



Objective financial stability for law firms

Tier 1

Medium risk of financial instability - internal report trigger

Tier 2

High risk of financial instability - internal action trigger

Tier 3

Financial instability - SRA reporting trigger

Tier 1

Medium risk of financial instability – internal report trigger

- Any late payment of creditors e.g. service providers (but not including insurance, file storage, HMRC, payroll, or landlord – go directly to Tier 2)
- Firm reliant on external funding to meet overheads on a regular basis i.e. not cash flow positive
- Returned items on the firm's office or client account due to insufficient funds
- Expected departure of clients/individuals/teams which will have a significant impact on future income
- [Insert your own triggers]

Action required : COLP to report risk to the Board, with recommended course of action. Review after [4] weeks. If insufficient progress is made, escalate to Tier 2.

Tier 2

High risk of financial instability – internal action trigger

- Lack of visibility on finances (e.g. no cash flow forecasts)
- Late payment to HMRC or file storage - [1-30] days
- Uncertainty of paying insurance, staff and/or rent within [7] days of payment due date
- Less than [£X] held in the business account at any time
- [£X] overdrawn for [X] consecutive days
- Breaks bank covenants
- Levels of debt may become unsustainable (borrowings in excess of net assets)
- Requires significant borrowing to remain a going concern
- [Insert your own triggers]

Action required : Emergency Board meeting convened to take action to address financial risk. Review after [2] weeks. If insufficient progress is made, escalate to Tier 3.



Tier 3

Financial instability – SRA reporting trigger

- Late payment to HMRC – [30+] days
- Inability to pay insurance premium, staff or rent on payment due date
- Levels of debt unsustainable
- Cannot obtain finance
- Fraud event on client account where the firm is unable to replace missing funds
- Any other indicators of serious financial difficulty
- Any “relevant insolvency event” occurs (see SRA Glossary <https://bit.ly/31X6NBw>)

Action required : COLP (or any regulated individual, if the COLP is unwilling to do so) to make a report of serious financial difficulty to the SRA

Notes

This is designed to be an objective tool for law firm managers to help manage financial stability risks, and to identify when the SRA self-reporting threshold has been met.

You should model it on your own firm’s structures, governance arrangements and processes.

The trigger points are based largely upon factors that the SRA considers are indicators of firms in financial difficulty and distress.

Notwithstanding the hard reporting threshold, the SRA encourages early engagement from firms who find themselves in, or anticipate, serious financial difficulty.

Relevant SRA Standards and Regulations

Standard 2.4 of the Code of Conduct for Firms:

“You actively monitor your financial stability and business viability...”

Standard 3.6 of the Code of Conduct for Firms:

“You notify the SRA promptly:

(a) of any indicators of serious financial difficulty relating to you;

(b) if a relevant insolvency event occurs in relation to you...”