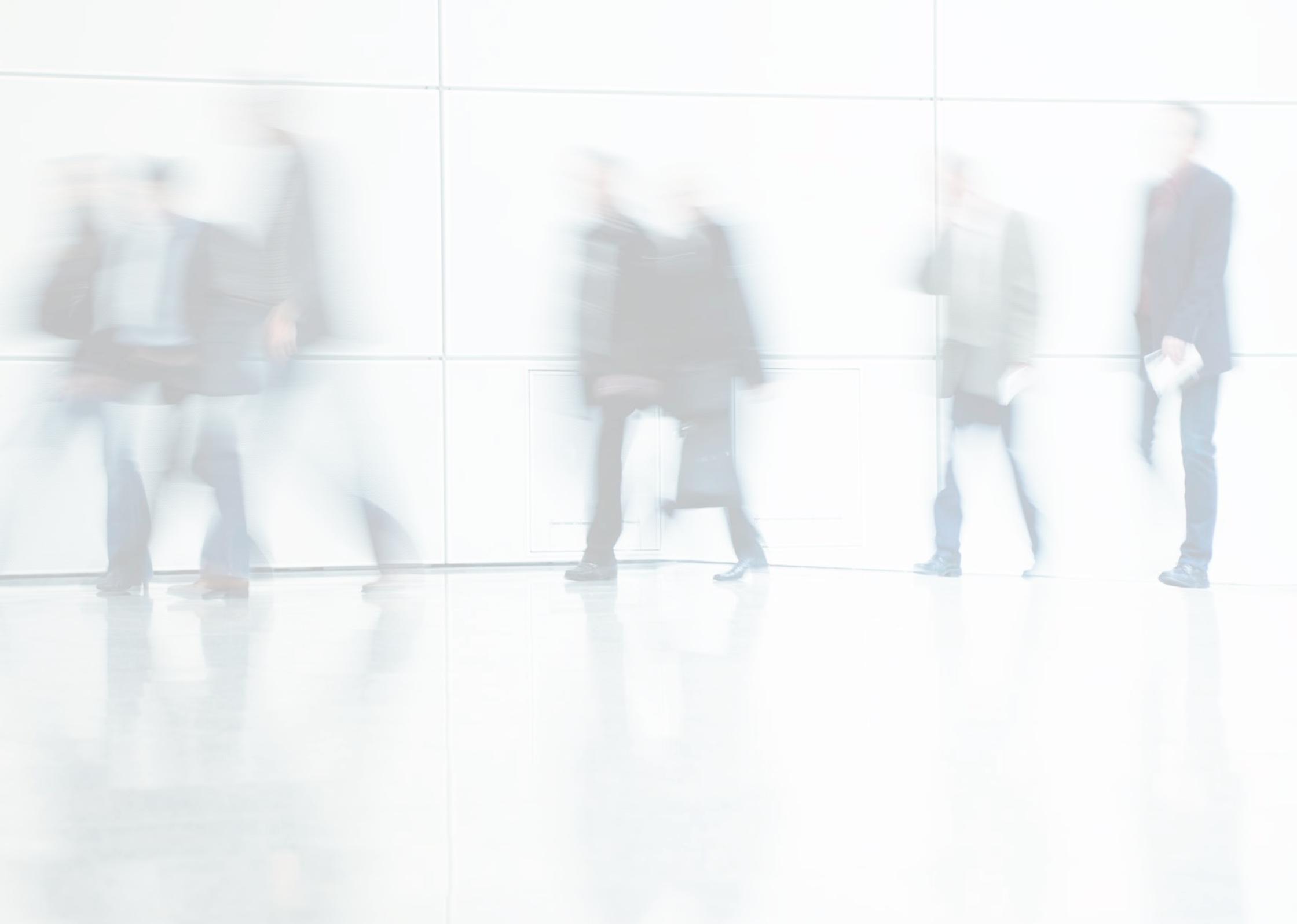




REPORT 1: BDO LAW FIRM LEADERSHIP SERIES 2017

MANAGING RAPID CHANGE

THE SCOTTISH PERSPECTIVE



INTRODUCTION



MARTIN GILL
LEAD PARTNER
BDO SCOTLAND

Law firm leaders agree that the pace of change in the legal industry is accelerating, yet many firms continue to provide legal services in the same way they have done for decades. Others are adopting more corporate structures, diversifying their service offering, innovating with

technology, and experimenting with new ways to provide better value and efficiency to their clients.

