



# Face Facts

## Legal

MacIntyre Hudson LLP's Legal Sector publication for UK solicitors and law firms



## Using the downturn to your advantage



Credit crunch. Unemployment. Toxic debt. With the headlines as gloomy as they are, anyone could be forgiven for being pessimistic. However, for good business people, now is the time to take the sort of root and branch review of the way a firm works and ensure that when the upturn comes, your firm is fitter and stronger, having learnt from past mistakes.

"There is no better time than now to make sure your business is lean and efficient," comments Grant Gleghorn, Head of MacIntyre Hudson's Legal sector group.

"A depressed market is still a very substantial market and presents significant opportunities, especially among smaller businesses, which have often neglected many important legal issues (e.g. terms of trade, service contracts, shareholders' agreements). A downturn tends to bring the problems caused by inefficient commercial practice into sharp focus. Make sure your practice comes out of the recession a better business than when it went in."

By considering the following actions, you could weather the storm and actually prosper when your competitors are struggling:

### Clear out your toxins

Many firms carry large amounts of unrealisable work in progress – not only old time that hasn't been cleared after a matter is completed but also time built up on files for clients who have failed, or which is just not chargeable. Not only will clearing this work out help your tax bill, it will also make your management accounts more accurate. Also, take a realistic view of your debtors and provide for them promptly.

### Retain your customers

Twenty percent of your clients generate eighty percent of your profit. Why not focus on these clients for the next six months? Keep in close contact with them and link your best people to them. Do they have any contacts who they can refer you to?

### Retain your people

In tough times you must protect your best people. How can you make sure you keep the ones you need? Do they have contracts? Do you reward them and show how much you appreciate their efforts?

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### Using the downturn to your advantage

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#### Management accounts and budgets

Run your business and control your expenditure based on your management accounts, not out of date budgets, and make sure they give you valid information. Flex your budgets at least quarterly and apply corrective action promptly.

#### Cash flow

Cash is the life blood of every business. You need to get as much cash as you can into the business and protect it once you have it. Chris Stratton, Head of MacIntyre Hudson's Business Strategy Group, suggests identifying where you have cash stored: "Is it with clients who are slow to pay? Can you reduce your overheads? Can you stop spending in any areas or slow down the speed at which money goes out?"

#### Improve your profit

Cash and profit are closely related. "Around twenty percent of your expenses are due to waste in your business" explains Chris. "By removing that waste, the savings become instant profit (and probably cash). If you had to double your profit within three months what would you do? Why not do it anyway? Do you really know what profit you make each year / month / day?"

#### Target today's market

There is a lot of work out there still, but it probably isn't what was forecast in your marketing

plan. For example, some firms have generated significant fees through marketing aimed at firms experiencing problems in the recession.

Landlord and tenant, debt, family law and employment - to name but four - have been busy areas of work for some firms. However, you may need to be more creative in marketing and pricing (e.g. retainers and fixed fees) to win business.

#### Maintain your energy

Time management is the biggest thing to address in tough times. Again, twenty percent of what you do generates eighty percent of the benefit you are to your firm. Look at what you are doing for the rest of the time and perhaps cut down on some of the lower value activities.

Clare Jarrett, Lexcel Manager at the Law Society, thinks that many practices may be more prepared than they realise, commenting: "If you have implemented a supportive organisation-wide management framework (such as Lexcel)...it should help you identify risks and adapt to change with greater speed.

"While a framework may not prevent a negative impact, it should enable a thorough review which could help minimise the consequences to your business, making survival a little less daunting."

### Gaining finance in a downturn



Chris Marston, Head of Solicitors' Banking at Lloyds TSB Commercial, explains the ways that lawyers and solicitors can help their bankers to help them.

Few businesses in any sector can operate without debt. But finding the right balance is important. Firms should re-assess their debt structure and align this to the needs and nature of their business.

#### A healthy financing mix should include:

- Term loans - usually for the purchase or refinancing of long term assets
- Short term loans - often used for software purchase, PII premium or Practising Certificates
- HP & leasing - cars, office equipment, telecoms
- Overdraft - to finance working capital, i.e. WIP, disbursements, debtors

#### Overlooked source of finance

One source of financing that legal practitioners tend to overlook is themselves! What better demonstration of confidence in the firm's future than for partners to invest their own cash?

Banks may also be able to provide partner equity loans, sometimes unsecured, over periods as long as 25 years. This tangible show of commitment can make it more likely that a bank will provide the rest of the finance required. It can improve the gearing in the business too, and borrowing for this purpose can attract tax relief.

