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WilkinsonRead & PARTNERS

Making Partnerships More Profitable

In This Issue

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13/03/2012 - Improved Cash Collection for Law Firms - London

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Our CPD accredited training can be a cost-effective way to ensure you achieve results throughout your firm that will impact on bottom and top lines. More information.

The Profitable Partnerships Programme

This law firm business development programme helps partners and key solicitors to measurably and sustainably improve business development performance and profitability. We deliver tracking of performance across a range of key indicators, from new clients and instructions to monthly billing rates. More information.

Blog

Get involved in the debate - read our posts on the issues and challenges confronting your industry, and provide your own opinions on our Blog.

Monday January 30, 2012

Successful Partnerships

Dear Associate,

This month we focus on law firm finance in 2012. Simon White considers the WIP imperative, Barry Wilkinson addresses cost reduction, and our guest contributor Chris Marston of Lloyds TSB Commercial discusses how to re-shape your firm - and how to pay for it.

We are always happy to receive guest contributions. If you have an article you would like to share with our readers, please contact anthony.wilkinson@wilkinsonread.co.uk.

As ever, any comments are gratefully received.

The WRP Team.

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The WIP Imperative

At the recent Association of Partnership Practitioners seminar entitled "Managing a Professional Services Firm in Distress" the main speaker was Dermot Power – best-known as the administrator of Halliwells.

Dermot made the key point that in a recession demand for most legal services will fall. Not a good start to the year. He also indicated that (prior to the new recession) his firm had recently conducted independent business reviews for law firms turning over £30m-£90m. So not all of the problems are at the smaller firm end of the market!

One of his key insights was that over the last 20 years WIP has played a major role in changing the funding structure of law firms.

Lending Against WIP

The banking crisis and recession that resulted exposed the

Cash Management for Law Firms – Ark Group Sector Report

Recognising our expertise in the area, Wilkinson Read & Partners have written a definitive sector report on Cash Management for Law Firms. The report, available here from publishers the Ark Group, addresses in detail the cash flow challenges facing legal firms of all sizes, and details specific strategies for improving cash management and achieving rapid yet sustainable results.

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questionable quality and recoverability of much WIP. It also exposed how little the lenders truly understood the asset against which they were lending. Naturally, this means that lenders are far less keen to lend against WIP.

The conventional view is that firms need to do two things – firstly, to be far more circumspect in their accounting for and valuation of WIP internally; and secondly to be far clearer in their communication with the bank of how and why the WIP justifies its valuation.

Regular readers will know that we very strongly believe in a third imperative, which is to pay far more attention to the cash flow and the realisation of the WIP. Put simply – turn it into cash as quickly as possible.

A Cultural Shift

As the research for our 2010 report Cash Management for Law Firms identified, to do this successfully requires a cultural shift. Fee earners need to be educated in the cash flow imperative and have appropriate cash flow standards (rather than targets), established for each work type and rigorously adhered to.

If we are heading into a recession then firms need to be extra vigilant in adhering to standards. If work is scarce there is a temptation to take on work on unclear or less stringent terms – which will only lead to increased WIP and worse cash flow, just at the time when positive cash flow is needed.

Fee earners must appreciate that WIP is essentially a wasting asset and performance measures must be far more clearly focused on bills collected, rather than bills raised or – even worse – chargeable hours created.

It 2012 is going to be a difficult year, financial disciplines will be crucial not only in work in progress management, but also in cost management. For advice on cash collection, please see our Ark Masterclass in March 2012.

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Cost Reduction in the New Legal Market

In December the Ark/Managing Partner Group held their annual financial and business planning conference, at which I presented on "Taking a Structural Approach to Managing Cost". By coincidence, a short Youtube video appeared this subject on another blog.

In this short video Professor Richard Susskind says that “the only trend that matters for 2012 is the more for less challenge,” in which lawyers will continue to try to find ways to deliver the highest quality service at the lowest possible cost.

Professor Susskind notes that the pressure on in-house legal teams is enormous and they will be asking law firms to consider new efficiencies in the coming year.