In BDO's 2016 survey of Scottish independent law firms*, certain key areas of change were identified by respondents including increased consolidation in the Scottish legal market, the need to invest in technology and the likelihood that the staff to partner ratio would increase.

Many of the findings remain consistent with the results of this survey whilst some differ significantly from the responses of firms outside of Scotland. Ultimately, it is the responsibility of law firm leaders to drive the internal changes needed to respond to challenging external market forces.

One law firm leader brilliantly quoted Bill Gates to sum up why firms needed to take the longer term view:

“We always overestimate the change that will occur in the next two years and underestimate the change that will occur in the next ten. Don't let yourself be lulled into inaction.”

Our research shows that technology is expected to have the greatest impact on law firms over the next five years. Technology has had a significant impact on all business and the professional services sector is not immune to this.

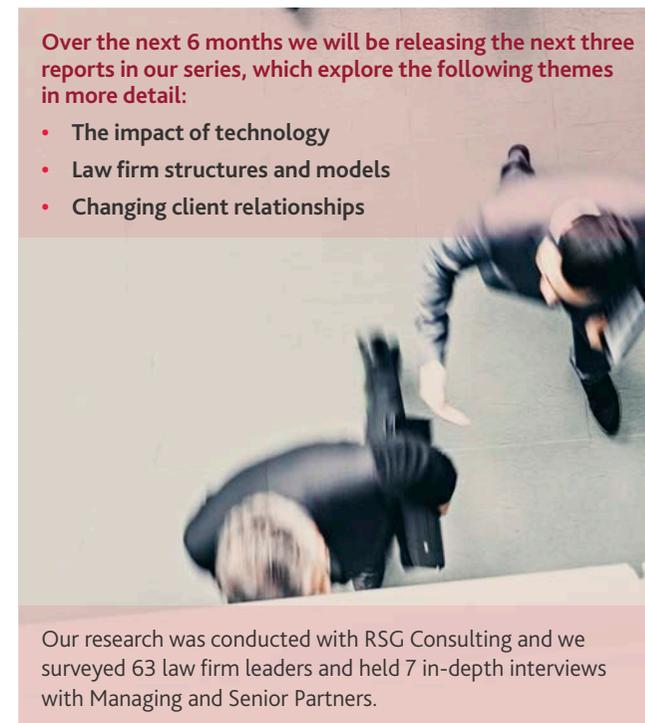
Law firms have adapted through the years to use technology to facilitate better client delivery and this will continue to be the main driver going forward. One of the main challenges of technology today is how to fund the investment in order to keep as up to date as your competitors.

A key decision is whether you want to be a leader in this field or a fast follower. Then the follow on question is how you bridge the funding gap.

Law firm leaders will need to consider what they want their firms to achieve and choose a course to reach their goal. The ability to be nimble to change direction is critically important and changing too late could spell disaster in terms of loss of competitive advantage.

Over the next 6 months we will be releasing the next three reports in our series, which explore the following themes in more detail:

- The impact of technology
- Law firm structures and models
- Changing client relationships



Our research was conducted with RSG Consulting and we surveyed 63 law firm leaders and held 7 in-depth interviews with Managing and Senior Partners.

