

The Law

Armstrong Watson's specialist publication for the legal profession

Spring 2013

Business Protection for Legal Firms

Has your firm got the right level of protection in place?

Land Remediation Relief

How much do you know about this often forgotten tax relief?

The Solicitors Professional Indemnity Insurance Market

We take a detailed look at this insurance and how upcoming changes in the market may affect firms.

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Welcome to the Spring 2013 edition of The LAW, the specialist publication for the legal profession from the legal sector team at Armstrong Watson.

Specialists are available from all of our 14 offices to provide pro-active support and advice to lawyers

in compliance and business improvement matters. This publication is designed to allow us to share our collective experience in acting for lawyers throughout the UK.

If you would like any further information on the issues raised within The LAW, or if you would like to work with us, please contact me :
Call 07828 857830 or email me at andy.poole@armstrongwatson.co.uk

I also keep our law firm clients up to date with more immediate developments in the legal profession via Twitter. If you would like to follow me, I'm @AW_AndyPoole

One recent development is that the Law Society has released an updated guide to insurer insolvency; information for solicitors with Lemma policies: and a PII practice note. If you would like any further information on that, or anything else referred to in this publication, please contact me.

Andy Poole

Andy Poole
Legal Sector Director

In this edition:



Business Protection for Legal Firms

Andy Kilby, Managing Director of Armstrong Watson Financial Planning, discusses how essential the right level of cover is for legal firms.

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Land Remediation Relief- the forgotten tax relief

David Robinson, Tax Consultant talks us through the potential benefits of this often forgotten and under-utilised tax relief.

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The Solicitors Professional Indemnity Insurance Market

Andy Poole, Legal Sector Director, reviews the current market conditions.

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ABS Applications

Andy Poole, Legal Sector Director, delivers an update on the work Armstrong Watson are doing with SIFA to deliver support for those considering becoming an ABS.

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How We Help Law Firms

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Business Protection for Legal Firms

Andy Kilby, Managing Director of Armstrong Watson Financial Planning



Like businesses in other sectors, it was inevitable that the legal sector would be impacted by the global economic downturn and law firms have had to look closely at their profitability and perhaps realign their costs. Whilst it is encouraging to see an improving trend, with profits once again increasing for many firms, this does not always translate in to improved cash flow for the business. Currently, many Partners do not draw their full profit share, perhaps for cash flow reasons, or indeed, to finance investment within the business, and consequently the level of Partners' capital accounts within many legal firms is increasing.

This increasing Partner capital share within a firm will present a financial challenge when a Partner retires, but there is normally time to create a succession plan to ensure the firm is protected against the loss of an individual Partner at retirement; in terms of both their day-to-day contribution to the firm and the repayment of their capital account. A frequently overlooked and perhaps more significant challenge or risk to the business is the unplanned exit of a Partner through death or long term ill health. Not only will the firm's finances be affected by the sudden loss of a Partner, there will also be an unplanned significant cash requirement to facilitate the repayment of the Partner's capital.

Most firms have a Partnership Agreement in place and the first step to managing this risk is to ensure that the death or ill health of a Partner is robustly

covered within the agreement, however, this does not really address the associated financial risks to the firm. At a time when the business is likely to suffer the combined impact of lost key skills and the need for client relationships to be reallocated, there is also the question of how cash is raised to repay the capital account of the Partner concerned. It is surprising how often this part of the planning isn't considered. The easiest way to protect the firm financially is to ensure that in the event of the death or serious ill health of a Partner, a cash lump sum is made available to the remaining Partners, of sufficient value to repay the capital of the Partner concerned.

This can be achieved by arranging suitable life cover, or to ensure greater protection, combined life and critical illness cover. The cost of life cover has reduced in recent years and, in general, life assurance premiums are very modest for the capital sum potentially payable. Including critical illness cover (where a capital sum is payable on diagnosis of a qualifying medical condition) does increase the cost of cover, but should still potentially be considered given the significant financial protection it can offer and the fact that a claim as a result of serious illness is more likely than one for death.

If a law firm chooses to adopt a corporate structure instead of partnership, similar principles apply and a suitable Shareholder Agreement should be in place supported by life, and perhaps, critical illness protection to cover the value of individual shareholdings.

It is vitally important to ensure that any protection arrangements are structured correctly - both tax efficiently and cost effectively. Armstrong Watson's Financial Planning Consultants work in conjunction with our Legal Sector Specialists to ensure we are able to provide proactive bespoke advice and solutions to help you protect both profit and capital, and indeed, the future prosperity of your business. **Contact us to find out how we can help.**



Land Remediation Relief – the forgotten tax relief

David Robinson, Corporate Tax Consultant

Since 2001 companies have been able to claim tax relief on the remediation of contaminated land or buildings on 150% of qualifying expenditure.

