

Pressure Points

A study of the changing legal services landscape

Executive summary

Confidence in uncertain times:

- Two thirds of respondent firms (66%) described themselves as either very confident or confident that their firm would achieve *significant growth within the next two years* (i.e. achieve over a 10% increase in profits year-on-year).

Competition is the biggest threat to law firms:

- Competition from new entrants into the legal services market, specifically from those under the Alternative Business Structures (ABS) model, was scored as the *greatest threat* to law firm businesses over the next five years - respondents scored competition from new entrants an average of '4' out of a possible '5' (with '1' indicating a threat of least significance and '5' a threat of greatest significance).
- Firms rated challenging economic and social conditions as the next most visible threat, (3.5), followed by the challenge of increased law firm competition fuelled by mergers & acquisitions (3.1).

Challenges ahead:

- Recruitment challenges and, specifically, increasing the number of lateral hires was identified as the number one *management challenge* for businesses over the next five years - respondents scored this challenge an average of '4.1' out of a possible '5' (with '5' a challenge of the greatest significance).
- Delegating more work to associates and trainee solicitors was seen as the *most effective strategy* considered by firms in response to increasing pressure on profitability - respondents scored delegation an average of '3.9' out of a possible '5' (with '5' marking a challenge of greatest impact).

The next most effective strategy was outsourcing to a fixed fee law firm subsidiary (3.5), followed by outsourcing to an offshore legal process outsourcing company (2.9); and delegating more work to paralegals (2.6)

- Managing client relationships was the *strategic need* identified by more than half of law firms as their most important priority over the next 12 months (55%) - the next closest was introducing non-lawyer management to their firms, by less than one in five respondents (18%).

Use of IT:

- More than six out of 10 respondents (61%) felt that a *greater use of IT* (especially, online legal documents and the accessibility that online communication brings for clients) would help their business.

Fixed fees:

- Over half of respondents (53%) expected greater client pressure on fee levels owing to a *general move away from the hourly rate* towards fixed fees.

Confidence in uncertain times

Pressure Points, a report by LexisNexis and Jures, examines the changing legal services market place.

The ongoing reform agenda under the Legal Services Act 2007, often likened to the City's 'Big Bang', the mass deregulation of financial services of 1986, began last October 2011 with the introduction of alternative business structures (ABSs).

At the time of going to press, there are 20 ABSs licensed by the Solicitors Regulation Authority (SRA).

More interesting than the number of ABSs are the striking range of models to have been approved, the enthusiasm of large consumer and private equity businesses to invest, and the willingness of a new generation of legal businesses to innovate in the delivery and pricing of services.

The Co-op, together with two high street practices, became the first SRA-licensed ABSs at the start of the year, making the retailer the first consumer brand into legal services.

The SRA has also cleared the takeover of Russell Jones & Walker by the Australian consumer law firm Slater & Gordon becoming the first foreign owned ABS. RJW chief exec Neil Kinsella has said that his firm had been preparing the ground for such reforms for over a decade, indicating real foresight in reshaping the market for consumer and business legal services.¹

Last month Irwin Mitchell became the largest top 100 firm to adopt the ABS model and also the first firm to be granted multiple licences by the SRA. A few days later Parabis Law became the first private equity-backed ABS.

Irwin Mitchell was reported to be 'gearing up to become the first British law firm to float on the Stock Exchange under new rules that will allow non-lawyers to own shares in legal practices', as *The Times* put it back in April 2010. Having announced its intention to go ABS in April 2011, six months ahead of the October start date, it announced that it had instructed Espirito Santo Investment Bank to identify opportunities for external investment. Now, with the regulatory process completed, law firms will have to react to this changed dynamic.²

In a recent Jures survey, over half of law firms (54%) described as either 'compelling' or 'very compelling' as a reason for ABS conversion accessing private equity (or other third-party investment) to finance their firm's growth.³ Whilst there have only been a few examples of external investment in law firms, despite the apparent enthusiasm of law firms, their scale also sounds a note of ambition.

Earlier in 2012 Duke Street confirmed an investment of up to £200m in personal injury umbrella firm Parabis Group (including claimant business Cogent Law and defendant firm Plexus Law). Duke Street bought a 'significant stake' in the group valuing the deal between £150m and £200m with the intention (in the words of Duke Street partner Iain Kennedy) of 'transforming the business from a professional services firm to a business process outsourcer, and to drive the continued consolidation of the legal services industry'.⁴

The private equity house Palamon Capital Partners also took a majority stake in QualitySolicitors (not an ABS) last October which funded its high profile £15m advertising campaign designed by Team Saatchi.

