Adapting to a new world

PwC Law Firms' Survey 2019

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This is the 28th PwC Law Firms' Survey.
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Our Law Firms' Advisory Group harnesses the expertise of specialists nationally and internationally to provide assistance with:

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

We would like to thank all other members of the LFAG who helped with this year's survey, particularly Colleen Dunn, Jen Smith, Sanah Faridi, Heather Stacey, Josh Noble, David Moloney, Alyson Reeves, Tom Oliver, Ben Lamb, Alex Quant, Dan Wicks, Dan Holmes, Paul Brady, Richard Jones, Tanzina Brooks and Malcolm Wren 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 2019 exchange rates for comparability).

UK top tier – UK headquartered firms where global revenues exceed £1bn (prior year restated to 2019 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.

Table of contents

Introduction and key themes 02

1 Global financial performance 16

2 UK financial performance 18

3 Business support 20

4 People 22

5 Financing 24

6 Cyber risk 26

Introduction and key themes

Introduction

The theme for our 2019 Law Firms' Survey is 'Adapting to a new world'. The digital revolution means that the world of professional services is changing, and fast. Firms need to invest in technology, and transform their workforces to drive productivity and innovation. At the same time, levels of economic and political uncertainty are high and firms need to remain agile to find and exploit opportunities for growth.

Set against this context, the UK legal sector has continued to show great resilience in challenging times. In a year that has included continued uncertainty over Brexit, signs of weakness in Eurozone and global economies, China-US trade tensions, and heightened geopolitical risk in the Middle East, it is impressive that a large majority of firms were able to report both revenue and profit growth (albeit at slower rates than we saw in 2018). Firms that have invested in their international offices over the past few years are now reaping the rewards, with revenue and profit growth of overseas offices outstripping that of the UK. Given the macro-economic environment in the UK, and as firms continue to protect themselves against the possible impact of Brexit, we expect to see even greater investment into international markets by the larger firms.

Profit per full equity partner ("PEP") remains a focal point for the financial health of firms and is still a key metric in driving retention and recruitment. UK PEP continues on its upward trajectory across all bandings, although outside the Top 10 a significant contributor to this growth has again been equity management. Meanwhile, many firms continue to suffer the squeeze on profit margins that we have seen over the past few years.

The workforce is changing faster than ever before, as are employees' expectations of how, when and where they want to work. High staff turnover suggests that law firms need to improve in this area to meet expectations and ensure they can recruit and retain the best talent. Now more than ever we are seeing a demand for firms to digitally upskill their workforce and foster a culture that fuels innovation and transformation, whether through hiring, training, investment in start-ups/labs, or alternative workplaces. The successful firms of the future will be those that engage with their employees, are flexible and creative, and embrace diversity and inclusion as part of workplace culture.

Technological advancement continues to generate opportunities and challenges for the legal sector. To remain relevant, firms of all sizes need to engage with the step change we are witnessing, whether through cloud adoption, automation of delivery models, or revolutionary product innovation. Our 2019 survey results indicate that law firms continue to take small steps, but with few developing or implementing market-changing technology programs. Only a handful have a clear and flexible strategy for realising the benefits of innovation, backed up with clear objectives and measurable metrics to monitor success.

Cyber risk is an area of serious concern for law firms: data security and privacy are hot topics in the media and corporate reputations are quickly tarnished. It is therefore disconcerting to see relatively low levels of senior management involvement in crisis management exercises, and few firms where cyber risk is managed at Executive Board level.

Technological change and innovation require both upfront and ongoing financial investment. This is never straightforward in a full distribution model when the likely payback period of investment extends a number of years into the future. Our survey results show an overall increase in funding from partner capital and current accounts, a slow down in distributions and firms grappling with deteriorating in-year lock up. In the current environment of fast-paced change, financing is a crucial issue for law firms and for some, a change in culture and behaviours towards working capital management is needed to secure financial stability. Meanwhile, IPOs and private equity funding remain options for those firms prepared to dilute equity in return for funding.

So: finding the right markets for investment; ensuring growth is sustainable and profitable to protect margin; building a culture that is relevant and attractive to today's workforce; and making the right choices for technology investment to capitalise on opportunities whilst managing the increasing risks of a technologically enabled world......these are the challenges which law firms need to address.

Global financial performance

Global financial performance has been relatively strong in 2019, with 80% of Top 10 and 86% of Top 11-25 firms delivering fee income growth in excess of 5%. This was accompanied by profit growth in most firms: 80% of Top 10 firms grew net profit (by between 4% and 11%), whilst three quarters of Top 11-25 firms grew profit (by between 1% and 18%). These are positive results, particularly given the challenging nature of both the UK and global markets.

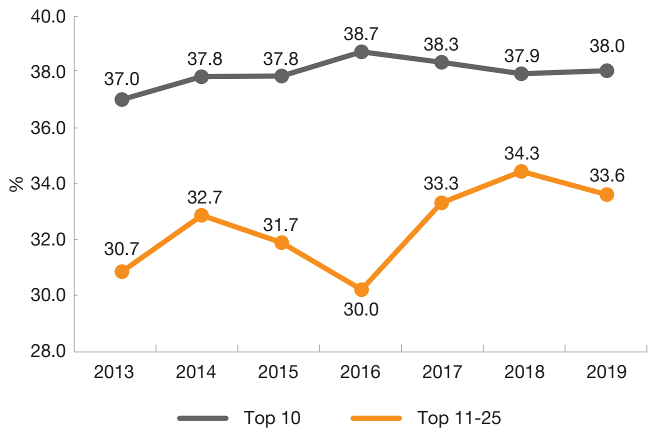
Average fee income increased in the Top 10 by 6.1% to £1,037m, and in the Top 11-25 by 8.1% to £270m. Profit growth averaged 6.5% to £406m for Top 10 firms, and 5.8% to £92m for Top 11-25 firms.

Global firms are responding to the ever increasing pressure on UK fee income and profits by focussing their growth efforts on the international market - a strategy which is paying dividends. Top 10 firms sourced 74% of fee income and 85% of profit growth from international offices, amounting to an average of £44m and £21m in real terms. Of the fee income growth, approximately half arises in Western Europe (£23m of fee income growth and £11m of profit).

From a profitability perspective, Top 10 firms have maintained their global net margin before full and fixed share equity partner remuneration at 38.0% (2018: 37.9%), although the UK element of this fell by 1.3 percentage points to 40.3% whilst the international element increased by 1.5 percentage points to 36.7%. For Top 11-25 firms, the margin fell by 0.7 percentage points to 33.6% reflecting both the difficult UK trading conditions and a growing cost base as these firms continue to invest in the international market.

There is a clear difference in global partnership structures between Top 10 and 11-25 firms, with the latter utilising the fixed share partner grade significantly across global offices. This has a notable impact on results: the 4.4 percentage point gap in margin before full and fixed share partner remuneration grows to 12.5 percentage points after fixed share remuneration is taken into account (Top 10: 35.8%, Top 11-25: 23.3%).

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



Global – Average percentage profit and loss account

	Top 10		Top 11-25	
	2019	2018	2019	2018
	%	%	%	%
Fee income	**100**	**100**	**100**	**100**
Staff costs – fee earners	26.2	26.5	28.6	28.2
Staff costs – non-fee earners	13.2	13.8	14.4	13.8
Property costs	8.2	8.6	8.3	8.5
IT revenue costs	2.3	2.4	2.5	2.6
Marketing & BD costs	1.4	1.4	2.0	2.1
Finance function costs	1.1	0.9	0.7	0.8
Depreciation	1.5	1.9	1.9	1.8
Insurance costs	0.7	1.0	1.3	1.1
Bad debts and disbursements	1.0	1.1	1.5	1.6
Foreign exchange differences	0.3	0.5	-0.1	0.3
All other costs	6.1	4.0	5.3	4.9
Profit before fixed share equity remuneration	**38.0**	**37.9**	**33.6**	**34.3**
Fixed share equity partners' remuneration	2.2	3.2	10.3	10.0
Net profit margin	**35.8**	**34.7**	**23.3**	**24.3**

A wide performance gap between UK and US top tier firms continues across all KPIs (note: we define a top tier firm as one with global revenue greater than £1bn). The net profit margin differential illustrates this point clearly, with UK law firm performance at 36.4%, well behind the US equivalent of 45.7% - that equates to an average of £152m of profit or £317k of PEP.

This performance gap is driven by a small number of key factors that UK firms may say are out of their control: for example, high levels of utilisation in US firms for which there is arguably no appetite in the UK; and billing rates achieved, which US firms appear to be able to increase year after year. The latter is perhaps an area where UK firms could seek to reduce the gap, although in a saturated market threatened by new entrants that might come at the expense of market share.

UK financial performance

Considered in isolation, UK fee income performance appears strong, with 89% of Top 100 firms reporting growth (compared to 84% in 2018). However, the rate of growth has slowed to a firm average of 5.9%, compared with 8.3% in 2018. Last year, 50% of Top 10 firms grew fee income in excess of 10%, whilst none exceeded single digit growth this year; and although 23% of Top 11-100 firms recorded double-digit fee income growth in 2019, that fell from 38% in 2018. On top of this, 13% of firms in the Top 50 saw a decline in fee income.

Top 10 firms will be disappointed that margin erosion has continued for the fifth consecutive year, to a low of 35.5% in 2019. This is a 4.5 percentage points fall from the 2014 high of 40%. In recent years we have noted the impact of rising staff costs and the pressure on newly qualified salaries has been well publicised. However, the Top 10 staff cost ratio has actually fallen by 1.5 percentage points in the current year, due to savings in the non-fee earner staff cost ratio.

The staff cost ratio benefit, along with other cost ratio savings, has been more than offset by the significant increase in “other costs” ratio from 2.4% to 6.1%. Some of that movement likely stems from investment costs - whether to support system implementations, or more experimental innovation; the drag on margin may be an unavoidable consequence of investing to build a sustainable business.

Margins have also fallen slightly for Top 11-25 firms (from 28.8% to 28.5%) and Top 51-100 firms (from 24.6% to 22.9%). Only Top 26-50 firms reported a net profit margin improvement, albeit that was minimal from 24.2% to 24.7%.

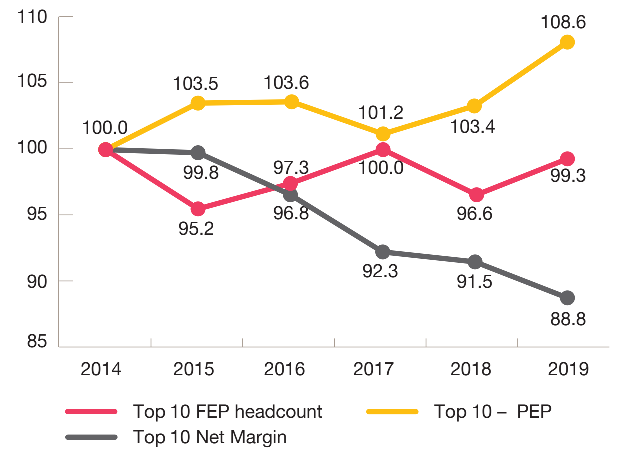
Comparing fee income and profit movements is interesting. Whilst 13% of Top 50 firms recorded falls in fee income, 39% reported profit reductions. In the Top 51-100, all firms increased fee income, but 29% experienced profit falls. It is clear that there continues to be significant pressure on profits in the UK legal sector.

