The Law Society's Leadership and Management Section

Financial Benchmarking Survey 2024

The Law Society

In association with Hazlewoods LLP

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DRIVING LIFELONG PROSPERITY

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Foreword

Productivity and profitability are perennial challenges for law firms. The whole of the UK economy has experienced turbulence and challenge over the survey period. It is therefore no surprise that this turbulence shows in the data.

This year's financial and benchmarking survey sees a drop in the number of billable hours with a modest drop of 23 hours per year, reflecting the ongoing productivity challenge in the sector where completion of the legal work, client management, business development and supervision are just some of the challenges to productivity as evidenced by the billable hours recovered deceasing. The 6.8% median practice fee income increase is a modest positive in the other direction.

Taken as a whole, the findings focus on not just challenges for law firm leaders but the need for good management habits in terms of work in progress, collection of fees and to build on the income growth across the sector, which is insufficient to protect profitability year on year.

The data suggests areas to focus on to enhance the future for all law firms. For those who did not take part, looking at the trends can help with their planning and future management and taking part next time will not only enhance the data but also give access to a personalised summary of your firm against the benchmark results.

The benchmarking aspect will help those who took part to be more profitable in future years. By using our data, leading your law firm should get that little bit easier. Good luck.

Paul Bennett
Chair, Law Management Section Executive Committee
February 2024

About the Leadership and Management Section

The Leadership and Management Section is a community designed specifically to help partners, leaders, managers and operational staff in legal businesses excel at what they do.

The Section delivers essential best practice knowledge and insights in key legal practice management areas such as operations, people management, leadership, finance, business development, strategy, innovation, client care, quality and regulation.

As a member of this community, you can be confident you're up to date with the latest in legal practice management with access to a wide range of exclusive content, events and support delivered by practice management experts, including managing partners and legal consultants.

The comprehensive range of services and benefits includes:

- Managing for Success quarterly magazine
- A regular Leadership and Management Section e-newsletter
- Dedicated member-only portal featuring relevant resources, including topical news, updates and on-demand event recordings
- In-person and online events and networking opportunities
- Exclusive Law Society library benefits such as priority access to Law Society library services, first item free on Lawdocs, the Law Society library document delivery service*, and 50% off all chargeable Law Society library services**
- 20% discount on Law Society publications
- Opportunity to share your expertise and raise your profile within the community by contributing to the Section's programme of activities.

Membership of the Leadership and Management Section is open to solicitors along with professionals who are involved in the management of a legal practice or department (whether it is HR, IT, innovation or marketing).

Individual membership costs £199, but why not take advantage of even greater savings with our corporate membership deal? For only £399 your firm can nominate up to six staff members (and £60 for each additional person), who can all enjoy the benefits of being a Leadership and Management Section member.

For more information, visit:
https://communities.lawsociety.org.uk/leadership-and-management
email: MSadmin@lawsociety.org.uk
telephone: 0207 320 5804

Will works with the Law Society's Leadership and Management Section Committee to plan and deliver the member offering, identifying key areas of concern for the membership. Will also helps deliver practical guidance and know-how through a variety of resources, including online and in-person events, editorial content, a quarterly magazine and regular newsletters. For any feedback in relation to the Section offering please contact us via membershipengagement@lawsociety.org.uk.

Will Graves
Membership Engagement Manager, The Law Society

* Subject to standard page limits, terms and conditions and for current judicial proceedings or non-commercial purposes.
** Including additional research on top of the standard 30 minutes, the Lawdocs Service (first item free), and printing and photocopying services.
*** All benefits are valid between 1 November 2023 - 31 December 2024. Applies to all Law Society Section members, and members must state from initial contact that they are a current Section member when requesting any of these services.

About Hazlewoods LLP

The *Leadership and Management Section Financial Benchmarking Survey* is written and produced by the Legal Team of Hazlewoods LLP.

Hazlewoods is a Top 35 accountancy practice with a niche specialism in advising the legal profession. We have worked with law firms since 1992, and we have a dedicated team of over 50 individuals who work with law firms all day, every day.

We are retained by over 200 law firms countrywide on a recurring basis, and advise at least 40 others each year on projects such as practice strategy, mergers and acquisitions, structure advice and implementation, external equity investment and dealings with the SRA. The scope of our service goes far beyond the normal compliance-based services provided by the majority of other accountancy practices, and we have a tremendous range of contacts in the sector. See more at **www.hazlewoods.co.uk/sectors/legal-accountants.aspx**

This is the 15th year that we have compiled the Leadership and Management Section Financial Benchmarking Survey. Over this period, our experience and understanding of the sector have enabled us to develop and constantly refine the questionnaires and interpret the results.

Should you have questions about anything at all in it, we would be delighted to hear from you (**legal@hazlewoods.co.uk**)

We would like to thank all law firms that took the time to complete and return the questionnaires, and we hope that you find the report both interesting and useful in your firm.

About Lloyds Bank

Lloyds Bank Commercial Banking is delighted to again sponsor the annual financial benchmarking survey, which provides vital benchmarking data for law firms. As the most in-depth of its kind, it is an invaluable tool for law firm owners and managers to understand best practice and to make the right business decisions.

At Lloyds Bank Commercial we work closely with solicitors to provide funding and support that meets the specific needs of your business. Our specialist Relationship Managers are Lexcel-trained, understand practice management standards and the opportunities and threats that face the profession. They are also trained in the SRA Accounts Rules to ensure we complete the housekeeping processes correctly. We have a range of support available to the legal profession, from funding professional indemnity insurance to providing card payment solutions. We also support firms to bring in new partners through partner capital loans and to manage client money through a range of secure accounts.

2023 saw the sector impacted by similar challenges faced by the UK economy as a whole, with the slower real estate market driving reduced activity in conveyancing firms and the higher interest rate environment and inflationary pressures resulting in lower activity in corporate transactions. Overall, firms continued to manage through this well, and our Legal Specialist RMs continue to work with our clients to discuss potential efficiencies, such as use of embedded payments, as well as means of supporting with working capital funding needs.

Becci Wicks
UK Head of Legal, SME & Mid Corporate
Lloyds Bank Commercial Banking
www.lloydsbank.com/solicitors

LLOYDS BANK

Introduction

Members of the Law Society's Leadership and Management Section are represented in law firms across England and Wales. For over 20 years, the Leadership and Management Section has produced the annual Leadership and Management Section Financial Benchmarking Survey with the active participation of that membership and support from the wider legal practice community. The survey is widely regarded as one of the leading annual health check reports for smaller and mid-sized practices.

This report is unique in providing detailed accounting and business metrics collected directly from solicitor firms across England and Wales, allowing those firms and others – particularly from the mid-market – to benchmark their performance against peers and over time.

The 2024 survey was carried out between July and November 2023 and, as detailed in the following section, the majority of participants have either a 31 March or 30 April accounting date.

147 law firms from across England and Wales have taken part with a combined turnover of over £1.5billion, and we anticipate that most of the participants' income relates to domestic work.

As in previous years, all participants provided two years' data, i.e. the most recent accounting period and the previous one, which has allowed us to compare two years' results on a true like-for-like basis.

Many of the charts throughout this report include the results for two accounting years. Most charts include three figures for each turnover band; the lower quartile, median and upper quartile. The results for 2023 are shown as columns and numbers, and the like-for-like results for 2022 are shown as a dash, i.e. '-' .

Participants are analysed in more detail in the following section.

We consider that the response rates that we have seen for this voluntary survey are very good compared to other financial surveys of professional firms. In order to allow the findings to be statistically valid, we only provide full results for categories where at least 30 firms participated in the survey.

This year, we had more than 30 participants for each turnover band, and therefore the charts and statistics quoted throughout this report reflect the full figures across all sizes of firms. Other than in the following section, we do not differentiate between firms with turnover greater than £10m and those with turnover greater than £35m.

For ease and consistency, throughout this report, we refer to the owners of the practices as Equity Partners.

Participants

147 law firms from across England and Wales took part in this year's survey, comprising almost 16,000 partners and employees. The fee income of all participants totals over £1.5billion - an average of £10.4million per practice.

As in previous years, we have categorised firms based on turnover. The turnover bands and the number of participants in each band are shown in the table below.

The total number of firms in England and Wales in each band is also shown.

Turnover band	Total number of practices	Number of participating firms	%
Up to £2million	8,119	32	0.4%
£2million to under £5million	743	36	4.8%
£5million to under £10million	285	40	14.0%
£10million to under £35million	203	33	16.3%
£35million+	148	6	4.1%
Total	**9,498**	**147**	**1.5%**

There was a good proportionate participation amongst firms with a turnover greater than £5million. There was a lower proportionate participation from firms with turnover below £2million, but this is due to the number of smaller firms, with the majority of firms being in the smaller band.

As shown in the chart on page 7, the majority of participants had either a 31 March or 30 April accounting date. It is worth noting therefore that, from the 2023/24 tax year onwards, self-employed individuals and partners will be taxed on a tax year basis, rather than an accounting year basis, i.e. individuals will pay tax on profits arising in each tax year, regardless of their firm's accounting date. This will affect sole practitioners, partnerships and LLPs that do not prepare their accounts to either 31 March or 5 April. Limited companies are not affected. We therefore expect to see a greater proportion of firms with a 31 March or 5 April year end date in future years, as firms aim to make the preparation of personal tax returns easier.

The locations of the participants are as follows:

Region	Number of participating practices
Eastern	12
Greater London	27
Midlands	21
North East	4
North West	10
South East	29
South West	32
Wales	3
Yorkshire	9
Total	**147**

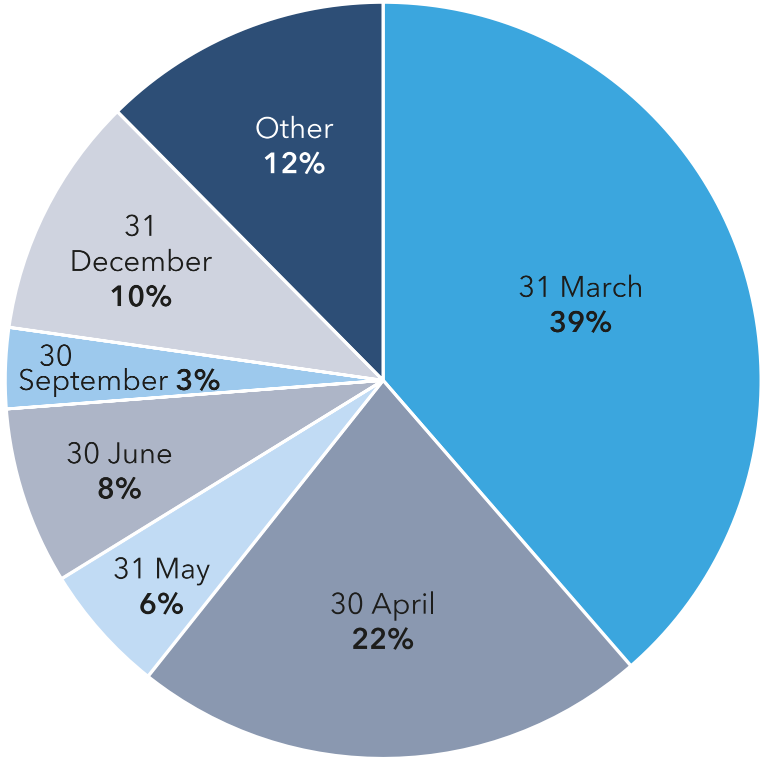
92% of participants traded as either a Limited Liability Partnership (LLP) or limited company. The remaining participants were unincorporated partnerships or sole practitioners. This is in different proportions to the percentages for the legal sector as a whole. According to SRA statistics, 55% of law firms were operating as a limited company, and 16% were operating as an LLP at the end of November 2023. These statistics, and more, can be viewed here: **www.sra.org.uk/sra/research-report/regulated-community-statistics/**

This difference between the survey participants and the sector reflects the fact that a large proportion of mid-sized firms have taken part again this year as the majority of the Top 200 law firms are either an LLP or limited company.

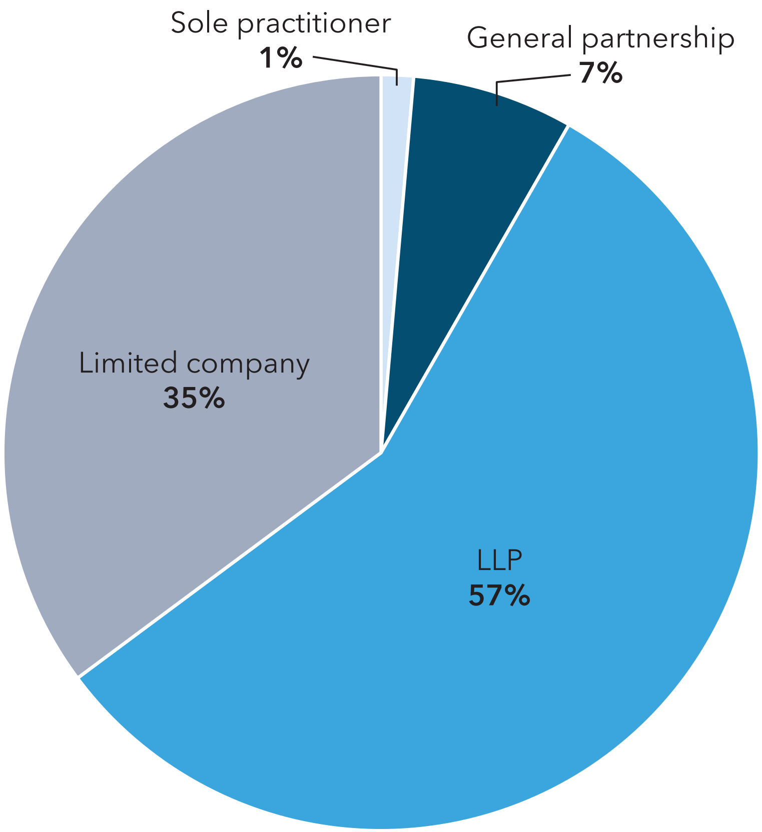
The SRA's statistics also show that the number of limited companies has increased by 84 in the last two years, whilst the total number of firms of all types has fallen by 457 over the same period. The total number of unincorporated partnerships and sole practitioners fell by 511 over this period.

Perhaps due to the rising rates of corporation tax, the number of limited companies has remained relatively static over the latest 12 month period.

Financial year end of participating practices



Structure of participating practices



Looking back

Our recent surveys looked closely at the impact of the Covid-19 pandemic on law firms' finances and noted that, despite the clear challenges, firms on the whole performed stronger than expected in their 2021 and 2022 financial years.

Last year's findings showed a median increase in practice fee income of over 9%, but costs had also increased, most notably the cost of fee earners increased on average by over 6% and there was a median fall in net profit per equity partner (before adjusting for notional salaries for equity partners) of almost 2%.

We also saw that firms were struggling to maintain chargeable hours, with a fall of 2.5% compared to the prior year.

Since then, the global economic outlook has presented new challenges to firms as many basic overheads, affected by the fallout of the war between Russia and Ukraine, rose sharply during 2022 and continued to rise for most of 2023.

As the industry was finding its way back to normality after the effects of Covid-19 began to subside, a fresh set of unexpected and unprecedented challenges presented itself.

A fresh set of challenges, but also new opportunities

As noted above, the majority of firms that took part in this year's survey have either a 31 March or 30 April financial year end.

As a result, these findings represent the first full year of many of the challenges currently facing firms, such as high inflation, increased bank base rates and record energy prices.

Most law firms that we speak to carry out pay reviews that tie in with their year ends, and so it is likely that the majority of firms in our survey had fixed salaries for the 2023 year end early in 2022, before many of the cost of living increases had really taken hold. As seen later in this report, this has meant that salary costs did not increase significantly out of line with normal fee growth, and it is likely that we will see the delayed impact next year.

The challenges of not just recruiting, but also retaining, high quality staff have remained as acute as ever.

The adverse financial environment has presented some opportunities; most notably the increase in interest income earned by many firms on the large amounts of client account balances held by them in the course of carrying out work for clients. In the vast majority of cases, this increase has been purely incidental, driven by increased bank base rates, rather than through significant amounts of effort on the firms' part.

In some cases, we have seen this interest income make up a significant, sometimes primary, component of profitability. This is analysed further in section 6.

This increase comes with a warning however, and firms are advised to treat interest income as a temporary bonus, rather than as a sustainable element of profitability.

Furthermore, firms that are considering spreading the tax impact of the change in the tax basis period are reminded that the tax payable on interest cannot be deferred, and so adequate provision must be made to cover this.

Looking forward

As we have said before, key to meeting the ongoing challenges in the sector is getting the most from staff, providing the best possible client service efficiently, and charging for it accordingly.

Using benchmarking information to improve your performance

Fee earner breakeven point

By combining our findings throughout this report we are able to calculate the expected breakeven point for a fee earner. This is defined as the fees a firm must generate per fee earner before any profit (sometimes also referred to as fee earner contribution) is earned. As illustrated below, this is substantially more than simply the median cost of a fee earner.

	2023 £	2022 £
Median fee earner cost, including notional salaries for equity partners (Figure 5.5)	63,993	62,347
Median support staff cost per fee earner (Figure 5.10)	22,731	22,402
	86,724	84,749
Median non-salary overheads per fee earner (Figure 6.9)	43,886	38,791
Breakeven point per fee earner	**£130,610**	**£123,540**

Working on an average target of, say, 1,100 chargeable hours per annum per fee earner, or 220 chargeable days per annum, this equates to the following:

	2023 £	2022 £
Cost per hour	£118.74	£112.31
Cost per day	£593.68	£561.55

In Figure 4.5 we see that the median fee income per fee earner in 2023 was £147,285, which equates to £133.90 per hour based on 1,100 chargeable hour per annum. This means that 89% of fees earned by a fee earner are used to cover their costs. Looking at it another way, if a firm has a 31 March year end, on average it takes until 17 February for a fee earner to earn sufficient fees to cover his or her total costs for the year, and for the practice to start earning 'super-profits' for the equity partners.

These figures assume an average of five chargeable hours per day, but as we see at Figure 4.8, the median number of actual chargeable hours recorded by fee earners in many firms is well below 1,100 chargeable hours per annum, and seems to be going down, not up.

