

A short paper and notes on the issue of listing of law firms in New South Wales

by
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to the
**Joint NOBC, APRL and ABA Centre for Professional Responsibility Panel
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of Law from a Professional Responsibility Perspective"**

**NOTES ON THE LISTING OF LAW FIRMS IN NEW SOUTH WALES AND
ON THE INCORPORATION OF LAW FIRMS**

1. Listing of Australian national law firm Slater & Gordon

On 21 May this year incorporated legal practice, Slater & Gordon made legal and corporate history when it apparently became the first law firm in the world to list on the Australian Stock Exchange. The firm has more than 95 million shares on offer and another 12 million non-voting shares. Shares in the firm, issued at \$1, closed at \$1.40, on volume of 8.2 million on the first day of trading.

While it may be the first, Slater & Gordon will most likely not be the last law firm to float. Integrated Legal Holdings in Western Australia has lodged a prospectus with the Australian Securities and Investments Commission (ASIC). It hopes to raise \$12 million that will be used to buy legal practices. Other firms and consortiums have had informal discussions with the Office of the Legal Services Commissioner (OLSC) concerning possible listing.

Public listing, poses unique concerns and challenges for a regulator of legal services. Of primary concern is the tension between a practitioner's duties owed under the *Legal Profession Act 2004 (NSW)* (LPA) and the requirements of a director, officer or employee under the *Corporations Act 2001 (Cth)* (Corporations Act).

In the sphere of corporate law in Australia, the Corporations Act advocates for the paramountcy of the rights and protection of shareholders. Accordingly, there is a latent tension between a solicitor's professional obligations and a solicitor's duties to a company's shareholders. This, along with the other problems listings raise will be discussed in Section 6 of this paper.

2. History of Incorporation

Traditionally, solicitors in NSW practiced as sole practitioners, or in partnership with other lawyers. There was little appeal in practising in any other structure such as a multidisciplinary partnership (MDPs) or a solicitor corporation because of the imposition of numerous conditions on these structures.

In relation to solicitor corporations for example, whilst incorporation was permitted pursuant to the *Legal Profession (Solicitor Corporations)*

Amendment Act 1990, the Law Society placed strict controls on solicitor corporations in that only an “approved solicitor” could hold voting shares in such corporation, and only an “approved person” could hold shares in such companies. Such controls, it appears existed to ensure that only solicitors and their families controlled solicitor-corporations.¹

Similar restrictions were placed on MDPs making them an unpopular choice for legal practice. In 1994, legislative amendments were introduced to try and liberalize the conditions attaching to MDPs. Although the rules liberalized some of the conditions, two rules remained which continued to restrict their appeal.

The first restriction was that lawyers were required to retain the majority voting rights in the MDP. The second restriction was that lawyers were required to retain at least 51% of the net income of the partnership, thereby limiting the income of non-lawyers to 49% of the net income earned by the MDP.

In 1998, a Report entitled the “National Competition Policy Review of the Legal Profession Act” (National Competition Policy Review) determined that despite the earlier attempt at liberalizing the rules for MDPs, the rules governing MDPs were still anti-competitive and should be repealed. As a result, in December 1999 the rules were amended such that it was no longer necessary for lawyers to retain the majority voting rights in an MDP, and the net income of the MDP could be shared by lawyers and non-lawyers without restriction.

Despite the availability of these alternative forms of legal structures, lawyers continued to be reluctant to move away from the traditional structure of sole practitioner and partnerships. The primary concern was about the possibility of conflicts that might arise if they entered into business arrangements with non-lawyers. In addition many lawyers perceived that “it would not be possible to maintain professional and ethical standards if lawyers entered into business arrangements with members of other occupational groups.”² Therefore, the use of MDPs and solicitor corporations was not widely embraced by the NSW legal profession until 2001 with the advent of new legislation permitting incorporation.