'The relief has received comparatively little press coverage and as a result there have probably been many missed opportunities.'

In fact it was one of the tax reliefs that were going to be abolished as part of the Office of Tax Simplification's (OTS) Tax Reliefs Review in 2011. Approximately 1,300 companies a year utilise the relief, so it was pleasing to hear that it was reprieved. Respondents argued that removing the relief would affect the regeneration of uneconomic brown field sites when The Treasury issued its response to the OTS' Review in December 2011. We can therefore now use the relief with confidence that it has a future.

Land Remediation Relief (LRR) is a relief from corporation tax only. It provides a deduction of 150% from taxable profits, for qualifying expenditure incurred by companies in cleaning up land acquired from a third party in a contaminated state. The company is required to have a major interest in the land to qualify for LRR, which is defined as 'freehold' or having a 'lease of at least seven years'. The land has to be in the UK.

'For example if a company spent £10,000 on expenditure qualifying for LRR, it would get a deduction of £15,000 against its taxable profits.'

Therefore, if you are advising individuals or partnerships (LLPs or traditional) that are purchasing land or buildings where there has been significant contamination, it would be well worth asking them to seek specialist tax advice to ensure that opportunities to utilise LRR are not missed.

'Land or buildings are in a 'contaminated state' if there is contamination present as a result of industrial activity such that it is causing or could cause relevant harm to the health of animals or humans, or significant damage to buildings or pollution to groundwater and rivers etc.'

A typical example of this is asbestos removal.

LRR is also available for the removal of contamination arising from arsenic, radon and Japanese knotweed. These are the only exceptions to the requirement that the contamination must have resulted from industrial activity. Nuclear sites don't qualify.

Qualifying expenditure includes the cost of establishing the level of contamination, removing the contamination or containing it so that the possibility of relevant harm is removed. There is, however no relief if the remediation work is not carried out.

'A fundamental principle of the relief is that the polluter or any party connected to the polluter cannot have the relief.'

Nor can a Landlord claim Land Remediation Relief for cleaning up contamination caused by one of their tenants.

The costs of Landfill Tax are excluded from qualifying for LRR, although the costs of removal of contaminants to a landfill site are eligible for the relief.

Derelict Land Reinstatement

In 2009 LRR was extended to those companies bringing land that has been derelict since 1st April 1998 back into use, provided it was derelict when it was acquired by the claimant.

'The land doesn't have to be "contaminated" in the traditional sense of the relief.'

Rather it may have been derelict because it contains materials which have previously been uneconomic to remove. This new relief recognises this and will be available for qualifying costs on the removal of the following:

- post-tensioned concrete heavyweight construction;
- foundations of buildings or machinery bases;
- reinforced concrete pilecaps;
- reinforced concrete basements;
- underground pipes or other apparatus for the supply of utilities or for drainage or sewerage.

LRR Tax Credits

If claiming LRR (including Derelict Land Reinstatement) creates or increases a loss, this can be surrendered to HMRC for a payment equal to 16% of the qualifying loss.

'This is equivalent to a 24% tax credit on the actual expenditure before the 150% uplift.'

If you'd like to speak to our tax team about any of the issues covered in this article, we'd be happy to arrange a personal meeting. Please contact your local Armstrong Watson office on 0808 144 5575 or email help@armstrongwatson.co.uk.



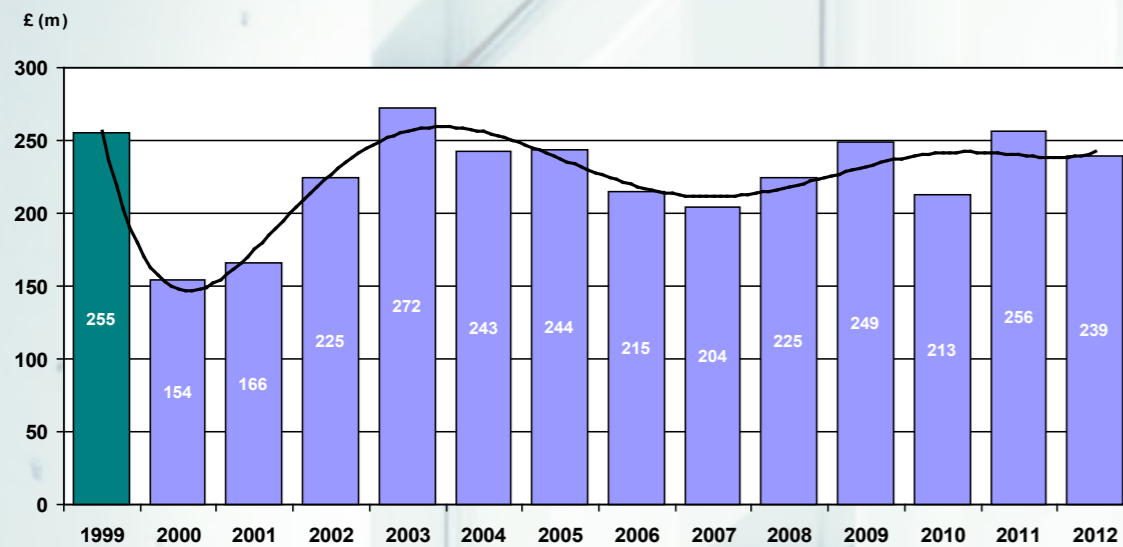
The Solicitors Professional Indemnity Insurance Market

