaid legal services, plan designers were more focused on finding attorneys to participate in the plan and less focused on selling the plan to consumers.¹¹² Unfortunately, plan designers soon realized that although their plans were sound and would provide the services promised, few consumers, if any, were interested.¹¹³ The plan designer's then shifted their focus to marketing and selling the plan to the consumer.¹¹⁴

¹⁰⁷ *Id.*

¹⁰⁸ *Id.* (explaining that the distinction between open and closed panels is less important today because most plans utilize a mixture of both to better serve their plan members).

¹⁰⁹ *Id.*

¹¹⁰ *Id.*

¹¹¹ *Id.* at 44-45.

¹¹² *Id.* at 45.

¹¹³ *Id.*

¹¹⁴ *Id.*

The plan member can be a member of the general public, an employee, or a member of an association that sponsors a plan.¹¹⁵ The plan member is the client, not the association or employer.¹¹⁶ Furthermore, whether directly or indirectly, depending on whether the fees are paid by or on behalf of the plan member, the plan member is the source of funds for the legal service plan.¹¹⁷ Thus, a successful legal services plan must begin with the consumer.

For the most part, a successful plan is created on behalf of a group and the group acts as the “plan sponsor.”¹¹⁸ The group “may be made up of the employees who work for a specific company, members of the union, credit union depositors, or association members.”¹¹⁹ When a group becomes a plan sponsor, the plan is usually set up in the group’s name and the group brings “the plan its endorsement.”¹²⁰ The group’s endorsement gives the plan validation and access to current and future members of the designated group, which in turn creates a sustainable fund to allow the plan to thrive.¹²¹

Lawyers. The next component of legal service plans consists of the lawyers who will be performing legal services for the plan members. The plan designer organizes a panel of lawyers, whether closed or open, into a “contract service provider panel.”¹²² The plan’s panel of lawyers “may consist of one lawyer or a group of lawyers who agree to the terms and conditions under which the plan is operated.”¹²³

Generally, attorneys that are enrolled in various legal service plans are required “to meet certain qualification procedures that may include a minimum number of years in active practice, academic requirements, and screening processes that investigate the potential network member with the state and local bar associations.”¹²⁴ Furthermore, legal service plans most frequently require

¹¹⁵ *Id.* at 46.

¹¹⁶ *Id.*

¹¹⁷ *Id.*

¹¹⁸ *Id.*; see Heid & Misulovin, *supra* note 60, at 340 (explaining the need for a pool of consumers to design a sustainable group legal plan, especially as an employee benefit).

¹¹⁹ Schwartz, *supra* note 59, at 46.

¹²⁰ *Id.*

¹²¹ *Id.*

¹²² *Id.*

¹²³ *Id.* at 46 – 47; see Heid & Misulovin, *supra* note 60, at 341 (stating that “[t]hese [attorney] panels may vary from one attorney or firm servicing a small group under formal contract, to a national network of law firms that have agreed to provide services for all plan subscribers”).

¹²⁴ Heid & Misulovin, *supra* note 60, at 341.

“their members to carry professional liability insurance with a minimum of \$100,000 coverage for legal malpractice.”¹²⁵ Because most attorneys within a legal service panel are in the middle of their career, with an average of ten to fifteen years of experience, these minimum requirements are usually a non-issue.¹²⁶

Plan Administrator. Although it is not required for a plan to operate, most profitable and successful legal service plans utilize a plan administrator or third party to manage the day-to-day operation of the plan.¹²⁷ Depending on state law, the plan administrator is usually someone other than the law firm that provides legal services to the plan participants.¹²⁸ The plan administrator “handles plan finances, collects contributions, enrolls members, provides plan descriptions and forms to members, processes and pays claims and files reports required by regulatory agencies.”¹²⁹ Also, the administrator is responsible for establishing and maintaining “complaint adjudication mechanisms to serve the needs of both plan members and service providers who may have a dispute regarding [the] plan[s] coverages, rules or claims,” which, concerning group and prepaid legal service plans, is a vital part of their continued success.¹³⁰

Recently, plan sponsors and trustees have trended towards delegating plan administrative duties to established insurance companies in the form of “administrative services only” contracts or as a part of a group insurance policy.¹³¹ As current regulations gain further clarity, insurance companies are well-equipped to handle large groups of plan members or policy holders and generally are familiar with federal and state regulatory requirements surrounding group and

¹²⁵ *Id.*

¹²⁶ Click, *supra* note 68, at 67 (referring to remarks by Bill Badger, executive director of the National Resource Center for Consumers of Legal Services).

¹²⁷ See generally Schwartz, *supra* note 60, at 47-48.

¹²⁸ *Id.* at 47; compare TENN. SUP. CT. R. 8, RPC 7.3 (stating that “the lawyer may not own or direct [a] legal services plan himself,” but may participate in a prepaid legal service plan, and Tenn. Sup. Ct. R. 8, RPC 6.3 states “A lawyer may serve as a director, officer, or member of a legal services organization”) with R. REGULATING FLA. BAR 9-2.1 (stating that “[a] managing attorney shall not be permitted to operate a plan in this state without first obtaining approval by the board of governors to establish such plan”).

¹²⁹ Schwartz, *supra* note 60, at 47.

¹³⁰ *Id.*; see Heid & Misulovin, *supra* note 60, at 345 (describing the importance of ensuring the quality of legal services delivered through the plan by recording and addressing plan member complaints).

¹³¹ Schwartz, *supra* note 59, at 47-48; Heid & Misulovin, *supra* note 60, at 335 (explaining that insurance companies are also becoming heavily involved in the group and prepaid industry primarily due to the demand of their large institutional clients for group legal plans).

prepaid legal services.¹³² In most cases, insurance companies “have a system set up to ensure that each plan member receives a certificate describing his or her coverage,” and, pertaining to employee benefit plans, “the insurance company may contribute text to a comprehensive summary plan description booklet published by the employer to advise employees of all fringe benefits for which they are eligible.”¹³³

Underwriter. The final important component of a group or prepaid legal service plan is the underwriter. Although not required for a legal services plan to function, the underwriter is another potential third party that bears the financial risk for the plan.¹³⁴ Under the majority of circumstances, “the most typical underwriting arrangement involves the use of an insurance company, whose assets guarantee the payment of claims or the provision of legal services regardless of whether the plan collects sufficient contributions.”¹³⁵ On occasion, some plan sponsors will act as their own underwriter by utilizing their assets as the “guarantee mechanism.”¹³⁶ However, in this circumstance the plan sponsor still has the ability to protect itself “against overutilization or an unexpectedly high claims cost by purchasing reinsurance through a commercial insurance company.”¹³⁷

Relatively recently, state regulations governing group and prepaid legal service plans have created financial guidelines for plan designers to follow in order to establish a viable and compliant legal service plan.¹³⁸ For instance, Tennessee’s regulation regarding financial requirements for establishing group and prepaid legal service plans reads as follows:

- (1) An insurer shall meet the following requirements to become licensed under this Act: (a) An insurer shall, at all times, maintain

¹³² Schwartz, *supra* note 59, at 48.

¹³³ *Id.*

¹³⁴ *Id.*; TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. JACKSONVILLE, Florida, 2008 WL 8010813 (Sept. 30, 2008) (stating that U.S. Legal Services of Tennessee, Inc. accepted all coverage applications, and, therefore, “there is essentially no underwriting of potential policyholders).

¹³⁵ Schwartz, *supra* note 59, at 48.

