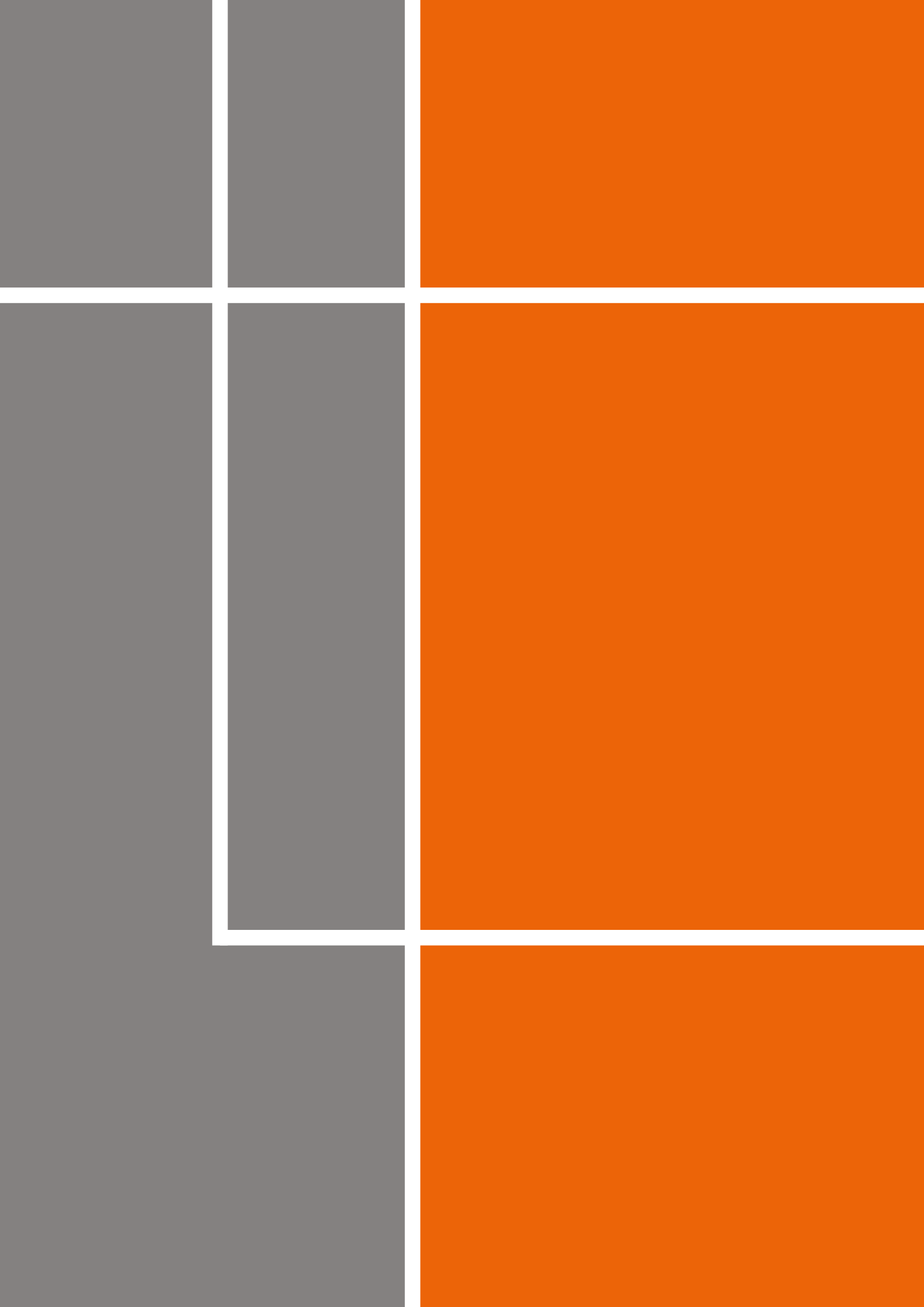


Resilience through change

PwC Law Firms' Survey 2018



**This is the 27th PwC survey on law firms.
The editorial team for 2018 consists of:**



David Snell

David leads our Law Firms' Advisory Group (LFAG). He works closely with and advises national and international law firms on all aspects of their accounting, finance, strategy and business issues.



Kate Wolstenholme

Kate is head of our business services sector and is a lead assurance partner within our LFAG. With a focus on the legal sector, she works with a number of international law firms on audit, accounting and strategy issues.



Leon Hutchinson

Leon is an assurance senior manager who works with a number of national and international law firm clients, advising them on accounting issues and SRA Accounts Rules compliance.



Catherine Usher

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



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 strategy and implementation.



Stephen Tebbett

Stephen is a partner in our specialist working capital management practice. He has a breadth of experience working hands on with clients to help them deliver significant cash flow improvements.

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

- Cost reduction and outsourcing
- Assurance and business advisory services
- Compliance with SRA Accounts Rules and associated regulatory requirements
- Mergers and acquisitions
- Direct and indirect taxation
- Working capital management
- Limited Liability Partnerships (LLPs) and other structuring advice
- Partner reward
- Strategic consultancy
- Employee and employer issues (reward structures and taxation)
- International taxation and accounting
- International restructuring
- 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 Jo Parr, Sanah Faridi, Colleen Dunn, Charlie Mirrington, Tom Oliver, Qian Song, Alyson Reeves, David Baxendale, Alex Quant, Dan Wicks, Dan Holmes, and Alice Johnson who contributed significantly to the production of this report.

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). 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 have 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. All key data and charts are available through our online tool which participants are able to access.

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 is not fully reproduced here or in the online benchmarking tool. If you would like further information in relation to the responses to any of the questions please contact one of our editorial team.

Definitions

US top tier – US headquartered firms where global revenues exceed £1bn (prior year restated to 2018 exchange rates for comparability).

UK top tier – UK headquartered firms where global revenues exceed £1bn (prior year restated to 2018 exchange rates for comparability).

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.

Bandings – Top 10, Top 11-25, Top 26-50 and Top 51-100 firms have been categorised by global fee income. The analysis for these bandings of firms has been adjusted to exclude high volume firms where their impact is considered significant.

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Introduction and key themes

Introduction

Despite current levels of political and economic uncertainty, 2018 was a strong year for the legal sector. Fee income growth exceeded that experienced in 2017, and a greater proportion of firms were able to translate this fee income growth into improved profitability. However, growing profits remains a key challenge for firms of all sizes, particularly in an environment where fee earner costs continue to rise and the pace of change requires significant investment to future-proof the firm.

Technology remains a key theme of this year's survey, bringing both opportunities and challenges. More firms are taking steps to develop and utilise technology, whilst also driving efficiencies in working practices, getting the best use of office space in the right locations and innovating through new legal services. However, the challenge for many is in moving technological developments from research and piloting into full scale implementation. Meanwhile, cyber attacks are becoming increasingly common and Boards now see this as a much greater and real risk to their business. This presents a major threat for the legal sector, as firms hold significant client funds and information that is attractive to fraudsters and other criminals.

From a workforce perspective we are seeing new dynamics and challenges. In response to productivity issues in previous years, this year's survey shows increases in both actual and target chargeable hours, combined with some decrease in fee earner numbers. However, this increased pressure on the workforce sits alongside demands for new working lifestyles from the younger generation of lawyers. Firms are responding by introducing new initiatives, including flexible and virtual working, work-life balance measures, and greater alignment of strategy with employee values. The focus on diversity continues, with publication of gender pay gap shining a stronger light on the steps that still need to be taken. At the same time, firms are having to consider the workforce of the future, and the impact that automation, artificial intelligence, and extension of traditional legal services will have on the number and skillset of future partners and employees.

Despite the geo-political climate, client demand for truly global capability continues to drive merger activity in the sector, with a number of firms looking to international expansion, both to support their client base and to take advantage of growth opportunities outside the UK. Amongst the mid-tier, UK to UK mergers also provide the opportunity to leverage scale to facilitate investment and innovation.

The uncertainty of Brexit, of course, looms over the legal sector. In the short term, firms are seeking to capitalise on Brexit-related advisory work, though some have identified the risk of a significant negative effect on the sector in the medium and longer term due to the knock-on impact of Brexit on the wider economy. As well as the impact on financial performance, firms are focusing on the potential impact to the wider regulatory environment in which they operate, their organisational structure and their people.

The global perspective

Global performance has been generally positive in 2018. Top 10 average fee income has grown 5% (2017: 8%) to an average of £980m, and for Top 11-25 firms growth exceeded 2017 levels at 11% (2017: 7%) to £250m. Profit growth is also impressive for Top 11-25 firms at 13% (2017: 7%), but less so for Top 10 firms at 2% (2017: 10%).

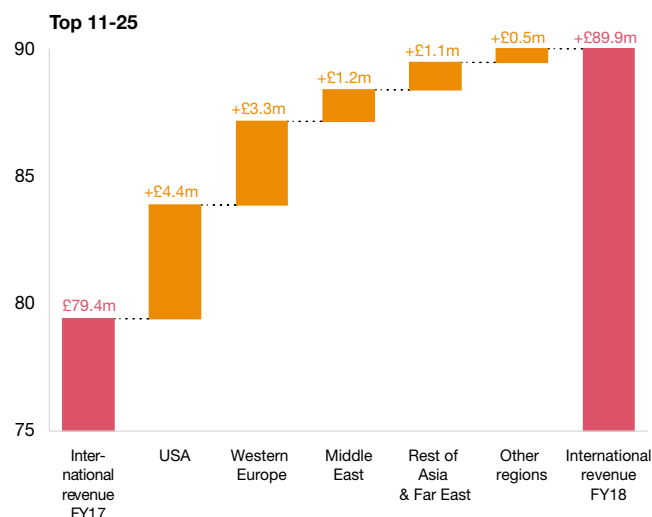
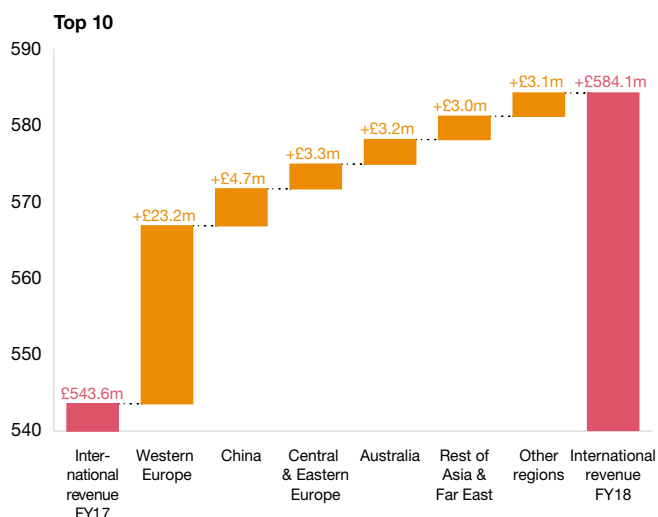
It is important to recall that in 2017, global law firms headquartered in the UK benefited significantly from the weakening of Sterling, most notably against the Euro and US dollar. The impact of currency on Top 10 firms in 2018 was minimal, whilst in 2017 revenue benefitted by 4.9% and profits by 4.4%. Adjusting for this, Top 10 firm performance held up well in 2018.

This year, growth in global fee income for Top 10 firms was driven by international offices. They represent 83% of total global fee income growth prior to impact of exchange, compared to 50% in 2017. It is the established Western Europe region that provided the bulk of international fee income growth at 57%, with China the next best performing region at 12%. Global fee income growth in Top 11-25 firms was much more spread, with UK offices providing 55% and international offices 45%.

Our results are analysed against the backdrop of the differing partnership models adopted by global firms, which can make margin comparisons difficult. If we consider global net profit margin before full and fixed share equity partner remuneration, the Top 10 suffered a 0.4 percentage point reduction to 37.9% which represents a second year of deteriorating margins (2016: 38.7%). In contrast, Top 11-25 global firms have improved this measure by 1 percentage point to 34.3%, so closing the profitability gap on their bigger rivals.

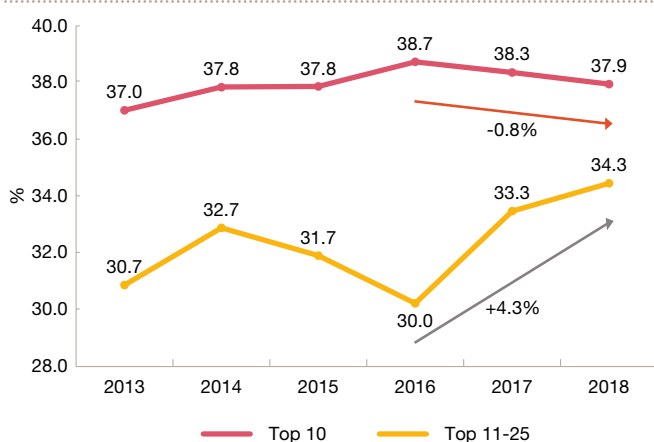
The above is impacted by the full equity partner and fixed share equity partner mix. Whilst this has remained consistent for Top 10 firms (at 80%/20% in both 2018 and 2017), there has been a definite shift for Top 11-25 firms (from 61%/39% in 2017 to 49%/51% in 2018) and this has been caused by a slight change in mix of firms and an apparent change in partnership models for a small number of firms in that banding.

Movement in international revenues by region



Once fixed share equity partner remuneration is taken into account, the impact on margins between the Top 10 and 11-25 firms is less significant. Top 10 firms' average net profit margin (after fixed share partner remuneration) has fallen from 35.0% to 34.7%, whilst Top 11-25 firms achieved a small improvement from 24.1% to 24.3%. At this level, a notable performance gap of 10.4 percentage points exists between the bandings.

