

Beyond COVID 19: What will law firms need in a Finance Director?



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The last few months of 2020 with COVID 19 has put significant strain on Finance Directors, with banks requiring cash flow forecast scenarios, nervous partners, socially distant management meetings and cash flows under pressure. Many Finance Directors also have significant COO-style responsibilities, adding to an already tough portfolio. Cash flow is the issue most mentioned to us - the very lifeblood of any law firm. Some Finance Directors are delivering brilliantly; the performance of others has shown that they may not be right for their law firm to overcome the serious challenges for law firms which are going to present themselves in the near future.

See your Finance Director as more than just a number cruncher who has kept the firm in-line regarding expenses and runs so many spreadsheets that they are the only one that understands them. Firm's should have an FD who adds value from the day they join the firm, who is integral to the success of the business. More than ever FD's are getting involved with all aspects of decision making, are becoming trusted partners and are far removed from being number crunchers.

Undoubtedly there are stereotypes in Finance Director roles within the sector, who have been with the firm for years and have often grown as the business does, not qualified accountants but qualified by experience. They will never dream of challenging assumptions made in the firm about the business. For the role to really succeed it must be allowed to adapt so that FD's have a place at the table with partners and are recognised as being vital for business success. We are now seeing FD's being given shadow or actual equity, directly linked to profitability, and this ensures that they take the pleasure and pain of success. If they make you more profitable, they are rewarded accordingly. If, however the market changes and recession hits they are not rewarded.

They must add value to your business plans not just in the present, but in the long-term future and the analysis they run will be vital to that. Commercial acumen and seeing the bigger

picture will help you to advise teams because with accurate figures you may well challenge revenues, performance and profitability. That in turn will help operationally and can be used in a collaborative way to get the best from your teams. If your FD is at the heart of the business working to help partners and fee-earners in the longer-term clients will see value creation within the firm.

Every function within the firm will benefit from a financial thought process to help that function and the firm as a whole. They will help functions be cost effective and more efficient if they are seen as integral to the firm and not an interference to that individual business function. The bottom line will improve if the silo mentality is broken down to a more collaborative approach.

The current crisis has accelerated trends which were already underway- agile working, increased digitalisation, paper-light offices, clients wanting higher levels of service at lower cost, better management of risk (with attempted frauds much increased over the COVID 19 crisis), increasing pressure on margins and lengthening cash flows.

These pressures all demand higher performance from Finance Directors who must manage their firms' finances ever more efficiently to ensure that firms both survive and are able to keep up with competitors. The board needs to be able to trust the financial information and debate it with their FD, knowing the numbers are not ambiguous and really will aid complex business decisions and mitigate risk.

In addition, a high performing FD will help you identify and articulate key performance indicators and will provide high level management information to support and help you drive decision making within the bigger picture of your strategic business plans. The role is evolving to a degree where we are seeing CFO/COO roles, where individuals are so valued that they are now seen as part of operations and not just finance. This then becomes even more of a central role and helps firm wide operational transformation.

So, what should be the key capabilities and qualities that the Finance Director of 2021 and beyond will need to have?

He or she will in particular need to be an expert in at least all of the following areas:

- Ensuring best practice finance and operational procedures
- Managing working capital and improving profitability
- Ensuring 'financial stability' and managing financial risk - Managing bank, audit and regulatory relationships
- Business planning, strategy, and importantly implementation
- Advising on reward structures and their impact on performance
- Managing support services
- Evaluation of opportunities such as a proposed merger neutrally and objectively

The Finance Director should:

- set clear goals, robust methodology, objectivity and timeliness. These may relate to annual budgets and business plans or new business initiatives, mergers, joint ventures and UK or overseas investments.
- always consider the firm's goals and objectives, lay out the options and recommend a course of action. The advice should bring consistency to decision making.
- ensure that a firm has access to the full range of financial measurement ratios and other Key Performance Indicators and that the firm's business performance is closely monitored to accelerate cash flow and strong profit performance and eliminate weak financial performance.
- Recommend whether specific investments or divestments (of a human capital or other nature) should be carried out

With teams working largely from home for the foreseeable future, having robust systems that can provide (in as near real time as possible) access to relevant, actionable financial information (not just raw data) to partners is increasingly necessary and the technology to achieve this is already very much available. The days when the finance teams were the High Priests of *Financial Information Overload* controlling the issue of data (often in spreadsheet form rather than in graphical form) have, in firms having Finance Directors of the kind we recommend, gone. Leaders and partners alike need to be able to access the key information and understand the implications for them and their teams so that they can take timely action.

Crucially, profitability needs to be properly measured so that the right management decisions for the future can be made. If you are not able to access profitability by matter, matter type, client, client segment, partner and team you should be asking questions.