THE PACE OF CHANGE IS ACCELERATING SIGNIFICANTLY

LEADER
GLOBAL LAW FIRM

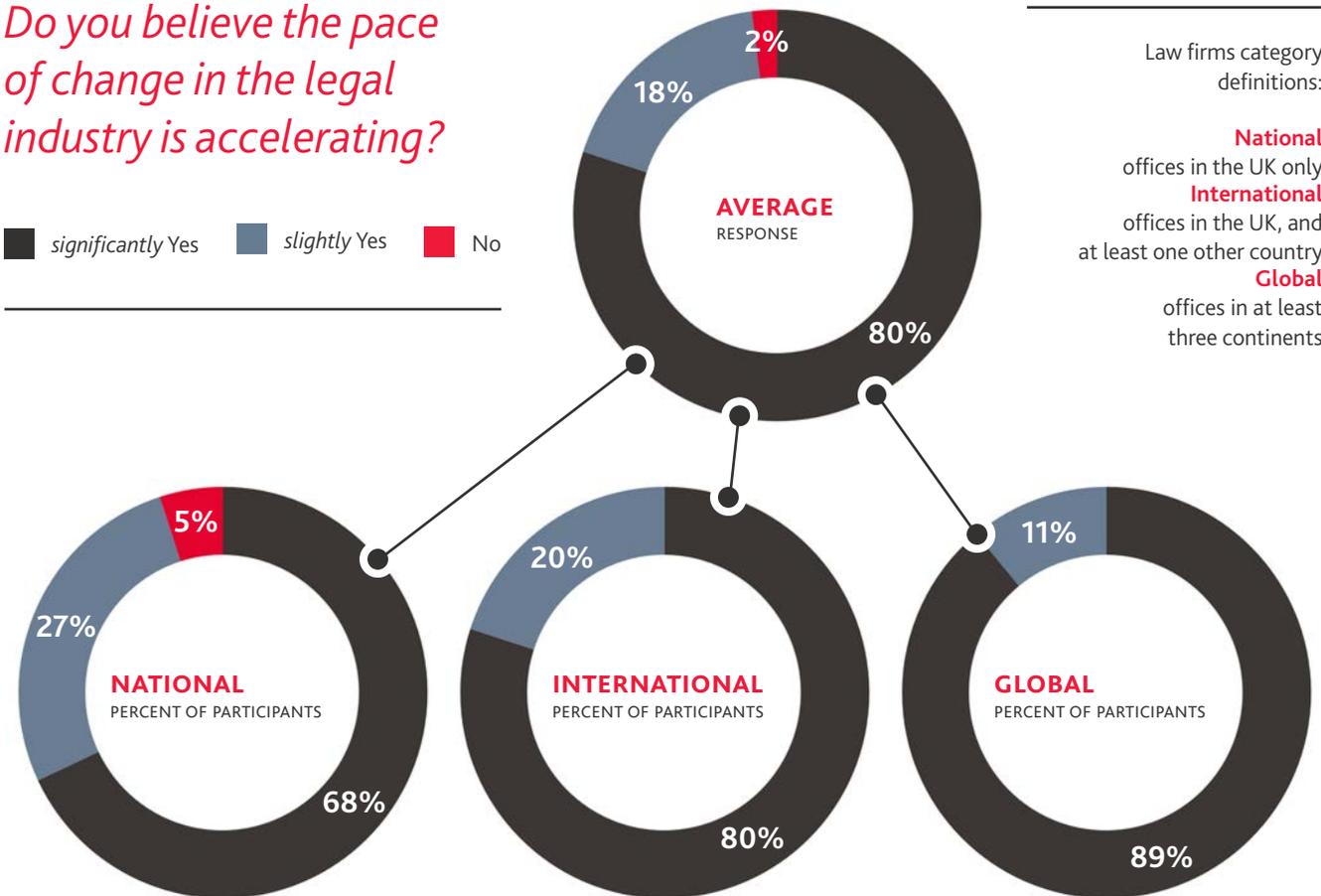
“Ten years ago, law firm managing partners would have said that law firms would largely stay the same. That’s completely changed.”