Andy Poole, Legal Sector Director

Proposed changes to the Assigned Risks Pool (ARP) and scrapping the single renewal date are expected to bring significant changes to the solicitors' professional indemnity insurance (PII) market, which could result in alterations to premiums for many firms.

'Such changes, in general, did not take place for many firms with the 2012 renewal, but that may be due to the introduction to the market of a number of new insurers.'

At times of change like this, it is often worth looking back at the results of previous modifications to the market. The following graph tracks the qualifying insurer total premiums each year since the last year of the mutual Solicitors Indemnity Fund (SIF) in 1999.



It is clear to see that despite inflation in the intervening period, premiums in 2012 were still some £16m lower in absolute terms than the last year of the SIF.

Jake Fox, Leeds-based Director at specialist professionals PII broker Prime, notes that

"It is worth reminding ourselves that in 1999, the SIF provided just £1m of cover for around 9,000 firms. Open market insurers now provide higher minimum levels of cover for over 11,000 firms".

The reduction in total premiums from 2011 to 2012 will have been welcomed by many, although there are of course exceptions to that. In my experience, the premiums for most firms were not too dissimilar to 2011.

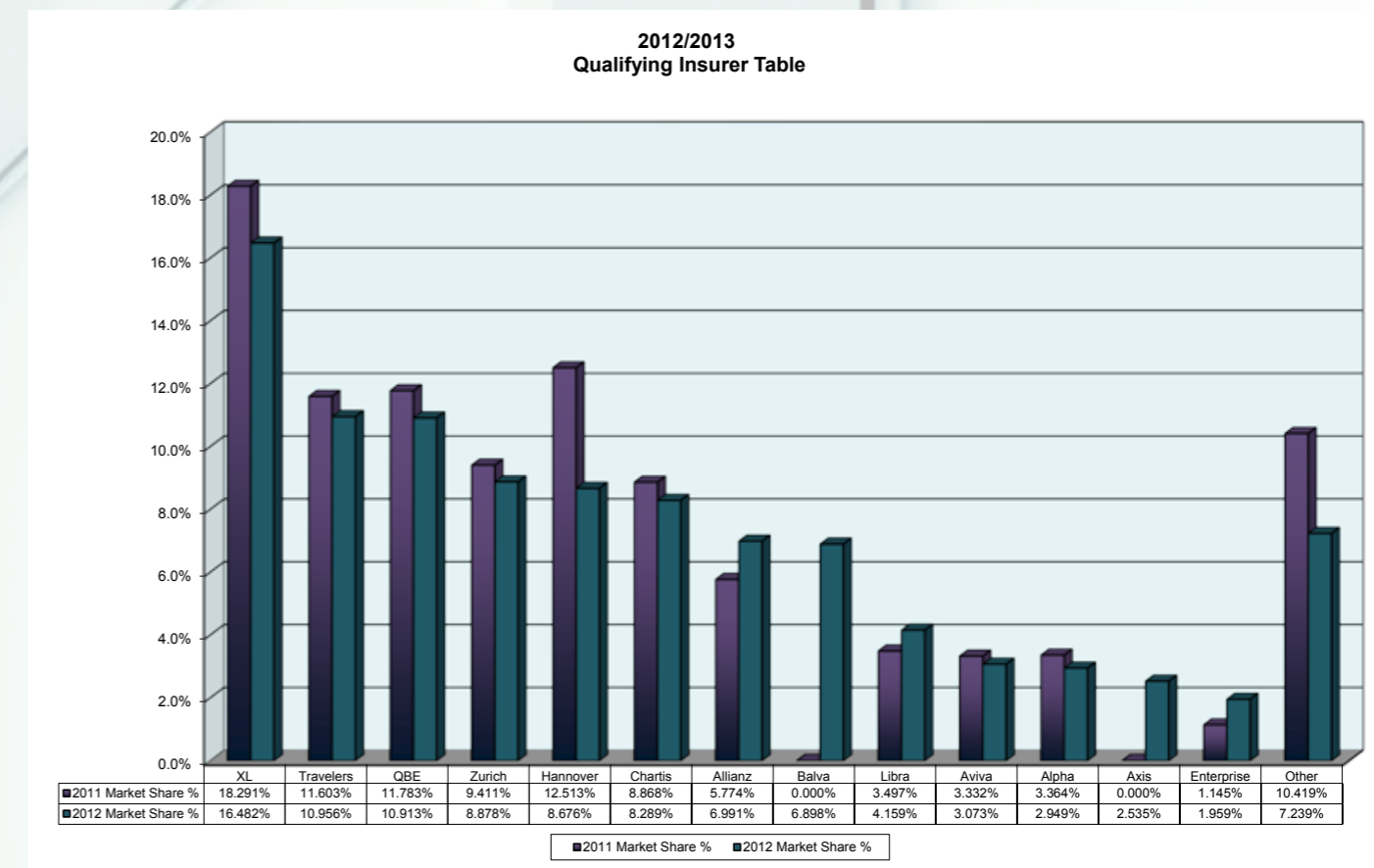
It could be argued that the reason for the overall reduction in premiums was due to additional competition brought about by new insurers entering the market in 2011 and 2012. Jake Fox has a view on this, "There is considerable debate surrounding the experience of some of these insurers in the PII sector and more importantly their financial rating.

