

ABS – ownership proposals now made clearer

On 4 May 2011 the Law Society issued their long awaited guidance note on Alternative Business Structures. You can find it at www.lawsociety.org.uk/productsandservices/practicenotes/abs/4966.article

The legal press has been full of stories about equity investment, floatations and the like. Let's be clear in saying that for the majority of law firms, this really is of very little interest. Firstly, providers of venture capital are only interested in investing where they can at worst double their money within five years, and you need an ongoing exit for that to happen. And anyone who has advised on flotations will know that even on AIM the costs are enormous, with no guarantee of raising significant amounts of cash.

All of this is mainly of relevance to the providers of scalable, commoditised services such as personal injury. So what about everyone else?

Key points are:

1. Ownership

- a) Pretty much anyone will be able to take an ownership stake. It will be up to the SRA to reject anyone they do not see as being 'fit'. They must not however be criminals, of violent disposition, bankrupts or have previous regulatory 'issues'. So the door is definitely wide open.

Whilst in some ways this is of course a threat as well as an opportunity, it does present some great tax planning opportunities for practices. An obvious one is for partners' spouses to take an ownership share, and hence an income share too. If you

do not fancy that, spouses can always take a share in a related services type company. This can save tax of £10,000+ per partner per year if you implement it correctly.

- b) All practices need to have at least one owner who is a qualified solicitor or an approved equivalent.
- c) Owners with shares of less than 10% are not subject to any form of approval process, so long as they cannot exert 'significant influence' over it. There does not seem to be guidance in respect of practices where all owners have a stake of less than 10%, and this will need clarifying pre 6 October.

2. The ABS itself must:

- a) be approved by the SRA
- b) have a practising address in England or Wales
- c) have approved PI insurance
- d) have two compliance officers, one of whom must be a solicitor (or equivalent) and a supervisor

The approval application is still being developed at the time of writing this note, and the application fee is not known either. There will be a suitability test as part of the process, and the SRA will have the sanction of refusal.

Continued overleaf..



So, why be an ABS/MDP?

This is a serious question, and needs serious thought within your practice. All sorts of amalgamations of activities are possible, so no one will be limited for choice. The main question for you to have certainty on is "what's the point".

Many legal practices are continuing to have a challenging time at the moment getting both income levels and profitability to where they need to be. In addition, succession planning is an added area of difficulty. Taking these things into account, the last thing many practices need right now is an overly time consuming, or worse still, failed ABS venture. Some points to be mindful of here are:

1. Some new ventures will have a high set up cost and overspending on initial promotional activity almost always happens. Work on a period of 2 years to breakeven and you might not then be disappointed.
2. Professionals (including Accountants, Estate Agents, Architects, and IFAs) do not have a strong track record of branching out into new areas. It is difficult.
3. If the creation of an ABS/MDP includes a merger with another type of organisation e.g. IFA, you need financial strength, strong discipline and clear leadership to make it work. Merging two weaker businesses only creates an even weaker one.
4. Do your homework on the effect of future conflicts of interest you might create with clients, introducers etc. This might be a significant risk in itself.
5. Really figure out what it is you are seeking to achieve. You are bound to be more skilful at your existing profession than integrating and running a new one.
6. Some new services may be both relatively straightforward to set up and more complimentary to your existing offering e.g. costing services.

There is no doubt that ABS/MDP represents an opportunity. It will just not be for everyone and needs very careful handling.

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