Areas to focus on

Sections 5 (Employment costs) and 6 (Profitability) include some pointers on key overheads, such as fee earner costs, support staff costs and accommodation costs, and these may help to identify areas for potential savings.

However, we expect the breakeven point to continue to increase. UK inflation remains high and this puts continued pressure on firms to increase wages.

Alongside this, high energy costs are pushing utility bills and other overheads upwards at an alarming rate.

Section 4 (Fee income) is therefore a key section for firms looking to increase profitability.

Fee earner performance

Fee income is driven by a combination of fee earner numbers per partner (fee earner gearing), chargeable hours recorded (productivity) and the amount billed and received for each of those hours recorded (recovery rate).

While fee earner gearing is an important metric when the industry is growing, it is clear from our findings at section 4.8 that the ability for fee earners to convert their time into chargeable hours is a challenge. Put simply however, the greater the productivity and recovery of fee earners, the higher the income.

For example, let's imagine a firm with 20 fee earners, all with an hourly chargeout rate of £195. Fee earners record an average of 1,100 chargeable hours each per year, and recover (i.e. bill) 80% of the recorded WIP value, resulting in total fee income of:

20 x £195 x 1,100 x 80% = £3.43million

If the fee earners are able to increase the recovery rate by just 1%, annual fee income and profitability will increase by £42,900.

A 1% improvement in productivity represents just one additional (and chargeable) 6-minute unit per fee earner per day.

A 1% improvement in both productivity and recovery increases income and profits by almost £80,000.

Time recording

In our experience, not all fee earners in many firms fully time record. This is often the case where the work is fixed fee, for example in residential conveyancing.

We sometimes see firms adopting a policy whereby fee earners are only required to record chargeable time and/or there is no minimum on the number of hours that must be recorded each day. This can result in a lack of accountability for non-chargeable time and can also have a negative impact on overall time recording.

Where fee earners do fully time record, it is common to see fee earners recording somewhere around four or five chargeable hours per day, and sometimes lower than this.

This raises an important question: if you do not know how long it takes to do a job, because your fee earners do not record their time, how will you be able to tell if it is profitable and therefore worth doing at all or whether individual fee earners are working efficiently? If fee earners are making the decision to not record all the time they have taken on a matter, you also risk a further reduction being made at the point of billing, or 'double discounting' and, while this will make an individual fee earner's recoverability statistics look good, it will damage underlying profitability.

Furthermore, without a full-time recording policy that is monitored and enforced, it is difficult to properly establish what 'capacity' looks like, and so working towards an appropriate level for fee earner gearing becomes difficult too.

In these situations, firms need to consider why time is not being fully recorded. Is it because work is being pushed down too much and fee earners feel out of their depth, or is there a deeper cultural point that needs to be addressed, with staff members feeling under pressure to charge less time to a particular matter?

Capturing all time spent on a client matter, for all work types, is essential, as too is capturing non chargeable time. Fee earners should be provided with targets for both productivity and recovery, which can then be monitored, and the process of recording time and billing should be made as simple as possible. Where fee earners are seen as 'rain makers', their use of business development time should also form part of the monitoring process.

Coming up with suitable productivity/ chargeable hours targets for each grade of fee earner can be difficult. We would expect more senior people with non-fee earning responsibilities to have a reduced productivity target, whereas more junior people with no other responsibilities at all should be looking at an above average target of upwards of, say, 1,200 or 1,300 hours. In some cases, where matter volumes are high, and the nature of work is more routine, this could go even higher. This may sound like a lot, but even after allowing for holidays, sickness, and other absences, it amounts to fewer than six chargeable hours per day.

Once you arrive at a target level of productivity and recovery, this should allow you to calculate target fees per fee earner, as well as for the firm, and compare them to our findings in section 4. You should be aiming to be in the upper quartile for your turnover band, which will hopefully move you into the upper quartile in section 6 (Profitability).

It is important to distinguish the benefits of time recording from the benefits of pricing work correctly. Nowadays, most client work performed by participants in this survey will be charged on a fixed fee basis. Clearly, valuing work properly is essential, but only with accurate and complete time recording will firms be able to assess whether the fees they have arrived at are reflective of the amount of work involved and, most importantly, are profitable.

Management information

Monitoring the performance of individual fee earners and the firm is only possible if you have accurate and reliable management information (MI). In our experience, many firms struggle to extract useful data from their practice management software, either because they do not know how or because their software has poor functionality and reporting capabilities.

Firms should use good quality MI to measure and track a small number of meaningful key performance indicators (KPIs). While there is no 'one size fits all' approach to measuring success in a business, and KPIs will commonly measure both financial and non-financial factors, there are common themes that will allow firms to benchmark themselves against their peers, and that is what this report explores.

If you already have good MI, consider sharing it with all fee earners. In our experience, the potential upside from doing this usually outweighs any potential drawbacks. Individuals who understand how they can have a positive impact on a firm's performance will often adapt their behaviours accordingly, and may feel that they have a greater personal investment in the business.

Key headlines in this year's survey (explanations for all of these will follow later):

6.8%
median practice fee income

median fee income per equity partner
£1,124,103

median cost of employed fee earner
£63,993
£62,347 2022

6.8:1
fee earners to partners

median chargeable hours
2023 **793** hours
2022 **816** hours

138
+1 day
year end lock up

median fee earner cost per hour **£118.74**

median fees per hour **£133.90**

median 'super profit'
2022 **£101,375**
2023 **£94,325**

turnover spent on non salary overheads
2023 **28.3%**
2022 **27.7%**

- Median practice fee income increased by 6.8%.
- Median fee income per equity partner of £1,124,103 (2022: £1,023,831).
- The median cost of a fee earner, including fixed share partners and notional salaries for equity partners, was £63,993 per fee earner, compared to £62,347 in 2022.
- The ratio of fee earners to equity partners decreased to 6.8:1 from 7.1:1 in 2022.
- The median number of chargeable hours recorded per fee earner was 793, down from 816 in 2022.
- The median hourly cost of a fee earner (based on 1,100 chargeable hours per year) was £118.74, compared to median hourly fees per fee earner of £133.90.
- The median spend on support staff, including secretaries, reception, HR, finance and other back office functions, was £22,731 per fee earner, compared to £22,402 in 2022.
- The median spend on non-salary overheads per fee earner was £43,886 compared with £38,791 in 2022, and as a proportion of fee income, non-salary overheads increased slightly, to 28.3% from 27.7% in 2022.
- Total year end lock up days (WIP and debtors combined) increased slightly from 137 days to 138 days.
- Median equity partner capital (combined total of capital account, current account and tax reserves in a partnership, or retained profits and directors' loan accounts in a limited company) rose slightly from £311,743 to £313,020 per partner.
- Median net profit per equity partner (before deducting notional salaries for partners) fell from £211,204 in 2022 to £209,650 in 2023.
- When we adjust the net profit figure to include a notional salary cost for equity partners, and also notional interest on partner capital, the median 'super-profit' for the year was £94,325 compared to £101,375 in 2022.

Fee income 4.

As in previous years, we start our detailed analysis by reviewing income growth. We have measured income performance by equity partner and by individual fee earner. We reveal the effects on revenue from changing the gearing in a practice; that is, the ratio of fee earners to equity partners.

Most of the charts throughout this and later sections include the results for two accounting years, and the results are analysed into turnover bands. Most charts include three figures for each turnover band; the lower quartile, median and upper quartile. The results for 2023 are shown as columns and numbers, and the results for 2022 are shown as a dash, i.e. - . The dashes show the like-for-like 2022 results for the participants in this year's survey, so may not correlate exactly with the findings from last year's survey.

Key points are:

- 73% of the participants in the survey reported year-on-year fee growth in 2023, with 34% seeing growth of over 10%. Smaller practices in the survey saw a wider range of fee change than other turnover groups, as shown in Figure 4.1.
- This is the 14th consecutive year that we have reported a median fee increase, although it should be noted that the composition of the sample across those 14 years will have varied. The last time we saw a general reduction in fees was in 2009, when firms were struggling with the impact of the global recession of the time.
- Participants reported median fee income per equity partner of £1,124,103 compared to £1,023,831 in 2022 – an increase of 9.8%.
- Following a small reduction in last year's survey, employment law bounced back strongly, with a median increase of over 13%, while all other specialisms registered positive results.

Figure 4.1: Change in fee income compared to previous year's fee income (%)

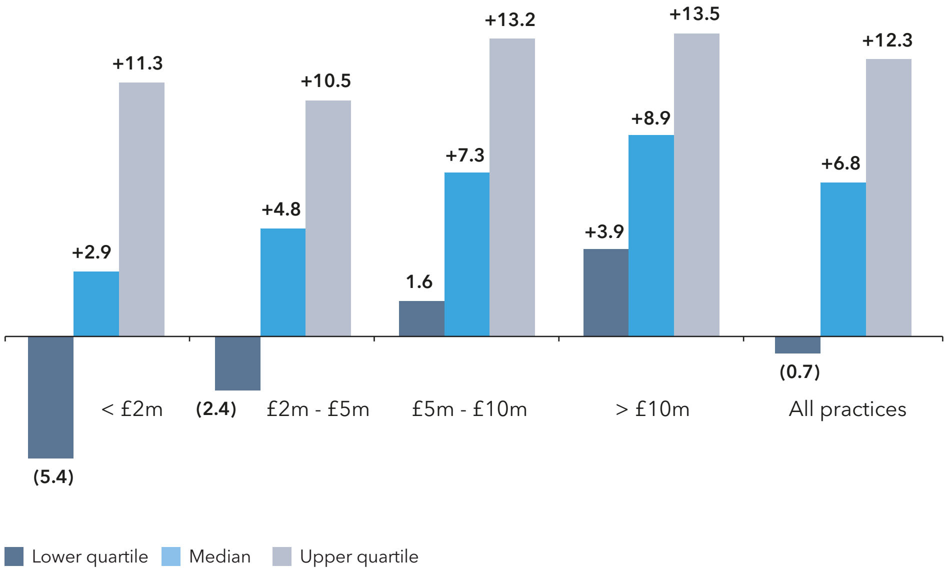


Figure 4.2: Median changes in fee income over the last 15 years (%)

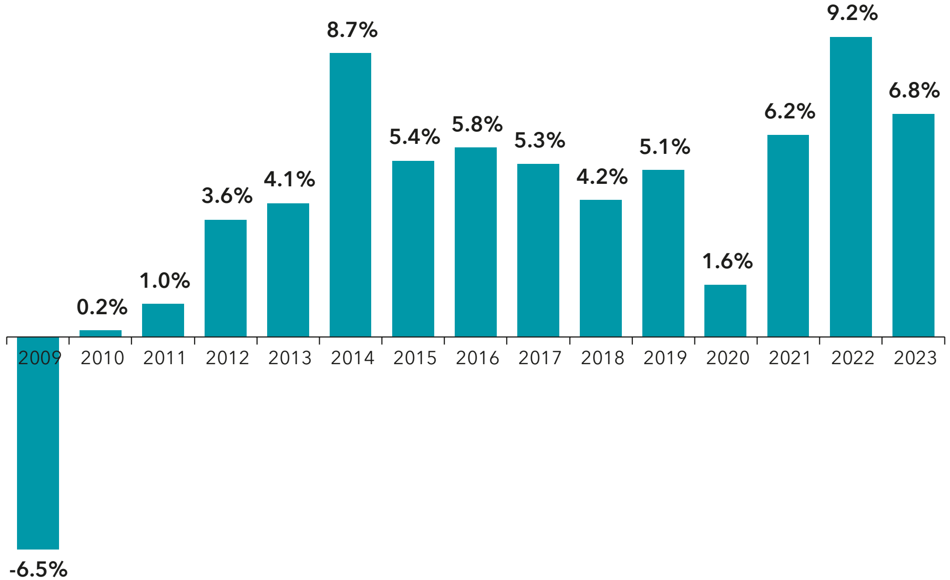
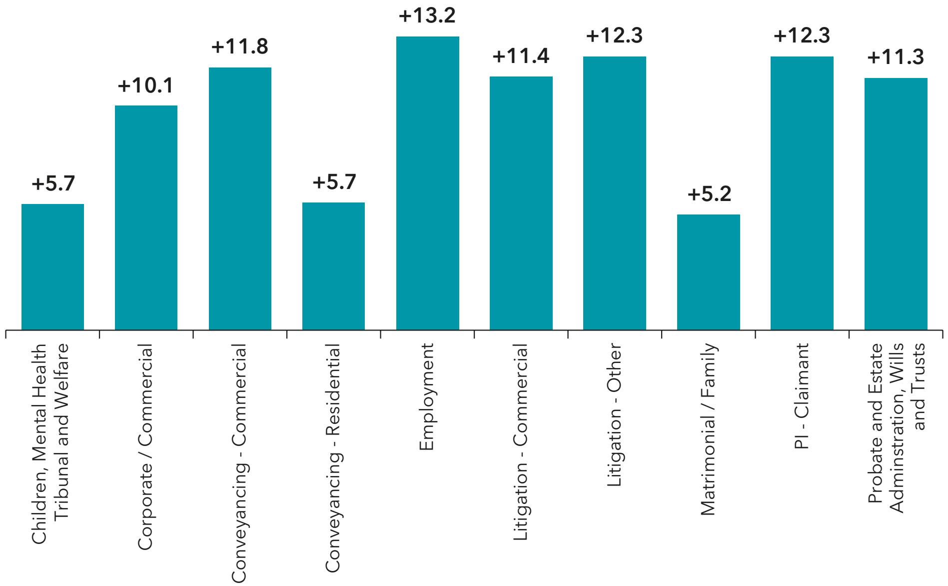


Figure 4.3: Change in fee income compared to previous year's fee income by specialism (%) (median figure only)

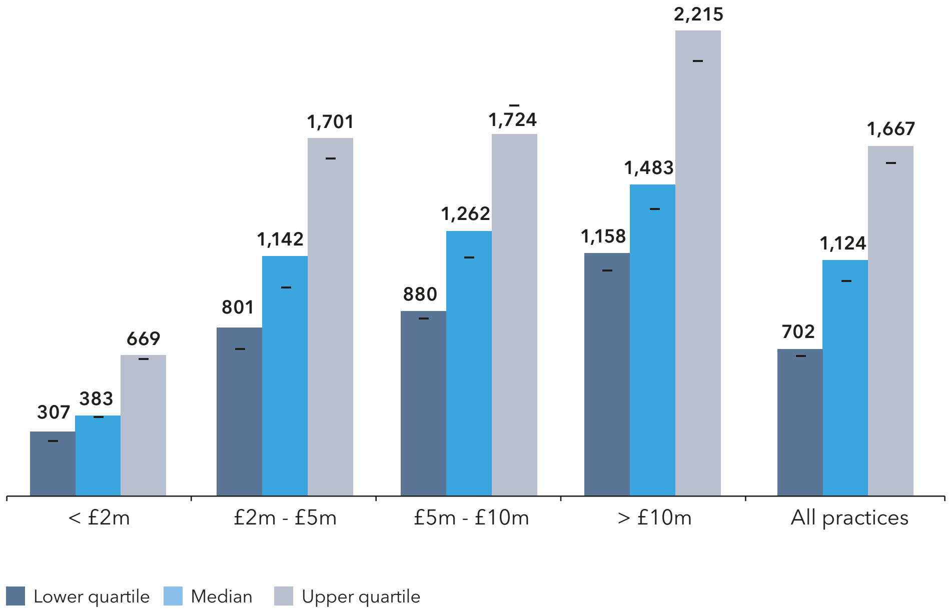


Equity partner performance

The majority of participants in the survey reported minimal changes to the number of partners between 2022 and 2023.

For most firms, the growth shown in Figure 4.1 has resulted from increased fee income per equity partner, rather than a reduction in partner numbers. All turnover groups saw a rise in fee income per equity partner, with a median growth of 9.8%.

Figure 4.4: Fee income per equity partner (£'000)



Income by individual fee earner

Key points here are as follows:

- The total number of fee earners for participating firms was 9,196 compared to 8,907 in those same firms in 2022.
- Average fees per fee earner were £147,285, compared to £138,925 in 2022 - an increase of 6.0%. Firms across most turnover bands saw an increase, apart from those in the £2m-£5m band, which saw a fall of 3.3%.
- Despite the overall positive picture, fees per fee earner is a recurring issue for all firms to focus on, and alongside this there needs to be close monitoring of productivity and recovery rates as discussed previously. Our view is that if fee earners are not fully recording both chargeable and non-chargeable time, then it is very difficult to know whether work is being carried out efficiently and profitably, or what real fee earning capacity looks like.
- Participants in this year's survey reported a median of 793 chargeable hours recorded per fee earner, compared to 816 in 2022. Firms have continued to tell us that staff recruitment is a big challenge and that existing members of staff are dealing with higher workloads. This is at odds with the financial information and highlights the importance of staff accurately recording, and ultimately charging, their time properly.

