

The legal needs of small businesses – summary briefing for legal services providers

About the research

- Commissioned by the Legal Services Board, the independent body responsible for overseeing regulation of legal services in England and Wales
- Analyses the experiences of small firms in today's economy, showing the origin of legal problems that they face and their strategies for dealing with these problems, including where they seek advice and their experiences of doing so
- The largest ever survey of small firms' interactions with the legal sector – an online survey of 10,528 respondents, including 1,463 also interviewed in 2013

Key findings

- **The number of legal problems faced by small firms reduced significantly over the last two years** - reflecting better trading conditions. The most common problems related to trading, employment and taxation. Other businesses were the main source of problems. Larger small businesses, and businesses with BME and disabled business owners-managers, were most likely to experience problems
- **Half of firms reporting a legal issue said it had a negative impact**; one-quarter of them reported loss of income and one-fifth reported health related problems. Total annual losses to small firms due to legal problems is estimated at £9.79bn.
- **The large majority of firms had little contact with legal advisers**. Less than 1 in 10 either employed in-house lawyers or had a retainer with an external provider. Over half of firms experiencing a problem tried to resolve it by themselves. When advice was sought, accountants were consulted more often than lawyers
- **Only 13% of firms viewed lawyers as cost effective** – little improved since the 2013 survey. Microenterprises were the least likely to view lawyers as affordable
- **Satisfaction that law and regulation provide a fair trading environment increased from 30% in 2013 to 45% in 2015** – improving economic conditions as well as improvements in the regulatory environment may explain this change

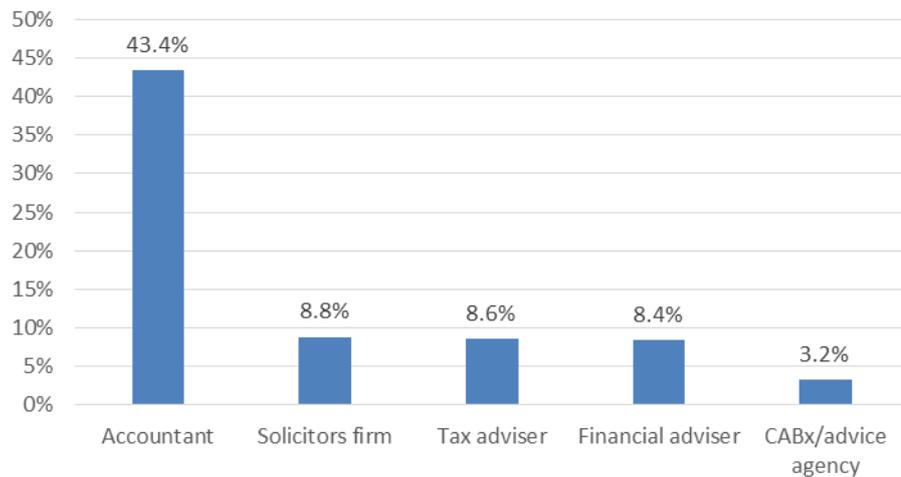
Implications for legal service providers

1. Small firms – those employing up to 50 people – comprise 99% of all businesses. These firms contribute 33% of UK business turnover and 48% of employment. Small firms will encounter a range of legal issues as they start up and grow, and given their small size they will often need to turn to external experts as a means of overcoming their limited in-house capacities and capabilities.
2. This new research is important for legal services providers first, in terms of understanding the challenges that small firms face; second in terms of how legal services providers are meeting the demand for legal advice; and finally, how legal services providers may further develop their provision for small firms. The marketplace for legal services is dynamic in terms of demand, as firms face an increasing variety of legal problems and on the supply side, as new entrants and sources of legal advice become available. It is important that suppliers of legal advice continue to adapt and meet the changing demands of the marketplace.
3. Legal services providers would benefit from understanding how small business owners' seek to resolve their business problems; the role of their trusted sources of advice and why they choose to avoid, or take up, professional legal advice.

