

**JOINT CONFERENCE OF THE FEDERATION OF EUROPEAN BARS AND  
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Legal markets in the aftermath of the Financial Crisis: How regulators  
struggle to keep pace

According to Charles Dickens "the one great principle of the English law is to make business for itself".

That may be true for some lawyers but many are now struggling to survive. Statistics would seem to show that the Legal Services sector in the UK is still one of the fastest growing sectors and that the turnover of the sector has now returned to pre-recession levels. For 2010/11 the turnover for the sector reached £25.49 billion compared to £25.47 billion in the year 2007 to 2008.

However, the turmoil in financial markets has had an effect on all sectors in the United Kingdom and the legal profession has faced immense financial pressures from general economic conditions, Legal Aid cuts and costs reforms. There is also now more competition.

What has been the response to those pressures?

In a report commissioned by the leading firm of Eversheds and entitled "Law Firm of the 21<sup>st</sup> Century – The Clients Revolution" the view is taken that the recession has in fact accelerated change in the legal sector by 10 years and as such has acted as a catalyst to such change, with a result that a traditionally inefficient sector now has to put value and efficiency first. Hourly rate billing gives way to value billing. In commerce and industry the client is recognised as holding power in the legal supply relationship and in consequence the status of in-house general counsel has risen considerably. Globalization of markets – particularly a move to the East and technology developments were equally thought to have influenced changes in the legal sector. Amongst the UK lawyers consulted in preparing the report the Legal Services Act (often blamed for the current problems) was seen as having the least impact. That view may not be shared across the legal profession.

At one time only qualified lawyers, usually operating in partnerships, were permitted to offer legal services. That has now changed. The Legal Services Act allows non lawyers to own, run or invest in legal businesses. The concept of alternative business structures is now a reality. The first licence for an ABS was issued in March 2012, since then nearly 200 licences have been issued. The profile of applicants is varied. Some are traditional firms who wish to recruit and reward high quality non legal staff; others wish to attract outside

investment. The greatest change however has been the entry of big businesses into the legal market for example the Co-operative Group, Admiral, a large insurance firm and BT have all acquired licences. In 2006 the Co-op began offering limited legal services to its members and promoted those services to its 17 million weekly shoppers. As an ABS it can now provide them to anyone. Much of its work is done over the telephone and on line and is priced on a fixed fee basis. Within 5 years the Co-op hopes to employ 3000 staff, most of them lawyers, which would make it the largest legal enterprise in the Country.

Competition from entities undertaking non reserved work who are able to operate beyond the reach of existing regulation (for example Will writers) and from ABS's may well therefore offer a greater threat than the financial crisis.

Are the regulators keeping pace with the changes that are taking place in part resulting from the recession. One of the most significant current issues for the Solicitors Regulation Authority (SRA) is the number of firms in serious financial difficulty. Where firms are insolvent or face significant regulatory defaults the outcome is often intervention by the Regulator and closure. In 2012 the SRA undertook 30 interventions at a cost to the Solicitors Profession of £1.2 million. In the first quarter of 2013 the SRA intervened into 12 firms and were in communication with another 56 firms in relation to possible intervention. The budgeted cost for interventions in the current year is now some £10.126 million! It is not just small firms who have been subject to interventions but also large practices and in one case a "Top 100" firm have fallen casualty to the intervention process. In a large number of reported cases it was the financial viability of the firm that brought about the intervention resulting from factors such as imprudent property investments or the loss of market share following government changes to Legal Aid, costs and referral fees in personal injury cases.

In a response to the changing business models available to the legal sector there have been regulatory changes. Instead of regulation by prescription directed at the individual a change has now been made to Outcome Focused Regulation of the entity so that regulatory action would be directed at the authorised or licensed body rather than at individuals. It is for the entity concerned to establish a culture backed up by systems and practices which guarantee the observance of the professional duties owed to the client. Arguably this form of regulation increases accountability and drives a business to be more conscious of compliance issues with the newly appointed Compliance Officers responsible for legal practice and financial affairs acting as internal watchdogs. It is too early to judge whether the change will prove effective, but certainly some law firms perceive the current compliance requirements to be both burdensome and disproportionate.

So what steps are UK lawyers taking to respond to the changing environment:

They are adopting different business models

They are recognising the need to preserve liquidity and to maintain working capital not merely an overdraft facility (as illustrated by Clifford Chance's recent capital call on its partners)

They are putting in place more rigorous financial controls in relation to billing and disbursements

They are introducing fixed fee and value billing

They are reacting more quickly to change and are more ready to take those hard decisions – whether to merge, retire or consolidate

They are more aware of the need to cross sell services within the firm to existing clients and to market services

They are embracing technology and its potential for delivering on line services and legal knowledge

They are recognising the need to provide added value services and "unbundled" services

It may well be that this is the modern day equivalent of the Dickensian Lawyer making business