Figure 4.5: Fee income per fee earner (£'000)

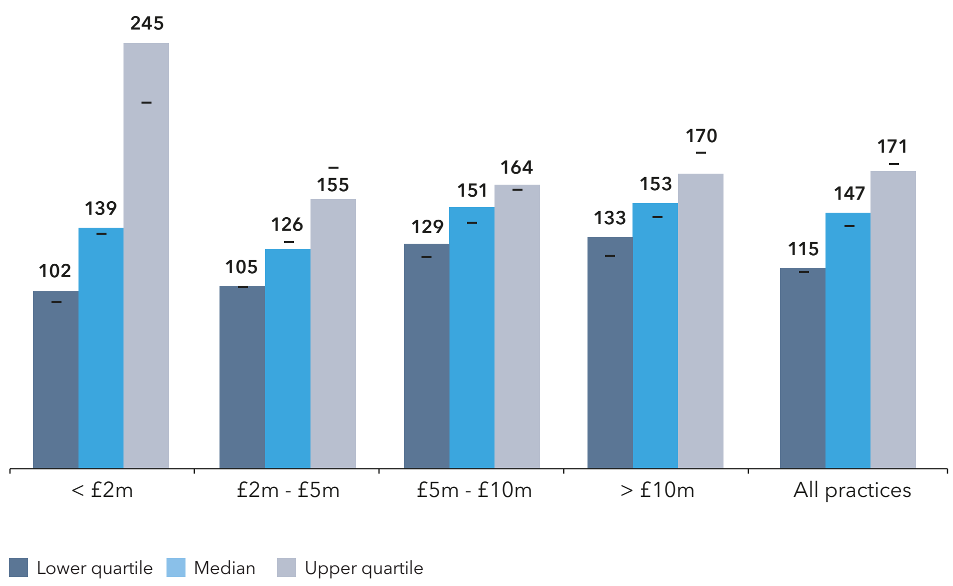
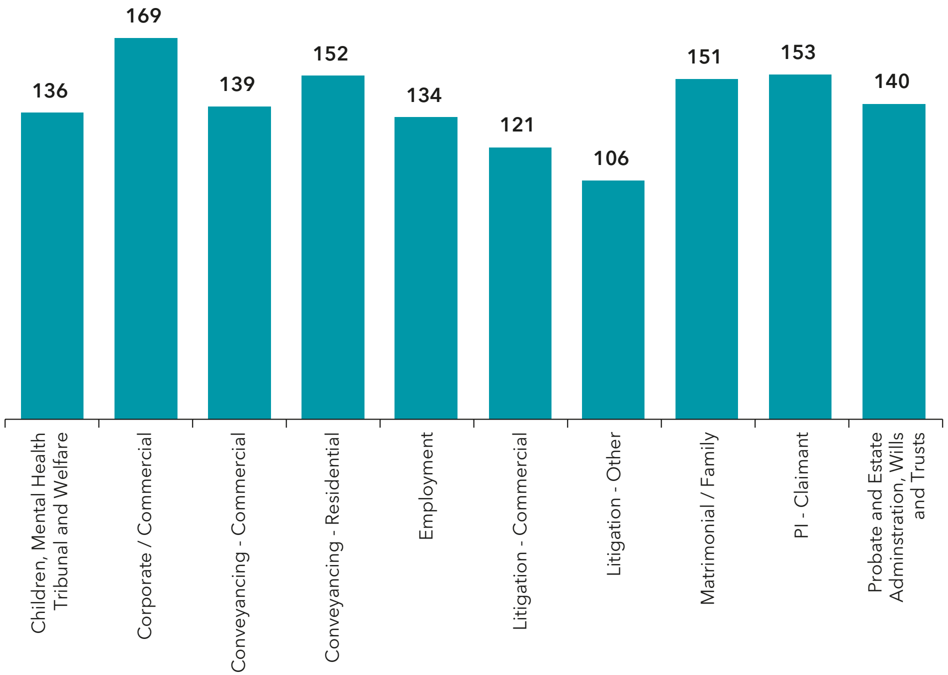


Figure 4.6: Fee income per fee earner by specialism (£'000) (median figure only)



Fee earner gearing

Fee earner gearing (the ratio of fee earners to equity partners) is a key indicator, not only as an absolute measure, but also as a trend over time.

In our calculations we have included equity partners in the number of fee earners unless they are non-lawyer managers. For example, if a firm comprises two equity partners and three other fee earners then the ratio is 2.5:1 (i.e. five divided by two).

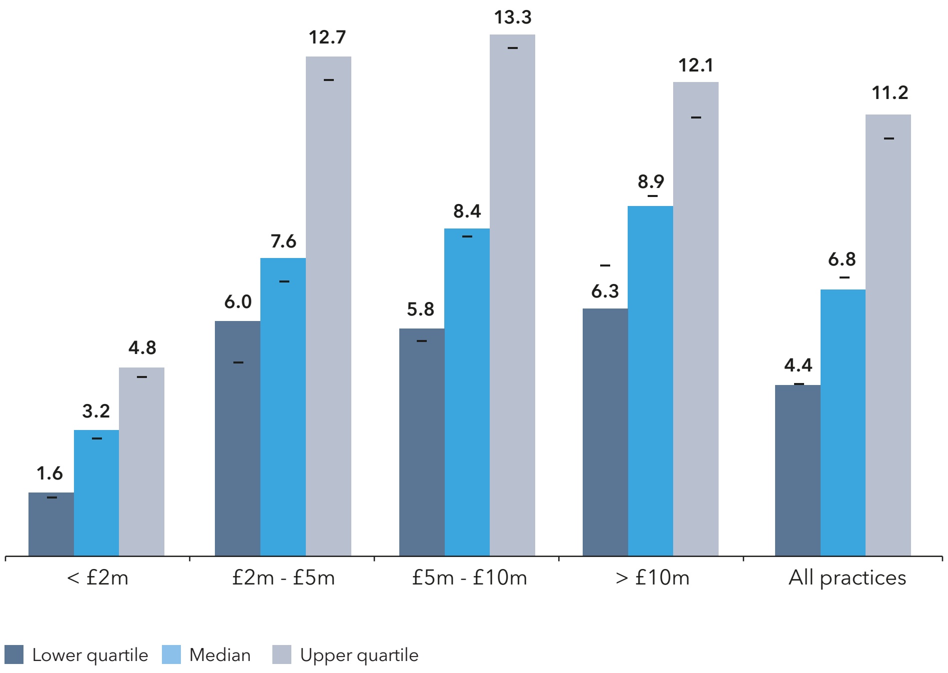
In improving economic conditions, the ratio of fee earners to equity partners tends to increase as firms grow, with the opposite happening in times of recession.

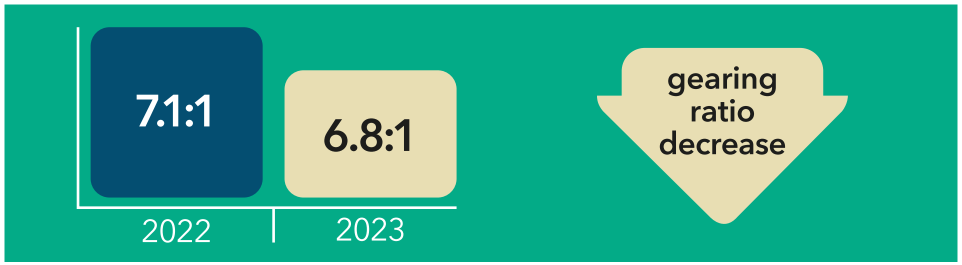
This is certainly true in our surveys. Back in 2009, when Hazlewoods first carried out the survey, the median ratio was 4:1, and the general economic climate then was challenging. Since then, we have seen a steady rise in fee income, and the gearing ratio gradually crept up to 6.0:1 immediately prior to the pandemic. While the current year shows a median of 6.8:1, this has fallen from 7.1:1 in 2022.

As noted previously, we have not seen a significant rise in the number of equity partners across firms and so, while firms continue to struggle to find and keep high quality employees, there is clearly no appetite to increase gearing unnecessarily.

Another factor to be aware of is that fee earner gearing can vary between different departments in the same firm, and we tend to see higher gearing in teams such as residential conveyancing and high-volume personal injury work, and lower gearing in more specialised technical teams, such as complex litigation and corporate work, which generally require a larger amount of senior fee earner involvement.

Figure 4.7: Number of fee earners per equity partner





Chargeable hours

As explained in section 2, productivity (i.e. the amount of chargeable time recorded) has a direct impact on fee income and profitability, as every additional chargeable unit that can be recorded and billed goes straight to the bottom line.

We asked participating firms for the total number of chargeable hours recorded by all of their fee earners (including partners), and the findings are shown at Figure 4.8.

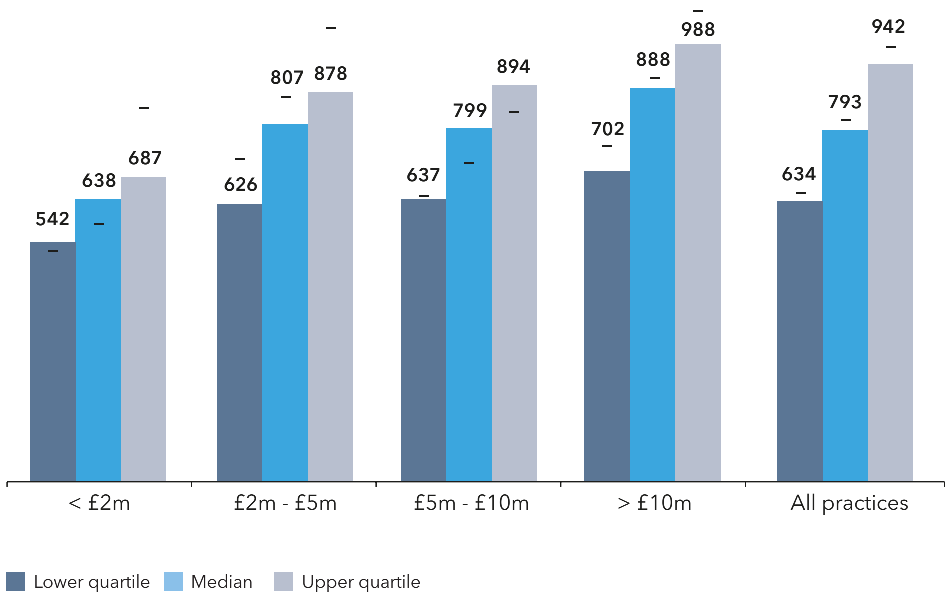
The findings are likely to be a surprise, as the general rule of thumb used by many firms is that fee earners should be charging between 1,000 and 1,100 chargeable hours per year.

An overall reduction in the median number of chargeable hours, from 816 in 2022 to 793 in 2023, is concerning, and continues the trend seen last year when we asked firms for information for the first time.

When you consider that a full time fee earner working 35 hours per week has a capacity of 1,600 chargeable hours per year, after allowing for holidays, sickness and training, it is a surprise that the actual median is so low.

As noted in section 2, we would expect more senior people with non-fee earning responsibilities to have reduced productivity, but more junior people with no other responsibilities at all should be looking at upwards of 1,200 or 1,300 hours, depending on work type and experience.

Figure 4.8: Chargeable hours recorded per fee earner



Employment costs

People represent not just the greatest asset for law firms, but also the primary cost. The total costs are broken down into three principal categories:

- Equity partners
- Fee earners
- Support staff

Figure 5.1 compares the total cost of all these people against fee income. This includes notional salaries for equity partners, which we have once again set at the same level of the median highest employed fee earner's salary for the size of practice, plus 15%, to reflect Employer's NIC and employer pension contributions.

The median 2023 total is 61.6%, compared to 61.4% in 2022, giving a median gross margin/contribution of 38.4% (2022: 38.6%). This slight drop in margin indicates that fee earner costs have risen by slightly more than the growth in fee income that we saw in the previous section.

As noted above, most law firms that we speak to carry out pay reviews that tie in with their year ends, and so it is likely that many firms in our survey had already fixed salaries for the 2023 year end early in 2022 before many of the cost of living increases had really taken hold. It is likely therefore that we will see the delayed impact next year.

As noted in previous years, a key challenge facing all law firms is the need to attract and retain high quality staff. This, and the ongoing increases in cost of living, mean that firms have felt under greater pressure to increase salaries, but many firms have struggled with how best to structure increases in remuneration.

In our experience, very few firms elected to make one-off lump sum payments to staff, choosing instead to focus on their overall remuneration packages, including options such as staff bonuses, increased levels of employer pension contributions, improved holiday entitlements and the introduction of other benefits such as health cover.

Many firms have been cautious about locking in large % salary increases tied to high inflation rates that should ultimately return to 'normal' levels. We have seen that staff members have been largely receptive to non-salary related benefits.

Although we have not yet seen a significant rise in employment costs as a percentage of fee income, it is likely that this will increase over time unless firms can effectively address the apparent fall in chargeable hours per fee earner.

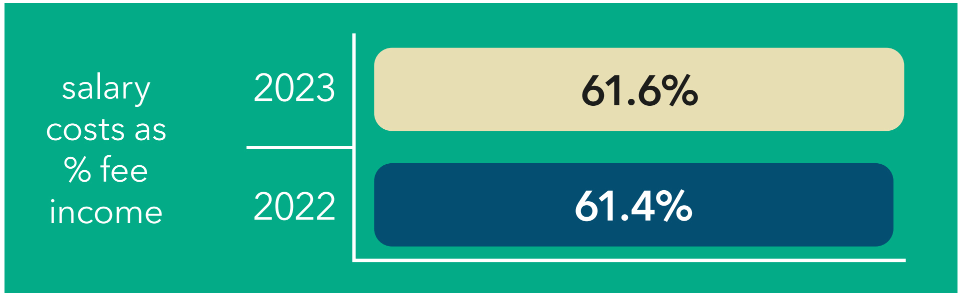
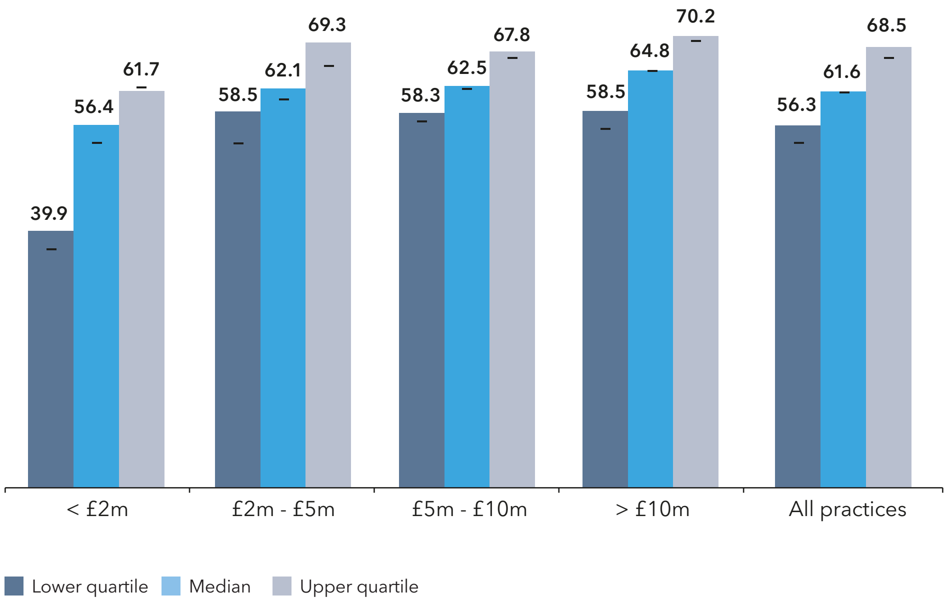


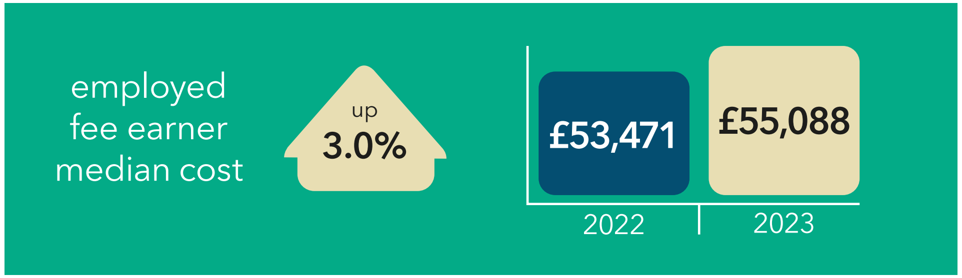
Figure 5.1: Total salary costs, including notional salaries, as a percentage of fee income (%)



Employment costs – employed fee earners

Having established the contribution margin, we can now look in more detail at how much firms are spending on their employees. In Figure 5.3 we include salaries, fixed share partners, consultants, temporary staff and all usual payroll and pension costs for fee earning staff. However, no redundancy or recruitment costs are included here, nor any notional salaries for equity partners.

In terms of actual head count on a full-time equivalent basis, the total number of people employed in a fee earning capacity across all participants in our survey was 9,196 in 2023, compared to 8,907 in 2022 – an increase of 289 people (3.2%).



Key findings are:

- Expenditure on fee earners as a percentage of fee income is consistent for larger firms but higher for firms with turnover lower than £5m.
- The median cost of an employed fee earner rose by 3.0%, from £53,471 in 2022 to £55,088.
- The average fee earner cost is not consistent across all turnover bands, and as you might expect, rises in line with firm size. Firms with the highest fee income are generally employing more expensive staff, as shown by the notional salaries detailed in section 6.

Figure 5.2: Expenditure on employed fee earners as a percentage of fee income (%)

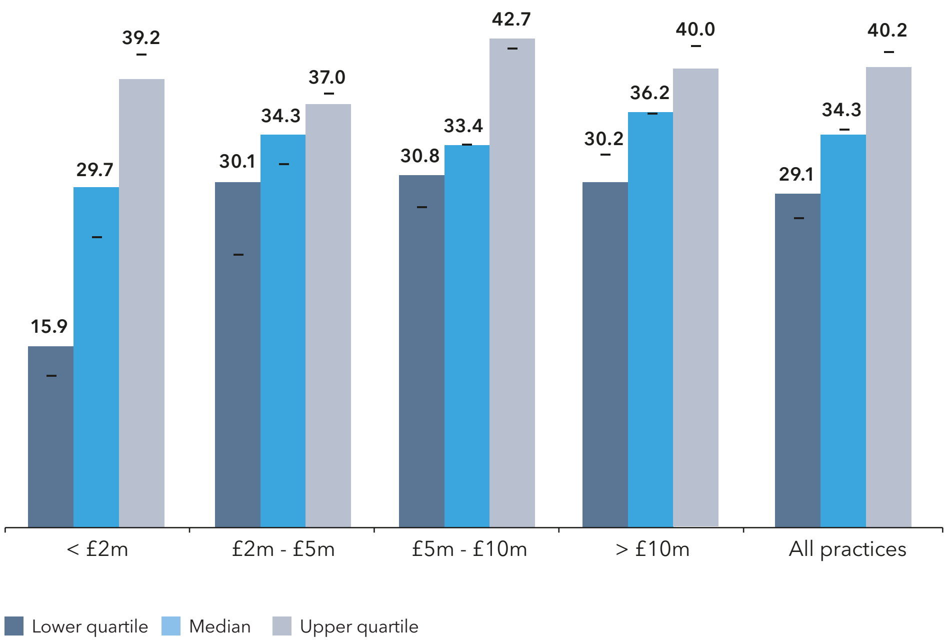
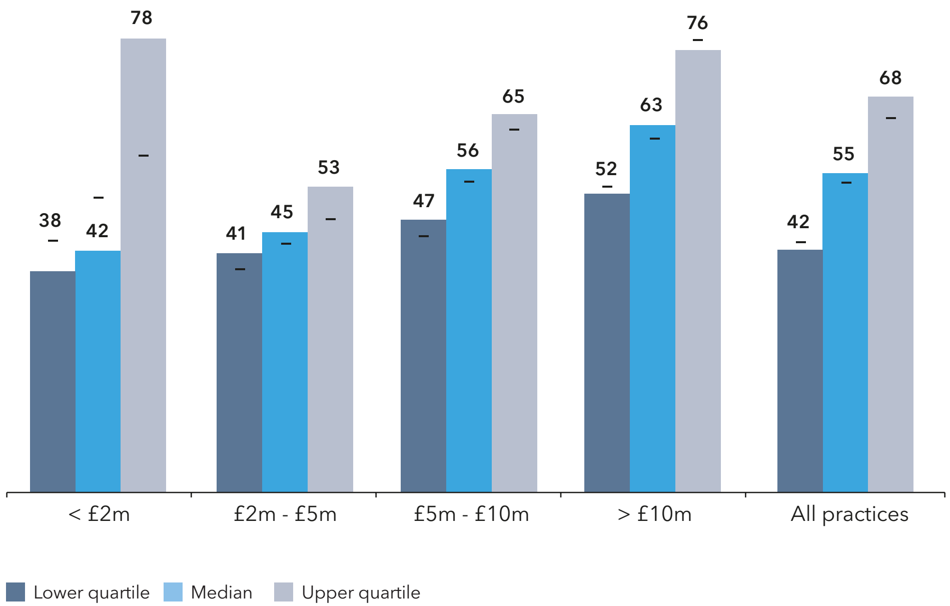


Figure 5.3: Cost per employed fee earner (excluding notional salaries for equity partners) (£'000)



Employment costs – all fee earners, including equity partners

Building on the results in Figure 5.3, we now show the cost per fee earner, including a notional salary cost for equity partners. This graph shows the "true" cost of a fee earner, combining employee salaries, fixed share partners' profit shares, consultants, temporary staff and normal payroll and pension costs, and a notional cost for the equity partners.

