# Embracing change to succeed

## PwC Law Firms' Survey 2020

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**This is the 29th PwC Law Firms' Survey**
The editorial team for 2020 consists of:

### Kate Wolstenholme

Kate leads our Law Firms' Advisory Group ("LFAG") and works with national and international law firms on audit, accounting and strategy issues. She is chair of PwC's Risk Committee and a member of PwC's Supervisory Board, Audit Committee and Public Interest Body.

### Leon Hutchinson

Leon leads the audit and SAR work for a number of national and international law firm clients.  He regularly advises on accounting issues and heads up PwC's SRA Accounts Rules team.

### Tony Hodgson

Tony is a partner in our consulting practice. He leads assignments with law firms in areas such as pricing, matter management, business support services and IT.

### David Baxendale

David is a partner in our Deals business who advises various law firms and other financial stakeholders on sources of funding and appropriate funding structures.

### Catherine Usher

Catherine is part of our people & organisation team. She focuses on the legal sector, advising on partner reward structures and performance management, competency frameworks and diversity.

### Aidan Sutton

Aidan leads our professional partnerships tax practice nationally which advises more than sixty UK and US-headquartered law firms, providing services from partnership and partner compliance to tax risk and governance, working across our network in all the territories where our clients operate.

Our Law Firms' Advisory Group harnesses the expertise of specialists nationally and internationally to provide assistance with:

- Audit
- Direct and indirect taxation
- Strategic consultancy
- IT strategy, selection and implementation (Finance / PMS, HR and CRM)
- Cost reduction and outsourcing
- Mergers and acquisitions
- Compliance with SRA Accounts Rules and associated regulatory requirements
- Working capital management and financing
- Limited Liability Partnerships and other structuring advice
- Partner reward
- Employee and employer issues (reward structures and taxation)
- International secondments
- Internal audit and other risk management services; for example, cyber and information security

We would like to thank all other members of the LFAG who helped with this year's survey, particularly Colleen Dunn, Jen Smith, Sanah Faridi, Ryan Brason, Lynn Hunter, Dan Wicks, Dan Holmes, Lucinda Norton, Josh Noble, Craig Shaw, Oliver Humphries, Ben Lamb, Tiarnan Branson, Tanzina Brooks, Richard Jones, Sophie Elwin, Danielle Bennett, Matthew Timmons and John Patterson who contributed significantly to the production of this report.

In addition to the information presented in this report, all participating firms have access to an interactive online benchmarking tool that holds a vast amount of data from our survey. This tool also benchmarks each individual firm's results against their associated peer group banding. We present below a screenshot from our online benchmarking tool.


Please contact a member of our Law Firms' Advisory Group for a demonstration of our online benchmarking tool to see how you compare to your peers.

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The survey results are presented by size of firm using the bandings Top 10, Top 11-25, Top 26-50 and Top 51-100, except where otherwise stated (analysis for these bandings of firms has been adjusted to exclude high volume firms where their impact is considered significant). The classification is by annual global fee income.

Our report is based on survey responses from firms at consistent response rates to prior years. We've also drawn upon selected information from our quarterly survey and, where relevant, other published financial information. This summary document focuses on the key findings from our survey.

Our thanks are due, as always, to the firms which participated in this survey. We appreciate that the questionnaire takes considerable time to complete. All of the responses are processed in full and we have a significant amount of data that isn't fully reproduced here. If you'd like further information on the responses to any of the questions, please contact one of our editorial team.

## Key definitions

- Global Top 10 – Top 10 (by global revenue) UK headquartered firms where international revenue exceeds 20% of total revenue.
- Global Top 11-25 – Top 11-25 (by global revenue) UK headquartered firms where international revenue exceeds 20% of total revenue.
- UK – Operations of all UK offices only.
- International – Operations of all international offices only.

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# Overview and key themes

## Introduction

Our survey results this year reflect both the impact of ongoing uncertainty over the terms of the UK's departure from the EU, and the coronavirus (COVID-19) pandemic in the last quarter of the year to 30 April 2020. From the implementation of UK lockdown in March, most law firms moved swiftly to put measures in place to reduce the impact. These included a combination of reduced partner distributions, salary freezes, bonus deferrals, reduced working weeks, curtailment of discretionary spend, and shoring up of debt facilities. Against this sobering backdrop, our more optimistic theme for this year's survey is **'Embracing change to succeed'**, reflecting the opportunities that exist for firms to drive positive improvements from the disruption that has been forced on the sector.

Prior to the beginning of lockdown, the legal sector was already facing challenges. Last year's survey highlighted these under the theme 'Adapting to a new world' – which continues to be relevant in the current environment.

Challenges included:

- ensuring sustainable and profitable growth
- building an attractive culture for today's workforce
- investing in the right technology.

These challenges have not gone away, but firms will now be considering how to tackle them in a very different environment. Our survey reveals that COVID-19 is viewed as the most significant threat to law firms meeting their future ambitions over the next 2-3 years. Budgets, ambitions, and strategies have been and will continually be revisited and refreshed accordingly.

The **challenge of achieving profitable growth** is reflected in the current year results across all key metrics; for example 42% of Top 100 firms experienced falls in net profit; Top 10 firms' UK net profit margins fell for the sixth consecutive year; and UK PEP has reduced across all Top 100 bandings. Whilst it's easy to blame COVID-19 for these results, analysis of our quarterly surveys throughout 2019/20 reveals that profits had already begun to deteriorate well before the start of the final quarter of the financial year.

The workforce itself has experienced the biggest impact from COVID-19. Very quickly, staff have had to adapt to remote working. Whilst the impact has been severe, law firms have been given an opportunity to fast track **positive cultural changes** in areas such as work/life balance, hybrid working, use of office space, diversity and inclusion, mental health, and upskilling staff in digital technologies. With trust under the spotlight due to COVID-19, employers have the opportunity to **build trust with their workforce** by acting transparently and fairly, shouldering the financial burden whilst protecting jobs so far as possible, and demonstrating their core values of care and community.

With technology progression becoming an increasing priority for many firms in recent years, the **importance of IT** came to the fore right at the start of the COVID-19 lockdown. IT systems were put to the test and some firms had to invest quickly to ensure they could support their entire workforce remotely at very short notice. This stimulus will allow firms to assess the extent to which their IT systems are fit for purpose and make important further changes for the future. Considerations will include: moving data and applications to the Cloud, making more effective use of IT in firm-wide decision making, increasing efficiency and digitisation in end-to-end processes, and encouraging ongoing innovation to take advantage of emerging technologies.

Whatever IT improvements are introduced, it's of equal importance that the workforce have the capabilities and motivation to use this IT and generate the intended benefits and, therefore, firms should ensure there is a clear focus on change management, communication, and training alongside their IT investments.

Investment in IT should also include responding to the **ever growing cyber risk**, which has further increased during the pandemic. Whilst the response to cyber risk has improved over recent years, support and commitment at the governance level could be improved. Less than a quarter of all Top 100 firms have cyber committees that report into those charged with governance and this could impact the 'tone from the top' in this critical area.

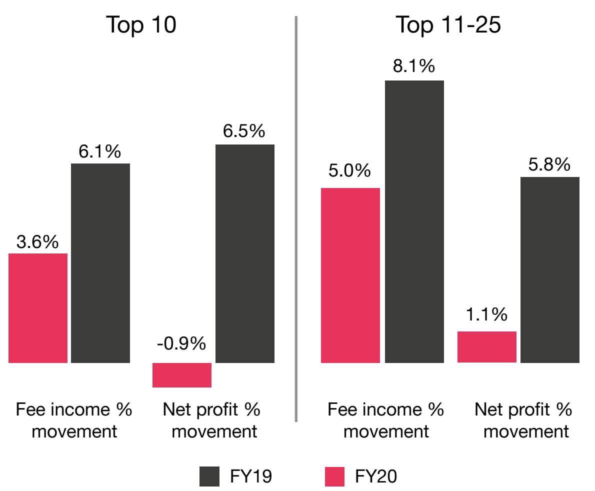
So, the future will definitely have its uncertainties for the legal sector. But we believe those firms that build on the work initiated in their immediate COVID-19 response, and embrace the innovation displayed, will emerge the strongest.

## Global financial performance

Global financial performance has been mixed across the Top 10 and 11-25 firms and is not as strong as in 2019. Whilst **modest fee income growth** has been achieved, this is not consistently reflected in firms' profitability. All Top 10 firms delivered fee income growth, at an average of 3.6% (2019: 6.1%) to £1,064m. However, average net profit (before full and fixed share equity partner remuneration) fell by 0.9% (2019: growth of 6.5%) to £399m.

Top 11-25 firms fared slightly better, with average fee income growth of 5.0% (2019: 8.1%) to £295m. But again, fee income performance was not reflected at the net profit level. Average profit growth was much lower, at 1.1% (2019: 5.8%) to £96m. Also, Top 11-25 firms saw a much bigger swing in profit performance by firm, with 25% posting profit growth in excess of 10% and a further 25% suffering profit reductions over 10%.

### Global fee income and net profit movements




**Global net profit margins have suffered,** with Top 10 firms experiencing a fall of 2.8 percentage points (before fixed share equity partner remuneration) from 38.0% last year to 35.2% this year. Top 11-25 firms saw a drop of 2 percentage points to 31.6% this year. The moderate increases in fee income have been more than offset by costs, with the movement on fee earner staff cost ratio featuring heavily as last year's salary war came home to roost. The monetary impact on Top 10 and 11-25 firms is approximately £23m and £10.6m respectively and this individually reduced net profit margin by 2.2 and 1.1 percentage points. We also see insurance costs continuing to rise, whilst savings have been made at the marketing and Business Development (BD) level with firms moving quickly to cut discretionary spend as the pandemic hit.

Fixed share equity partners continue to be significantly more prevalent in Top 11-25 firms than Top 10, making up 46% and 23% of total partners respectively. The impact on the margin performance gap is evident with the difference of 3.6 percentage points before fixed share equity remuneration (Top 10: 35.2%, Top 11-25: 31.6%) growing to 8.8 percentage points after fixed share equity partner remuneration (Top 10: 31.7%, Top 11-25: 22.9%). These performance gaps have narrowed since the prior year, when they were 4.4 and 12.5 percentage points respectively.

Global financial performance has been impacted by COVID-19, with regional and country lockdowns beginning with China in January 2020 and spreading to many other countries over the course of the financial year and beyond. There are also other factors that will have impacted performance - for example the ongoing uncertainty of the UK's exit from the EU, and the protests in Hong Kong over new government regulation throughout much of the Summer and Autumn 2019. With the backdrop of these various headwinds, the current year global results, particularly around profitability, are understandable.

## Global — Average percentage profit and loss account

| | Top 10 | | Top 11-25 | |
|---|---|---|---|---|
| | 2020 | 2019 | 2020 | 2019 |
| | % | % | % | % |
| **Fee income** | **100** | **100** | **100** | **100** |
| Staff costs — fee earners | 28.4 | 26.2 | 29.7 | 28.6 |
| Staff costs — non-fee earners | 12.2 | 13.2 | 14.4 | 14.4 |
| Property costs | 8.5 | 8.2 | 8.2 | 8.3 |
| IT revenue costs | 2.3 | 2.3 | 2.5 | 2.5 |
| Marketing & BD costs | 1.1 | 1.4 | 1.5 | 2.0 |
| Finance function costs | 1.0 | 1.1 | 0.9 | 0.7 |
| Depreciation | 2.0 | 1.5 | 1.9 | 1.9 |
| Insurance costs | 1.2 | 0.7 | 1.4 | 1.3 |
| Bad debts and disbursement | 1.2 | 1.0 | 2.1 | 1.5 |
| Foreign exchange differences | -0.2 | 0.3 | 0.1 | -0.1 |
| All other costs | 7.1 | 6.1 | 5.7 | 5.3 |
| **Profit before fixed share equity partners' remuneration** | **35.2** | **38.0** | **31.6** | **33.6** |
| Fixed share equity partners' remuneration | 3.5 | 2.2 | 8.7 | 10.3 |
| **Net profit margin** | **31.7** | **35.8** | **22.9** | **23.3** |

## UK financial performance

Approximately 10% of the year to April 2020 was spent under COVID-19 lockdown and this doubtlessly impacted the financial performance of UK law firms. However, further analysis of the UK financial results does underline the fact that there was ongoing economic pressure in the legal sector prior to the pandemic.

