Preparing for ABS

Ian Muirhead on the importance of business management processes and procedures

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The precedent for the outcomes-focused approach to regulation on which the Solicitors' Regulation Authority (SRA) has embarked is provided by the Financial Services Authority (FSA), and it is no coincidence that the SRA's new Director of Regulation, Samantha Barrass, was recruited from the FSA. The multi-disciplinary world heralded by the *Legal Services Act* demands conformity in regulation and the FSA is seen, with good reason, to be the template regulator for the modern age.

The FSA went through a learning curve in its approach to regulation. When it came into being in December 2001 it introduced a ten-volume, 40,000 page handbook, but within a few years it became clear that this was too unwieldly an instrument for a fast-changing world and one with which few regulated firms could reasonably be expected to come to terms. Hence the move to what was first called principles-based regulation, and now, with the emphasis on consumer outcomes, is referred to by the FSA as outcomes-based regulation.

This seeks to place the rules in the context of the working environment in which they are applied, and provides guidance as to how firms should create the environment which is appropriate to their own type of business. Inevitably this leads to subjectivity in the way in which compliance with the rules is assessed, at the expense of certainty, but to the surprise of many regulated firms, the system has worked.

Business management

Central to the FSA's approach is what it refers to somewhat misleadingly as treating customers fairly (usually abbreviated to 'TCF'), but in fact relates to business management processes and procedures. The underlying principle is that any inefficiency is likely to be inimical to the interests of the client, and therefore non-TCF; and bearing in mind the lack of management in many law firms, it is pleasing to see similar principles being adopted by the SRA. A Law Management Section report of 2009 concluded with the words 'Perhaps the main requirement for all of these (structural) options will be good and well developed management and skills only found in a minority of firms at present'; and more recently Jeremy Hand of private equity house Lyceum Capital Partners commented in *The Lawyer* of 9 August 2010: 'You need management, clear strategy, capital and sound execution. I'm not sure how many traditional (law) firms offer this combination'

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The SRA Consultation Paper of 28 May 2010, 'The architecture of change – the SRA's new handbook', reads across to the principles of TCF almost line for line:

- The business plan
- Managerial responsibility
- Consistency of processes
- Internal monitoring of standards
- Management information analysis
- Analysis of complaints
- Client satisfaction surveys
- Regulatory visits to discuss client relations.

Moving on

Initially, financial advisors confronted by TCF regarded it is yet another unwelcome regulatory burden. But as a result of the thorough way in which the FSA has implemented the initiative – on-line guidance, regional seminars, actual or virtual visits to individual firms, and enforcement action where necessary – firms have come to appreciate the way in which TCF has assisted them to emerge from the cottage industry mode in which so many operated. In the words of the FSA: 'TCF should become an integral part of firms' business culture – a continuous process, not something that firms can implement and forget'.

Many law firms still operate as cottage industries, and one of the major flaws in their business is the failure to collect client data beyond that which is required in relation to the current transaction, and the consequent failure to maintain firm-wide client databases. This reinforces clients' impression that solicitors have no interest in developing and maintaining a wider relationship with them, and it does nothing to address the comment by the Managing Partner of Trethowans that 'Law in many instances is seen as a distress purchase. Generally, clients try to avoid spending any money on legal services unless they have to' As the Society of Trust and Estate Practitioners repeatedly points out, the pivotal role in the post-*Legal Services Act* world will be that of the trusted advisor, of whatever profession, who coordinates the various professional inputs required for the conduct of clients' affairs. Arguably, this is the role that solicitors held before the legal monopolies blunted their commercial instincts, and it is a role to which they should again be aspiring.

Client database

Solicitors are sometimes accused of being people with a problem for every solution, and they have a tendency to be pre-occupied with the downside potential of developments, rather than seeking to leverage the upside. Consequently, the

objective of delivering high standards of client service is viewed not from the point of view of providing advantage to the client, but that of minimising risk for the solicitor, by avoiding taking on undesirable clients and ensuring that rigorous money laundering systems are in place. This overlooks one of the main flaws in solicitors' business model, namely the lack of firm-wide databases which will permit on-going client contact and the retention of client loyalty. As was pointed out in *Managing for Success* in February 2010: 'Many law firms do not undertake (Know Your Client procedures) in as great a level of detail as, for example, financial services companies.. and should consider how doing so could provide benefits to them in the long term.'

The SRA's requirement that all Alternative Business Structures (ABS) should appoint a Head of Legal Practice (HOLP) and a Head of Finance and Administration (HOFA), and the recommendation in the SRA's May Consultation Paper that all law firms should appoint compliance officers with corresponding responsibilities, reflects the FSA requirement that firms appoint holders of 'controlled functions' and is a welcome recognition of the need for managers within law firms to wield authority that complements their regulatory responsibility. This should assist firms to address the long-standing problem of what has been referred to as the 'confederation of sole practitioners syndrome' and has been highlighted by the Law Society's Lexcel practice management unit: 'One of the challenges that practices can experience is the protectiveness that partners or client-facing staff can feel towards their clients. This reluctance may stem from the understandable concern of not knowing the quality of client service or processes used by a colleague'

Developing a firm-wide client database enables firms to target their services more effectively by segmenting the client base and refocusing on the clients whose profile matches their own specialisations, and who are seen to be profitable. In the new era of ABS it is unlikely that many law firms would be advised to take onto their books consumers whose main pre-occupation is

with price rather than quality, and who may therefore be better served by Tesco or the Co-op. The Legal Services Policy Institute of the College of Law has suggested that the greatest danger posed to solicitors by the new competitors for the provision of legal services will lie in their superior capability in relation to branding, supply chain management, phone and online services, longer opening hours, less jargon and better complaints handling – all of which relate principally to the lower end of the market.

Consistency of processes and output will be another important requirement. Procedures need to be seen to have been laid down and adhered to, with a clear audit trail, if the risk of individual members of the firm going off on a frolic of their own is to be contained. The firm must be seen to operate as a team, with clear direction and coordination; an objective that should also counter the threat of members of the team leaving and taking 'their' clients with them.

Also important is that firms' managers should not only establish business plans, but should also monitor performance through agreed Key Performance Indicators and canvass input from both clients and staff. Many firms already conduct client surveys, but few firms organise regular staff briefing meetings, the minutes of which are agenda items for management meetings, whose own decisions are in turn fed back to the staff. Equally, few firms investigate client comments and complaints sufficiently rigorously, preferring to tick the boxes required to get the clients off their backs. The questions that should be asked are: is this comment/ complaint a reflection on the firm or the individual staff member? If the former, do the firm's processes need to be reviewed? If the latter, is this a matter of training or discipline? If training, should the individual's personal development plan be reviewed? What training has taken place already? Was it monitored? Should it be repeated? And does the comment or complaint reflect on the firm's objectives or market positioning?

Significantly, the Consumer Panel of the Legal Services Board, in its August 2010 response to the SRA Consultation Paper on outcome-focused regulation commented: 'The SRA should consider an approach, akin to Treating Customers Fairly in financial services, where a small number of key consumer outcomes, firmly rooted in the client experience, lie at the heart of the regulatory framework.'

For firms seeking to take advantage of the opportunity presented by the Act to reduce their dependence on transactional business and to provide a more comprehensive service, which will assist them to build enduring client relationships, the synergy between complementary professional disciplines is clearly the principal concern. However, the experience of those other professionals in adapting to the demands of outcomes-focused regulation can be a valuable added bonus; and fee-based independent financial advisors tick both these boxes.