UK - Average percentage profit and loss account

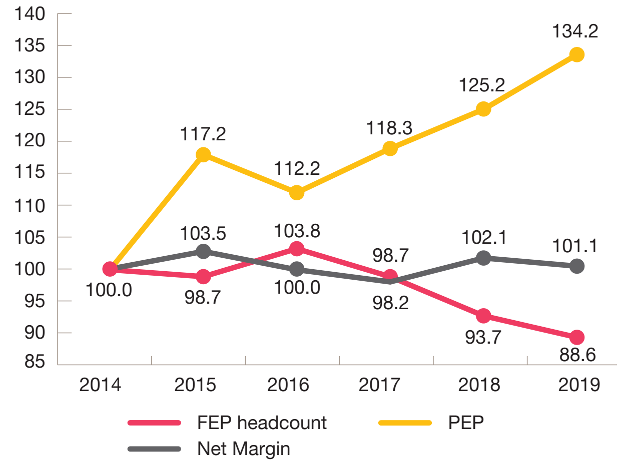
	Top 10		Top 11-25		Top 26-50		Top 51-100	
	2019	2018	2019	2018	2019	2018	2019	2018
	%	%	%	%	%	%	%	%
Fee income	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**
Staff costs – fee earners	26.7	26.7	26.6	28.3	29.0	27.8	30.6	30.4
Staff costs – non-fee earners	11.2	12.7	14.5	13.5	14.2	14.5	14.7	14.3
Property costs	8.7	8.7	8.4	7.7	8.6	9.1	7.7	8.0
IT revenue costs	2.2	3.1	2.9	2.8	3.1	3.0	3.1	3.0
Marketing & BD costs	1.5	1.2	2.1	1.9	2.0	2.0	2.1	2.2
Finance function costs	1.2	0.9	0.6	0.6	0.5	0.6	1.0	0.7
Depreciation	1.6	1.9	2.0	1.9	2.2	2.5	1.8	1.8
Insurance costs	0.9	1.2	1.3	1.2	1.7	1.8	1.7	2.3
Bad debts and disbursements	0.6	1.0	1.5	1.1	1.1	1.1	1.0	1.2
Foreign exchange differences	0.4	0.5	0.1	0.0	0.0	0.0	0.3	0.0
All other costs	6.1	2.4	3.8	6.0	4.1	3.8	5.0	4.7
Profit before fixed share equity remuneration	**38.9**	**39.7**	**36.2**	**35.0**	**33.5**	**33.8**	**31.0**	**31.4**
Fixed share equity partners’ remuneration	3.4	3.1	7.7	6.2	8.8	9.6	8.1	6.8
Net profit margin	**35.5**	**36.6**	**28.5**	**28.8**	**24.7**	**24.2**	**22.9**	**24.6**
Staff cost ratio (all staff costs)	*37.9*	*39.4*	*41.1*	*41.8*	*43.2*	*42.3*	*45.3*	*44.7*
Staff cost ratio (all staff, inc. FSEP costs)	*41.3*	*42.5*	*48.8*	*48.0*	*52.0*	*51.9*	*53.4*	*51.5*

PEP has continued to grow across all bandings to record levels. For example, Top 10 firms increased PEP by 5.1% to £1,120k and this was also on the back of an increase in full equity partner headcount of 3%. Further, Top 10 firms have managed to increase PEP over the last 5 years, despite minimal movement in headcount: PEP is up 8.6% from 2014 to 2019, whilst full equity partner headcount has fallen by just 0.7%. The management of partner headcount, though, has had an impact on Top 11-25 firms where PEP is up by 34.2% since 2014 and partner headcount is down 11.4%.

Trend in UK net profit margins vs PEP vs full equity partner headcount – Top 10 (2014 base: 100)



Trend in UK net profit margins vs PEP vs full equity partner headcount – Top 11-25 (2014 base: 100)



Trend in UK profits vs full equity partner headcount vs PEP (2018 to 2019)

	Average UK profits before full equity partner remuneration	Average UK full equity partner headcount	Average UK Profit per full equity partner		
	2018 to 2019 movement %	2018 to 2019 movement %	2019 £'000	2018 £'000	2018 to 2019 movement %
Top 10	0.3	2.8	1,120	1,066	5.1
Top 11-25	3.0	-5.4	734	729	0.7
Top 26-50	3.0	0.0	516	467	10.5
Top 51-100	4.2	-7.4	460	381	20.7

Business Support

With slowing growth in fee income and continued pressure on profit margins, it is no surprise that "improving the use of technology" and "standardising and centralising processes" remain the top two overall priorities for Business Support functions.

The main priorities for Finance functions continue to be "pricing and profitability" and "working capital". The backdrop of this is the continuing high level of fee income write offs.

More firms are employing specialists across business support functions: for example, in pricing (a further 16% of Top 100 firms are employing specialists in this area, up to 63% in total), legal project management (+19% to 51%) and strategy and innovation (+20% to 70%).

There is a significant volume of activity around "foundation" IT projects. More than half of Top 100 firms (56% compared with 42% last year) have either recently delivered or are underway with projects to implement key "foundation" technologies, demonstrating how critical IT has become to the sector.

Adoption of digital and emerging technologies advanced again this year, with a greater proportion of Top 100 firms having established some form of mobile apps, automated document production, data visualisation, AI, and smart contracts.

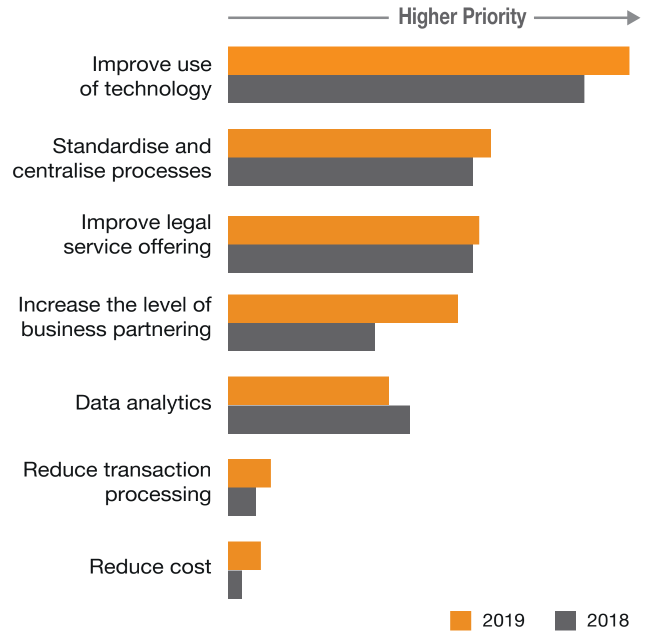
However, other emerging technologies remain less mature, with approximately 40% to 50% of firms still only at research stage with robotic process automation (RPA), big data and predictive analytics and blockchain.

Of the Top 100 firms 43% identified AI as the technology that is most likely to disrupt the legal sector over the next 5 years. This compares to 10% citing blockchain and smart contracts as the next most likely technology to disrupt the sector.

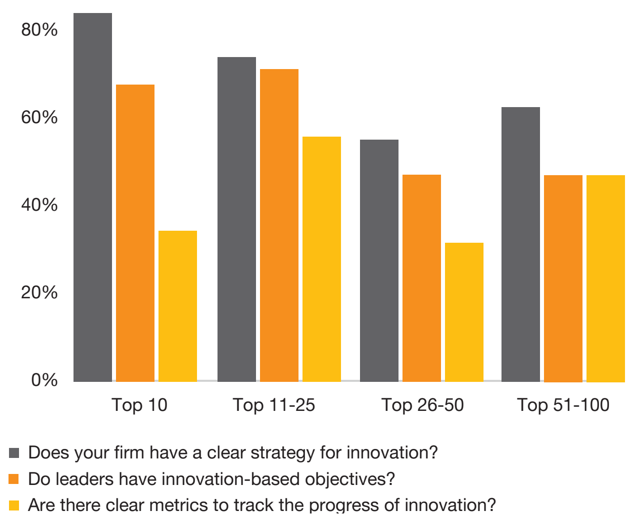
There has been a lack of IT investment in previous years and current year spend as a percentage of fee income is lower than seen in other sectors. There is, perhaps, "technical debt" building up in a number of law firms, whereby under investment in technology is resulting in a lack of capability that means proportionately larger future investment will be needed. Firms do need to consider if their overall IT investment is adequate to support the future needs of the business, including investment in innovation.

Although "innovation" is currently a buzzword in the sector, only 65% of Top 100 firms feel they have "a clear and flexible strategy for realising the benefits of innovation". Further, only 55% of firms have "innovation based objectives" for leadership and only 42% have clear metrics in place to track progress. Innovation is necessary to respond to disruption; and to deliver real results, a firm's innovation strategy must be considerably more than ideation. The more advanced firms recognise where their strategies are incomplete or limited, and are working to address that.

Top priorities for business support over the next twelve months (Top 100 firms)



Processes on innovation – % of firms that responded "yes" to key questions



People

Achieving an optimal resourcing model is an ongoing challenge for law firms and falling utilisation and increasing spare capacity has been an issue for a number of years. We are, therefore, surprised that a large number of firms have increased headcount in the current year, with most of this across the junior fee earner grades. Finding the optimal headcount to ensure utilisation is maximised, whilst not putting a brake on growth, is an eternal challenge. The ability to transfer skills from one practice area to another, or to combine permanent with contract staff, are routes to increase agile resourcing. Some in the professional services sector are now using resourcing technology to match people to projects, ensuing an even and unbiased distribution of workload and to optimise utilisation; this is likely to increase, particularly as we move further towards a gig economy with increasing use of contractors and a contingent workforce.

Headcount

	Top 10			Top 11-25			Top 26-50			Top 51-100		
	Av. 2019	Av. 2018	% change 2018-19	Av. 2019	Av. 2018	% change 2018-19	Av. 2019	Av. 2018	% change 2018-19	Av. 2019	Av. 2018	% change 2018-19
			%			%			%			%
Full equity partners	146	142	3%	70	74	-5%	59	59	0%	25	27	-7%
Fixed share equity partners	51	58	-12%	69	59	17%	53	66	-20%	26	15	73%
Non-equity partners	15	1	1,400%	10	16	-38%	1	1	0%	15	12	25%
Total Partners	**212**	**201**	**5%**	**149**	**149**	**0%**	**113**	**126**	**-10%**	**66**	**54**	**22%**
> 5 year pqe	265	249	6%	185	191	-3%	136	136	0%	75	53	42%
3-5 year pqe	122	128	-5%	57	82	-30%	48	50	-4%	34	26	31%
1-2 year pqe	149	132	13%	61	50	22%	40	43	-7%	27	18	50%
Newly qualified	86	48	79%	32	29	10%	25	24	4%	19	10	90%
Legal executives and paralegals	199	166	20%	110	90	22%	112	117	-4%	75	49	53%
Trainees	132	140	-6%	59	53	11%	39	40	-3%	34	19	79%
Total fee earners (including partners)	**1,165**	**1,064**	**9%**	**653**	**644**	**1%**	**513**	**536**	**-4%**	**330**	**229**	**44%**
Business services and secretarial	851	805	6%	442	377	17%	327	350	-7%	183	149	23%
Total	**2,016**	**1,869**	**8%**	**1,095**	**1,021**	**7%**	**840**	**886**	**-5%**	**513**	**378**	**36%**

Chargeable Hours

	Top 10			Top 11-25			Top 26-50			Top 51-100		
	Av. 2019	Av. 2018	% change 2018-19	Av. 2019	Av. 2018	% change 2018-19	Av. 2019	Av. 2018	% change 2018-19	Av. 2019	Av. 2018	% change 2018-19
Full equity partners	1,103	1,185	-7%	1,047	934	12%	972	930	5%	906	960	-6%
Fixed share equity partners	1,055	1,156	-9%	1,054	956	10%	1,012	988	2%	948	929	2%
> 5 year pqe	1,401	1,423	-2%	1,305	1,248	5%	1,144	1,213	-6%	1,054	1,080	-2%
3-5 year pqe	1,494	1,510	-1%	1,379	1,349	2%	1,283	1,239	4%	1,176	1,146	3%
1-2 year pqe	1,499	1,500	0%	1,358	1,331	2%	1,278	1,238	3%	1,136	1,139	0%
Newly qualified	1,460	1,462	0%	1,282	1,302	-2%	1,150	1,096	5%	1,109	1,107	0%
Legal executives and paralegals	962	967	-1%	1,092	1,042	5%	936	966	-3%	904	1,012	-11%
Trainess	1,142	1,183	-3%	1,032	1,081	-5%	939	944	-1%	855	905	-6%

Increased headcount at junior grades has not removed a key resource issue highlighted in previous years: the growing bulge of experienced fee earners at the >5 year pqe grade. This grade continues to represent a significant proportion of fee earner headcount from newly qualified upwards. Law firms need to consider the impact this is having on efficient resourcing models, both across practice areas and on individual assignments. Decisions taken around work allocation clearly also impact development and morale for grades below > 5 years pqe.