¹³⁶ *Id.*

¹³⁷ *Id.*

¹³⁸ *Id.* at 48; TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF PRE-PAID LEGAL SERVICES OF TENNESSEE, INC. ADA, OKLAHOMA, 2004 WL 5702813 (Dec. 31, 2011) (describing Tennessee’s Department of Commerce and Insurance examination of Pre-Paid Legal Services, Inc. assets and liabilities, and its ability to sustain operations after a large impact on its assets and surplus funds).

capital of at least \$100,000. (b) In addition to the requirement of paragraph (a) above each insurer shall have and maintain surplus of at least one-third (1/3) of gross premium; (c) Any person transacting the business of legal insurance on January 1, 1990 shall meet the surplus requirements of subpart (b) supra by December 31, 1991. (d) Each insurer licensed under this act shall satisfy the commissioner that it has and shall maintain on deposit with the state treasurer at least \$100,000 in cash or its equivalent; but the commissioner may, in his discretion, accept as an equivalent bonds of the United States, or any agency or instrumentality of the United States which have been included in the three highest grades by any of the recognized securities rating firms, bonds of this state, bonds of the state of domicile, or bonds publicly issued by any solvent institution created or existing under the laws of the United States or any state thereof which have been included in the three highest grades by any of the recognized securities rating firms. Notwithstanding the foregoing, the commissioner may decline to accept as a deposit any specific issue of securities that he has determined may not provide the necessary protection to policyholders and creditors in the United States. This deposit shall be an admitted asset on the financial statement of the plan.¹³⁹

However, these financial guidelines are promulgated merely to establish legal service plans for state licensing purposes; thus, capital requirements for legal service plans can vary depending on the services covered by the plan, the amount of plan members, and the fee agreement between the plan and the legal service providers.¹⁴⁰

C. *Ordinary Legal Services Covered*

One of the most important determinations for a plan designer to make when establishing a legal service plan is “the type and level of legal services for which the plan will pay [for].”¹⁴¹ Arriving at that final determination requires the plan designer to consider many factors. Factors that must be considered are (1) what type of legal services the plan members will find useful, (2) how much premiums must cost to create a viable legal service plan, and (3) how the attorney-participants will be compensated for their services.¹⁴² Each factor will be discussed below.

¹³⁹ TENN. COMP. R. & REGS. 0780-01-60-.05 (1991).

¹⁴⁰ See generally Schwartz, *supra* note 59, at 48.

¹⁴¹ *Id.* at 48.

¹⁴² See *id.* at 48-49.

As previously discussed, group and prepaid legal service plan formats can vary widely. Similarly, the types of legal services covered by a legal service plan tend to vary from plan to plan.¹⁴³ For most legal service plans, especially those plans that utilize the comprehensive plan format, the plan designer's mission is "to provide the plan member[s] with coverage for common types of legal problems faced by middle-income individuals and families."¹⁴⁴ At the very least, most plans offer unlimited phone consultations and limited attorney correspondence with adverse parties.¹⁴⁵ However, more comprehensive plans can cover "a vast array of administrative, consumer, financial, family and estate law matters, as well as . . . non[-]felony criminal charges."¹⁴⁶ Legal service plan benefits "can be stated either in terms of the type of legal problems covered or the type of lawyer service for which the plan will pay."¹⁴⁷

A legal service plan's coverage of plan members is its best marketing tool for recruiting new members.¹⁴⁸ The broader and more accessible a legal service plan's benefits are, the more value and appeal the plan will have to potential plan members.¹⁴⁹ Therefore, many plan designers build their group and prepaid legal service plans to cover most of the specific legal concerns of their target group.¹⁵⁰ For example, U.S. Legal Services created a legal service plan exclusively marketed to commercial drivers in Tennessee "with legal benefits designed to meet the needs of . . . drivers and [their] compan[ies]."¹⁵¹ By focusing on a niche group, U.S. Legal Services was able to estimate their plan members' projected utilization rates and narrow their legal service benefits coverage to their core group's common legal concerns.

¹⁴³ *Id.* at 48.

¹⁴⁴ *Id.*

¹⁴⁵ *Id.*

¹⁴⁶ Maute, *supra* note 2, at 939.

¹⁴⁷ Schwartz, *supra* note 59, at 48.

¹⁴⁸ See Heid & Misulovin, *supra* note 60, at 343.

¹⁴⁹ *Id.* (describing consumers delight with the benefits they receive under comprehensive plans).

¹⁵⁰ Schwartz, *supra* note 59, at 48.

¹⁵¹ TENN. DEP'T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. JACKSONVILLE, FLORIDA, 2008 WL 8010813, at *10 (Sept. 30, 2008). The CDL Protector offered by U.S. Legal Services provides coverage for moving, non-moving and Department of Transportation violations, representation in case of a major accident, personal legal consultation services, coverage for pre-existing matters, license suspension and revocation hearings, financial coaching, and identity theft. *Id.*

All legal service plan designers tend to limit their plan coverage to control costs and to limit their risk of overutilization.¹⁵² This limitation of plan coverage is done in a combination of three ways: (1) limitation of the type of legal service covered, (2) limitation of the actual cost, in terms of money or the representation, and (3) limitation in the number of hours of attorney time for which the plan will pay.¹⁵³ Occasionally, the plan will simply specify “each service for which the plan will pay or provide, regardless of the cost or the time spent.”¹⁵⁴ Generally, coverage limits are specified in the plan member’s benefit schedule upon enrollment into the plan.¹⁵⁵

For the most part, benefits and exclusions of a legal service plan “reflect the basic policies and desires of either the group or the plan operator.”¹⁵⁶ However, some exclusions are necessary to comply with statutory requirements.¹⁵⁷ Moreover, other exclusions are necessary for economic reasons and “to avoid abuses in the use of benefits.”¹⁵⁸ For instance, “legal services related to class actions, patents or copyrights, appeals, small claims court actions and tax preparation typically are excluded from plan coverage,” and, generally, if a plan member is entitled to coverage of their legal fees or reimbursement from another source, the majority of plans will not cover legal services related to that matter.¹⁵⁹

Except for free and access legal service plans, group and prepaid legal service plan operators generally charge their plan members a fixed monthly, quarterly, semi-annual, or annual premium.¹⁶⁰ When setting the cost of premiums for plan members, the actuarial soundness of the plan is of utmost importance.¹⁶¹ Although many states do not require the actuarial review of a legal service plan before its implementation, it is common practice for a plan to retain a

¹⁵² Schwartz, *supra* note 59, at 49.

¹⁵³ *Id.*

¹⁵⁴ *Id.*

¹⁵⁵ *Id.*

¹⁵⁶ *Id.*

¹⁵⁷ *Id.* (stating that “qualified legal service plans receiving special tax treatment under Section 120 of the Internal Revenue Code,” which was discontinued in 1992, “must provide only ‘personal legal services’ as defined in the statute and regulations”). Furthermore, “[t]he major limitation imposed by the statutory requirement is that legal services related to business concerns in which an employer has an interest cannot be covered.” *Id.*

¹⁵⁸ *Id.*

¹⁵⁹ *Id.* at 49-50.

¹⁶⁰ See Heid & Misulovin, *supra* note 60, at 340.

¹⁶¹ See Maute, *supra* note 2, at 939.

professional actuary to assist with rate and policy formation.¹⁶² In order to ensure the financial success of a group or prepaid legal plan, plan designers and operators must strike a balance between customer satisfaction and “the value received for the monthly premiums. . . .”¹⁶³

In order to protect the plan’s assets, many plan operators state their plan premiums as a range.¹⁶⁴ For instance, Pre-Paid Legal Services (“Pre-Paid Legal”), recently renamed LegalShield, states that its “basic legal service [c]ontract can range in cost from \$16 to \$25 per month, depending in part, on the schedule of benefits.”¹⁶⁵ Furthermore, if plan members subscribe to the plan through their employer’s payroll deduction system, “the [company] has contracts available . . . where rates can range from \$14.95 to \$23.95.”¹⁶⁶ Pre-Paid Legal also offers small business owners a prepaid legal solution where a contract “may cost either \$75 or \$125, depending on the number of employees.”¹⁶⁷ Similarly, U.S. Legal Services (“U.S. Legal”), offers its individual Traffic-Max plan for a monthly price of \$20 to \$100.¹⁶⁸ U.S. Legal also serves physicians with prepaid legal services through its Physician Shield plan, which comes at a price of \$750 to \$1,500 per year.¹⁶⁹

Normally, legal service plans accept all enrollees who apply to become plan members.¹⁷⁰ Hence, very few plans utilize any underwriting procedures for potential plan members.¹⁷¹ However, notwithstanding the industry’s lack of

¹⁶² See TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. JACKSONVILLE, FLORIDA, 2008 WL 8010813, at *14 (Sept. 30, 2008).

