Clean House or Bleak Future
Considerations Post LASPO

Part I

Two hundred smaller law firms folded during the third quarter of this year, or roughly two percent of all firms. Should this rate continue there would be few if any law firms in existence within a decade. This will not be the case, but it is becoming more and more obvious that there will be far fewer legal firms operating within a relatively short period.

The SRA has identified approximately twelve hundred firms that are at risk of insolvency and it would appear that there are about fifteen percent of these under intense monitoring. This problem is not just a manifestation of firm size, as more than ten percent of these are from among the top two hundred. Is it coincidental that this is occurring in the wake of LASPO or Legal Aid, Sentencing and Punishment of Offenders Act 2012? This Act dealt with three distinct areas: 1) legal aid, 2) litigation funding and costs and 3) sentencing and punishment.

It was argued by the Government that it was necessary to reduce spending on both criminal and civil legal aid. The expectation is that the measures will cut £200m from the annual £2 bn. legal aid bill. Legal aid was intended, as a matter of policy, to help as many people as possible (subject to eligibility requirements) and, in theory at least, provided help for a range of legal problems, but has turned out to be unsustainably expensive. It was theoretically available for a range of civil legal problems, providing a means for people to pursue legal action where the costs involved would otherwise prevent them from doing so. As an element of social policy, legal aid was intended to be made available only to those who needed such funding. A potential claimant would have their claim assessed according to both the merits of the claim and means testing so that the assessment would consider the reasonableness of their claim and their level of disposable income; to receive funding, a claimant would have to pass both these tests. Legal Aid has been abolished for personal injury claims leaving impecunious litigants with meritorious claims with fewer alternatives.

Over the past two decades, litigants who were ineligible for legal aid typically made CFA arrangements with their solicitors, especially with regard to personal injury claims. However, under the terms of the Conditional Fee Order 2013 the client, not the defendant, must pay the success fees ("the uplift") and any after-the-event premium from their damages (with a few exceptions including insolvency). Additionally, under the provisions of LASPO, costs are now controlled and the success fee element of a CFA has been capped at 25% for personal injury claims.

The restrictions caused by these changes has caused progressive firms of lawyers running practices with a large personal injury or legal aid client base to seek alternative funding sources. However, the traditional source of funding, bank overdraft facilities, is no longer freely available for this type of lending. The question is why?

Tighter underwriting controls at banks uncovered the reality that many law firms have poor or no financial management structures in place. It is also an undeniable truth that when financial problems have become obvious there has been an inclination to bury the heads in the sand. Until recently, the SRA became involved only after firms became insolvent, but now it has taken on a greater degree of regulatory oversight. It is to be hoped that this measure will help to contain the problem, but of itself it can not eliminate it.

Legal firms that do not manage their cash-flow, monitor DBA and CFA income proportionality and have a strict claims quality control procedure in place are likely to enter stormy waters. Conversely, for those that do, there are alternatives that can ensure that not just the status quo is maintained but that the business is further developed.

Gearóid Ó Ceallaigh is Managing Director of Trusted Litigation Capital, a third party litigation fund that will open for business in the near future.