Working capital management is a priority ("Cash is king") and there will be firms who will cease to operate in the next twelve months because of cash deficits and partner unwillingness to provide further capital. This needs to be measured from a market facing, client / matter / work perspective as well as from a firm-wide, department, team, partner, and associate viewpoint. It is crucial that your Finance Director should therefore:

- Understand what your bank is looking for if it is to be able to fully support your firm rather than just hoping to rely on a gentleman's agreement and a fragile overdraft facility. Banks are generally open to well-managed firms which are strategically active, not over leveraged and where there is evidence of effective and well managed working capital that can tell a sound financial story.
- Actively manage and review WIP and ensure that debtors are managed fully, making fee earners and partners responsible for their cash collection.
- Benchmark cash collection rates as well as profit generation because the two do not necessarily go hand in hand or follow one another.
- Educate partners and fee earners on how to manage their clients differently to improve cash generation
- Understand that PII renewals will need a sound business case presented to show that the firm has done everything possible to mitigate Covid-19 risks. Insurers are concerned about financial stability, cyber-attacks and fraud attacks. Your FD should ensure that all areas of risk have been assessed and show that your approach is such that all areas of potential risk have been considered.

Cost-effectiveness is key in a slowing economy. The Finance Director should:

- Ensure that costs are minimised and working capital is efficiently managed to maximise the firm's cash flow, sitting down with partners (or via the Finance team) to drive this
- Ensure that accounting, tax and compliance issues are fully and effectively managed.
- Engage in a mentoring / coaching relationship with partners and other fee earners to improve their understanding of the firm's financial goals and to help them maximise their contribution to the firm's success including training the firm in Financial Awareness
- Be reviewing all contracts with suppliers to ensure that they are all still '*best value*'.

The Finance Director of the future should also be able to help the firm meet the difficult challenges now facing legal practice by:

- Benchmarking performance across different client groups and comparing to external benchmarks.
- Leading pricing strategies to maximise client revenue, build market share and leverage capacity.
- Providing financial modelling to demonstrate the impact of various reward structures, both immediately and over time, taking into account a range of assumptions and advising on how performance criteria should be weighted.

To do this, Finance Directors must be IT literate and ensure that systems upgrades are well managed and that appropriate desktop technology is available to partners and others in order to enable them to perform their roles more effectively. Technological changes and analytics tools enable significant efficiencies, leveraging data to draw out commercial insights critical to give your firm an advantage in a marketplace where everyone strives to be different or better than their competitors and gain strategic advantage.

Finally, the Finance Director should be a key member of the leadership team. One study recommended that the Managing Partner/Finance Director should be like Captain Kirk and Mr Spock – with one providing inspiring leadership and the other having the integrity and strength to stand up to the leader- including stating where the proposed decision is “not logical”. We have seen too many “Yes men” Finance Directors lead firms into difficulties. If you are a Managing Partner, do you consider your Finance Director a strong right hand complementing what you do and vital in delivering results, or does your Finance Director just give you raw data with no analysis, instead of providing quality financial information? And importantly, is the information you receive in “real-time” to enable you to take timely action, or is it historic because of the time delay in getting it to you?

The ‘right’ Finance Director should, as well as taking responsibility for the finance team, also manage broad business, operational and support team issues, which should free up Managing Partners to manage strategy and deal with partnership issues and client relationships. Having said that, a Managing Partner has ultimate responsibility for the performance and well-being of a firm and should always be able to hold his / her own with a Finance Director on essential financial management issues. In reality the relationship between a Managing Partner and a Finance Director should be a partnership, working together in harmony to create a ‘top team’. The FD should be able to help you become more forward looking, help you see where future challenges and opportunities may arise.

As the legal market consolidates, the FD is an integral part of any acquisition process, particularly where firms need scale to compete. They should also be integral to the integration process. The financial analysis that they provide is a critical aid to the CEO or Managing Partner and they also need to have the integrity and strength to say no to the wrong merger.

Given the uncertain economic outlook, firms cannot afford to settle for second best. The traditional Finance Director and team that was comfortable in the good times may not be right to take the firm forward into what are undoubtedly going to be more difficult and uncharted times.

In short, the ‘right’ professional, highly qualified and skilled Finance Director should be capable of improving business performance, and ensuring a firm’s future prosperity and, if so, will repay his or her cost many times over.

The FD should have a combination of skills to help you meet your business objectives. The right individual will motivate and inspire not just their own team but the wider firm staff at all levels.

Do you have a Finance Director who just produces the numbers or are you looking for someone who can support you in leading the firm to being a *winner* in 2021 and beyond? Some are already excellent; some can be coached to improve; but some, sadly, will need to be replaced in the interests of a firm’s long-term survival.

We would be delighted to talk confidentially about any of these issues- feel free to contact us.

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