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Hazlewoods

Legal Focus

INSIDE

Latest on the SRA's consultation for protecting client money

Last December, the SRA released its consultation on 'protecting client money', with a closing date for responses of 20 February 2026. Last month, the SRA published the findings from the consultation, together with a list of changes that they plan to make, which includes the mandatory submission of Accountant's Reports for all non-exempt firms holding client money, and separation of COLP and COFA roles from unilateral decision makers.

Our thoughts on the announcements

At the time the consultation was released, the SRA had already identified a notable level of non-compliance with the existing rules – around 10% of firms inspected had failed to obtain an Accountant's Report. Against that backdrop, it is perhaps unsurprising that mandatory submission has now been introduced. More broadly, it reflects a shift towards greater visibility and earlier intervention, rather than relying on issues only coming to light when something has gone wrong.

One positive outcome is that the SRA has retained the current exemption thresholds. However, firms will now need to complete an annual declaration confirming whether they are exempt or have complied with the reporting requirements. While this is intended to strengthen accountability, it does introduce another administrative step, and the effectiveness of self-certification will depend on how robustly it is enforced in practice.

The requirement for reporting accountants to submit reports directly is another significant change. Although responsibility ultimately remains with the law firm, this does represent a shift in process. At Hazlewoods, we have always submitted reports on behalf of our clients, but the current mySRA process is far from straightforward. With many firms sharing common filing deadlines (typically September or October) this creates a bottleneck for larger accountancy firms handling multiple submissions, and equally a challenge for smaller firms that may be unfamiliar with the system.

In our consultation response, we highlighted the importance of making both the declaration and submission processes as simple and efficient as possible. Based on current systems, there is still some way to go.

The more debatable proposals relate to governance. The SRA is proceeding with the separation of COLP and COFA roles in higher-risk firms. We broadly supported this for larger practices where governance structures are more complex and the risks associated with concentration of responsibility are greater.

It is not entirely clear how or if the changes will impact firms. In a document published on the SRA's website last month, the SRA noted that "Our proposals offer flexibility for firms to choose how they respond to the new rules. We do not propose to set prescriptive criteria around the types of individuals who could not hold compliance roles under the new rules. It is up to firms to determine the impact of the rules in their particular circumstances. Nor are we prescribing how firms comply with the new rules. Firms can decide the best arrangements to suit their business. They can choose to reassign the compliance roles, or to adjust their governance structure, to change their arrangements for decision making. That approach could mean existing role holders remain eligible under the new rules."

The SRA has decided to use a turnover threshold of £600,000. To put this into context, during the 2024-2025 practising certificate renewal reporting timeframe, 3,525 firms (39%) operated with an annual turnover of more than £600k. This threshold would exclude a significant proportion of single owner practices, but there are still many firms who will exceed this threshold and struggle to separate the roles effectively. The role of COFA, with the risk attached, is unlikely to be appealing to an employee and if an employee did accept the position, would they be willing and able to contradict their boss if necessary?

It is reassuring, however, that the client money threshold has been increased to £2 million. The original £500,000 proposal would have captured the majority of smaller firms. For example, an individual conveyancer operating in London, where the average house price in London is £559,000-£661,000, could exceed the original threshold with just one transaction, or a private client lawyer could exceed £500,000 with just a couple of ongoing clients. In those scenarios, the cost of appointing an external COFA, which is often in the region of £5,000 per month, could easily exceed the fees generated.

The changes may mean that we see a whole new tranche of COFAs in the near future who will need guidance and support. We'll be offering it for our clients, but it will be interesting to see what (if any!) additional resources are going to be provided by the SRA.

And on to the next one...

On Friday 19 June, the SRA launched its next consultation linked to their focus on protecting client money held by solicitors:

Notifying the SRA of changes to help identify and act on risks.

As part of the Consumer Protection Review, the SRA identified the need for collecting different and more timely information from firms in certain circumstances to help spot and target risks. This need has been emphasised by the recent number of high-profile firm failures with significant sums of client money being stolen or lost.

The SRA decided that its immediate priority was to target three key areas from the November 2024 consultation that focused on strengthening protections for client money within the current system, in order to make a difference more quickly.

1. The SRA has already announced the requirement for all Accountant's Reports to be filed, as well as declarations for firms who are exempt, as a response to evidence that a proportion of firms were not obtaining Accountant's Reports as required
2. Again, an announcement has already been made with regard to separating the roles of COLP and COFA from those with unilateral decision-making abilities in larger law firms
3. Now the SRA has turned its attention to improving oversight of firms significantly changing their profile, including as a result of sales, mergers and acquisitions.

The SRA has stated that it is moving towards a more intelligence-led, proactive supervisory regulatory model, and that significant progress has been made in risk and data capability to help spot risks earlier and to increase capacity to respond to them. However, the SRA admits that more needs to be done to ensure there are strong data foundations, which will allow it to move from reactive to proactive regulation of the sector.

