

The legal needs of small businesses – summary

briefing for policy makers

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 owner-managers, were most likely to experience problems
- **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
- **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

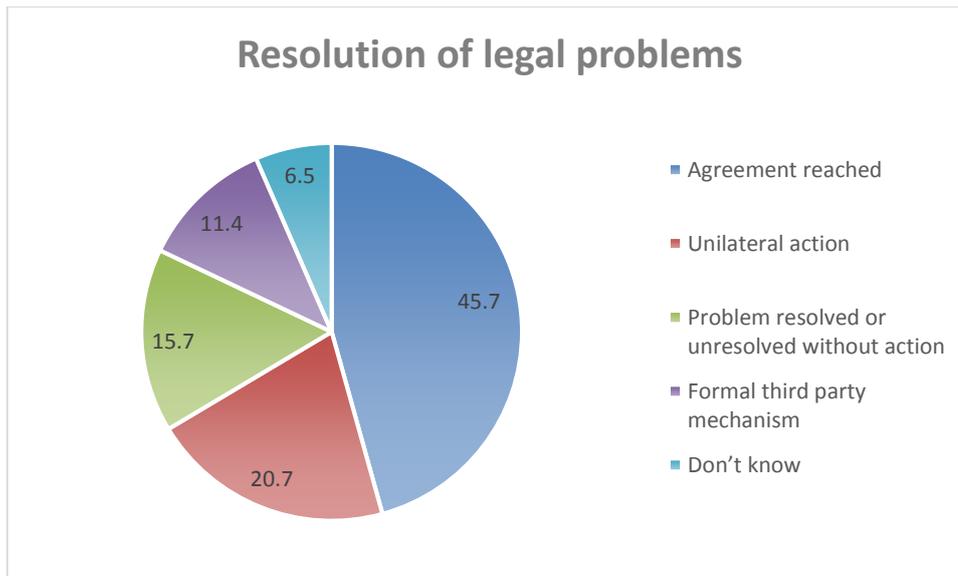
- **Satisfaction that law and regulation provide a fair trading environment increased from 30% in 2013 to 45% in 2015** – improving economic conditions as well as improvements in the regulatory environment may explain this change

Implications for Government departments / policy makers

1. It has been a strategic aim of successive governments to make the UK the best place in the world to start and grow a business. Small firms are integral to this aim, as demonstrated most recently in the Enterprise Bill (2015) which seeks an improved regulatory environment and a better understanding among small businesses of where to seek support when they have disputes with other businesses.
2. For policy makers, this new research is important: first in terms of helping to identify business problems that derive from the environment within which small firms operate; and second by providing evidence on small firms' advice seeking and take up in dealing with legal problems, including advice from government support agencies.

Impact of legal problems faced by small businesses

3. The number of legal problems faced by small firms has reduced significantly over the last two years reflecting better trading conditions. Slightly less than a third (29%) of respondents reported one or more problems in the past 12 months, compared with 37% in the 2013 Survey.
4. The most common problems were related to trading: almost 20% of firms reported such a problem, followed by employment (6.5%), taxation (6.0%) and regulation (5.4%). Given plans to create a Small Business Commissioner to help tackle payment disputes and other unfair practices, it is important to note that the sources of problems faced by businesses were mainly with other businesses (49%). This was followed by individual members of the public (18%), government (16 %) and employees (10%).
5. Government policies place emphasis on alternatives to court for resolving disputes. Most commonly, issues were resolved by the parties, either in agreement or by one side acting unilaterally, rather than through legal means or through the involvement of third parties. Only 2.3% of problems were resolved by a court or tribunal, reduced from 3.4% in the 2013 Survey. Generally the findings mirror those in the 2013 Survey: a large proportion of the firms try to settle informally and succeed in doing so.



6. Larger small firms are much more likely to encounter problems than smaller ones. This is not surprising since larger small firms are more likely to experience a broad range of internal issues and have relations with a wider group of external stakeholders. There is also a dynamic element to this point. As a firm grows it will encounter additional, often new, legal issues and problems. Particular types of problems are met at different stages of enterprise development, such as employment issues and intellectual property management matters. This also suggests that the demand for specific types of legal services varies with size of firm. Certain services will be required early on as the business grows. BIS and other providers need to bear this in mind when providing focused support.