Trend in global profit margins before full and fixed share equity partner remuneration



The debate around international strategy remains. Firms that have invested in international markets have seen greater fee income growth, and for the first time international offices have contributed significantly more than the UK to fee income and profit growth in Top 10 firms. There are also certain regions (USA and Australia) that are ahead of the UK in terms of utilisation. However, net profit margins continue to lag behind those of the UK.

US top tier performance continues to significantly exceed that of the UK top tier (note: we define a top tier firm as one with global revenue greater than £1bn). The performance gap has also widened from 2017 to 2018 in respect of most KPIs. Some highlights on the difference in performance include:

- UK top tier average PEP of £1,176k is 41% less than the US top tier PEP of £1,994k.
- Only one UK top tier firm managed to exceed the average profit margin performance for all US top tier firms of 45.9%, and this was exceeded by only 0.1 percentage points.
- If an average UK top tier firm could match the average profit margin of a US top tier firm, net profit would increase by £137m (26% of 2018 net profit) and PEP by £277k (24% of 2018 PEP).

The reason US top tier firms are able to outperform their UK counterparts is down to two main factors: higher fee earner utilisation rates, and the ability to pass on increased costs to clients through regular rate increases.

Global – Average percentage profit and loss account

	Top 10		Top 11-25	
	2018	2017	2018	2017
	%	%	%	%
Fee income	100	100	100	100
Staff costs – fee earners	26.5	25.8	28.2	28.5
Staff costs – non-fee earners	13.8	14.0	13.8	14.1
Property costs	8.6	8.3	8.5	8.3
IT revenue costs	2.4	2.5	2.6	2.8
Marketing & BD costs	1.4	1.5	2.1	2.0
Finance function costs	0.9	0.9	0.8	1.0
Depreciation	1.9	2.1	1.8	2.0
Insurance costs	1.0	1.0	1.1	1.5
Bad debts and disbursements	1.1	1.1	1.6	1.2
Foreign exchange differences	0.5	0.3	0.3	0.0
All other costs	4.0	4.2	4.9	5.3
Profit before fixed share equity remuneration	37.9	38.3	34.3	33.3
Fixed share equity partners' remuneration	3.2	3.3	10.0	9.2
Net profit margin	34.7	35.0	24.3	24.1

UK financial performance

At first glance, performance appears to have improved significantly in 2018, with higher fee income growth evidenced across the sector relative to 2017. Almost 90% of Top 100 firms achieved fee income growth, and some 40% of firms reported double digit growth.

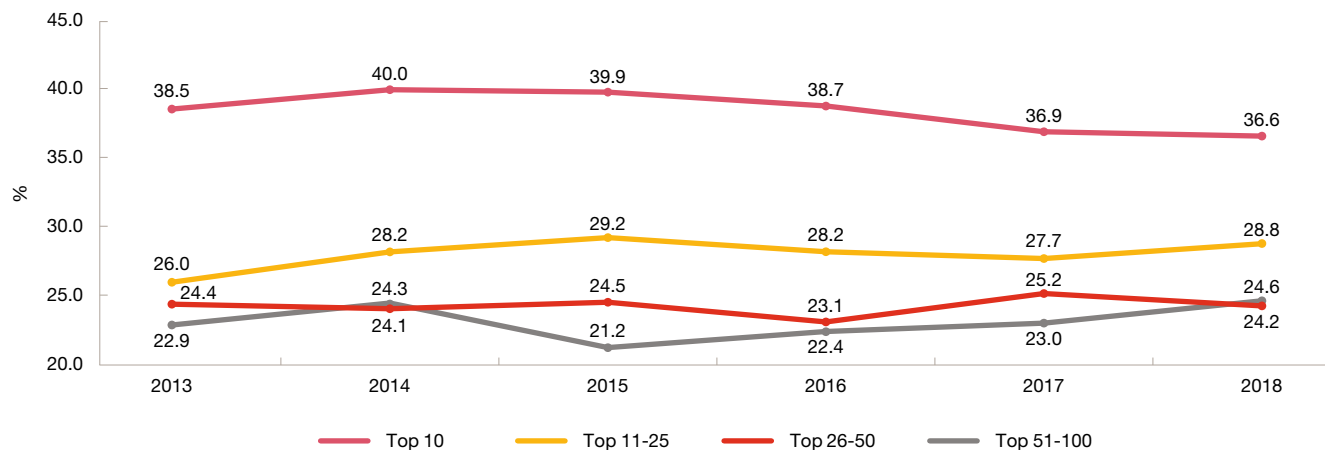
However, ongoing challenges in UK law firm performance remain evident as increased fee income has not necessarily translated to overall profit improvement; indeed, profit margin erosion has continued for many as firms struggle to contain costs. In particular, higher staff costs continue to adversely impact margins, predominantly in larger firms: staff cost as a percentage of fee income grew from 38.5% to 39.4% across the Top 10, continuing a four year trend. Increased salary costs are still being driven upwards by US firms and this inevitably impacts across the whole sector as firms compete to retain and attract the best staff.

Whilst the overall staff cost ratio has fallen slightly outside the Top 10, this is due to efforts to manage non-fee earner costs through controlling support headcount.

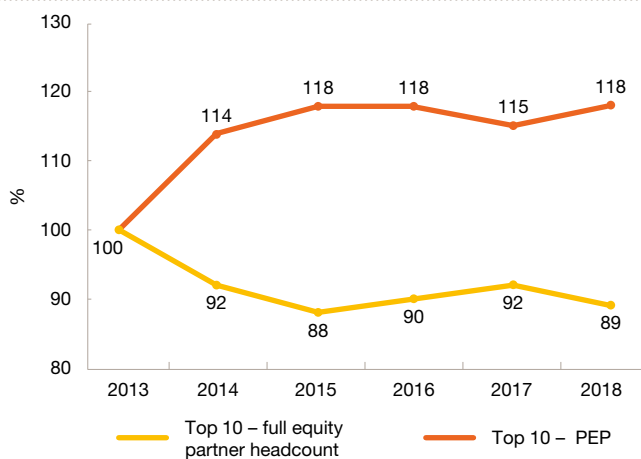
Almost 30% of Top 100 firms experienced a reduction in profit in the year (on top of a record 48% in 2017). For Top 10 firms, profit margin has fallen for the fourth consecutive year to 36.6% (2017: 36.9%, 2014: 40.0%). Top 11-25 firms are closing what was once a much bigger performance gap on the net profit margin KPI – now 7.8 percentage points behind the Top 10 (compared with 11.8 percentage points in 2014). There has been a convergence of performance across the Top 26-50 and 51-100 firms over the last four years with the Top 51-100 banding actually outperforming the average margins achieved by the Top 26-50 in 2018 (24.6% vs 24.2%).

On average, all bandings in the Top 100 have improved PEP and at individual firm level most have maintained and increased this KPI. In the Top 25 firms this is largely as a result of managing partner headcount.

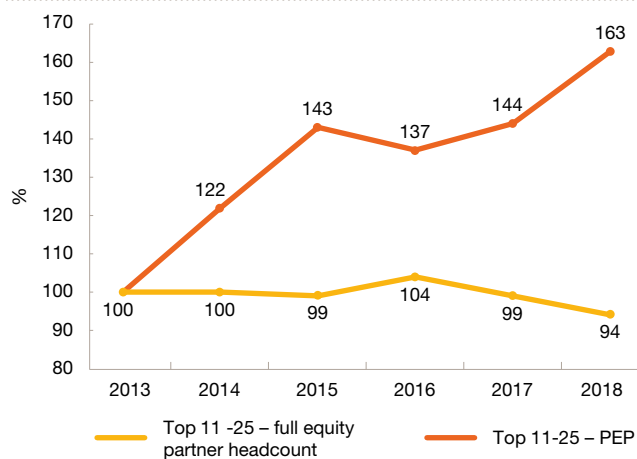
Trend in UK net profit margins



UK – trend in full equity partner headcount and PEP – Top 10 (2013 base: 100)



UK – trend in full equity partner headcount and PEP – Top 11-25 (2013 base: 100)



UK - Average percentage profit and loss account

	Top 10		Top 11-25		Top 26-50		Top 51-100	
	2018	2017	2018	2017	2018	2017	2018	2017
	%	%	%	%	%	%	%	%
Fee income	100	100	100	100	100	100	100	100
Staff costs – fee earners	26.7	25.5	28.3	28.2	27.8	27.6	30.4	31.1
Staff costs – non-fee earners	12.7	13.0	13.5	14.3	14.5	14.7	14.3	14.5
Property costs	8.7	8.5	7.7	8.3	9.1	8.3	8.0	8.0
IT revenue costs	3.1	3.0	2.8	3.2	3.0	3.6	3.0	3.3
Marketing & BD costs	1.2	1.4	1.9	1.9	2.0	2.5	2.2	3.0
Finance function costs	0.9	1.0	0.6	0.8	0.6	1.0	0.7	0.8
Depreciation	1.9	2.1	1.9	2.2	2.5	2.0	1.8	1.7
Insurance costs	1.2	1.2	1.2	1.4	1.8	1.9	2.3	2.1
Bad debts and disbursements	1.0	0.9	1.1	1.0	1.1	0.9	1.2	0.8
Foreign exchange differences	0.5	0.4	0.0	(0.1)	0.0	(0.2)	0.0	0.0
All other costs	2.4	2.5	6.0	4.8	3.8	4.0	4.7	5.1
Profit before fixed share equity remuneration	39.7	40.5	35.0	34.0	33.8	33.7	31.4	29.6
Fixed share equity partners' remuneration	3.1	3.6	6.2	6.3	9.6	8.5	6.8	6.6
Net profit margin	36.6	36.9	28.8	27.7	24.2	25.2	24.6	23.0
<i>Staff cost ratio (all staff costs)</i>	<i>39.4</i>	<i>38.5</i>	<i>41.8</i>	<i>42.5</i>	<i>42.3</i>	<i>42.3</i>	<i>44.7</i>	<i>45.6</i>
<i>Staff cost ratio (all staff, inc. FSEP costs)</i>	<i>42.5</i>	<i>42.1</i>	<i>48.0</i>	<i>48.8</i>	<i>51.9</i>	<i>50.8</i>	<i>51.5</i>	<i>52.2</i>

Business support

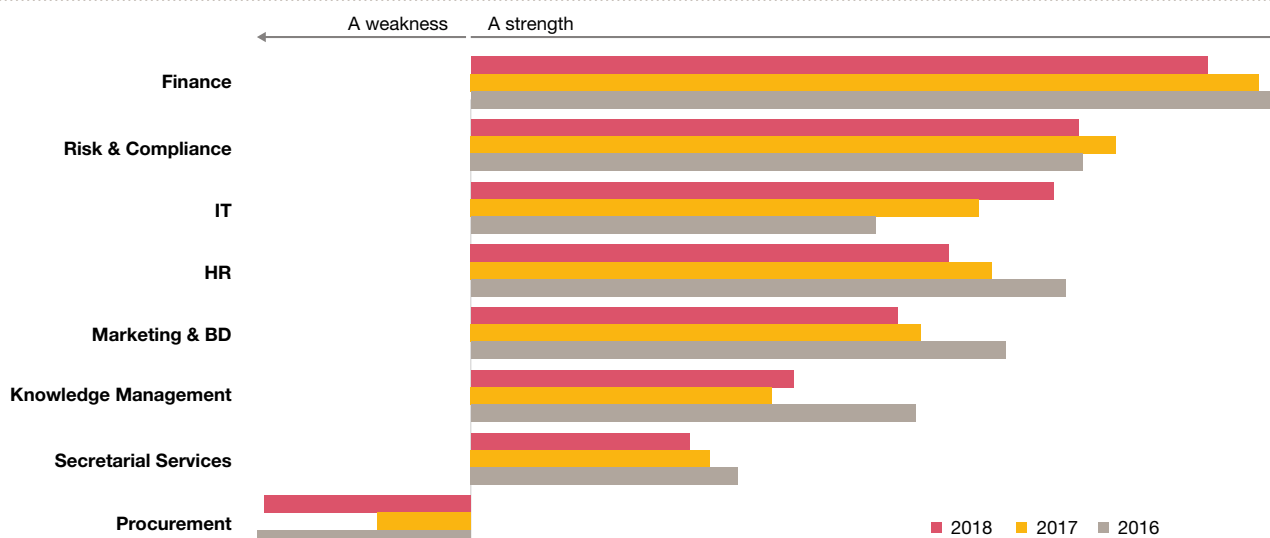
Consistent with the 2017 survey results, the top three priorities for business support are 'Use of technology', 'Improvements in legal service offering' and 'Standardising and centralising of processes'. The area that has grown the most in respect of business support priorities is the use of 'data analytics to make informed and timely decisions'. It will be interesting to see how Artificial Intelligence is developed and used in the legal sector as its adoption becomes more common place over the short and medium term.

Speed of technological change is clearly of great concern and it is critical that firms continue to leverage new technologies that enable them to disrupt their traditional business and operating models. It's good to see the sector showing a marked increase in the maturity of digital and emerging technology, most notably Artificial Intelligence, Smart Contracts and Blockchain Solutions. But for many, these technologies are still in the pilot stages reflecting the challenges of operationalising and commercialising new technologies.

