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WilkinsonRead & PARTNERS

Making Partnerships More Profitable

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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.

Tuesday March 26, 2013

Successful Partnerships

Dear Associate,

This month Barry Wilkinson addresses the tightening of the 'gastric band' affecting mid-market firms, and introduces quantity as the key element of the profit equation - in the face of financial warning signs from the SRA.

As ever, any comments or shares are gratefully received.

The WRP Team.

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Tightening the Gastric Band

Two years ago, while researching our white paper, we coined the phrase ‘the gastric band’ in reference to the three forces - deregulation, technology, and globalisation and low-cost competition – squeezing the middle market.

This was based on observing other markets, and on feedback from those working in and around the profession. We also echoed Bill Gates’ warning of overestimating change in 2 years, and underestimating it over 10 years.

A related key point made in a recent piece by Adam Smith Esq was that, despite apparent business as usual, ‘fee pressure, low cost providers, reduced leverage, and lateral hiring are moving in swift undercurrents.’

The North-Western ‘Cull’

According to a recent survey, almost 1 in 5 managing partners of North-West PI firms are considering closing their practice, partly as a response to the referral fee ban.

What we see emerging is effectively a ‘triage’ of firms. Firstly, there are definite ‘winners’. These will be the minority. Another minority of firms is the ‘no-hopers’ –

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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poorly run and with little chance of survival. Hopefully no-one reading this will fall into that category!

However, the vast majority of firms have the potential to survive and prosper, if they do the right things.

Attributes of Winners

By pure coincidence, I have been delivering a seminar this month in Liverpool on the attributes of winners. We address 20 distinct issues under five categories:

• Finance;
• Clients & Markets;
• People;
• Products & Services; and
• Management.

We ask delegates to score themselves on a 1-5 scale for each attribute, giving a total score out of 100. We also focus particularly on areas of particular weakness – attributes where they have scored themselves less than 3 out of 5.

Most delegates are in fact stronger than they think, and by clearly identifying both strengths and weaknesses, partners can focus their attention on the things that could threaten their independence.

The Co-operative Model

But a word of warning – Andrew Otterburn (a colleague on the Law Management Section Committee) took part, pretending to answer on behalf of the Co-op. They came out with 90 out of 100. Clearly, the competition is strong and things won't get any easier for incumbent firms.

However, those management teams who take the challenge seriously and focus on areas of commercial threat and opportunity will have a good chance of consolidating their own position in the market. An attitude of realism combined with belief will serve firms well.

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Mind your P's and Q's

The SRA recently announced three key financial 'warning signs' it will use to assess firms' financial stability over the next year, indicating who will face the threat of regulatory action – and even insolvency.

The indicators are: drawings exceeding profits; borrowing exceeding net assets; and borrowing over a certain level. Firms showing two or three of these will be given a red rating, and 'Red-rated firms are... in serious financial difficulties, with the potential to collapse. Such firms will be required to prepare detailed contingency plans and obtain professional insolvency advice.'

It's all about P's and Q's

A major focus for firms should, then, be on managing costs to reduce the borrowing requirement. This is all about P's and Q's – price and quantity. A basic tenet of economic theory is that Revenue = Price x Quantity. We use a very similar equation as a basis for cost reduction:

Cost = Price x Quantity

Experience has shown that there is much more scope to reduce costs by focusing on volume rather than price. When we look at profit, the equation becomes:

Profit = (Revenue – Cost) * Quantity

That is to say, the amount of profit the firm makes is inextricably linked to quantity. Nowhere is this more clearly the case than in Personal Injury (see above). Around a quarter of North-West firms surveyed felt that profitability will fall by 50%, with 1 in 10 believing it will drop by as much as 80%.

Profitable Portal?

Whether portal work will become inherently unprofitable depends on your perspective – some believe that doing portal work profitably (at a fixed fee of £500) is not possible.

However, with a properly functioning IT system, the time taken by a fee earner to process a straightforward portal case can be less than 3 hours. The work does not need a qualified lawyer, rather a trained paralegal – in which case the income will amount to over £150 per hour - and the staff cost to less than a tenth of that. So the gross profit margin should be 90%.

The price in such cases is not the problem. Once again, it is quantity that matters.

To generate quantity requires paying much more attention to marketing and selling. Referral fees may be banned, but outsourced marketing programmes will take their place.

This is why perspective matters. For outsiders, a market with an established demand, a potential gross margin of 90% and a lack of true innovation from the incumbent suppliers, will see a major opportunity. This is why the "reverse take-over" by claims managers of established PI firms, or setting up their own legal process businesses (as ABS), makes sense.

Open markets are unforgiving, and it is possible that those in the North-West who prophesy the end of their practices will be proved right.

This may of course prove to be overly pessimistic, but what is absolutely clear is that the quantity component of the cost and income equation is crucial.

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LSN Finance Briefing

The issue of financial management in law firms has never been more important, and a recent publication by the Legal Support Network underlines some of the most pressing issues for managers.

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