



Pointmaker

THE PRICE OF LAW

Jim Diamond

SUMMARY

- The top commercial law firms in the City of London are regarded as some of the best legal practices in the world. The top seven firms in the City employ tens of thousands of people, and bring substantial tax revenue into the country – generating billing revenues of over £1 billion each in 2015.
- However the hourly rates for a partner at a top London firm now exceed £1,000, the highest level ever recorded. In nominal terms the top City of London law firms charge almost the same amount per hour as their American legal cousins except that the UK firms charge their clients in sterling.
- Those seeking to comply with UK legal procedure are forced to pay extremely high costs to do so – high enough to restrict access to law, particularly for smaller business clients for whom bills can be prohibitive.
- This is occurring for three main reasons. The primary cause of the escalation in rates can be attributed to the increasing complexity of the UK tax and legal systems. The Hong Kong tax code, for example, widely considered the most effective in the world, is 276 pages long. The British tax code, which has more than trebled in size since 1997, is currently over 22,000 pages long.
- Furthermore, the lack of transparency on legal costs allows top law firms virtual control over their prices. Transparent pricing is vital for a marketplace to function fairly and efficiently. Yet it does not exist within the market for UK commercial law. Average hourly rates for commercial legal services are not published online.
- Finally, the remarkable similarity in the rates charged by each of the Magic Circle law firms suggests a shortage of competition between them – the differential between hourly rates charged to clients tends to be in the region of only 5%. While there is no suggestion of collusion between the companies concerned (which would of course be illegal under UK competition law), such close price similarity is indicative of a less-than-perfectly functioning market.
- Steps should be taken to ensure fair practice in legal procedure. The “billable hour” is an outdated and unsustainable billing method for legal services to continue. Alternative billing methods must be considered, including Lord Justice Jackson’s recent proposals to move to a fixed fee basis – the Lord Chancellor should give full consideration to these proposals in order to ensure that the legal market place thrives in the long term, and that the price of law is not punitive.



1. INTRODUCTION

The top commercial law firms in the City of London are regarded as some of the best legal practices in the world. The top firms in the City employ tens of thousands of people, and bring substantial tax revenue into the country – generating billing revenues of over £1 billion each in 2015. At a time when the UK services sector is only just beginning to exploit fully the opportunities posed by globalisation, law firms are well positioned to become a highly valuable sector of the economy.

However, these law firms are some of the most expensive providers of legal services in the world. They are also some of the least transparent, particularly in terms of pricing: while they do publish yearly statistics on the performance of their firm, from turnover to profit per partners, they do not publish information on the hourly rates charged to their clients.

2. HOURLY RATES

The 2015 Jim Diamond Hourly Rate Survey (JDHRS, See Appendix 1) reveals that the average partners' rate for partners at the Magic Circle¹ law firms has reached a new record of £850 per hour² (The yet to be published 2016 JDHRS, already has collated information that reveals top partner hourly rates are now as high as £1,100). The rate the firm's clients are currently charged per hour for a newly qualified solicitor falls between £350 and £400 per hour. As a newly qualified solicitor at a top commercial law firm can bill annually between 1,600 and 1,800 hours,³ they are therefore generating up to, and in excess of, £500,000 a year in fee income.

Hourly rates for partners in the mid-1980s were in the region of £150 to £175, reaching £200 to £250 by the end of 1980s, in nominal terms. The 1990s also saw the growth in size of the top legal companies from approximately 50 partners in the mid-1980s to 500 partners by the end of 1990s. Table 1 below shows the rapid rise of hourly rate for Partners since 2003.

Table 1: Average Hourly Rates for Partners at the top commercial law firms, real terms⁴

2003	£498 to £598
2005	£546 to £674
2007	£766 to £858
2008	£710 to £888
2009	£521
2010	£729 to £813
2011	£644 to £752
2013	£713 to £866
2015	£775 to £850

Source: Jim Diamond Hourly Rates Survey, CPS analysis

It is noticeable how sensitive the hourly rates are to the general economic conditions; the economic downturn of 2007-08 preceded a marked reduction in hourly rates in 2009. As the economy recovered, so too did the rates for Partners (but at a much faster rate). As *The Lawyer* pointed out in 2010:⁵

"Today's astonishing findings from costs lawyer Jim Diamond shed an entirely new, and in some

¹ i.e. Allen & Overy, Clifford Chance, Freshfields Bruckhaus Deringer, Linklaters, and Slaughter & May.