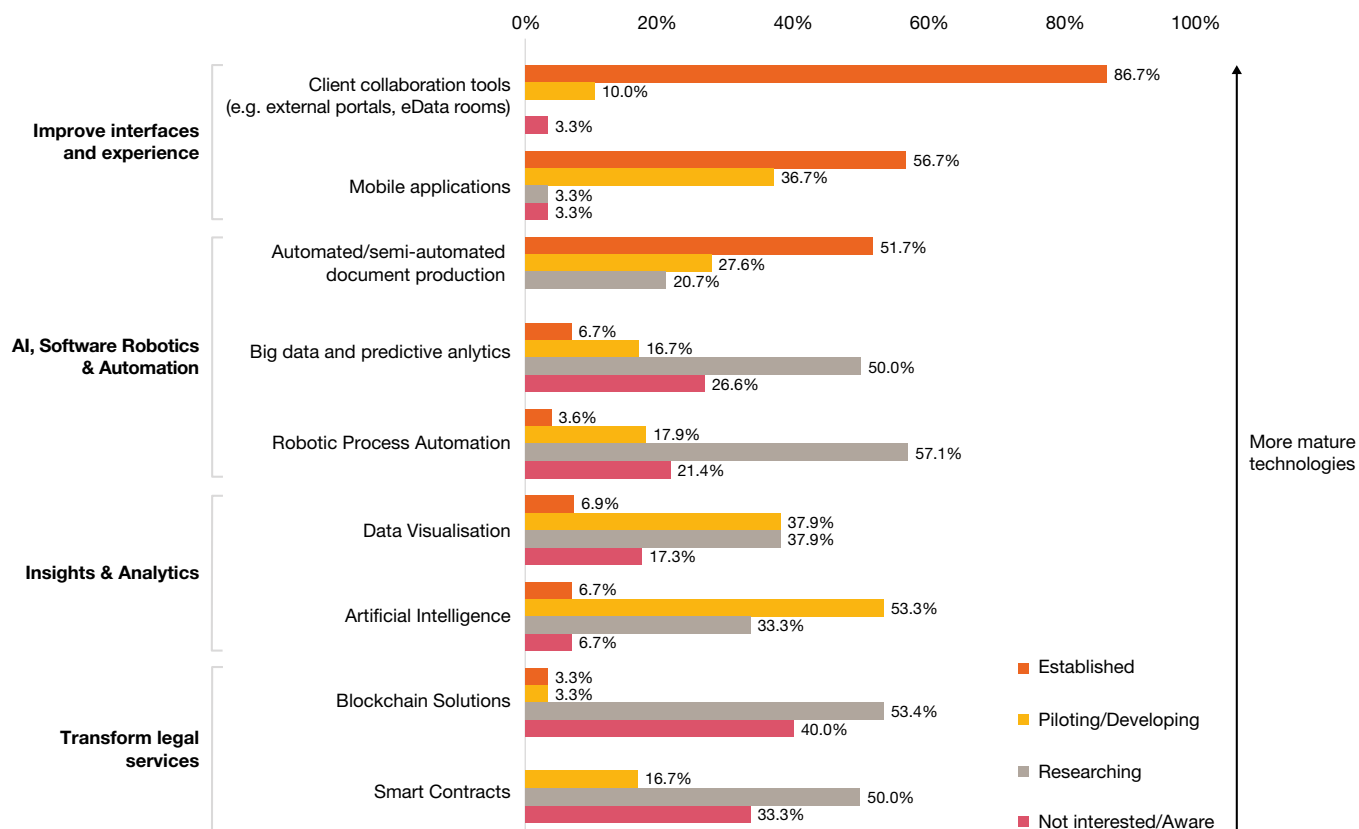
The best finance teams are balancing the delivery of effective finance operations and provision of business insight to the practice. This is evidenced by 'pricing & profitability' being the top ranked priority for finance, followed closely by 'working capital'. Might next year be the first year we see a much needed improvement in both?

It's encouraging to see the perceptions of the IT function improving (for the fourth consecutive year). However, the need to fix 'foundation IT' such as practice management systems (PMS), human resource systems (HR), and client and matter inception systems (CMI), is inhibiting investment in more strategically disruptive technologies. With a wave of firms needing to address PMS replacements between now and 2022 (a hard deadline associated with a systems end of life), often coupled with improvements to CMI, HR and CRM, firms need to ensure appropriate levels of funding are secured, whilst taking an honest view of the available bandwidth and capability to implement these solutions. In particular, having a specialist programme and change management capability and treating these programmes as a business change (not simply a technology implementation) are essential if firms are to succeed.

Qualitative assessment of support functions (Top 100 firms)



Has your firm established the following digital and emerging technologies? – Top 100 firms



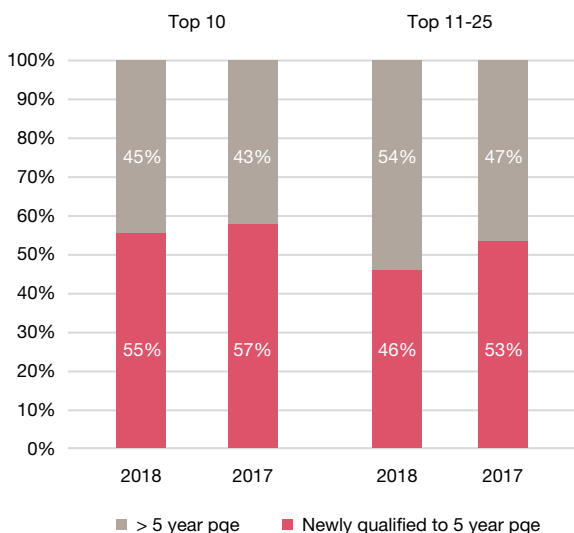
People

This year's survey shows that workforce management and remuneration structuring continue to represent key challenges at the Board level. Finding the right level and mix of staff is critical to delivering improved profitability, particularly in a market that is undergoing significant change.

We have seen a trend of decreasing UK fee earner numbers in many firms this year, particularly in the Top 25 firms (Top 10: by 3%, Top 11-25: by 11%) and mainly at the junior fee earner level. This has had a knock on impact of increased chargeable hours across all bandings and the vast majority of grades, whilst target hours have also increased. This is coupled with tight management of partner numbers and follows last year's focus on achieving efficiency and improving profitability through reduction of business support headcount.

These statistics point to an improved focus on resource management. However, given the limited effect on profit margins, continued focus is required to ensure that optimal mix of fee earners is achieved so that the right work is done by the right people. The > 5 year pqe grade represents a growing proportion of fee earner headcount in the Top 25, suggesting an increasing and expensive bottle-neck at this grade. The survey shows that the average cost per fee earner has increased, reflecting both the war for talent as UK firms seek to compete with US counterparts, and an increasingly senior mix of staff.

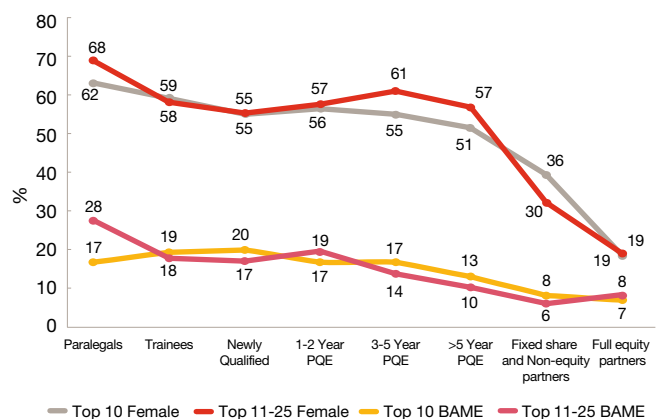
Fee earner headcount mix



Firms across all bandings continue to move towards more performance oriented partner reward models and away from the traditional lock-step model. Performance targets vary, but profit is a prevalent metric across all bandings. Working capital performance appears less widespread as a KPI despite the required focus on lockup. Ensuring that the approach to partner reward and performance management incentivises the right behaviours is vital for Boards in driving their strategy forward.

Diversity and in particular gender equality continue to be noted as board level priorities; however, progress remains slow. Female representation at partner level has increased, albeit marginally. Over the last 5 years it is the Top 51-100 firms that have achieved greater progress than the Top 50 bandings, where the proportion of female partners is still below 20%. The pattern of decreasing female representation further up the organisation is also mirrored for BAME employees. Initiatives that firms are adopting to support equality of career progression include mentoring/sponsorship initiatives, introduction of flexible working practices and widespread unconscious bias training. Additionally, a number of firms are focusing on raising awareness of mental health and initiatives focused on well-being, social inclusion and gender identity.

Diversity cascade (% representation)



At the end of the first year of disclosures under the new UK gender pay gap reporting requirements, the survey shows that law firms are taking differing approaches to whether their reported gender pay gap includes partner pay or not. Additionally, more requirements may be on the horizon, with potential future reporting on the BAME and disability pay gaps amongst a number of initiatives highlighted for future consideration. These new reporting requirements will not only broaden the public and governmental scrutiny on firms, but bring new challenges as organisations struggle to collect information in an area where data quality is notoriously patchy.

Headcount

	Top 10			Top 11-25			Top 26-50			Top 51-100		
	Av. 2018	Av. 2017	% change 2017-18	Av. 2018	Av. 2017	% change 2017-18	Av. 2018	Av. 2017	% change 2017-18	Av. 2018	Av. 2017	% change 2017-18
			%			%			%			%
Full equity partners	142	147	-3	74	78	-5	59	53	11	27	24	13
Fixed share equity partners	58	53	9	59	61	-3	66	58	14	15	18	-17
Non-equity partners	1	2	-50	16	35	-54	1	2	-50	12	12	0
Total Partners	201	202	0	149	174	-14	126	113	12	54	54	0
> 5 year ppe	249	254	-2	191	171	12	136	142	-4	53	52	2
3-5 year ppe	128	120	7	82	87	-6	50	44	14	26	21	24
1-2 year ppe	132	152	-13	50	69	-28	43	41	5	18	19	-5
Newly qualified	48	63	-24	29	37	-22	24	18	33	10	9	11
Legal executives and paralegals	166	171	-3	90	124	-27	117	101	16	49	45	9
Trainees	140	139	1	53	60	-12	40	38	5	19	19	0
Total fee earners (including partners)	1,064	1,101	-3	644	722	-11	536	497	8	229	219	5
Business services and secretaries	805	770	5	377	400	-6	350	287	22	149	147	1
Total	1,869	1,871	0	1,021	1,122	-9	886	784	13	378	366	3

Chargeable Hours

	Top 10			Top 11-25			Top 26-50			Top 51-100		
	Av. 2018	Av. 2017	% change 2017-18	Av. 2018	Av. 2017	% change 2017-18	Av. 2018	Av. 2017	% change 2017-18	Av. 2018	Av. 2017	% change 2017-18
			%			%			%			%
Full equity partners	1,185	1,101	8	934	908	3	930	911	2	960	910	6
Fixed share equity partners	1,156	1,081	7	956	927	3	988	940	5	929	859	8
Non-equity partners	-	-	-	981	986	-1	1,004	865	16	1,056	1,027	3
> 5 year ppe	1,423	1,380	3	1,248	1,195	4	1,213	1,155	5	1,080	1,006	7
3-5 year ppe	1,510	1,410	7	1,349	1,349	0	1,239	1,233	1	1,146	1,025	12
1-2 year ppe	1,500	1,396	7	1,331	1,273	5	1,238	1,227	1	1,139	1,082	5
Newly qualified	1,462	1,437	2	1,302	1,166	12	1,096	1,126	-3	1,107	973	14
Legal executives and paralegals	967	933	4	1,042	1,013	3	966	1,032	-6	1,012	867	17
Trainees	1,183	1,039	14	1,081	1,073	1	944	934	1	905	729	24

Financing

A number of factors have caused law firms to re-appraise their financing arrangements during the year. These include the need to fund investment in systems and new technologies, workplace changes or simply the need to re-visit financing levels and structures that have been in place for some time.

There has been limited movement in capital account balances across most bandings with a decrease per partner outside the Top 10. We assume this reflects an increase in the profile of junior full equity partners who are investing less capital, rather than a planned per capita reduction.

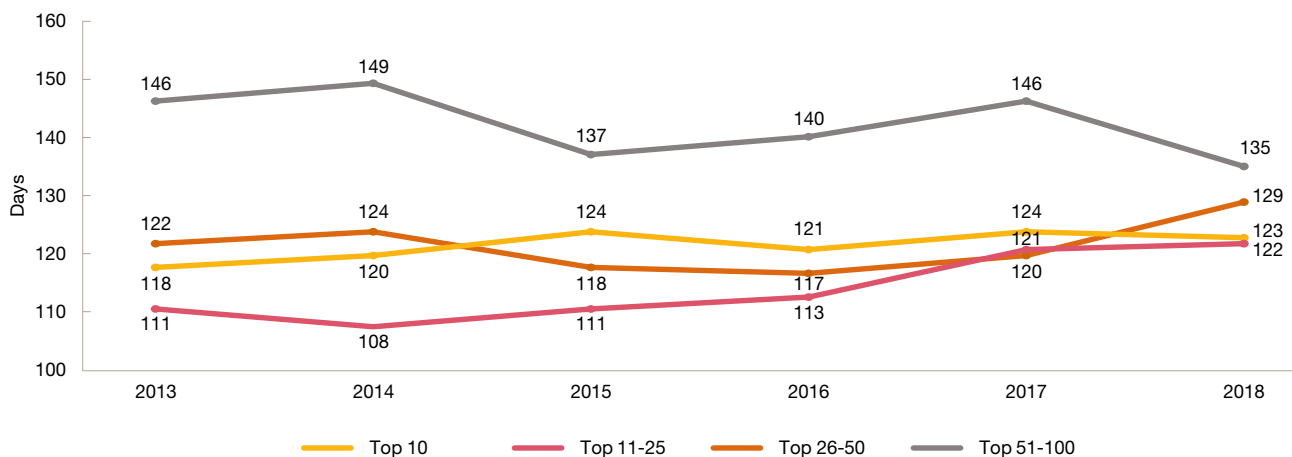
There has, though, been a general increase in UK current account balances across most firms. The only banding not showing an average increase is the Top 26-50 (down 26% to £240k). The rise in current account balances is reflective of (i) increasing profits for a number of firms; and (ii) a delay in profit distribution; for example, in Top 11-25 firms, on average, profit distribution in the year profit was earned has fallen from 58% in 2017 to 49% in 2018. This is now significantly less than the 55% applied, on average, by Top 10 firms.

