

# Legal Sector Breakfast Briefing

Tuesday 11 November 2014

This briefing qualifies for 1 hour CPD – Authorisation Ref: EKQ/ARWA

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Tuesday 11 November 2014

## Welcome

Simon Lenney  
Yorkshire Bank

 Yorkshire Bank

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## Introduction

Andy Poole  
Legal Sector Partner  
Armstrong Watson

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# Legal Sector Breakfast Briefing

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- |         |  |
|---------|--|
| 8.00am  | - Arrival and breakfast                |
| 8.30am  | - Welcome                              |
| 8.35am  | - Briefing – Through the looking glass |
| 9.30am  | - Q & A                                |
| 10.00am | - Close                                |

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Zoe Holland  
Managing Director  
Zebra LC

The logo for Zebra LC is displayed within a dark blue rectangular box. The word "Zebra" is written in a white, serif font. Below it, the letters "LC" are written in a teal, sans-serif font, with a thin white horizontal line above the "C".

Zebra  
LC

# Through the Looking Glass



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## 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; IPs;
- Private equity; new entrant ABS; ATE
- Projects : £WIP books at £250k to a discreet project on a £100 million t/o firm with external investment
- Challenges: visibility is in demand





**What's under the bonnet?**

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## 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;

## Example DD Scope

- 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



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## WIP DD

- 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





# The Team



**THE TEAM**

## 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 keeps sticking (private client and litigation);
- Commercial property : specialist areas without a specialist eye.

## Impact of Technical Risk

- Handle with care
- Process with key supervision points
- Undervalued & Under-settled
- Indemnity risk : all areas
- Timescale: driving cash & profitability
- Litigation cases being allowed to 'drift'

Firm WIP	Retainer	Risk
£88,198.00		Green
£31,970.00		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

**YEAR OF THE BRAG**

£160k black listed : nil rated on value



## Cost Budgeting



- Lack of understanding  
Poor liaison between firm & external draftsmen  
Little case planning: putting costs at risk  
Assumptions insufficient detail



## Cost Team Trends

- Cost: paying over the odds
- Inaccurately drafted Bills
- Delay in service and thus loss of interest
- Poor negotiation
- Little 'added value' service

## Gold Star Costs Teams

- Costs panels & SLAs
- Costs Master & Proclaim (Utilisation)
- Complex injury: well drafted & timely served Bills of Costs
- Benchmarking % recoverability & hourly rates
- Structured relationship between firm & costs firm

## Maximising WIP

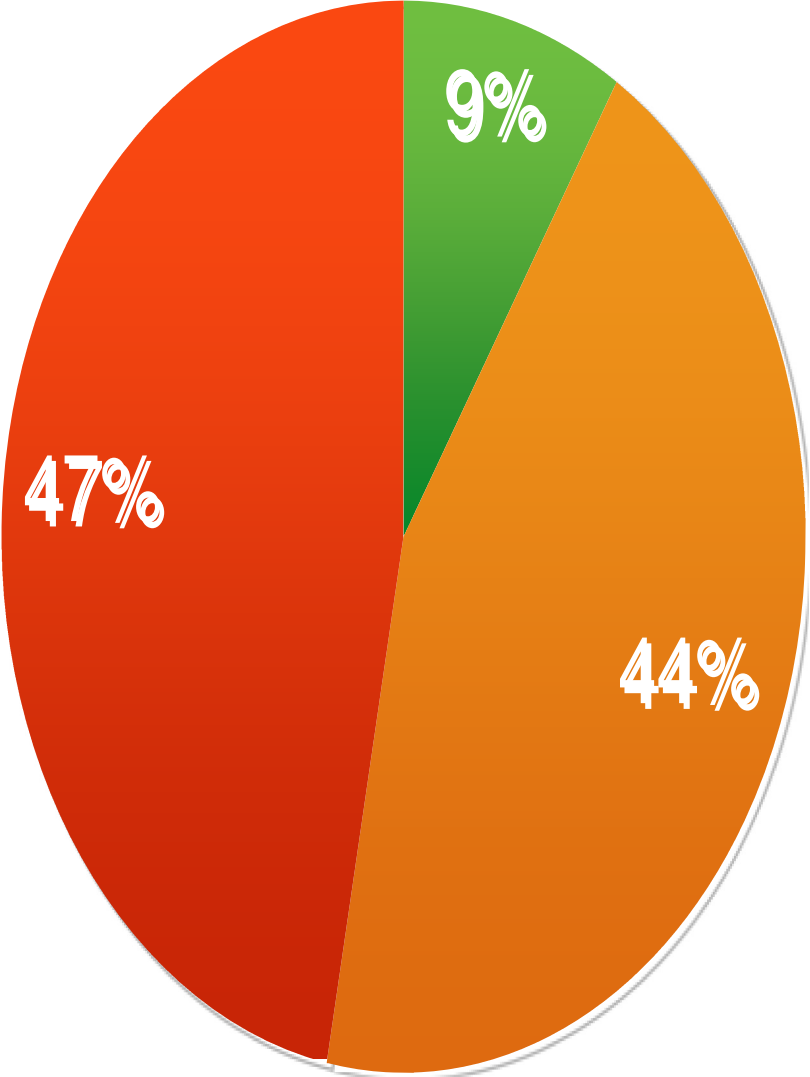
- Quality commodity & proof
- Process and case management
- MI that is accurate and targeted (aged WIP)
- Ability to differentiate admitted & non admitted WIP
- Benchmarking % recoverability & hourly rates