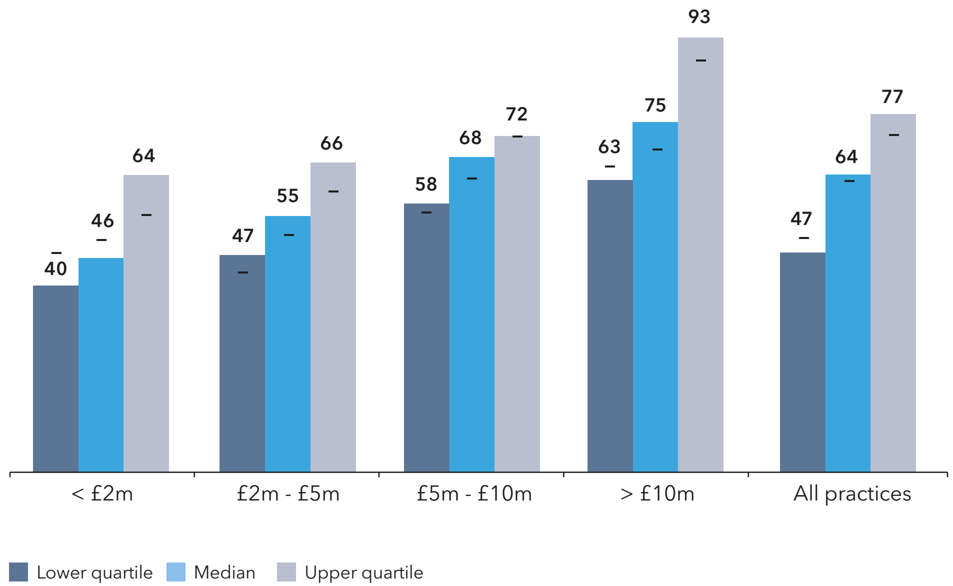
Notional salaries are based on the highest fee earner salary for the turnover band, plus an extra 15%, to reflect the additional costs that would have been incurred if the equity partners had been employed, such as employer's NIC and pension contributions.

When equity partners are included, the median 'true' cost of a fee earner increases to £63,993, up 2.6% from £62,347 in 2022.

Notional salary rates are shown on Figure 6.4. The median notional salary across all turnover bands is £123,000 although, as with other staff costs, notional salaries vary depending on the size of the firm.

The median notional salary increased by 7.1% in 2023, with the highest median increase being seen across £2m-£5m turnover firms.

Figure 5.4: Cost per fee earner (including notional salaries for equity partners) (£'000)



Employment costs - support staff

In terms of actual head count on a full-time equivalent basis, the total number of people employed in a non-fee earning capacity across all participants in our survey was 6.577 in 2023, compared to 6,387 in 2022 – an increase of 190 people (3.0%).

secretaries per fee earner
0.48:1

other support staff per fee earner
0.37:1

median cost per support staff
Consistent

Consistent
median support staff cost per fee earner

Within that total we looked in more detail at their specific roles and identified the following statistics:

- The number of secretaries per fee earner increased very slightly, from 0.47:1 to 0.48:1.
- The number of other support staff per fee earner (accounts, administration, marketing, receptionists, IT, etc.) also increased slightly from 0.36:1 to 0.37:1.
- As a result of these small increases in support staff gearing, the total expenditure on support staff as a percentage of fee income has increased slightly, from 16.1% to 16.6%.
- The median cost per member of support staff (including secretaries) was largely unchanged at £26,289 in 2023 compared to £26,224 in 2022 and the median support staff cost per fee earner, including secretarial support, was similarly static at £22,731 in 2023, compared to £22,402 in 2022.
- These results suggest that firms are generally satisfied with their levels of non-fee earning staff members, and are operating at a reasonably efficient level.

Figure 5.5: Expenditure on support staff as a percentage of fee income (%)

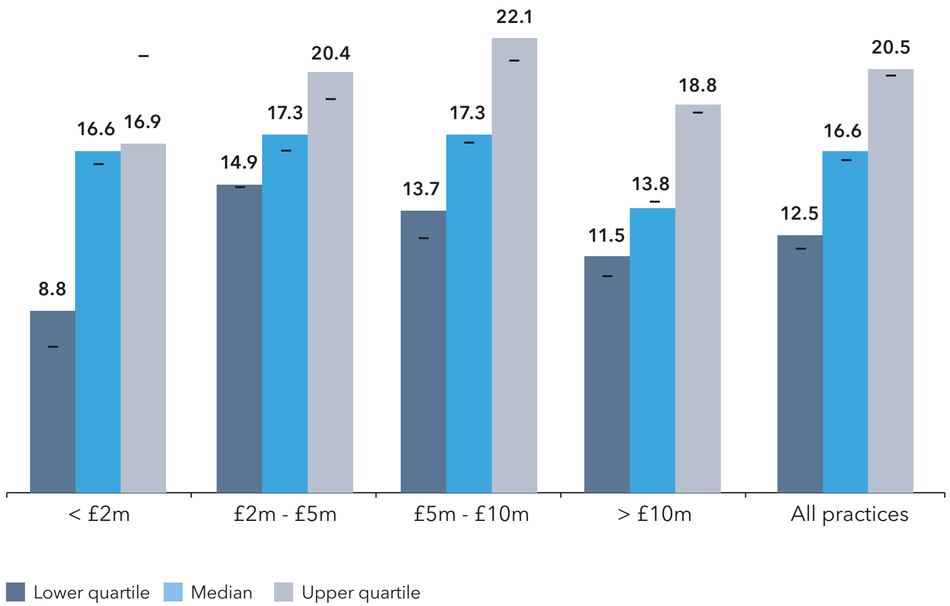


Figure 5.6: Cost per support staff member (£'000)

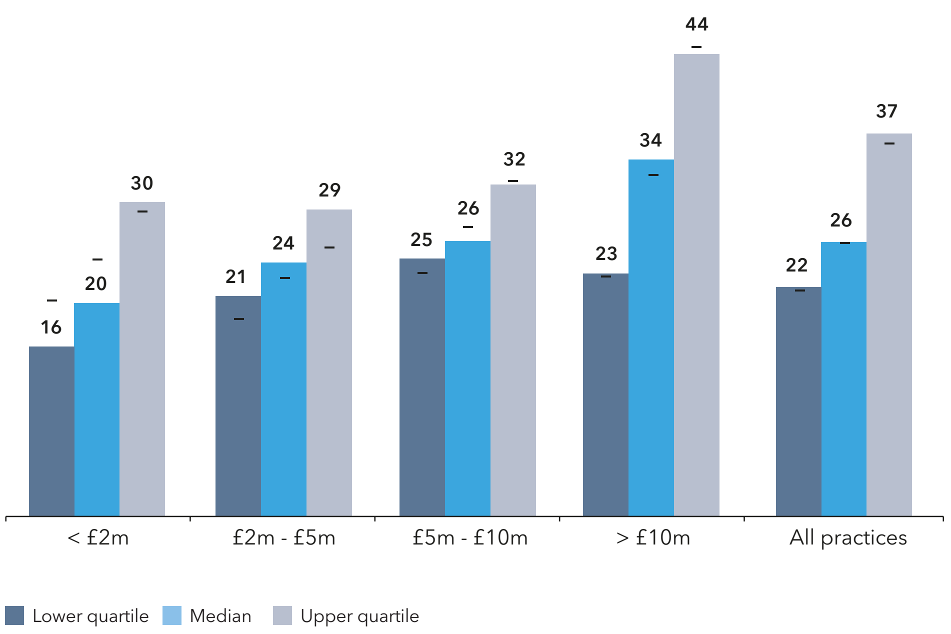


Figure 5.7: Number of secretaries per fee earner

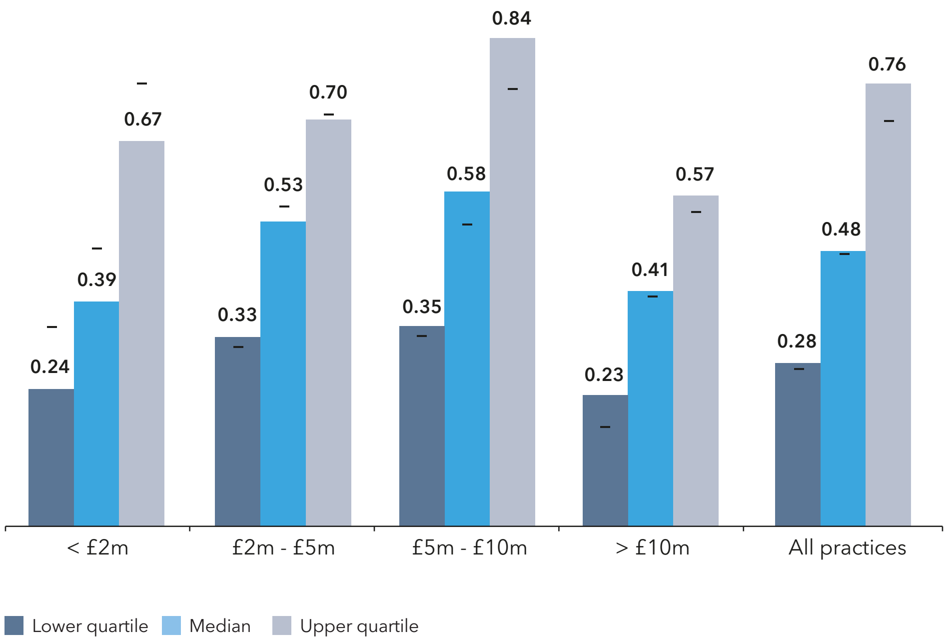


Figure 5.8: Number of other support staff per fee earner

Figure 5.9: Cost of support staff per fee earner (£'000)

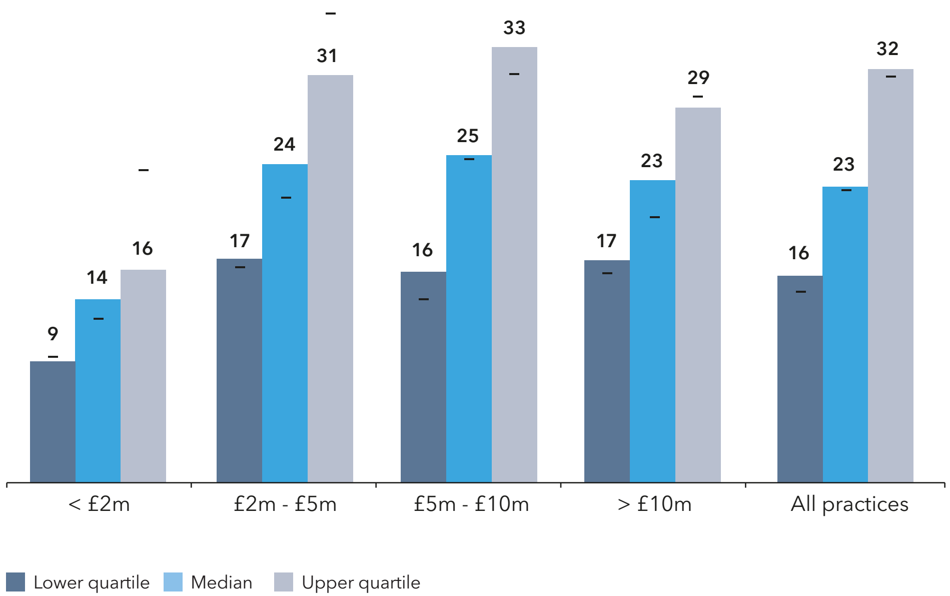
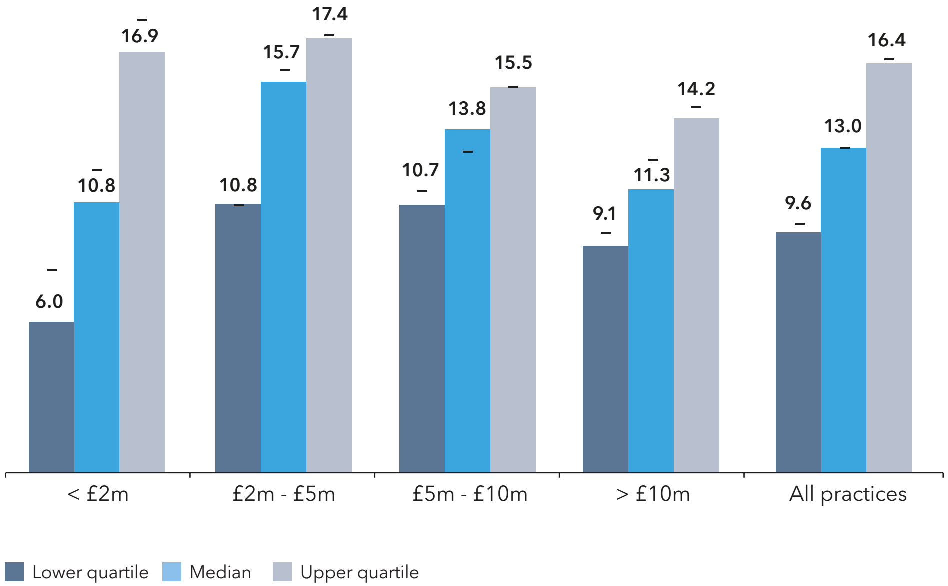


Figure 5.10: Total FTE headcount per £1million of fee income



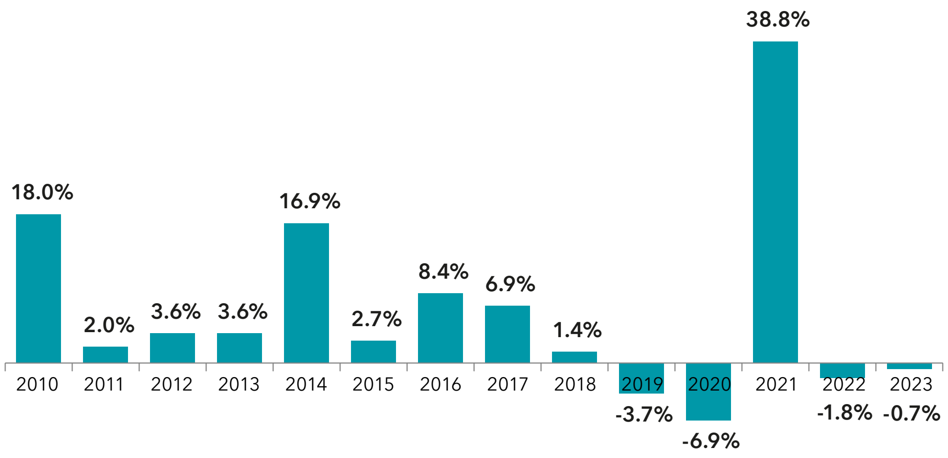
6. Profitability

Last year, we reported that, following higher than expected profitability across many firms during Covid, levels of profit per equity partner (PEP) had returned to pre-Covid patterns, with firms overall reporting a small fall. We noted that 2021 had been an exceptional year for many however, and that profit levels remained well above pre-pandemic levels.

In 2023, PEP has fallen again for the second year in a row, though only by a relatively modest amount.

The chart opposite summarises median changes in PEP as reported in our last 14 surveys. Whilst the composition of the sample will have varied each year, it provides a useful reminder of how firms have fared in that time and highlights the fact that, whilst we have seen recent drops in PEP, in aggregate these have been well below the increase seen in 2021.

Median changes in PEP (%)



This year, we saw a very steep increase in interest received by firms on money held in their client accounts. Across all the firms surveyed, total net interest income rose to £27.5m in 2023, compared to £2.6m in 2022, representing a total increase of over 1,000%. The median increase across all firms in this report was 824.0%.

If we were to remove interest earned from the 2022 and 2023 PEP totals, we would see that 2023 PEP fell by 7.85%, rather than the 0.7% shown in the chart on the previous page. Because of uncertainties around how long the current high levels of interest will remain, we would view this as a more realistic measure of the fall in sustainable trading PEP across firms.

Despite this rise in interest income, median net profit margins fell from 22.3% in 2022 to 21.0% in 2023, with the firms with turnover below £2m seeing the largest fall, from 30.6% in 2022 to 24.4% in 2023.

Over a quarter of fee income was spent on non-salary overheads, with a median cost per fee earner of £43,886, compared to £38,791 in 2022. These overheads made up 28.3% of fee income in 2023 compared to 27.7% in 2022.