Whilst the majority of Top 100 law firms (70%) did report increases in fee income this year, this is notably down on prior years (2019: 89%, 2018: 84%) and **absolute growth levels have reduced**. Top 10 and 26-50 firms are most impacted with an average fee income increase of only 1.8% (2019: 4.1%) and 2.6% (2019: 3.3%) respectively. There was 4.9% fee income growth in both the Top 11-25 and 51-100 bandings (2019: 6.3% and 9.2%). In addition, a third of firms across the Top 50 bandings experienced falling fee income in 2020 compared to just 13% in 2019.

The evidence from our survey suggests that **pressure on profitability** exists more now than ever, with 42% of Top 100 firms reporting a fall in profits. This is up from 36% in 2019 and 30% in 2018. The extent of profit reductions in the current year is also a cause for concern. Of those firms reporting falling profits, 69% reported reductions in excess of 10% and 44% were greater than 15%. With the ongoing impact of COVID-19, halting and reversing this will be a clear challenge. A short-term strategy to minimise the effects on fee income and profit is imperative, with a longer term view of how the firm can operate, grow and thrive in what may be quite a different environment.

The Top 10 have been unable to halt the continued decline in net profit margin each year since the 2014 high of 40.0%. The fall this year has been one of the most significant over the last six years, at 1.7 percentage points to 33.8%. This compares to a 1.0 percentage point fall to 27.5% in Top 11-25 firms and a 2.5 percentage point fall to 22.2% in Top 26-50 firms.

Top 51-100 firms' average net profit margin has improved, from 22.9% to 26.3%, overtaking Top 26-50 firms' performance and now only 1.2 percentage points behind the Top 11-25. We note that this improved performance in Top 51-100 firms is due in part to a change in partnership models in some firms, although on a like for like basis their average margin has still increased above that of the Top 26-50 banding.

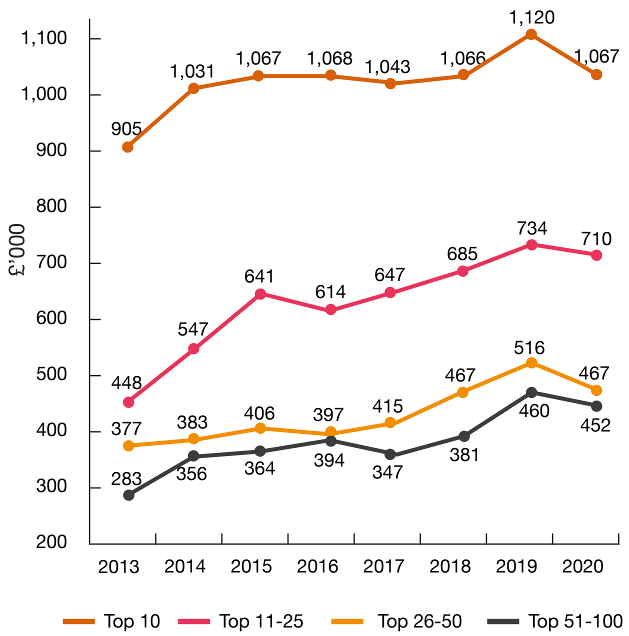
## UK — Average percentage profit and loss account

| | Top 10 | | Top 11-25 | | Top 26-50 | | Top 51-100 | |
|---|---|---|---|---|---|---|---|---|
| | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 | 2020 | 2019 |
| | % | % | % | % | % | % | % | % |
| **Fee income** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** |
| Staff costs — fee earners | 27.8 | 26.7 | 27.4 | 26.6 | 30.0 | 29.0 | 30.7 | 30.6 |
| Staff costs — non-fee earners | 11.1 | 11.2 | 14.0 | 14.5 | 15.1 | 14.2 | 14.0 | 14.7 |
| Property costs | 9.3 | 8.7 | 8.2 | 8.4 | 8.6 | 8.6 | 7.6 | 7.7 |
| IT revenue costs | 2.4 | 2.2 | 2.8 | 2.9 | 3.6 | 3.1 | 3.3 | 3.1 |
| Marketing & BD costs | 1.1 | 1.5 | 1.6 | 2.1 | 1.9 | 2.0 | 2.2 | 2.1 |
| Finance function costs | 0.7 | 1.2 | 0.7 | 0.6 | 0.6 | 0.5 | 1.0 | 1.0 |
| Depreciation | 2.0 | 1.6 | 2.1 | 2.0 | 2.1 | 2.2 | 1.7 | 1.8 |
| Insurance costs | 1.1 | 0.9 | 1.6 | 1.3 | 2.0 | 1.7 | 2.0 | 1.7 |
| Bad debts and disbursement | 1.3 | 0.6 | 1.8 | 1.5 | 1.5 | 1.1 | 1.7 | 1.0 |
| Foreign exchange differences | - | 0.4 | - | 0.1 | (0.1) | - | - | 0.3 |
| All other costs | 6.4 | 6.1 | 5.2 | 3.8 | 4.1 | 4.1 | 4.1 | 5.0 |
| **Profit before fixed share equity partners' remuneration** | **36.8** | **38.9** | **34.6** | **36.2** | **30.6** | **33.5** | **31.7** | **31.0** |
| Fixed share equity partners' remuneration | 3.0 | 3.4 | 7.1 | 7.7 | 8.4 | 8.8 | 5.4 | 8.1 |
| **Net profit margin** | **33.8** | **35.5** | **27.5** | **28.5** | **22.2** | **24.7** | **26.3** | **22.9** |
| Staff cost ratio (all staff costs) | 38.9 | 37.9 | 41.4 | 41.1 | 45.1 | 43.2 | 44.7 | 45.3 |
| Staff cost ratio (all staff, inc. FSEP costs) | 41.9 | 41.3 | 48.5 | 48.8 | 53.5 | 52.0 | 50.1 | 53.4 |

**Rising fee earner staff costs** are a major contributor to profit erosion, with the full impact of last year's salary wars and falling utilisation both taking their toll. The impact is most evident in Top 10 and 26-50 firms, with the staff cost ratio increasing in these bandings by 1.0 and 1.9 percentage points respectively. For Top 10 firms, the increase in senior fee earner headcount, whilst reducing the number of junior fee earner staff, will have exacerbated this issue somewhat. Interestingly, the pandemic has offered an opportunity to reverse this trend with many firms seizing the opportunity to rebase pay in the short term at least.

In recent years, excellent growth in profit per full equity partner ("PEP") has been achieved by all Top 100 bandings to record levels in 2019, aided by the management of full equity partner headcount. However, this has not been sustained in 2020 with profit pressures now also impacting partner profits. There have been **falls in PEP across all Top 100 bandings**: Top 10 - down 4.7% to £1,067k; Top 11-25 - 3.3% to £710k; Top 26-50 - 9.5% to £467k; and Top 51-100 - 1.7% to £452k.

## Trend in UK profit per full equity partner




## People

Previous surveys identified a bulge at the senior fee earner grades, coupled with decreasing chargeable hours and spare capacity. Firms outside the Top 10 have taken some action this year by balancing out fee earner grades; for example, Top 11-25 firms have reduced headcount >5 years post qualified experience (pqe) by 11%. In contrast, Top 10 firms have increased the number of senior fee earners (>5 years pqe) by 10% whilst 1-2/3-5 years pqe remained flat and newly qualified headcount was reduced by 28%.

**Utilisation in the Top 50 has fallen** across all grades, with the exception of fixed share equity partners and paralegals in the Top 10, 6-8 years pqe in the Top 11-25 and >5 years pqe in the Top 26-50. The largest reductions in chargeable hours are in Top 10 and 11-25 bandings. For example, there have been falls of between 2% and 8% across the newly qualified and post qualified grades. Top 51-100 firms reported modest increases across all grades below partner level, except newly qualified and >9 years pqe.

The resulting impact of headcount and chargeable hours movements is **rising spare capacity**. Across all bandings and grades from 1-2 years pqe to >9 years pqe, spare capacity is at least 10%, with the exception of 3-5 years pqe in Top 51-100 firms (8%). The more senior the fee earner, the more stark the issue, with >9 years pqe having between 18% and 20% spare capacity across the bandings.

It is critical that firms address the general pattern of reduced chargeable hours and increased spare capacity in the context of the COVID-19 pandemic. Many firms are reconsidering their ways of working and are faced with important decisions on how best to adapt their workforce strategy and utilise their people to fit a revised strategic direction, be that a reduction in headcount at some levels, an increase in working across practice areas or enhancing the role of technology in the delivery of legal services. Looking to the future, the use of AI tools for resourcing may provide a route to improving both utilisation and fair work allocation, with removal of unconscious bias in resourcing cited generally as a key step in firms' increasing focus on diversity and inclusion ("D&I").

## UK headcount

| Headcount | Top 10 | | | Top 11-25 | | | Top 26-50 | | | Top 51-100 | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Av. 2020 | Av. 2019 | % change 2019-2020 | Av. 2020 | Av. 2019 | % change 2019-2020 | Av. 2020 | Av. 2019 | % change 2019-2020 | Av. 2020 | Av. 2019 | % change 2019-2020 |
| Full equity partners | 151 | 146 | 3% | 72 | 70 | 3% | 57 | 59 | -3% | 28 | 25 | 12% |
| Fixed-share equity partners | 48 | 43 | 12% | 58 | 69 | -16% | 59 | 53 | 11% | 13 | 26 | -50% |
| Non-equity partners | 2 | 15 | -87% | 1 | 10 | -90% | 1 | 1 | 0% | 14 | 15 | -7% |
| **Total partners** | **201** | **204** | **-1%** | **131** | **149** | **-12%** | **117** | **113** | **4%** | **55** | **66** | **-15%** |
| 9+ year pqe | 148 | 287 | 10% | 106 | 185 | -10% | 85 | 136 | -4% | 33 | 75 | -23% |
| 6-8 year pqe | 167 | | | 60 | | | 45 | | | 25 | | |
| 3-5 year pqe | 125 | 125 | 0% | 69 | 57 | 21% | 56 | 48 | 17% | 28 | 34 | -18% |
| 1-2 year pqe | 140 | 140 | 0% | 53 | 61 | -13% | 49 | 40 | 23% | 22 | 27 | -19% |
| Newly qualified | 53 | 74 | -28% | 33 | 32 | 3% | 22 | 25 | -12% | 10 | 19 | -47% |
| Legal executives and paralegals | 162 | 175 | -7% | 63 | 110 | -43% | 125 | 112 | 12% | 53 | 75 | -29% |
| Trainees | 141 | 133 | 6% | 60 | 59 | 2% | 40 | 39 | 3% | 18 | 34 | -47% |
| **Total fee-earners (including partners)** | **1,137** | **1,138** | **0%** | **575** | **653** | **-12%** | **539** | **513** | **5%** | **244** | **330** | **-26%** |
| Business services and secretarial | 928 | 875 | 6% | 389 | 442 | -12% | 349 | 327 | 7% | 138 | 183 | -25% |
| **Total** | **2,065** | **2,013** | **3%** | **964** | **1,095** | **-12%** | **888** | **840** | **6%** | **382** | **513** | **-26%** |

## UK chargeable hours

| Headcount | Top 10 | | | Top 11-25 | | | Top 26-50 | | | Top 51-100 | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Av. 2020 | Av. 2019 | % change 2019-2020 | Av. 2020 | Av. 2019 | % change 2019-2020 | Av. 2020 | Av. 2019 | % change 2019-2020 | Av. 2020 | Av. 2019 | % change 2019-2020 |
| Full equity partners | 1,086 | 1,103 | -2% | 986 | 1,047 | -6% | 927 | 972 | -5% | 897 | 906 | -1% |
| Fixed-share equity partners | 1,064 | 1,055 | 1% | 1,017 | 1,054 | -4% | 974 | 1,012 | -4% | 886 | 948 | -7% |
| 9+ year pqe | 1,257 | 1,321 | -5% | 1,215 | 1,305 | -7% | 1,125 | 1,144 | -2% | 1,042 | 1,054 | -1% |
| 6-8 year pqe | 1,286 | | -3% | 1,307 | | 0% | 1,201 | | 5% | 1,156 | | 10% |
| 3-5 year pqe | 1,404 | 1,433 | -2% | 1,322 | 1,379 | -4% | 1,265 | 1,283 | -1% | 1,204 | 1,176 | 2% |
| 1-2 year pqe | 1,417 | 1,499 | -5% | 1,312 | 1,358 | -3% | 1,274 | 1,278 | 0% | 1,155 | 1,136 | 2% |
| Newly qualified | 1,345 | 1,460 | -8% | 1,202 | 1,282 | -6% | 1,140 | 1,150 | -1% | 1,038 | 1,109 | -6% |
| Legal executives and paralegals | 1,064 | 962 | 11% | 976 | 1,092 | -11% | 920 | 936 | -2% | 930 | 904 | 3% |
| Trainees | 1,083 | 1,142 | -5% | 989 | 1,032 | -4% | 883 | 939 | -6% | 869 | 855 | 2% |

D&I initiatives continue to be a key part of the people agenda in law firms. There is evidence of positive change, although the pace is gradual rather than radical. With renewed emphasis on social justice and equal opportunity within society, D&I credentials are increasingly forming part of the recruitment process (as well as the procurement process). It is therefore **imperative for law firms to have a clear D&I strategy** and demonstrate progress.