The competitive challenge for law firms

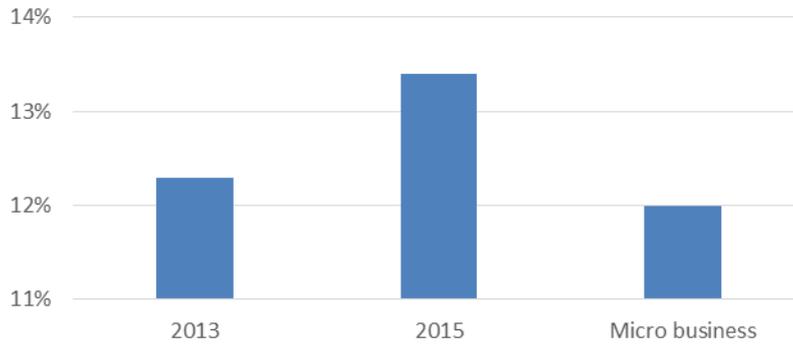
4. The market opportunities for legal service providers appear extensive. In 2015, respondents reported experiencing around 40,000 problems over the previous 12 months. Legal problems were hurting small firms: 26% having a problem reporting loss of income; and 9% loss of a contract or customer. Total annual losses to small firms, as a result of legal problems, is estimated at £9.79bn.
5. The research shows that the marketplace for legal advice for small firms is far from the exclusive domain of lawyers. Only around 20% of those with a reported legal problem drew upon the legal profession. Since lawyers are not normally the first port of call for small businesses for advice on business problems, other suppliers are in a stronger position to offer legal advice. Accountants in particular have been expanding their portfolio of advice, such as in HR and employment matters, and are seeking innovations in their market offerings. Accountants are now permitted to provide probate work and the Legal Services Act provides scope for them to expand into other reserved areas of work in the future.

Top 5 business support services used in last year



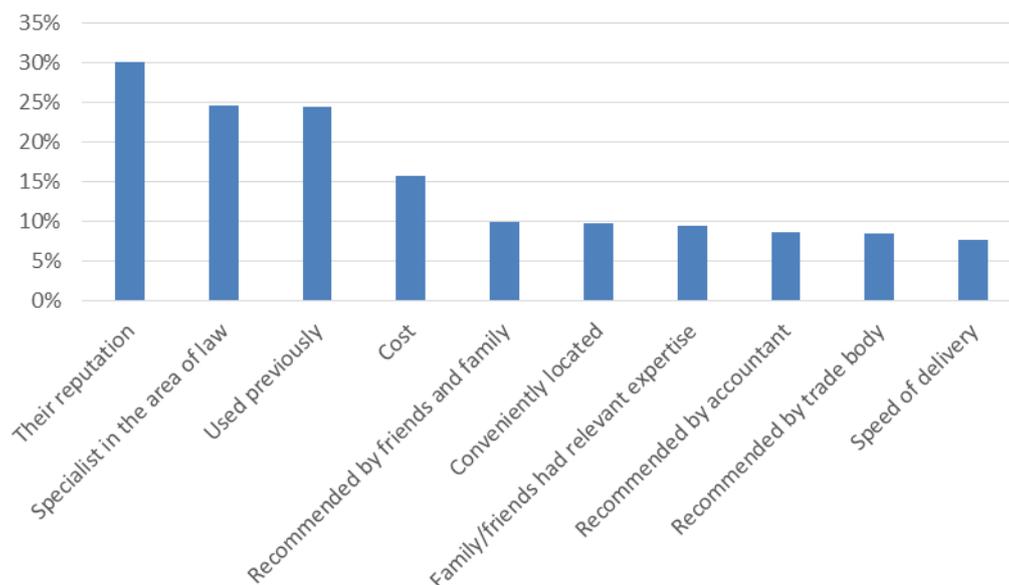
6. Small firms tend to approach a lawyer only after they have considered other ways of resolving a problem. Almost 50% of respondents strongly agreed or agreed with the statement that they *'use lawyers as a last resort to solve business problems'* compared with 12% who disagreed strongly or disagreed. They also tend to avoid having legal services on a long-term, standby basis, preferring to pay for advice and services as and when required. Further, 87% of small firms do not have any in-house legal expertise. This lack of ongoing legal capacity distinguishes them from large organisations. Indeed, within the sample of firms, larger small firms faced more legal problems than micro firms but were only marginally more likely to utilise in-house or external retainer solutions.
7. An unequivocal finding is that cost is a major deterrent to taking up legal advice. Almost a half of respondents disagreed with the statement that *'Lawyers provide a cost effective means to resolve legal issues'*; only 13% agreed with the statement. This compares to 12% in the 2013 survey and thus represents no appreciable improvement during the last two years. However, if we only include those that have actually used a lawyer, those agreeing or agreeing strongly with the above statement rises to 52%. This suggests that the challenges of accessing lawyers are both *perceived* as well as *experience-based*. Micro firms were particularly likely to view lawyers as not cost-effective.