On 1 July 2001 the *Legal Profession (Incorporated Legal Practices) Act 2000* (“the 2000 Act”) and the *Legal Profession (Incorporated Legal Practices) Regulation 2001* (“Regulations”) came into force in New South Wales. The 2000 Act and Regulations enable providers of legal services in NSW to incorporate by registering a company with the Australian Securities & Investment Commission (ASIC). Once registered with ASIC, the rules that govern the framework of the ILP are found not only in the company’s constitution, the Legal Profession Act and the Regulations, but also in the Corporations Act.³

In first introducing the Act as a Bill into Parliament the New South Wales

1. The Hon Jeff Shaw QC MLC, *Incorporation of Legal Practices under the Corporations Law*, 68 LAW SOCIETY JOURNAL (NSW), 67, 67-70 (1999).

2. Parliament of NSW, Legislative Council Hansard, 23 June 2000 at 7624.

3. The Corporations Act 2001 (Cth) was previously known as the “Corporations Law.”

Attorney General said:

“The Government is of the view that incorporation will lead to more transparent management structures in law firms, because of the requirements of the Corporations Act. Within a corporate structure, the accountability of individuals for the management of the practice will be enhanced, and this is likely to lead to better delineation of responsibilities within firms and to more efficient service provision.”⁴

OLSC statistics show a steady stream of NSW firms have been incorporating since 2001. At present the total number of ILPs in NSW as at 17 April 2007 is 745 with 629 of these having finalised the Law Society approval process.

Based on last years' Law Society figures, there were 4278 firms in New South Wales (including both traditionally structured firms and ILPs) as at December. Assuming little movement in this figure, we can estimate that ILPs now compose about 18% of all firms in NSW (up from 16% in January 2007). We understand that this figure is similar for other States that have now legislated to allow incorporated legal practices.

At the time of writing these notes there are 43 multi-disciplinary practices in New South Wales, and the number appears to be decreasing.

Under none of the recent legislative reforms which allow incorporation in various forms in New South Wales, have multi-disciplinary practices been popular. This is perhaps due to the fact the often cited benefits of “one stop shopping” may not deliver the level of benefits desired. The present multi-disciplinary practices in New South Wales are largely made up of two different groups:

- Property services firms. These practices tend to have a combination of solicitors, real estate agents, accountants or developers, sometimes associated with fund-raisers or local government experts.
- Financial services practices. These practices can include solicitors, tax advisors, accountants and investment or financial consultants. In Australia, financial services practices (other than incorporated legal practices) are regulated under the Financial Services Reform Act. Law firms are exempt from this legislation as are multi-disciplinary practices which have incorporated as ILPs providing financial services except where those financial services would include mortgage practices and/or the development of taxation or financial schemes.

The Law Council of Australia and the Standing Committee of Attorneys General undertook, over several years, a project known as the Model Laws Project. The outcome of this project was the development of a set of model laws relating to the regulation of the legal profession, and these model laws

4.Parliament of NSW, *supra* note 2, at 7624.

received the assent of all Attorneys-General in Australia in June 2004. The LPA represents (in part) the adoption by NSW of the model laws.

The model laws contain, among other things, core provisions allowing the incorporation of legal practices in all jurisdictions in Australia, on terms identical to the NSW model.

In addition to NSW, other jurisdictions have enacted legislation to give effect to the model laws, including to permit incorporation, some of which have recently come into force.

While not all jurisdictions have yet enacted legislation to give effect to the model laws, all Australian states and territories now permit corporations as defined by the Corporations Act to provide legal services. We are therefore very close to incorporation being available Australia wide on terms substantially the same as the NSW model

3. The current legislative regime

The principal legislation governing the legal profession in New South Wales is the *Legal Profession Act 2004 (NSW)* (the LPA) and the *Legal Profession Regulations 2005*.

Pursuant to Part 2.6 of the LPA 2004 a legal service provider is permitted to incorporate and provide legal services either alone or alongside other legal service providers who may, or may not be “legal practitioners.” The primary structural requirement of an ILP is that at least one legal practitioner director must be appointed.⁵ The legal practitioner director is generally responsible for the management of the legal services provided in NSW by the ILP. The legal practitioner director is defined as a director of an incorporated legal practice who is an Australian legal practitioner holding an unrestricted practicing certificate. Section 142(2) provides that it is an offence if an incorporated legal practice does not have any legal practitioner directors for a period exceeding seven days.