The Black Lives Matter movement has increased firms' focus on BAME with representation rising slightly and firms now setting themselves more challenging targets.There has been a steady increase in female representation at partner level amongst the Top 50 firms, from 19% to 22%. Firms continue to look to their trainee ranks to boost the proportion of female talent in the workforce, with typically over 60% female representation at this level. However, the continuing drop-off in representation from trainee to partner level serves as a reminder of the scale of the task facing law firms in creating organisations which reflect the markets they serve. Looking to the future, we expect to see firms use the sudden shift towards remote working brought about as a result of the COVID-19 to embrace more agile working practices, which may have a positive impact on gender representation.

## Financing

The pandemic has taken **working capital performance from a priority to an imperative** for most firms. Even those that were well positioned pre-pandemic are now closely assessing their end-to-end cycles and taking further steps to ensure a safe level of liquidity headroom to allow for any future shocks like those faced by the profession following lockdown.

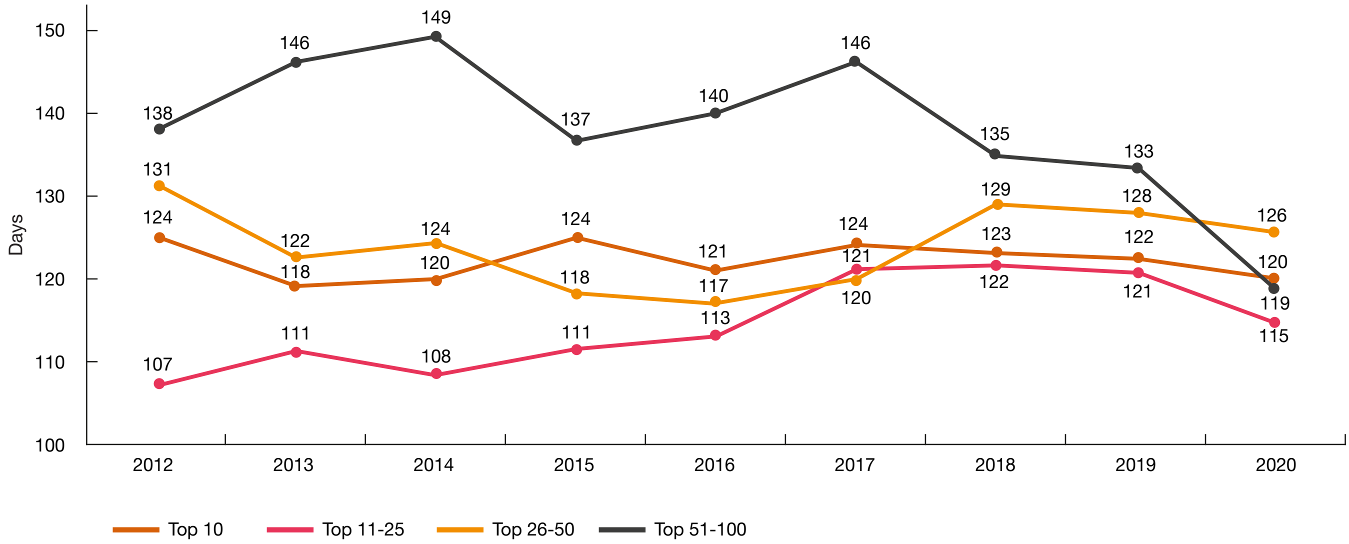
Cash collection initiatives and financing decisions linked to COVID-19 have impacted our current year analysis. All bandings improved their year end total lock up performance, with the Top 51-100 firms making the most substantial reductions (for the fourth consecutive year), from 133 to 119 days. The improvements made in the Top 50 bandings range from 2 to 6 days and the best performing banding continues to be the Top 11-25 firms at 115 days.

The emphasis being placed by firms on improving their use of technology and centralising processes in their support functions could help to unlock cash if this is properly executed. Despite the improvement in overall lock up, the total value of cash locked up across the Top 100 firms remained fairly flat at £3.7bn. Therefore, there remains a substantial source of value which could provide much needed liquidity.

In response to COVID-19, many law firms have taken action around their external financing. The Top 50 bandings increased their external finance as a larger proportion of overall funding, with the most significant increases in the Top 11-25 (up from 21% to 28%) and Top 26-50 (up from 12% to 17%). This was principally through revolving credit facilities and short/medium term loans.

Given the challenging economic outlook and an uncertain road ahead, firms must continue to shore up cash collection performance and secure access to adequate sources of liquidity. This will help ensure coverage of future fixed costs and other liabilities, including tax payments, and will avoid more severe cost cutting measures.

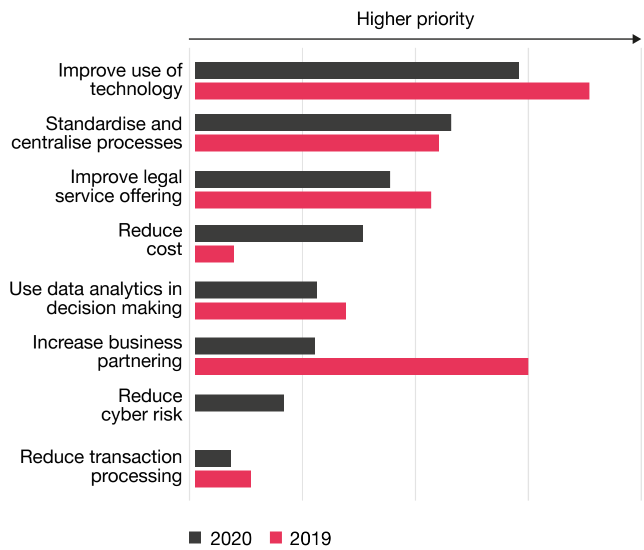
## Trend in average UK year end total lock up days




## Business support

Whilst the top three priorities remain the same as last year ('Improve the use of technology', 'Standardise and centralise processes', and 'Improve legal service offering'), **the pandemic has dramatically increased the priority of 'Cost reduction'** in this year's survey. This mirrors a trend last seen in the year that followed the 2008 economic crisis; and the focus on cost reduction will inevitably become increasingly important the longer the pandemic continues.

## Top priorities for business support over the next twelve months



Almost all firms have taken 'no regrets' decisions and paused investments that, whilst important, could wait until the outlook is more certain. For many, the plan is to re-start paused investments later in the calendar year as further delays could ultimately be detrimental to the business in the longer-term. The cost reduction focus has enabled firms to **pinpoint and prioritise essential investments**, whilst halting the 'nice-to-haves' and reshaping other initiatives to make them more cost effective.

Whilst all firms have had to be short-term focused in recent months, the most agile are now looking to the future and considering how recent experiences will result in permanent change. At the heart of this will be an acceptance that people will continue to work remotely for a proportion of their working week and that the **use of real estate will need to be re-thought** in support of new ways of working and to be cost-effective. This degree of change will need careful planning to ensure that new ways of working meet the needs of clients, are motivating to fee earners and staff, and allow partners to continue to lead the business effectively.

Underpinning these future changes will be the need for **continued technology enhancements**. These are likely to include the use of a range of productivity tools to keep teams connected and working effectively. The move towards the Cloud will undoubtedly continue to support the improved use of data and applications. Having made investments in legal technologies and back office systems (such as Finance/Practice Management and HR systems) in recent years, many firms are now turning their attention to equipping their partners and staff with the latest Client Relationship Management ("CRM") technologies in order to enhance client connections and be more effective in the markets in which they operate.

## Governance and risk

For the first time this year, recognising the importance of strong and agile decision-making in the face of a "Black Swan" event such as COVID-19, our survey includes a section on governance.

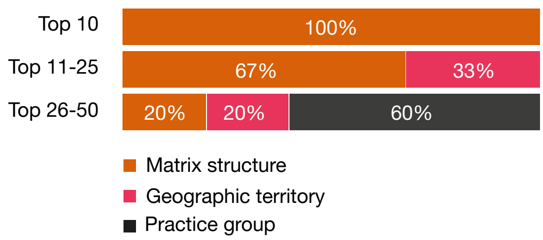
Governance of partnerships is an art, not a science - there is no 'one size fits all' model. However, given the increasing focus on governance in the world of private business (as well as listed companies and regulated industries such as financial services), law firm governance has been slower than most to adapt. Fast-paced developments in technology, economic influences impacting strategy, and growing expectations from society mean that law firms need to **ensure their governance arrangements remain fit for purpose** in today's environment.

There are a number of law firms that are operating under historic governance structures (including the combination of legacy arrangements on merger), with little rationalisation over time. This has resulted in arrangements that have been inherited by the current generation of management/partners rather than being specifically designed to suit the business of today.

Our survey reveals that Top 10 firms are primarily managed through a matrix structure. Whilst this is also the model of choice for Top 11-25 firms, a third of those are instead managed by geographic territory, whilst the Top 26-50 firms, tending to be less international, favour the practice group structure.

Whilst matrix governance and global networks are beneficial for business in a number of ways, these factors do increase the complexity of a firm's governance arrangements and can add layers of unnecessary bureaucracy. This is reflected in the 83% of Top 10 firms that believe overly complex governance structures may inhibit agile decision making in the future.

### How global law firms are managed




Recent events such as Brexit and COVID-19 have made it clear that those firms with strong leadership, agile structures and efficient decision making processes were able to respond quickly and effectively to business needs. Boards with a clear understanding of their purpose and values were also able to cut through the noise and articulate their decisions to key stakeholders (e.g. partners, staff and clients) in a timely manner that engendered trust.

There is no consistent industry standard for law firms to conduct governance reviews, but it can be a helpful exercise for boards to periodically reflect on the relevance of a firm's governance arrangements and alignment with the strategy, risks and stakeholder requirements of today. Firms reported that key areas of governance focus include financial and operational performance, refreshing the strategy, diversity and inclusion, and risk/reputation management, but many identified a lack of time/capacity within the governance function as an obstacle to success.

