



Legal Sector Breakfast Briefing

Thursday 28 January 2016

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Accountants, Business & Financial Advisers
A track record of providing solutions to the legal profession





Legal Sector Breakfast Briefing

Welcome

Simon Campbell

Relationship Manager – Commercial, Clydesdale Bank

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Legal Sector Breakfast Briefing

Introduction

Andy Poole

Legal Sector Partner, Armstrong Watson

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The Law Society





Thursday 28 January 2016

- 8.00am - Arrival and breakfast
- 8.30am - Welcome
- 8.35am - Briefing – Understanding the risk, value and opportunity in WIP
- 9.30am - Q & A
- 10.00am - Close





Understanding the Risk, Value & Opportunity in WIP

Zoe Holland, Founder & Managing Director

Zebra
LC[®]

RISK | VALUE | OPPORTUNITY



You can stop, if you want, with the
Z, and most people stop with the
Z,
but not me.

*“On Beyond Zebra” Dr.
Seuss*

Through The Looking Glass



Visibility – Comfort & Confidence



- Why do banks, funders & investors want to know more?
- WIP & risk DD and its role
- Positive - under the skin of the business
- Profiling - adding value

VALUE | RISK | OPPORTUNITY



- Role as DD Auditors
- M&A; Bank Funding;
- Private Equity; New Entrant ABS; ATE
- Projects - £WIP books at £250k to a discreet project on a £100 million turnover firm with external investment
- Challenges – visibility is in demand



Example DD Scope

- Risk status and benchmarking of WIP
- A forced sale valuation of WIP assuming recovery rates of 20% & 30% based on sample RAG review
- Case management capability, technical capability, oversight and compliance
- Identify any hidden and unaccounted costs such as medical reports
- Identify within the sample and trends where interested parties have a call over cost recovery
- Assess WIP levels post and pre April 2013 as part of the sample audit to report upon consistency in quality, valuation and recovery
- Assess whether the Firm's PII cover is suitable for work undertaken

Troubled Waters



Technical Auditing & Review



- Value & Risk
- Cash Flow
- Profitability
- Indemnity Risk
- Brand Protection

Technical Auditing & Review



- Lifeblood – quality of commodity and how is it managed (operationally & financially)?
- Specialist auditors, lawyers, costs, financial & barristers
- Sample auditing against key criteria for value & risk
- Fairpoint Group PLC & North Edge Capital
- Bank funding (NatWest, HSBC & Yorkshire Bank)

WIP Profiling



- Risk Rated
- RAG Rating
- Black Listed = Nil Value
- PLC Board Approved Methodology
- Costs & Retainer Issues
- Litigation/Completion Risk Profile
- Technical & Operational Capability



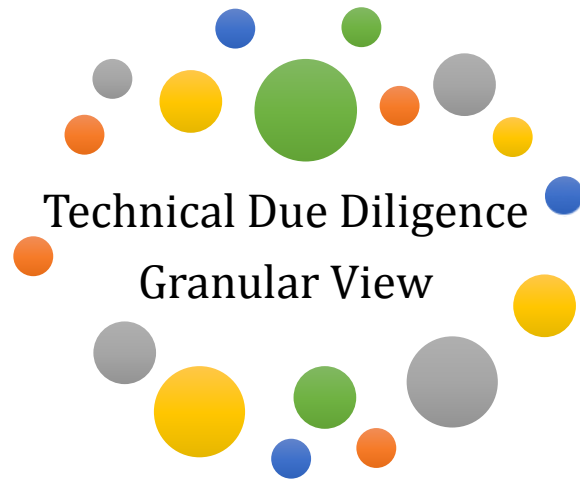
New Entrant Investors



- Weekly/monthly WIP valuation
- Risk profiling of key areas of legal service
- Governance & indemnity risk
- Visibility around technical & operational capability & performance



Granular Visibility



FIELD AUDIT

REPORT



Retainers & Funding Risk

- Retainer problems
- Hourly rates & fee earner Grade 'gearing'
- Reasonableness time recorded
- Litigation: Part 36 risk
- Proportionality & complexity scaling



Litigation Risk Factors

- Poor quality commodity
- Profile of admitted; denied and no decisions
- CN, NIHL & Serious fraud
- Risk of negligence: out of depth
- Mitchell & Denton issues: undermining WIP
- Indemnity & OFR risk

Trends – Undermining WIP



- Defective Retainers (not all remediable retrospectively)
- Concurrent Retainers - LSC & CFA funding
- Confusing/insufficient explanation of the new 25% success fee
- Costs letter estimates not reflecting the work & level of fees being charged on a case



