



Face Facts

Legal

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



Planning for the challenges of 2010



Emerging from a recession can be a dangerous time for any firm as they struggle with cash flow to finance improving levels of work. 2010 remains uncertain and, for many law firms in particular, it could be a defining watershed.

Some of the challenges law firms are now facing are:

- the changing needs of clients
- managing higher performance
- the increasing burden of compliance
- managing cash and building profitability.

Having worked hard to restructure and become 'lean' in a tough economy, will you remain lean and use better times to build profits or will you open the floodgates of spending to recruit again?

Don't be fooled into thinking that things will be the same as before. Clients and markets may now have changed or disappeared. Your clients are likely to want different services and be more demanding on service levels and price. You may need to 're-invent' your firm to provide services:

- that clients want;
- to higher standards; and
- at prices that clients are prepared to pay.

Client satisfaction

Forward planning will be key to gaining a competitive advantage. Firms will need to focus on the fundamentals – clients and the ability to provide them with what they want. Client satisfaction will be the only real measure of success.

Compliance

Compliance is mandatory. Law firms must do it and do it well, regardless of their size and resources. A systematic approach to managing compliance is needed and a cost / benefit analysis regarding resource is a good starting point for putting it in place.

Performance and rewards

Managing people's performance and how performance is rewarded are likely to be the issues of 2010. Already we are seeing major law firms reviewing their partnership models to ensure that reward structures are aligned to achieving strategic goals in a more competitive, post-Lehmann era.

Complacency can be the greatest danger to law firms. Whilst good financial management underpins the ability to grow (and to survive), firms need to ensure that they make the most of their clients and people.

Concentrate on cash generation initiatives to improve cash management but also deal with the 'triple whammies' of underpricing, under-recording of billable time and under-recovery of recorded WIP when billing.

With active planning and implementation, 2010 can be a great year for those law firms prepared to change for the future.

For further information, please contact your local office.

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Reducing waste

Waste in a legal business is defined as any activity which does not add value to the client.

Waste reduction can be one of the most effective ways of increasing profitability and cash flow by reducing costs and removing inefficiencies. In most cases, around 20% of costs can be attributed to waste. This is inherent in processes and procedures that have often built up over many years.

Identifying waste is not always easy as they are usually hidden costs, often missed when practices undertake cost reviews. However, when the stakes involved include cash flow, profitability and long term survival, can you really afford to overlook this area?

Seven key areas to monitor:

- Overproduction – duplication or work produced with no guarantee of billing.
- Waiting – time tied up waiting for the next step. Consider the time spent waiting for client instructions or on excessive travelling to/from clients.
- Transporting – movement of people and information. Poor workflow systems and inefficient communication mediums can all create wastage.
- Inappropriate processing – is the right tool, process and person being used for the job? Consider the grade of fee earner allocated to tasks and who undertakes non-chargeable work.

- Unnecessary inventory – for most legal practices WIP remains a key issue, with cash being tied up in unbilled time. Regular and prompt billing, accurate charging and advanced fee negotiation can all play a role in reducing WIP build up.

- Unnecessary motions – simple areas such as poor office layout, stop/start mentalities and disorganisation all create waste.

- Defects – these may result in additional time/costs being incurred. Do you have sufficient levels and quality of training, are briefings clear and is your database accurate?

Eliminating waste

Commitment to a structured waste reduction programme has been proven to achieve a return on investment of at least three to one.

The Waste Reduction Programme (WRP), developed by MacIntyre Hudson's Business Strategy Group, identifies waste resulting in improved profitability and cash flow. It evaluates processes and procedures objectively - giving you control, protection and cost savings while liberating your own resources to focus on core business priorities.

Find out more about how you can reduce the waste in your firm by contacting our Business Strategy Group at strategicplanning@mhllp.co.uk



Are your affairs compliant?

HM Revenue and Customs (HMRC) have recently launched a tax amnesty, officially named the 'Tax Health Plan', targeted at the medical profession. However, it has been speculated that lawyers and barristers will be next on their list.

The plan currently encourages doctors and dentists to disclose undeclared income upon which UK tax is due. They will be required to pay unpaid tax, interest and most likely a reduced 10% fixed penalty. It is likely that this tax amnesty will be followed by further amnesties on other professions during 2010.

With this in mind, now could be the right time to look into key areas which HMRC may identify as high risk and ensure that your affairs are compliant.

Attention will be focused on undeclared income arising from other sources in particular, for example, income from directorships or from acting as

a Judge. If necessary, HMRC will exercise their power to obtain information from third parties (as they have with doctors), therefore it is important to ensure that all income has been disclosed.

As UITF 40 adjustments can have a significant impact on your taxable income; work in progress needs to be correctly accounted for. Particular care should be taken when accounting for contingent work in progress.