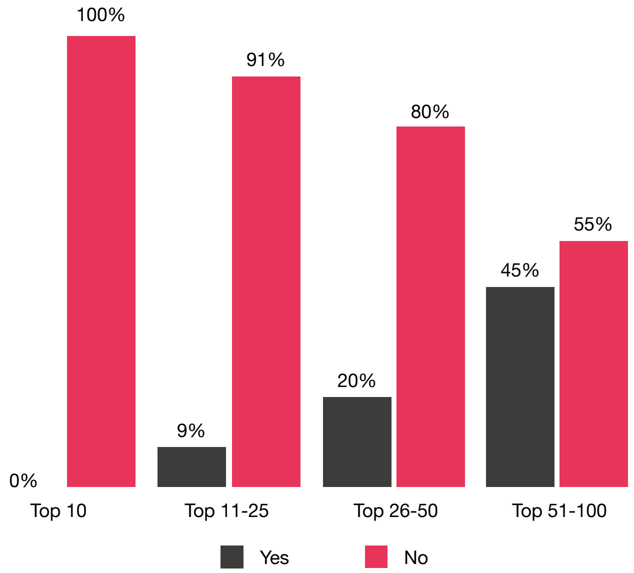
With the current focus on environmental and social impact, strong governance acts as a framework in which businesses can review their impact on all facets of the wider environment in which they operate. The pandemic has shown how some businesses have responded to Environmental, Social and Corporate Governance ("ESG"), and in return have received a renewed legitimacy to operate.

Law firms need to consider the reputational risk if they do not reflect the values and behaviours of their stakeholders (including clients, and current/future employees) in their operations. Whilst half of Top 100 law firms oversee social and ethics matters at board level, this feels for many to be just the start of a significant journey; consideration needs to be given to turning discussions into actions. Improvements in transparency, reporting and stakeholder engagement will also increase trust and reputation in the legal profession's approach to ESG.

**Cyber security** remains a key challenge for law firms and the sector is increasingly being targeted as firms hold both a wealth of sensitive data and large amounts of client money. This year's participants deemed cyber risk the second greatest threat to law firms meeting and/or exceeding their ambitions in the period from now until 2022, with only COVID-19 ranking higher. Overall, 71% of Top 100 firms stated they were "somewhat concerned" or "extremely concerned" about the cyber security threat. For Top 11-25 firms, cyber security was ranked the greatest threat.

Effective cyber security governance is a key component to understanding and managing risk effectively. Boards should be aware of the cyber threats to their firm and have a real understanding of exposure. Despite the continued threat, effective cyber security governance does not appear to be appropriately prioritised by law firms. Only 22% of Top 100 firms have a Cyber Committee that reports into the party charged with governance. This statistic is lowest in Top 10 and 11-25 firms, at 0% and 9% respectively.

### Percentage of law firms with cyber security committees reporting into corporate governance forums




In the absence of defining a comprehensive board approach to cyber security - one that genuinely manages risk rather than implementing 'standard' control frameworks in the hope they are sufficient – the question will remain as to whether the board is fully engaged in relevant cyber decision making. There is a risk that without embedding cyber security into corporate governance processes, boards will not be able to make the tough decisions required to effectively respond to cyber security threats, allocate sufficient funds to cyber security investment, be able to explain their approach to stakeholders, and be able to drive good practice. All firms are different, but each board needs to set its own direction and tone for cyber security.

## Future

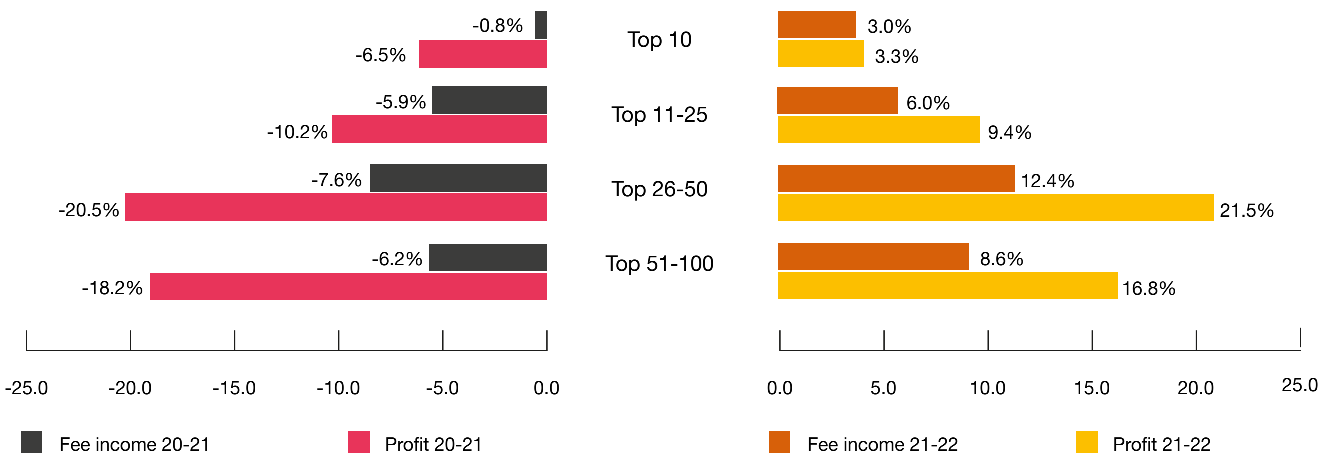
As expected, given the current COVID-19 pandemic, along with the political and economic uncertainty related to Brexit, law firms are concerned about financial performance in the short term and this is reflected in financial forecasts.

Of the Top 100 firms, 81% were either 'extremely concerned' or 'somewhat concerned' that COVID-19 would stop their firm meeting its ambitions in the period up to 2022. However, with other important risk factors to juggle it is important that adequate resources are committed across all key areas of risk (e.g. response to Brexit, speed of technological change, lock up improvements, etc).

Across all Top 100 bandings, there is a consensus that fee income will fall during 2020/21. The average fall across the bandings ranges from 0.8% in Top 10 firms to 7.6% in Top 26-50 firms. The expected falls in profit are much more significant, ranging from 6.5% in Top 10 firms to 20.5% in the Top 26-50. Early indications post-30 April (the typical year end for our survey) are that the post-COVID-19 period results are not perceived to be as bad as first feared. But with the pandemic ongoing and potential future unseen circumstances, firms are maintaining a cautious approach to financial management.

The outlook for 2021/22 is much more positive, with the majority of Top 100 firms expecting increases in fee income and profit outweighing the anticipated reductions during 2020/21. Top 26-50 firms are the most positive in this period, with expected revenue and profit increases of 12.4% and 21.5% respectively.

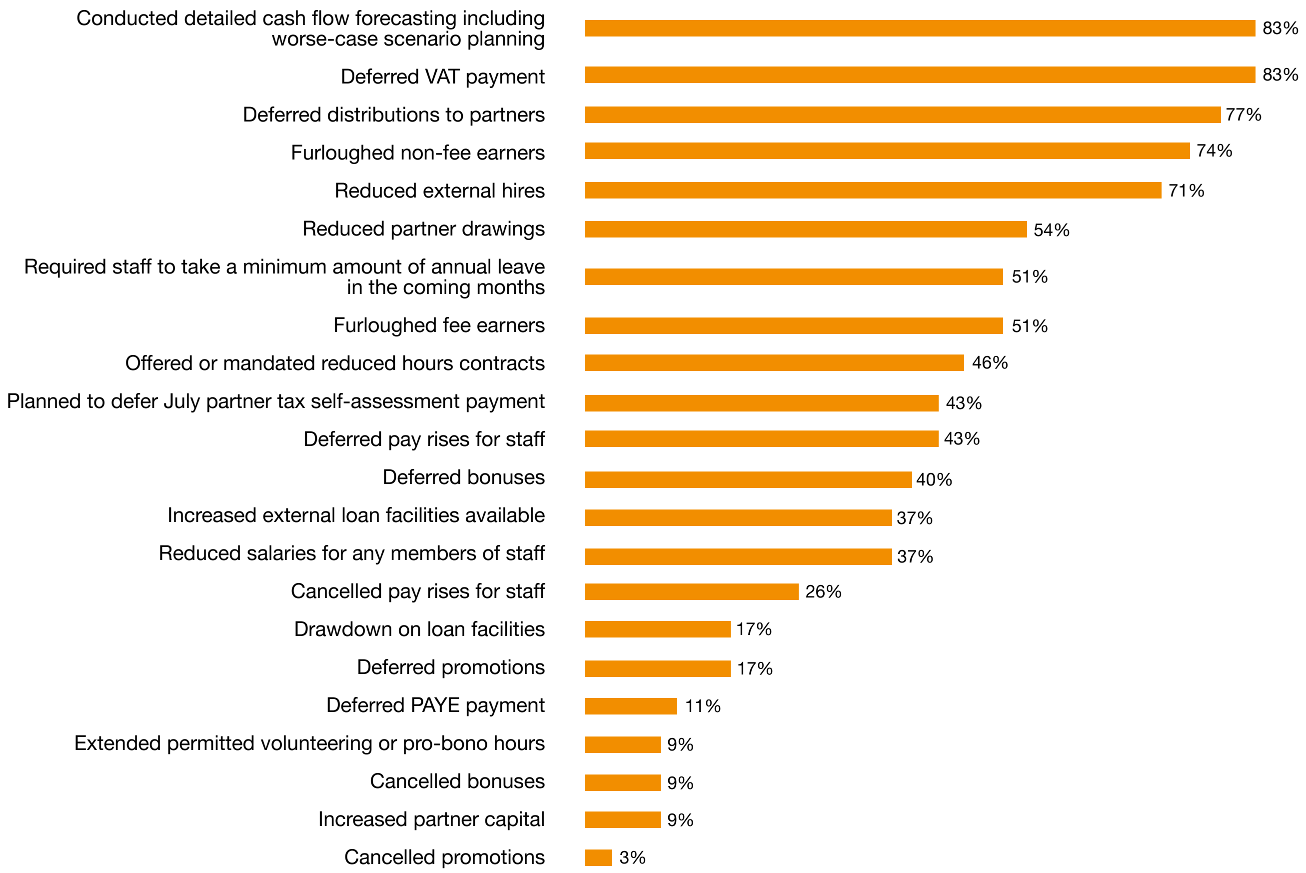
### Predicted movements in fee income and profits: 2019 to 2020 and 2020 to 2021 (%)




In our survey for the final quarter to 30 April 2020, we requested views on the consequences of COVID-19 to date and the expected impact looking forward. Whilst this survey was completed in late May/early June, it did demonstrate the extent to which law firms reacted to the start of the pandemic. For example, a majority of firms took actions to support liquidity and/or reduce cost. Across the Top 100 firms, 83% deferred VAT payments, 74% furloughed non-fee earners, 51% furloughed fee earners, 71% reduced external hires and 46% offered or mandated reduced hours contracts.

The financial burden in many law firms is being shouldered by partners, with 77% of Top 100 firms deferring distributions to partners and 54% reducing partner drawings. Staff members have also been impacted though, with 51% of the Top 100 requiring staff to take a minimum amount of annual leave over the summer months, 43% deferring pay rises and 40% deferring bonuses. Some firms are cancelling pay rises (26%), rather than deferring, while others are reducing existing salaries (37%).

## Law firms response to the onset of COVID-19



# At a glance



# 1. Global financial performance

## Global headcount

- Global Top 10 and 11-25 firms have, on average, increased their headcount since last year.
- Top 10 firms have focussed their headcount investment in business support staff, with a 7.5% increase. Partner and fee earner headcount has grown modestly, by 1.7% and 0.8% respectively.
- Conversely, Top 11-25 firms have invested more in their fee earner headcount, an increase of 17.9%. Business Support staff headcount is also up significantly, at 11.3%, whilst partner headcount is up 2.8%.

## Global fees

- All Top 10 global firms grew fee income, with two thirds of these firms achieving growth of between 1% and 5% and the remainder growing fee income by between 5% and 8%.
- Half of Top 11-25 firms grew global fees by between 1% and 5%, whilst 38% reported growth in excess of 5%. Fee reductions of less than 3% occurred in the remainder of firms.
- For the second year running, international offices are feeding the majority of increases in global fee income. In Top 10 Firms, 72% of fee income growth was achieved through international offices. In Top 11-25 firms this was 63%.