The almost unanimous view from 98% of the law firm leaders surveyed is that the pace of change in the legal industry is accelerating. Four out of five believe it is accelerating significantly. We are at a tipping point for the global legal industry, said one law firm leader, and there is more urgency for change than ever before.

Global law firm leaders were more likely to describe the pace of change as accelerating significantly (89%) than those at international law firms (80%), while national law firm leaders were the least likely (68%).

Do you believe the pace of change in the legal industry is accelerating?

■ significantly Yes ■ slightly Yes ■ No



Law firms category definitions:

National
offices in the UK only
International
offices in the UK, and at least one other country
Global
offices in at least three continents

TECHNOLOGY WILL HAVE THE GREATEST IMPACT ON LAW FIRMS OVER THE NEXT FIVE YEARS

LEADER
GLOBAL LAW FIRM

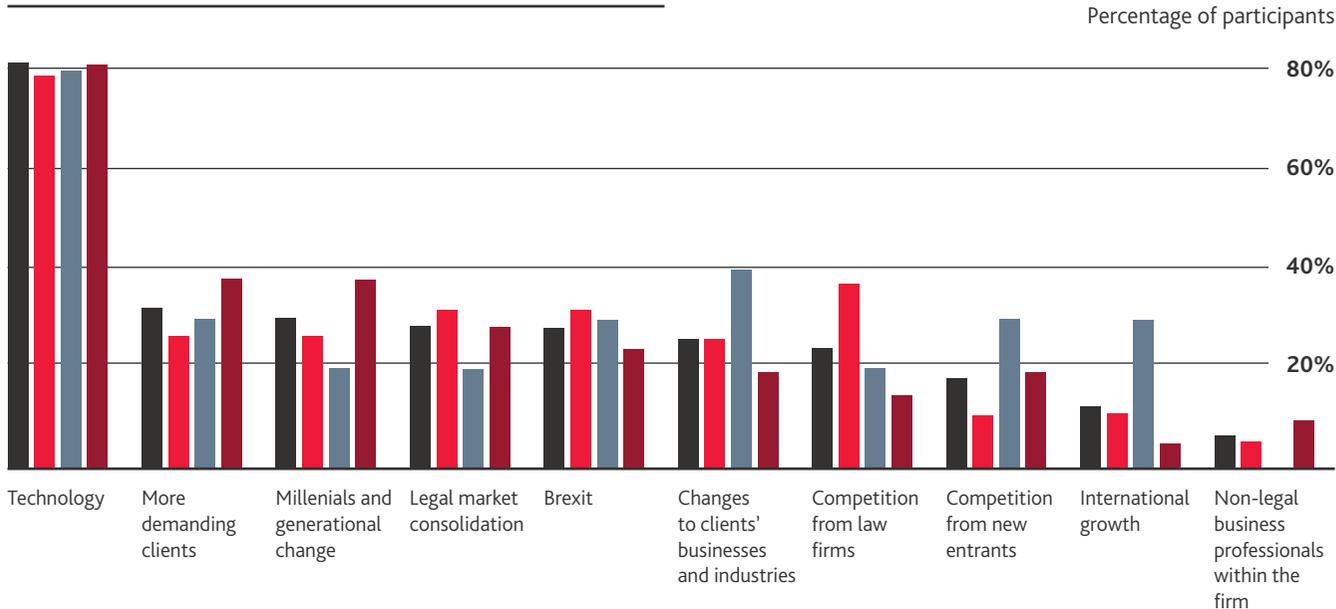
“Technology has been changing the world for a long time. Why should law be any different?”

The pace of technological change has increased rapidly across industries. While law firms have been slow adopters in the past, an explosion of legal technology start-ups has quickly made a range of technologies more relevant and available. Approximately four-fifths of participants from global, international and national law firms pointed to technology as the factor most likely to have the greatest impact on their firms over the next five years. Overall, and within every geographic group, participants were at least twice as likely to select technology as any other single factor.