Also consider motor expenses. Taxable income could be understated if these have not been correctly calculated - specifically if the correct private use adjustment has not been applied. Therefore it is imperative that the correct split between business and private use is documented; ideally a detailed log of mileage should be maintained.

If you are concerned that this may affect you please contact your local office.



“...claims against solicitors started to rise during the recession with many being due to mortgage fraud.”

The cost of fraud

2009 was a year where fraud was rarely out of the headlines. Online banking fraud increased by 55%, insurance fraud rose by 24% to £1.9 billion and identity fraud rose 74% in the first half of 2009 alone. There was a 72% increase in the number of directors disqualified for financial crime and the number of reported frauds was up by 72%. The biggest fraud ever, involving Bernard Madoff and \$65 billion, reached court and almost every area of the economy showed major increases in fraud – including the legal sector.

Claims against solicitors started to rise during the recession with many being due to mortgage fraud. Fraudsters who took out mortgages using false documentation left their lenders with huge losses when they defaulted on their repayments. A number of lenders have since attempted to recoup losses from the solicitors involved in the transactions. As a result, current indications are that the market

for professional indemnity insurance in 2010 is becoming more costly for solicitors. However, the good news is that fraud is a financial cost that can be measured and reduced like any other. Indeed, one of the biggest studies of fraud ever undertaken* found that two thirds of organisations lose between 3% - 9% of their expenditure to fraud. Nevertheless, there is evidence that when accurately measured and understood, this can be reduced by up to 40% within 12 months, with a 12:1 return on the costs of the work.

For more information about reducing fraud, contact Jim Gee, Director of Counter Fraud services, on 020 7429 4100 or email jim.gee@mhllp.co.uk

**The Financial Cost of Fraud Report*, published by MacIntyre Hudson and the Centre for Counter Fraud Studies at University of Portsmouth in November 2009.



Legal Services Act – act now!

Due at the end of 2011, the Legal Services Act could change the legal profession in England and Wales forever. Many law firms are already actively looking at the threats and opportunities that the Act presents.

How can you take advantage of it?

The advantages of the Act include the ability for law firms to receive external investment from non lawyers. This could take the form of a sale of equity or a flotation on the stock market. Various private equity houses are already considering investments in this new asset class.

Multi disciplinary practices will also be accelerated by the act with cross profession mergers between solicitors and accountants highly likely.

However, the most dynamic impact is likely to be the creation of Alternative Business Structures enabling non-lawyers to provide legal services. Dubbed “Tesco Law”, various brands including Co-op and RAC will be competing with traditional solicitors to offer

low cost high volume legal work. One way for existing solicitors to counter the threat of Tesco Law is to become part of a legal brand themselves. Being part of a brand will attract large savings on core services as buying power is increased whilst also creating a strong market presence for the benefit of its members. Members will benefit from marketing campaigns and business development techniques previously unavailable to them as smaller stand alone firms.

There is no doubt that consumers will have a greater choice than ever in buying legal services next year. For solicitors, the opportunities in the Act require planning, an open mind and the desire to adapt.

For more information on preparing for the Act, attracting investment or joining a brand contact Jon Yantin - jon@lawinvest.co.uk

Jon Yantin is a director of Law Invest Asset Management Ltd, owner of the High Street Lawyer.com brand.



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VAT exemption for insurance introduction services



A recent decision at the Court of Appeal (Trader Media Group) may affect insurance related commissions received by legal firms. In this case the Court found that an online introducer of

customers to insurance providers was an agent supplying insurance intermediary services which are VAT exempt. The taxpayer was paid a commission each time a customer took out a policy. Although the taxpayer in this case did more than a "click through" (they had collaborative arrangements with intermediaries) it demonstrates that it is not necessary to act as an insurance agent in the traditional sense, to have VAT exempt commissions.

This will affect firms receiving commissions relating to insurance products who may have incorrectly charged VAT.

Whilst there is an opportunity to recover overpaid VAT this may need to be passed back to their insurance customer. It will also open up discussions about future contract values and there may be renegotiation by insurance companies about the level of commissions that will be paid in future. Please note that exempt income must be taken into account by businesses and the partial exemption position must be reviewed to ensure that VAT recovery on costs is not restricted. Legal firms may not realise that they have VAT exempt income and the implications that this has.

VAT changes 1/1/10

Legal firms will be aware of the VAT changes that came in on 1 January 2010 in relation to services sold to and purchased from businesses outside the UK. It means that an extra level of compliance has been added to ensure that cross border transactions are reported on an European Sales List and that invoices comply with the changes. To check that your firm is VAT package compliant and prevent penalties being incurred in the future please contact Alison Horner VAT Director on 01604 624011 or alison.horner@mhllp.co.uk.

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MacIntyre Hudson LLP has 10 offices across the UK. We are also the UK member of Morison International with independent member firms worldwide.

For more details see www.morisoninternational.com

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