Section 143 of the LPA 2004 provides that Australian legal practitioners who provide legal services on behalf of an incorporated legal practice in the capacity of an officer or employee of that practice, maintain the professional privileges of an Australian legal practitioner and must therefore comply with their usual professional obligations. In addition to the normal duties owed by partners and employed solicitors the LPA 2004 and the Regulations provide for additional responsibilities for legal practitioner directors of ILPs.

The additional responsibilities include:

- (i) A general responsibility on the solicitor director for management of the legal services provided by the incorporated legal practice - this responsibility probably does not extend beyond those general

⁵ Section 140(1) of the LPA 2004.

responsibilities that partners have to the general management of their partnership.

- (ii) The implementation and maintenance of “appropriate management systems” to enable the provision of legal services in accordance with the professional obligations of solicitors and the other obligations imposed by or under section 140(2) and (3) of the LPA 2004. Failure to implement and maintain “appropriate management systems” is declared to be professional misconduct.
- (iii) A responsibility to report to the Law Society any conduct of another director of the practice that has resulted in or is likely to result in a contravention of that person’s professional obligations or other obligations imposed by or under the Act.⁶
- (iv) Report to the Law Society any professional misconduct of a solicitor employed by the practice.
- (v) An obligation to take all action reasonably available to deal with any professional misconduct or unsatisfactory professional conduct of a solicitor employed by the practice.⁷

A firm wishing to incorporate must liaise with ASIC and comply with that organisation’s requirements to create a corporate vehicle. It must also notify the Law Society of New South Wales (the Law Society) of its intention to commence trading as an ILP.

While the Law Society provides general information to the potential ILP about the advantages and disadvantages of incorporation, this does not extend to any firm specific due diligence. The Law Society role extends only to ensuring that certain documentation (including a certificate of incorporation, a certificate of insurance and a company search which reveals the appointment of at least one solicitor director with an unrestricted practising certificate) is produced. No analysis of the appropriateness of any particular firm incorporating is undertaken, either by the Law Society or the OLSC.

This deficiency notwithstanding, the OLSC has worked closely with the Law Society, LawCover, the provider of professional indemnity insurance in New South Wales, and the College of Law, the largest provider of continuing legal education in New South Wales, to develop an educative programme to assist legal practitioner directors to comply with their professional responsibilities.

The OLSC has, in practice, by agreement with the Law Society, assumed the role of auditing ILPs for compliance with the LPA and Regulations pursuant to sections 140(3) and 670 of the LPA. The test for compliance is found in part in s 140(3) of the LPA, which provides that a legal practitioner director must ensure that “appropriate management systems” are implemented and maintained by the ILP. A failure to do so is capable of being professional

⁶ Section 140(4) of the LPA 2004.

⁷ Section 141 of the LPA 2004.

misconduct.

Audits are a necessary part of the OLSC's regulatory powers and the OLSC may audit an ILP or any legal practice in New South Wales pursuant to its powers under the LPA. In particular where the OLSC is concerned about the appropriateness of an ILP's management system, the OLSC may commence an audit.

The ultimate objective with respect to auditing any law practice is better practice management and compliance with the LPA⁸. The OLSC acts as a guide in this respect although disciplinary action can be taken against the Legal Practitioner Director as a result of an audit.

The OLSC is able to audit a practice's systems; files and behaviour reflected in a returned self-assessment form. An ILP can be also subject to a Compliance Audit which refers to compliance with the LPA, the Regulations and the Professional Conduct and Practice Rules and is not limited to management systems.

The LPA does not define "appropriate management systems." Accordingly, the OLSC has collaborated with the Law Society, the College of Law and LawCover to determine the objectives to be met to help ascertain whether an ILP has "appropriate management systems" in place. The approach formulated is an "education towards compliance" strategy in which ILPs must show that they have procedures in place which evidence compliance with what the OLSC considers to be the ten objectives of a sound legal practice.