The legal sector remains relatively attractive for providers of finance and high street banks, whether through direct funding or through financing of partner capital. Direct external funding remains low at between 18% and 21% of total funding across the Top 100 bandings. It remains to be seen whether the need to invest more heavily in the future will result in more firms taking the direct external funding route in the coming years, or perhaps the IPO opportunity that we have seen some firms pursue recently.

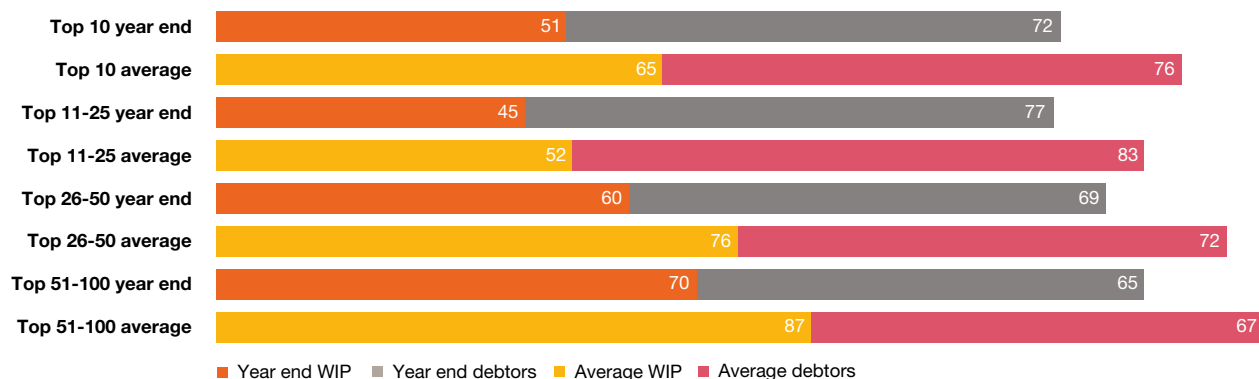
Against this relatively benign funding environment, the high level of lock up within firms has been a consistent negative theme for many years. Despite broad acknowledgment that this is an industry wide issue, the statistics continue to worsen year on year.

It is not uncommon for larger firms to be running on average lock up of 5-6 months. There are many factors contributing to this, but one contributor is the challenge of managing multiple e-billing platforms. Firms are presently acting as a funding source for their clients and this should be factored into pricing discussions. As the need for finance grows, it is clear that a solution needs to be found to reduce lock up through the year.

Trend in average UK year end total lock up days



UK year end and average WIP and debtor days

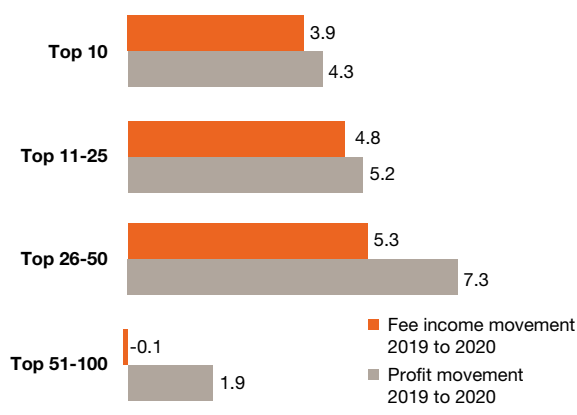


The future

What does the future hold for UK law firms? It's with some certainty that we can say the competitive nature of the sector will remain. There also will be a continuing need to invest in technology, and new entrants, along with US law firms, will look to disrupt. Further, the challenges of Brexit and the Cyber threat will not go away.

Despite the challenges, law firms are generally optimistic about the short term. None of the firms who responded to our survey expect a fee income or profit decline in the period 2018 to 2019. A significant number also expect profit growth to outstrip fee income growth in the period 2019 to 2020. But based on past record, these expectations may be considered too optimistic; for example, at least a third of Top 100 firms experienced profit reductions over the last three years.

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



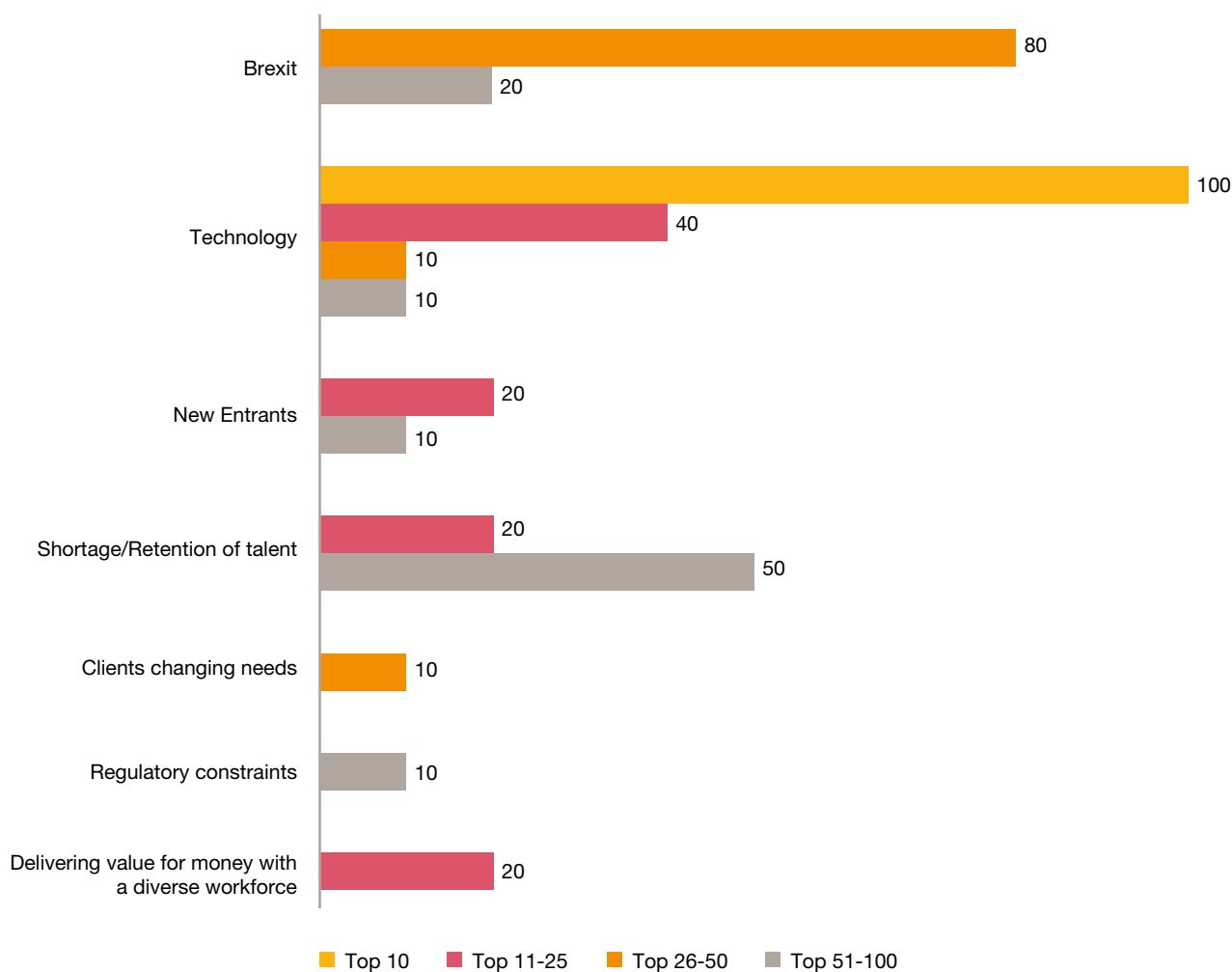
Will mergers help deliver profit growth? A number of firms are considering merger between now and 2020, including 40% of Top 10, 27% of Top 11-25 and 46% of Top 26-50 firms. Merger types do vary, with Top 10 firms looking to non-UK based entities (perhaps to expand a US footprint), whilst mid-tier firms are focused on smaller UK mergers.

There are many threats to law firms achieving their growth ambitions, but those that cause the biggest concern are Brexit, shortage of talent, cyber threats and technology.

Our survey received varying answers by size of firm when we asked what was the one key challenge facing the legal sector over the period from now until 2020. All Top 10 firms identified technology, as did 40% of Top 11-25 firms. However, 80% of Top 26-50 and 50% of Top 51-100 firms view Brexit and shortage/retention of talent as the key challenges respectively.

We set out on page 13 the factors law firms should consider in respect of the most significant threats they have identified.

What is the most significant challenge facing the legal profession over the period from now until 2020



We note in respect of Brexit specifically, a significant number of firms have set up a taskforce or committee to deal with the regulatory, structural and people aspects of Brexit and this is most prevalent in larger firms. 100% of the Top 10 firms say they have a committee that is dealing with regulatory and structural aspects, and 86% on people aspects. In Top 11-25 firms, this falls to 73% (regulatory), 64% (structural) and 36% (people). For those firms with limited focus to date, it will be imperative to respond soon.

These are certainly challenging, but exciting times in the legal sector. We will continue to see change. We will continue to see new entrants. We will continue to see exciting and new technology. Successful firms will need to demonstrate both agility and resilience through these challenging times.



Brexit

- What changes in structure in respect of EU offices will be required?
- Will processes and procedures need updating to adapt to a new regulatory environment?
- Will the firm's people be able to move freely to work throughout the EU?
- With the current outcome on Brexit still very much an unknown, is the firm ready to quickly adapt upon conclusion of Brexit negotiations?
- Is the firm ready and able to respond to the opportunities that Brexit will bring?



Shortage of talent

- Is there a process to spot and nurture talent?
- Is there clear career progression so that such talent can see how they will progress through the firm?
- Is there a flexible working culture that meets the needs of the workforce?
- Is there a policy on hiring and attracting new talent?
- Is the total package to employees, above cash remuneration, made clear?
- Does the firm communicate enough and in the right way with its employees?



Cyber threats

- If your firm were to experience a cyber event, how agile will it be to respond and recover quickly?
- Are Board members aware of their role and what they would need to do in response to a cyber event?
- Is there a clear documented business disaster recovery and business continuity plan that has been tested in at least the last twelve months?
- Would all employees know what to do in a cyber event?
- Have employees received adequate training in the last twelve months on their role in avoiding a cyber event?

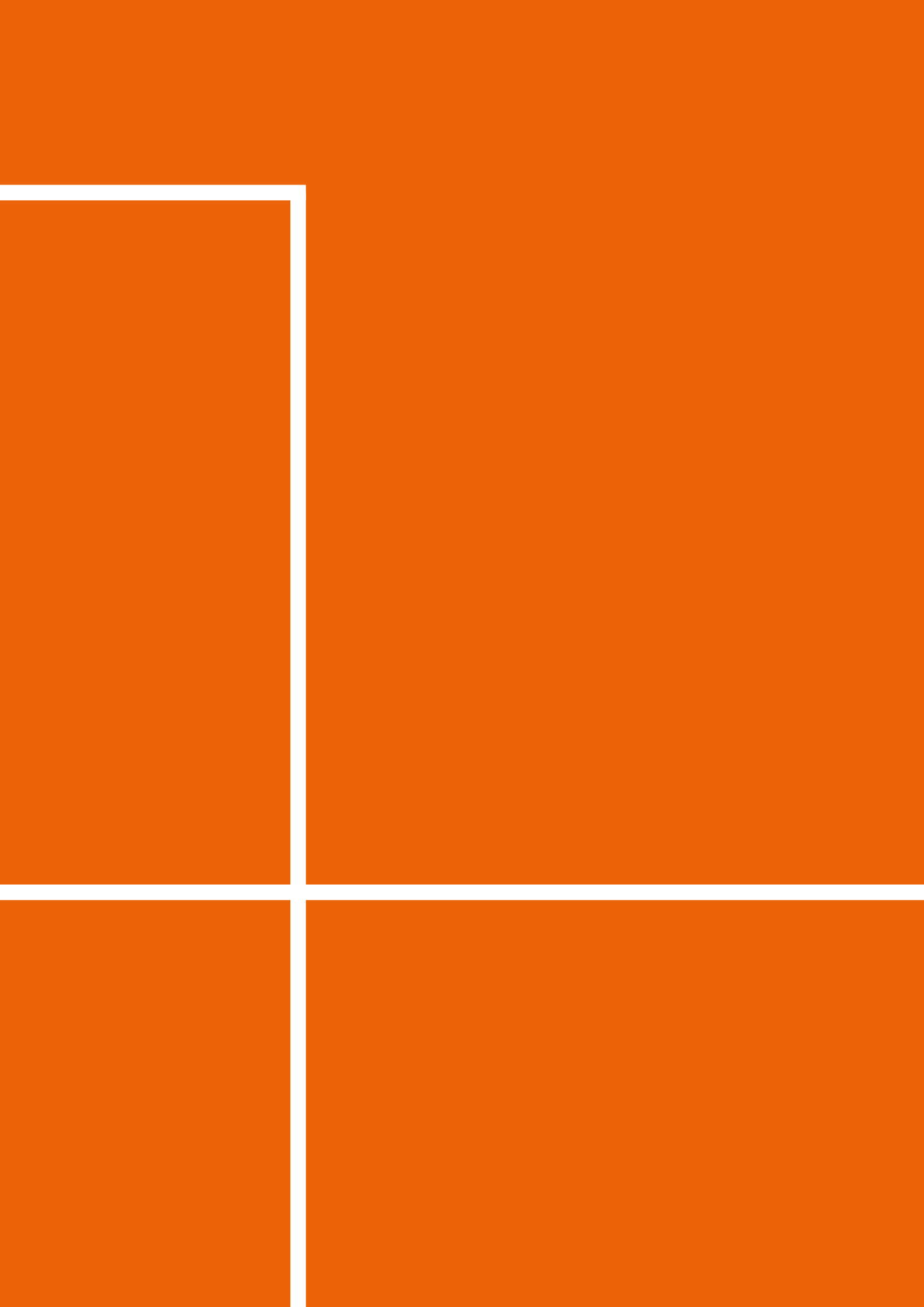


Technology

- Are the technology 'basics' in place that allow the firm to operate effectively on a day to day basis?
- Does the firm have a technology improvement plan?
- Is the firm aware of all available emerging technologies and do they know which ones have a 'best fit' for the organisation?
- Is the firm able to ensure all new technologies adopted are secure?
- How will the firm fund the continuing need for technology investment?