² While interviewing Roger Lowe, Senior Responsible Officer for the sale of Eurostar, Shareholder Executive, at the Public Accounts Committee, Stephen Phillips QC MP asked why Freshfields were able to bill a senior partner out at £1,000 an hour during the Government's £757 million sale of its stake in Eurostar.

This was later denied by Freshfields. See <http://www.legalcheek.com/2015/11/the-freshfields-firm-charges/>

³ Rollonfriday.com, *Lawyers at Baker & McKenzie to work an extra 100 hours a year*, 2013.

⁴ ONS Consumer Price Inflation, October 2015.

⁵ *The Lawyer*, September 2010.



quarters probably not entirely welcome, light on the past couple of years' trading environment for the UK's leading lawyers. The fact that not one magic circle partner was willing to go on the record for a story about a resurgence in law firm pricing smacks of embarrassment at a time when lawyers are supposed to be bending over backwards to accommodate clients. According to Diamond's annual survey, hourly billing rates at the majority of UK firms are back up where they were before the recession".

If the findings were astonishing in 2010, they are even more so today; *The Lawyer* has reported that the total annual revenue of the top 28 legal firms in the UK now stands at £15.2 billion in 2015. The equivalent sum in 2011 was £11.4 billion in real terms, an increase of 34% in just four years.

The increase in fee rates is compounded by the increased number of professionals who are now likely to be involved in a transaction.

Charging by the hour is outdated & unnecessary

Hourly rates are inefficient, opaque and encourage inefficiency. Other top corporate industry charges by results, not hour. Hourly rates have been widely criticised, including most recently by Lord Justice Jackson, who, speaking at the IPA Annual Lecture last month, stated that:

"The present level of costs and complexity of civil litigation has evolved over time under the influence of costs shifting and the system of 'hourly rate' remuneration. Remuneration on a time basis rewards inefficiency. Unrestrained costs shifting drives parties to leave no stone unturned: the more costs mount up, the more determined each party becomes to ensure that the other party pays them. The result is inevitable – a civil justice system which is exorbitantly expensive."⁶

Despite such criticism top law firms appear resistant to adopt innovative and more efficient charging methods – unlike their peers in corporate accounting and consulting firms.

3. WHY ARE RATES SO HIGH?

Complexity

The primary cause of the escalation in rates can be attributed to the increasing complexity of the UK tax and legal systems. The Hong Kong tax code, widely considered the most effective in the world, is 276 pages long. The British tax code, which has more than trebled in size since 1997, is currently over 22,000 pages long.

As the First Parliamentary Counsel and Permanent Secretary of the Cabinet Office, Richard Heaton, has explained:⁷

The law is regarded by its users as intricate and intimidating... That experience echoes observations that have been made about statute law for many years. The volume of legislation, its piecemeal structure, its level of detail and frequent amendments, and the interaction with common law and European law, mean that even professional users can find law complex, hard to understand and difficult to comply with.

Other external explanations include a deterioration in the quality of parliamentary draughtsmanship, globalisation (in that cross-border cases require expertise across different jurisdictions and therefore a greater range of expertise) and the growth of super-national organisations.

A lack of transparency

In addition to these external pressures, there are also industry-specific factors for the rapidly increasing cost of commercial law. In particular, the absence of price transparency.

⁶ Lord Justice Jackson, IPA Annual Lecture, January 2016.

⁷ Richard Heaton, *When laws become too complex*, Cabinet Office, 2013.



Transparent pricing is vital for a marketplace to function fairly and efficiently. Yet it does not exist within the market for top commercial law firms. Average hourly rates for law firms are not published online (although smaller English legal practices do often publish their hourly rates).

This failure has been recognised by two trade organisations, the Legal Services Board, the regulator of the legal market place, and the Law Society.⁸ The former produced a report in 2012, on the *Charges of the Legal Market Place*. In the opening paragraph of the report it was stated that “*The [Regulatory Information Review] found limited information on charging methods*”. The report had only two reference points on hourly rates; the guideline hourly rates set by the HM Courts and the Tribunals Service Costs Committee (which related solely to costs of third parties in civil litigation); and the JDHRS. The regulator of the legal industry did not know the hourly rates charged by the top commercial law firms.

Nor has the English and Welsh Law Society (Law Soc) published information on the hourly rates either. They did publish a Tool Kit on Costs Management in November 2013, which included the JDHRS. The Law Society has little or no information on what hourly rates have been charged by the top commercial law firms over the last decade.

A similarity in rates

The JDHRS suggests that over the last two decade there has been a remarkable similarity in the rates charged by each of the Magic Circle law firms: the differential between hourly rates charged to clients tends to be in the region of only 5%. While there is no suggestion of collusion between the law firms concerned (which would of course be illegal under UK competition law), such close price similarity is

indicative of a less-than-perfectly functioning market.