Crucially, they won’t be content with 10% savings, they will be looking for nearer 30-40% and that won’t be achieved simply through fixed fees and discounts for volume.

The points made by Professor Susskind happen to be very close to the content of my presentation, in which I highlighted the following main points.

Cutting Costs and Adding Value

• Cost-cutting in recent years has largely been about reducing capacity, which is about getting less from less. Cost management is about getting more from less – and this is what the client wants.

• Managing costs is not simply about reducing the level of cost, but getting a better result from your expenditure – adding value.

• There is an implicit assumption that this distinction is decided by job title – "fee earners" or "fee burners". This assumes that everything that fee earners do adds value and nothing done by non-fee earners can add value, which is clearly nonsensical.

• Professional service firms "buy and sell hours". Our analysis has shown that most medium-sized firms “buy” 3 hours for every hour they are able to sell. If the unsold hours bring in work, contribute to higher prices or satisfy regulators they are worthwhile. The task of management is to minimise "non-value adding" hours.

• This requires a review and analysis project by or on behalf of the Finance Department. Away from the largest firms, where many departments have fewer than five people, translating a 20% activity reduction into payroll cost reductions becomes very difficult – which may account for why many provincial firms have found it more difficult to reduce their cost base than the largest city firms.

• Many firms lack the internal resources and political influence to do the necessary research and get recommendations accepted. So for many firms it makes sense to outsource a greater proportion of activities to organisations with the requisite experience.

Changing the Balance of Presumption

The balance of presumption must change, and as Professor Susskind said in his closing remarks, "you can't achieve those savings by changing the pricing structure, and that means outsourcing and off shoring".

We will be running an Ark/Managing Partner Masterclass on this subject in May 2012.

Please email barry.wilkinson@wilkinsonread.co.uk

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Re-shaping your firm – and how to pay for it

Law firms have traditionally been seen as solid, reliable businesses – and this is often what customers value. However, I'm often struck by the lack of foundations from a financial perspective.

If the firm's balance sheet is conceived as a building, then the capital invested by the owners represents the foundations. In too many firms, the lack of incentives to retain profits means this capital is insufficient for the purpose. This restricts growth and encourages a lifestyle attitude to business – a disadvantage against new, well-funded competitors.

A strategy that everyone's signed up to

Many partnerships are characterised by competing priorities, preferences and prejudices, which often causes real stress for partners. The benefits of getting everyone, including non-partner solicitors and support staff, on the same bus can be remarkable. Effective performance management systems and provision for feedback can help embed a united culture.

Embracing IT

Good IT can help with:

• Financial management - high quality and timely MI

• Performance management, using a wide range of performance data – not just hours billed and recovery rates

• Online document preparation, reducing costs and outsourcing work to the client!

• Case management systems

• CRM systems, allowing a focused approach to active client relationship management

A Client-Centred Approach

Satisfied clients will use you again and recommend you to others. More enlightened firms will consider imaginative pricing structures and payment options, and get a deeper understanding of the client's needs.

However, firms must also accept that there's nothing wrong with selling, so long as the focus is on helping to solve the client's problems, and that everyone in the firm has a role to play in this sales process.

Take Advice

There are a few sources of quality advice worth exploring:

• Your accountants, particularly if they are members of the Institute of Chartered Accountants' Solicitors Group. As professionals, they understand your non-corporate view of the world, client confidentiality and professional standards. They can help you with financial management and, crucially, financial forecasting.

• Member groups – such as Lawnet and Connect2Law.

• The Law Society's Law Management Section. The LMS Annual Financial Benchmarking Survey is the most in-depth analysis of law firm performance in the market.

• Bank managers

• Non-executive directors

Financing the firm

The main sources of finance for a law firm include:

• Equity – the most expensive form of finance as it dilutes ownership. It also takes away independence, but can facilitate much faster growth and bring a more corporate approach.

• Debt – cheaper, although there are interest and administrative costs. Debt must be repaid, although firms retain independence, and borrowing has never been cheaper.

• Owner capital – cheaper still, but there is an opportunity cost for the owners.

• Clients – no, not the client account! But managing lock-up effectively by improving billing, credit control and the disbursements will free up money for development and growth.

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