We have looked in further detail at the breakdown of this expenditure, and in particular specific costs such as professional indemnity insurance cover, marketing, accommodation costs, staff recruitment and external staff training later in this section.

There is no single obvious area of increased spend across most firms this year, though there has been an ongoing trend of increases in costs such as marketing and PI insurance.

If we combine the findings in sections 4, 5 and 6 of this survey, we arrive at the proportions shown on the following pie chart.

Overheads and profitability as a proportion of fee income (median results only)

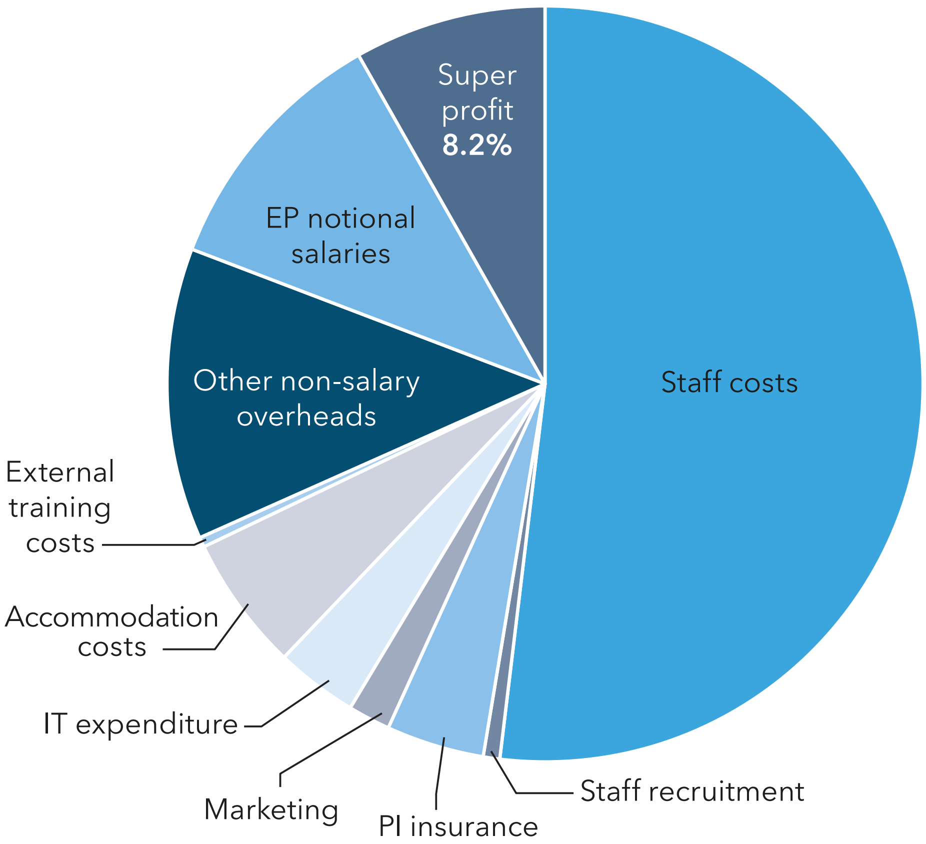


Figure 6.1: Profit per equity partner (£'000)

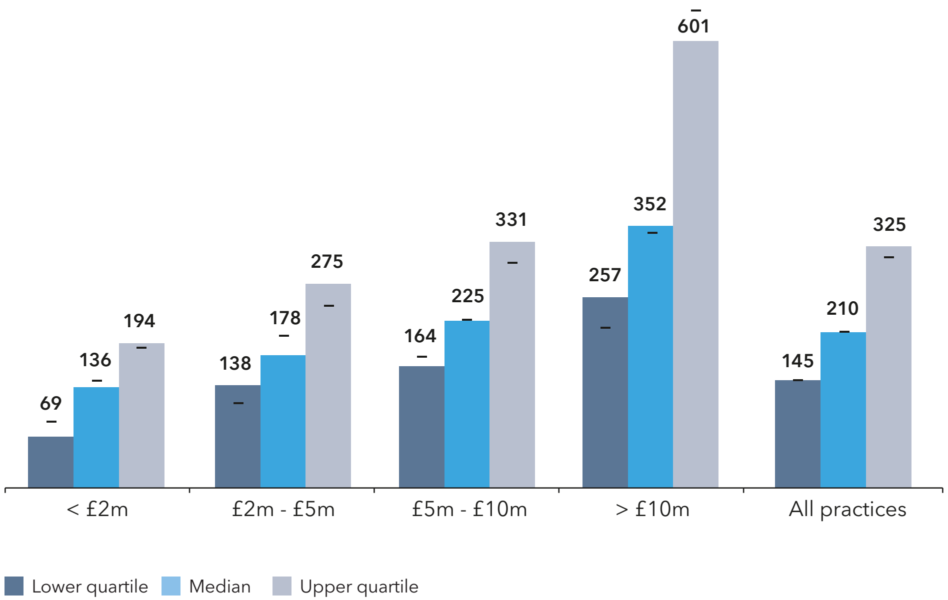


Figure 6.2: Profit per fee earner (£'000)

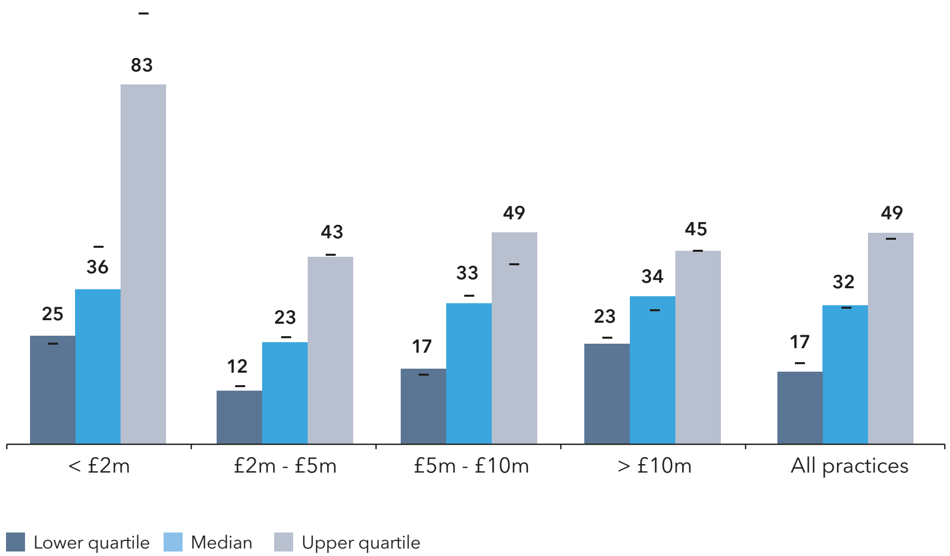
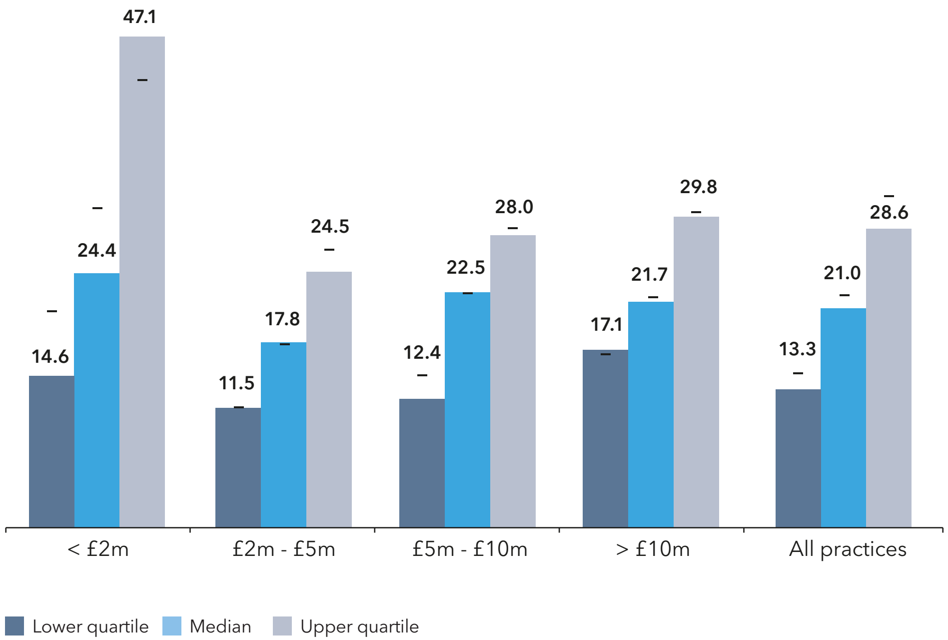


Figure 6.3: Profit as a percentage of total income (%)



Profitability – return on investment, i.e. super-profit

As law firm owners, equity partners expect to be rewarded with a 'salary' equivalent for the work that they do. They also expect a return for their capital invested in the practice and an additional super-profit for the additional risk that they face through being business owners rather than employees. We refer to these three layers of remuneration as notional salary, notional interest and super-profit.

As noted in section 5, equity partner notional salaries have been calculated based on firms' highest fee earner salary plus an extra 15% to reflect the incidental costs of employment such as employer's NIC and pension contributions.

Notional interest has been set at 5% of partner capital/company reserves for 2023 and 3% for 2022. For a number of years, the notional interest rate used in this report had remained at 3% to reflect the level of inactivity with bank base rates. For the 12 months between March 2022 and March 2023, the Bank of England base rate increased by 3.5% at a fairly consistent rate, hence the increase in the notional rate applied this year.

Total super-profits are simply the net profit less notional salaries and notional interest.

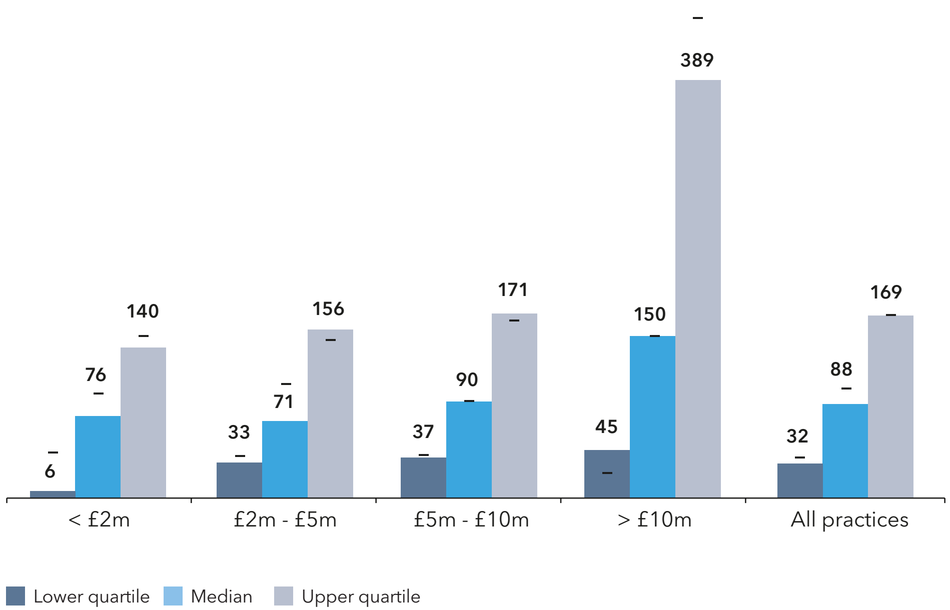
In Figure 6.4 we show the super-profit per equity partner. In 2023, the median super-profit was £87,697, compared to £101,375 in 2022. This fall is expected due to a number of factors:

- The drop in PEP that we saw in Figure 6.1
- The increase in the notional salary per equity partner seen in Figure 6.4

We also noted that super-profits per fee earner have fallen, from a median of £13,244 in 2022 to £12,264 in 2023.

15% of firms in our survey reported a super-loss, suggesting that partners in those firms could (in theory) have earned more by being employed somewhere else.

Figure 6.4: Super-profit per equity partner (£'000)



Notional salaries (£'000)

2023	50	104	118	189	123
2022	49	85	125	179	115

Figure 6.5: Super-profit per fee earner (£'000)

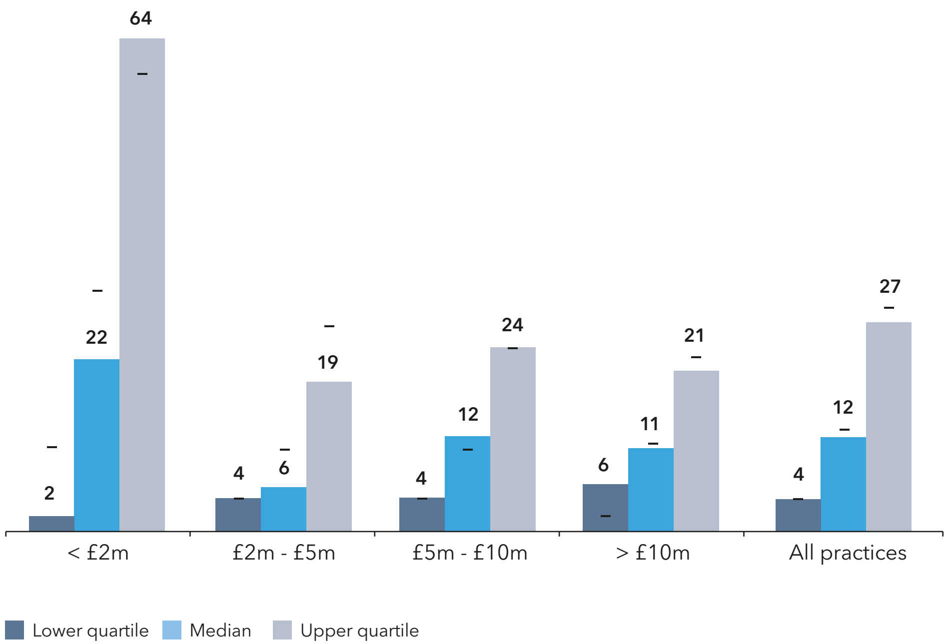
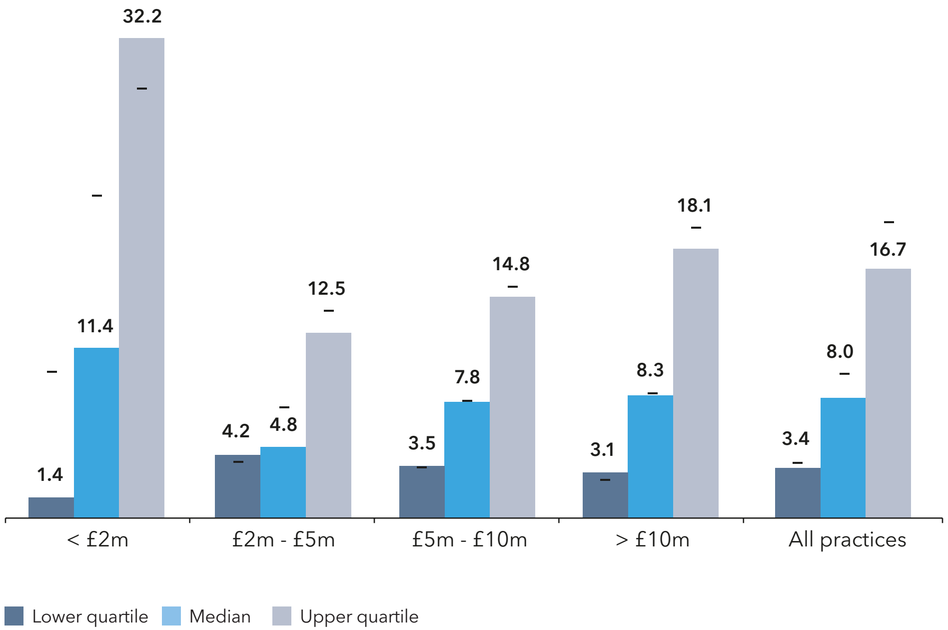


Figure 6.6: Super-profit as a percentage of total income (%)



Return on capital employed (ROCE)

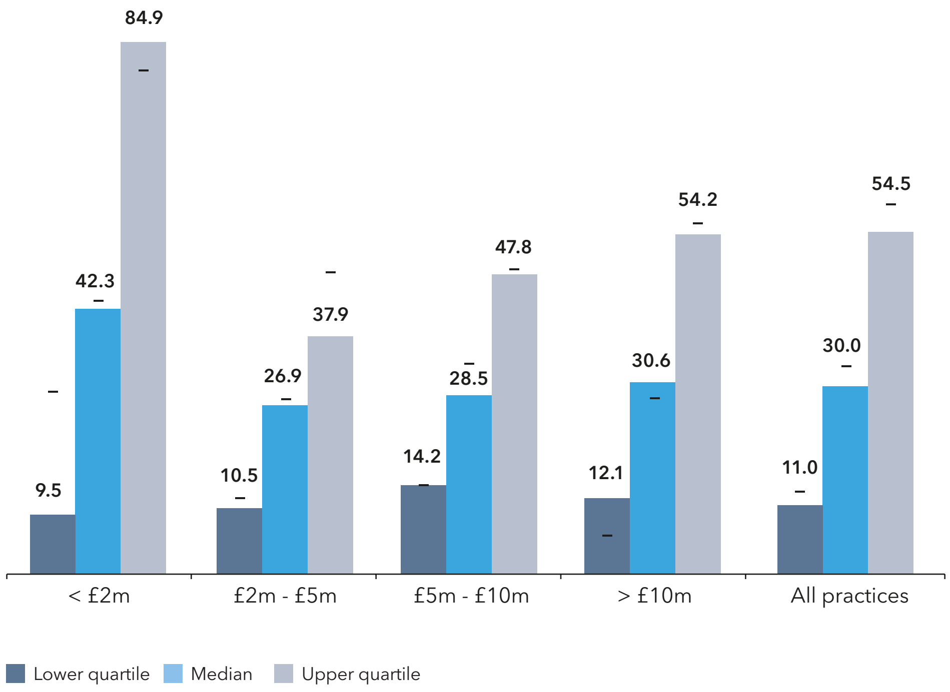
ROCE is a measure of the returns made by a firm on the resources available to it. For a law firm, ROCE is measured in terms of super-profits as a percentage of partner capital in a partnership or LLP or retained profits and share capital in a limited company.