At a Glance

1. Global financial performance
2. UK financial performance
3. Business support
4. People
5. Financing
6. Future analysis
7. Risk



1. Global financial performance

At a glance

Global headcount

- Top 10 firms have managed headcount whilst Top 11-25 firms have continued to invest.
- Top 11-25 firms have now grown partner and fee earner headcount from 2016 to 2018 by 50% and 59% respectively. This is impacted by (i) consolidation in the mid-tier; and (ii) lateral hiring. In the same period, Top 10 firms reduced both partner and fee earner headcount by 2%.

Global fees

- A number of firms achieved impressive global fee income growth; 38% of Top 25 firms recording double digit percentage growth. On average, Top 10 firms increased global fees by 5.2% (to an average of £980m), with 86% of growth coming from international offices. Top 11-25 firms achieved an 11.3% increase (to £250m). No global firm experienced a reduction in global fees.
- In terms of spread, 70% of Top 10 firms increased fees by 1-5%, whilst 30% grew fees by 11-15%. For Top 11-25 firms, 44% increased fees by 5-10% with the remainder equally spread across the 1-5%, 11-15%, 16-20% and 21-25% brackets.

Global profits

- Top 10 firms grew global profits by 1.7% to an average of £388m, a rate significantly less than growth in fee income. Conversely, Top 11-25 firms grew global profits by 12.6% to an average of £87m, outstripping fee income growth of 11.3%.
- Global net profit margin (before full and fixed share equity partner remuneration) has fallen for the second year running for Top 10 firms to 37.9% and this is principally due to a 0.7 percentage points increase in the fee earner staff cost ratio (to 26.5%), representing an additional average cost to firms of £6.9m (or £20k per full equity partner).
- Top 11-25 firms grew global net profit margin by 1 percentage point to 34.3% following a reduction in the fee earner staff cost ratio by 0.3 percentage points to 28.2%, adding £750k to net profit (or £6k per partner).
- The difference in global partnership models between Top 10 and 11-25 firms impacted the above, as the net profit margin difference grows to 10.4 percentage points (34.7% v 24.3%) when profit after fixed share equity partner remuneration is considered.

Movements in foreign exchange rates

- Movements in foreign exchange rates have had limited impact on law firms in the current year. For Top 10 firms, fees fell by £1.3m (0.1% of total), whilst profits benefitted by £0.5m (0.1%). In the prior year, fees and profits benefitted by £43.7m (4.9%) and £16.2m (4.4%) respectively.
- Foreign exchange movements have reduced fee income and profits in Top 11-25 firms by £1.9m (0.8%) and £0.6m (0.7%) respectively, compared to a benefit in prior year of £6.3m (3.2%) and £1.9m (2.8%).

International analysis

- International net profit margins of Top 10 firms continue to lag behind UK performance by between 3.9 (Australia) and 25.9 percentage points (Africa). Top 11-25 firms' UK margin performance is ahead of international counterparts by between 5.6 (Rest of Asia and Far East) and 24.5 percentage points (China – where the margin is only 4.3%).
- Top 10 and 11-25 firms recorded growth in 1-5 years ppe average chargeable hours in all regions, except Western Europe for the Top 11-25. Top 10 firms' chargeable hours for 1-5 years ppe is led by USA (1,675 hours) and Australia (1,524 hours) and both exceed the UK average (1,478 hours). Top 11-25 firms' UK hours were 1,324, and the nearest international office is Australia at 1,242.

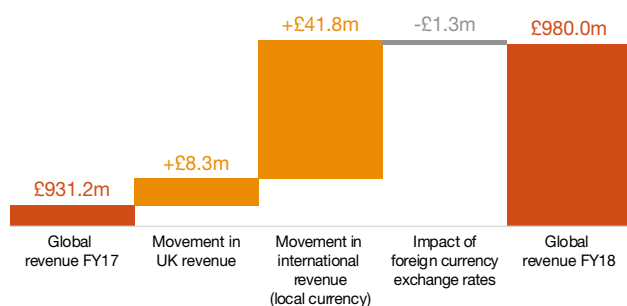
UK top tier vs US top tier

- US top tier firms continue to significantly outperform the UK top tier in respect of all KPIs; for example, US top tier firms achieved an average PEP of £1,994k which is 41% (£818k) ahead of the UK top tier performance (£1,176k).
- Average fee income and net profit in the US top tier grew by 6.8% and 8.0% respectively. This compares to 7.1% and 6.1% in UK top tier.
- Only 25% of UK top tier firms achieved profit growth greater than fee income growth, whilst the corresponding figure for the US top tier is 43%.

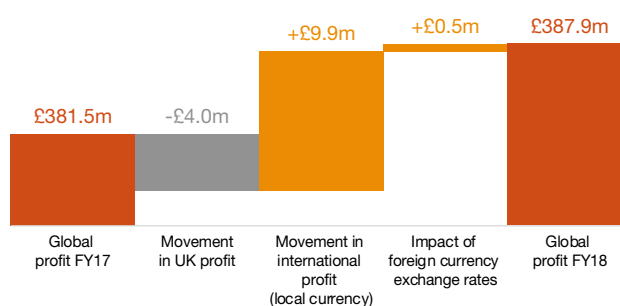
Global fee income and profits: source of growth

The international offices of Top 10 global law firms have contributed significantly more to revenue and profit growth than UK offices. For Top 11-25 firms, the spread of growth is more even between UK and international offices.

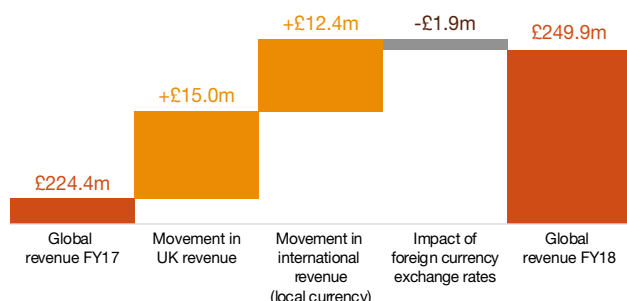
Top 10 – Revenue



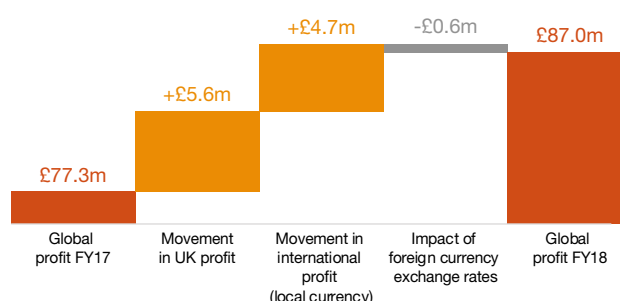
Top 10 – Profits



Top 11-25 – Revenue



Top 11-25 – Profits



UK top tier vs US top tier – Net profit margins

The US top tier's net profit margin of 45.9% is significantly higher than the UK's at 36.7% and if the UK could bridge this gap it would have a significant impact on overall profits and PEP.

UK top tier



US top tier



The difference

- 9.2 percentage points
- £135m profit
- £275k PEP

■ 2018 ■ 2017

2. UK financial performance

At a glance

Fees

- Over 80% of firms increased fee income across each of the Top 100 bandings, and 91% of firms overall (2017: 75%). Average fee income growth was 5.0% and 9.2% for Top 10 and Top 11-25 firms respectively (2017: 2.5% and 2.3%). For Top 26-50 firms, average UK fee income growth was 7.2% (2017: 3.7%) and for Top 51-100 firms, 10.0% (2017: 2.5%).
- Overall, 39% of participating firms experienced double digit growth in fee income. In 2017 this was limited to 4%.
- The increase in fees flows into a number of KPIs, such as fees per fee earner which is up, on average, across all bandings: Top 10 by 3.9%, Top 11-25 by 4.4%, Top 26-50 by 3.7% and Top 51-100 by 8.2%.
- Fees per chargeable hour have increased across all Top 100 bandings. The Top 10, 11-25 and 26-50 bandings have seen increased rates per hour of between 1.4% and 3.9% compared to 3.4% and 7.6% on average in 2017. Firms in the Top 51-100 have, on average, experienced a 12.9% increase.

Staff costs

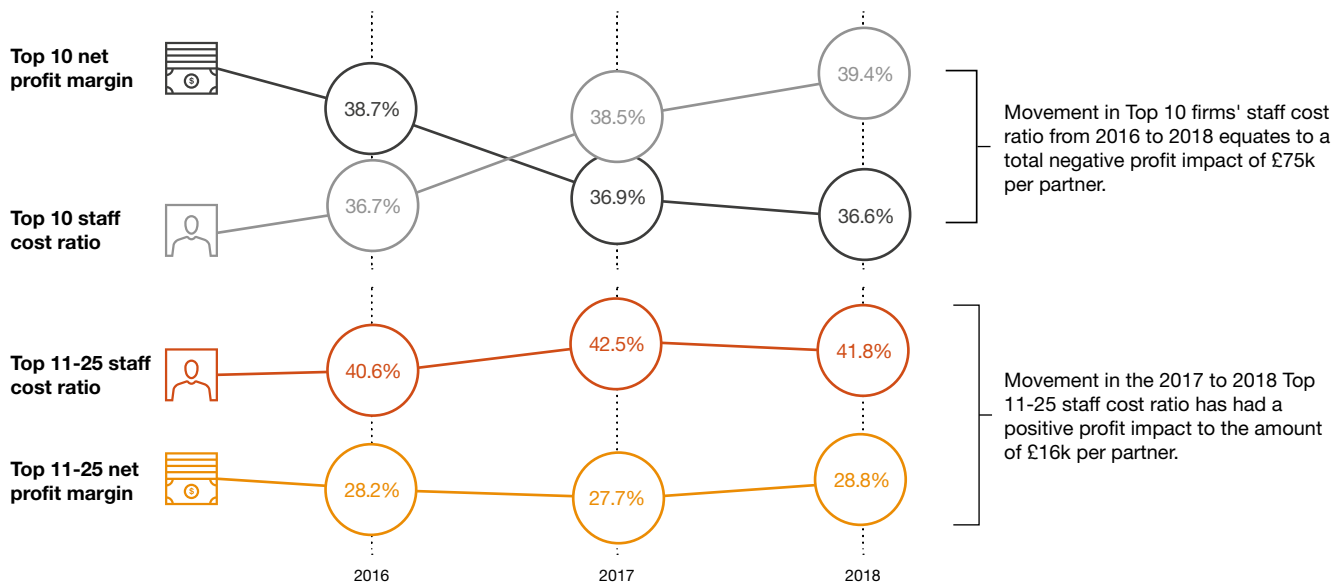
- There has been an increase in fee earner staff costs for all bandings except for Top 51-100 firms. This is most prevalent in the Top 10 where the fee earner staff cost ratio has increased by 1.2 percentage points to 26.7%. Consistent with all bandings, Top 10 firms have controlled non-fee earner costs; therefore, the overall staff cost ratio impact is limited to an increase of 0.9 percentage points to 39.4%. This has contributed to further erosion of profit by, on average, £3.6m. Within the Top 10 there has been a mix in staff cost ratio movements, with 57% experiencing an increase in the staff cost ratio. This results in a wide ranging impact from movement in staff costs from a benefit of £9.0m to increased costs of £21.5m.
- The overall staff cost ratio has decreased in Top 11-25 and 26-50 firms due to falls in non-fee earner staff costs, resulting in an effective profit increase of £1.4m and £0.2m respectively.
- The increase in fee earner cost per chargeable hour exceeds the growth in fee income per chargeable hour for all bandings. Top 10 firms' fee earner cost per chargeable hour has increased by 3.2% to £98 and by 5.3% to £99 in Top 11-25 firms. Top 26-50 and 51-100 firms recorded a 7.5% and 14.7% increase respectively to £86 (for both bandings).