Small firms who agree 'lawyers provide a cost effective means to resolve legal issues'



8. Despite the role of cost as a deterrent to using legal services, it was not the single most important factor influencing choice of lawyer. Provider reputation, legal specialism and prior use were the most important reasons for choosing particular providers – all featuring above cost considerations. Recommendations from family and friends, accountants and trade bodies were also important. This finding has parallels with surveys on individual legal need. The distance between law firms and small firms, plus the importance of recommendations and prior use in small firms’ purchasing decisions, suggests that legal professionals need to be more proactive and *communicate their offerings* much more effectively.

10 most important factors in choice of provider



9. Although lawyers may have an advantage of possessing institutional trust, if they are to develop relations with small firms this requires building upon with relational trust. Current strategies include advertising events within legal

professional circles and awareness raising activity, but the research suggests they need a greater presence to inform small firms of their services and costs.

Possible strategies

10. One possible approach is for law firms to make stronger strategic ties with other key business support providers who have close connections with small firms to ensure that they become an embedded part of support networks. Intermediaries such as accountants, national agencies, local authorities, trade bodies and chambers of commerce may help put legal services providers more on the 'map' and enhance a network of contacts. It will also help break down any misperceptions that small business owner-managers have regarding lawyers.
11. There is also a national and regional element to this approach. Given the plethora of small business initiatives by government to promote business growth, innovation and exports, building a legal component into these initiatives could help to break down the perceived and real barriers between small firms and legal services providers. Embedding legal services into the initiatives and activities of other agencies may provide a key to overcoming these barriers.
12. One major implication of the findings is a need for *greater clarity on the type of services offered for small firms and their cost*. It has also to be recognised that the small business population is not homogeneous and may require some market segmentation. This report has found the micro-firms in particular to be very reluctant to take up legal advice in its current form despite the growth in this business format. Business segmentation approaches by legal services providers may include targeted services for business start-ups, firms of differing ethnic minority origin and those run by owners with a disability, or specific sector offerings where these are relevant.
13. Set against the above context, it may be argued that legal professionals would *benefit from closer ties with small business owners through education and educational institutions*. Business schools are being promoted as hubs of support for small firms, both in terms of placing students in small firms and providing development programmes for small firms themselves (See BIS, 2013; and Small Business Charter).¹ There is a potential role for legal services to be an integral component of such initiatives and reach small firms. This would help legal

¹ See for example, the Small Business Charter. <http://smallbusinesscharter.org/>; and BIS 2013 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/198165/growing-your-business-lord-young.pdf

services professionals understand the challenges of running a business and the need to show that they can help businesses create value. A higher profile within universities may also help lawyers understand some of the concepts used in business and economics studies, such as transaction costs and information asymmetries, and thus help shape their offerings to small businesses. Indeed, many smaller practices in the legal profession encounter such challenges themselves, either as self-employed individuals or partnerships, and so the trust gap identified in the report may not be as wide as perceived.

14. Given the image amongst many business owners of lawyers as expensive and irrelevant to solving small business problems, there needs to be a *strong communications initiative at the level of the legal profession with small business groups as a whole*. This should be designed to break down the information barriers between lawyers and small business owners. It may be important for example, to portray legal service providers as helping anticipate and thus avoid legal problems rather than being advisers of last resort.
15. Within this context, the Chancellor in his 2015 Budget announcement stated that the Government will provide information for SMEs on accessing and using legal services, which will be included on the Citizens Advice and the GREAT business websites. The Government believes that SMEs, like all consumers, need access to information to engage proactively in this market, including knowing when and how to get legal advice. This research underlines the need for such initiatives to enhance SME awareness and engagement with legal services when appropriate.