After technology, leaders named different factors depending on the geographic profile of their firms. Global firm leaders were most likely to say competition from other law firms would have the greatest impact. International firm leaders pointed to changes to clients' businesses and industries, while national firm leaders were more likely to say more demanding clients and millennials and generational change would have the greatest impact.

Which of the following do you believe will have the greatest impact on your firm over the next five years?

■ All Firms ■ Global ■ International ■ National



MANY FACTORS WILL TRANSFORM LAW FIRMS



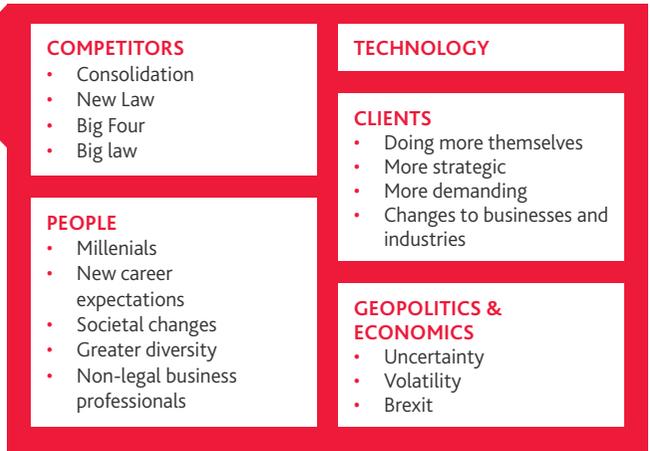
While it was the most frequent response, technology is not at the top of every law firm leader's agenda. Just as important for many are changes to their clients, legal and economic markets, and their people. Survey respondents and interviewees pointed to a wide range of factors which would drive change at their firms over the next five or ten years.

Clients

Increased competition from in-house legal teams as they grow, hire and develop greater expertise, handle higher level and more strategic work themselves, and use technology to automate routine legal tasks will have a direct impact on large law firms. Leaders say that continued demand for ever more efficient legal services and greater value is forcing them to find ever new ways to resource and deliver legal services, and consider offering a wider range of legal and ancillary services.

Competitors

Big law firms were singled out for their potential to impact the market as first movers. "They have the best ability to reengineer legal services." As increased use of technology and automation make law firms more capital intensive businesses, scale is important. Law firm leaders expect to see continued consolidation in the mid-market, and strong competition from new entrants and the Big Four accounting firms.



People

People in law firms increasingly want to work differently, with more flexibility, control, and in more varied careers. Societal and generational changes impact how they will expect to be able to work in the future. Technology is an important driver and enabler of these changes. As firms respond to societal changes and business arguments to hire lawyers from different socio-economic, national, and educational backgrounds and address gender inequality, the make-up of the firm will be more diverse and draw on a wider and stronger talent pool.

Few said non-legal professionals within law firms would have the greatest impact on their firm over the next five years. However, they are expected to play an increasingly important role in changing how legal services are developed and delivered.

Geopolitics and economics

The most important factor for some law firm leaders is the political and economic uncertainty facing the globe. As one said, "It is difficult for clients to set their strategies, and we follow our clients."

Law firm leaders predict greater volatility and less certainty in global markets, which will impact their clients' deal activity and businesses. One described it as being "on iceberg watch."

Brexit

Brexit was the fifth most frequent response to the question of what would have the greatest impact on law firms. While some believe lawyers will benefit from a temporary uptick in regulatory work as regimes and rules change, more are pessimistic about potential long term impacts on workflows. Most concerns were around uncertainty and the potential impact on the financial industry.