¹⁶³ Maute, *supra* note 2, at 940.

¹⁶⁴ Heid & Misulovin, *supra* note 60, at 340 (explaining that a group legal plan’s premiums can range from as low as \$1 to as high as \$25 per month, but, on average, a legal plan member’s monthly premium is between \$12 and \$20).

¹⁶⁵ TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF PRE-PAID LEGAL SERVICES OF TENNESSEE, INC. ADA, OKLAHOMA, 2004 WL 5702813, at *8 (Dec. 31, 2001). Pre-Paid Legal’s basic legal service contract “is sold as a package consisting of . . . five (5) separate benefits.” *Id.* at *9. These benefits consist of preventative legal services, motor vehicle legal services, trial defense services, IRS Audit Legal Services and other legal services, all of which are subject to certain exceptions and exclusions. *Id.*

¹⁶⁶ *Id.* at *8.

¹⁶⁷ *Id.*

¹⁶⁸ TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. NEWBERN, TENNESSEE, 2004 WL 5702800, at *12 (Sep. 30, 2003).

¹⁶⁹ *Id.*

¹⁷⁰ See Schwartz, *supra* note 59, at 48.

¹⁷¹ TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. NEWBERN, TENNESSEE, 2004 WL 5702800, at *12 (Sep. 30, 2003);

underwriting procedures, “profit margins on group and prepaid legal services are estimated to hover around fifteen percent, a number that is four times greater than that for group health plans.”¹⁷² This statistic indicates that legal service plan designers are efficiently projecting the necessary cost of premiums to cover any losses experienced by the utilization of the plan’s benefits. For example, Pre-Paid Legal, in their Form 10-K filing with the Securities and Exchange Commission, while describing their claims management and premium determination process, stated:

The Memberships we sell generally allow members to access legal services through a network of independent law firms (“provider law firms”) under contract with us. Provider law firms are paid a monthly fixed fee on a capitated basis to render services to plan members residing within the state or province in which the provider law firm attorneys are licensed to practice. Because the fixed fee payments by us to benefit providers do not vary based on the type and amount of benefits utilized by the member, this capitated arrangement provides significant advantages to us in managing claims risk since we know the percentage of Membership fees that will be paid to the benefit providers to deliver the Membership benefits and the timing of such payments. At December 31, 2010, Memberships subject to the capitated provider law firm arrangement comprised more than 99% of our active Memberships. The remaining Memberships, less than 1%, were primarily sold prior to 1987 and allow members to locate their own lawyer (“open panel”) to provide legal services available under the Membership with the member’s lawyer being reimbursed for services rendered based on usual, reasonable and customary fees, or are in states where there is no provider law firm in place and our referral attorney network described below is utilized. During 2010, our provider law firms processed more than 2.2 million requests for service, an average of 1.6 per Member. A request for service represents a member’s request for assistance on a specific legal matter. These requests usually include multiple telephone consultation(s) and often include document review(s), letter(s) written or telephone call(s) made to third parties on the members’ behalf, preparation of last will(s) and testament(s) and other legal assistance . . . Although not all of our provider law firms maintain specific records of how often the legal engagement leads to additional fees being paid by members to the

see generally Heid & Misulovin, *supra* note 60, at 340 (explaining that once premiums are *Paid*, plan members are officially enrolled into the plan and can partake in the benefits offered).

¹⁷² Heid & Misulovin, *supra* note 60, at 336.

provider law firm, provider law firms representing approximately 99% of our Membership base reported that on average, less than 1% of these requests for service resulted in additional fees being paid by the member to the provider law firm.¹⁷³

D. Plan Attorney Compensation

Now that proper descriptions of attorney services covered by legal service plans and how plans determine the cost of their plan members' premiums have been discussed, it is important to explain how lawyers or legal service providers are compensated under most group and prepaid legal service plans. In the vast majority of cases lawyers who participate in a particular group or prepaid legal service plan are required to execute a service agreement with the plan operator.¹⁷⁴ Although the agreement can cover a plethora of terms, arguably the most important terms deal with how the legal service provider will be compensated.¹⁷⁵

Although attorney compensation systems tend to vary widely among legal service plans, there are two main arrangements utilized by many established plans: the capitated arrangement and the "retain-as-needed" arrangement.¹⁷⁶ Generally the capitated arrangement is used for a closed-panel network of attorneys.¹⁷⁷ The capitated arrangement allows the legal service plan to pay the participating law firm, or individual lawyer, on "a per active member per month basis."¹⁷⁸ This arrangement works best for a plan that uses a closed-panel network to serve its plan members because it allows the plan to easily "know the percentage of [m]embership fees that will be paid to the benefit providers to deliver the Membership benefits and the timing of such payments."¹⁷⁹ Therefore, the capitated arrangement, coupled with a closed-panel network of lawyers, gives the

¹⁷³ Pre-Paid Legal Services, Inc., Annual Report (Form 10-K) (Dec. 31, 2010).

¹⁷⁴ See Heid & Misulovin, *supra* note 60, at 341.

¹⁷⁵ *Id.* (describing particular terms covered by the attorney service agreement such as required years of experience, academic requirements, potential conflicts of interest, and professional liability insurance requirements).

¹⁷⁶ See TENN. DEP'T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. JACKSONVILLE, Florida, 2008 WL 8010813, at *20 (Sept. 30, 2008) (describing U.S. Legal Services, Inc., decision to employ the "retain-as-needed" arrangement since it was a proven method to serve an open-panel plan); see also Pre-Paid Legal Services, Inc., Annual Report (Form 10-K) (Dec. 31, 2010) (describing Pre-Paid Legal Services, Inc., use of the capitated arrangement method to compensate their network of "provider law firms").

¹⁷⁷ See generally Pre-Paid Legal Services, Inc., Annual Report (Form 10-K) (Dec. 31, 2010) (outlining the parameters governing capitated arrangements).

¹⁷⁸ *Id.*

¹⁷⁹ *Id.*

legal service plan an effective way to manage their over-utilization risk.¹⁸⁰ Alternatively, in most cases the “retain-as-needed” arrangement is a better option for an open-panel network of attorneys.¹⁸¹ The “retain-as-needed” arrangement allows the legal service plan to locate a local lawyer wherever their plan member needs assistance “and arrange for individual representation and payment.”¹⁸² This arrangement operates efficiently for an open-panel network of attorneys because the legal service plan’s members can feasibly utilize their benefits wherever and whenever they are necessary, which is the most intriguing feature of open-panel plans.¹⁸³

Both payment arrangements have their positive aspects, but they both also come with drawbacks. For instance, in the case of capitated arrangements, because they are usually closed-panel plans, geographical, expertise, and conflict-of-interest issues tend to permeate plan member’s complaints.¹⁸⁴ Under a capitated arrangement as stated above, the legal service provider is on most occasions an individual law firm or individual lawyer.¹⁸⁵ Therefore this individual must have the ability to satisfy all plan members in a given area, and when the law firm or lawyer cannot deliver, the plan’s reputation and effectiveness suffers. On the other hand, in the case of “retain-as-needed” arrangements, which are usually coupled with open-panel plans, over-utilization risk management is a significant

¹⁸⁰ *Id.*; see generally Heid & Misulovin, *supra* note 60, at 342-43 (describing the benefit of a closed-panel plan to both the legal service provider and the legal consumer).