In the context of the returns made to the owners of a law firm, we use super-profit, as this takes account of notional salaries for partners, and notional interest on partners' capital and so is representative of the reward to the partners for the risk they take in being owners of the business.

The results show a median ROCE of 30.0% for 2023, compared to 33.0% in 2022. Naturally, firms looking to attract new partners will be more successful with higher levels of ROCE and the range of returns between the lower performers and the higher performing firms is apparent.

ROCE is a key measure for potential investors in law firms, including other law firms and other acquirers who will pay more when a practice is achieving ROCE in line with the best performers in their size category, particularly when the costs of borrowing for investment are currently much higher than they used to be.

Figure 6.7: Return on Capital Employed (super-profit as a percentage of partner capital) (%)



Non-salary overheads

The charts over the next few pages show that, whilst firms have continued to work hard to control their overheads, there has been an increase overall, albeit a modest one. Overall, non-salary overheads have remained fairly consistent, across all turnover bands.

As shown on the historical analysis, the amounts spent on marketing have returned to pre-pandemic levels as firms have re-embraced physical activities rather than relying solely on their online presence. There has also been a continued increase in the proportion of fee income being spent on PI insurance, though this rise is not as sharp as those seen between 2019 and 2021.

IT expenditure has continued to rise as, although much of the expenditure on bringing home working into normal practice is in the past, many firms have begun to restart projects that had been paused due to Covid. We are also seeing large increases in software costs, partly driven by consolidation.

Median spend on non-salary overheads (as a % of fee income)

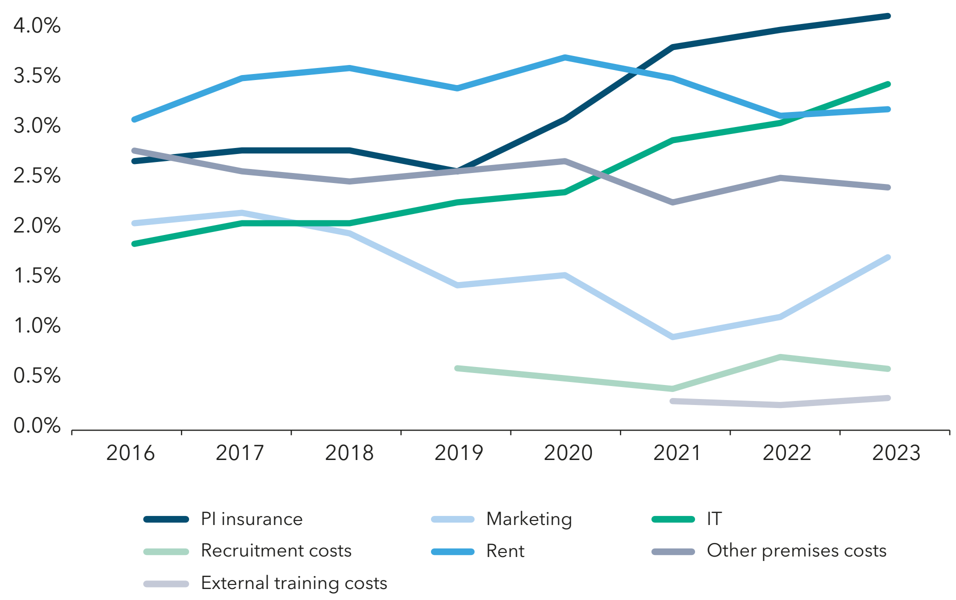


Figure 6.8: Non-salary overheads as a percentage of fee income (%)

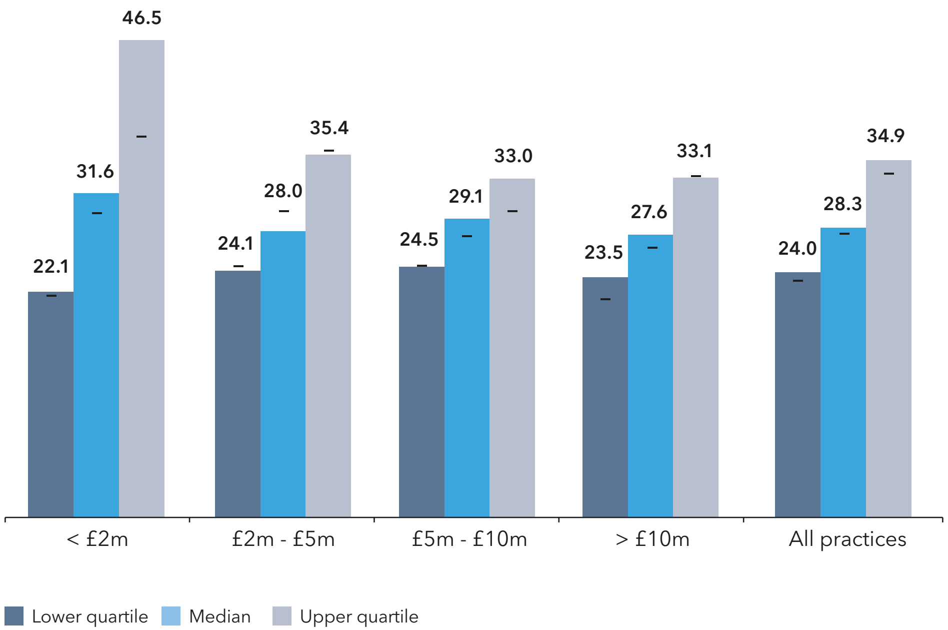


Figure 6.9: Non-salary overheads per fee earner (£'000)

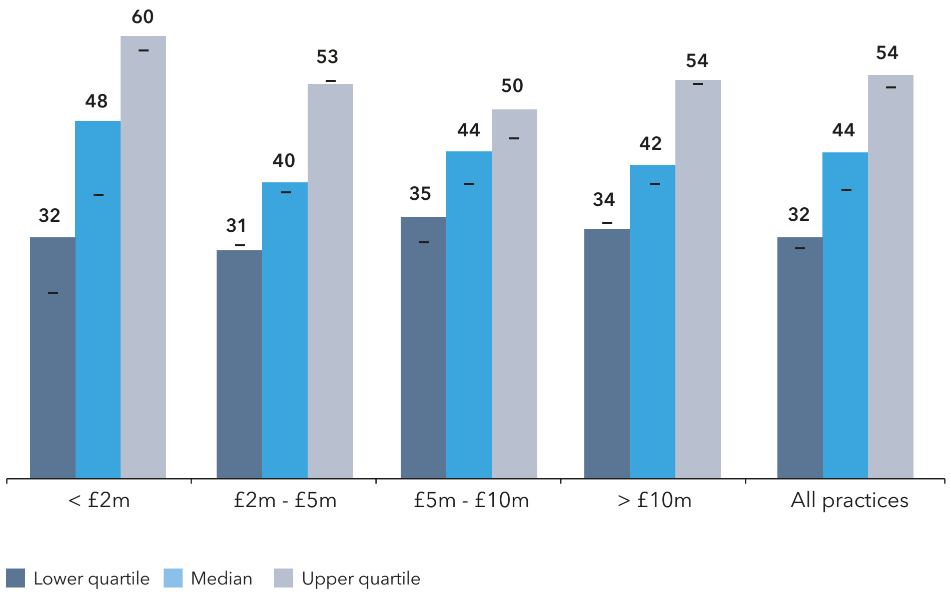


Figure 6.10: PI insurance premium expenditure as a percentage of fee income (%)

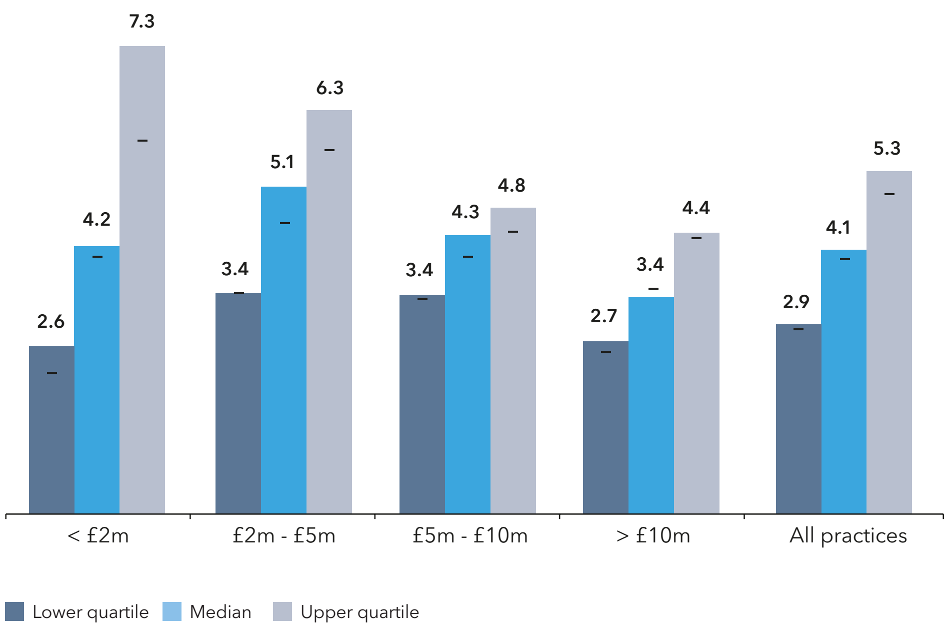


Figure 6.11: Marketing expenditure (including staff costs) as a percentage of fee income (%)

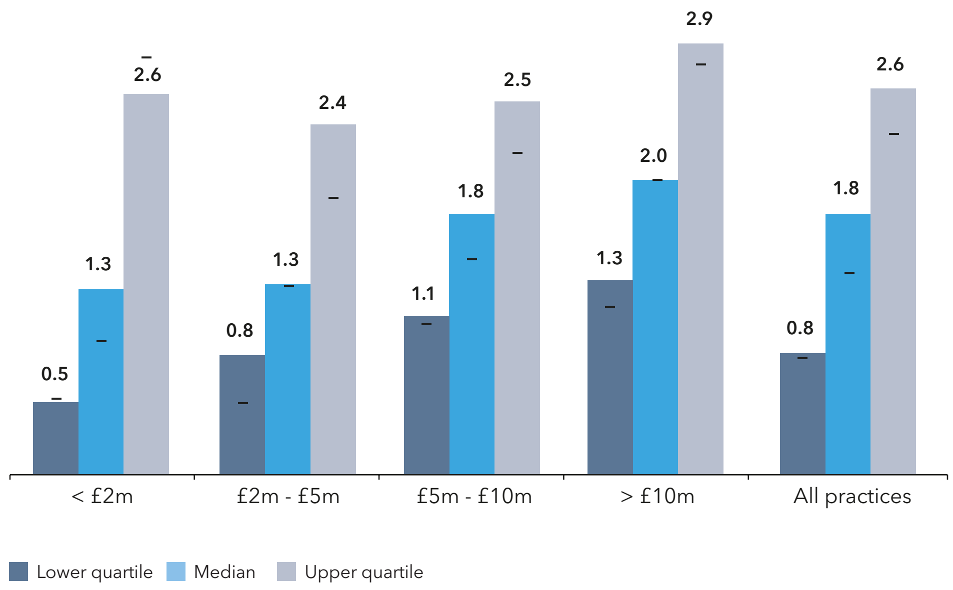


Figure 6.12: IT expenditure (including IT support, IT consultants and cloud-based storage) as a percentage of fee income (%)

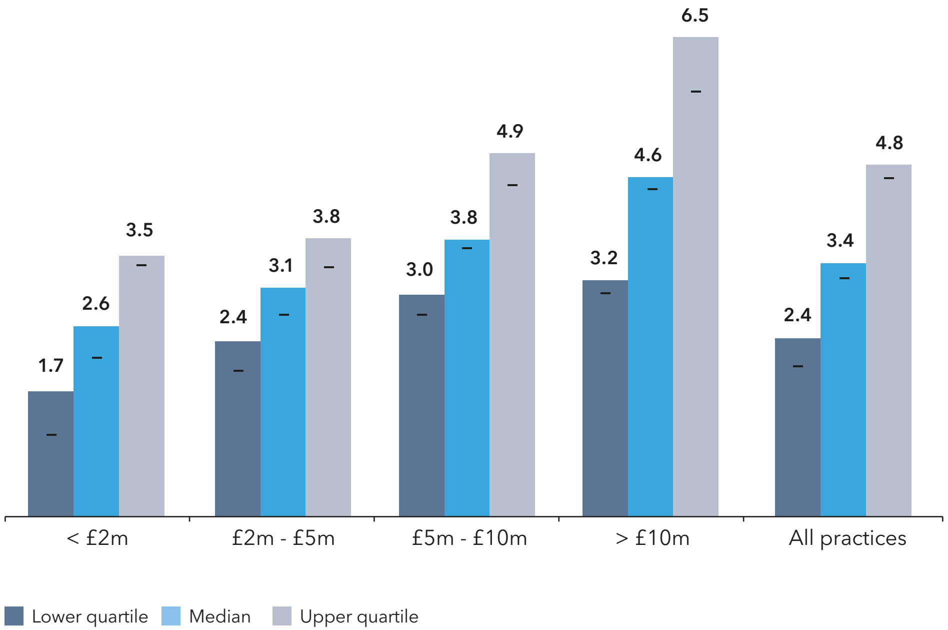


Figure 6.13: Staff recruitment costs (external or in-house) as a percentage of fee income (%)

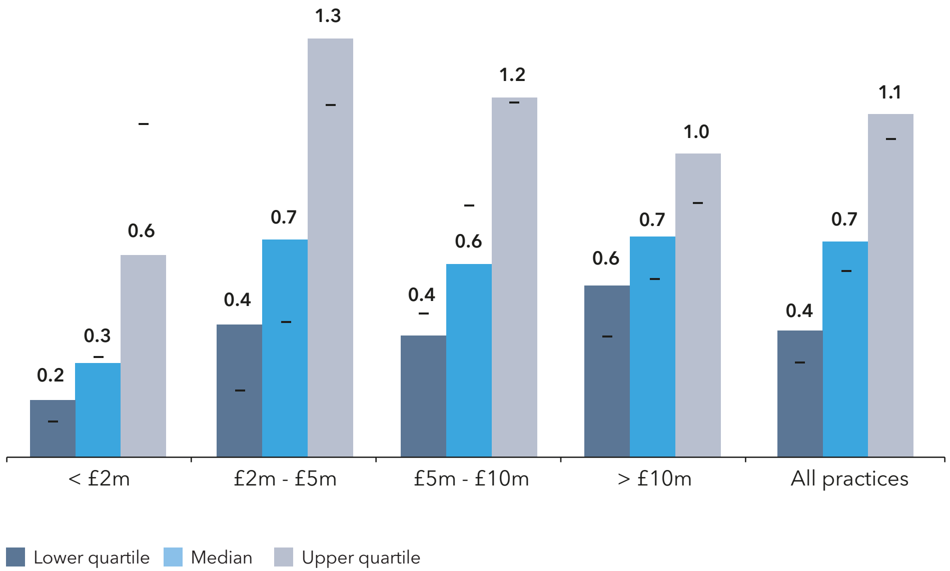
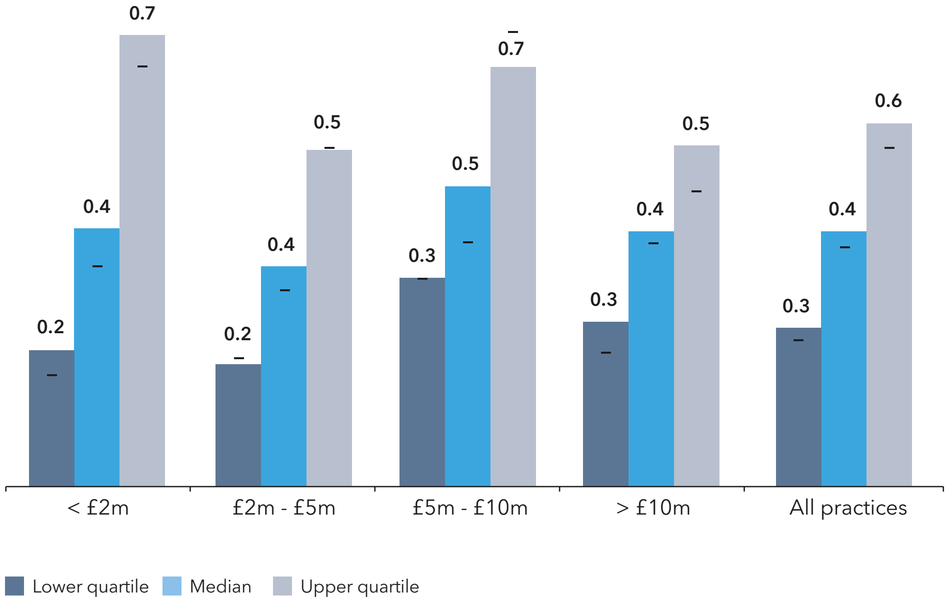


Figure 6.14: External training costs as a percentage of fee income (%)



Accommodation costs

After staff-related costs, accommodation costs are usually the next largest expense for any law firm. Accommodation costs typically consist of rent, rates, office insurances and office running costs such as day to day utilities.

The results here show a median spend on accommodation costs of 5.7% of fee income, up slightly from 5.6% in 2023.

As noted previously on the historic analysis, rent costs, which had been decreasing over the past couple of years, have now stabilised as firms have found a better understanding of their office space requirements, though we expect to see this statistic fluctuating over time as long-term leases come to an end.

A few firms in the survey pay a reduced rent on their premises, either because the property is owned by the principals or former principals of the firm, or because they have managed to negotiate reduced rent with their landlords. Where this is the case, those firms have provided us with a current market rental value so that the results shown are comparable across the board.

It was surprising to see that other premises costs had not increased more than reported here, at 2.4% of fee income in 2023 compared to 2.3% in 2022. One of the major components of these costs are energy related and last year we predicted that these costs would increase significantly following the sharp increases in wholesale prices over the course of 2022. It is possible that cost control and energy efficiency measures introduced during the height of the Covid lockdown will have had an impact on controlling these rises to some degree, combined with reduced spending on repairs and maintenance, and it will be interesting to see how firms have fared in next year's report.