The ten objectives or "ten commandments" as they have become known, are as follows:

1. Competent work practices to avoid negligence
2. Effective, timely and courteous communication
3. Timely delivery, review and follow up of legal services to avoid instances of delay
4. Acceptable processes for liens and file transfers
5. Shared understanding and appropriate documentation from commencement through to termination of retainer covering costs disclosure, billing practices and termination of retainer
6. Timely identification and resolution of the many different incarnations of conflicts of interest including when acting for both parties to a transaction or acting against previous clients as well as potential conflicts which may arise in relationships with debt collectors and mercantile agencies or conducting another business, referral fees and commissions etc.
7. Records management which includes minimising the likelihood of loss or destruction of correspondence and documents through appropriate document retention, filing, archiving etc and providing for

⁸ There are two types of audit that can occur under the LPA. The first is a general power to audit any law practice regardless of entity status (section 670(1) (Compliance Audit)). The second is an audit of an ILP which is broken into two components – compliance of the ILP with the requirements of Part 2.6 of the LPA and management of the provision of legal services (section 670(2)(a) & (b) (ILP Audit)).

- compliance with requirements as regards registers of files, safe custody, financial interests
8. Undertakings to be given with authority, monitoring of compliance and timely compliance with notices, orders, rulings, directions or other requirements of regulatory authorities such as the OLSC, Law Society, courts or costs assessors
 9. Supervision of the practice and staff
 10. Avoiding failure to account and breaches of s61 of the Act in relation to trust accounts.

To enable legal practitioner directors to assess their management systems, a standard “self-assessment” document has been developed and is sent to all legal practitioner directors as part of the impending ILP review programme. It is acknowledged that since ILPs vary in terms of size, work practices and nature of operations, an approach of “one size fits all,” requiring the fulfillment of uniform criteria, would be inappropriate.

Instead, the self-assessment document contains concepts to consider when addressing each of the ten objectives and then examples of what an ILP *may* do to evidence compliance with each of the objectives. For example, under the objective of maintaining “competent work practices to avoid negligence,” a concept to consider is that, “fee earners practise only in areas where they have appropriate competence and expertise.” The self-assessment document then suggests that an example of a procedure that will evidence compliance is that there is “a written statement setting out the types of matters in which the practice will accept instructions and that instructions will not be accepted in any other types of matters.” The self-assessment document also contains a column within which the legal practitioner director can rate the ILP’s compliance with each of the ten objectives as either “Compliant,” “Non-Compliant” or “Partially Compliant.”

Our approach to the regulation of ILPs – self-assessment based on the “ten commandments” – is essentially a systematisation of ethical conduct. Each of the “ten commandments” refers to certain behaviours which, if followed, will result in an ethical outcome. In this way, the management systems the OLSC oversees and enforces are themselves value-based, and can be distinguished from those professional standards which seem to have existed in a vacuum in other industry regulating regimes.

This approach sits well within the OLSC’s general philosophy of regulation that a regulator should:

- (i) ensure compliance with the relevant laws, rules and regulations;
- (ii) consistently questions those laws, rules and regulations both for relevance, and in assessing their impact upon both the profession and the community at large, and to make appropriate recommendations for change or improvement; and
- (iii) educate the profession and consumers of legal services with the goal of creating a culture within the profession whereby compliance itself becomes cultural. Once such a culture is achieved, it follows that there will be a reduction in the number of complaints received

by my Office. In fact, it has been a long standing stated aim of my Office to reduce the number of complaints about lawyers.

In order to manage the self-assessment process more effectively and efficiently, the OLSC has commenced a project to implement a database to automate the management of ILPs in NSW. The core functionality of the ILP system will be that it manages the self-assessment process by ILPs of the practice's management system. The new system will still require an ILP to rate its compliance against the ten management objectives to meet the requirement of an appropriate management systems under the LPA.

NSW has taken the lead in developing the ILP system and is working with the Legal Services Commissioners in Queensland and Victoria in arriving at common business rules on how ILPs are managed across the states. OLSC has engaged a vendor to build the system to manage ILPs and a portal for the exchange of information between OLSC, ILPs and other stakeholders.