Law firms do appear to be focusing on the diversity and inclusion (D&I) agenda; for example, there is a gradual trend of increasing female representation at partner level. However, as law firm statistics (along with the wider professional services sector) remain below that seen in senior leadership roles in other sectors, there is still work to do to address the imbalance.

Top 25 firms have more established strategies at partner level for gender representation, but there is a way to go in terms of BAME representation. Top 10 firms have increased BAME representation in the last 2 years, although it has reduced in the Top 11-25 banding.

Whilst the majority (71%) of firms do set targets for female representation at partner level in the Top 25, explicit targets for BAME representation are minimal (Top 25: 18%). We are aware that an increasing number of law firms are considering establishing BAME targets and careful consideration and analysis is required. Firms should ensure that targets are based on realistic internal expectations of what success in this area would look like, based on the current workforce, as opposed to a broad brush approach based on wider market precedent.

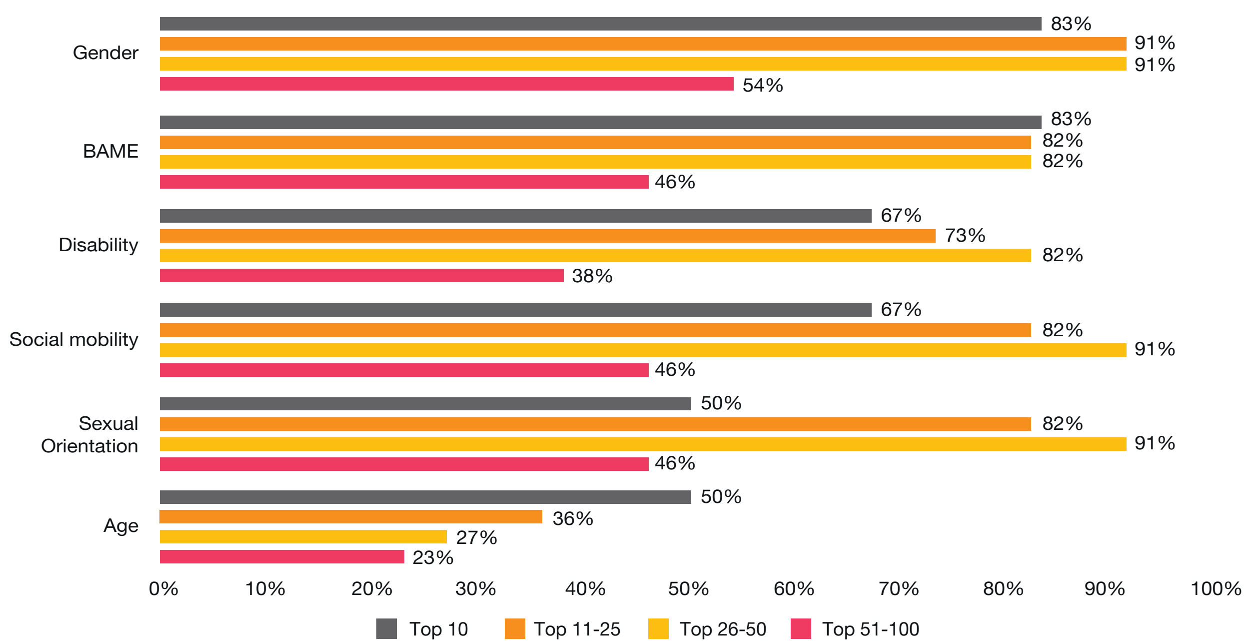
D&I initiatives will take time to effect, but clear articulation of an understanding of the issues, and how firms plan to address these challenges, will give confidence to internal and external stakeholders that progress is being made. Recruitment is cited as a key pillar of firms' D&I strategy; however, there are likely to be opportunities for firms to go further on a cultural level to embed a truly diverse and inclusive environment.

Financing

As firms look to the longer term, they recognise that continued investment in technology, people and the workplace (amongst other things) are required.

Firms have started to take action, with a significant number increasing their financing, either through the external banking market or absolute levels of partner capital/current account balances. Over half of all Top 100 firms have renegotiated banking facilities during the year and 63% of these increased their facility level. Further, the average levels of total partner capital and current accounts have increased: Top 10 - up 6.7% to £1,050k; Top 11-25 - up 12.7% to £817k; Top 26-50 - up 17.9% to £586k; and Top 51-100 - up 5.9% to £486k.

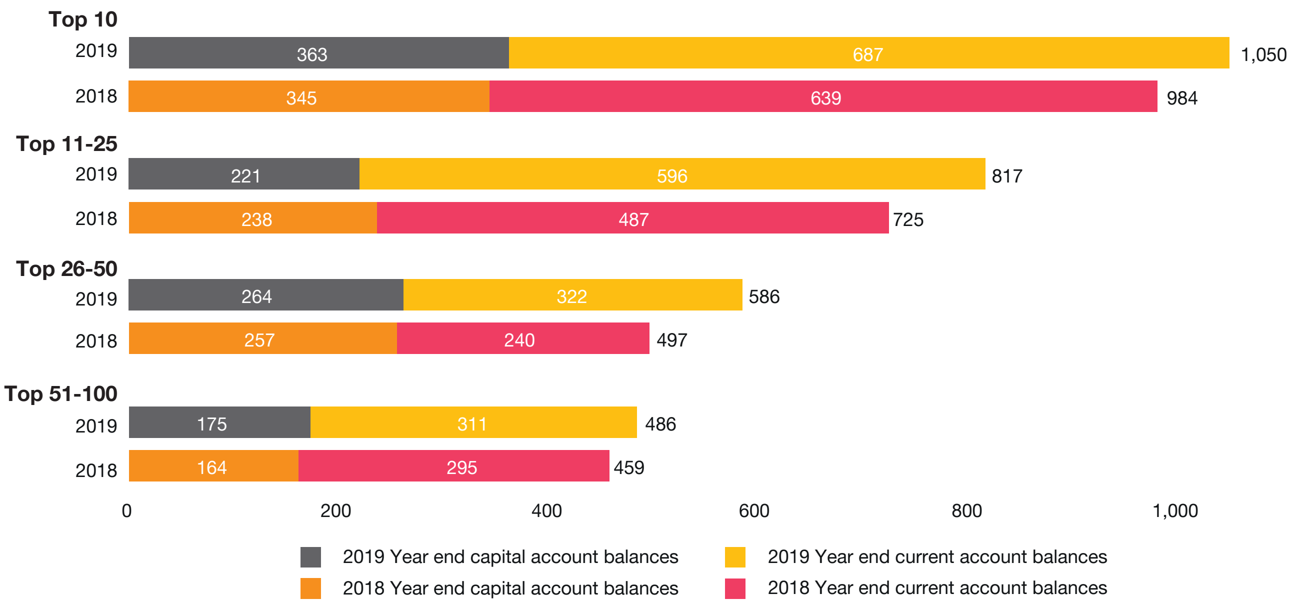
Areas where strategies are in place to address diversity issues



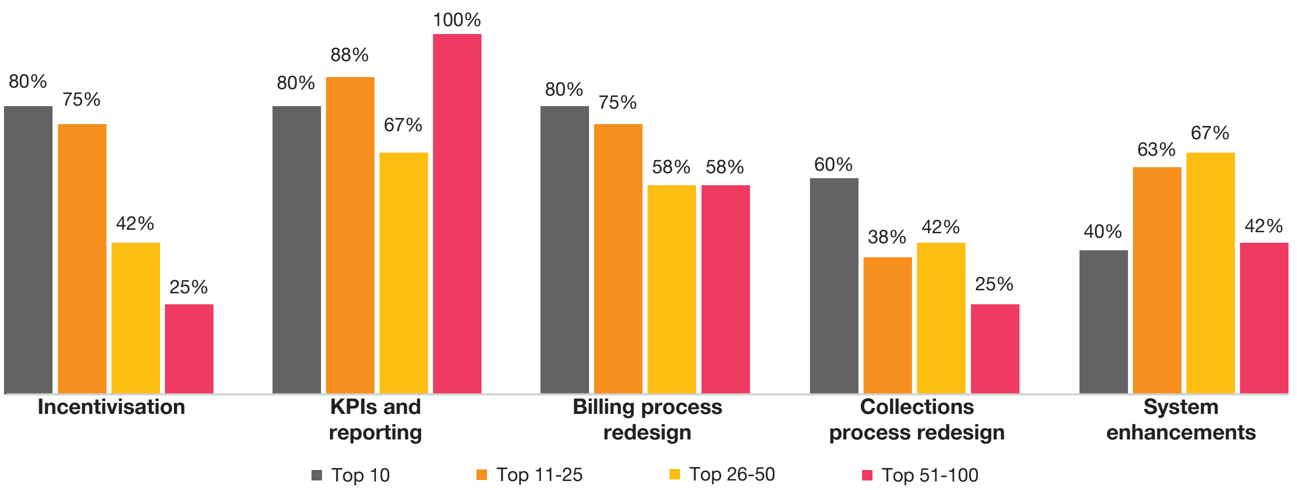
Despite the need for financing, firms continue to struggle with unlocking their cheapest source of finance through reduction of working capital. Whilst all bandings have improved year end lock up performance, there has been a marked deterioration in average lock up in Top 10 and 11-25 firms. The difference in year end to average lock up across the bandings ranges from 11.7% (Top 26-50 firms) to 18.7% (Top 10 firms). This means there is a significant lost cash opportunity, based on the difference in year end and average lock up, ranging from £2.5m in Top 51-100 firms to £32.5m in Top 10 firms. Improving cash to this extent would go some way to supporting the investment needs of the firm.

Larger firms continue to be impacted by challenging e-billing requirements, although development of RPA technology may reduce the administrative burden in this area. Elsewhere, a sustained focus on process discipline and customer payment behaviour can have a significant impact: firms need to ensure commercial thinking, supporting processes, systems and operating models are aligned to this goal from contract through to cash.

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



Key focus areas for lock up improvement



Cyber risk

Cyber security is a risk for all organisations. Law firms are increasingly targeted as they hold both a wealth of sensitive data and large amounts of client money. Unsurprisingly therefore, 76% of Top 100 firms said they were "somewhat concerned" or "extremely concerned" about cyber security.

According to the National Cyber Security Centre's (NCSC) 2018 report 'The cyber threat to UK legal sector', the most significant cyber threats that law firms face are phishing, data breaches, ransomware and supply chain compromise. Our survey supports this assessment, with respondents reporting phishing attacks as most common. In Top 10 firms, malware infection and loss or leakage of confidential information are the second and third most common incidents.

Known infection by viruses or malicious software appears surprisingly low outside Top 10 firms, with our survey reporting very few "significant attempts to break into the firm's network". Whilst Top 10 firms are more likely to be targeted, this suggests smaller firms may be failing to detect being compromised.