Profits

- A total of 29% of firms reported lower profits in 2018 (2017: 48%), but only 8% of firms in our survey reported a reduction in both fee income and profits (2017: 25%).
- Profit declines were most prevalent across Top 10 and 11-25 firms, where almost half experienced falling profits.
- Top 10 firms' average profit margins continue to fall, from a high of 40.0% in 2014 to 36.6% in 2018. This represents a further fall of 0.3 percentage points from 2017, with the most significant factor being increased fee earner staff costs. Further, the performance gap to Top 11-25 firms is narrowing, where margins have increased by 1.1 percentage points to 28.8%, achieved through a reduction in non-fee earner staff costs.
- A key development this year was that the profit margin for Top 51-100 firms (24.6%) has now overtaken those for the Top 26-50 firms (24.2%) following a 1.6 percentage point improvement for the Top 51-100 and a 1.0 percentage point fall for the Top 26-50.
- Average PEP improved across all bandings. In Top 10 firms, the fall in partner headcount (from 147 to 142) was a key contributing factor that improved average PEP from £1,043k to £1,066k. With consistent partner headcount, average PEP would have fallen to £1,030k.
- Whilst profit increases contributed to a rise in Top 11-25 firms' PEP of 12.7% to £729k, movement in partner headcount again plays a part (fall on average from 78 to 74). With consistent partner headcount, average PEP would have been £692k (increase of 7.0%).
- Both Top 26-50 and 51-100 firms increased PEP to £467k and £381k respectively, despite higher partner headcount.

Movement in net profit margin and staff cost ratio: 2016 to 2018

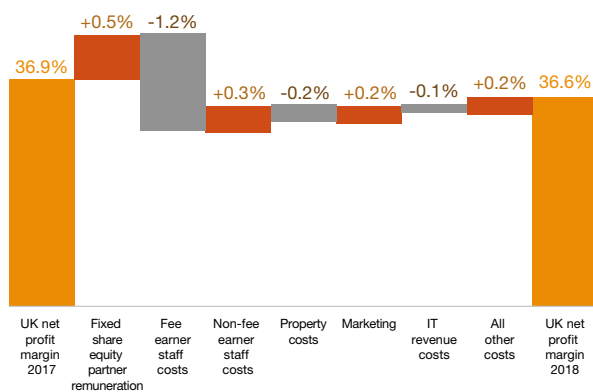
Increasing staff costs has continued in Top 10 firms; however, Top 11-25 firms have managed to reverse the trend of previous years and reduce the staff cost ratio by 0.7 percentage points.



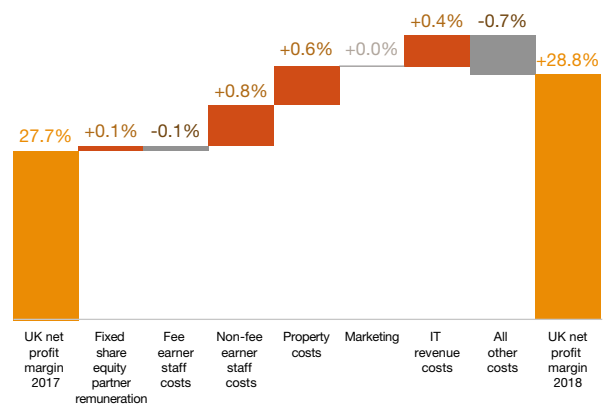
Net profit margin bridge: FY17 to FY18

Fee earner staff costs is the greatest contributory factor to the net profit margin fall in Top 10 UK law firms, whilst Top 11-25 firms have benefited from cost savings on non-fee earner staff costs and property costs.

Top 10 firms



Top 11-25 firms



3. Business support

At a glance

Overall

- Finance and Risk & Compliance continue to be perceived as the two strongest performing support functions in 2018 and IT has overtaken HR as the third strongest performing function.
- The top priority for Business Support remains 'improving the use of technology'. Interestingly, 'standardising and centralising processes' is still an important priority but is now ranked third, with 'supporting improvements in service offering' gaining in importance as the second highest priority.
- 'Data analytics' has significantly grown in importance for the second year running and is now the fourth highest priority for business support functions. In 2018, 68% of Top 50 firms have data and analytics specialists in place (averaging six specialists per firm).
- It is becoming increasingly common for law firms to employ specialists within business support to enhance the capability of functions. In the current year, there has been a significant rise in the deployment of specialists, particularly in Top 10 firms where all now have 'Resource & Capacity Management', 'Digital & Emerging Technology', and 'Strategy, Business Innovation, and Transformation' specialists in place. It is, of course, more difficult for Top 51-100 firms to make these sorts of investments, with no more than 17% of these firms having specialists in any area.

Technology

- While many IT functions continue to focus on the need to replace core systems (e.g. PMS and HR), more than 50% of Top 100 firms are either planning to or have already commenced projects relating to Risk & Compliance or Data Analytics.
- Adoption of digital and emerging technologies has increased across all bandings compared with prior year. Firms continue to recognise that these technologies will play a key role in both client service and efficiency, with 'client experience' and 'operational efficiencies' remaining top drivers for adoption. Compared with the prior year, firms in the Top 26-50 and 51-100 have significantly increased their interest across the full suite of technologies through research and pilot projects.

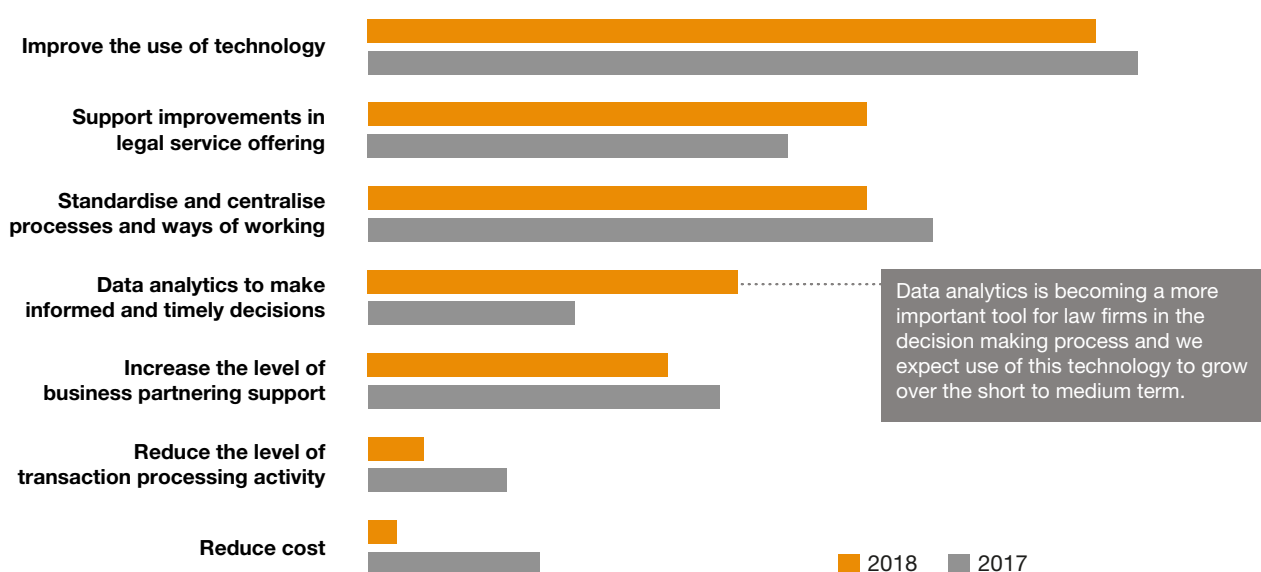
- Adoption of more conventional technologies has progressed since last year, with more than 50% of Top 100 firms now having adopted mobile apps, client collaboration tools, and automated/semi-automated document production. There is a significant gap in maturity between these technologies and more emerging technologies, such as Artificial Intelligence (AI), Smart Contracts and Blockchain Solutions.
- As last year, 80% of Top 10 firms are piloting AI and this could relate to an expansion of pilot projects as firms seek to more widely consider AI technology. As in 2017, the Top 11-25 remain the most mature users of Robotic Process Automation (RPA) with more than half having established or begun piloting this technology.

Finance

- The main priorities for the finance function are pricing and profitability, working capital and process efficiency.
- With regard to firms' management information (MI), accuracy, breadth and granularity of reporting remain broadly satisfactory. However, accessibility and levels of automation remain key areas of focus for Finance, along with the ability of the function to provide insight from MI to management.
- Given the prioritisation of working capital for finance functions, write-offs of WIP remain a key challenge for all firms. 60% of Top 10 firms in the last year wrote off between 15% and 20% of their fee income. If we assume for these firms an average write off equating to 17.5%, this amounts to £159m of lost global fee income. The extent of fee income written off in Top 26-50 firms is also significant, with all firms writing off at least 10% of fee income and 57% writing off more than 15%. The survey revealed 'not billing for changes in scope' and 'inaccurate estimates' to be the most common causes for fee income write offs.

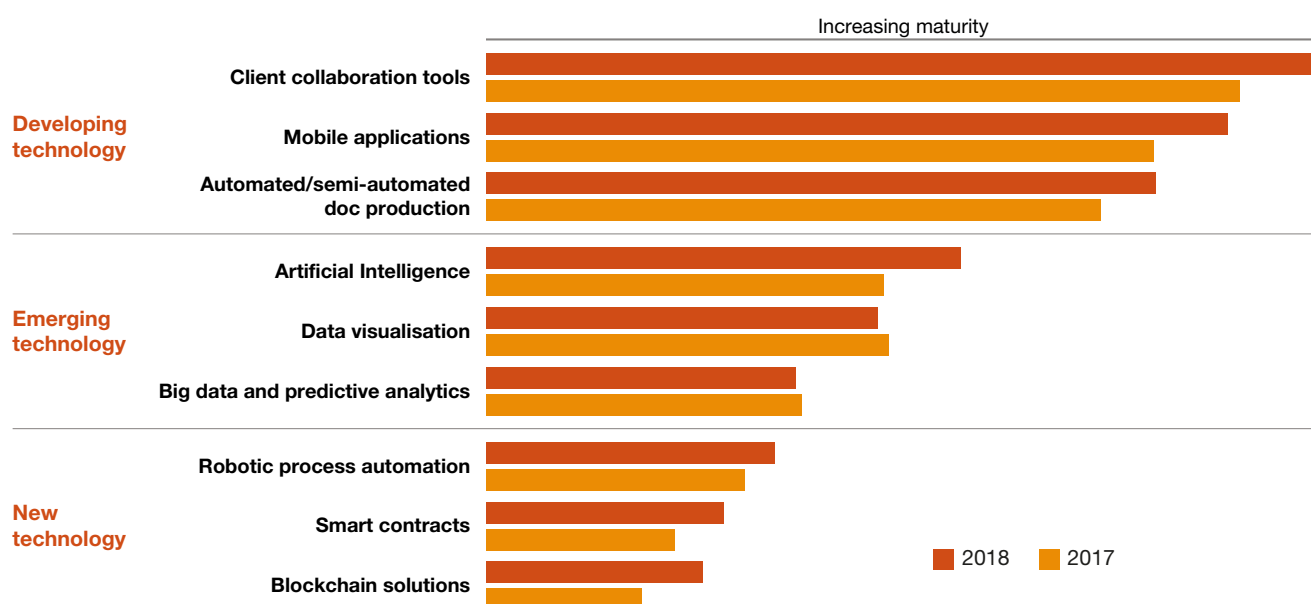
Top priorities for business support in the next 12 months (Top 100 firms)

Technology is a key focus area for business support, including improving its use, standardising and centralising processes and using emerging technologies like data analytics.



Maturity of digital and emerging technology (Top 100 firms)

Developed and emerging technology continues to grow, but the lack of take up on new technology still exists.



4. People

At a glance

Headcount

- Average total fee earner headcount has fallen across the Top 25 bandings. The fall in fee earner headcount in the Top 10 and 11-25 firms was on average 3% and 11% respectively. In contrast, the Top 26-50 saw an increase of 8%, with the Top 51-100 seeing an increase of 4.6%.
- In Top 25 firms, the greatest reduction in fee earners is below the >5 year pqe grade. Numbers in the newly qualified grade fell in the Top 10 by on average 24% and in the Top 11-25 by 22%. Headcount in the 1-2 years pqe grade fell by 13% in Top 10 and by 28% in Top 11-25 firms. These reductions appear to be managed attrition in response to falling utilisation in recent years, rather than wholesale redundancies. We note that the Top 26-50 firms appear to be investing in people, with the newly qualified headcount up by 33%.
- The > 5 year pqe grade represents a growing proportion of fee earner headcount in Top 25 firms. Given the tight management of partner numbers, this suggests an increasing bottle-neck at this grade which may be a concern in terms of retaining key talent and ensuring effective and cost efficient allocation of resource.
- This year the survey shows an increase in business support headcount in the Top 10 (5%) and Top 26-50 (22%) but a continued reduction in the Top 11-25 (6%).

Chargeable hours

- Following declining utilisation in 2016 and 2017, there has been a general increase in actual chargeable hours in Top 10, 11-25 and 26-50 firms across the majority of grades. For example, the average increase across the 1-5 years pqe grade is 5.9% to 1,478 hours in the Top 10 and 2.8% to 1,309 hours in the Top 11-25. Further, the survey reveals an increase in target chargeable hours for all grades in the Top 25.
- Average spare capacity (i.e. excess headcount based on the difference between target and actual chargeable hours) in the Top 50 has fallen and reflects improved utilisation and falling fee earner headcount. The reduction in average spare capacity is seen from 1-2 year pqe up to partner level in Top 10 and 26-50 firms, but is not reflected in the Top 11-25 where only the >5 year pqe and newly qualified grades reduced their spare capacity as targets were increased.