4. AREN'T HIGH RATES JUSTIFIED?

Top law firms are entrusted with the highest value transactions; and they are expected to provide the highest quality service undertaking work on some of the most complicated legal cases. They are required to demonstrate extraordinary international reach and an expertise that allows them to work on legal matters that span the globe. However despite their position as foremost in the legal profession there is evidence that such high rates should not be expected.

Top accounting firms are cheaper

Over the last several years top level accounting firms have been gradually re-entering certain areas of the legal market.⁹ These firms have been undercutting Magic Circle firms by applying streamlined cost-saving techniques developed in corporate accounting – many simpler legal processes are automated and, importantly, accountancy firms charge by the results achieved, not the hour.

Admittedly top accounting firms aren't yet tackling the high level cases that top law firms handle. However there is good reason to believe that the firms plan to continue growth of their legal departments and will soon attempt to compete at the highest level – although they will struggle to secure such work initially as they do not have the same legal reputation that the Magic Circle enjoy. This is an indication that clients of Magic Circle law firms are to some extent paying for the name rather than the expertise – expertise which demonstrably could be provided at lower cost.

⁸ The Legal Services Board is the independent regulator of the entire legal market place, covering solicitors, barristers, legal executives, cost

consultants et al, while the Law Society is the “trade” body representing solely solicitors.

⁹ The Economist, *Attack of the bean-counters*, 2015.



Clients of top law firms distrust their fees

Evidence suggests that large clients have long been concerned with the level of legal costs and distrust top law firms to charge them fairly. Over a decade ago a world class investment bank was forced to circulate a document to its London lawyers outlining the terms and conditions of their legal contract in an attempt to crack down on perceived inefficient billing practices. The document stressed that the hourly rates charged by the law firms should not be higher than that charged to its peers. Furthermore it demanded that when a bill was presented it must include “the names of each partner, associate and para-professional at [the law] firm who performed services ... and the amount of time spent by each”, broken down into discrete tasks.

5. US LAW FIRMS HOURLY RATES

The National Law Journal publishes an annual survey of law firms billing in 2014 across the US legal market place.¹⁰ It is even able to produce statistics on the individual law firms. The top 14 law firm’s average partner rate was under \$980 per hour. Associate rates ranged from \$290 to \$670 per hour. Of the top 14 law firms, 11 are based in New York, a city with similar living costs to London. Hourly rates have not escalated as quickly in the US as they have in the UK: according to the *National Law Journal*: “Although the rates charged have gone up in recent years, the amounts that clients pay have not kept pace with inflation, legal industry leaders say.”

In nominal terms the top UK law firms charge almost the same amount per hour as their American legal cousins save the UK firms charge their clients in sterling.

6. SOME ATTEMPTS AT REFORM

Several attempts have been made to address the high costs of legal advice. None, so far, has been successful.

The Law Society recognised the importance of setting budgets over two decades ago, when they introduced the Solicitors Costs Information Code in 1991. The code was amended in 1999, 2007 and 2011. Each version was intended to establish a protocol for better costs information for a client both before instructing a law firm and throughout the case/matter.

The latest version is the Solicitors Regulation Authority Code of Conduct, which was established in October 2011.¹¹ This takes the code to a higher level as “the relationship with your client is a contractual one which carries with it legal, as well as conduct obligations”.

The frequency with which the code has been amended over the years suggests that it has been less than successful in practice. Indeed, in 2009 the Master of the Rolls, Sir Anthony Clarke, asked Lord Justice Jackson to conduct a review of legal costs in civil litigation. The aim of the review was to provide recommendations in order to promote access to justice at proportionate cost. It is a striking indication of the failure of the legal profession and its regulators that the judiciary felt it necessary to attempt to control the spiralling level of legal costs.

Lord Justice Jackson’s reforms, introduced in 2013, referred to a legal costs “big bang”. One of the fundamental components was the introduction of Costs Management in civil litigation. This included a template to be used in formulating detailed budgets to be used at the case management hearings, Budget Precedent H. However, most civil

¹⁰ *National Law Journal, Annual Survey of Law Firm Billing Rates for Partners and Associates*, January 2014.

¹¹ www.sra.org.uk/solicitors/handbook/code



legal matters do not involve court hearings of any sort – where no such protection is in place.