¹⁸¹ See TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. JACKSONVILLE, FLORIDA, 2008 WL 8010813, at *20 (Sept. 30, 2008). For example, U.S. Legal’s description of its “retain-as-needed” arrangement stated:

This agreement, although approved, was designed for the development of a network of “capitulated” attorneys which the Company decided to forego in favor of a “retain-as-needed” system of attorneys. Since the Company provides services of an attorney in whatever part of the United States or Canada where the policyholder’s violation occurred or where legal service is requested, the Company’s service method is to locate an attorney in the local area and arrange for individual representation and payment. A contract is made with a local attorney where the Company negotiates a price for the services to be provided and makes the arrangements for payment once the services are provided. *Id.*

¹⁸² *Id.*

¹⁸³ See *Id.*; see generally Julia Field Costich, *Joint State-Federal Regulation of Lawyers: The Case of Group Legal Services Under ERISA*, 82 KY. L.J. 627 (1993) (explaining the benefits, and challenges, of the open-panel format).

¹⁸⁴ See Pre-Paid Legal Services, Inc., Annual Report (Form 10-K) at 12.

¹⁸⁵ *Id.* at 8.

concern.¹⁸⁶ Generally, legal service plans that employ a “retain-as-needed” arrangement experience a much higher underwriting loss ratio.¹⁸⁷ More than likely, this is due to the plan being at the mercy of its network of lawyers whose rates, instead of being predetermined, are determined at the time their plan member requires service.¹⁸⁸

V. CURRENT REGULATORY LANDSCAPE

A. Model Rules of Professional Conduct

Although the ABA, has no authority over the practice of law anywhere in the country, its ethics codes nonetheless have been adopted and heavily relied upon by state courts and legislatures, which gives the ABA’s ethics codes the force of law.¹⁸⁹ Since the early 1980’s, “the majority of U.S. states have altered their ethical rules to reflect those presented in the Model Rules . . . making it the ethical standard by which group legal services will primarily be scrutinized.”¹⁹⁰ According to the Model Rules, group and prepaid legal services are not prohibited, but “certain ethical requirements must be adhered to in order to protect the rights of the member of the plan obtaining group legal services.”¹⁹¹

For example, Model Rule 1.6, absent a waiver, requires lawyers to maintain their client’s confidentiality.¹⁹² In some circumstances, merely reporting a client’s name and informing the legal service provider that the lawyer has been retained may be considered a disclosure of confidential information.¹⁹³ For group and prepaid legal services, confidentiality may necessitate the use of an independent consulting firm as a middleman, combined with comprehensive computer programs, in order to disguise the connection between the attorney, the

¹⁸⁶ See TENN. DEP’T OF COMMERCE & INS., REPORT ON EXAMINATION OF THE U.S. LEGAL SERVICES OF TENNESSEE, INC. JACKSONVILLE, FLORIDA, 2008 WL 8010813, at *22 (Sept. 30, 2008) (stating that the company’s combined loss ratio significantly increased after implementing its “retain-as-needed” arrangement).

¹⁸⁷ *Id.*

¹⁸⁸ See *id.*

¹⁸⁹ Thomas R. Andrews, *Nonlawyers in the Business of Law: Does the One Who has the Gold Really Make the Rules?*, 40 HASTINGS L.J. 577, 588-91 (1989).

¹⁹⁰ Heid & Misulovin, *supra* note 60, at 353.

¹⁹¹ *Id.*; see Costich, *supra* note 183, at 636.

¹⁹² See MODEL RULES OF PROF’L CONDUCT R. 1.6 (1983).

¹⁹³ See Samuel J. Levine, *Legal Services Lawyers and the Influence of Third Parties on the Lawyer-Client Relationship: Some Thoughts From Scholars, Practitioners, and Courts*, 67 FORDHAM L. REV. 2319, 2319-27 (1999).

client, and the subject matter for which the client requires representation.¹⁹⁴ Moreover, “some plans may even allow a lawyer to list their client as a ‘John Doe’ for the purposes of reporting that the plan has been used by a member who desires absolute anonymity.”¹⁹⁵

For another example, Model Rule 1.8(f) mandates that, even with the client’s consent, “third parties must refrain from ‘interference with the lawyer’s independence of professional judgment or with the client-lawyer relationship.’”¹⁹⁶ To further complicate matters, inquiring about “information relating to representation of a client is protected as required by [Model] Rule 1.6.”¹⁹⁷ In 1994, in order to clarify Model Rule 1.8(f)’s application to for-profit legal plans, the Maine State Bar Association inquired “whether a group legal service provider may mandate that participating lawyers apply and review standardized legal documents (such as wills) in order to assure its plan members of receiving a certain standard of care from the plan attorney.”¹⁹⁸ In that dispute, at issue was a contract that allowed lawyers to modify the standardized documents “only if necessary to comply with state law.”¹⁹⁹ The contract further required that the lawyer should not “induce any client to take an action contrary to the terms of the participating attorney agreement or . . . suggest to a client that documents prepared by [the provider] are lacking or inferior in any manner.”²⁰⁰ The Maine State Bar found that the contract imposed by the legal service plan requiring its participating legal service providers to adhere to a particular standardized document “violated state bar ethics rules governing the intrusion of third parties

¹⁹⁴ Heid & Misulovin, *supra* note 60, at 353; see Wayne Moore & Monica Kolasa, *AARP’s Legal Services Network: Expanding Legal Services to the Middle Class*, 32 WAKE FOREST L. REV. 503, 513 (1997) (discussing the system by which membership evaluation surveys are sent and the method by which the confidentiality of the AARP Legal Services Network member is maintained).

¹⁹⁵ Moore & Kolasa, *supra* note 194, at 513. The AARP Legal Services Network allows members to merely present a network lawyer with a membership card for use of the service plan. In the case of telephone consultations, presentation of a membership number is all that is required. *See id.*

¹⁹⁶ Heid & Misulovin, *supra* note 60, at 353 (quoting MODEL RULES OF PROF’L CONDUCT R. 1.8(f)(2) (1983)).

¹⁹⁷ MODEL RULES OF PROF’L CONDUCT R. 1.8(f)(3) (1983).

¹⁹⁸ Heid & Misulovin, *supra* note 60, at 353; see Prof’l Ethics Comm. of the Board of Overseers of the Bar, Formal Op. 147 (1994), in 10 ME. B.J. 98 (1995).

¹⁹⁹ Heid & Misulovin, *supra* note 60, at 353; see Prof’l Ethics Comm. of the Board of Overseers of the Bar, Formal Op. 147 (1994), in 10 ME. B.J. 98 (1995).

²⁰⁰ Prof’l Ethics Comm. of the Board of Overseers of the Bar, Formal Op. 147 (1994), in 10 ME. B.J. 98 (1995).

upon the personal judgment of a lawyer in the representation of their client and that Maine attorneys were prohibited from entering into such contracts.”²⁰¹

Another ethical concern that legal service plans face is the conflict of interest that may arise when two or more plan members are adversaries in the same legal dispute. However, for the most part, this issue is easily resolved by appointing independent legal representation for one of the members, thus eliminating the conflict of interest issue.²⁰² A similar arrangement is also required when “conflicts also may arise between plan clients and nonplan clients.”²⁰³ Generally, to remedy this issue, many legal service plans also exclude from their coverage “matters or disputes arising between members of the same plan . . . [and] [i]n some situations, such as divorce, the plan benefits inure to the named plan member, not to the member's spouse or dependents.”²⁰⁴

The biggest difference between current ethical concerns under the Model Rules and past ethical concerns in the Code is their treatment of fee sharing between lawyers and non-lawyers. For instance, Model Rule 5.4²⁰⁵, which prohibits fee sharing with non-lawyers, exempts legal service plans, even when they are for-profit plans.²⁰⁶ Furthermore, although Model Rule 7.2(c) prohibits a lawyer from providing “anything of value to a person for recommending the lawyer's services,” it explicitly exempts “the usual charges of a . . . legal services organization,” which includes legal service plans.²⁰⁷ Moreover, comment six of Model Rule 7.2(c) states that “[t]his restriction does not prevent . . . [a] prepaid legal services plan [from paying] to advertise legal services provided under its

²⁰¹ Heid & Misulovin, *supra* note 60, at 353.