Leverage and Cost

- The range of the ratio of fee earners to non-fee earners is from 1.3 in Top 10 firms to 1.6 in Top 11-25 firms and all bandings have remained consistent with prior year.
- There has been a mix of movements in the ratio of fee earners to full equity partners. Top 10 and 26-50 firms saw this ratio grow, from 6.7 to 7.2 and from 8.3 to 9.1 respectively. The fall in this ratio in Top 11-25 firms was from 7.7 to 7.5 and in Top 51-100 from 9.9 to 9.0.
- The trend of increasing fee earners per secretary has halted this year, with only the Top 26-50 increasing this ratio, from 4.3 to 4.4. Top 11-25 firms held this ratio at 5.2, whilst it fell for the Top 10 and 51-100 firms, from 5.9 to 5.6 and from 5.0 to 4.0 respectively.
- Costs per fee earner have increased across all bandings (in the Top 25 by 8% and in the Top 26-100 by 7%) which reflects (i) increasing pay levels resulting from the competition in attracting and retaining talent; and (ii) the movement in mix of grades.

Partner remuneration

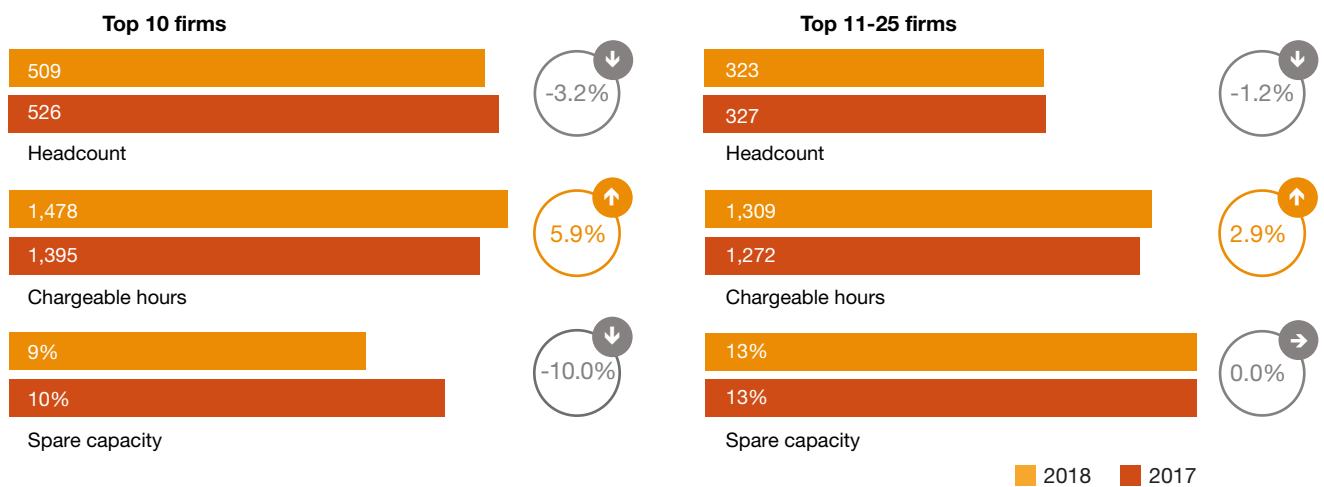
- Performance-based partner reward models continue to be most prevalent in the Top 50. Profitability, fee income and chargeable time remain key metrics that impact partner remuneration. For Top 10 firms, referral of work is a more prevalent metric than in other bandings and working capital is an increasingly important performance measure outside the Top 10.

Diversity

- Female representation at partner level has increased over the last 5 years, with Top 51-100 firms leading the way (2011-2018 Top 10: 13.2% -18.5%, Top 51-100: 15.9% - 23.5%). Firms across all bandings continue to recruit more females than males at trainee level.
- In Top 10 and 11-25 firms, BAME representation is low at partner level, reducing from 19% and 18% at trainee grade respectively, to 7% and 8% at full equity partner level.
- At the time of survey completion, a significant number of firms had not included partners in their gender pay gap reporting; however, we know that a number of law firms have since reported gender pay gap including partners.
- Despite the level of attention that gender pay gap generates, 39% of all Top 100 firms stated they had no planned actions to address gender pay gap. For those that do have plans, the most common are learning and development, and reward.

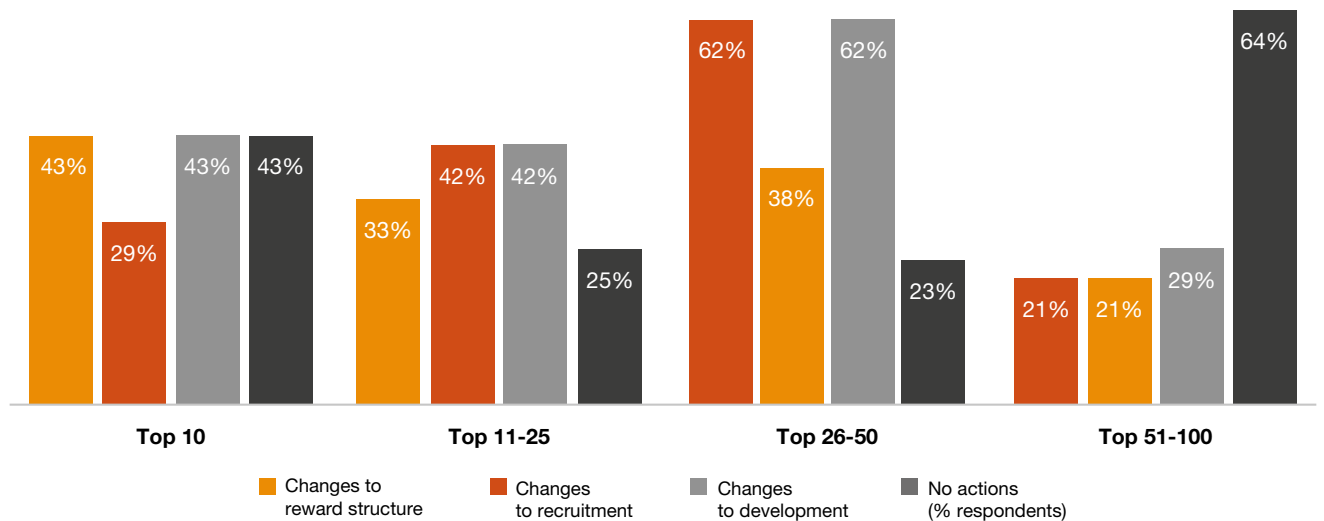
Movement in headcount, chargeable hours and spare capacity (1 - >5 years pqe grade)

The reduction in headcount in the 1- >5 years pqe grades has had a positive impact on utilisation and for the Top 10 firms, reduced spare capacity.



Actions planned in response to Gender Pay Gap

There is a worryingly significant number of firms that are planning no actions in response to their gender pay gap.



5. Financing

At a glance

Lock-up

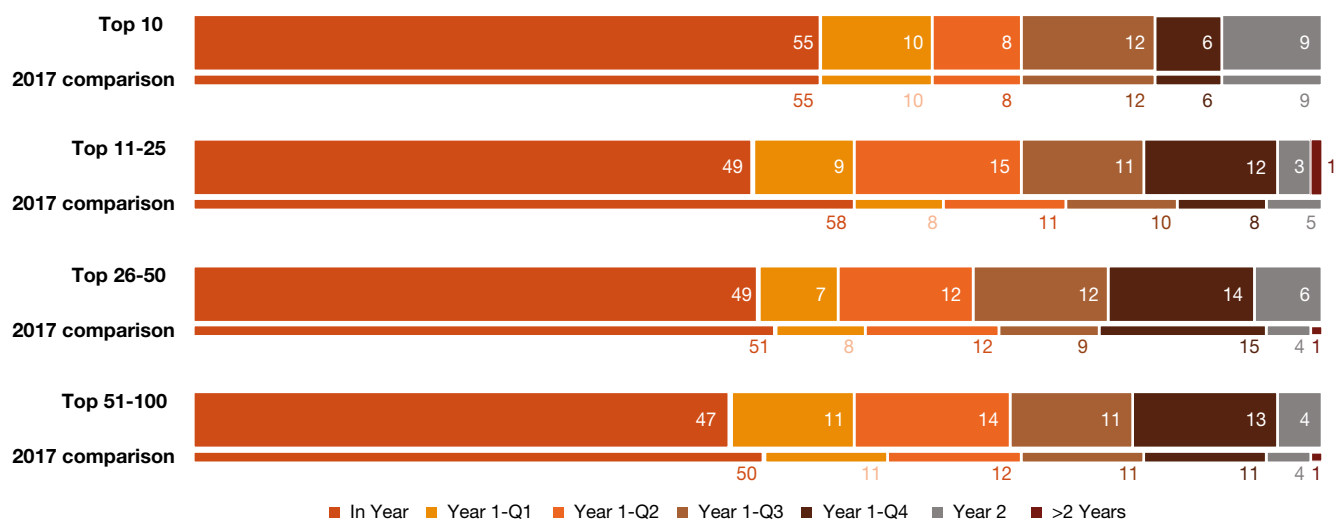
- Year end lock-up performance has deteriorated in Top 11-25 and 26-50 bandings by 1 day to 122 and by 9 days to 129 respectively. Top 10 firms have posted a small improvement from 124 to 123 days, whilst Top 51-100 firms significantly reduced year end lock up by 11 days to 135.
- There remains a significant gap between average and year end lock-up (between 13 and 19 days across all bandings).
- Significant opportunities still exist for firms to improve their 'matter-to-cash' performance and reduce their dependence on external debt. For example, an average Top 10 firm could generate £16.3m of cash by reducing lock-up to 108 days, being top quartile performance.
- The survey demonstrates that firms are beginning to take action to address the lock-up challenge. More firms, for example, are linking remuneration to partner lock-up performance or introducing sanctions on distributions. In the Top 10 this year, 70% reported that equity partner remuneration was now linked to lock up performance and 50% for non-equity partners.
- Lack of sanctions and incentives was cited by a third of Top 10 firms as the most significant reason for ineffective working capital management. Alongside this, problems persist around contract set-up, billing, WIP management, collection processes and data quality. All of these aspects are roadblocks to developing a cash conscious culture.
- Leading firms are making progress through initiatives including: (i) building standard terms into contracts; (ii) streamlining e-billing; (iii) enhancing practice management systems to support integrated time recording (i.e. automated timesheet entry through to billing); (iv) setting meaningful KPIs & targets linked to remuneration, with both sanctions and rewards; and (v) using data analytics to equip practice staff and partners with user-friendly visualisation of performance.

Funding

- This year saw a reduction in the proportion of external funding for all bandings except the Top 11-25, which saw an increase from 19% to 21%. In the Top 10, there was a drop from 20% to 18% which reversed the trend seen in 2017. This could well be a result of increased profitability and the knock-on effect of an increased partner current account. Partner current accounts have increased across most bandings as follows: Top 10 by 17% to £639k, Top 11-25 by 29% to £487k and Top 51-100 by 14% to £295k.
- We are seeing a heightened interest across the sector in considering alternative sources of finance, including IPO, private equity investment and litigation funding.
- There has been a drop off in facility renegotiations compared to prior year, particularly for firms below the Top 10. The majority that did renegotiate facilities, increased their level of borrowing (63% of all Top 50 firms).
- With the exception of the Top 10, which remained consistent at 55%, the proportion of profit distributions paid in the year it is earned fell. This was most notable in the Top 11-25 category that saw a fall from 58% to 49%.

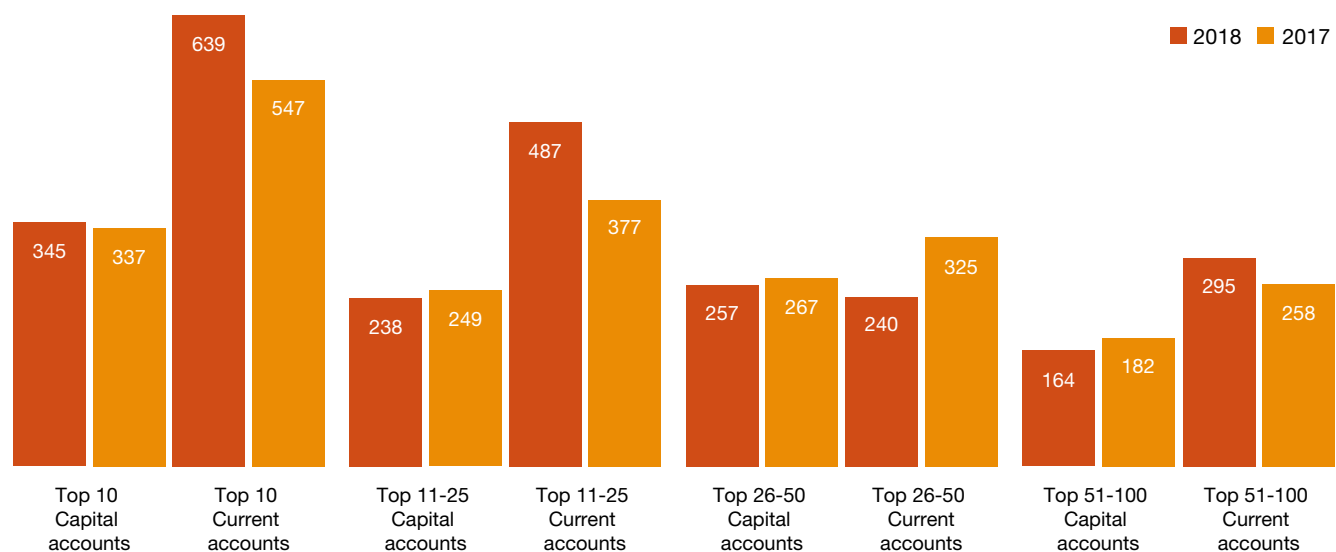
Timing of partner profit distributions

Outside the Top 10, profit distributions have been delayed from the year in which profit is earned to the following year.



Full equity partners average UK capital and current accounts balances

Capital accounts have remained relatively consistent with prior year, particularly in the Top 50 bandings, whilst current accounts have increased across most bandings: Top 10 by 17%, Top 11-25 by 29% and Top 51-100 by 14%.