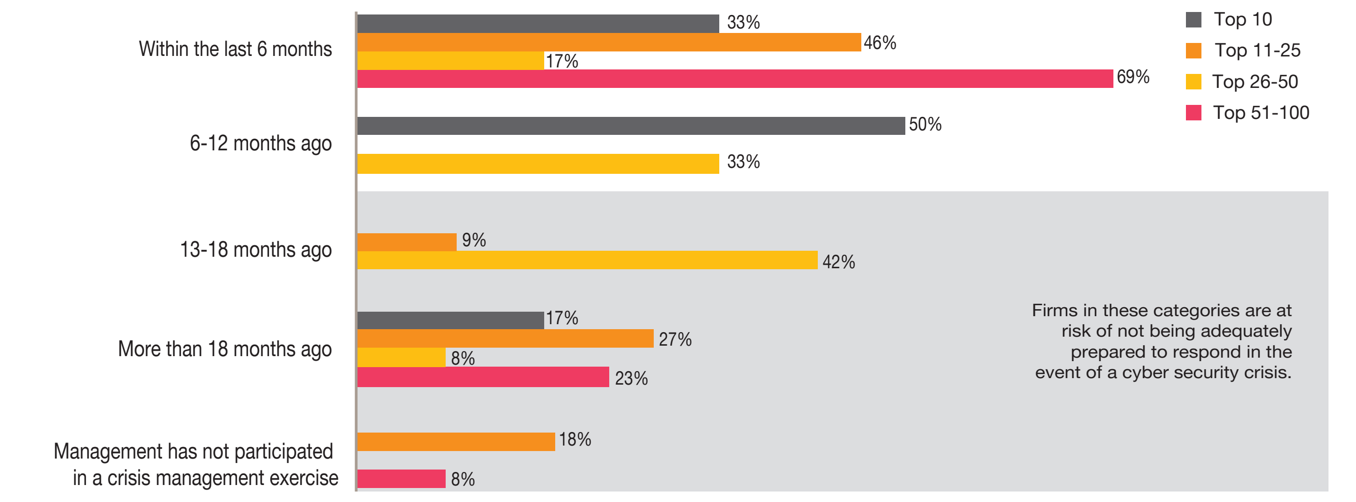
Our Business Support section notes that all firms have identified "improving use of technology" and "standardising and centralising business processes" as priorities over the coming year. Re-engineering business processes and rationalising IT applications are key enablers to improved cyber security. Stripping out complexity helps strip out cost, but it can also facilitate improved security. Fewer, simpler systems are easier to maintain and keep secure.

As law firms expand globally, so does their 'attack surface area'. Law firms will increasingly need to be secure, and be able to assure clients that they are so. This can involve a huge amount of effort, especially given increasingly challenging bespoke questionnaires. Commensurate investment in security (particularly where growth is fuelled by investment outside the UK) will help firms to be on the front foot.

Whilst our survey indicates that all firms have suffered cyber security-related incidents, outside of the Top 10 senior management participation in annual crisis management exercises is low. In the Top 10, 83% of senior management have been involved in an exercise in the last year. This drops to 46% in Top 11-25, 50% in Top 26-50 and 69% in Top 51-100 firms.

Given the risks, including reputational damage, senior management need to fully participate in a crisis management exercise at least once each year.

Senior participation in a crisis management exercise...



How can you make your law firm more 'securable'?

Cyber security is about far more than being able to demonstrate that security is good enough, whether to regulators and customers, or even in litigation. Compliance is important, but the real challenges are to make choices that reduce exposure, transform operations to minimise opportunity for attackers and essentially make your firm more 'securable'. We set out below a summary of factors that all law firms should consider in making their organisation more securable.

Look at things afresh

Look at new ways of thinking, new architectures and a rebuilding of technology infrastructure.

Re-engineer

Re-engineer business processes and rationalise IT applications, making processes more fit for the digital age.

Security in IT projects

Include security at the initiation of IT projects to ensure that requirements are included from the start.

Don't complicate a system

Avoid layering security controls onto already overly complex environments – this makes security hard and costly and more likely to fail. Rather, change what you have to make it easier to control. Stripping out complexity makes systems easier to maintain and secure.

Obtain comfort over security

Along with key IT checks over such things as vulnerability scanners, penetration testing and program update checks, firms should ensure their people are regularly tested to see how they respond to, for example, simulated phishing attacks.

The Future

Confidence over future performance in our prior year survey has had mixed results - predicted fee income levels were generally achieved, but not so with profit. Unsurprisingly, given the current political and economic uncertainty, firms this year are more cautious in their outlook. In the short term (2019/20), most firms expect modest fee income growth with profit improvement lagging. There are stark differences between top and bottom line expectations in the Top 11-25 (fee income and profit up 5.3% and 1.4% respectively) and Top 51-100 firms (5.8% and 1.5%).

This caution is replaced with greater optimism for 2020/21, with all bandings except the Top 51-100 expecting profit growth to exceed fee income increases. Top 10 firms are most confident of their ability to improve margin, setting profit growth at 6.8% compared to fee income at 4.6%.

Deal activity

There has been a growing appetite for deal activity in the UK legal sector, with 57% of Top 10 firms and 36% of Top 11-25 firms responding that mergers are at least somewhat likely within the next two years (2018: 40% and 27% respectively).

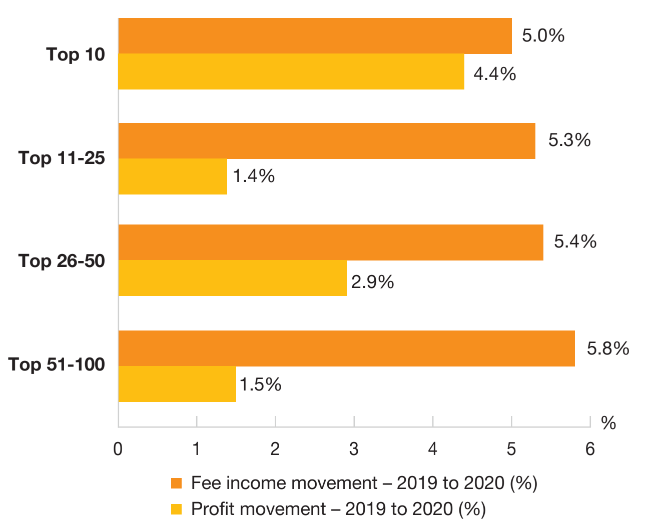
Those firms operating at the top end of the spectrum (in terms of market share) will continue to diversify their operations, geographically and along service lines. These firms are increasingly exploring deal/merger opportunities with international players to further tap into more profitable international markets, especially the US.

In the mid-tier, efforts to gain scale, new service capabilities and a broader geographic focus are more likely to be through consolidating with smaller or similar-sized firms. This can provide a stronger platform for future investment and attracting talent.

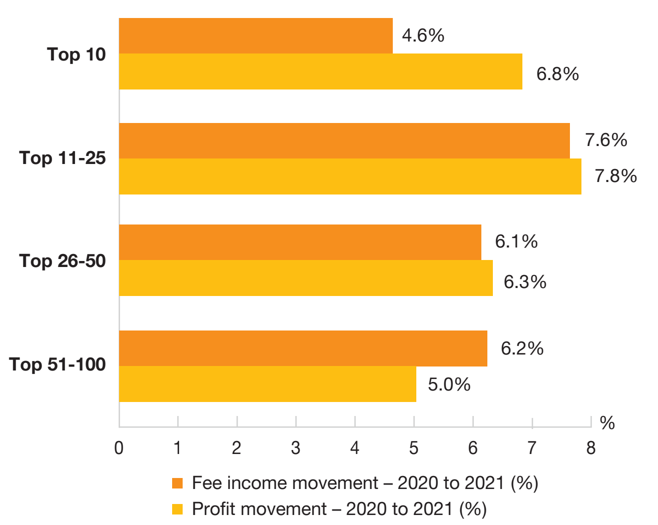
Certain mid-tier firms are also increasingly considering IPOs (or potentially PE investment) as a means to realise value and deal with inter-generational issues, gain access to growth funding and attract/incentivise talent.

There has been growing investor interest in alternative delivery models. This is reflected in the high market valuation for companies with disruptor status. Private equity firms are attracted by their cash generative nature, high scalability and opportunities for future growth.

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



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

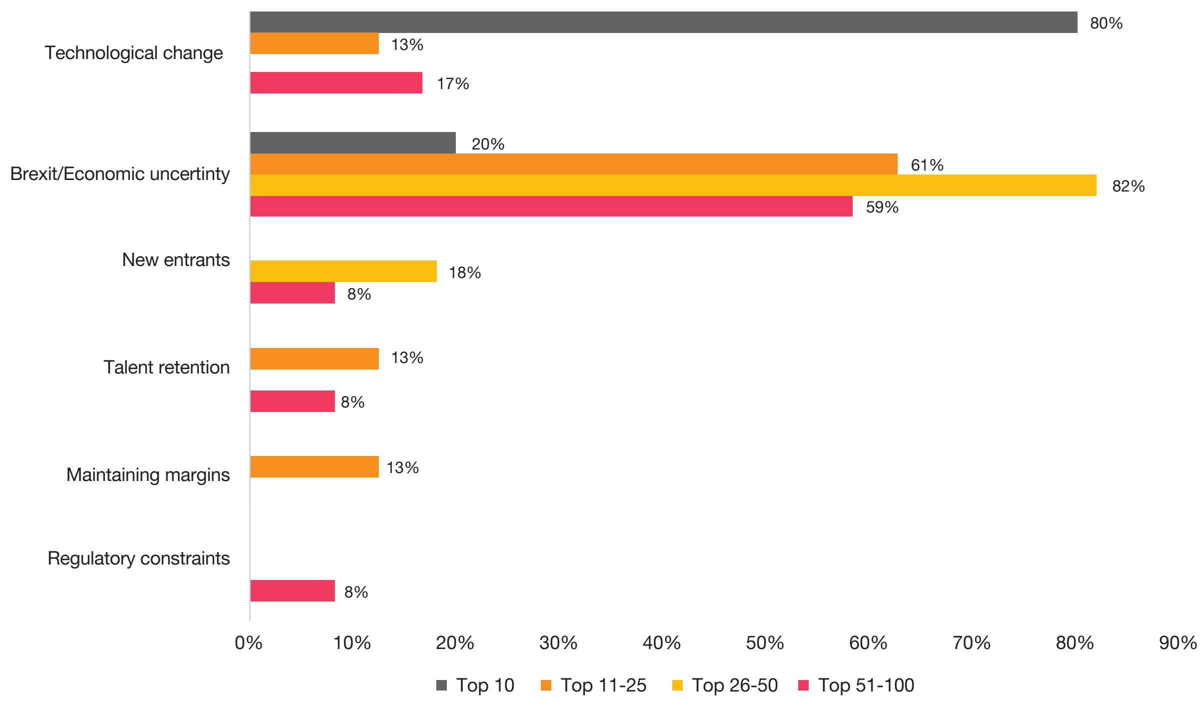


Key future challenges

As the deadline for Brexit gets closer, more firms see this as a key challenge to their financial performance aspirations. Whilst no Top 25 firm reported Brexit as their key challenge in 2018, 20% of Top 10 and 61% of Top 11-25 firms have done so in 2019.

Most Top 10 firms (80%) view technological change as their key challenge over the next 2-3 years. This is not surprising, as it is the larger firms who have and will continue to lead the way in using and developing emerging and digital technologies to improve efficiency and profitability.

The most significant challenge facing the legal profession over the next 2-3 years



At a Glance

1. Global financial performance

2. UK financial performance

3. Business support

4. People

5. Financing

6. Cyber risk

1. Global financial performance

Global headcount

- Top 10 firms have increased headcount, with a 1.7% and 14.8% increase in partner and fee earner numbers respectively.
- Partner headcount is up in Top 11-25 firms by 3.8%, but fee earner numbers have reduced by 3.5%. The latter is in stark contrast to fee earner growth of 59% between 2016 and 2018, with these firms now looking to consolidate their investment in workforce to improve profitability.