## Global profits

- The good results in fee income growth are not consistently mirrored at the net profit level. Average global profits in Top 10 firms fell by 0.9%, whilst they increased by 1.1% in Top 11-25 firms.
- There are significant swings in net profit performance across the Top 25 firms, with 43% reporting profit reductions. Profit reductions of over 10% were experienced by 14% of Top 25 firms, whilst the same number of firms also reported profit growth in excess of 10%.
- International offices have, generally, contributed profit growth to the global picture, but this has been offset by a negative profit performance in UK offices.
- International net profit grew by 2.1% in Top 10 firms and by 5.2% in Top 11-25 firms (after accounting for the minimal impact of exchange rate movements). This compares to a fall in UK profit of 4.5% in Top 10 firms and 1.5% in Top 11-25 firms.
- Average global net profit margins (before full and fixed share equity partner remuneration) have fallen significantly from prior year. The Top 10 global net profit margin of 35.2% is down by 2.8 percentage points from prior year. Top 11-25 firms recorded a similar trend, with a fall in their average global net profit margin of 2.0 percentage points to 31.6%.

## Global costs

- The key cost ratio movement that impacts upon global net profit margins is the fee earner staff cost ratio. In Top 10 firms, this increased from 26.2% to 28.4%. In Top 11-25 firms, the increase was from 28.6% to 29.7%.
- Non-fee earner staff costs in Top 10 firms fell by 1 percentage point to 12.2% and it remained consistent in Top 11-25 firms at 14.4%.
- All other cost ratio movements in both bandings were 1 percentage point or less.

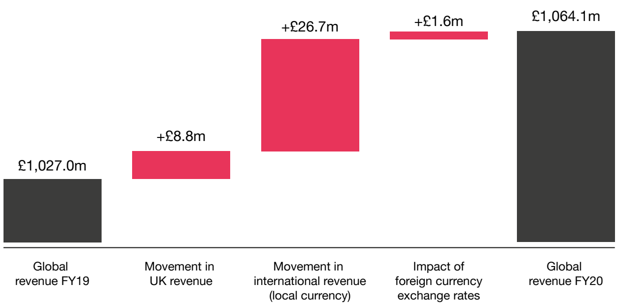
## International analysis

- All Top 10 regions increased net profit margins by between 4 and 8 percentage points, with the exception of the following falls (i) Western Europe - 2.5 percentage points to 32.0%; (ii) Middle East - 5.8 percentage points to 14.8%; and (iii) China 1.3 percentage points to 20.8%.
- Regions posting increases to the net profit margin in the Top 11-25 were Western Europe (up 4.8 percentage points to 17.5%), Middle East (up 5.4 percentage points to 11%) and Australia (up 4.2 percentage points to 20%). This compares to a fall in net profit margins in China and Rest of Asia & Far East, being a 7.9 and 5.3 percentage points fall respectively to 8.4% and 15.9%.

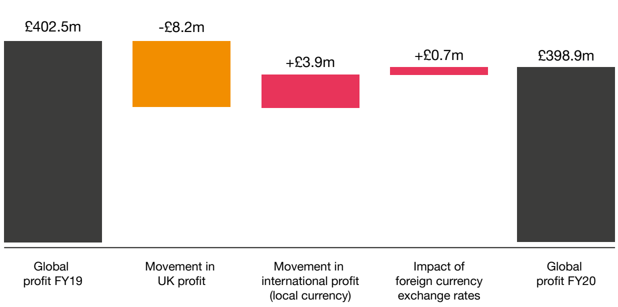
## Global fee income and profits: source of growth

The majority of growth for global law firms is being achieved in the international network and this is particularly evident in respect of profit, where reductions in the UK have been partially offset by a positive international performance.

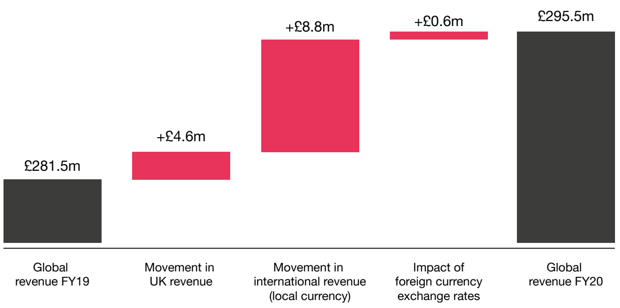
**Top 10 – Revenue**



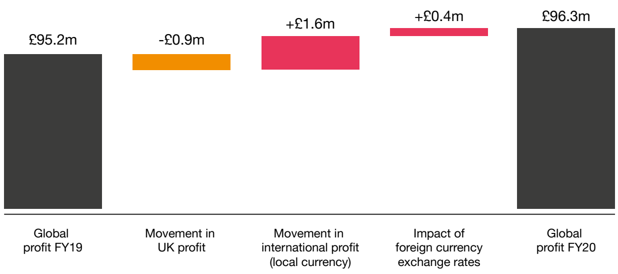

**Top 10 – Profits**




**Top 11-25 – Revenue**

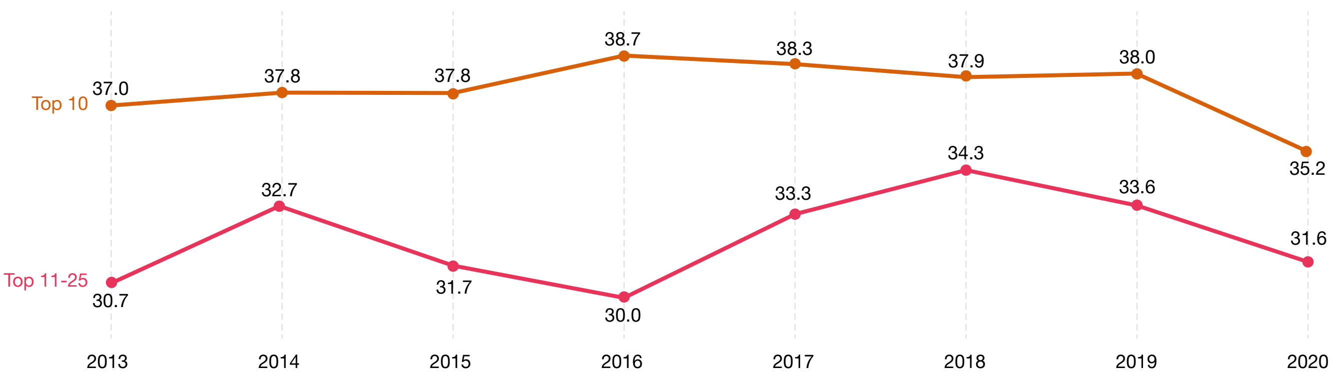



**Top 11-25 – Profits**




## Trend in global profit margins

Both Top 10 and 11-25 firms have suffered reductions in their global profitability in the current year; with Top 10 firms global net profit margin (before full and fixed share equity remuneration) falling by 2.8 percentage points to 35.2% and Top 11-25 firms fell by 2.0 percentage points to 31.6%.



# 2. UK financial performance

## UK fees

- The average fee increase achieved by Top 100 firms has fallen for the second successive year to 3.7%. In 2019 and 2018 this was 5.9% and 8.3% respectively.
- There is a variance in the average UK fee income growth by banding, with Top 10 and 26-50 firms achieving 1.8% (2019: 4.1%) and 2.6% (2019: 3.3%) respectively; Top 11-25 and 51-100 firms performed better with 4.9% growth in each banding (2019: 6.3% and 9.2%).
- No Top 10 firm reported a double digit fee increase for the second year running. Other bandings in the Top 100 saw between 18-20% of firms achieving double digit fee income growth. A small number of firms (less than 10% in the Top 100), achieved double digit growth in both 2019 and 2020.
- Fees per fee earner have remained broadly consistent across the Top 10 and 11-25, with no movements in excess of 2% (Top 10 down 0.2% to £414k; Top 11-25 down 1.2% to £321k).
- Top 26-50 firms saw a decrease in fees per fee earner of 5.9% to £223k; although on a like for like basis the decrease is much lower at 2.3%.
- Top 51-100 firms increased fees per fee earner by 10.1% to £207k; although, on a like for like basis the increase is much lower at 3.3%.
- All bandings except the Top 26-50 have managed to increase fees per chargeable hour and this is despite a general decline in utilisation across the Top 100: Top 10 up 5.1% to £331, Top 11-25 up 5.3% to £300; and Top 51-100 up 6.5% to £213. It appears these firms have achieved better rates, or utilised more expensive grades, in the delivery of work. Top 26-50 firms recorded a fall of 2.2% to £223.

## Fee income write offs

- Although some firms have successfully reduced the level of fee income write offs, continued (or renewed) focus is evidently required to drive down this statistic to an acceptable level.
- The number of firms reporting write offs of between 15 and 25% across the bandings are as follows: Top 10: 33%; Top 11-25: 20%; Top 26-50: 40%; and Top 51-100: 60%.

## UK costs

- Whilst the average staff cost ratio by banding has remained within 2% of prior year, it appears most firms continue to experience a higher staff cost base.
- The staff cost ratio (excluding fixed share equity partner remuneration) is up across the Top 50 bandings: Top 10 - 38.9% (2019: 37.9%); Top 11-25 - 41.4% (2019: 41.1%); and Top 26-50 - 45.1% (2019: 43.2%).
- The staff cost ratio fell for Top 51-100 firms from 45.3% last year to 44.7% this year. However, this is partly due to a change in mix of respondents and on a like for like basis there is a slight increase in the staff cost ratio.
- Fee earner costs (rather than business support staff) are driving the staff cost ratio increase, with this cost growing by between 0.8 and 1.1 percentage points across the Top 50 bandings.
- These increases are despite a fall in fee earners in Top 10 and 11-25 firms. Although, in Top 10 firms the reduction in fee earners has been focussed on junior staff with a partial offsetting increase in senior fee earners.
- The fixed share equity partner remuneration cost ratio has remained relatively steady across the Top 50 bandings, with a reduction of between 0.4 and 0.6 percentage points.
- The Top 26-50 firms is the only band to increase both the fee earner and non-fee earner staff cost ratio, by 1.0 and 0.9 percentage points respectively, and this is driven by a rise in headcount in both of these staff categories.

## Support functions cost as a percentage of fee income

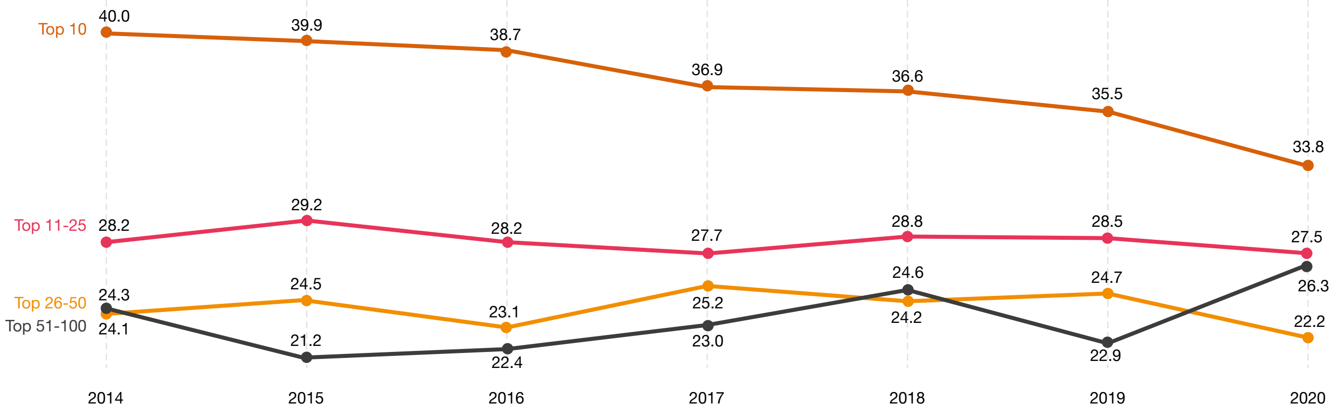
- Support function costs as a percentage of fee income (including salary costs) are broadly consistent with last year. The only movement in excess of one percentage point for any category across all bandings was ‘Marketing & BD’ in Top 26-50 firms (2020: 3.2%, 2019: 4.5%).
- The most significant costs across all bandings are ‘IT Revenue’, ‘Secretarial Support’ and ‘Marketing & BD’.