Innovation in service delivery and pricing follows investment as a feature of the new legal services landscape. The key message in the Co-op's move into legal services is expected to be a low-price, fixed fee tariff for family work. Fixed pricing in divorce is an innovation in an area of law where the hourly rate prevails. If priced correctly, the promise of price certainty will be well received by consumers. It will also be well timed as the Legal Aid and Sentencing and Prevention of Offenders Act 2012 will withdraw publicly funded legal advice from family law matters except for cases involving domestic violence in April 2013.

There is an interesting parallel between such innovation and the launch of Riverview Law in the world of commercial legal services. According to one commentator, Riverview is 'the first new entrant of the ABS era to enter the commercial market' (and 'the boldest-ever post-Legal Services Act move involving the Bar' according to another). The idea behind Riverview (also not an ABS) is to offer annual contracts – or fixed fees – for unlimited legal advice for every type of corporate client from SMEs to FTSE 100 companies. At the forefront of the Riverview proposition is the Bar. Out of a team of some 75 lawyers, there are 43 barristers including 12 QCs.

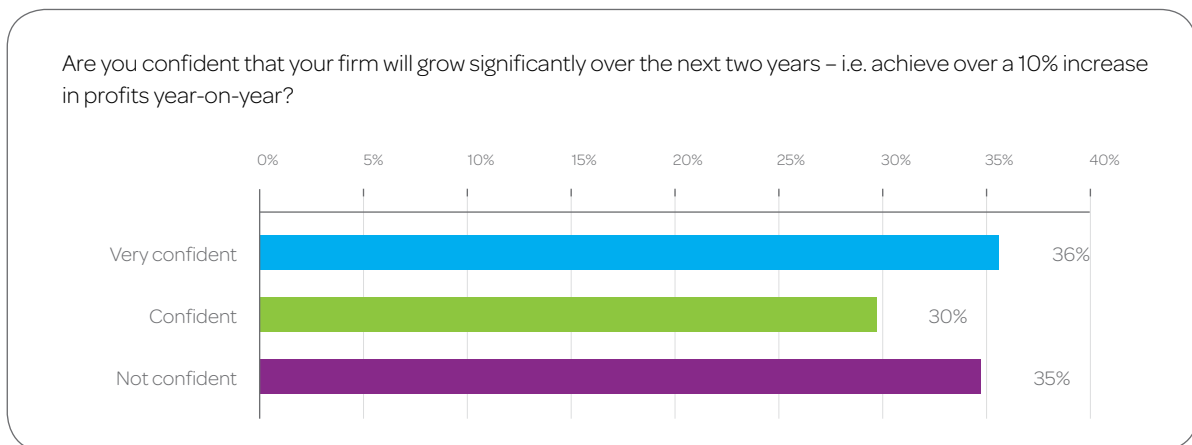
Riverview is backed by partners from the global law firm DLA Piper through holding company LawVest. As DLA's joint senior partner Sir Nigel Knowles has put it the relationship works both ways. 'It allows us to say to clients that we don't do this work anymore, we're not geared up for it. But rather than turn you away we can say we've taken a strategic stake in the business that does handle this work and we can introduce you to LawVest.'⁵

Another key concept behind Riverview (in addition to fixed pricing and direct access to barristers for specialist legal advice) is free unlimited access to its online legal and business libraries.

Such developments are set against an economy mired in the longest double dip recession since the Second World War.

This is a report that, drawing on newly commissioned research, seeks to identify those 'pressure points' for law firms in a changing legal services market, in looking at those critical issues around which will determine the success or failure of modern law firms.

With that in mind, the confidence of many respondent firms might surprise commentators.



¹ ABSolutely Fabulous: a study of alternative business structures and their role in a changing legal market

² Brave New Worlds: new thinking in legal services

³ ABSolutely Fabulous: a study of alternative business structures and their role in a changing legal market

⁴ Law Society Gazette, February 6, 2012

⁵ The Lawyer, February 20th

Competition is the biggest threat

Respondent firms were asked to identify and rate 'threats' to their businesses over the next five years in order of significance.

Score the following threats to your own business over the next five years in order of significance ('1' having least significance and '5' most significance):

- Increased law firm competition fuelled by mergers & acquisitions: 3.1
- New legal services entrants coming into the market under the ABS model: 4
- Greater retention of work in-house: 2.3
- Managing challenging economic and social conditions: 3.6
- Increases in legal process outsourcing to meet client demand: 2

Competition from new entrants coming into the legal services market as a result of the adoption of ABSs is seen as the most potent threat ('4' out of a possible ranking of '5') – a greater threat than that posed by the economy (3.6) or new law firm competition driven by mergers (3.1).