Global fees

- Average global fee income has grown by 6.1% to £1,037m for Top 10 firms, with 80% recording growth of between 5% and 11%. The remaining 20% experienced a 1% reduction in fee income.
- Top 11-25 firms grew global fees to £270m (up 8%), with half recording growth of between 11% and 16%, 38% recorded growth between 5% and 10% and the remaining 12% reported minor reductions in fee income.
- 74% of Top 10 fee income growth was achieved through improved international performance (up £44.0m), compared to UK growth of £16.2m. In Top 11-25 firms, this split was more even, with UK and international growth of £10.0m and £8.4m respectively.
- Movements in foreign exchange had only a limited impact on fee income movements. Top 10 firms saw a reduction of £0.7m and Top 11-25 firms experienced a rise of £1.7m.

Global profits

- Top 10 firms recorded average profit growth of 6.5% to £406m. Top 11-25 firms fell short of Top 10 performance, with an average profit increase of 5.7% to £92m.
- 77% of Top 25 firms grew profits, whilst the remaining 23% experienced falls in profit of between 6% and 10%.
- International offices contributed more to profit growth than UK firms. For Top 10 firms, international offices grew profit by 9.5% before accounting for exchange rate movements (equating to £20.9m of global growth) compared with 2.8% in the UK (or £4.8m of global growth). The story is similar in the Top 11-25, with 11.4% (£2.8m) international and 3.0% (£1.8m) UK profit growth respectively.
- Top 10 firms' global net profit margin (before full and fixed share equity partner remuneration) has increased slightly, by 0.1 percentage points to 38.0%. Top 11-25 firms posted a 0.7 percentage point fall to 33.6%, mainly due to an increase in staff costs.

Movements in foreign exchange rates

- Movements in foreign exchange rates have had limited impact on law firms in the current year.
- Top 10 firms' fees and profits were negatively impacted by movements in foreign exchange rates, by £0.7m and £1.0m respectively.
- Top 11-25 firms benefited from foreign exchange rate movements, by £1.7m on fees and £0.4m on profits.

International analysis

- All Top 10 regions increased net profit margins by between 3 and 6 percentage points, with the exception of (i) Africa, where the net profit margin increased from an average of 11% to 21%; and (ii) Australia, where there was a fall of 9 percentage points to 24%.
- Top 11-25 firms' performance was more mixed. Western Europe and Middle East both recorded falls of 7 percentage points to 13% and 6% respectively. China also increased their net profit margin from 4% to 16%, whilst Rest of Asia and Far East recorded a fall of 2 percentage points to 21%.
- The UK to international profit margin performance gap is narrowing. Top 10 UK net profit margin now stands at 35.5% and this is 1 percentage point ahead of Western Europe performance. The gap has reduced for most other regions, but remains significantly behind UK.

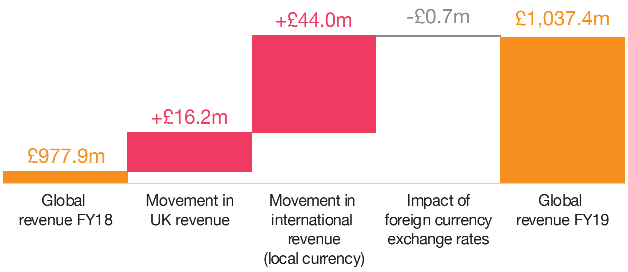
UK top tier vs US top tier

- UK top tier firms continue to be outperformed by their equivalents in the US in respect of all KPIs; for example, average US top tier PEP stands at £2.4m, significantly ahead of the UK top tier performance of £1.3m.
- Average fee income and net profit in US top tier firms grew by 9.0% and 9.3% respectively and this compares with the UK at 6.4% and 5.2%.
- In the US top tier, 35% of firms achieved double digit revenue and profit growth. This compares with 13% and 38% respectively in the UK top tier.

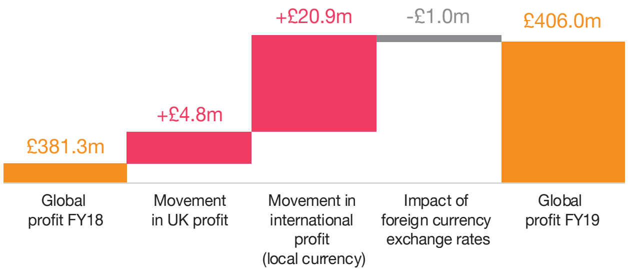
Global fee income and profits: source of growth

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.

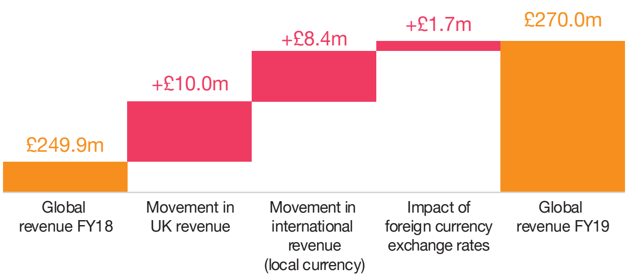
Top 10 – Revenue



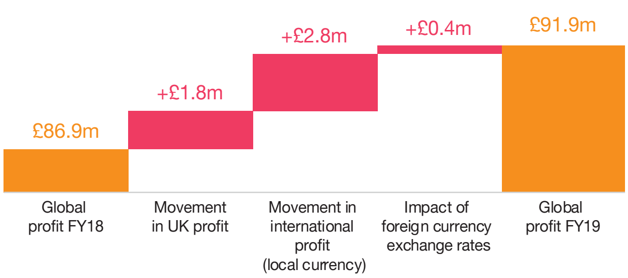
Top 10 – Profits



Top 11-25 – Revenue



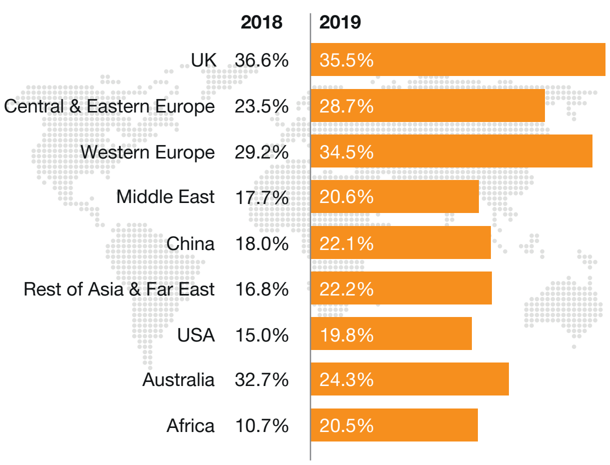
Top 11-25 – Profits



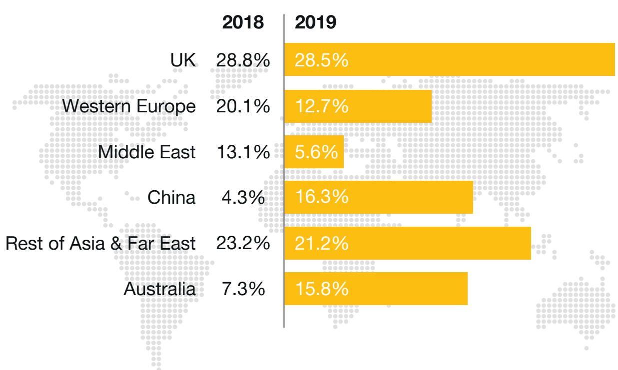
Net profit margins: UK vs international regions

UK net profit margin continues to be well ahead of all international regions, with the exception of Top 10 Western Europe where the net profit margin is only 1.0 percentage point behind UK.

Top 10 firms



Top 11-25 firms



2. UK financial performance

Fees

- More firms experienced fee income growth in 2019: 89% of the Top 100 vs 84% in 2018. However, the average growth levels have been reduced from 8.3% in 2018 to 5.9% in 2019.
- Top 10 and 11-25 firms grew UK fee income by 4.1% and 6.3% respectively (2018: 5.0% and 9.2%). Top 26-50 and 51-100 firms grew by 3.3% (2018: 7.2%) and 9.2% (2018: 10.0%).
- Top 51-100 firms saw the greatest proportion of firms achieving double digit growth at 36% (2018: 29%). This compares with no Top 10 firms (43% in 2018), 27% of Top 11-25 and 7% of the Top 26-50.
- Fees per fee earner have continued to grow, at 5.1% in the Top 10 (to £415k), 7.3% in Top 11-25 (£325k), 5.8% in Top 26-50 (£237k) and 2.7% in Top 51-100 firms (£188k). These increases are despite a general trend of rising fee earner headcount in larger firms.
- Fees per chargeable hour have increased across all Top 100 bandings, most notably in the Top 11-25 and 26-50, 7.1% and 7.0% respectively (2018: 3.9% and 1.4%) to £285 and £228 per hour. The Top 10 firms reported an average increase of 4.3% (2018: 1.7%) to £315 per hour, whilst the Top 51-100 reported a 0.5% fall (2018: increase of 12.9%) to £200 per hour.

Costs

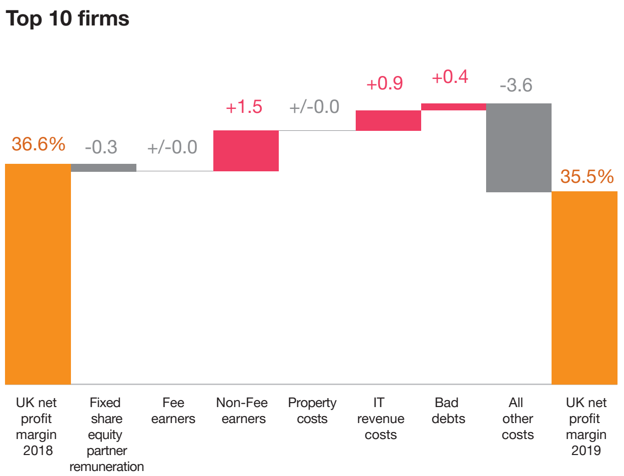
- The total staff cost ratio (excluding fixed share equity partner remuneration) remained within 1.5 percentage points of 2018 across all bandings.
- Top 10 firms maintained the fee earner staff cost ratio at 26.7%, whilst Top 11-25 firms reported a fall of 1.7 percentage points to 26.6%. With known increases in legal sector salaries, this can only be attributed to fee income growth either matching or being greater than staff cost inflation.
- Top 10 non-fee earner staff cost ratio has decreased by 1.5 percentage points to 11.2%, equating to an average additional profit of £6.4m.
- Top 11-25 non-fee earner staff cost ratio increased by 1 percentage point to 14.5%, and this partially offsets the fall in the fee earner staff cost ratio noted above.
- In all bandings, the gross profit margin per hour increased, both by value and margin percentage. This was due to the increase in fee income per chargeable hour exceeding the increase in fee earner costs per chargeable hour. Top 10 firms' fee earner cost per chargeable hour has increased by 5.1% to £103, whilst fee income per chargeable hour has grown by 4.3%, effectively adding £8 to the bottom line for every additional £13 of fee income.
- Top 51-100 firms is the only banding where cost per chargeable hour fell by 3.5% to £83.

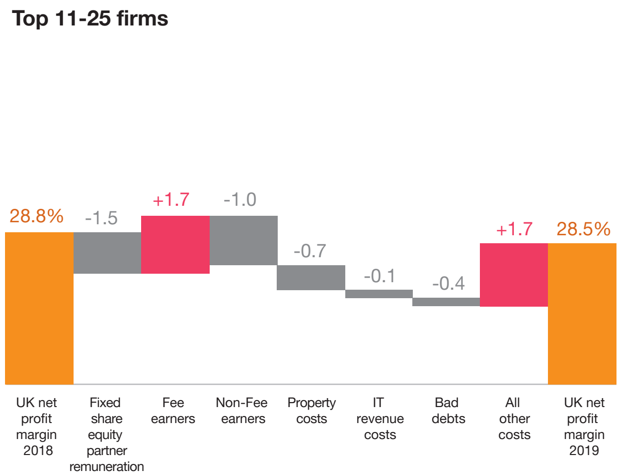
Profits

- A significant number of firms continue to feel pressure on profits, with over one third of all Top 100 firms reporting falling profits in 2019 (2018: 29%). Of the 89% of firms reporting fee income growth, just under two thirds translated this into increased profit.
- The trend of declining profit margins has continued for Top 10 firms for a fifth year, from 40.0% in 2014 to 35.5% in 2019 (36.6% in 2018). Top 11-25 and 51-100 firms also reported falling margins; by 0.3 percentage points to 28.5% and by 1.7 percentage points to 22.9%. Top 26-50 firms were the only banding to increase the net profit margin, from 24.2% to 24.7%.
- The Top 10 to 11-25 firms' net profit margin performance gap continues to narrow. This was 11.8 percentage points in 2014 and is now 7.0 percentage points.
- Despite falling margins, average PEP continues to grow and has reached record highs across all bandings. This, in part, is a result of movement (or management) of partner headcount.