²⁰² See Costich, *supra* note 183, at 637.

²⁰³ Ronald P. Glantz, *Building Your Small Firm Practice on a Prepaid Foundation*, 48 FLA. B.J. 48, 52 (1994) (discussing a possible situation where an attorney may be forced to withdraw because of a conflict).

²⁰⁴ *Id.*

²⁰⁵ See MODEL RULES OF PROF'L CONDUCT R. 5.4(a) (1983) (“A lawyer or law firm shall not share legal fees with a nonlawyer...”); see also MODEL RULES OF PROF'L CONDUCT R. 6.3 cmt. 1 (1983) (advocating that lawyers “support and participate in legal service organizations”). This is an indication that Model Rule 5.4's application should be limited to payment for the impermissible solicitation of clients. Therefore, the Model Rules should generally be interpreted broadly so as to permit all variations of group legal services, provided they do not directly violate other ethical restrictions. CHARLES W. WOLFRAM, MODERN LEGAL ETHICS § 16.5.5, at 916-17 (1986).

²⁰⁶ See ABA Comm. on Prof'l Ethics and Grievances, Formal Op. 355 (1987) (“Participation of a lawyer in a for-profit prepaid legal service plan is permissible under the Model Rules, provided the plan is in compliance with the guidelines in this opinion”).

²⁰⁷ See MODEL RULES OF PROF'L CONDUCT R. 7.2(c) (1983).

auspices.”²⁰⁸ Also, under most circumstances, the Model Rules restrictions upon certain types of advertising and solicitation of clients do not extend to the marketing of group legal service plans.²⁰⁹

According to the Model Rules, lawyers are able to participate in a group or prepaid legal service plan that “uses personal contact to solicit potential members generally.”²¹⁰ However, lawyers may not own, have an ownership interest in, or direct the legal services plan itself.²¹¹ Furthermore, the plan, when soliciting its members and potential members, “may not target particular persons who are known to need legal services in a particular matter.”²¹² Therefore, the Model Rules clearly distinguish between the legal service plan, which can solicit members, and the lawyer, who may not.²¹³ However, fortunately for lawyers, “the lawyer can solicit the plan.”²¹⁴ “[I]n other words, the lawyer can contact the representatives of a group, such as a union, insureds, companies, etc., and urge these representatives to set up a prepaid legal services plan for its members.”²¹⁵

The final ethical concern that group and prepaid legal service plans sometimes face is the unauthorized practice of law (“UPL”). UPL has been more of a concern for new web-based legal service plans that have a national presence and offer other legal services, and less of a concern for established plans that focus solely on utilizing a network of lawyers to service their plan members.²¹⁶

²⁰⁸ MODEL RULES OF PROF'L CONDUCT R. 7.2 cmt. 6 (1983).

²⁰⁹ See MODEL RULES OF PROF'L CONDUCT R. 7.3 (1983); see also MODEL RULES OF PROF'L CONDUCT R. 7.3 cmt. 6 (1983) (“This Rule is not intended to prohibit a lawyer from contacting representatives of organizations or groups that may be interested in establishing a group or prepaid legal plan for their members... for the purpose of informing such entities of the availability of and details concerning the plan....”).

²¹⁰ LEGAL ETHICS, LAW. DESK BK. PROF. RESPONSIBILITY § 7.3-3 (2013-2014 ed.); see *Shapiro v. Kentucky Bar Ass'n*, 486 U.S. 466 (1988) (which gave constitutional protection to targeted, direct mail advertising, any complete prohibition of targeted mail now raises severe constitutional issues).

²¹¹ LEGAL ETHICS, LAW. DESK BK. PROF. RESPONSIBILITY § 7.3-3 (2013-2014 ed.) (“[T]he Rules are very clear that the lawyer himself or herself cannot engage in ‘personal contact’ (solicitation) with the members.”).

²¹² MODEL RULES OF PROF'L CONDUCT R. 7.3 cmt. 9 (1983).

²¹³ LEGAL ETHICS, LAW. DESK BK. PROF. RESPONSIBILITY § 7.3-3 (2013-2014 ed.)

²¹⁴ *Id.*

²¹⁵ *Id.* (“This distinction is purportedly justified by the fact that the lawyer, when he is soliciting the representatives of a proposed plan is not engaging in solicitation but in advertising because this ‘form of communication is not directed to a prospective client,’ but to the representatives of the plan who are ‘acting in a fiduciary capacity seeking a supplier of legal services for others who may, if they choose, become prospective clients of the lawyer.’”); see MODEL RULES OF PROF'L CONDUCT R. 7.3 cmt. 7 (1983).

²¹⁶ See Clark, *supra* note 3, at 285.

Generally, UPL is governed by rules of professional conduct or by criminal statutes.²¹⁷ Model Rule 5.5, which governs UPL, states:

(a) A lawyer shall not practice law in a jurisdiction in violation of the regulation of the legal profession in that jurisdiction, or assist another in doing so. (b) A lawyer who is not admitted to practice in this jurisdiction shall not: (1) except as authorized by these Rules or other law, establish an office or other systematic and continuous presence in this jurisdiction for the practice of law²¹⁸

Sections (c) and (d) contain a list of narrow exceptions to this general prohibition.²¹⁹ The best example of the concern faced by internet-based legal service plans can be found in LegalZoom's registration statement to the SEC, which states:

Our business model includes the provision of services that represent an alternative to traditional legal services, which subjects us to allegations of UPL. UPL generally refers to an entity or person giving legal advice who is not licensed to practice law. However, laws and regulations defining UPL, and the governing

²¹⁷ Clark, *supra* note 3, at 275; *see, e.g.*, N.J. STAT. ANN. § 2C:21-22 (West 2012) (criminalizing knowing engagement in the unauthorized practice of law in New Jersey).

²¹⁸ MODEL RULES OF PROF'L CONDUCT R. 5.5 (2011) (mandating that lawyers may not practice in jurisdictions where they do not hold a license to practice).

²¹⁹ *See id.* Subsections (c) and (d) state:

(c) A lawyer admitted in another United States jurisdiction, and not disbarred or suspended from practice in any jurisdiction, may provide legal services on a temporary basis in this jurisdiction that: (1) are undertaken in association with a lawyer who is admitted to practice in this jurisdiction and who actively participates in the matter; (2) are in or reasonably related to a pending or potential proceeding before a tribunal in this or another jurisdiction, if the lawyer, or a person the lawyer is assisting, is authorized by law or order to appear in such proceeding or reasonably expects to be so authorized; (3) are in or reasonably related to a pending or potential arbitration, mediation, or other alternative dispute resolution proceeding in this or another jurisdiction, if the services arise out of or are reasonably related to the lawyer's practice in a jurisdiction in which the lawyer is admitted to practice and are not services for which the forum requires *pro hac vice* admission; or (4) are not within paragraphs (c)(2) or (c)(3) and arise out of or are reasonably related to the lawyer's practice in a jurisdiction in which the lawyer is admitted to practice.