In a separate question, respondents were asked to identify from a list of five factors (business models; client expectations; economy; marketplace; and regulatory) the one factor that had the single greatest potential to challenge the success of your firm. More than four out of 10 respondents selected 'marketplace' (43%) - compared to only 23% who identified 'economy'.

Strategic needs

The strategy most commonly identified as the most effective in terms of increasing law firm profitability was to increase law firm gearing – in other words, the ratio of fee-earners who are not profit-sharing partners to profit-sharing partners.

Delegating work to associates and trainees was scored 4 out of a possible 5. There was a more ambivalent response in relation to the delegation of work to paralegals (2.6). After delegation, outsourcing was seen as the most effective strategy, especially to a fixed fee law firm subsidiary (3.5).

In terms of responding to increasing pressure on profitability, which of the following strategies do you think law firms would find more effective? (With '1' having least significance and '5' most significance):

- Delegating more work to associates and trainee solicitors: 4
- Delegating more work to paralegals under the supervision of an associate: 2.6
- Outsourcing work to an offshore legal process outsourcing company: 2.9
- Outsourcing work to an onshore UK-based outsourcer: 2.50
- Outsourcing work to a fixed-fee law firm subsidiary (as an ABS): 3.5

The majority of respondents rejected the notion that greater risks accompanied increased delegation (42%) with almost one in four respondents (24%) strongly disagreeing with the notion.

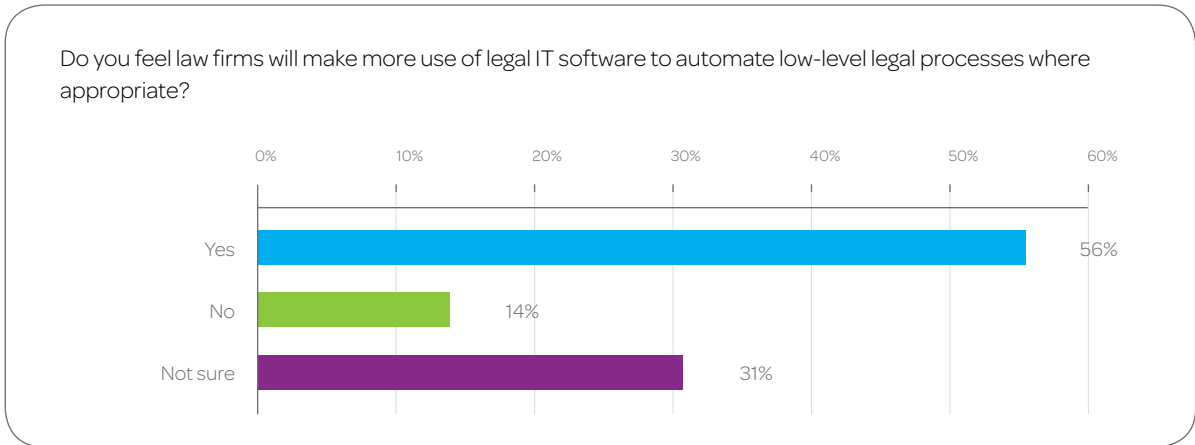
The management challenge deemed to be most significant over the next five years was the need to increase the number of lateral hires.

Score the following management challenges for your business over the next five years ('1' having least significance and '5' most significance):

- Retaining talent by developing alternatives to partnership for associates: 3.7
- Enhancing social mobility and diversity within law firms: 2
- Addressing fee-earner recruitment and retention issues: 3.3
- Modifying partnership structures to encourage greater performance by partners: 3.3
- Introducing better financial discipline over management of law firm finances: 3.5
- Increased lateral hires alongside greater emphasis on talent management: 4.1