**Benchmarking & the stats**

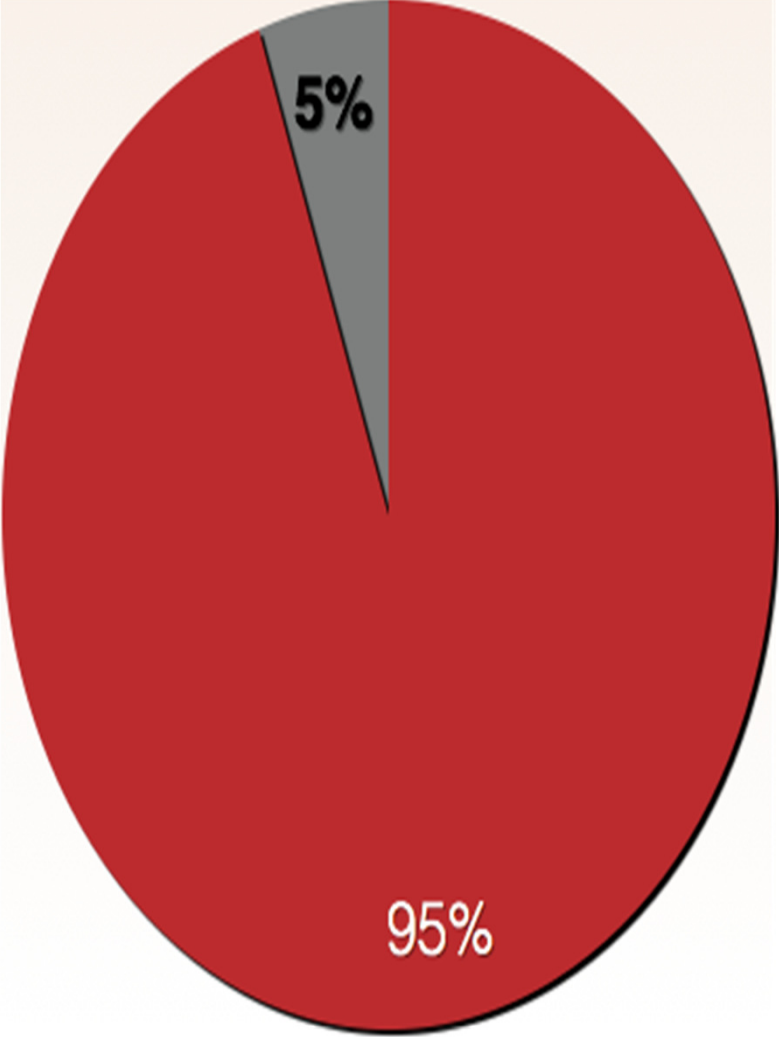
WIP risk profiling



**WIP stats**



**High risk WIP**



**What we see**



## Risk | Value | 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

- 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

## Shift from Legal Aid

- 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)



## 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

## **New entrant: post integration**

- Live WIP profiling data
- Assessment of settlement/completion risk & costs recovery risk
- Ongoing WIP valuation not year end
- Tracking movement & quality of WIP

## Technical WIP DD in M&A

- “Assessing the recoverability and cash conversion of the WIP of the acquisition target formed a key part of our overall due diligence programme.”
- “Understanding and diligencing complex legal matters across a variety of contingent and non-contingent work-types required a particular blend of legal and financial expertise and this is exactly what Zebra brought to the evaluation process.”

**Zoe Holland**

Managing Director

Zebra LC

Thank You



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## Questions and Conclusion

Sue Carter  
Yorkshire Bank

 Yorkshire Bank

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*we're with you...*