Firms are already required to notify the SRA of material changes to information previously provided. However, the SRA has admitted that, in practice, it is often not told of changes that may be considered material in the context of protecting client money at the time that they happen.

The SRA plans to introduce a broad rule requiring firms to notify it of certain events as and when they arise. Rather than provide a list of specific events now, the SRA wants to be able to change or introduce new events that will require a firm to make a notification, as well as when a notification would be required and the information needed.

For now, the SRA is proposing to prescribe two events which will require firms to:

- pre-notify the SRA of a merger or acquisition that has reached the Heads of Terms stage or equivalent; and
- notify the SRA when they begin to receive or hold client money, having previously reported that they do not do so at either authorisation or through the most recent practising certificate renewal.

Why is the SRA focusing on mergers and acquisitions? The consultation notes that a merger or acquisition can significantly change the risk profile of a firm, and describes potential risk scenarios that might arise, such as:

- Firms may acquire other firms in order to access large client account balances, and firms may adopt complex business and governance structures across a group that make it harder to spot illegitimate money transfers
- Firms expand into areas of law or adopt financing arrangements that incentivise high volumes of cases or rapid growth without sufficient regard to client outcomes
- Finally, risks arising from poorly executed change or expansion beyond a firm's capacity and capability. This includes, for example, inadequate systems, governance or expertise to support entry into new practice areas, or ineffective integration following an acquisition.

The proposal is that a merger or acquisition that is being contemplated and that has reached the Heads of Terms or equivalent stage is deemed a notifiable event. However, as the period between Heads of Terms being signed and completion can be variable, the SRA has suggested that it should be notified at least 30 days prior to the likely completion date for the merger or acquisition and as close to 30 days in advance as possible.

Information that the SRA will want to see includes:

- The names and turnover of both firms in discussions;
- The amount of client money held by both firms;
- Expected completion date;
- The number of acquisitions by both firms in the previous 24 months; and
- The planned structure of the merged firms.

It's important to note that in both events this is a notification only, i.e. the SRA is not suggesting that they should have to approve either an M&A event or the holding of client money.

Firms have until Monday 17 August to respond.

Meet the team – Harry Galpin

People are the essence of the Hazlewoods Legal team. In this section, we get to know more about Harry Galpin, Associate Director.

What drew you to Hazlewoods originally?

I was particularly drawn to Hazlewoods as they are sector specialists and highly regarded as advisors to the legal industry. The combined experience and knowledge within the team is staggering and I am looking forward to learning a great deal from my colleagues and working with high profile clients.

What is one thing that surprised you about working at Hazlewoods?

The firm is growing and expanding into new markets very quickly. It is inspiring how this has been achieved organically without shifting focus on the core values of the business.

What do you enjoy most about your role?

I enjoy building long lasting relationships with my clients so that I understand their commercial objectives and can ensure that our advice is suitably tailored.

I mostly focus on easing the tax burden for my clients so that they can focus on their busy lives.

What do you enjoy about the office locations?

Each office is unique and very easy to travel to. As I live a 20-minute walk away from our Cardiff office, it is great to be local to the market and I am always available to see clients face to face whether for a formal meeting or a coffee.

What is the best advice you can give to someone just starting out in their career?

Not to worry if you make a mistake, it is how you learn.

What should clients be currently thinking?

There is cash pressure being felt across the sector, driven in part by the ongoing impact of basis period reform, capital investment requirements, salary and employer NIC increases as well as a downturn in transactions. Firms need to be aware of the potential impact and consider if they require additional funding, either externally or via partner capital calls.

I am also keeping an eye on the Interest on Lawyers' Client Accounts Scheme (ILCA) consultation. In recent years, some firms have earned significant interest from such sources and the proposals should therefore be considered in any forward planning.

What is the best career lesson you have learned so far?

Tackle the difficult job first thing in the morning.

Can you share any insights regarding the current legal sector?

If you operate as an LLP it is important to be aware that the salaried member rules remain an area of interest for HMRC. Firms should ensure they review and document the conditions annually to ensure compliance or seek advice if needed.

Separately, if a firm is required to pay the economic crime levy, it is important to note that this is not a tax deductible expense, with legislation specifically stipulating this. As this feels somewhat contrary to the usual 'wholly and exclusively' rules, it is worth a reminder to check compliance.

What would you do (career-wise) if you were not in this current job?

I wanted to be a professional cricketer, but would more likely have been a PE teacher.

What do you like doing in your spare time?

I am a Charlton Athletic fan... which brings me joy about once every 5 years.

Do you have significant influence?

To most members of an LLP, the answer to this would be a simple yes.