## UK profits

- The theme of “profit pressure” has continued during 2020. Other than the Top 51-100 banding, average net profit declined compared to 2019.
- The Top 10 trend of falling net profit margins continues into its sixth year and this year’s fall is significant, from 35.5% to 33.8% (this is 6.2 percentage points below the 40% high in 2014).
- The net profit margin performance gap between Top 10 and 11-25 firms has narrowed again this year to 6.3 percentage points (Top 11-25 net profit margin - 2020: 27.5%, 2019: 28.5%); this was 11.8 percentage points in 2014.
- In previous years, full equity partner headcount was managed to achieve PEP results; however, this has not been mirrored in the current year. Average PEP has fallen across all bandings (by between 1.7% and 9.5%), something not experienced since 2013 and reverses the record PEP highs of 2019.

## Movement in net profit margin: 2014 to 2020

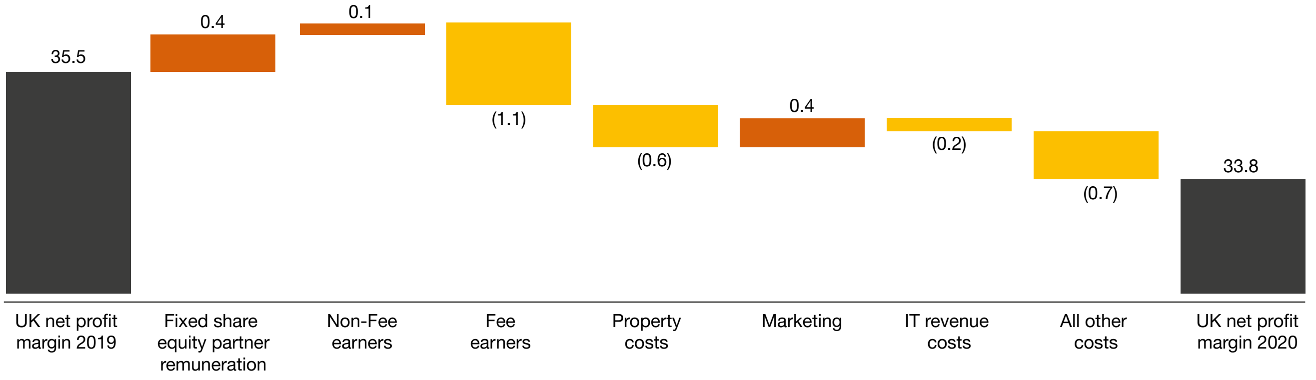
Top 10 firms have experienced a steady decline in their average net profit margin since 2014, whilst there has been more volatility in this KPI for the bandings outside the Top 10.



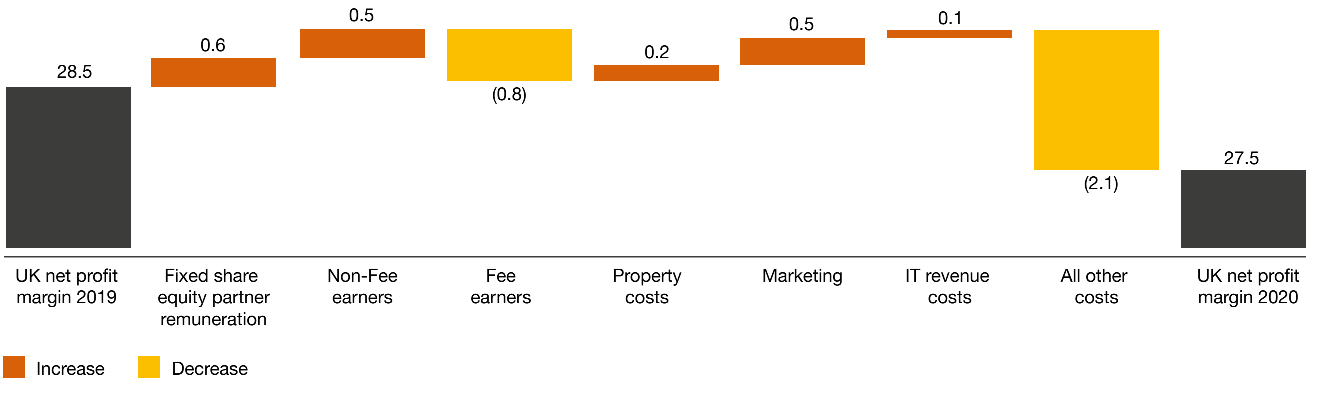

## Net profit margin bridge: 2019 to 2020

Both Top 10 and 11-25 firms have made savings on non-fee earner costs and marketing costs; however, these have been eroded by the increase in fee earner and fixed share equity partner remuneration costs. Other general costs have also impacted the fall in net profit margin.

**Top 10**




**Top 11-25**



# 3. People

## Headcount

- Total headcount has increased in Top 10 (3%) and Top 26-50 firms (6%), but fallen in the Top 11-25 (-12%) and Top 51-100 (-25%). We note that Top 51-100 firms are impacted by a change in mix of respondents, and on a like for like basis, headcount has remained relatively static.
- Full equity partner headcount rose in Top 10 (3.4%), 11-25 (2.9%) and 51-100 firms (12.4%), reversing the trends of recent years. This headcount did fall by 3.4% in the Top 26-50.
- The role of the non-equity partner has virtually disappeared in Top 25 firms, with an average headcount of two in Top 10 firms and one in the Top 11-25.
- Movement in fee earner headcount in Top 11-25, 26-50 and 51-100 firms is almost identical to the total headcount movements noted above.
- Top 10 firms fee earner headcount remained static; however, there has been a change in mix by grade of staff. 6-8 years pqe/>9 years pqe headcount is up 10%, whilst newly qualified and paralegals are down 28% and 7% respectively.
- In contrast, Top 11-25 and 26-50 firms reduced headcount amongst the most senior fee earner grades (6-8 years pqe and >9 years pqe), by 10% and 4% respectively.

## Leverage

- The ratio of fee-earners to full equity partners fell across all bandings, with the exception of the Top 26-50 where there was an increase from 8.7 to 10.6; although, on a like for like basis the Top 26-50 ratio was consistent with prior year.
- The reduction in the Top 51-100 firms (10.3 to 8.4) brings this group more into line with the Top 25 firms (Top 10 - 2020: 7.2, 2019: 7.7; Top 11-25 - 2020: 7.0, 2019: 8.7).
- The trends noted above reflect the general reduction in fee earner headcount and increases in full equity partner numbers.
- There has been no movement in the ratio of fee earners to non-fee earners (or business support staff) in the Top 11-25 (1.5), 26-50 (1.6) and 51-100 firms (1.8). There was a slight fall from 1.3 to 1.2 in Top 10 firms.

## Chargeable hours

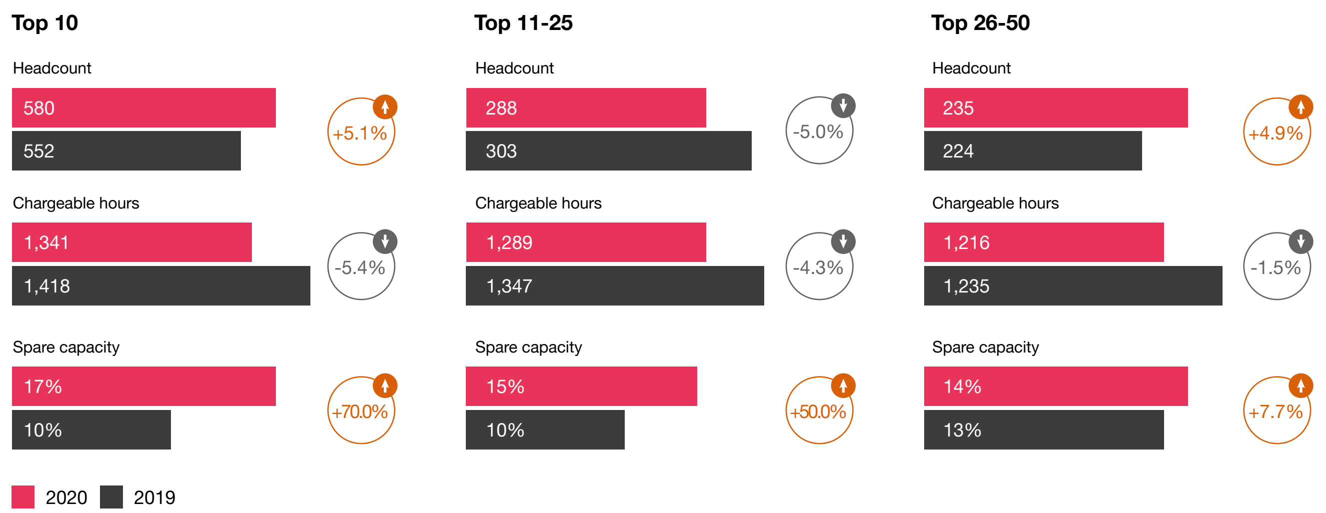
- Chargeable hours have fallen across the vast majority of grades in the Top 50 bandings.
- Top 10 firms have reported the most significant falls across the qualified fee earner group.
- Average chargeable hours in Top 26-50 firms have seen little movement amongst most qualified fee earners grades (no more than 2%).
- Top 51-100 firms' average chargeable hour levels have proved more robust than larger firms, with increases of between 2% and 4% across all grades except full and fixed share equity partners (down 1% and 7% respectively) and newly qualified (down 6%).
- Movements in chargeable hours (and headcount) have impacted upon spare capacity across all grades, with a steep rise in the Top 10 (12.6% to 18.5%) and Top 11-25 firms (13.6% to 18.4%), whilst remaining flat in Top 26-50 firms (16.8%). The Top 51-100 firms managed to reduce spare capacity from 17.4% to 14.2% across all grades, although on a like for like basis, spare capacity was broadly flat.

## Diversity

- The trend of rising female representation at partner level in the last seven years continues across all of the Top 100 bandings, other than the Top 26-50, with notable increases this year: Top 10: 20.4% to 21.8%; Top 11-25: 18.1% to 20.5% and Top 51-100: 18.4% to 29.3% (26.8% on a like for like basis). Top 26-50 firms have seen a slight fall: 19.9% to 19.2% (although on a like for like basis an increase to 20.4%).
- At trainee level for all bandings of firms, there continues to be more females than males (57% and 59% in the Top 10 and 26-50 respectively; 65% and 66% in the Top 11-25 and 51-100).
- BAME representation has risen slightly amongst the Top 10 firms at both partner level (6.8% to 7.6%) and trainee level (21.7% to 24.2%). This trend is mirrored for Top 11-25 firms at trainee level (11.5% to 12.1%), but not at partner level (4.5% to 3.8%).

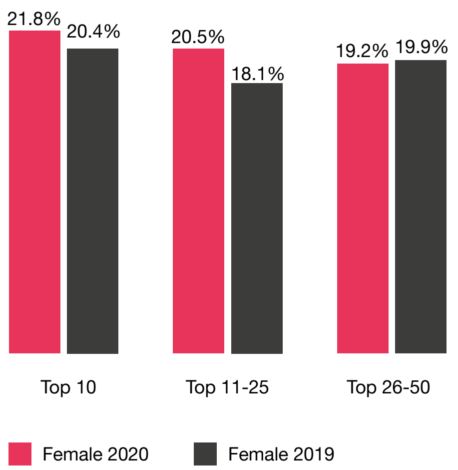
## Movement in headcount, chargeable hours and spare capacity (1 - >9years pqe)

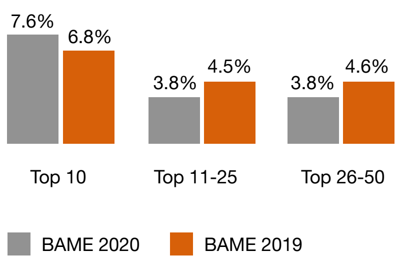
Spare capacity has risen sharply in Top 10 and 11-25 firms, with chargeable hours reducing amongst all sizes of firm.




## Gender and ethnicity representation at partner level

While female representation at partner level is rising across the board (other than in the Top 26-50), the trend in BAME representation is mixed, with a fall amongst the Top 11-25 and Top 26-50 firms.