Trends – Undermining WIP & Risk

- Poor technical skill : not maximising profit costs
- Risk of under settlements: serious injury & more complex injuries such as PTSD and chronic pain
- Optimism bias: Non Tefal WIP that just keep sticking (private client and litigation)
- Commercial property : specialist areas without a specialist eye

BRAG Rating



Firm WIP	Retainer	Risk
£88,198.00	Black	Green
£31,970.00	Black	Red
£61,551.00		Green
£6,561.00		Green
£41,860.00		Black
£19,550.00		Green
£17,890.00		Green
£100,500.00		Green
£94,150.00		Red
£25,085.00		Black
£141,335.00		Green
£1,107.00	Black	Orange
£44,175.00		Orange
£29,005.00		Orange
£102,700.00		Green
£49,980.00		Red
£6,075.00		Red
£4,010.00	Black	Orange
£18,955.00		Green
£37,450.00		Green
£2,880.00	Black	Orange
£1,877.00	Black	Red
£9,100.00		Green
£12,420.00	Black	Red
£4,010.00		Orange
£1,676.00		Red
£2,445.00	Black	Red
£34,785.00		Orange
£16,637.00		Green
£9,615.00		Green
£29,245.00	Black	Red

£160k black listed:
nil rated on value

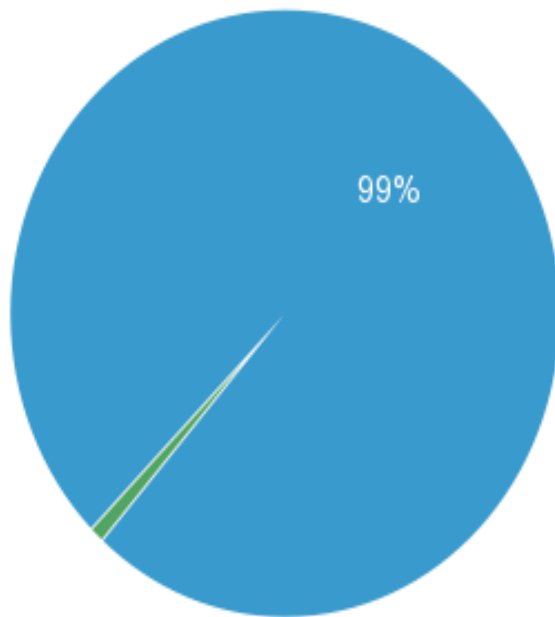
YEAR OF THE BRAG

WIP Profiling - Retainers

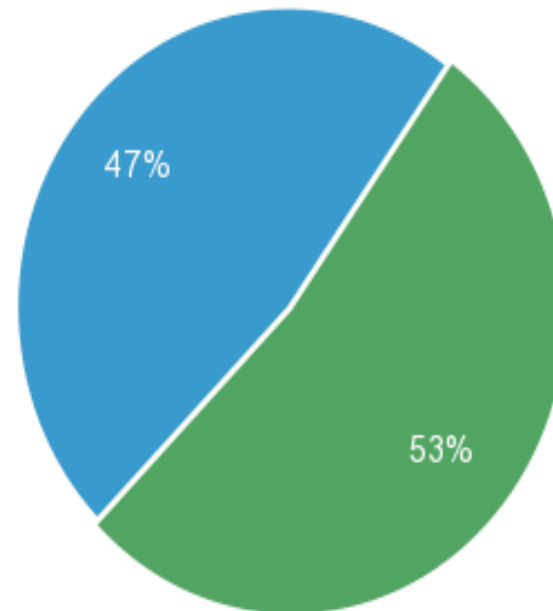


Audit Question : Any Issues with Retainer?

