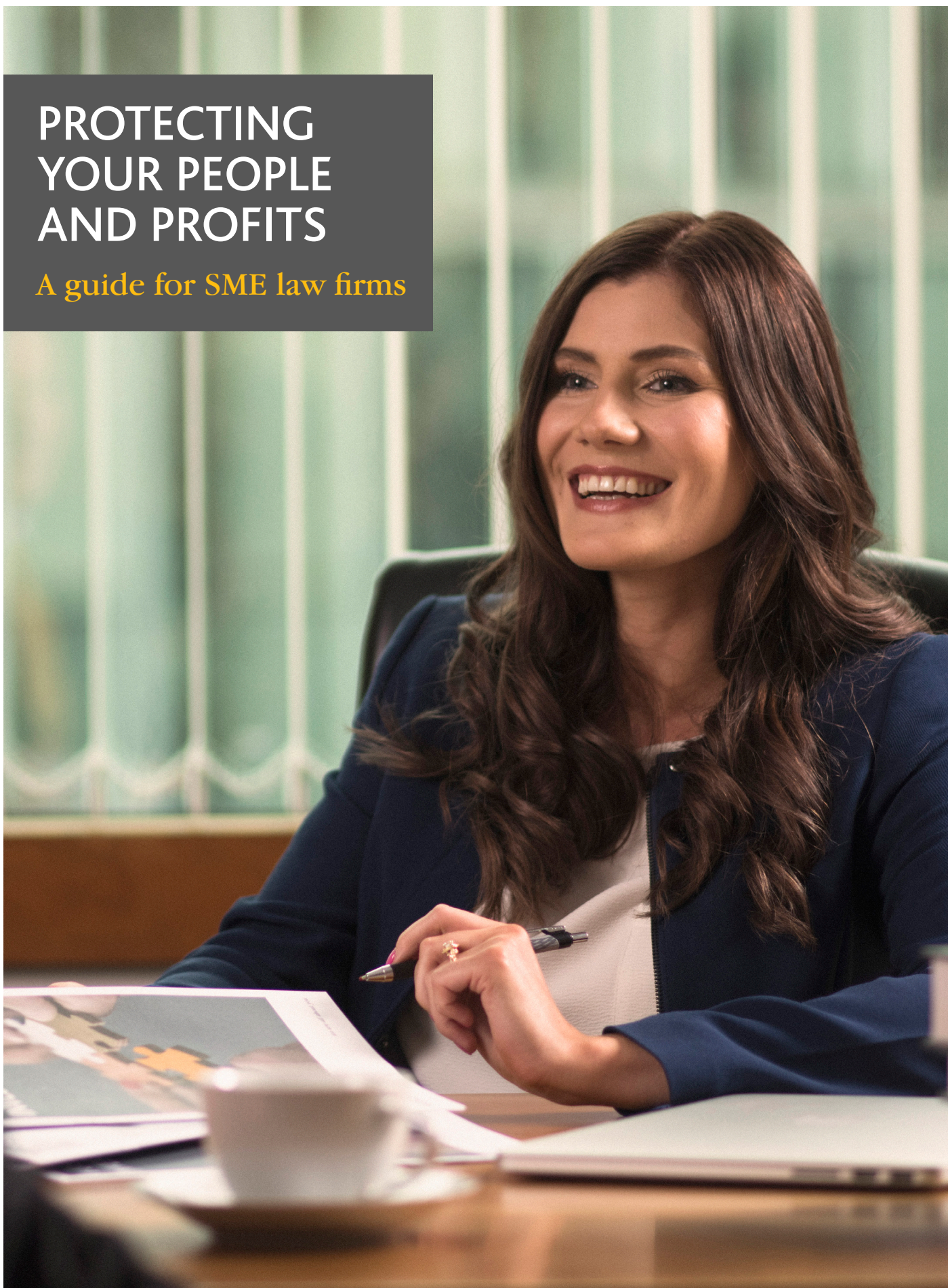


WESLEYAN

we are all about you

PROTECTING YOUR PEOPLE AND PROFITS

A guide for SME law firms



Key to any successful SME law firm, is stability. The ramifications of losing a partner or key person may disrupt a firm beyond the difficulties of recruiting an appropriate replacement. It could affect business continuity, staff morale and disrupt client relationships. In addition, a firm could lose a technical or knowledge skillset that is difficult to replace. Finally, there may be cash flow and other financial difficulties to navigate if a fee earner is unable to continue working.