You may be a significant fee earner, maintain complex budgets or contribute substantially to marketing. This enables the business to succeed and demonstrates your influence internally to the firm.

HMRC, on the other hand, will now use the Supreme Court's decision in BlueCrest Capital Management (UK) LLP v HMRC to decide if there is 'significant influence' when applying the Salaried Member Rules.

Salaried Member Rules

The Salaried Member Rules allow HMRC to determine whether an LLP member is truly self-employed rather than trying to disguise employment to benefit their tax position.

If you meet all the following conditions you will be treated as an employee:

- **Condition A (Disguised Salary):** It is reasonable to expect that at least 80% of the amount payable to the member is fixed or does not vary with the overall profits or losses of the LLP
- **Condition B (No Significant Influence):** The member does not have significant, managerial influence over the affairs of the LLP as a whole
- **Condition C (Low Capital Contribution):** The member's actual capital contribution to the LLP is less than 25% of the "disguised salary" they are expected to receive in that tax year.

So, to be treated as a self-employed taxpayer you must fail one of the conditions above.

Many firms fail condition C by asking their partners to contribute at least 25% of their profit share as capital. In general, this is the easiest and most formulaic of the conditions to fail.

Significant influence

The court's approach in BlueCrest provides updated guidance on what the significant influence detailed in Condition B is.

It is not achieved through being a commercially important individual to the success of the LLP. Instead it should be decided by a close examination of the LLP agreement to establish the main source of a member's influence.

This is because the relevant influence must derive from an individual's rights and duties as a member, as opposed to de facto influence existing outside the statutory and contractual framework of the LLP.

What now

In many traditional law firms the partners contribute sufficient levels of capital to fail Condition C. The firm may also operate a points-based profit-sharing model by reference to overall profitability of the LLP, which would mean condition A is also failed. BlueCrest therefore has no impact.

If, however, partners are relying on failing condition B, it is important to ensure that significant influence is still being met by ensuring that:

a) their rights and duties as a member are clearly set out in the partnership agreement

b) the member has real-world influence over the affairs of the entire LLP at the highest level

c) The rights and duties are exercised in practice with clear evidence being maintained should HMRC ever require evidence.

As a reminder, it is recommended that partnership structures should be reviewed on a proactive basis and timely basis especially given HMRC's renewed interest in this area of taxation.

HMRC propose changes in how law firm partners will pay tax

At the 2025 Autumn Budget, the Government announced changes to the timing of Income Tax Self-Assessment (ITSA) payments for one group of taxpayers.

From April 2029, HMRC will require ITSA taxpayers with sufficient PAYE income to make ITSA payments through PAYE each payday — likely divided into equal payments through the year.

The Government has recently also issued a consultation on the potential for other groups of ITSA taxpayers, such as self-employed law firm partners, to make tax payments more regularly throughout the year, closer to the point at which taxable activity takes place.

Many OECD countries, including Canada, France, and Australia, already operate systems where tax is paid much closer to the point of earning and HMRC are now focused on earlier collection of tax, which is not a surprise when looking at the road map they set out through Making Tax Digital.

The proposal

The Government is looking to make the change to more frequent payments – either quarterly or even monthly – from April 2029. The payments that will be made will be based upon an individual's tax liability for 2027/28 albeit allowing for adjustment to be made if income is expected to be lower, just in the same way as payments on account can be reduced now if required.

The impact for law firms

In the year of change, law firms will be paying on account of their tax for 2028/29 in January 2029 and July 2029 in addition to making payments on account for 2029/30 starting from April 2029. This will effectively accelerate the outflow of cash from the practice.

The Government has recognised this and the consultation suggests that there may be some transitional support in terms of allowing firms a longer period of time in the first period to deal with this. It may be similar to when Basis Period Reform came in in 2023/24 in that firms could elect to deal with the acceleration of tax payments over a maximum of five years which will just finish when the new system comes in! It is probably unlikely that the Government will be as generous this time.

Key challenges

We would expect to see a number of challenges to firms if these proposals are implemented:

- Firms will need to revisit how they reserve for tax to minimise the cash flow pressure of having to make more regular payments. This could also impact the timing of drawings being made to partners
- The impact on working capital would need to be considered to mitigate against any risk that this may pose to the operation of the wider business. A renewed focus on lock up and early invoice raising and collection should be considered
- Firms who borrow to fund tax liabilities may need to consider the timing of payments under the old system for payments on account and how that will interact with the new system. This may be the time to step back and review the whole structure of funding within the practice to ensure it is fit for purpose in the medium term
- Internal finance teams may face pressure to model tax liabilities more regularly and compliance costs will likely increase.

The consultation ends on 4 August.

Conclusion

The Government is seeking to modernise the tax system, helping individuals manage liabilities more effectively while reducing debt and improving compliance. As stated, there is clearly an ambition by HMRC to start collecting tax earlier and reduce the risk of default.