AUDIT 1



AUDIT 2



What's Under The Bonnet





DATA

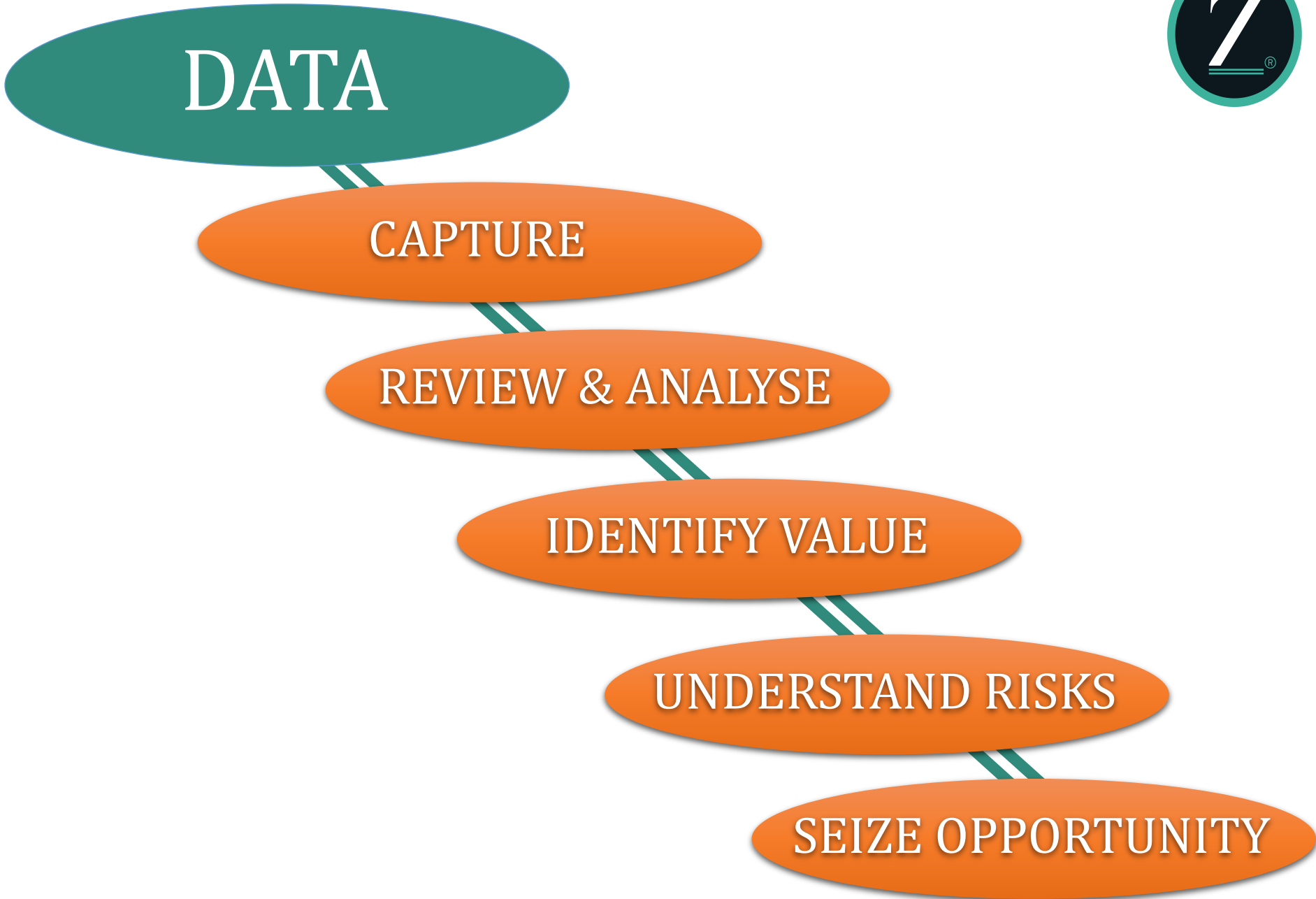
CAPTURE

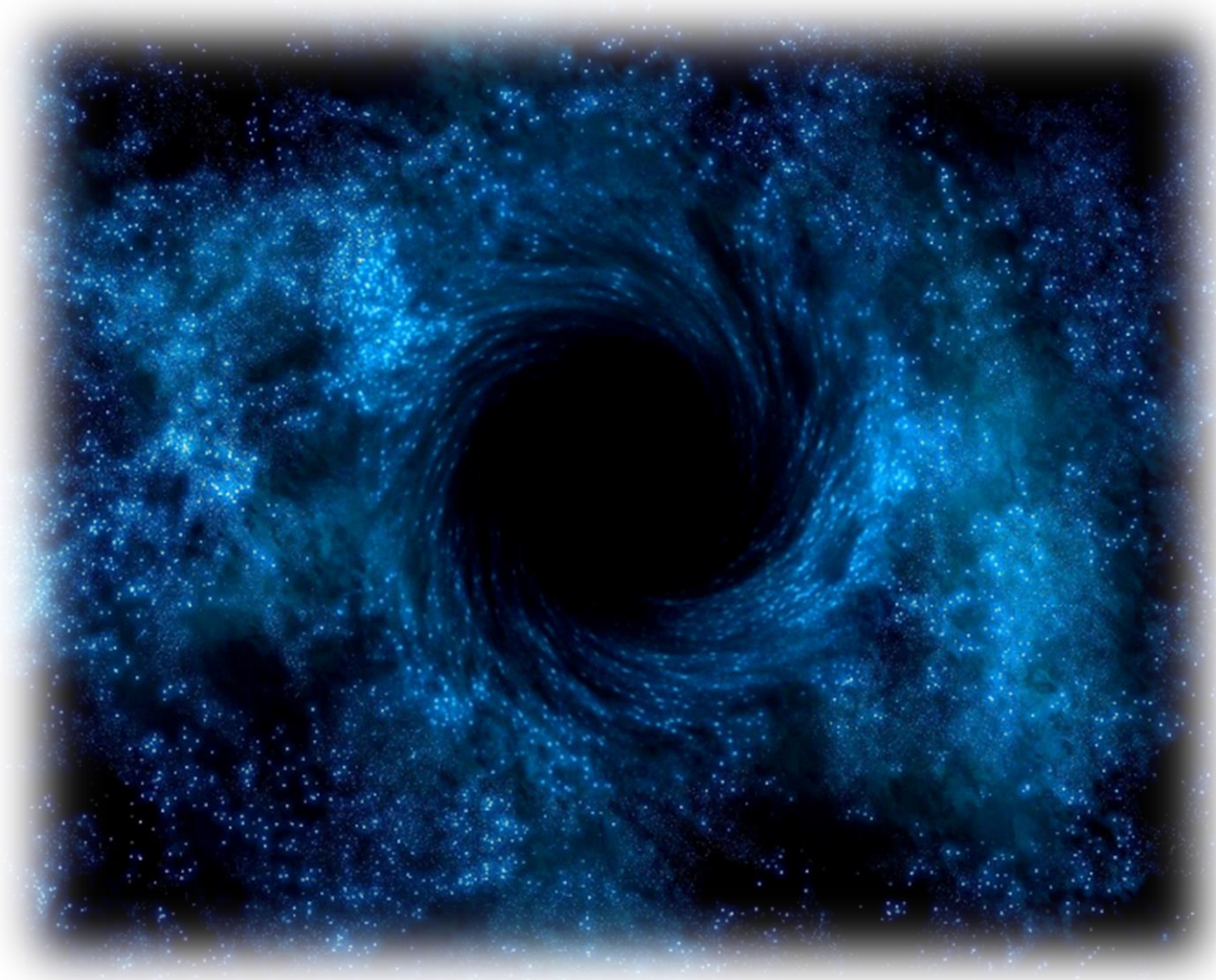
REVIEW & ANALYSE

IDENTIFY VALUE

UNDERSTAND RISKS

SEIZE OPPORTUNITY





How Well Do You Know Your Commodity?





How Good Is The MI? (Litigation)