4. Advantages and Disadvantages of Incorporation

Advantages

(a) Limited Liability

One of the major reasons firms choose to incorporate is because once a company is registered with ASIC, the capital in the company is constituted by one or more shares and each shareholder's liability is limited to the shareholder's investment in the corporation. Limited liability is a benefit for the former partners of a legal partnership who opt to incorporate. For the first time, the former partners—now shareholders in a company—can feel that their liability for their business debts is limited.

(b) Asset Protection

Prior to registering a company with ASIC, a company constitution must be drafted. In drafting a constitution, the directors and shareholders may be given any combination of rights of ownership, control and distribution in the profits of the company by choosing the types of shares that will constitute the company. This can lead to protection of personal assets where creditors are concerned.

Conversely, in a traditional partnership structure a creditor that obtains judgement against the partnership can enforce the judgement against the partners personally. In general terms, therefore, creditors of an ILP, where there is a suitable structure, will have access only to the business assets of the firm rather than the personal assets of shareholders.

(c) Share ownership

Firms also choose to incorporate because a corporate structure also offers flexibility in terms of share ownership. For example, shareholders may be

non-lawyers including employees, family members, other companies or trusts. Furthermore, if non-lawyer shareholders are appointed to the board of directors, the ILP could benefit from the broadened range of skills that are brought to the ILP's management.

From a commercial perspective, ownership of a share also tends to be more attractive than an interest in a partnership given the transferability of shares. In this respect, a shareholder may sell his/her existing shares, buy further shares, and retain shares to supplement retirement income or transfer shares by way of testamentary gift. For the ILP, shares also enable the company to reduce its share capital and thereby obtain greater control over the company by way of an "off market" or, in the case of a public company, an "on market," share buy back.

In addition, ILPs offer flexibility in allowing for rainmakers or others who bring work or add value to the firm without being able to show thus specific amount of profit that their activities create (eg a lawyer's monthly costs tabulation).

(d) Capital raising

Another reason as to why firms choose to incorporate is that they are able to expand without using debt to do so. Under a corporate structure additional capital may be raised through various mechanisms. For example, a company may grant security over its assets or issue unsecured debentures, bills of exchange and other debt securities. A company can also raise equity capital by floating on the stock exchange or retaining profits, rather than distributing dividends to its shareholders. While such debt and equity raising facilities are available to a corporation such as an ILP, they are not available to a partnership.

(e) Taxation advantages

Incorporation also provides significant financial advantages for shareholders and directors. For example, in Australia a company must pay federal income tax on its taxable income at 30% per annum while the highest level of personal tax is generally set at 47%.⁹ After paying such tax, a company then has discretion as to whether or not to distribute its net profits by way of dividends. If the company does pay tax and distributes an after-tax or "franked dividend" to shareholders, the shareholder is entitled to an imputation credit for the tax paid when calculating their taxable income in their personal tax return.

(f) Better Management

Incorporation provides a more efficient management system which is of particular importance in large partnerships. A corporate structure permits the division of decision-making power between directors, shareholders and employees to be tailored to the needs of an ILP. Such unbundling of roles means enhanced accountability for workers and a subsequent tightening of control over different practice areas, but less autonomy for the former partners

9. The New Business Tax System (Income Tax Rates) Act (No. 1) 1999 (Cth) reduced the company tax rate to 30% from 34% for the 2001-2002 and later years of income.

of a firm. A separation of roles also means that those contributing to the success of the ILP as solicitor directors, managing directors and employees are more accurately remunerated according to their performance.

Additionally incorporation offers management options that are more flexible than those available under a partnership structure. For example, while a non-lawyer Chief Executive Officer (“CEO”) may be appointed either by a partnership or an ILP to head up the business, a CEO’s management autonomy is often impeded in a partnership by the wishes and desires of the individual partners. In contrast, a CEO of an ILP operates in a bona fide corporate environment and is answerable only to the board of directors.

The appointment and removal of a legal practitioner director is also much easier under a corporate structure.

(g) Employees

Evidence suggests that employee motivation and loyalty can be more profound in companies where staff incentive schemes such as bonus shares or options are offered to employees.