Some ITSA taxpayers are already experiencing change in relation to reporting income and expenses through Making Tax Digital (MTD), which seeks to move record keeping closer to real time. It is noted, however, that MTD still does not have a confirmed mandatory start date for law firm partners, and it will be interesting to see how these proposals may change this.

As we saw with Basis Period Reform, the impact could be significant if firms fail to plan well ahead for any change.

Intro to Hazlewoods OMB Tax team

Our owner-managed business (OMB) Tax team, led by Gemma Read, Tax Partner, provides a comprehensive range of tax compliance and advisory services to privately owned businesses. The team advises a diverse client base, from sole traders and property investors to larger corporate groups and their shareholders.

The team manages the full spectrum of tax compliance requirements across corporate, partnership and sole trader structures. Alongside core company and partnership tax return filings and payments, the team supports clients with the reporting of employee taxable benefits and employee share transactions.

The team also handles tax compliance for a large number of investment companies, with specialist expertise in the taxation of stocks and shares portfolios and cryptocurrency investments.

For business owners, the team prepares annual personal tax returns and assists clients with capital gains tax filings for the disposal of property, shares, and other assets.

Key compliance topics for owner-managed businesses

Making Tax Digital (MTD)
The introduction of MTD for Income Tax represents a fundamental shift for sole traders and property investors, with quarterly digital reporting of income and expenses being phased in over the next three years. For those mandated for the 2026/27 tax year, the first quarterly returns must be filed by 7 August 2026. MTD places greater emphasis on accurate, real-time record-keeping and the team is supporting clients with quarterly submissions, helping them implement appropriate bookkeeping systems, and providing advice on software.

Payrolling of benefits in kind (BIKs)
From April 2027, payrolling will become mandatory for car, van, fuel, and medical benefits provided to employees. Other benefits in kind will come within scope from April 2028. Whilst this should streamline year-end compliance, it requires robust payroll processes and accurate valuation of benefits throughout the year. The team is supporting clients in preparing systems and processes ahead of the transition.

HMRC enquiries and disclosures
HMRC continues to take a more proactive approach to compliance, with increased enquiry activity supported by the growing use of third party data. The team manages all correspondence with HMRC on behalf of clients, ensuring enquiries are handled efficiently and robustly. Where historic issues are identified, the team also supports clients with voluntary disclosures, helping them regularise their position and minimise potential penalties.

Increasing compliance demands
Reporting obligations continue to expand, with the introduction in 2025/26 of a requirement for company directors to report more detailed information relating to their shareholdings, including any dividend income they receive from those companies.

In addition to these new reporting requirements, HMRC have recently published a consultation on requiring companies to provide them with details of transactions with their shareholders, which could include cash withdrawals, loans, dividends and other distributions. The proposals, if implemented would further increase the compliance burden for owner-managed companies.

OMB tax advisory

Gemma and her team advise clients throughout the business lifecycle, from the initial structuring of new ventures through to expansion, succession planning and pre-sale structuring.

Recent projects have included:

- Advising on the transfer of a property investment business from an LLP structure to a limited company
- Implementing a holding company structure to support a client's growth strategy and future acquisitions
- Advising an incoming shareholder on a management buy-out structure, including liaising with HMRC to obtain advance clearance and undertaking remuneration planning, to ensure tax efficient extraction of profits from the company
- Advising on a demerger to separate two businesses within a company, following a shareholder dispute
- Advising on the establishment of a family investment company as a strategy for passing wealth down the generations in a controlled and tax efficient manner, including ongoing support with tax compliance obligations for the company and family shareholders.

Key advisory topics for owner-managed businesses

Rising tax costs and profit extraction complexity
Higher CGT rates and a less generous BADR regime make early, proactive planning increasingly important, particularly ahead of a sale. At the same time, changes to dividend taxation, income tax thresholds and National Insurance have made profit extraction more complex, requiring careful balancing of tax efficiency and cash flow needs.

Greater HMRC scrutiny of restructuring
The November 2025 Budget introduced a more rigorous approach to pre-transaction clearances, meaning that individual steps within certain transactions may now be challenged, even where the overall commercial rationale is clear. This places greater emphasis on early planning, robust documentation and clear commercial justification.

Inheritance tax (IHT) changes for business assets
100% relief from IHT for business assets such as shares in a trading company is now restricted to the first £2.5m of qualifying assets per individual. For some business owners this has resulted in increased exposure to IHT, reinforcing the need for proactive and structured planning.

Attracting and retaining talent tax-efficiently
Businesses are looking at ways to incentivise key employees, including tax-efficient benefits, share schemes, and bonuses. Whilst there are many options available, careful structuring is required to ensure that there are no unintended tax consequences and that any associated HMRC reporting is accurate and timely.

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