This guide will help you to:

- ▶ understand the potential financial and functional impact of losing a key person
- ▶ discover how your business could compensate for the impact of lost income, should a key person be unable to work
- ▶ think about your firm's business continuity and succession plans
- ▶ evidence your continuing competence in line with the Solicitors Regulation Authority requirements in demonstrating *"an adequate understanding of the commercial, organisational and financial context in which you work and your role in it."*

Introduction

As individuals, we all have varying levels of protection in place. For example, house and car insurance to protect our property, and critical illness/mortgage protection to protect our financial futures. We also protect our immediate finances through cover such as income protection and our future finances through retirement planning and pension contributions.

The same protection needs apply to the majority of SME law firms. The physical assets to protect include commercial property, company vehicles and people, in the form of personal liability. Less tangible, but equally as important to protect, are your firm's profits and ownership.

What are the consequences and considerations if a key person, or fee earner, within your firm is unable to work? Do you have adequate protection in place to mitigate against the risks of this?

"Losing a key team member can have a serious impact on your ability to continue operating, and even be fatal to a firm's future."

Management Today, January 2016

We've identified four essential steps to protect your people and profits:

1

IDENTIFY THE RISKS

2

UNDERSTAND THE BUSINESS AND PERSONAL IMPACT OF A KEY PERSON (INCLUDING A PARTNER) BECOMING UNABLE TO WORK

3

CONSIDER HOW THE DEATH OF A PARTNER COULD IMPACT YOUR BUSINESS

4

CONSIDER WHETHER YOUR LAW FIRM AND IT'S PEOPLE HAVE ADEQUATE PROTECTION IN PLACE

1

IDENTIFY THE RISKS

The success of any firm hinges on its people. Take a managing partner or key employee out of the equation and profitability, or even the ability to maintain business as usual, can be seriously affected.

A key step in business continuity planning is to identify the people whose absence would seriously disrupt day to day operations. This isn't as straightforward as just protecting law firm partners, it's recognising any key person, relationship manager or significant fee earner. Think about the people in your law firm and consider whether they're:

- ▶ the single point of dependency for any specialist skills or knowledge your firm needs
- ▶ heading up a team or department
- ▶ the key contact for an important client relationship
- ▶ a significant fee earner.



Consider the risk of absence to your law firm

No business is free from this risk, because no individual is free from the possibility of ill health. In a February 2017 survey of Junior Lawyers, 55% of respondents admitted to feeling 'unable to cope as a result of stress' in the last month*. And in 2015, more than a third (34%) of income protection claims paid by Wesleyan were as a result of mental ill-health.

2

UNDERSTAND THE BUSINESS AND PERSONAL IMPACT OF A KEY PERSON (INCLUDING A PARTNER) BECOMING UNABLE TO WORK

If your firm was in the situation where a key person or linchpin employee couldn't work due to illness or injury, it's important to understand what the immediate and long-term business ramifications might be.

Imagine a scenario in which the key person is one of the top profit generators in a law firm. They are responsible for bringing in 50% of the firm's revenue and they manage valuable relationships with a number of the firm's key clients. On top of this, the firm has recently taken a loan based on its business performance before the loss of this key person.

Given the potential attributes of the key person, their loss could have a significant impact on the business.

For example, profits drop with the loss of income they used to generate. The firm's relationships with key clients are disrupted. A suitable replacement is sought and their remuneration package is higher as they have to be bought in at short notice, and on a temporary basis. In addition, the management team have to spend more time in the business to maintain client relationships, manage the key person's workload and recruit their replacement. Finally, the firm has difficulty maintaining the loan repayments and other liabilities due to the disruption to cash flow.

Mitigating the impact of losing a key person

Consider **key person insurance** to protect your law firm against the impact of sickness-related absences (or even death). The benefits could safeguard your profits, cover costs of hiring a locum and help towards paying the fixed costs of your business.

The impact on an individual who is unable to work can also be significant

For instance, if an individual is unable to work through illness, employer and/or government sick pay may not be enough to meet their day-to-day living costs, household bills, rent or mortgage payments. This could lead to a drop in lifestyle quality, and affect their ability to afford things like holidays, cars, entertainment and school fees. Consequently, the family/individual may have to rely on their savings to fill the financial gap, which are likely to diminish quickly. As the individual is unable to work, savings can't be replenished, potentially putting the family home in jeopardy.