Brexit concerns

- How will it impact clients and City of London's standing as an international financial and professional services centre?
- How will it impact London's role as a legal and disputes centre if judgements are not automatically enforceable in the EU?
- Will international law firms headquartered in the UK be able to continue to operate in other EU jurisdictions on the same basis as they can now?
- Will data protection laws allow firms to keep employee records for European staff in their UK headquarters?
- Will it impact firms' ability to employ talented EU nationals in their UK offices?

HOW DO LAW FIRM LEADERS ENSURE THEIR FIRMS ARE AGILE AND ADAPTABLE ENOUGH TO MEET CHANGE?

Asked what the most important factor was in ensuring their firms were agile and adaptable enough to meet change, the six factors most mentioned, in descending order were:

1. Culture & mindset

2. Leadership

3. People & skills

4. Understanding client needs

5. Technology

6. Structure

Two-fifths of the leaders surveyed said that the right culture and mindset would allow them to adapt and would underpin their firm's success. Creating the right culture and fostering an open mindset was also described as the most difficult challenge for law firm leaders. One found it more effective to talk about "professionalisation, evolution or modernisation, rather than change". Importantly, a strong culture also protects law firms from losing talented lawyers in a market that continues to see a great deal of lateral movement by partners.



"It's important to make culture part of the client agenda. Partners see it as important if you can show how clients care about it."

Law firm leaders described the culture and mindset they needed in the following ways:

THINKING DIFFERENTLY | OPEN MINDEDNESS |
 PREPAREDNESS TO CHANGE | RECOGNITION OF
 THE NEED TO CHANGE AND ADAPT FROM THE TOP |
 WILLINGNESS TO EMBRACE CHANGE |
 BEING OPEN TO CHANGE | ACCEPTING THE NEED
 TO CHANGE AND STAY AHEAD OF THE CURVE |
 GLOBAL MINDSET | CAN-DO ATTITUDE | DYNAMIC
 | ADAPTABLE | EXTERNALLY-FOCUSED | FLEXIBLE
 | WILLING TO INNOVATE | OPEN MINDED |
 EMBRACING OF INNOVATION IN ALL ITS FORMS
 | NON-INSTITUTIONAL | OUTWARD-LOOKING |
 UNCOMPLACENT | A HIGH PERFORMANCE CULTURE
 COMBINED WITH REALISTIC PARANOIA |
 FLUID AND EVOLVING

HOW DO LAW FIRM LEADERS ENSURE THEIR FIRMS ARE AGILE AND ADAPTABLE ENOUGH TO MEET CHANGE?



Strong leadership not just from the managing partner, but across the whole partner group was considered a crucial factor in adapting to change. It was the second most mentioned component in a firm's ability to adapt. Leaders need to be more proactive than in the past, require strong people skills, persuasiveness, and the ability to engage with all parts of the business to ensure they are bought into a programme of change.

Ultimately, change driven from the top requires time, a clear strategy or roadmap, as well as the right **people and skills** within the firm to execute and deliver it.

Understanding client needs was the next most mentioned factor. One law firm leader suggested "getting very close to clients in a trusted adviser sense and truly understanding - shaping even - their needs."

Access to **the right tools and technology** will allow lawyers to change the way they work from the ground up. It will change the way legal services are delivered, as well as the way lawyers work by making agile working easier.

The practical challenge raised by one law firm leader was, "once you have created seeds or pockets of excellence, how do you cross pollinate to other practices or areas of the firm?" Solutions mentioned by others include changes to the **law firm structure**. One suggested changes to, "some important aspects of our compensation system, which don't encourage people to behave in a team oriented collaborative manner."

Or rather than cultivating an adaptable and agile firm, one law firm leader suggested that in a time of uncertainty, it is so difficult to predict what will happen, the best course of action is often not to react, but simply decide on a path and stick to it.

"Thinking through the issues at first principle level and talking to clients to understand their needs will inform how to respond to market changes and avoid expensive missteps with technology."