Figure 6.15: Accommodation costs as a percentage of fee income (%)

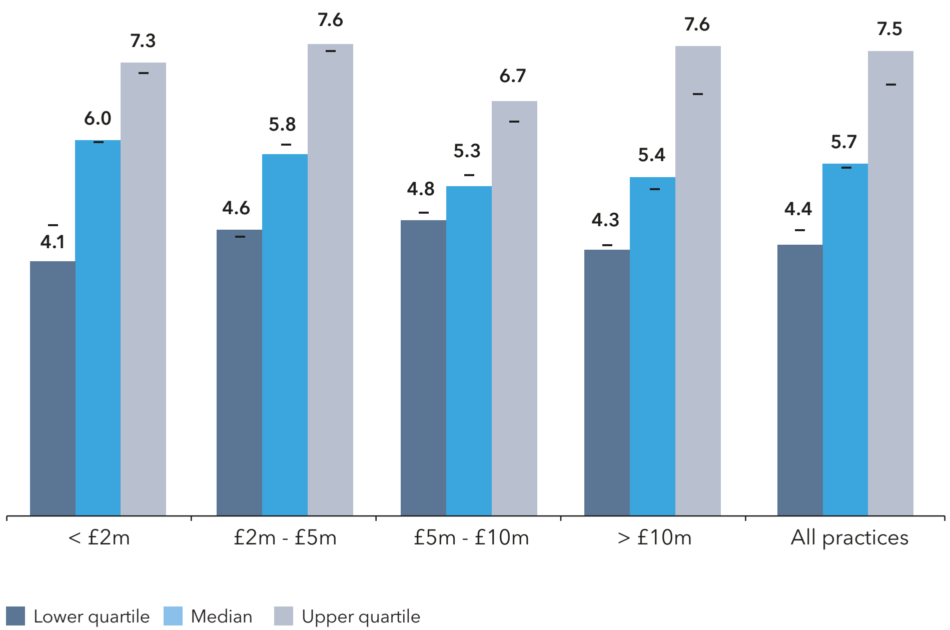


Figure 6.16: Premises rental payments as a percentage of fee income (%)

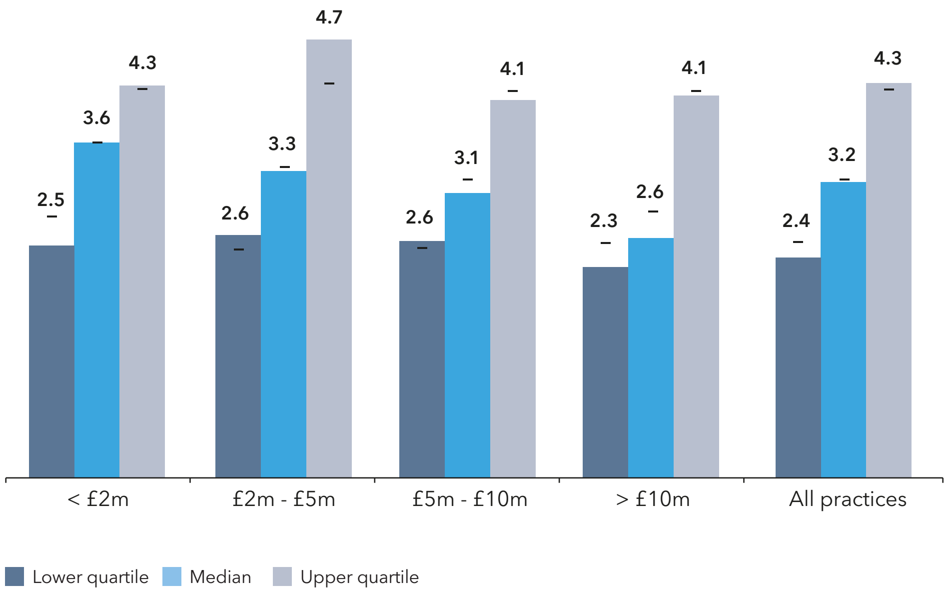
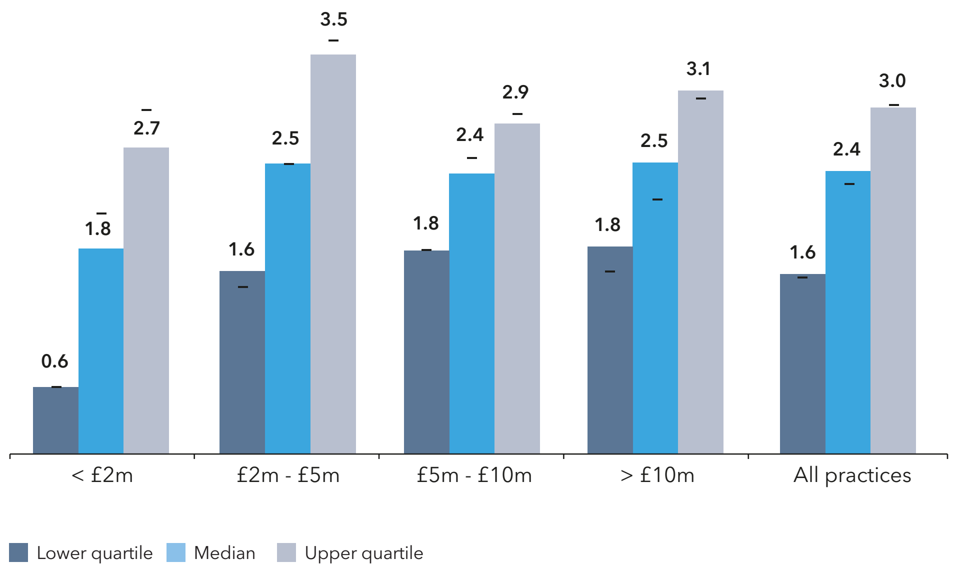


Figure 6.17: Other premises costs (rates, light and heat and maintenance) as a percentage of fee income (%)



7. Characteristics of profitable firms

In this section we examine the characteristics of the firms that achieved above-average levels of profitability in this year's survey and compare them against the same characteristics of the firms that achieved lower than average levels of profitability. We have focused on six key areas:

- Fee earner gearing;
- Fee income per equity partner;
- Fee income per fee earner;
- Total salary costs, including notional salaries for equity partners;
- Non-salary overheads;
- Total lock up days.

The figures shown in the following charts have been calculated by separating all participants into two groups: those with net profit per partner above the median shown in Figure 6.1, and those with net profit per partner below the median, in each turnover band. We then reanalysed these two groups, to calculate new median figures, so that we can more easily represent what a well performing firm looks like relative to a firm that is underperforming.

The six charts in this section show two bars for each turnover band. The bars on the left are the figures for the firms with above-average levels of profitability, and the bars on the right are for the firms with lower than average levels of profitability.

Figure 7.1: Fee earner gearing (median figure only)

Figure 7.2: Fee income per equity partner (£'000) (median figure only)

Figure 7.3: Fee income per fee earner (£'000) (median figure only)

Figure 7.4: Total salary costs, including notional salaries, as a percentage of fee income (median figure only)

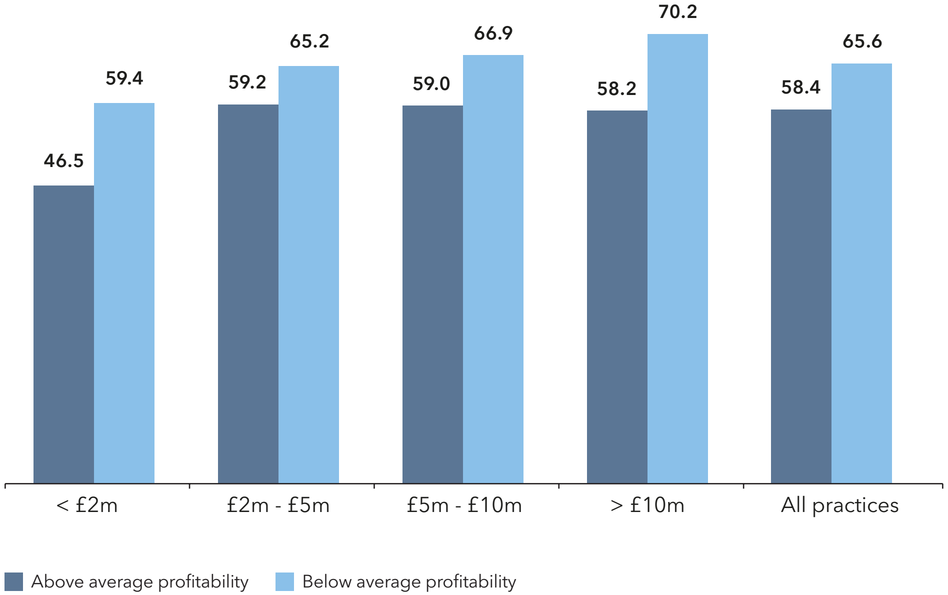


Figure 7.5: Non-salary overheads as a percentage of fee income (median figure only)

Figure 7.6: Total lock up days (median figure only)

8. Working Capital

It is always challenging to conclude on trends on working capital management in a survey of law firms, as lock up (work in progress and debtors combined) can vary dramatically across differing areas of law.

This year, the median number of combined lock up days has increased slightly, from 137 days in 2022 to 138 days in 2023.

Whilst WIP days fell slightly, this was offset by a small rise in debtor days.

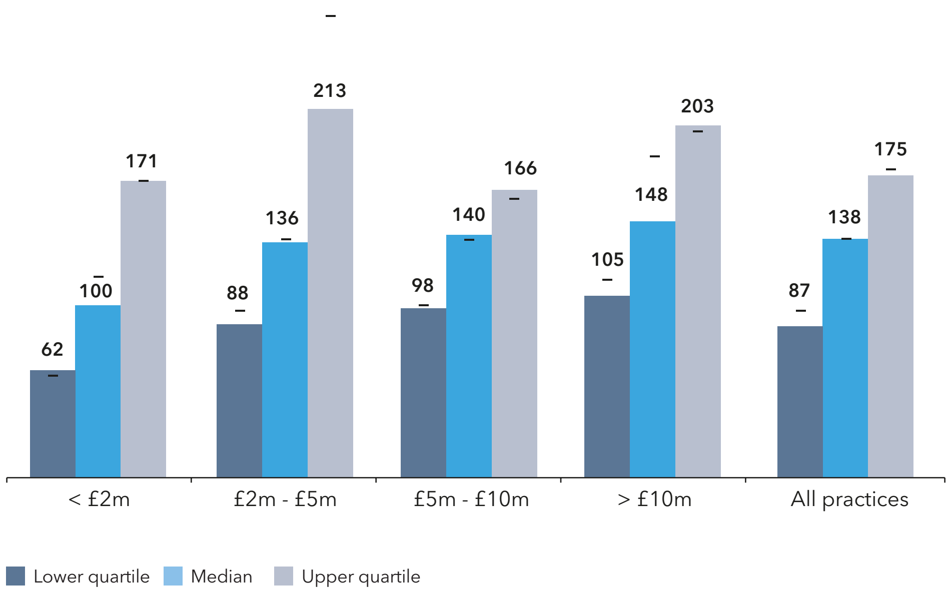
It is worth remembering that any improvements in overall lockup, however incremental, will have a positive impact on cash flow.

To put this in context, a firm with turnover of £10m would free up almost £30k of cash for every day's reduction in lock up.

Although it might seem challenging to implement a permanent improvement to lockup, imagine a scenario where most fee earners in a firm raise their bills around the end of the month or just before the financial systems are closed for month end. If those same fee earners were to raise their bills consistently throughout the month, they could, in theory, reduce their lockup by a couple of weeks and the £30k of freed up cash noted above might then become £300k of free cash. For many firms, that can make a huge difference to their overdraft or other borrowing requirements.

As a matter of good financial hygiene, firms need to ensure that they continue to focus on reducing lock up where at all possible, as high lock up can not only lead to adverse cash flow issues but often also leads to increased bad debt exposure too.

Figure 8.1: Total lock up (days)



WIP days

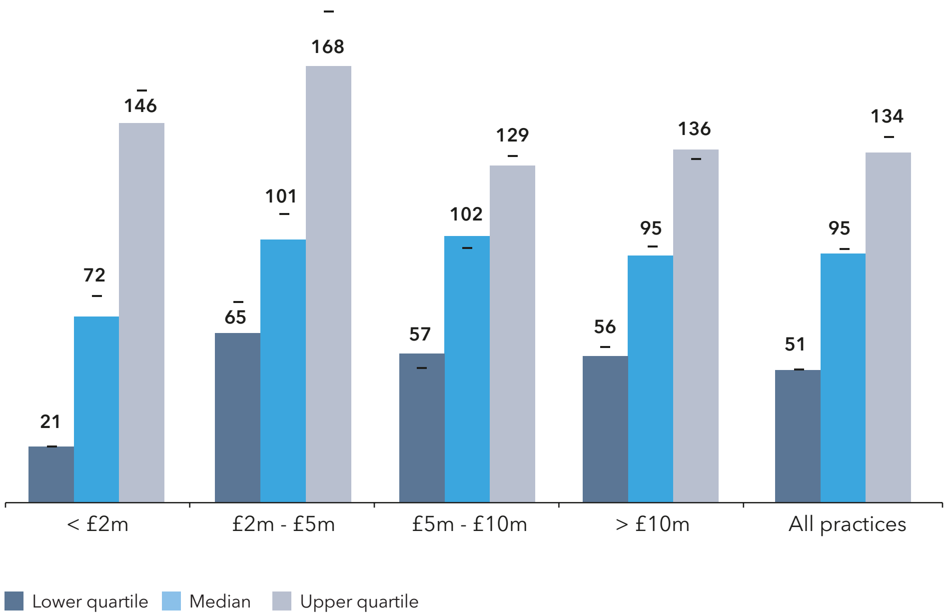
Work in progress (WIP) days have been calculated based on total WIP per participants' time records, as opposed to the figure included in their year end accounts, as, for many firms, the figure in these accounts does not include large amounts of contingent WIP.

We typically see firms that operate conditional fee agreements carrying a large amount of contingent WIP that is not reflected in their year-end accounts, and it is just as important for those firms to be able to monitor that WIP as it is for firms that raise interim bills as matters progress.

While firms tend to focus on credit control as the primary tool to manage lock up, good financial hygiene starts at an earlier stage than chasing debts, and the best performing firms have robust polices that ensure that all time is captured properly, in a timely manner, and that time is billed as soon as the work is complete (and the client is still happy), rather than waiting until the month or quarter end. As noted previously, small improvements to billing practices can have a very positive impact on cash flow.

WIP days fell from 97 days in 2022 to 95 days in 2023.

Figure 8.2: WIP days



Debtor days

Debtor days rose from 36 days in 2022 to 37 days in 2023 and so there are some important points to remember:

- Fee earner training on managing lock up can make a huge difference. In our experience, many fee earners do not fully understand the correlation between what they do within their day job and how it impacts on firms' finances.
- Small changes to standard practice, such as raising bills as soon as the work is complete, or raising more frequent interim bills where the work type allows, can make a big difference to how soon you get paid. Moving away from billing at month-end to billing across the month can also result in clients paying a full month earlier. A client who is happy with the outcome of a case may well pay more quickly if they receive the bill promptly. For those clients that are not as happy, prompt billing gives everybody the opportunity to resolve the matter while knowledge is still fresh.
- Many firms continue to carry large amounts of unbilled disbursements, and often do not ask for money on account of them, even in areas where it should be straightforward for them to do so (e.g. property work). Too many firms continue to extend unnecessary free credit to clients by funding disbursements from the office account rather than using the client's own money.
- It can often be helpful to remove fee earners from the credit control function entirely. Fee earners generally do not like having difficult conversations with clients, and appointing a dedicated credit controller can allow balances to be chased sooner and more effectively, as well as taking a lot of the emotion out of the process and will allow fee earners to focus on fee earning. However, any policy should allow some degree of flexibility, and in some cases, it is the fee earner who is better positioned to negotiate a favourable outcome.

Figure 8.3: Debtor days

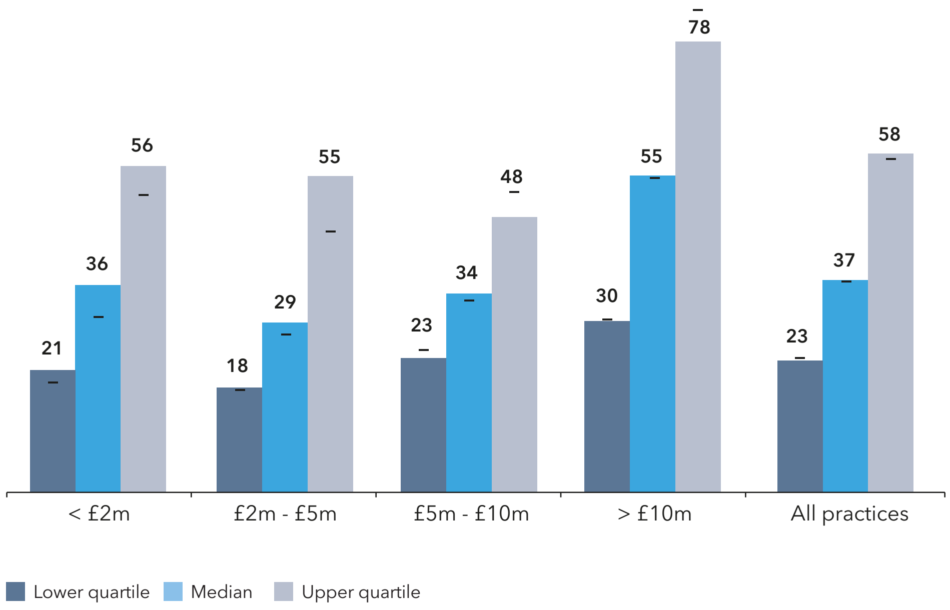
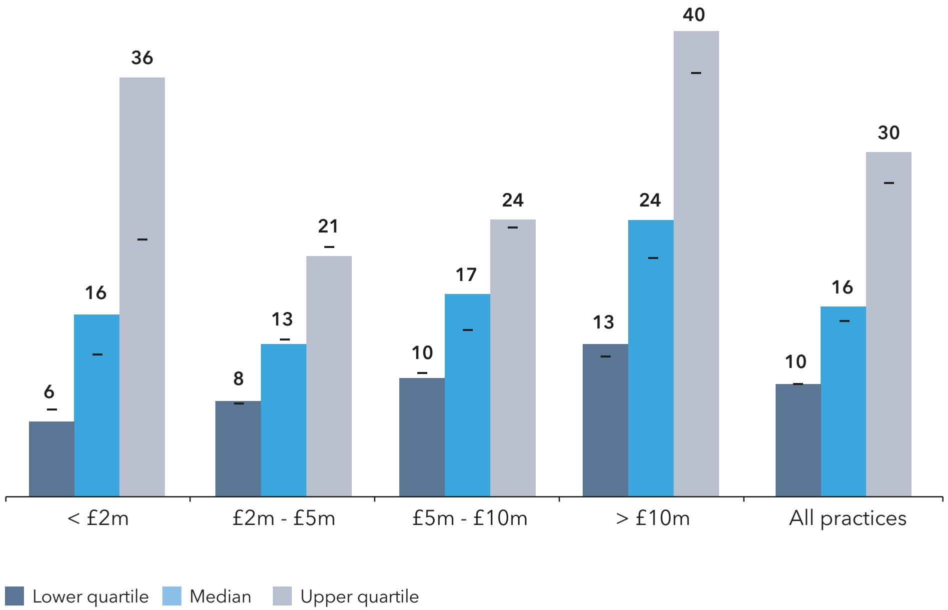


Figure 8.4: Debtors per fee earner (£'000)



Working capital – equity partner funding

Equity partner capital in a partnership or LLP is the total combination of capital account, current account, and tax reserves. In a limited company, capital comprises share capital, retained profits and directors' loan accounts.