# 4. Financing

## Lock up

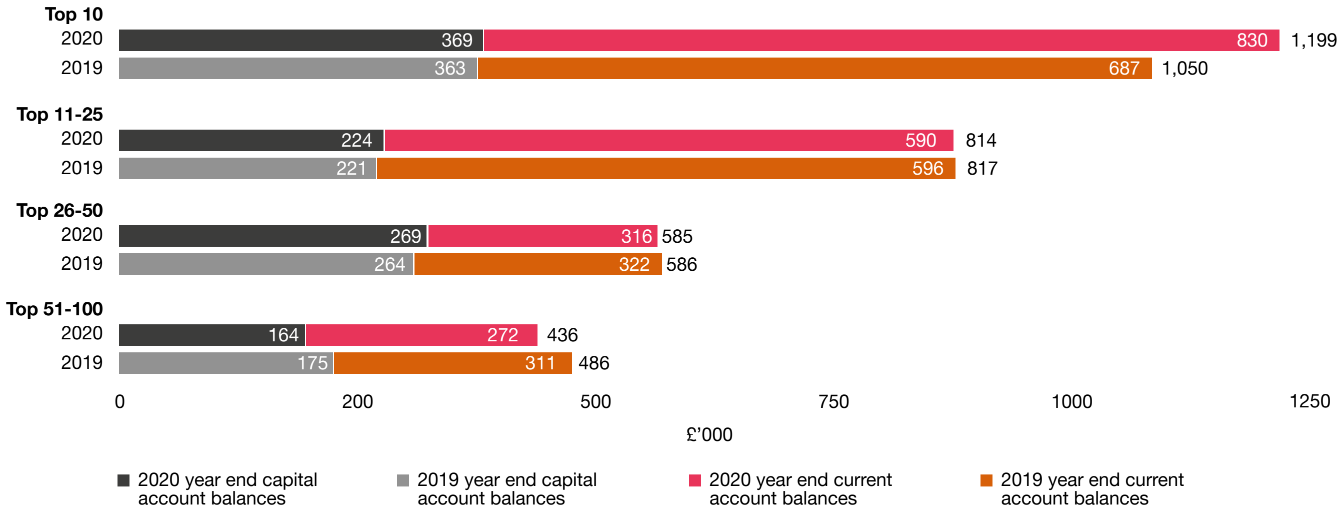
- The majority of law firms completing our survey have a 30 April year end and, therefore, will have benefited from the significant push on cash collections to improve the cash position post the onset of COVID-19. This is reflected in our data.
- All bandings improved the year end lock up position by between 2 and 14 days: Top 10 - 122 to 120 days; Top 11-25 - 121 to 115 days; Top 26-50 - 128 to 126 days; and Top 51-100 - 133 to 119 days.
- For the third consecutive year the Top 51-100 firms were the most improved, decreasing total year end lock up by 14 days (133 to 119). The Top 51-100 firms have historically been the worst performers by some distance, but this year has seen a step change in performance. This is a sign that efforts to tighten working capital processes are starting to bear fruit in this banding.
- Notwithstanding the year end and COVID-19 impact focus on cash, it is also evident that working capital improved during the year with all bandings reducing their average total lock up. The most significant improvements have been in the Top 11-25 (from 144 to 132 days) and Top 51-100 (151 to 132 days).
- There is still a significant gap between year end and average lock up performance, from 13 days in the Top 51-100 to 29 days in the Top 10.

## Finance

- Law firms have taken steps to engage with finance providers to draw down facilities.
- All bandings, with the exception of the Top 51-100, increased the proportion of their UK financing from external sources (Top 10: 17% to 18%; Top 11-25: 21% to 28%; Top 26-50: 12% to 17%). In some individual firms, the increase was substantial.
- Top 51-100 firms' external financing represented 14% of total financing, down from 15% in 2019.
- 65% of firms that saw a change in their external funding position used shorter-term finance vehicles (RCFs and short/medium term loans).
- Top 10 firms increased the average total of capital and current accounts per partner, by 14% to £1,199k (2019: £1,050k). This growth is wholly attributable to the increase in the average current account per partner (2020: £830k, 2019: £687k).
- Top 11-25 and 26-50 firms average capital and current account balance per partner was almost identical to prior year, totalling £814k and £585k respectively; however, this hides some substantial movements. For example, 36% of the Top 11-25 increased partner current accounts by more than 10% compared to last year.
- The average capital and current account levels in the Top 51-100 firms fell by 10% to £436k.
- For all Top 100 bandings, except the Top 11-25, the proportion of in-year partner profit distributions increased; however, this is likely to be reflective of a pre-COVID-19 outlook and we expect efforts to conserve cash will result in a different picture moving forwards.
- The prior year Top 11-25 firms' in year partner profit distribution was significantly higher than other bandings at 62% (other bandings 2019: 47% to 51%), but is now more in line at 53% (other bandings 2020: 53% to 56%).

## Year end capital and current account balances per full equity partner

Whilst the average current account per full equity partner has increased substantially in the Top 10, there has been little movement in Top 11-25 and 26-50 firms and a reduction in the Top 51-100. In the Top 50 bandings, average capital account per full equity partner is similar to last year.




## UK year end financing

External year end financing has increased across all bandings in the Top 50 with some individual firm increases being significant.

# 5. Governance and risk

## Board priorities for the next 2-3 years

- The top three board priorities for the next 2-3 years across the Top 100 firms are 'Financial and operational performance', 'Refreshing the firm's strategy', and 'D&I'.
- Financial and operational performance is of particular importance for firms outside the Top 10: 91% of Top 11-25, 93% of Top 26-50 and 56% of Top 51-100 firms rate this as one of their top three priorities. Conversely, only 33% of Top 10 firms did likewise.
- Top 10 firms are most focussed on D&I, with 82% ranking it as a top three priority. This compares to 45% in Top 11-25, 69% in Top 26-50 and 22% in Top 51-100 firms.
- Whilst refreshing the firm's strategy was scored highly across the Top 100, it was the weighting of the Top 26-50 firms that caused this; 67% ranked this as a top three priority. This compares to between 17% and 27% across the other bandings in the Top 100.

## Barriers to effective governance

- All bandings in the Top 100 highlighted 'lack of time/ capacity to deal with volume work' as the biggest factor that hinders improvement in their governance functions, with between 45% and 83% selecting this across the bandings. As regulation and stakeholder expectations continue to increase, it will be important for firms to overcome this challenge.
- In the Top 10, 83% also identified 'Overly complex governance structures which inhibit agile decision-making' as an area that also hinders governance improvement. This issue is clearly more relevant to the larger firms, with only 18%, 20% and 9% selecting this area in the Top 11-25, 26-50 and 51-100 firms respectively.

## Partnership culture

- A law firms governance structure is, in part, a manifestation of it's partnership culture. An average of 82% of Top 100 firms' equity partners elect their Senior Partner, 84% elect their Managing Partner, and 59% elect their supervisory / oversight board. It is clear that consultation and communication between leadership and its primary stakeholder group, equity partners, is an important aspect of partnership culture.
- Only a minority of firms have their equity partners elect practice group heads; no Top 10 firms and between 20% and 27% across the Top 11-25, 26-50 and 51-100 firms.

## Adopting good governance practices

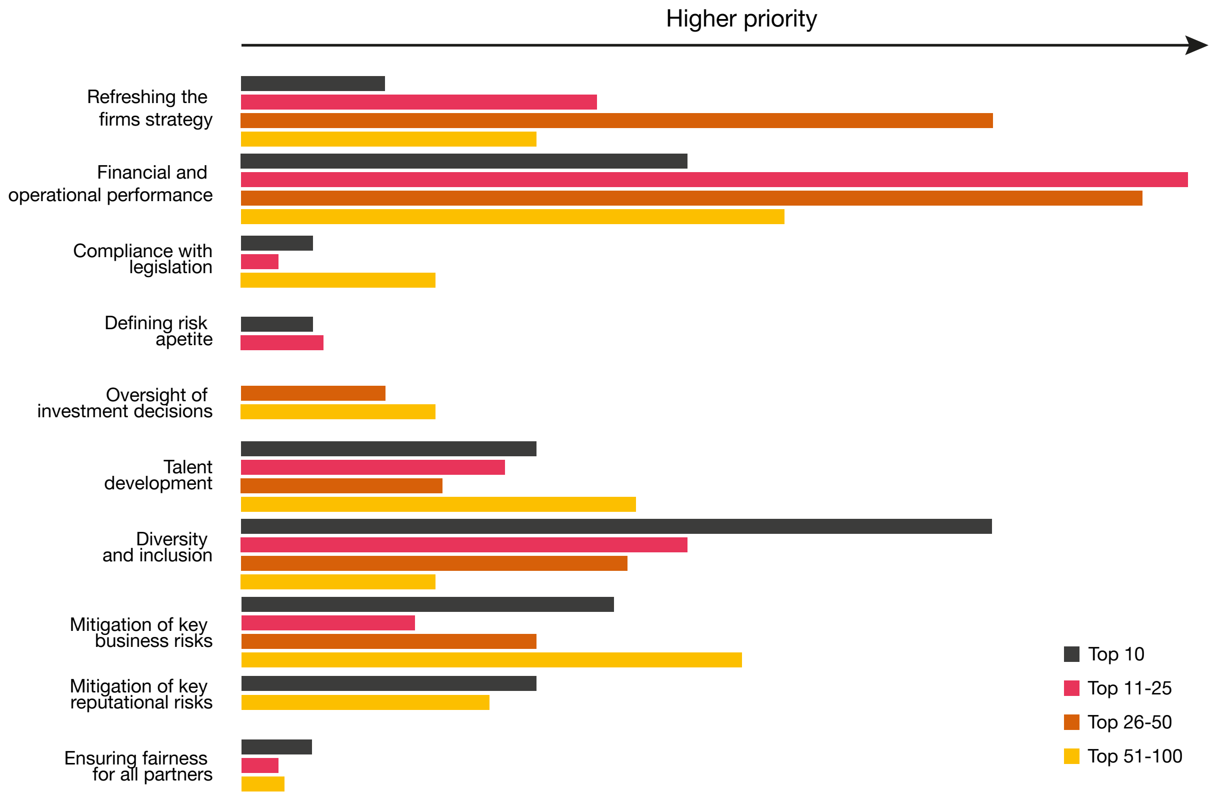
- A small number of law firms are voluntarily adopting governance best practices that are mandated in other organisations types (for example, listed entities). For example, independent non-executive finance professionals have been appointed to 33% of Top 10, 18% of Top 11-25 and 47% of Top 26-50 firms. No Top 51-100 firm stated they had such individuals in their governance party.
- 17% of Top 10 and 20% of Top 26-50 firms have also appointed independent non-executive lawyers to their boards, but none in the Top 11-25 and 51-100 firms.
- There is significant value in the role of an independent non-executive. They bring a different mindset to board discussions and can support by sharing external perspectives and providing objective and constructive challenge.
- On average, half of Top 100 firms oversee social and ethics matters at a board level, with 36% taking ownership for implementation. On average 24% of law firms delegate social and ethical responsibilities to a sub-committee of the board (ranging from 17% for Top 10 firms to 40% for Top 26-50 firms).

## Cyber risk

- Every respondent to our survey suffered a security incident this year and consistent with 2019, the most common attack method continues to be phishing.
- Criminals are evolving and developing techniques, and we've seen a huge increase in ransomware attacks this year. We expect this to continue in 2021.
- 'Cyber and Information Security' was added to our business support functions qualitative review for the first time this year and was reasonably well rated. Of the Top 100 firms, 44% rated it as a 'strength' and 54% considered this function to 'adequately support the business'. This is a positive indication that recent investments in these areas are paying off.
- There has been an improvement in participation by senior management in crisis management exercises (including a cyber attack). All senior management in Top 10 firms have completed such an exercise in the last year (2019: 83%). Top 11-25 and 26-50 firms have also improved this statistic to 55% (2019: 46%) and 79% (2019: 50%) respectively.
- There continues to be a significant number of firms who do not perform crisis management exercises at least annually: Top 11-25: 45%; Top 26-50: 21%; and Top 51-100: 36%.