Protecting your employees

Consider offering an **employee income protection plan**, which will replace some of the individual's earnings, until they're well enough to return to work.

Wesleyan's Employee Income Protection Plan is designed with legal practices in mind - meaning we can structure it to meet the specific needs of your firm.

You decide which employees you want to cover and in the event of a successful claim, we'll pay you an amount each month that replaces a proportion of their earnings, so that you can provide them with a continuing salary through your payroll.

You can also cover any National Insurance contributions you will have to continue paying as the employer. In some cases, you can also cover the pension contributions you make as the employer; safeguarding not just the employee's salary, but their retirement income too.

Offering income protection is also an attractive benefit to offer your current and future employees - helping you to stand out in a competitive marketplace.

3

CONSIDER HOW THE DEATH OF A PARTNER COULD IMPACT YOUR BUSINESS

Mortality is not something we normally like to think about. But as one of the business owners of your firm, you need to consider the possible implications of an unexpected death. For example, have you thought about:

- ▶ whether the deceased's next of kin would require a capital payment, rather than becoming a shareholder
- ▶ whether the remaining partners could afford to buy the deceased's share of the business
- ▶ whether the deceased's next of kin would want to play an active part in running the business if they became a shareholder (and can they add value to the day-to-day operations)
- ▶ how much extra time the remaining partners might have to invest in the business to compensate for the loss of income and work that was previously performed by the deceased.

The potential impact of a partners death

Imagine a scenario in which three shareholding partners have invested significant time and money in a law firm and are benefitting from its continued growth. Unfortunately, one partner dies unexpectedly. The remaining partners are able to continue, although at a reduced turnover. The next of kin of the deceased however, has no interest in the business and no skill to contribute to it's operation, but is entitled to the shares of the deceased.

In this example, the death of a partner could have a significant impact on the business

The remaining partners cannot afford to buy out the third share. It could be offered out to a third party (if one can be found). In the meantime, the deceased's next of kin could start pushing for a higher percentage of profits to be paid out to support their income. Whilst the remaining partners have to put more time into the firm to cover the work of the deceased.



The solution for the business

The principal solution would be to ensure that a **partnership protection policy** is in place as part of your partnership agreement.

Following the death of an insured partner, their share of the practice would become part of their estate and pass to their beneficiaries. With partnership protection in place, the remaining partners are able to collect a lump sum, giving them the opportunity to buy the third share from the beneficiaries of the deceased (should they want to sell). The inherited shares could be sold to any third party but with the right protection policy, a law firm has the money to retain the shares so current ownership can continue.

4

CONSIDER WHETHER YOUR LAW FIRM AND IT'S PEOPLE HAVE ADEQUATE PROTECTION IN PLACE

Having outlined a few scenarios and possible solutions, you will understand some of the protection options available, however, no two situations are exactly the same:

- ▶ As a firm you may already have a plan in place to compensate for a critical illness or the absence of a key person.
- ▶ You might already have some idea of what happens to partners' shares should they die.
- ▶ Partners may have left a will regarding their share of the business.
- ▶ You may not have discussed your appetite for risk as a firm yet.



Whether you already have some form of plan and protection in place, or none at all, it's a good idea to have a no-obligation review with one of our expert advisors. Together, with our legal specialism, risk management experience, continued claims support and flexible funding we can ensure your people and profits are protected to a level you're comfortable with.

We can help you plan

Arrange a financial review quoting 51018



financialreview@wesleyan.co.uk



0800 294 9052

(Lines are open 8am-8pm, Monday-Thursday - 8am-5pm Friday).

The information contained in this article does not constitute financial advice.

*Junior Lawyer Division (JLD) Survey, February 2017

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It is integral to how we think about our business and the way we look after our members, customers and our communities.

We believe mutuality has many advantages. It allows us to put our members and customers at the heart of all we do – rather than shareholders and the need to maximise short term profit – meaning we are able to focus on what’s right for those who invest in our business. Not just for today, but for the long term.

For over 175 years our mutual status has served us well, and we have no doubt it will continue to do so for many years to come.

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