The failure to observe the Costs Information Code by law firms has been commonplace over the last 24 years. Although contractual obligations were imposed on all law firms, in practice these obligations have not always been met. In particular, detailed budgets are rarely given to clients; outline budgets are often written on a single page; and costs are frequently underestimated. The problem was highlighted at a meeting at the 2009 Commercial Litigation Association Annual conference in which Lord Justice Jackson gave his first public presentation of his draft proposals. The author of this paper, a joint speaker at the Conference, asked the 50+ delegates from the top commercial law firms how many had ever produced a detailed budget. The response was fewer than five.

7. THIRD PARTY LEGAL FUNDING: SOME STEPS IN THE RIGHT DIRECTION?

Third Party Legal Funding has been permitted in England and Wales since 1967. However, until it was reformed as part of Lord Justice Jackson's 2013 reforms, it was limited to insolvency situations.

In simple terms, a third party funds a case on behalf of a claimant who may be unable or unwilling to bear the costs. In return the third party takes a share of the damages if the case is successful. The share varies, but ranges from 20% to 45% of the damages. If the litigation is not successful, the funder bears the costs it has agreed to fund. Third Party Legal Funding is significantly different to "No Win, No Fee" practices where the risk is borne by the client's solicitors (who therefore have an incentive to encourage clients to sue for personal damages).

Third Party Legal Funding is limited almost exclusively to large cases. In the three years since it was reformed litigation funding has promoted access to justice by enabling litigants to manage

their exposure to legal costs. In particular, companies acting in this area – who have raised over £1 billion to fund cases – are both experienced in managing legal costs and have established strict cost controls in order to manage the risk of their investment.

Two of the leading litigation funders have stated their views on this subject in conversations with the author of this paper:

Nick Rowles Davis, Managing Director of Burford Capital:

"Although the production of budgets is getting better, we still have to reject 50% of cases because of the weakness of the budgets submitted to us by the solicitors of potential clients. This is simply because they do not contain sufficient detail for us to assess the risk of funding the case".

Simon Druzniak, Investment Manager of Bentham Europe Limited (who set up in UK in May 2014, and are one of the biggest and original litigation funders):

"In our experience of budgets specifically with our track record in Australia, somewhere in the region of 95% of budgets produced to us from solicitors are exceeded once we fund a case at some stage."

8. CONSEQUENCES OF HIGH LEGAL COSTS

The high level of legal fees is an efficiency drain on commerce. British industry is forced to suffer a deadweight loss as excessive amounts of time and money must be spent dealing with legal issues. The County Court system is shambolic at present, with some Courts quoting between eight and 10 weeks to acknowledge correspondence.

Recent court fee increases are unprecedented. As an example, the court fee to issue the court proceedings for a case valued at £200,000 would be £10,000 – 5% of the case value. Including the



legal fees on a general commercial dispute of this nature, total legal costs could rise to as high as £150,000. Such fees could potentially damage small and medium sized firms engaged in litigation procedure.

Expensive hourly rates can also act as a productivity drain on the wider economy. The associated high salaries enjoyed by top law firms attract a significant proportion of top graduates – highly competent workers who could instead be employed elsewhere, in more productive industry.

9. CONCLUSION

Each one of the three main causes of the rapid increase in legal costs needs to be addressed:

- the ever-increasing complexity of the UK tax and legal systems;
- the lack of transparency on legal costs; and
- the lack of price competition between law firms.

The first of these is clearly a huge area, and beyond the scope of the current paper. The other two issues are vital features of competitive markets and their omission in the market for commercial law allows for serious inefficiencies in the form of inflated prices for clients. It is surely in the self-interest of all the top commercial law firms to avoid any suspicion that they may be involved in uncompetitive behaviour. However it should be a relatively simple task for either the Legal Services Board or The Law Society to collect and publish the hourly rates that are now being charged; and if necessary for the Office of Fair Trading and Competition Commission to investigate evidence of perceived or alleged collusion. A simpler method, for example, would be for the front-line regulator to insist on all law firms publishing hourly rates of their various fee earners on their own websites.

The “billable hour” is an outdated and unsustainable billing method for legal services to

continue. If the legal market place is to thrive in the long term, it must develop alternative billing methods. There must be radical changes to the billing/budget protocol.

More recently, early in 2016 Lord Justice Jackson has continued to criticise the failure to address the problem of high legal costs. In his words:

“High litigation costs inhibit access to justice. They are a problem not only for individual litigants, but also for public justice generally. If people cannot afford to use the courts, they may go elsewhere with possibly dubious results. If costs prevent access to justice, this undermines the rule of law.”

Lord Justice Jackson has put forward proposals for moving to a fixed fee basis for all litigation work, suggesting that fees are capped on the basis shown in Table 2, below.