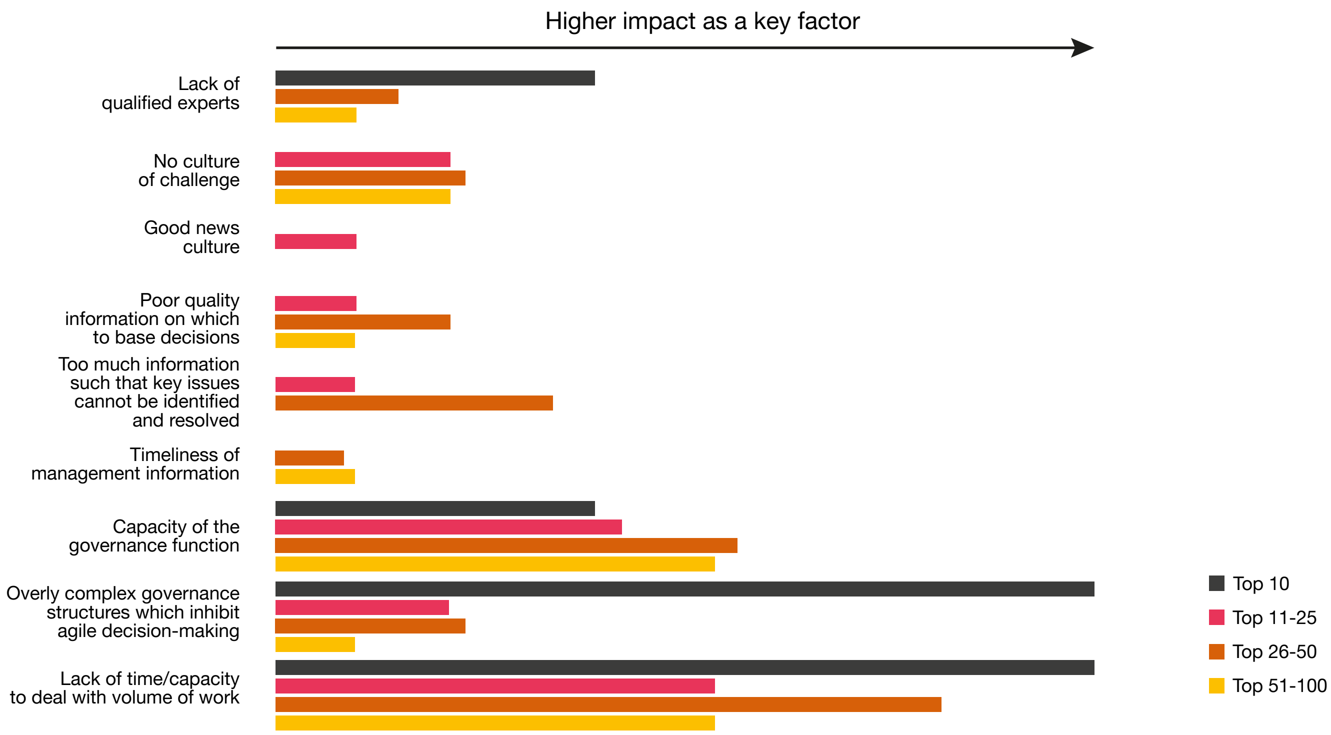
## Top priorities for those charged with governance

The key priorities for those charged with governance are 'Financial and operational performance' and 'Refreshing the firm's strategy' (except in Top 10). Top 10 firms are also very focussed on 'Diversity and inclusion'.




## Factors that hinder improvement of governance

The key factors that hinder governance improvements are 'Lack of time/capacity to deal with volume of work', 'Capacity of the governance function' and 'Overly complex structures which inhibit agile decision making', although the latter is focussed more on global firms.



# Appendix: Key performance indicators

## UK

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Top 10** | | | | | | |
| UK fees per chargeable hour (£)* | 328 | 283 | 297 | 302 | 315 | 331 |
| UK fees per full equity partner (£000) | 2,656 | 2,705 | 2,729 | 2,935 | 3,063 | 3,187 |
| UK fees per fee earner (£000) | 379 | 378 | 380 | 395 | 415 | 414 |
| UK profit per full equity partner (£000) | 1,067 | 1,068 | 1,043 | 1,066 | 1,120 | 1,067 |
| UK profit per fee earner (£000) | 157 | 154 | 152 | 152 | 155 | 148 |
| Profit margin (%) | 39.9 | 38.7 | 36.9 | 36.6 | 35.5 | 33.8 |
| Staff cost ratio (%) | 34.7 | 36.7 | 38.5 | 39.4 | 37.9 | 38.9 |
| 1->9 year PQE fee earner utilisation (hours) | 1,542 | 1,461 | 1,395 | 1,478 | 1,465 | 1,341 |
| Lock up days (year end) | 124 | 121 | 124 | 123 | 122 | 120 |
| Average number of full equity partners-UK | 140 | 143 | 147 | 142 | 146 | 151 |
| Average number of fee earners (incl. partners)-UK | 975 | 1,046 | 1,101 | 1,065 | 1,165 | 1,137 |

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Top 11-25** | | | | | | |
| UK fees per chargeable hour (£)* | 286 | 238 | 256 | 266 | 285 | 300 |
| UK fees per full equity partner (£000) | 2,239 | 2,160 | 2,277 | 2,416 | 2,491 | 2,473 |
| UK fees per fee earner (£000) | 296 | 289 | 290 | 303 | 325 | 321 |
| UK profit per full equity partner (£000) | 641 | 614 | 647 | 729 | 734 | 710 |
| UK profit per fee earner (£000) | 97 | 97 | 90 | 95 | 98 | 95 |
| Profit margin (%) | 29.2 | 28.2 | 27.7 | 28.8 | 28.5 | 27.5 |
| Staff cost ratio (%) | 40.3 | 40.6 | 42.5 | 41.8 | 41.1 | 41.4 |
| 1->9 year PQE fee earner utilisation (hours) | 1,366 | 1,333 | 1,272 | 1,309 | 1,347 | 1,289 |
| Lock up days (year end) | 111 | 113 | 121 | 122 | 121 | 115 |
| Average number of full equity partners-UK | 78 | 82 | 78 | 74 | 70 | 72 |
| Average number of fee earners (incl. partners)-UK | 741 | 715 | 722 | 644 | 653 | 575 |

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Top 26-50** | | | | | | |
| UK fees per chargeable hour (£)* | 223 | 203 | 210 | 213 | 228 | 223 |
| UK fees per full equity partner (£000) | 1,813 | 1,844 | 1,734 | 1,974 | 2,037 | 2,228 |
| UK fees per fee earner (£000) | 210 | 208 | 216 | 224 | 237 | 223 |
| UK profit per full equity partner (£000) | 406 | 397 | 415 | 467 | 516 | 467 |
| UK profit per fee earner (£000) | 55 | 51 | 56 | 61 | 68 | 55 |
| Profit margin (%) | 24.5 | 23.1 | 25.2 | 24.2 | 24.7 | 22.2 |
| Staff cost ratio (%) | 42.5 | 42.4 | 42.3 | 42.3 | 43.2 | 45.1 |
| 1->9 year PQE fee earner utilisation (hours) | 1,263 | 1,240 | 1,205 | 1,230 | 1,235 | 1,216 |
| Lock up days (year end) | 118 | 117 | 120 | 129 | 128 | 126 |
| Average number of full equity partners-UK | 51 | 51 | 53 | 59 | 59 | 57 |
| Average number of fee earners (incl. partners)-UK | 460 | 491 | 497 | 536 | 513 | 539 |

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Top 51-100** | | | | | | |
| UK fees per chargeable hour (£)* | 225 | 194 | 178 | 201 | 200 | 213 |
| UK fees per full equity partner (£000) | 1,847 | 1,708 | 1,627 | 1,630 | 1,959 | 1,792 |
| UK fees per fee earner (£000) | 181 | 181 | 169 | 183 | 188 | 207 |
| UK profit per full equity partner (£000) | 364 | 394 | 347 | 381 | 460 | 452 |
| UK profit per fee earner (£000) | 41 | 44 | 40 | 47 | 49 | 58 |
| Profit margin (%) | 21.2 | 22.4 | 23.0 | 24.6 | 22.9 | 26.3 |
| Staff cost ratio (%) | 43.6 | 42.8 | 45.6 | 44.7 | 45.3 | 44.7 |
| 1->9 year PQE fee earner utilisation (hours) | 1,061 | 1,050 | 1,038 | 1,122 | 1,122 | 1,139 |
| | | | | | | |
| Lock up days (year end) | 137 | 140 | 146 | 135 | 133 | 119 |
| | | | | | | |
| Average number of full equity partners-UK | 21 | 24 | 24 | 27 | 25 | 28 |
| Average number of fee earners (incl. partners)-UK | 205 | 209 | 219 | 229 | 330 | 244 |

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Outside top 100** | | | | | | |
| UK fees per full equity partner (£000) | 1,024 | 1,037 | 1,090 | 1,140 | 1,313 | 1,676 |
| UK fees per fee earner (£000) | 166 | 140 | 128 | 138 | 145 | 134 |
| UK profit per full equity partner (£000) | 213 | 233 | 210 | 269 | 333 | 330 |
| UK profit per fee earner (£000) | 45 | 36 | 28 | 35 | 37 | 27 |
| Profit margin (%) | 19.0 | 22.9 | 20.5 | 25.4 | 25.4 | 19.8 |
| Staff cost ratio (%) | 45.4 | 43.2 | 47.5 | 43.6 | 42.9 | 45.6 |
| 1->9 year PQE fee earner utilisation (hours) | 998 | 1,045 | 973 | 1,084 | 1,022 | 1,016 |
| | | | | | | |
| Lock up days (year end) | 163 | 135 | 154 | 139 | 134 | 131 |
| | | | | | | |
| Average number of full equity partners-UK | 16 | 15 | 14 | 16 | 15 | 11 |
| Average number of fee earners (incl. partners)-UK | 101 | 102 | 95 | 91 | 112 | 115 |

*Note: for 2015, UK fees per chargeable hour excluded full equity partner hours and for 2016 to 2020 it included full equity partner hours.

## Global

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Top 10** | | | | | | |
| Fees per all partners (£000) | 1,755 | 1,787 | 1,949 | 2,065 | 2,154 | 2,167 |
| Fees per fee earner (£000) | 362 | 352 | 379 | 408 | 410 | 387 |
| Profits per all partners (£000) | 692 | 723 | 790 | 810 | 916 | 804 |
| Profits per fee earner (£000) | 139 | 139 | 151 | 158 | 158 | 142 |
| Profit margin (%) | 37.8 | 38.7 | 38.3 | 37.9 | 38.0 | 35.2 |
| Staff cost ratio (%) | | 39.8 | 39.8 | 40.3 | 39.4 | 40.6 |
| Average number of partners-global | 475 | 480 | 477 | 473 | 481 | 489 |
| Average number of fee earners (incl. partners)-global | 2,253 | 2,393 | 2,390 | 2,354 | 2,640 | 2,666 |

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Top 11-25** | | | | | | |
| Fees per all partners (£000) | 984 | 982 | 1,039 | 1,052 | 1,102 | 1,162 |
| Fees per fee earner (£000) | 273 | 268 | 281 | 270 | 293 | 285 |
| Profits per all partners (£000) | 311 | 304 | 338 | 362 | 370 | 375 |
| Profits per fee earner (£000) | 87 | 82 | 91 | 93 | 98 | 92 |
| Profit margin (%) | 31.7 | 30.0 | 33.3 | 34.3 | 33.6 | 31.7 |
| Staff cost ratio (%) | | 42.0 | 42.6 | 42.0 | 43.0 | 44.1 |
| Average number of partners-global | 153 | 159 | 200 | 237 | 246 | 253 |
| Average number of fee earners (incl. partners)-global | 575 | 611 | 778 | 995 | 939 | 1,069 |

*Note: profit is stated before full and fixed share equity partner remuneration.

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