6. Future analysis

At a glance

Fee income and profits 2018 to 2020

- The vast majority of firms are optimistic on fee income and profit growth from 2018 to 2020, with a significant number of firms predicting that profit growth will outstrip fee income growth in the period 2019 to 2020.
- Top 26-50 firms' expectations stand out, with fee income expected to rise by 5.3% from 2019 to 2020, but profit to grow by 7.3%. Top 10 firms expect fee income and profit growth of 3.9% and 4.3% respectively, and the Top 11-25 expect increases of 4.8% and 5.2%. Top 51-100 firms expect fee income to fall by 0.1% on average and profits to increase by 1.9%. It should be noted, however, that previous years' surveys have shown that forecasts in the sector are invariably overly optimistic.

Merger activity by 2020

- The results of our survey suggest merger activity will continue over the next 2 years.
- 40% of Top 10 and 46% of Top 26-50 firms state that merger is somewhat likely, whilst 9% and 18% of Top 11-25 firms state merger is very likely and somewhat likely respectively.
- Merger types, though, will vary. Larger firms will seek mergers with non-UK based law firms (with UK/US mergers likely to lead the way), whilst mid-tier firms expect to merge with smaller UK organisations.

Threats to meeting the firm's ambitions

- Cyber threats, Brexit, shortage of talent and the speed of technological change are the threats that attract most concern for law firms.
- Cyber leads the way: 86% of Top 10 firms, 80% of Top 11-25, 92% of Top 26-50 and 86% of Top 51-100 firms are either extremely concerned or somewhat concerned about this threat. Clearly, law firms need to be focused on data security and the need to continuously protect themselves against the risk of cyber attack.
- New market entrants are also a concern for many mid-tier firms. 70% of Top 11-25 and 58% of Top 26-50 firms are somewhat concerned about this threat.
- The threats posed by inflation, exchange volatility (except a small number of Top 10 and 11-25 firms) and inability to finance growth are not a concern for the vast majority of firms.

Impact of Brexit

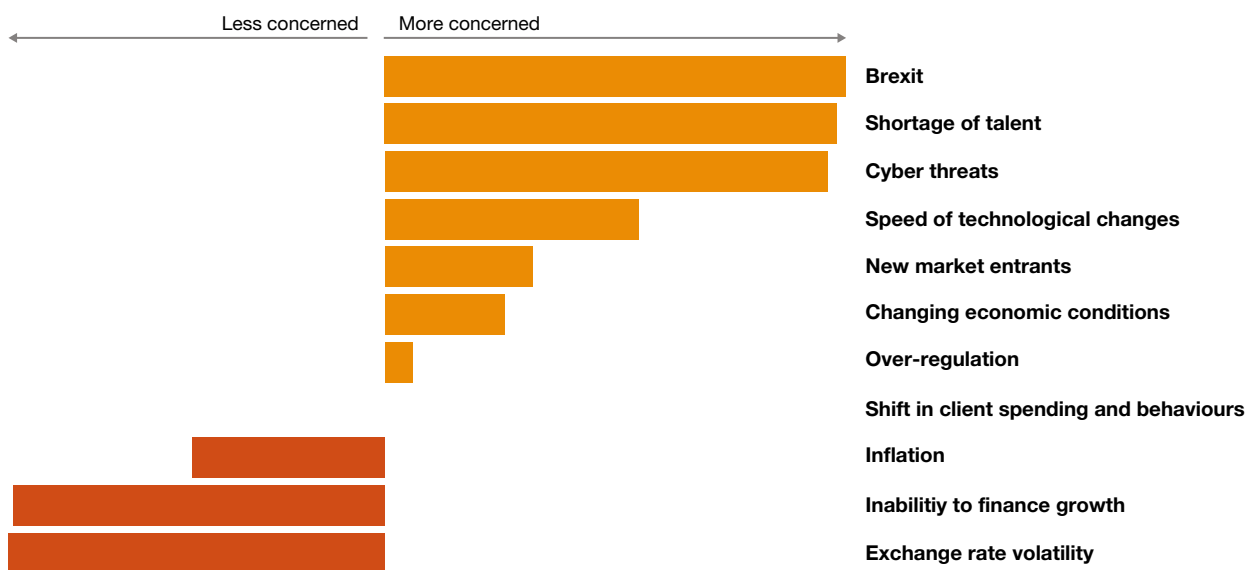
- No firms expect to relocate a head office, close a regional office or relocate a shared service centre due to Brexit and only a small number of firms expect movement in partner and staff headcount (maximum of 18% per banding).
- More firms expect movements in fee income (between 50% and 64% across the bandings) and costs (between 29% and 62% across the bandings) due to Brexit.
- A significant number of firms do not expect Brexit to impact their headcount, fee income or costs: 43% of Top 10, 27% of Top 11-25, 15% of Top 26-50 and 36% of Top 51-100 firms.
- All Top 10 firms have a committee focused on regulatory and structural aspects of Brexit and 86% on people aspects. The prevalence of Brexit committees falls through the bandings; for example, regulatory aspects of Brexit are covered by a dedicated committee in 73% of Top 11-25, 46% of Top 26-50 and 29% of Top 51-100 firms.

Key challenges facing the legal profession between now and 2020.

- 100% of Top 10 and 40% of Top 11-25 firms view technology as the key challenge facing the legal sector over the next 2 years.
- 80% of Top 26-50 firms view Brexit and 50% of Top 51-100 firms view shortage/retention of talent as the key challenges.

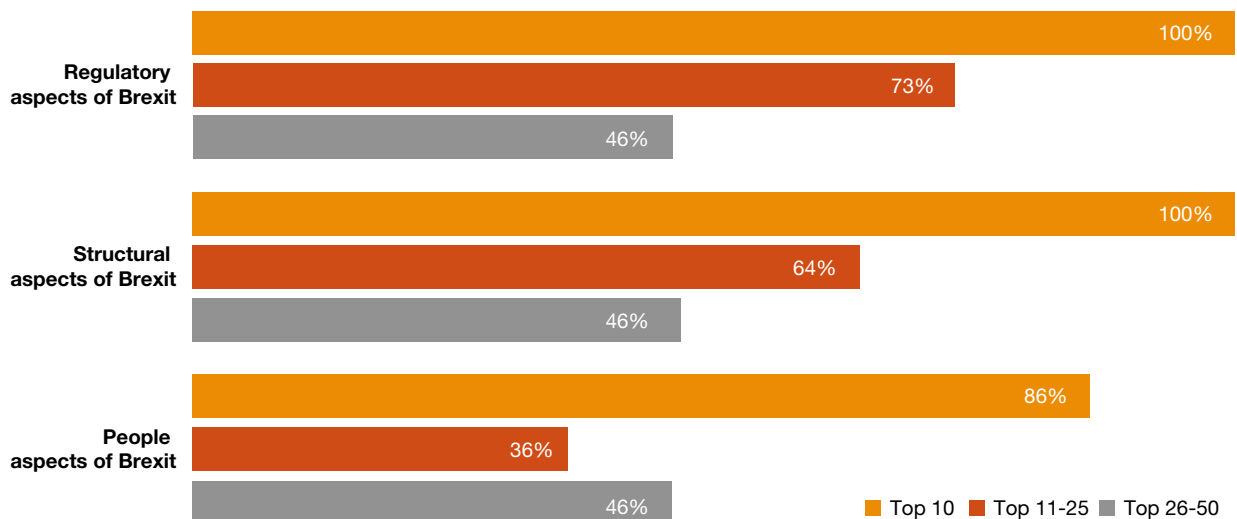
Concern levels on threats to growth - Top 100 firms

Law firms are most concerned with how Brexit, shortage of talent and Cyber threats will impact their future growth ambitions. The areas of least concern are exchange rate volatility (although some Top 10 and 11-25 firms do highlight this as a concern), inability to finance growth and inflation.



Number of firms with a dedicated committee on aspects of Brexit

All Top 10 firms have a dedicated committee covering regulatory and structural aspects of Brexit, but the number of such committees is lower in Top 11-25 and 26-50 firms.



7. Risk

At a glance

Information Security and Data Loss

- Information Security remains one of the foremost risks to the legal sector, with targeted attacks of organisations on the rise over the past 12 months. As law firms hold large volumes of client monies and confidential information, they remain a greater target from external threats.
- 60% of firms reported suffering a security incident during the year (consistent with 2017 at 61%).
- Whilst in 2017 33% of firms reported a security incident related to their own staff where there had been a loss or leakage of confidential information, this has risen to 46% in 2018. This statistic serves to highlight the importance of ensuring that staff are adequately trained to ensure that confidential information remains secure.
- With General Data Protection Regulations now live, it is important for firms to quickly identify and understand the nature and level of breaches, and to have a clear incident response plan to deal with reportable events.

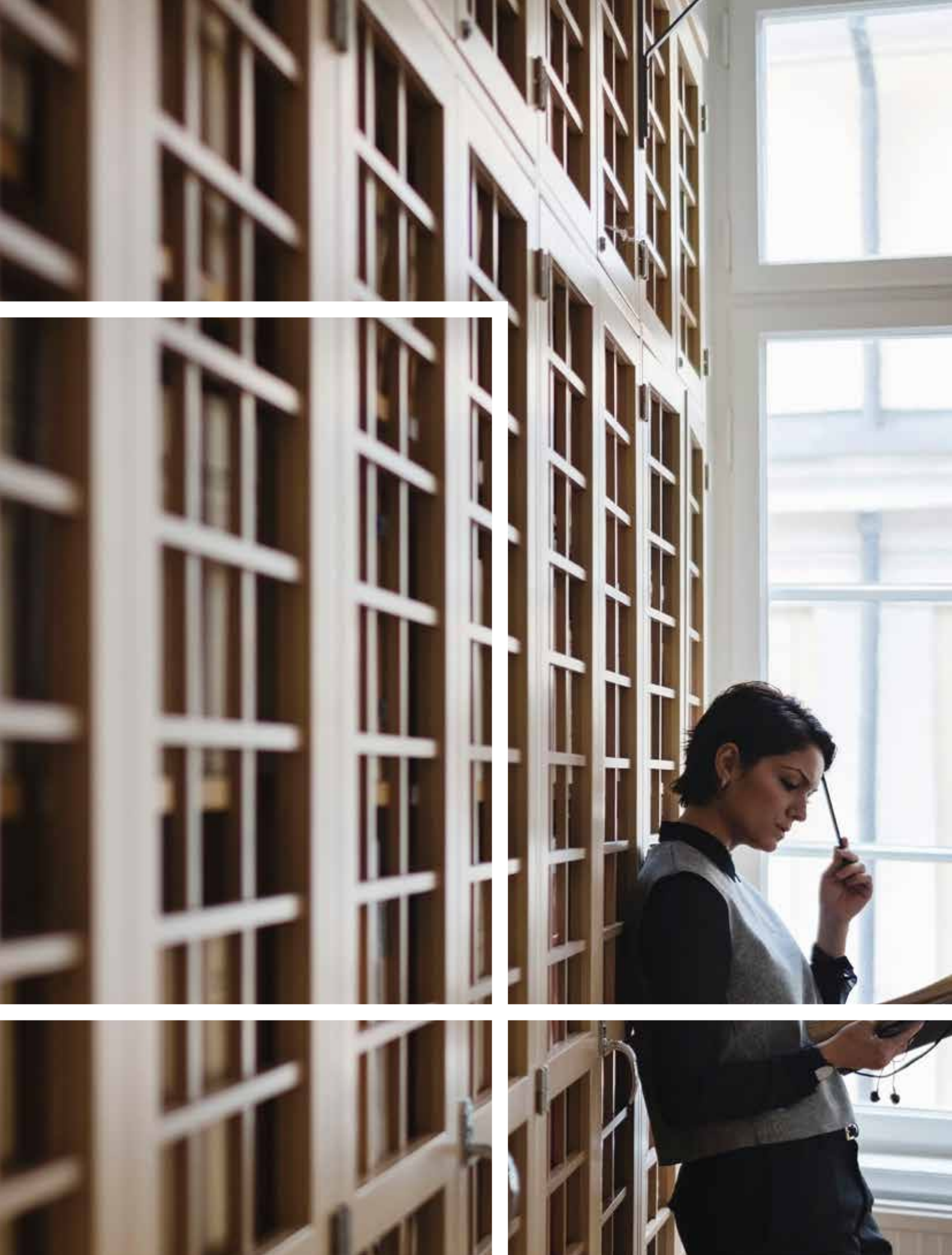
Business Continuity

- Only 27% of respondents were very confident that their IT Disaster Recovery testing has fully demonstrated that end to end operable services can be recovered in line with business recovery requirements.
- Only 54% of senior management have participated in a crisis management exercise in the past 12 months, with 14% of firms saying that senior management have not participated in the last 18 months.
- The statistics above suggest that in the event of a serious incident, some firms may not be fully prepared to respond appropriately.

Financial crime

- Scrutiny in relation to financial crime controls such as anti-money laundering, sanctions compliance and counter-terrorist financing is likely to be magnified in the foreseeable future.
- Not only is the regulatory net tightening around those perceived to be the 'enablers' of this activity, including lawyers, but the formation of the Office for Professional Body Anti-Money Laundering Supervision ('OPBAS') will also increase the attention paid to bodies such as the Solicitors Regulation Authority (and in turn, we expect the SRA to make more visits to law firms to check adherence to the rules).
- The emphasis is also changing: having systems and controls to mitigate financial crime risks is no longer going to be sufficient. Senior management will need to demonstrate that they have arrangements in place that are assessing the effectiveness of these controls.





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