Net profit margin bridge: 2018 to 2019

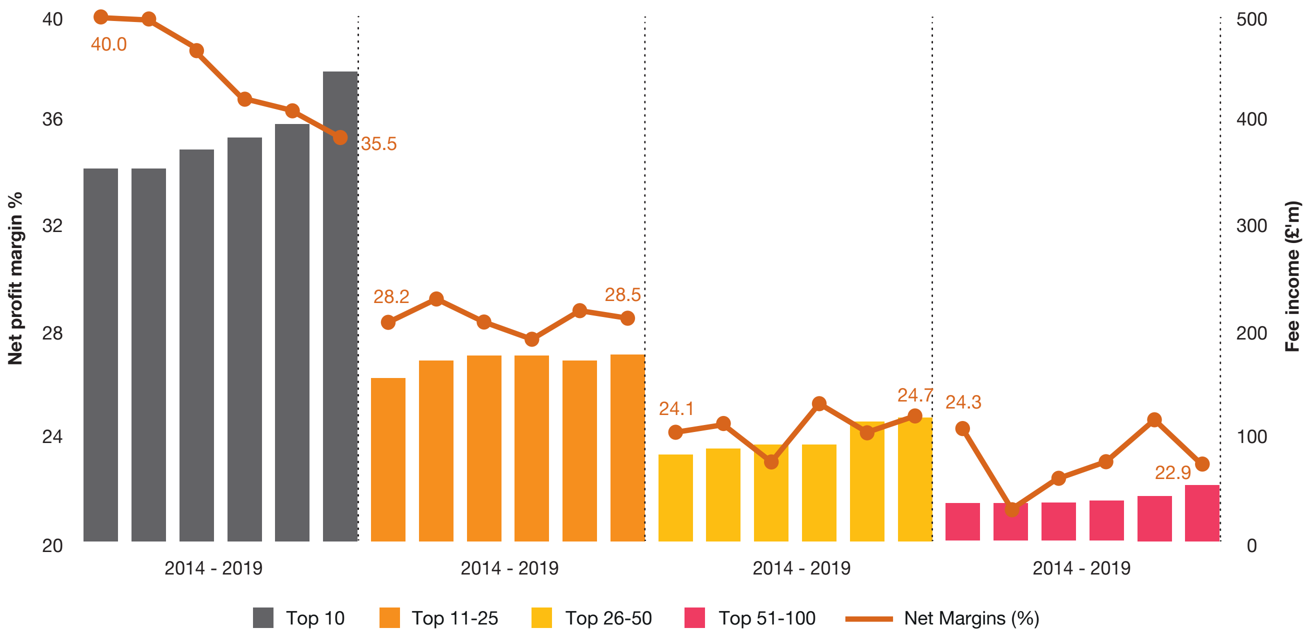
Top 10 firms have made savings in non-fee earner and IT revenue costs, but these have been eroded by higher other costs. Top 11-25 firms have experienced offsetting movements in fixed share equity partner remuneration costs and fee earner costs, whilst non-fee earner costs have increased.





Movement in UK fee income and net profit margin (2014 to 2019)

In Top 10 firms there has been a general trend over the last 5 years of increasing fee income, but falling profit margins. Whilst fee income has increased in the remaining Top 100 bandings, margins from 2014 to 2019 have shown more volatility in the intervening years.



3. Business support

Overall

- Finance, Risk & Compliance and HR are considered the strongest performing functions across all firms in 2019, with IT falling two places to fifth. Both Finance and HR reversed a three-year decline in their perceived performance, strengthening their position as higher-performing functions.
- Secretarial Services and Knowledge Management continue to be two of the lowest-rated functions. However, the perceived performance of Secretarial Services has improved considerably this year.
- Procurement remains the only function that, on average, is seen as a weakness by Top 100 firms, despite a significant improvement in performance.
- For the third consecutive year, the top priority for business support is "improving the use of technology". "Standardising and centralising processes" and "support improvements in legal service offering" also continue to be focus areas. The priority of "data analytics" has fallen, reversing the trend of recent years, despite a 25% increase in the number of firms reporting that they have data analytic specialists. A question remains whether firms are getting the most from their data in order to improve decision making.
- More than half of firms have delivered a "Time and disbursement capture", "HR and L&D", and "Mobile and remote access" project in the last 1-3 years and more than a third have delivered a Practice Management System or "Risk and compliance" project. Further, more than 30% of firms have a "Mobile and remote access", "Pricing", or "Data analytics" project underway.

Finance

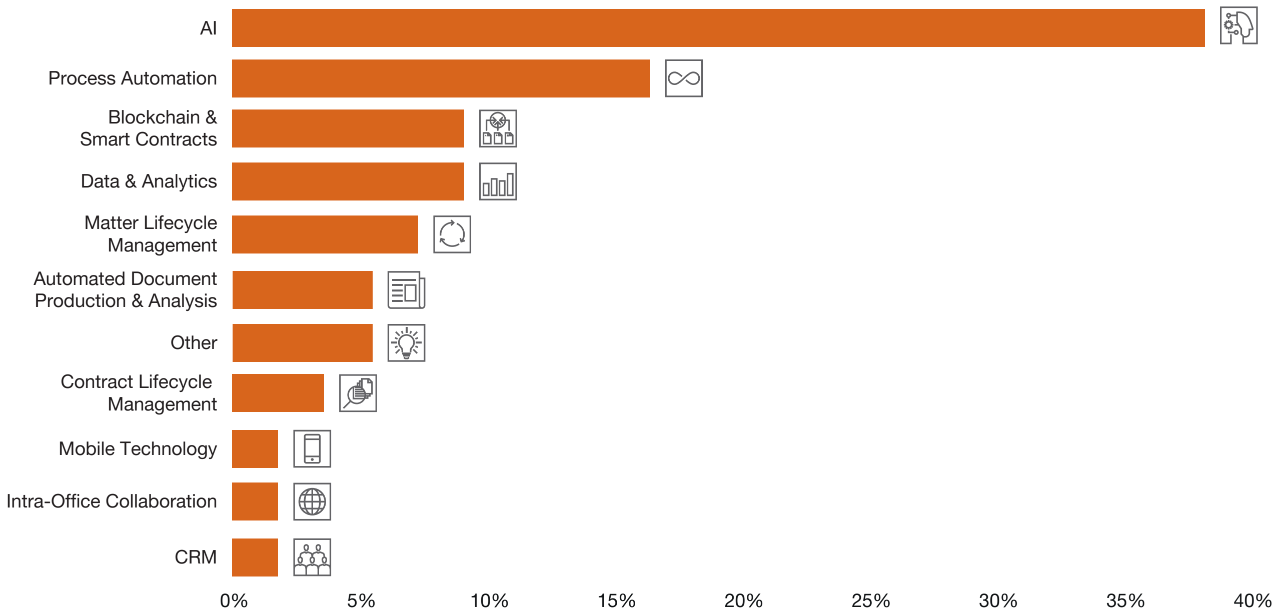
- The finance function's top three priorities are pricing and profitability, working capital and business analysis/ reporting. These priorities are reflective of the continued high fee income write off levels and widening gaps in year end and average lock up performance.
- The continued focus on pricing has resulted in a narrowing of the "pricing performance" gap between importance and perceived current performance for all except one of the key pricing behaviours. What will be frustrating for many firms is the inability to flow these improvements through to the high level of fee income write offs.

Technology

- Adoption of digital and emerging technologies has advanced again across all banding of firms. Adoption of more widely established technologies (e.g. mobile application, client collaboration tools, and automated document production) has progressed by at least 5% across the Top 100 since last year to between 53% and 74% of firms. Data visualisation and artificial intelligence (AI) technologies are established in half of Top 10 firms, and approximately a quarter of all Top 100 firms.
- Law firms predict AI will be the most disruptive technology in the sector over the next 5 years, cited by 38% of Top 100 firms. This compares with process automation at 16%, blockchain and smart contracts at 9%, and data and analytics at 9%.
- AI has started to mature most in Top 10 firms (50% established, 50% piloting); although smart contracts are less mature in these firms (0% established, 70% piloting). This compares to 16% for AI and 11% for smart contracts technology (established) across the Top 11-100.
- Despite the progress on emerging technologies, capital spend is relatively limited. On average, Top 100 firms reported capital investment in emerging technologies of only £597k in the last year.
- With the growing focus on innovation, new technologies, improvements in legal service offerings and associated investment, it is critical that firms have a robust strategy and metrics to manage the experimentation and change. The majority (65%) of Top 100 firms report that they have a clear and flexible strategy for realising the benefits of innovation - however, there is variation between bands from 80% of Top 10 firms to only 54% of Top 26-50 firms. Only 55% of Top 100 firms' leaders have innovation-based objectives and a minority (42%) have agreed metrics to track the progress of innovation.

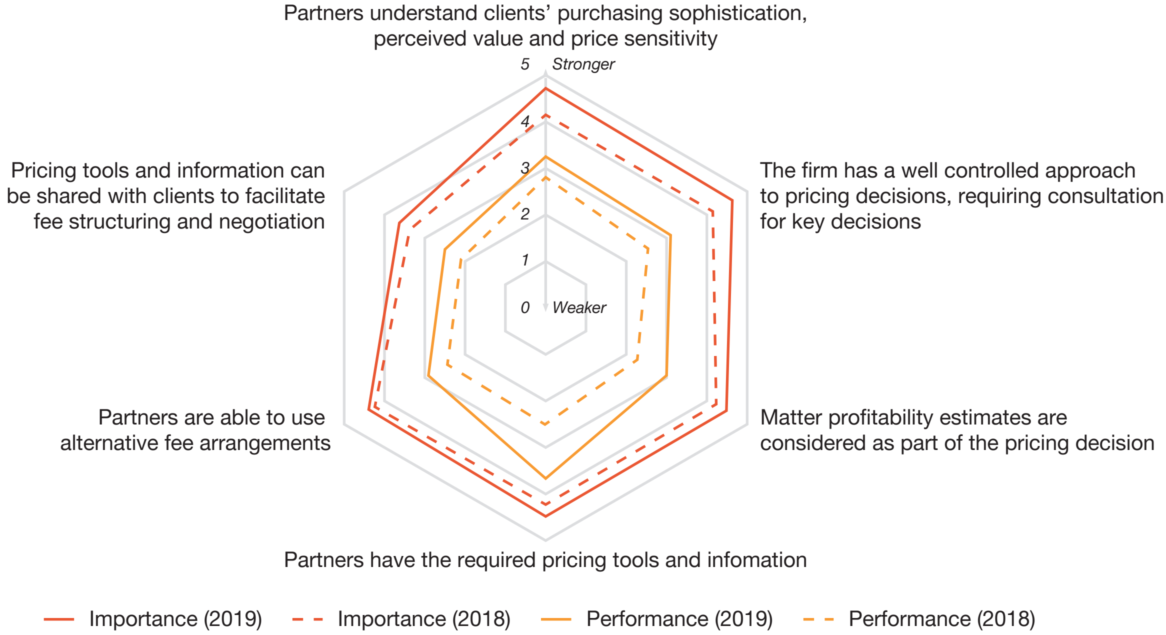
Disruptive technology over the next five years

Law firms predict AI will be the most disruptive technology in the legal sector over the next 5 years, cited by 38% of Top 100 firms. This compares to process automation at 16%, blockchain & smart contracts at 9%, and data & analytics at 9%.