THE SCOTTISH PERSPECTIVE

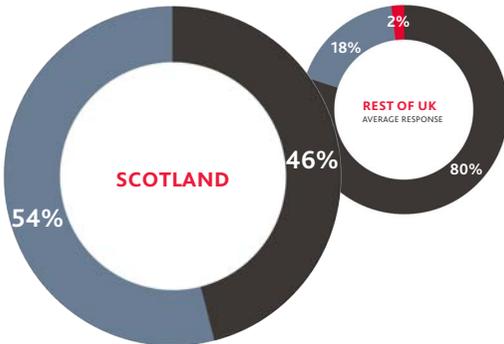
As part of BDO's series of reports on law firm leaders and managing change, we surveyed 63 law firm leaders based in the UK, including 13 at independent Scottish law firms.

While there were many similarities in the findings such as the expectation that technology will have a significant impact on their firms in the future, there were also differences in a number of aspects such as the impact of legal market consolidation.

While global, international, UK and Scottish law firm leaders are all poised to guide their firms through a new period of change, their views differed in some important areas.

Do you believe the pace of change in the legal industry is accelerating?

significantly Yes
 slightly Yes
 No



A less dramatic increase in the pace of change anticipated

The legal sector in Scotland has gone through significant change in recent years.

There has been a great deal of consolidation and a number of long established, independent firms have disappeared altogether. Interestingly, while Scottish law firm leaders all believe that the pace of change in the legal industry is accelerating, less than half (46%) described this change as "significant", compared with 80% of law firm leaders in the rest of the UK.

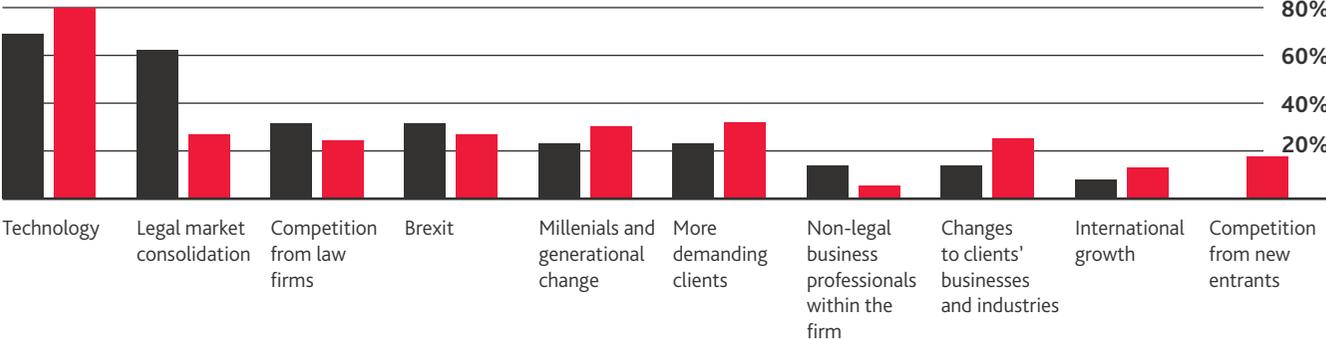
One explained that a rapid pace of change is normal for his firm. Firms like his have already seen their businesses transform over the past decade or so.

Others may be more focused on maintaining current profit levels and market position than dramatic growth. Financial constraints may also play a part.

One commented that "there is real change occurring in the world in terms of technology, but many law firms are not in a position to invest in it".

Which of the following do you believe will have the greatest impact on your firm over the next five years?