The participants in this year's survey reported a small median increase of less than 0.5% in individual partner capital, with a median total of £313,020.

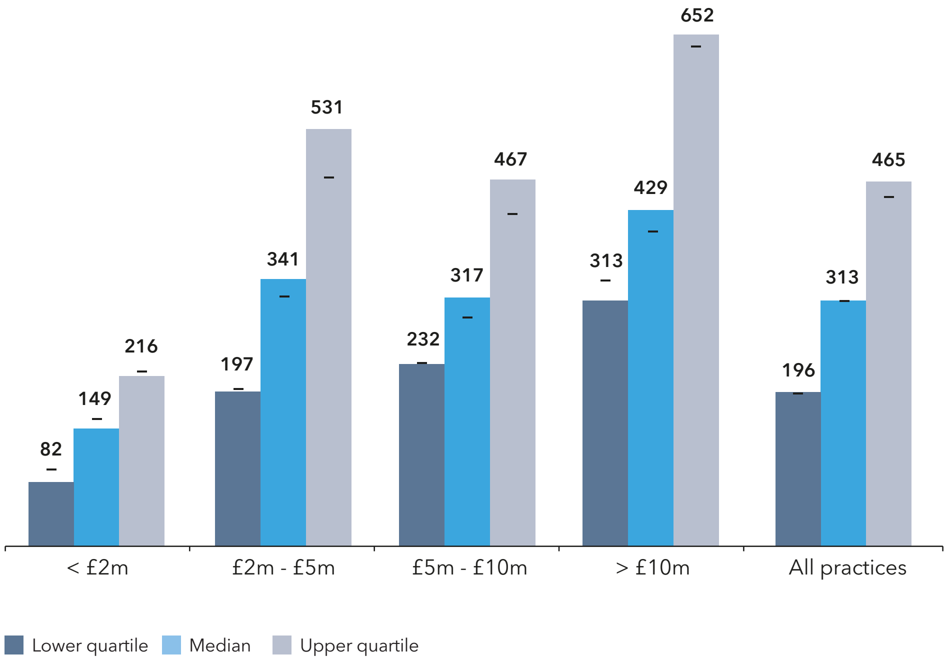
As noted earlier in this report, from the 2023/24 tax year, all self-employed individuals and partners are now being taxed on a tax year basis, rather than an accounting year basis, i.e., individuals will pay tax on profits arising in each tax year, regardless of the firm's accounting date. Limited companies are unaffected.

For most firms, the changes will not involve ultimately paying more tax – rather it is an acceleration of tax payments. Whilst many firms will opt to spread the accelerated tax over up to five years, firms will need to manage cashflow and managing lock up is key to this, as noted above. Firms will no longer be able to rely on partners' tax reserves to help fund their working capital in the same way that they always have.

We also recommend that firms consider introducing partner tax reserves into their accounts if they do not already have them, as this can help ensure that partners do not overdraw profits, leaving themselves short.

Finally, measuring and forecasting the ongoing working capital requirements of the firm is a key step in assessing the optimum level of partner funding.

Figure 8.5: Partners' account balances per equity partner (£'000)



Bank and other borrowings

84% of participants reported a positive office account balance at their most recent accounting date compared to 86% last year.

The median office account balance across all participants was £389,000, up slightly from £388,000 in 2022, with all turnover bands reporting a positive median balance.

27% of participants reported that they operated with no overdraft or bank debts at all. For those firms that had bank borrowings and/or a bank overdraft, the median amount per equity partner was £62,373 compared to £81,250 in 2022.

17% of firms told us that they used secondary funding to finance payments such as the firm's VAT, partners' tax bills and annual practicing certificate renewals.

Figure 8.6: Year-end office account bank balance (£'000)

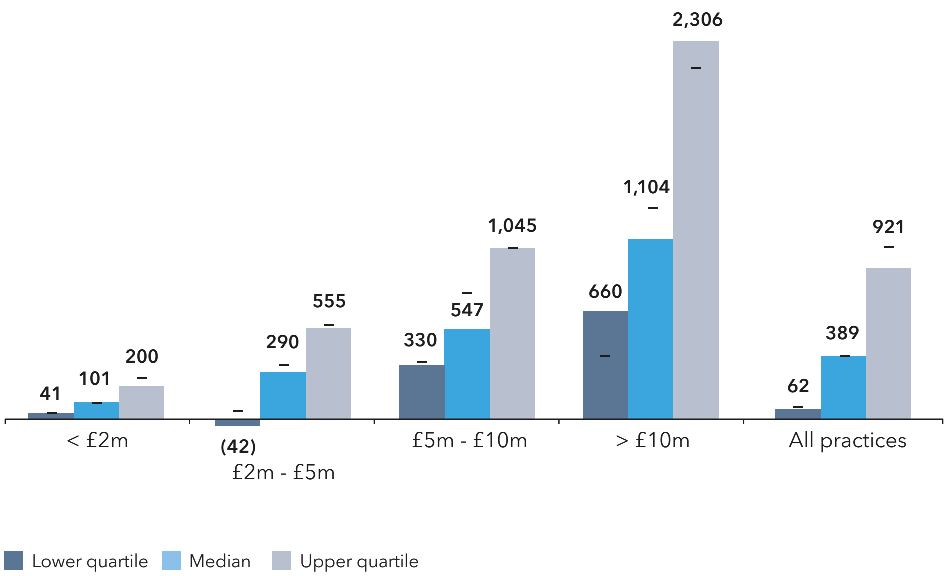


Figure 8.7: Bank borrowings per equity partner (£'000)

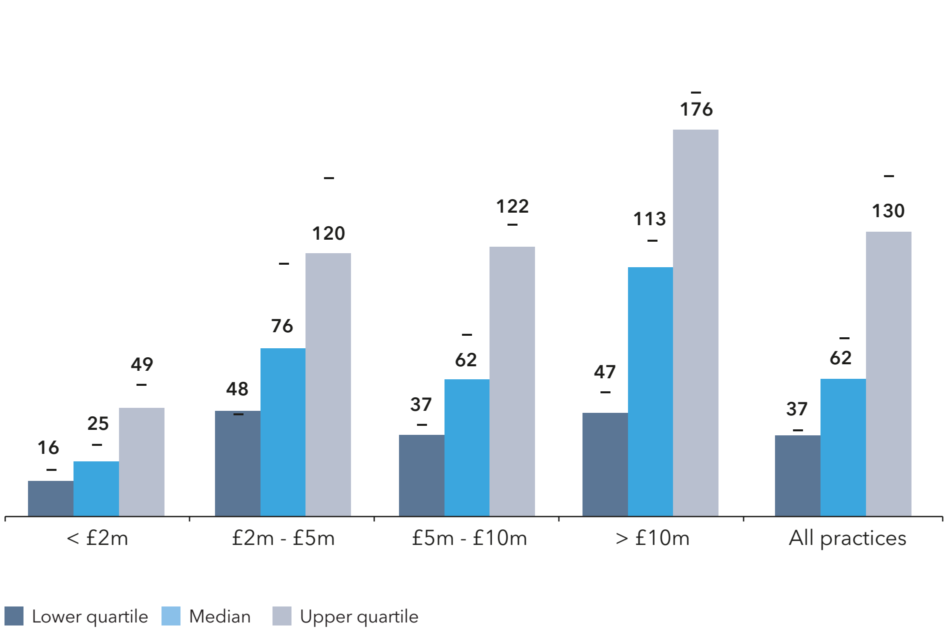
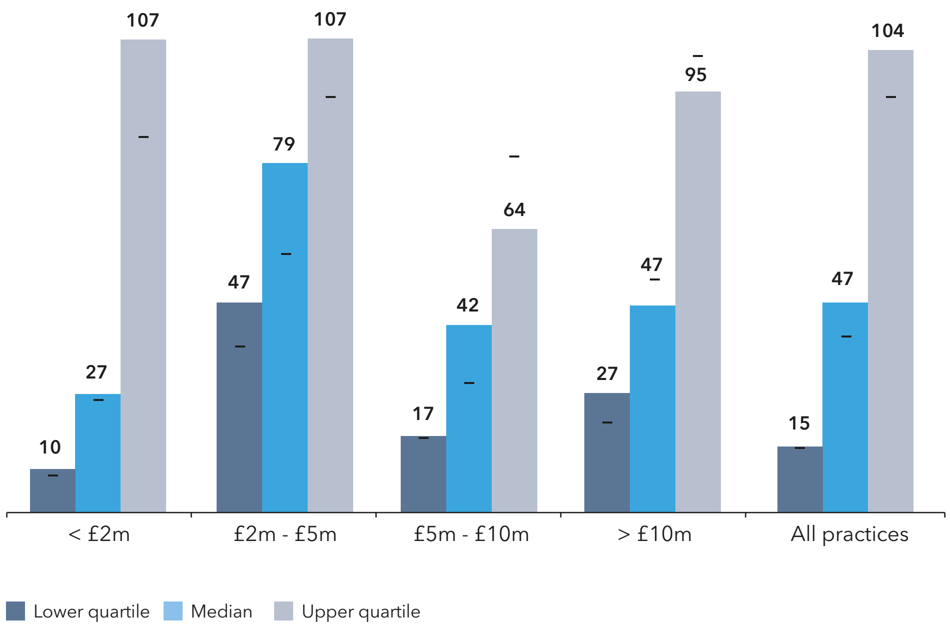


Figure 8.8: Other borrowings per equity partner (£'000)



Banks' attitude to lending

Banks have continued to lend to any business that represents a 'safe bet', and law firms are no exception.

There remains a reluctance to lend to firms specialising in areas where very high levels of WIP and disbursements often result in a corresponding high level of external working capital funding requirement over a protracted period.

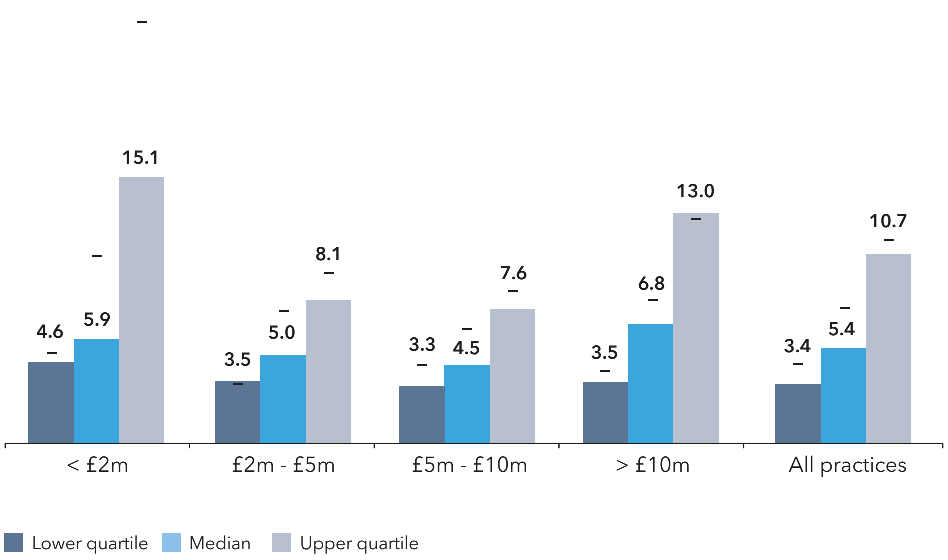
This is especially true where a large proportion of WIP is contingent, as the inherent uncertainty around recoverability, coupled with the difficulty in accurately valuing the WIP, can make it a less than safe bet.

Whilst most banks have lending options for incoming partners in a partnership or LLP, the options for people wishing to buy into a limited company are more limited, though we have seen some more products being offered over the last year or so.

Over recent years, some banks have been hit quite badly by law firms falling into administration, and so confidence in the sector generally remains below where it has been in the past. These issues have unfortunately continued, including the very high-profile collapse of the Axiom Ince Group and negative press that has surrounded the circumstances of the collapse, and so it seems likely that enthusiasm will remain muted, at least for the time being.

It is therefore important to remember that many banks pay close attention to the ratio of borrowings to fee income when assessing a firm's ability to make repayments, and so it is encouraging to see a reduction across the firms in the survey, with a median of 5.4% compared to 7.7% in 2022, much of which will no doubt be as firms have repaid borrowing through BBILS or CBILS.

Figure 8.9: Bank borrowings as a percentage of fee income (%)



9. Financial stability

In 2015, the SRA began risk-assessing law firms based on selected figures from their annual accounts. The three warning indicators identified by the SRA were:

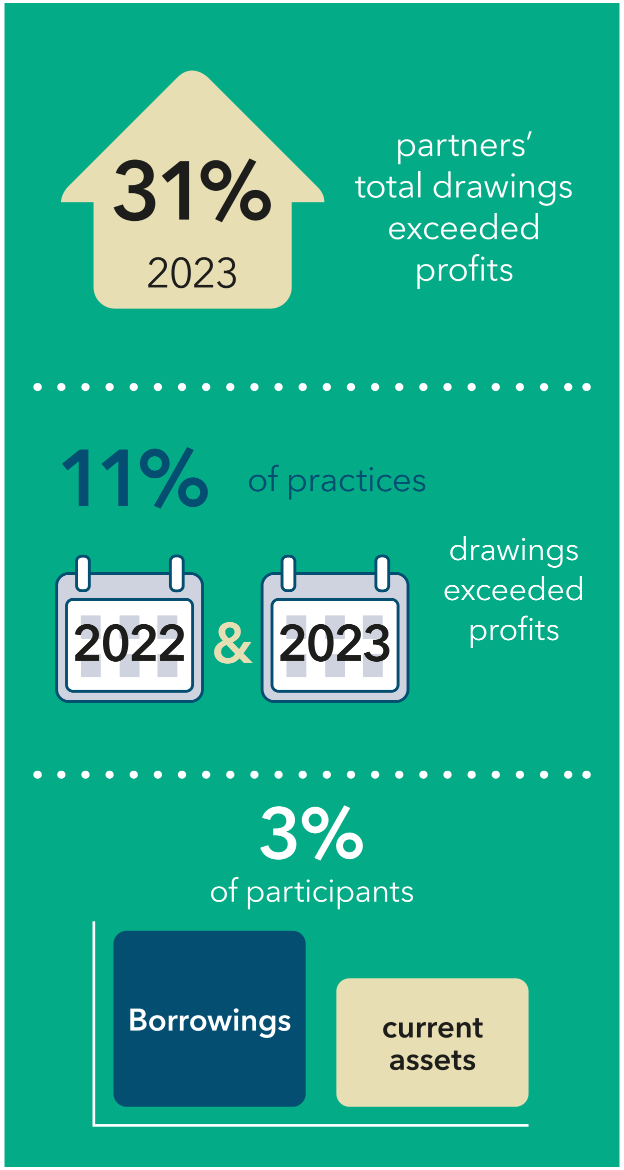
- Drawings in excess of profits.
- Borrowings in excess of net assets, i.e. net liabilities.
- Borrowings over a certain (undefined) level.

Based on these indicators, firms were assessed as red, amber, or green, resulting in differing levels of supervision from the SRA. For example, red rated firms received intensive supervision from the SRA, were required to provide the SRA with regular management information and contingency plans, and were told to obtain professional insolvency advice.

In recent years, the SRA have moved their attention to other matters, but the recent collapse of the Axiom Ince Group may well put this issue back in the spotlight. The SRA have faced questions over the last few months around their level of oversight, and so it feels likely that financial risk across the sector will make its way back to the top of the agenda.

Every year since 2015, we have analysed the information provided by participants to see how they fared against the SRA's original warning indicators. This year's findings are as follows:

- 31% of participants in this year's survey had taken drawings in excess of profits compared to 27% in 2022. 11% of firms reported that they had taken drawings in excess of profits in both 2023 and 2022. As we have noted in previous years, sometimes this is no more than a timing difference driven by when partners decide to withdraw profits and is more pronounced in firms that carry a large amount of contingent WIP.
- Borrowings exceeded current assets (WIP and debtors combined) for just 3% of participants.
- Finally, none of the firms in this year's survey had borrowings in excess of total partner capital, and partner capital increased in 53% of firms.



The short term future – fee predictions

Survey participants were asked for their projected fee income for the current 2024 financial year. Confidence was fairly high across firms in most turnover bands, with a median growth prediction for 2023/24 of 3.7%.

The upper quartile is predicting growth of 9.9%, whereas the lower quartile is predicting a 3.3% reduction in fees.

The smaller firms with turnover below £2m are less optimistic, forecasting a median reduction of 2.8%, with the upper quartile projecting an increase of less than 1%.

Although not linked to fee generation, it is worth remembering that, while interest rates remain at their higher than normal rates, firms should review their banking arrangements to ensure they are maximising their return on client money, while also looking again at their interest policies, as a de minimis limit of £50 is commonplace nowadays.

Figure 10.1: Predicted fee growth for the 2023/24 financial year (%)