(d) A lawyer admitted in another United States jurisdiction, and not disbarred or suspended from practice in any jurisdiction, may provide legal services this jurisdiction that: (1) are provided to the lawyer's employer or its organizational affiliates and are not services for which the forum requires *pro hac vice* admission; or (2) are services that the lawyer is authorized by federal or other law or rule to provide of this jurisdiction. *Id.*

bodies that enforce UPL rules, differ among the various jurisdictions in which we operate. We are unable to acquire a license to practice law in the United States, or employ licensed attorneys to provide legal advice to our customers, because we do not meet the regulatory requirement of being exclusively owned by licensed attorneys. We are also subject to laws and regulations that govern business transactions between attorneys and non-attorneys, including those related to the ethics of attorney fee-splitting and the corporate practice of law.²²⁰

The main concern for legal service plans in dealing with the threat of UPL is the fact that “nonlawyers are prohibited not only from practicing law directly, but also from forming partnerships or corporations that offer the services of lawyers to the public.”²²¹

B. ERISA

A plan is considered to be an employee welfare benefit plan subject to the Employee Retirement Income Security Act (“ERISA”) when it provides employees and their beneficiaries with prepaid legal service benefits, “whether through insurance or otherwise.”²²² However, according to the Department of Labor, “a prepaid legal services plan itself – that is, the plan as developed by a bar association or other provider group – does not become an ERISA welfare plan until it is adopted by an employer, an employee organization, or an employee beneficiary organization as the funding vehicle for delivering the benefits promised.”²²³ Once a legal services plan is subjected to ERISA regulation, state laws that relate to employee benefit plans are, for the most part, preempted by ERISA.²²⁴ However, in some cases, ERISA’s broad provisions will not “prevent a state court from approving a prepaid legal services plan authorized by state law and regulating the professional conduct of lawyers who render legal services

²²⁰ SECURITIES AND EXCHANGE COMMISSION, *LegalZoom.com Inc., Form S-1 Registration Statement*, http://www.sec.gov/Archives/edgar/data/1286139/000104746912005763/a2209299zs-1.htm#de73503_risk_factors (last visited May 14, 2014).

²²¹ Andrews, *supra* note 189, at 600.

²²² MICHAEL B. SNYDER, HUM. RESOURCES SERIES COMPENSATION AND BENEFITS, § 47:235 (2014); *see* Andrews, *supra* note 196, at 600.

²²³ MICHAEL B. SNYDER, HUM. RESOURCES SERIES COMPENSATION AND BENEFITS, § 47:235.

²²⁴ *Id.*

under the plan.”²²⁵ In 1975, the New York Court of Appeals defined the state’s regulatory functions as the following:

[T]o assess the authenticity of the plan, to assure its freedom from any taint of improper professional conduct, to preserve the attorney-client relation, to require full disclosure to prevent fraud or other wrong upon the public, and, above all, to make sure that future professional conduct on behalf of [prepaid legal service plans] ... remains subject to disciplinary control by the Appellate Division.²²⁶

One important goal of ERISA is to foster an environment that allows for the growth of group and prepaid legal service plans “by preempting the regulatory efforts of state bar associations and other state disciplinary authorities.”²²⁷ The legislative history provides evidence of congressional disapproval of the efforts by state bar associations to hamper the formation of closed-panel legal plans “through disciplinary regulations forbidding lawyer participation in plans that restrict client access to specified attorneys.”²²⁸ One of ERISA’s primary proponents stated it best: “[T]he State, directly or indirectly through the bar, is preempted from regulating the form and content of a legal service plan, for example, open versus closed panels, in the guise of disciplinary or ethical rules or proceedings.”²²⁹

The regulatory arm of ERISA “imposes explicit fiduciary duties on a wide range of individuals involved with employee benefit plans, including plan administrators and other defined parties in interest.”²³⁰ In general, ERISA describes this duty as acting with “the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and

²²⁵ *Id.*; In re 1115 Legal Serv. Care, 541 A.2d 673 (N.J. 1988); see Costich, *supra* note 183, at 644 (explaining that ERISA’s legislative history shows that ERISA is not meant to “preempt bar association ethical rules, guidelines or disciplinary actions”) (internal quotation omitted).

²²⁶ *Feinstein v. Att’y Gen.*, 326 N.E.2d 288 (N.Y. 1975); see also *Matter of UAW Legal Serv. Plan*, 416 N.Y.S.2d 133, 134 (N.Y. App. Div. 1979) (holding that ERISA does not preempt this level of regulation of state lawyers in a prepaid legal services plan).

²²⁷ Jay Conison, *The Federal Law of ERISA Plan Attorneys*, 41 SYRACUSE L. REV. 1049, 1086 (1990).

²²⁸ Costich, *supra* note 183, at 643.

²²⁹ *Id.* at 643 – 44; 120 Cong. Rec. 29,949 (1974) (statement of Sen. Jacob Javits).

²³⁰ Costich, *supra* note 183, at 642 “[B]y virtue of ‘providing services . . . to the [ERISA] plan,’ plan lawyers are ‘parties in interest’ and are thus prohibited from engaging in the furnishing of services to the plan for more than ‘reasonable compensation.’”); see 29 U.S.C. § 1002(14)(B) (2008) (defining “party in interest”); *Id.* § 1108(b)(2), (c)(2).

familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.”²³¹

Fiduciary cases involving ERISA’s provisions regulating group and prepaid legal service plans are “sparse but dramatic.”²³² For instance, in *Benvenuto v. Schneider*, the trustees of a union’s legal services benefit trust and the providing law firm were held liable for the overpayment of legal fees in the amount of \$292,800.²³³ The trustees did not meet their fiduciary duty to their trust’s members because they “failed to interview . . . any other law firm . . . failed to monitor utilization of the firm . . . failed to analyze the amount being paid . . . and failed to adequately insure that the assets . . . were being used properly.”²³⁴ The law firm received excessive amounts of payments compared to the services rendered and benefits received.²³⁵ The court levied sanctions on both the law firm and plan trustees for their breach of fiduciary duties.²³⁶ This case illustrates that, when there is proof of a breach of fiduciary duty by a plan trustee in an ERISA legal services benefit trust, plan attorneys also owe a fiduciary duty to the plan and can also be held liable for damages to the plan.²³⁷

When a legal services plan falls under the regulation of ERISA, there are steps that plan administrators and trustees can take to avoid breaching their fiduciary duties. To avoid liability for their conduct while administering the plan,

²³¹ Costich, *supra* note 183, at 643; 29 U.S.C. § 1104(a)(1)(B) (1988). The statute states, in pertinent part:

(a) Prudent man standard of care **(1)** Subject to sections 1103(c) and (d), 1342, and 1344 of this title, a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and-- **(A)** for the exclusive purpose of: **(i)** providing benefits to participants and their beneficiaries; and **(ii)** defraying reasonable expenses of administering the plan; **(B)** with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; **(C)** by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and **(D)** in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter and subchapter III of this chapter. *Id.*

²³² Costich, *supra* note 183, at 646.

²³³ *Benvenuto v. Schneider*, 678 F. Supp. 51 (E.D.N.Y.1988).

²³⁴ *Id.* at 52.

²³⁵ *Id.* at 54

²³⁶ *Id.* (citing 29 U.S.C. §1004(a)(1)(A), (B)).

²³⁷ Julianne Joy Knox, *Nieto v. Ecker: Incorporation of Nonfiduciary Liability Under ERISA*, 73 MINN. L. REV. 1303, 1310 & n. 32 (1989).

“plan trustees [can] do the following: identify the type of delivery system best suited to the needs of the group served, establish reasonable compensation levels, establish an actuarially sound schedule of benefits, and document the basis for each of these decisions.”²³⁸ Once the plan is established, “the trustees’ duties include employing qualified lawyers²³⁹, making timely payments to eligible beneficiaries, avoiding excessive payments, and scrupulously observing the rules concerning provision of services to themselves and other fiduciaries.”²⁴⁰

C. State Supreme Court and Insurance Department Regulations

Group and prepaid legal service plans created a regulatory issue for state courts and the collective bar. Although the Model Rules created a guide for lawyers to adhere to professionally, states still had the task of developing a regulatory mechanism to regulate legal service plans. The mechanism utilized by many states is a combination of their state supreme courts’ regulation²⁴¹ of legal service plans and registration requirements under various forms of state commerce and insurance departments.²⁴² This section will use Tennessee as an example to demonstrate the current regulatory mechanisms that govern group and prepaid legal service plans’ day-to-day operations, initial formation approval, and financial requirements.

The Supreme Court of Tennessee requires all legal service plans to file an initial registration statement and annual registration statements with the Board of Professional Responsibility.²⁴³ In order for a Tennessee-based legal service plan to remain in compliance with the Supreme Court’s compliance standards, it must adhere to the following:

²³⁸ ROGER D. BILLINGS, JR., PREPAID LEGAL SERVICES § 6.63 (Lawyers Co-op.1981 & Supp.1985).