Table 2: Lord Justice Jackson’s suggested figures for fixed legal costs reform

	Band 1	Band 2	Band 3	Band 4
Claim value	£25,000- £50,000	£50,001- £100,000	£100,001- £175,000	£175,001- £250,000
Total legal cost	£18,750	£30,000	£47,500	£70,250

Source: Lord Justice Jackson, IPA Annual Lecture, January 2016

This initiative by Lord Justice Jackson demonstrates that the problem of high legal costs is now recognised by the English Judiciary. That seven years after his initial reforms Lord Justice Jackson has felt it necessary to be so prescriptive shows that the problem has so far been intractable. These latest draconian proposals, if and when implemented, will have drastic consequences for the entire legal profession and will be a significant step towards ensuring fair practice in legal procedure.

The Lord Chancellor should therefore give Lord Justice Jackson’s proposals full consideration.



APPENDIX 1

The Jim Diamond Hourly Rates Survey

The JDHRS is collated from sources both within the law firms and from clients. It has been accepted as an accurate guide by both specialist trade media and broadsheet media since 1999, when it was first published. The Legal Services Board, The Law Society Tool Kit on Costs Management has also used the stats in their publications.

Hourly Rates (Nominal Terms)

1. City of London ('Magic Circle') firms

Year	Newly qualified–2 yrs PQE	5 yrs PQE	Partner
2003	£175-185	£245-280	£375-450
2005	£180-215	£250-300	£425-525
2007	£235-250	£375-450	£625-700
2008	£250	£350-400	£600-750
2009	£250	£375	£450
2010	£300-350	£450-550	£650-725
2011	£300	£425-510	£600-700
2013	£350-£425	£450-550	£700-850
2015	£350-£500	£500-£575	£775-£850

Note: Partner fees peaked in 2007 and 2008 in response to high levels of merger and acquisition activity immediately preceding the financial crash. They were recognised as being unsustainably high at the time.

2. US top law firms (London offices)

Year	Newly qualified–2 yrs PQE	5 yrs PQE	Partner
2007	£215-225	£325-360	£450-500
2008	£225	£300-375	£425-550
2009	£225	£325	£400
2010	£250-300	£450-550	£550-600
2013	£275-325	£450-550	£550-700
2015	£375-£525	£500-£595	£700-£900



3. Top London firms (outside the magic circle)

Year	Newly qualified–2 yrs PQE	5 yrs PQE	Partner
2003	£150-155	£215-225	£325-375
2005	£170-195	£225-300	£350-475
2007	£185-225	£285-315	£400-495
2008	£195	£250-295	£375-495
2009	£180	£250	£375
2010	£180-345	£285-535	£375-640
2011	£215-300	£325-425	£425-600
2013	£225-300	£325-475	£450-800
2015	£250-£350	£350-£495	£550-£800

4. National law firms with regional offices

Year	Newly qualified–2 yrs PQE	5 yrs PQE	Partner
2003	£100-140	£135-195	£185-250
2005	£125-160	£150-225	£19-315
2007	£185-210	£225-275	£350-375
2008	£195	£225-275	£300-375
2009	£175	£250	£325
2010	£175-210	£250-300	£325-450
2011	£175-240	£250-300	£325-450
2013	£195-275	£300-350	£400-500
2015	£195-295	£300-£350	£400-500

5. Jersey—top tier

Year	Newly qualified (advocate)	5 yrs PQE	Partner
2003	£150-160	£225-235	£300-350
2005	£175-215	£235-275	£325-400
2007	£195-225	£260-295	£400-450
2008	£225-250	£275-295	£450-500



2009	£275	£300	£475-525
2010	£285-325	£300-375	£475-575
2011	£285-325	£300-350	£400-475
2013	£285-325	£300-375	£475-550
2015	£285-350	£325-395	£495-625

6. Jersey—mid-range

Year	Newly qualified (advocate)	5 yrs PQE	Partner
2010	£225-250	£250-300	£325-400
2011	£225-250	£250-300	£325-400
2013	£250	£275-325	£425-495
2015	£250	£285-350	£375-495

7. Guernsey—top tier

Year	Newly qualified (advocate)	5 yrs PQE	Partner
2010	£250-275	£325-375	£400-475

8. Guernsey—mid-range

Year	Newly qualified (advocate)	5 yrs PQE	Partner
2010	£185-225	£225-275	£300-340

Source of survey figures:

As a costs lawyer, the author works on a daily basis in the field of legal costs. Hourly rates are continually discussed with lawyers, clients, litigation funders and others. These discussions are always conducted on a confidential basis.



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