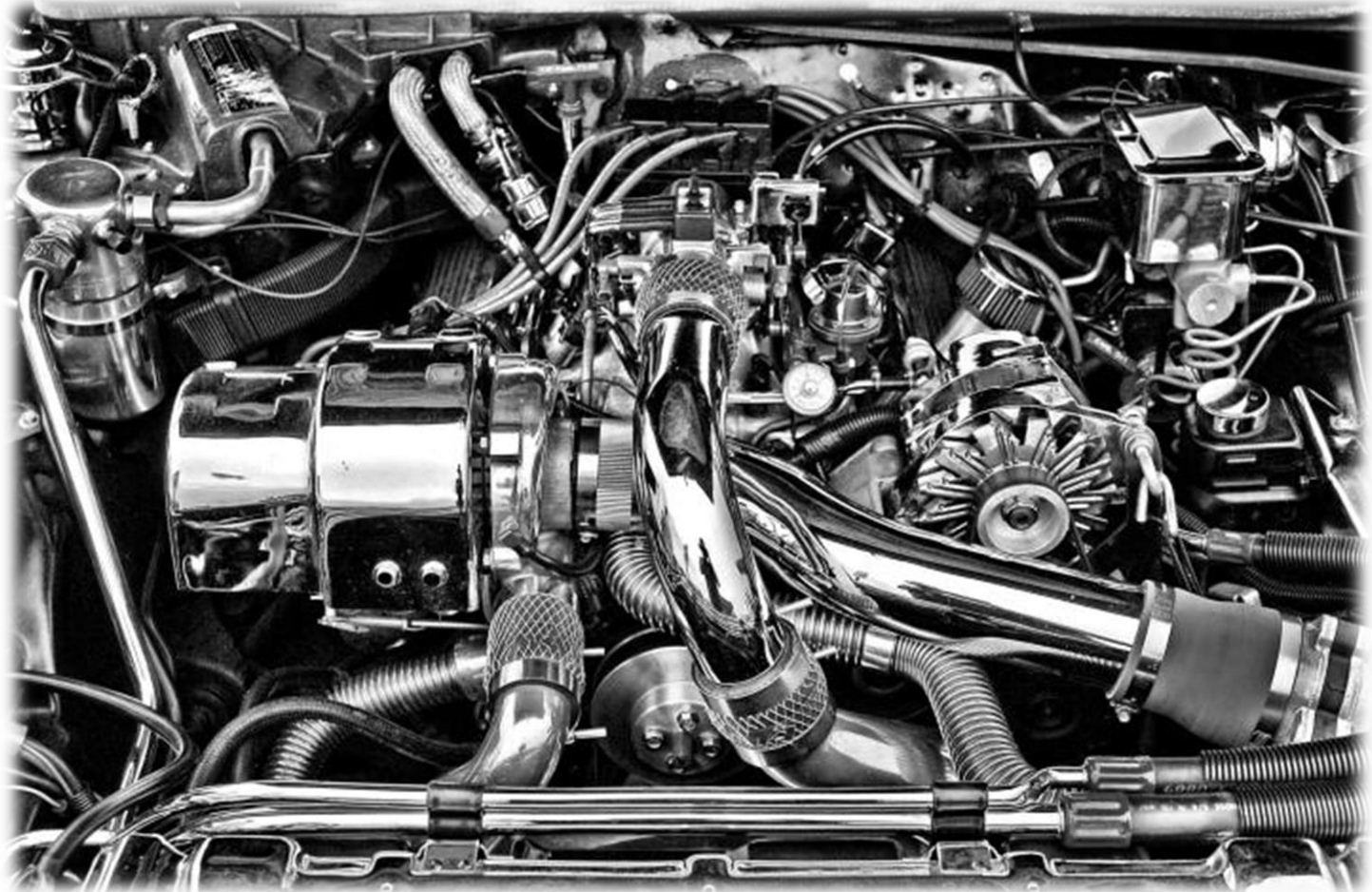
- Case type
- Breach & Causation status (CN)
- Full or Partial Admission
- Case stage reached
- Proceedings Issued? Served?
- Directions
- Quantum
- Complexity Scaling

How Good Is The MI?



- Case progression
- “Sleepers”
- Aged WIP – what does it indicate?
- Toxic WIP
- Indemnity risk files
- Costs recovery statistics
- Disbursements

What's Under The Bonnet?



What We See



VALUE | RISK | OPPORTUNITY



- £2.1 million audited WIP- 20% (WIP profile £10m)
- PI & CN
- Valuation & risk profiling
- 12 month fee generation forecast



Findings

- Different risk profiles
- Clear differential between risk factors on Retainers & funding
- Technical competency & skill
- 'Gearing' of the caseload
- Senior commercial & technical skill lacking

Findings (Cont'd)



- Retainers required immediate remedy
- BTE & LAA required urgent extensions
- Protection of WIP value
- Hourly rates too high: undermined WIP value
- Client care issues (OFR)
- Professional indemnity risk

Risk RAG Valuation



- £200,000 black listed (thus 10% of sample nil value)
- Indemnity risk (pre & post April CFAs)
- Lost opportunity of pre April Success Fee
- CN: high risk profile
- PI: medium risk
- Overall RAG value below 50%

What We See





Multi-Service Law Firm (New to Bank)

- PI
- CN
- Crime
- Property
- Private Client

Project Scope



Key credit issues for the bank:

- 1 Over trading - failure to convert WIP into cash receipts - especially in the areas of injury litigation
- 2 Quality of systems for monitoring and control of WIP
- 3 Split of WIP between disciplines
- 4 Can cash collection processes be improved to aid cash-flow ?
- 5 Current Valuation of WIP - is it on a conservative basis when looking at market norms?



Shift From Legal Aid

- How far implemented?
- Assessment of WIP write off in non contentious areas
- Indemnity risk profile in property
- Crime - profitability and approach to changes
- Assessment of own WIP value
- Comfort tangible shift away from Legal Aid
- WIP write off in non contentious areas – required improvement
- Indemnity risk profile in property – good (growing area)
- Crime - profitability and approach to changes (good)
- Assessment of own WIP value (reasonable)



Result

- Benchmarked within top Zebra centile
- Low risk WIP
- Low risk professional indemnity
- Did what it said on the tin!
- Bank had comfort



Lessons

- Quality & expertise
- Technology (IT systems)
- Low operational risk
- Financial management
- Healthy asset base (profitable & valuable WIP)
- Clear strategy
- Audit & review of data



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Questions and Conclusion

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