#### Management information

Bankers want to help their customers to survive these challenging times - a failed business is in nobody's interest. High-quality management information helps to show the real issues in a firm and should include:

- Profit & loss - with comparison to budget and comments on material variances.
- Balance sheet - to help the bank to understand movements of fixed and working capital as well as the profit position.
- Working capital analysis - to include WIP; debtors; disbursements (analysed by age and fee-earner / department / branch / office) and the often ignored creditors.
- Also critical to understanding a firm's financing needs is a note of new instructions (by fee earner / department / branch / office) and a cashflow forecast.

"There is a lot of work out there still, but it probably isn't what was forecast in your marketing plan...you may need to be more creative in marketing and pricing to win business."



## Solicitors' Accounts (Legal Services Act) amendment rules 2009

From 31 March 2009, The Solicitors Regulation Authority (SRA) is able to regulate Legal Disciplinary Practices (LDP's), resulting in amendments to the Solicitors' Accounts Rules (SAR). The Legal Services Act 2007 introduced firm based regulation and therefore the SAR has been extended to regulate sole practitioners, partnerships, companies and LLPs. It also applies to practices with non-solicitor lawyers as managers; practices where up to 25% of managers are not legally qualified; individual managers and employees of those practices and in-house lawyers.

### Amendments to rule 23

The Legal Services Act 2007 also established the concept of a 'manager'. Amendments to rule 23 now permit 'managers' to authorise withdrawals from client account. The term 'manager' means:

- A partner in a partnership
- A member of an LLP
- A director of a company

and may include managers that are not legally qualified. The Guidelines for Accounting Procedures and Systems recommend that firms establish clear procedures for ensuring that persons permitted to authorise the withdrawal of client money from client account have an appropriate understanding of the rules, including SAR rules 22 and 23.

### Controlled trust

The statutory concept of a 'controlled trust' has been abolished and therefore all money held by a practice will be categorised as either client money or office money. The same interest provisions will apply to all client money and as a consequence, if client money previously defined as controlled trust money is held in general client account then the interest provisions set out in SAR rule 24 will apply. Interest complaints will be handled by the Legal Complaints Service.

For further information on the amendments, please contact your local member of the Legal sector team.



## The ninth LMS Financial Benchmarking Survey



The 2008 LMS Financial Benchmarking Survey produced by the Law Management Section (LMS) and Robert Mowbray, sponsored by HSBC and in association with MacIntyre Hudson LLP, is now available.

The survey is based upon responses (from LMS members

in England and Wales) to a questionnaire which had to be submitted by December 2008. It covers a range of financial results such as fee income, profitability, employment costs and working capital management as well as management best practice topics.

### Highlights from the survey, taken from the responses of 108 firms, include:

Annual median fee income per fee earner	£110k
Annual median fee income per partner	£568k
Average fee earner cost of total fees	34%
Average cost of support staff (Greater London only)	£64k
Median profit for individual equity partners	£138k
Median profit for individual equity partners (Greater London only)	£268k
London median profit percentage	27.4%
Median cash lock up period	129 days
Percentage of Lexcel accredited firms	44%
LLP conversion percentage	47%

The above is just a snapshot of the detailed findings this survey offers.

Order your copy of this "essential tool" for managing partners, finance directors and department managers of member firms from the LMS online shop at: [www.lawmanagementsection.org.uk](http://www.lawmanagementsection.org.uk)

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### Is it time to change your year end?



Many law firms have financial year ends that are either 31 March or 30 April. Mike Hayes, Tax Principal at MacIntyre Hudson, assesses the benefits of both. With a 30 April year end, if profits are increasing, they are taxed a year later than would have been the case with a March year end.

Conversely, if your firm suffered reduced levels of profits in 2008/09, the tax on those reduced profits is for the 2009/10 tax year. This will mean reduced tax payments in January and July 2010.

A 31 March year end fits in with the fiscal year and tax reporting issues are that much simpler. If profits have reduced significantly, a March year end would bring:

- Reduced tax payments on account due on 31 January and 31 July 2009.

- If payments on account in January 2009 have already been made on the basis of a higher level of profits, then a tax refund may be due.
- The payments on account for 2009/10 will be based on the 2008/09 assessment and will be reduced accordingly.
- Whilst changing to March can give an immediate benefit in terms of tax payments, if profits increase they will be taxed one year earlier than would have been the case with an April year end. Again, you cannot change your year end back for a period of 6 years without prior HMRC consent.

#### Considerations

When considering a change from April to March, you should also take into account the following:

- You cannot change if you have done so within the previous 6 years without HM Revenue & Customs (HMRC) consent.

Individual calculations need to be undertaken to establish whether or not a change in year end would be beneficial for your firm. For more information, please contact your local member of the Legal sector team.

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