7. There is a marked variation in the propensity of different types of business owner to experience legal problems. Specifically black and minority ethnic (BME) owner managers, or owner managers with a disability, are significantly more likely to experience legal problems than other types of business owner. These two groups are also more likely to access legal advice. Closer analysis of the data suggests these differences are not explained by other factors, for example as a result of BME owner managers running businesses in certain sectors or of a specific size. Further qualitative data is required to provide informed insight into the reasons for this.

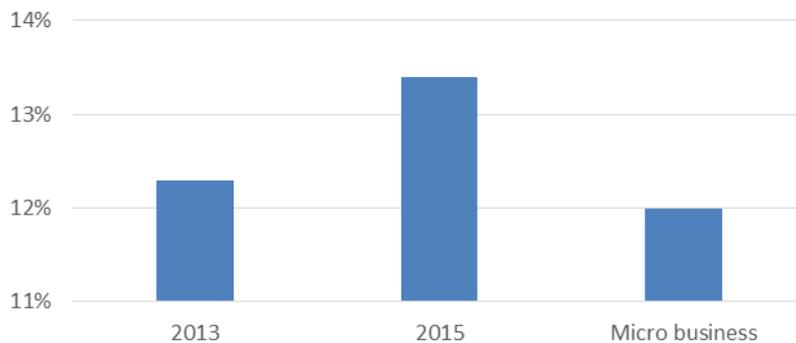
8. Approximately a half of all firms reporting a problem reported tangible impacts on business performance. The most frequently cited impact was loss of income (26%), followed by loss of customer/contract (9%). By calculating the mean (average) income loss across the whole sample (£1,881) and multiplying it by the total small business population in the UK (5,204,915), the total value of loss to small businesses is estimated as £9.79 billion in 2015.

9. The impact of legal problems on small firms is not only financial. They also have implications for the health and well-being of business owners and their staff. 20% of respondents reported between one and three prompted health issues as a result of a legal problem. Stress-related illnesses were reported by 16% of respondents. These health problems are likely to have knock-on impacts on health services and productivity, although these impacts would be very difficult to quantify.

Evidence of unmet legal need

10. The vast majority of small businesses (87 percent) do not have any internal legal capacity, or indeed an external legal capacity. The analysis shows that the demand for legal advice by small firms derives from a business problem that cannot be resolved by themselves, in the first instance, or by other trusted parties. In other words, small firms tend not to anticipate legal problems and choose to deal with them as and when they occur.
11. Despite this finding, one of the most striking results is that very small firms are not accessing external legal services, at least via lawyers, to any great extent. This may suggest that they are not resolving their problems satisfactorily. Only around 20% of those with a reported legal problem drew upon the legal profession. However, 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.
12. An unequivocal finding is that cost is a major deterrent to taking up legal advice. Almost half of respondents disagreed with the statement that *'Lawyers provide a cost effective means to resolve legal issues'*; and only 13% agreed or strongly agreed with the statement. This compares to 12% in the 2013 run of the 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'



13. Even so, although accessing legal advice may be challenging for some firms, because of its high cost, few firms reported that not being able to access legal advice had affected the growth of their business. Less than 5% of the sample as a whole, and 10% of those reporting a business problem disagreed or strongly disagreed with the statement that *'Not being able to find a suitable legal services provider when I need one has affected the growth of my business.'*
14. On the positive side, between 2013 and 2015 small business owners were more confident with respect to the fairness of the legal and regulatory environment for their business – increasing from 30% to 45%. This may be a reflection of the policies by successive governments to reduce the regulatory burden as well as businesses experiencing an improvement in the economic conditions in which they operate.
15. The legal profession needs to make stronger strategic ties with other key business support providers including accountants, national agencies, local authorities, trade bodies and Chambers of Commerce. This would help to put legal services providers on the map, so to speak, and also help to provide the basis of a network of contacts. Government departments are in a good position to play a role in brokering network relations between small business representative organisations and other intermediaries. This could form the basis of a strategy designed to increase engagement of legal services providers with very small businesses.