²³⁹ See *Id.* at §6.96.

²⁴⁰ *Id.* at §6.100 (citing ERISA Opinion Letter No. 78-29 (1978) (finding trust indenture provision authorizing reimbursement of trustee legal fees incurred in defending charges of violation of fiduciary duties unenforceable)).

²⁴¹ TENN. SUP. CT. R. 44 (“This Rule shall govern intermediary organizations as defined in RPC 7.6(a). An intermediary organization is a lawyer . . . prepaid legal service provider, or similar organization the business or activities of which include the referral of its customers, members, or beneficiaries to lawyers for the performance of fee-generating legal services or the payment for or provisions of legal services to the organization’s customers, members, or beneficiaries in matters for which the organization does not bear ultimate responsibility. . .”).

²⁴² See *Legalclub.com, Inc. v. Dep’t of Consumer & Bus. Servs.*, 50 P.3d 1196, 1197 (Or. Ct. App. 2002) (explaining that since Legalclub.com, Inc., was offering “legal expense plans,” they were subject to the Legal Expense Organizations Act).

²⁴³ TENN. SUP. CT. R. 44(A)(1).

(1) The organization shall not be owned or controlled by any participating lawyer, a law firm with which a participating lawyer is associated, or a lawyer with whom a participating lawyer is associated in a firm. (2) The customer, member, or beneficiary of the organization, and not the organization, shall be the client of the participating lawyer. (3) The organization shall assert no improper influence upon, nor shall it infringe upon, the attorney-client relationship or the independent professional judgment of the participating lawyer. (4) The organization shall not limit the objectives of the representation to be provided by participating lawyers to its customers, members, or beneficiaries, or the means to be used to accomplish those objectives, if such a limitation would materially impair the lawyer's ability to provide the client with the quality of representation that would be provided to a client who had not been referred to the lawyer by the organization. (5) The organization shall not request or require that a participating lawyer reveal information that is privileged or protected by RPC 1.6. (6) The organization shall not request or require that a participating lawyer take any action prohibited by, or fail to take any action required by, the Tennessee Rules of Professional Conduct. (7) Customers, members, or beneficiaries of the organization shall be informed that they may file a complaint of unethical conduct by a participating lawyer with the Board of Professional Responsibility, and informed of the method by which they may do so. (8) Any organization that is a prepaid legal insurance provider shall comply with Tennessee Code Annotated, Title 56, Chapter 43, known as the Tennessee Legal Insurance Act. (9) The organization shall permit the participation of not less than four (4) lawyers licensed to practice in Tennessee, not associated with each other in a firm, and each of whom maintains an office in the geographical area served by the organization; provided, however, that the organization may require such participating lawyers to: (a) meet reasonable and objectively determinable standards of competence and experience; and (b) pay a reasonable participation fee in conformance with RPC 5.4(a). (10) The organization shall not condition referral of its customers, members, or beneficiaries to participating lawyers upon a preliminary determination by the organization that the client's claims or defenses have merit or economic value; however, the organization may perform call screening as necessary to determine the applicability and availability of appropriate non-legal services. (11) The organization shall utilize reasonable procedures to assure that participating lawyers are properly licensed and competent to handle the matters referred to them. (12) The organization shall utilize reasonable procedures to

provide substitute counsel in the event that a lawyer to whom a matter is referred cannot undertake or continue the representation in compliance with the Rules of Professional Conduct or this Rule. (13) If the organization is a not-for-profit lawyer referral service, it may charge a fee calculated as a percentage of legal fees in compliance with RPC 5.4(a)(6). (14) The organization shall establish and implement a reasonable grievance or complaint procedure for the resolution of complaints or grievances by customers, members, or beneficiaries who are dissatisfied with the services or fees provided by the organization or its participating lawyers. (15) An organization shall apprise itself of any public disciplinary history of any participating lawyer and shall, when appropriate, review the files of the Board of Professional Responsibility concerning any such public discipline imposed on any participating lawyer before allowing that lawyer to participate in providing services.²⁴⁴

The Tennessee Supreme Court delegates its regulatory function to the Board of Professional Responsibility.²⁴⁵

In addition to the regulations proffered by the Tennessee Supreme Court, Tennessee also requires all legal service plan operators to register with the Insurance Division of the Tennessee Department of Commerce and Insurance (“TDCI”).²⁴⁶ According to the Tennessee Legal Insurance Act, all legal service plans must be registered with the TDCI,²⁴⁷ and no legal service plan can legally operate in Tennessee without first applying for a certificate of authority to sell legal service plan policies through the TDCI.²⁴⁸ Thereafter, the TDCI has full discretion to approve, modify, or reject a legal service plan according to its anticipated operations.²⁴⁹ In order to effectively regulate legal service plans, the TDCI requires an initial registration statement, proof of financial viability, and annual operating statements in accordance with the Tennessee Legal Insurance Act’s requirements.²⁵⁰

²⁴⁴ TENN. SUP. CT. R. 44(B)(1-15).

²⁴⁵ TENN. SUP. CT. R. 44 (A)(1).

²⁴⁶ TENN. COMP. R. & REGS. 0780-01-60-.03 (1991).

²⁴⁷ TENN. CODE ANN. § 56-43-105 (West 2008).

²⁴⁸ TENN. COMP. R & REGS. 0780-01-60-02 (1991).

²⁴⁹ TENN. COMP. R. & REGS. 0780-01-60-.03 (1991).

²⁵⁰ *Id.*

VI. HOW LEGAL SERVICE PLANS WILL MAINTAIN THEIR SUCCESS

The continued growth of group and prepaid legal services will be controlled by the regulatory policies that govern them.²⁵¹ Thus, governmental regulations, courts, and bar associations will hold the key to group and prepaid legal services' bright future or dark demise. Proponents and detractors of the expansion of group and prepaid legal services must realize that, unless regulatory bodies implement the same conservative and restrictive policies of the early twentieth century, legal service plans are here to stay and are on track to have groundbreaking effects on how legal services are delivered and procured in the future. These effects are personified by the impact that group legal services had on employee benefits packages in the early 1990's.²⁵² Although innovations in group and prepaid legal services have allowed the industry to remain successful into the twenty-first century, new and even more disruptive innovations are now being introduced.

A. The Internet's Impact on Legal Service Plans

According to many legal commentators, the U.S. system of legal regulation "inhibits innovation. Lawyers are blocked from innovations they might pursue by the heavy hand of legal regulation. Even worse, lawyers are not the only [potential legal service providers] blocked. . . ."²⁵³ Current regulations keep non-lawyer legal service innovators that could offer better or cheaper products from entering into the legal marketplace.²⁵⁴ Among these non-lawyer legal service innovators are internet-based group and prepaid legal service plan operators.²⁵⁵ Sites such as LegalZoom and RocketLawyer entered the legal marketplace with the intention of taking advantage of the changing nature of the delivery of legal services, and, although their business models include many forms of revenue derived from legal services, they both include internet-based legal

²⁵¹ See generally Campbell, *supra* note 89, at 34-37.

²⁵² Heid & Misulovin, *supra* note 60, at 339 (explaining the impact group legal services had on large and small companies employee benefit offerings).

²⁵³ Campbell, *supra* note 89, at 3.

²⁵⁴ *Id.* at 3-4 (citing "legal process outsourcers serving the U.S. legal market, online legal document vendors providing personalized wills to consumers, database companies providing actionable information on intellectual property holdings and enforcement, and marquee lawyers leaving their pre-eminent law firms to set up flat-rate boutiques with radically different firm structures" as examples of lawyer and non-lawyer innovators that offer better or cheaper products to legal consumers).