Disadvantages

(a) Ethical conflicts

The main disadvantage of incorporation is the inevitable conflict of economic versus ethical issues. In this regard, in a law partnership, a partner has an overriding duty to the court. In a corporate structure, directors have an overriding duty to the company and its shareholders.

For example, where an incorporated legal practice decides to settle a major piece of litigation as they decide it is in the best interest of the client to do so, the practices shareholders may suffer loss of potential profit. Under Corporations law the shareholder could sue the directors for such a decision. The challenge for regulators of the legal profession is to ensure, to the extent possible, that a lawyers primary duty to the Court or the client will prevail in any clash with a director’s duty to the corporation and shareholder.

Also troubling is the potential for breaches of a client’s legal professional privilege in incorporated legal practices where non-lawyers are intimately engaged in the delivery of the entities services. This will create new concerns over the use of ethical screens (Chinese walls).

(b) Payroll tax issues

A second disadvantage of incorporation relates to payroll tax issues. Where a legal practice incorporates, partner drawings and profit shares will be replaced by salaries and dividend distributions. To the extent they are replaced by salaries and total annual salaries and wages are more than \$600,000 per annum, payroll tax will be increased by those additional salaries to partners. Dividend distributions are not subject to payroll tax.

(c) Stamp duty issues

A third disadvantage of incorporating is the fact that stamp duty is not specifically exempted under the LPA 2004.

(d) Reporting requirements

In terms of financial reporting, an ILP must comply with the financial reporting requirements set out in the Corporation Act. Such requirements usually entail regularly submitting information regarding the company's financial position and the remuneration of solicitor-directors to ASIC.

In a similar way, if an ILP is floated on the ASX it must also comply with the ASX's rules with respect to financial reporting. In contrast, a partnership or sole practitioner is not required to disclose any financial information to the ASIC and ASX, thereby ensuring that a veil is effectively placed around the financial affairs of such legal practices.

(e) Transparency and continuous disclosure

We understand that some law firms are uncomfortable about the level of transparency required for listed companies in terms of directors (partners) shareholding, salaries or take home pay.

The need for continuous disclosure can also create problems, not least with regard to the traditional concepts of legal professional privilege and confidentiality often required by clients as to their identity.

5. Implications of the listing of law firms on the stock market

As stated at the beginning of this paper the advent of Slater & Gordon listing on the ASX has created several major issues for regulators of the legal profession to consider:

(a) Interplay between LPA 2004 and the Corporations Law

Australia is a Federation of seven jurisdictions with a centralised Federal Government and State and territory governments. Australia is a Parliamentary democracy.

In the sphere of corporate law in Australia, the Corporations Act advocates for the paramountcy of the rights and protection of shareholders. Accordingly, there is a latent tension between a solicitor's professional obligations and a solicitor's duties to a company's shareholders.

Historically, Corporations law was a power largely held by the States. In 2001 after a major controversy and debate which ran for decades, the States seeded their Corporations power to the Commonwealth so that uniformity throughout Australia could be achieved.

Prior to this, the Legal Profession Act 1987 (NSW) (LPA 1987) explicitly stated that where an inconsistency existed in the Corporations Act 2001 (Cth) (Corporations Act) and the LPA 1987, then the LPA 1987 would prevail to the extent of that inconsistency (section 47S).

The Legal Profession Act 2004 (NSW) (the LPA) attempts to incorporate the same concept by providing that Corporations Act displacement provisions are to be established by the Legal Profession Regulation 2005 (NSW) (the Regulation) (s163). The Regulation has not established any displacement provisions.

The OLSC has become aware that tension may arise between a practitioner's duties owed under the LPA and the requirements of a director, officer or employee under sections 181 - 184 of the Corporations Act.

We are firmly of the view that it is essential that the provisions of the LPA prevail over provisions of the Corporations Act to the extent of any inconsistency. The inconsistency could be apparent in circumstances where the practitioner's duty to the court or client, which must be paramount, causes a detriment to the corporation, thereby breaching the practitioner's duty to the corporation as established by the Corporations Act.