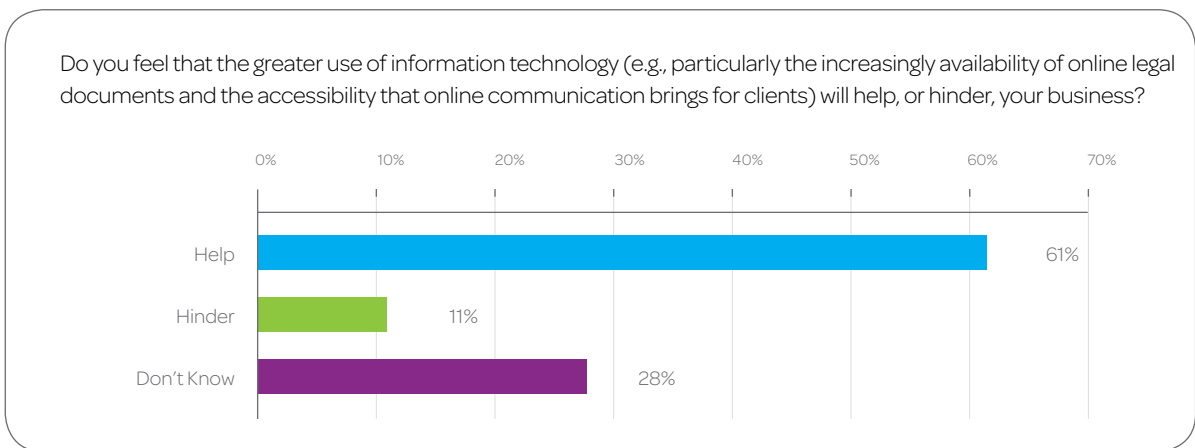
Use of IT

The prospect of increased automation and greater use of online legal documents in the legal services market – a feature of new market entrants and non-traditional providers of legal services such as banks and insurers - was seen by more than half of the respondents as inevitable.



More than four out of 10 respondents were satisfied that this carried no greater level of risk (42%) although the majority either thought that it did or were not sure (58%).

Respondents were also asked to choose from a list of 'indicators' of a changing legal services market which would have a critical impact on the way that their firm did business ('1' having least critical impact '5' most critical impact). Increased consumer demand for accessible legal advice scored the highest (4.1); followed by IT playing an increasingly significant role in delivering the services (3.4); increasing growth in legal process outsourcing solutions (3.2) and continued increase in the commoditisation of lower-level legal services (2.9).



Until recently there has been a reticence on the part of many lawyers to embrace IT and in particular online legal services.⁷ It seems that such nervousness has to a large extent been overcome. According to our survey, nearly two-thirds of respondents (61%) believe that online legal documents and the greater accessibility for clients offered by IT has a positive contribution to make.

⁷ 'The legal sector was and, to a large degree, still is, nervous about online and very reluctant to adopt it, mistakenly believing it will undermine the solicitor client relationship.' Brave New Worlds: new thinking in legal services, Jures 2012

Fixed fees

Respondents expect the move away from the hourly rate and towards fixed fee solutions – a striking feature of the new legal services landscape – to continue.

Do you expect further client pressure on fee levels as a result of an increasing move away from the hourly rate to fixed fee pricing structures to increase, stay the same, or decline?

- Increase: 54%
- Stay the same: 32%
- Don't know: 15%

To what extent do you agree with the following statements?

(with '1' indicating you disagree and '5' indicating you strongly agree)

- There will be increased demand for capped fees: 3.7
- There will be an increased appetite for fixed fee legal solutions: 3.9
- There will be a greater expectation of discounted rates for regular panel instructions: 3.4
- Clients will demand more added benefits such as secondments and CPD: 3.3
- Risk-sharing (through CFAs, contingency fees, and third-party funding) will become more popular: 3.3

'Pressure points': a study of the changing legal services landscape

Methodology: a survey of 101 mainly commercial law firms.

The survey was undertaken by legal research company Jures (www.jures.co.uk) working with online market research specialists Clarity Surveys (www.clarityuk.net). The report was commissioned by LexisNexis. For the purposes of the report, figures have been rounded up to the nearest decimal point - for full survey questions and results.

About LexisNexis

Over the past 200 years, we have combined a deep understanding of the legal profession with technology innovation to help practitioners work more productively, advise with confidence and better manage their organisations. Today, our services help lawyers apply legal intelligence to better meet your clients' needs.

About Jures

Jures is an independent research company dedicated to the legal services market.

The people behind Jures are the journalist Jon Robins and Gus Sellitto and Richard Elsen of Byfield Consultancy, the legal PR specialists (www.byfieldconsultancy.com).

About the author

Jon Robins is director of the legal research company Jures, freelance journalist and author. He has been writing about legal management issues for the national and specialist legal press for over 15 years. Jon runs www.thejusticegap.com. He is also a senior fellow in access to justice at the University of Lincoln. Thanks to Ben Rigby, legal journalist, for his help.

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