Pricing behaviours (Performance vs. Importance) for Top 100 firms

Continued focus on pricing has narrowed the "pricing performance" gap between firms' view of importance and current performance for all except one of the pricing behaviours.



4. People

Headcount

- Total headcount has increased in the Top 10 (8%) and Top 11-25 (7%), whilst falling in the Top 26-50 (-5%) and these reverse the movements of prior year. There appears to have been a significant increase in the Top 51-100 workforce; however, this is largely due to a change in mix of respondents. On a like for like basis the Top 51-100 total headcount increases have generally been between 1% and 6%.
- Partner headcount continues to be managed carefully, with reductions at full equity in the Top 11-25 and 51-100 (by 5.4% and 7.4% respectively). Top 26-50 firms, on average, have held full equity partner numbers flat, whilst Top 10 firms have seen a 2.8% increase.
- Top 10 firms have focussed on increasing junior headcount; for example, two thirds of these firms increased the number of newly qualified and paralegal and legal executives.
- In Top 11-25 firms, there is more of a widespread increase in headcount across the different fee earner grades, excluding 3-5 years pqe and > 5 years pqe where headcount decreased.

Staff turnover

- Staff turnover continues to be higher than expected compared to other professional service organisation sectors across the fee earner grades, with the exception of newly qualified and trainees.
- In the 1-5 years pqe grades, the largest turnover is for 3-5 years pqe for all Top 50 bandings (Top 10: 19%; Top 11-25: 19%, Top 26-50: 22%). This is above what we would consider as optimal attrition, and with high headcount at the > 5 years pqe grade, may suggest concern over opportunity for advancement.
- Staff turnover rates at the paralegal and legal executive grade continue to be high in a number of firms, reflecting the shorter term nature of contracts and high levels of mobility. The range across the bandings is from 14% in Top 51-100 firms to 42% in Top 10 firms.

Leverage

- As changes to business support headcount mirror those across the fee earner population, the ratio of fee earners to non-fee earners has remained generally flat (Top 10: 1.3 in 2019 and 2018, Top 11-25: down 0.1 to 1.5, Top 26-50: up 0.1 to 1.6; and Top 51-100: up 0.3 to 1.8).
- Top 10 and 11-25 firms have increased the ratio of fee earners to full equity partners, in Top 10 firms from 7.2 to 7.7 and in Top 11-25 firms from 7.5 to 8.7, and this reflects fee earner headcount increases and management of partner headcount.

Partner bonus performance conditions

- In Top 10 and 26-50 firms, there is an even weighting between personal and financial performance metrics driving bonus outcomes for fixed share equity partners. There is much greater emphasis on personal performance in Top 11-25 firms.
- It is important that all firms continue to embed key operational (such as reducing lock-up) and strategic priorities (such as referral of work) into their bonus targets, not just for partners, but also other fee earning staff.

Chargeable hours and utilisation

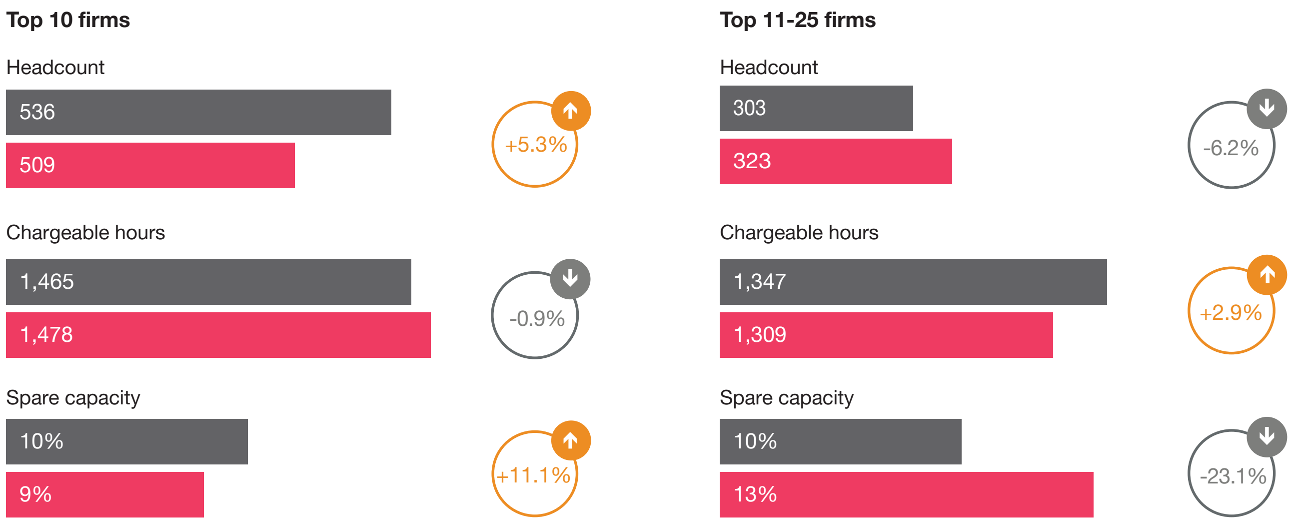
- Chargeable hours in Top 10 firms have fallen for full and fixed share equity partners (6.9% and 8.7% respectively) and trainees (3.5%) and are generally flat across the remaining grades.
- Top 11-25 firms have increased chargeable hours at all grades except newly qualified and trainees (down 1.5% and 4.5% respectively).
- Significant spare capacity continues across all bandings and all grades. Focussing on the post qualified grades, this ranges from 7% spare capacity for 1-2 years and 3-5 years pqe in Top 10 firms up to 21% for >5 years pqe in Top 51-100 firms.

Diversity

- The gradual trend of increasing female representation at partner level over the last 7 years (2012 to 2019) has continued for Top 10 (15.6% to 20.4%), Top 26-50 firms (14.4% to 19.9%) and Top 51-100 firms (14.4% to 18.4%). Over that same period, the percentage has dropped in Top 11-25 firms from 18.7% to 18.1% (2018: 19.3%).
- At trainee level, firms across all bandings continue to recruit more females than males (c.60% female representation across the vast majority of respondents).
- BAME representation in Top 10 firms at partner level is flat at 7%, whilst at the trainee grade it has grown from 19% to 22%. In Top 11-25 firms, BAME representation has fallen for partners (8% to 5%) and trainees (18% to 12%).
- In the Top 10, 83% stated that they had a strategy in place to address gender and BAME imbalances across the business. This compares with the majority of Top 11-25 firms, where 91% have strategies in relation to gender and 82% in respect of BAME. The strategies take the form of formal targets/policies for the most part, whilst some firms note initiatives such as parental support and internal networks.
- In terms of diversity targets, 83% of Top 10 firms have targets for female representation at partner level compared to 64% in the Top 11-25. In the Top 10 and Top 11-25, just under one fifth have targets for BAME representation at partner level.

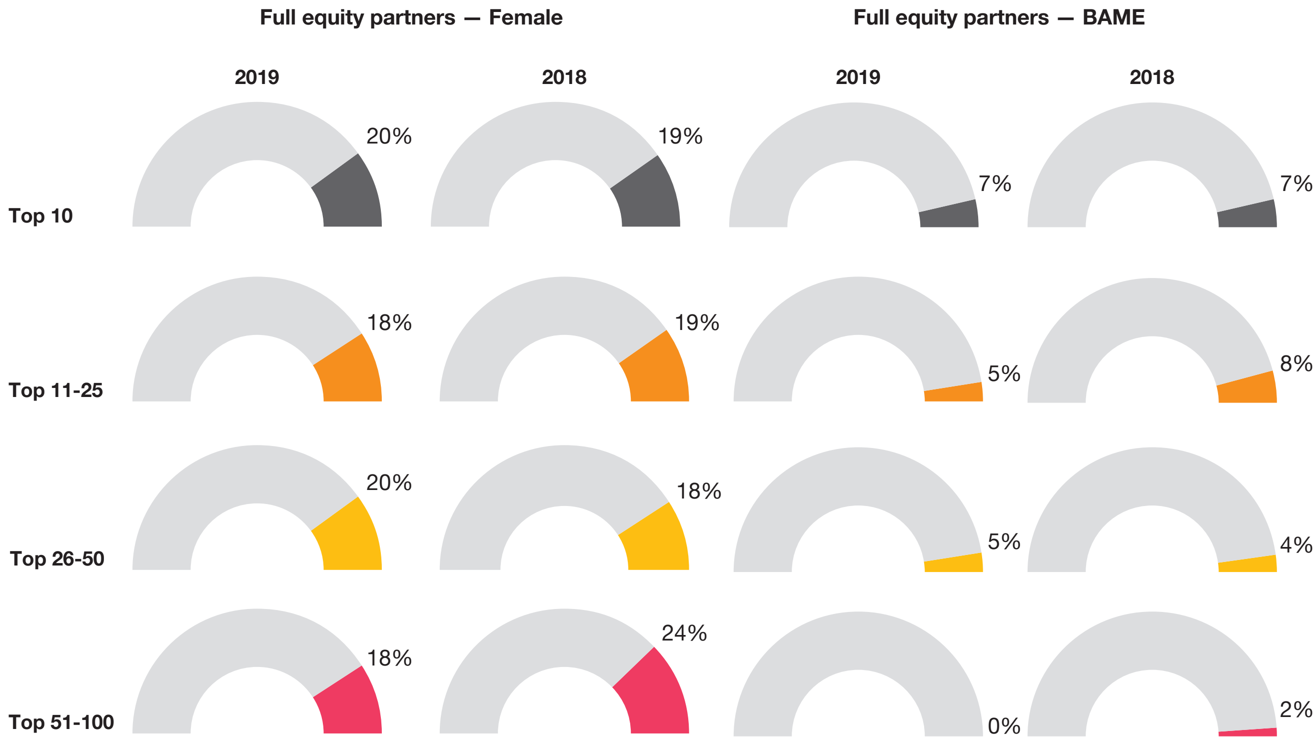
Movement in headcount, chargeable hours and spare capacity (1 - >5 years pqe grades)

Spare capacity for the 1 - >5 years pqe grades has increased slightly in Top 10 firms and fallen by 3 percentage points in Top 11-25 firms, resulting in a consistent spare capacity of 10% across both Top 10 and 11-25 firms in 2019.



Female and BAME representation at full equity partner level

From 2018 to 2019, there have been only minimal movements in respect of female and BAME representation at full equity partner level, with the exception of the significant drop of female representation in Top 51-100 firms.