It is understandable that firms are wary of being insured by these new market players, however as many solicitors have seen a fall in revenue, a number of firms have decided to run the risk in order to achieve a reduction in their PII premium".

Although insurers are required to be Qualifying Insurers, that status is achieved by agreeing to issue cover on Minimum Terms, and currently making a commitment to share their proportion of the ARP. The SRA do not verify an insurer's financial status. Fox continues,

"Lemma Europe was an unrated Qualifying Insurer that went into liquidation in September 2012. The risk with unrated insurers is that they will not be there when you need them. Should an insurer become insolvent, the additional cost of replacing cover on already fragile firms could be the straw that breaks the camel's back."

The more established insurers continue to hold their strong market position, as highlighted by the graph below.



In general, the more established insurers have been highly selective and have tried to maintain a consistent approach to underwriting.

'The graph highlights one major change in market share from 2011 to 2012, that of Hannover. Hannover entered the market in 2009 and reduced their share by 35% at the 2012 renewal. Perhaps this is a deliberate attempt to reduce their exposure.'

Jake Fox comments on other developments in the last renewal, "One or two insurers were unwilling to consider new business and the continuing theme is that insurers want to retain existing insureds while reducing their exposure to conveyancing and other property related risk. The 2012 renewal also saw a large number of early renewal offers being made, the benefits of which should be considered on an individual basis."

'Fox is convinced that the answers to questions asked about risk management were a key factor in the premiums obtained, and it will be interesting to see how the insurers react to the introduction of Outcomes Focused Regulation.'

Looking forward, next year will see the introduction of the Extended Policy Period to replace the ARP. It remains to be seen how that will impact on premiums, although with the wider economy continuing to struggle, it is difficult to see significant reductions.

The Law Society has released an updated guide to insurer insolvency; information for solicitors with Lemma policies; and a PII practice note.

Please contact us if you would like any assistance with either your PII renewal, or with implementing effective risk management processes and controls.



ABS Applications

Andy Poole, Legal Sector Director

Armstrong Watson has teamed up with SIFA to deliver seamless advice, support and management of ABS applications and

business planning services. Together we are perfectly placed to evaluate your options; advise on the process; prepare the necessary forecasts and business plans; prepare the compliance plans and risk registers; and manage interaction with the SRA.

Whether you are looking to introduce a non-lawyer owner; transfer ownership to spouse(s) as part of a tax efficiency review; or reviewing your options post LASPO, ABS may work for you.

If you are considering whether becoming an Alternative Business Structure would be beneficial for you, please contact me for a free initial no obligation meeting.

Armstrong Watson Legal Sector Surveys

We will shortly release the first in a series of surveys on trends and current practice in the legal sector.

The surveys will provide a health check on best practice and how the market is likely to change.

This in-turn will allow law firms to strategically plan for the future. All contributors will receive a full analysis of the results by size of practice.

The first survey will be on The Legal Services Act. Future planned surveys include trading structures; profit sharing bases; and methods of charging clients.

Keep an eye out for the first survey landing in your inbox.

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