²⁵⁵ Clark, *supra* note 3, at 248.

service plans into their product offerings to their customers.²⁵⁶ For example, pertaining to legal service plans, LegalZoom's management stated:

We intend to offer our subscription legal plans to a wider group of customers by making them available in additional states, bundling them with more of our services, and offering them on a standalone basis. We plan to invest in marketing campaigns to promote our subscription legal plans. Our aim is to reach a broader group of customers through our legal plans, including those who are unsure of their legal needs or who want the added comfort of speaking with an attorney.²⁵⁷

However, their inclusion of internet-based legal service plans has not come about without increased tension between the new providers and members of the organized bar.²⁵⁸

LegalZoom, in particular, has encountered heavy scrutiny from the legal community.²⁵⁹ This is likely due to LegalZoom's primary product offering of personalized legal documents. However, LegalZoom recognizes that its nationwide legal service plans can be a cause for legal concern as well.²⁶⁰ In its public offering registration statement filed with the Securities and Exchange Commission ("SEC"), LegalZoom addressed the uncertainty it faces through its legal service plan product offerings:

Regulation of our legal plans varies considerably among the insurance departments, bar associations and attorneys general of the particular states in which we offer, or plan to offer, our legal

²⁵⁶ *Id.* at 249.

²⁵⁷ SECURITIES AND EXCHANGE COMMISSION, *LegalZoom.com Inc., Form S-1 Registration Statement*, http://www.sec.gov/Archives/edgar/data/1286139/000104746912005763/a2209299zs-1.htm#de73503_risk_factors (last visited May 14, 2014).

²⁵⁸ Jennifer Smith, *No-Frill Legal Services Grow*, WALL ST. J., Dec. 3, 2012, available at www.webcitation.org/6GRQezkdt (noting the many legal conflicts between the traditional legal community and its online counterpart).

²⁵⁹ Clark, *supra* note 3, at 256-57 ("LegalZoom has had to do battle on many fronts and no less than seven states have expressed the opinion that LegalZoom is engaged in the unauthorized practice of law. In Missouri and California LegalZoom has had to pay damages to classes of consumers who claimed fraudulent and deceptive practices. In Pennsylvania, Ohio, Connecticut, North Carolina and Alabama bar authorities found unauthorized practice violations.").

²⁶⁰ SECURITIES AND EXCHANGE COMMISSION, *LegalZoom.com Inc., Form S-1 Registration Statement*, http://www.sec.gov/Archives/edgar/data/1286139/000104746912005763/a2209299zs-1.htm#de73503_risk_factors (last visited May 14, 2014).

plans. In addition, some states may seek to regulate our legal plans as insurance or specialized legal service products.²⁶¹

LegalZoom offers two membership options: small business legal plans and consumer legal plans.²⁶² Both membership options include the “LegalZoom Peace of Mind Review,” which not only includes ‘hundreds of automated online checks,’ but also careful review by ‘document scriveners’ for grammar, spelling, and completeness of information.”²⁶³

LegalZoom’s nationwide battle with regulatory mechanisms governing their entrance into the legal marketplace demonstrates that although the organized bar and government regulations have come a long way, they still have far to go before the industry can truly begin to foster innovations in the legal marketplace, particularly for internet-based group and prepaid legal services. “The bar has acknowledged and bemoaned the problem of access to the legal system for many decades, but no effective solution has been forthcoming.”²⁶⁴ With the advent of internet-based legal service plans that allow legal consumers to access the legal system like never before, the simple solution would seemingly be for the bar to support this new legal service delivery method. Yet, “at least twelve states have raised as many as eight separate legal objections to various aspects of internet based legal service delivery systems.”²⁶⁵ These objections have the effect of “reducing the supply of providers of legal services in any particular state, thereby assuring an increased supply of potential clients to the in-state license holders.”²⁶⁶ More to the point, these objections have the effect of decreasing the amount of competition that in-state license holders have to deal with, which directly affects the cost of legal services that legal consumers must pay.²⁶⁷

B. *Deregulation of the Practice of Law in Favor of Market Forces*

The American regulatory scheme governing the practice of law “has been shaped by the rules of the legal profession, and the rules limiting the competition from non-lawyers.”²⁶⁸ The strict application of statutes and rules “prohibiting the

²⁶¹ *Id.*

²⁶² *Id.*

²⁶³ Clark, *supra* note 3, at 270.

²⁶⁴ *Id.* at 292.

²⁶⁵ *Id.*

²⁶⁶ Gerard J. Clark, *The Two Faces of Multi-Jurisdictional Practice*, 29 N. KY. L. REV. 251, 265 (2002).

²⁶⁷ *See* Clark, *supra* note 3, at 293.

²⁶⁸ Campbell, *supra* note 89, at 28 – 29.

unauthorized practice of law has yielded economic inefficiency, including but not limited to causing basic legal services to be outside the reach of many or most consumers.²⁶⁹ These rules lock lawyers into one mode of value creation for consumers, and, simultaneously, limit new entrants from offering more efficient legal solutions that could increase the affordability of legal assistance.²⁷⁰

In the United States, legal practitioners must practice law in a specified manner. State rules and regulations based on the Model Rules of Professional Responsibility “set out in painstaking detail the characteristics of acceptable legal practice.”²⁷¹ Simply stated, the rules governing the practice of law seemingly define the product that legal service providers can and should deliver to consumers. Hence, the regulatory framework that is in place “mandates that lawyers deliver their services according to this model.”²⁷² Modification of individual rules will not make the required impact on the regulatory framework to foster a more innovative legal marketplace.²⁷³ Although drastic in scope, deregulation of the practice of law in favor of market forces is the most efficient way to foster a truly innovative environment in the legal marketplace.

The regulatory framework in place has some advantages in certain legal situations, typically complex situations, where highly-trained lawyers with the requisite legal knowledge are necessary to solve certain legal issues.²⁷⁴ However, pertaining to group and prepaid legal services, “situations can be identified whereby standardized solutions can be applied safely” without the use of highly-trained lawyers.²⁷⁵ Deregulation of the practice of law would allow for innovative legal service providers, including non-lawyers, to deliver value to an underserved or unserved portion of Americans.²⁷⁶

VII. CONCLUSION

Group and prepaid legal service plans have become commonplace among many forms of innovative legal service delivery methods. Their continued growth

²⁶⁹ LegalZoom.com, Inc. v. N.C. State Bar, No. 11CVS15111, 2014 WL 1213242, at *10 (N.C. Super. Mar. 24, 2014).

²⁷⁰ Campbell, *supra* note 89, at 29.

²⁷¹ *Id.*

²⁷² *Id.*

²⁷³ *Id.* at 30.

²⁷⁴ *Id.* at 32.

²⁷⁵ *Id.*

²⁷⁶ *Id.* (“Reformers can both identify niches where full legal training is not required and change the substantive law to be amenable to off-the-shelf-services.”).

is not only important for our evolving legal service industry, but it is a crucial part of the effort to increase access to legal services for middle-income Americans. However, similar to the conservative policies of the past, the regulatory framework in place continues to inhibit the requisite innovative organizational structures that will be necessary for group and prepaid legal service plans to flourish in the future.

Currently, legal service plans “ha[ve] been overwhelmingly positive and plan member satisfaction has been extremely well documented by the American press.”²⁷⁷ This positive view of group and prepaid legal plans has created, and should continue to create, a new trust for and appreciation of attorneys that has been almost non-existent in the legal community over the last century.²⁷⁸ Legal service plans give plan members access to low cost legal services, which allows middle-income Americans to “discover their legal rights, rather than forgo them.”²⁷⁹ These plan mechanisms entice “plan members to envision lawyers, not as greedy, expensive sharks who are likely to make what may already be a complex problem more painful and costly, but rather as reasonable and helpful troubleshooters capable of solving problems with a few phone calls or a well-placed letter.”²⁸⁰

²⁷⁷ Heid & Misulovin, *supra* note 60, at 364.

²⁷⁸ See generally Charles Silver & Frank B. Cross, *What's Not to Like About Being a Lawyer?*, 109 YALE L.J. 1443 (2000) (“In the late twentieth century, everyone complained about the decline of the legal profession.”).

²⁷⁹ Heid & Misulovin, *supra* note 60, at 364.

²⁸⁰ *Id.*