5. Financing

Lock up

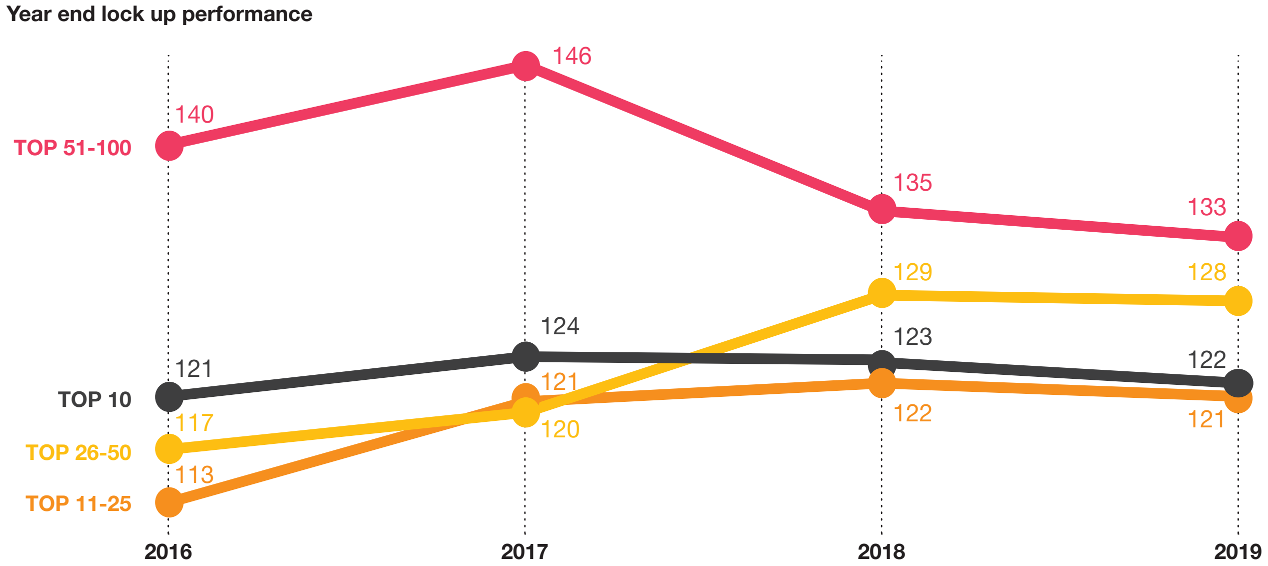
- For the first time in several years, year end lock up performance improved across all four bandings, albeit the improvement was only modest at a maximum of 2 days in each banding.
- For all bandings except the Top 10, WIP performance has driven this improvement, decreasing by between 5 to 7 days. This has obviously been offset by a deteriorating debtor day performance.
- In contrast to year end performance, average lock up has worsened for Top 10 and 11-25 firms by 9 days (to 150 days and 144 days respectively) and this more than outweighs the minor year end improvement.
- Both Top 26-50 and 51-100 firms improved average total lock up performance by 3 days (to 145 days and 151 days respectively). However, average lock up in all bandings continues to track significantly behind year end lock up and this represents a lost cash opportunity.
- An integrated operating model, with clear links between billing and collections teams and practice staff, will help firms achieve accurate and timely billing supported by an effective collections approach.

Finance

- Average full equity partner capital balances have increased across all bandings (by between 2.7% and 6.7%), except Top 11-25 firms where they have fallen by 7.1% to £221k as a result of a change in the mix of respondents. When removed, it becomes an increase of 4.5%.
- The above occurs alongside a varied change in the timing of partner profit distributions across the bandings. Top 10 firms, on average, reduced the proportion of profit paid in the year it is earned, dropping 8 percentage points from 55% to 47%. However, one firm's significant reduction caused this, with only minimal movements across the rest of the Top 10. The Top 11-100 bandings increased their in-year distribution, most notably the Top 11-25 with a 13 percentage point increase to 62%.
- As rising average lock up days are an increasing draw on cash, it is no surprise that a significant number of firms have refinanced during the year and the majority of those have increased the level of their facilities. For example, half of Top 10 firms refinanced during the year and all of these increased their facilities.
- Firms are not yet feeling the pinch from external lenders on their borrowings; approximately 70% of firms who renegotiated their facilities reported that existing interest rates and fees either stayed the same or decreased. It would appear that lenders, for the meantime, will continue to support the legal sector.

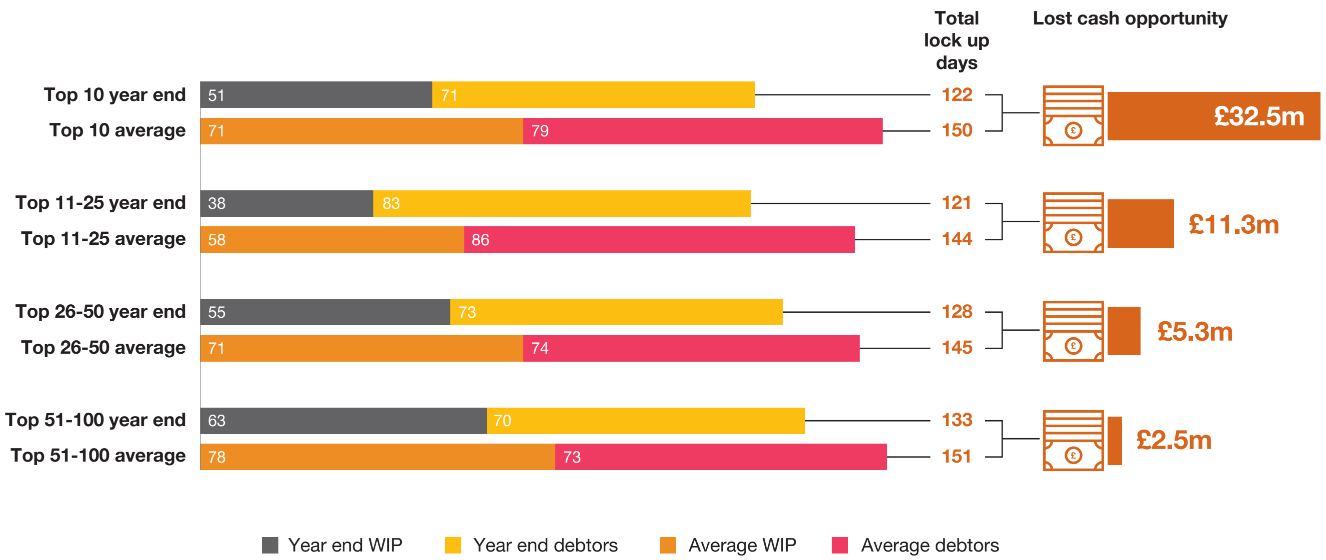
Trend in average UK year end total lock up days

Year end lock up performance has improved across all bandings by between 1-2 days. However, Top 11-25 and 26-50 firms' performance is 8 and 11 days higher than in 2016.



Year end versus average lock up and lost cash opportunity

There is a significant lost cash opportunity across all law firms due to the difference in year end and average lock up performance, amounting up to an average of £32.5m in a Top 10 firm.



6. Cyber risk

The cyber security threat

- Law firms consider the cyber threat to be greater than one year ago, the second greatest threat behind Brexit (up from 2018 when it ranked third).
- This year, every respondent to our survey suffered a security incident, with the most common attack being phishing.
- Amongst Top 10 firms, 100% suffered a phishing attack, 75% suffered a malware attack and 25% experienced network intrusion, DOS, and confidential information loss or leakage.
- In Top 11-25 and 26-50 firms, the top three attacks were phishing, other incidents caused by staff and loss or leakage of confidential information.
- Overall, network intrusion was the least common known cyber security attack and this, perhaps, implies poor detection capabilities across the legal sector.
- The insider threat is prevalent amongst all sizes of firms, with 75% of Top 10 and 90% of Top 11-100 having experienced incidents due to insiders over the last year.

IT capital spend

- Average global IT capital spend of Top 10 firms was much higher than that for the Top 11-25, at £17.2m (1.9% of global fee income) compared to £2.4m (0.9% of global fee income), albeit the range in the Top 10 is significant (£4.6m to £51.6m). This highlights a need for some firms to increase their level of IT capital investment.
- We acknowledge there are various demands on IT capital spend; however, investing to become more "securable" in the face of an ever increasing cyber security threat is clearly business critical.

Executive Ownership

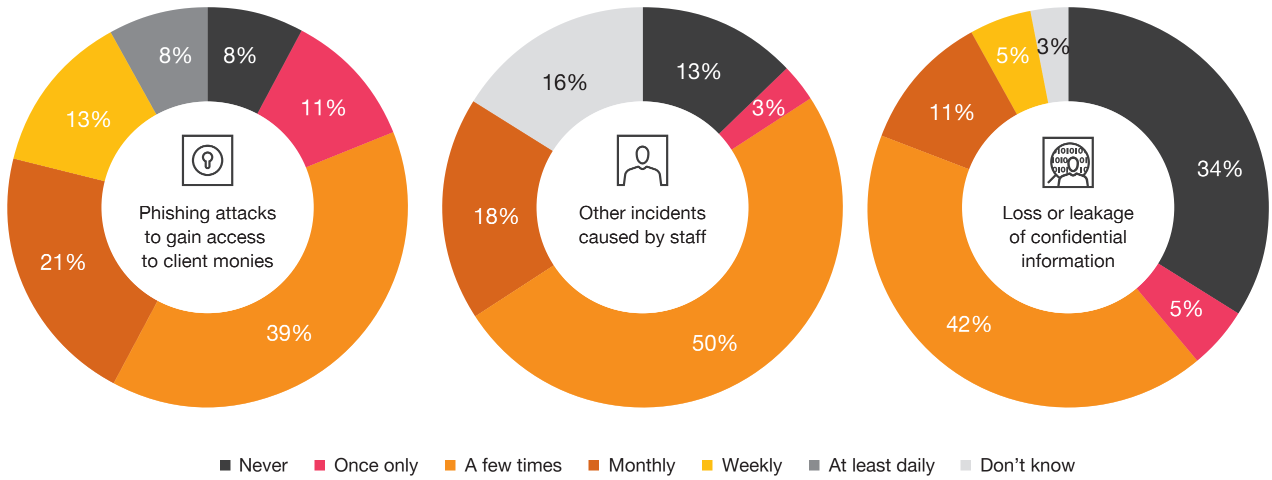
- Despite widespread acknowledgement of the cyber security threat, a number of law firms have no executive level risk ownership, true for 40% of Top 10 and 82% of Top 11-25 firms.
- For the larger firms in the Top 25, that may be reflective of Chief Information Security Officers ("CISOs") not sitting on boards. For others, a CISO may not even exist.
- Cyber security risks are not always receiving the due attention and budgetary considerations at the right level of influence. We consider it imperative that cyber security risk is owned at an Executive level and features on the Board Risk Register.

Crisis Management

- Crisis management is a key component of ensuring resilience against a cyber attack, but this area does not appear to be prioritised outside Top 10 firms.
- In Top 11-25 firms, 54% have either not had senior management participate in crisis management exercises or they have not done so for over 12 months. This compares to 83% of Top 10 firms that have had senior management participate in a cyber crisis management exercise in the last 12 months.
- There is a real risk that firms outside the Top 10 are not adequately prepared to respond effectively in the event of a cyber security crisis.

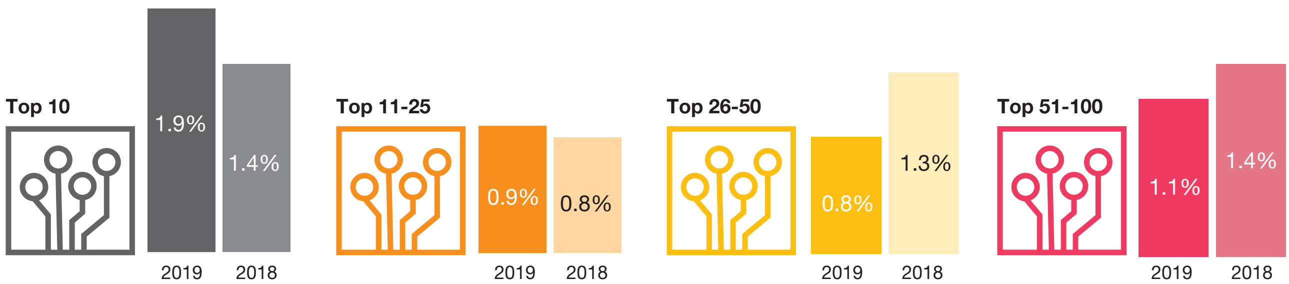
Frequency of cyber incidents suffered (Top 100 firms)

The most common cyber attack is in the form of phishing to gain access to client money, whilst incidents caused by staff and loss or leakage of confidential information are also common.



Total IT capital spend as a percentage of fee income

Total IT capital spend as a percentage of global fee income has increased in Top 10 and 11-25 firms, whilst it fell in Top 26-50 and 51-100 firms. Overall the 2019 IT capital spend as a percentage of fee income remains below the average when compared to other sectors, particularly with the spend required in order to make IT securable.



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