Scotland
 Rest of the UK



THE SCOTTISH PERSPECTIVE

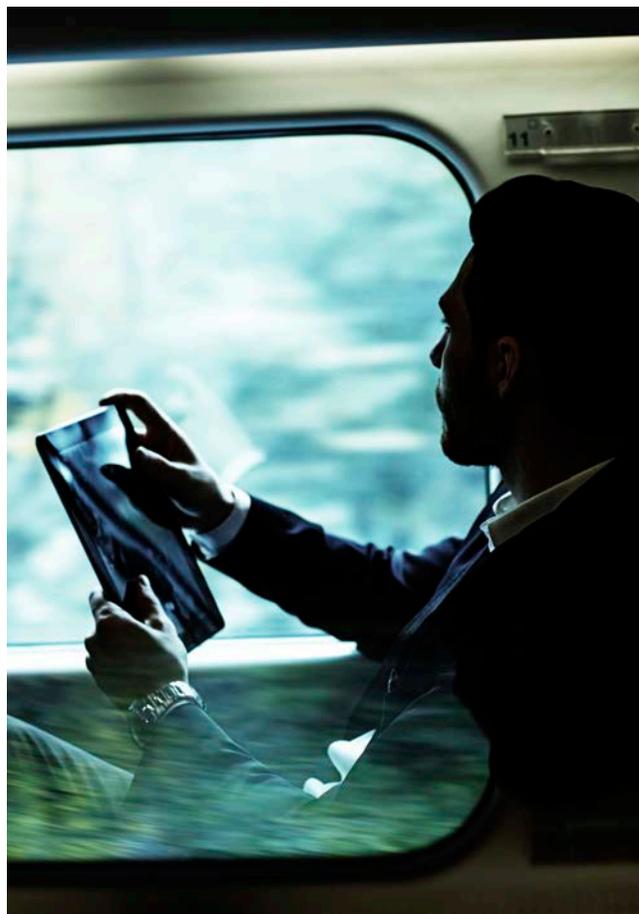
Legal market consolidation will disproportionately impact Scottish law firms

Technology was most mentioned within every grouping of law firms in the survey, including participants at Scottish law firms.

However, unlike firms in the rest of the UK, legal market consolidation was almost as important a factor in Scotland, named by 62% of leaders surveyed, compared with just 28% in the rest of the UK. This is consistent with BDO's survey of Scottish Independent Firms in 2016 where 63% of respondents predicted that consolidation would continue in the sector in Scotland.*

Scottish law firm leaders were also slightly more likely than others to name competition from other law firms and Brexit as factors which would have an impact. BDO's 2016 survey* found that 69% believed that there were still too many law firms and lawyers in Scotland. In terms of Brexit, a number of respondents called for the UK government to provide clarity with one remarking "create clarity quickly and solve the Scottish referendum question". Another commented that Brexit would have a significant impact on the Scottish economy "If you have a slowdown in the English and Welsh economy, even though it's not a recession in England and Wales, it will mean a downturn in Scotland." In addition, Indyref2 continues to loom large on the horizon providing a further layer of uncertainty.

Interestingly, no Scottish law firm leader selected competition from new entrants, compared with almost a fifth (18%) of leaders in the rest of the UK. This may be due to the lack of firms being created of a significant size and the tendency for these to be smaller or boutique offerings.



How will Scottish law firms stay nimble and adapt?

The right culture and mindset, leadership, people and skills, and to a lesser degree, technology, were the factors Scottish law firm leaders felt would ensure their firms were agile and adaptable enough to meet change.

One suggested it would be by "listening to and working with millennials to anticipate their - and most importantly clients' - needs." This was the only leader of the 63 surveyed across the UK to mention the need to listen to millennials or the next generation in response to the question.

Ensuring that their firms respond to client needs rather than market trends was mentioned by almost a third (31%) of all Scottish law firm leaders. Whether client demands or accurate and accessible financial data, the information on which decisions are made was also thought to be crucial.

Another pointed to the need for strong leadership and management in order to make fast decisions.

"Strong management with authority to make decisions quickly without everything having to be approved by a committee or a large group of partners. First mover advantage can win the day in a competitive situation."

FOR MORE INFORMATION:

MARTIN GILL

Lead Partner, Scotland
+ 44 131 347 0346
martin.gill@bdo.co.uk

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