An example of such inconsistency could be as basic as settling major litigation in accordance with the lawyer's duty to the court and the client but thereby causing a detriment to the corporation because of the diminution in fees earned.

The OLSC is presently holding discussions with the NSW State Government with a view to displacing the Corporations Act to the extent of any inconsistency with the LPA 2004 to ensure that the hierarchy of a lawyers duties; court, client then shareholder, will receive clearer legislative backing.

(b) Conflict of interest/duties and loyalty

In Australia a legal practitioner's primary duty is owed to the court. This then poses a problem for a listed corporation whose primary duty is to its shareholders.

Realising the possibility of this conflict between the duties owed to the company and shareholders and the duties owed to the court and to clients the OLSC worked together with Slater & Gordon prior to listing to ensure that Slater & Gordon's prospectus, constituent documents and shareholder agreements dealt with the issue.

As a result, the Slater and Gordon prospectus states:

The constitution states that where an inconsistency or conflict arises between the duties of the company (and the duties of the lawyers employed by the company), the company's duty to the court will prevail over all the duties and the company's duty to its clients will prevail over the duty to shareholders.

The primacy of a lawyer's duties to the court, as stated in the prospectus, are also reflected in Slater & Gordon's constituent documents and shareholder agreements.

(c) Goodwill of law firms

The listing of law firms also raises the issue as to whether law firms actually have any goodwill. Ascertaining the true worth of a law firm is very challenging

Slater & Gordon managed to convince prospective investors that they indeed have goodwill due to their significant market standing (branding) but it is doubtful that there are many law firms that would be able to demonstrate such standing in Australia.

Slater & Gordon are a niche national firm that has built up a powerful reputation and profile in the Australian legal market. They enjoy a strong position in the personal injuries and class action litigation market in Australia. Furthermore Slater & Gordon's prospectus states that they are one of the most recognisable names in Australia and that a study commissioned in 2004 found that general public awareness of the Slater & Gordon name was 60% nationally and 83% in Melbourne.¹⁰

There are very few firms in Australia that have built up such a powerful brand.

(d) Value of investing in a law firm

Another interesting issue raised by law firms listing is the value of investing in such a firm that decides to list. The question of whether people would actually be interested in investing in a listed law firm is still open. The stock market as we know it is a highly volatile and sensitive arena. So too are many law firms. Law firms are in a constant state of change with staff moving across firms and increasing attrition rates amongst employees.

Interestingly, Slater & Gordon did not seek to raise their capital directly from the market. They went to institutional investors and staff.

It is also interesting to note that Slater & Gordon's Prospectus states as one of the investment risks is the potential attrition of clients in addition to the possible attrition of senior practitioners and other legal staff.

(e) Incorporation as an exit strategy

Listing also raises concerns about the use of listing as an exit strategy for partners/legal practitioner directors. Listing on the stock market is a great way for partners and legal practitioner directors of an incorporated legal practice to make money if they decide to leave the practice. Once all the money has

¹⁰ Slater & Gordon Prospectus at p.10

been made in listing and the directors have left it is doubtful that there would be any value left for subsequent directors/shareholders.

The Slater & Gordon Prospectus attempts to placate some of these concerns by having staged processes by which the founding directors are required to stay for between three to six years to get the full economic value of their shareholding.

(f) Income splitting – sharing of fees with non-lawyers

Perhaps the biggest issue for US regulators is the concern created by the income splitting provisions or the sharing of fees between lawyers and non-lawyers in incorporated practices in Australia and the UK.

As discussed earlier, the legislative history which has allowed the creation of multi-disciplinary practices in New South Wales has been in place for almost 10 years, with the ability for such practices to incorporate now in place for six years. With the move to a national legal services market in Australia the ability for firms to list including multi-disciplinary practices will be available in all states and jurisdictions by the end of 2007.

Income splitting, as known in the US, will now be available for incorporated law firms not just where those firms are multi-disciplinary but where administrative and other non-legal staff are able to purchase shares in an incorporated legal practice which is purely a legal practice. This will produce difficulties in the US in how they characterise Australian (and soon UK) lawyers who wish to practice in America, even pro hac vice.