



The Law Society

The Law Society

Report and Financial Statements

31 December 2004

The Law Society

Report and financial statements 2004

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Council's report and statement of the Council's responsibilities

The Council of the Law Society (the "Society") presents their annual report together with the financial statements and auditors' report, for the year ended 31 December 2004. The consolidated financial statements include the financial statements of the Law Society and its subsidiaries (together the "group").

Constitution

The Society is incorporated by Royal Charter in Great Britain.

Principal activities of the society

The Society is the regulator of and representative body for solicitors in England and Wales. It serves society by working to improve access to the law. It provides services and support for solicitors themselves and sets and enforces the standards that underpin solicitors' work, maintenance of which is crucial to the profession's reputation.

Auditors

Deloitte & Touche LLP have expressed their willingness to continue in office as auditors and, a resolution to re-appoint Deloitte & Touche LLP as the Society's auditors will be proposed at the forthcoming Annual General Meeting.

Approved by Council of the Law Society and signed on behalf of the Law Society on 12 May 2005

E Nally

PRESIDENT

G Sandbrook

TREASURER

Statement of the Council's responsibilities

The Council is required under the bye-laws of the Society to cause proper accounts to be kept. In the exercise of this responsibility the Council has, as permitted by the Society's General Regulations, delegated this duty to the Main Board and the Finance & Resources Board which are thereby responsible for the preparation of the financial statements of the Society for each financial year which give a true and fair view of the state of affairs of the Society and the group as at the end of the financial year and of the surplus or deficit of the Society and of the group for that period. In preparing those financial statements, the Main Board and the Finance & Resources Board:

- have selected suitable accounting policies and then applied them consistently;
- made judgements and estimates that are reasonable and prudent;
- stated whether applicable accounting standards have been followed; and
- prepared the financial statements on the going concern basis.

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Council's report and statement of the Council's responsibilities (continued)

The Main Board and the Finance & Resources Board are responsible for ensuring proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Society. They are also responsible for the system of internal control, for safeguarding the assets of the Society and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors of the companies controlled by the Society, and whose accounts are consolidated with those of the Society, are required under the Companies Act 1985 to prepare financial statements, keep proper accounting records and safeguard the assets of the companies in a manner comparable to that described above.

The Main Board was formed on 1 July 2001. Its membership from 1 January 2004 to 31 December 2004 was as follows:

| | |
|-------------------------------|---|
| Edward Nally | (President from 15 July 2004, having been Vice President) |
| Peter Williamson | (President until 15 July 2004) |
| Kevin Martin | (Vice President from 15 July 2004, having been Deputy Vice President) |
| Fiona Woolf | (Deputy Vice President from 15 July 2004) |
| Angus Andrew | (resigned 5 March 2004) |
| Hilary Siddle | (retired 30 June 2004) |
| Rodney Warren | |
| Andrew Holroyd | |
| Geoffrey Sandercock | (Treasurer) |
| Richard Hegarty | |
| Helen Davies | (appointed 1 July 2004) |
| Alexandra Marks | (appointed 1 July 2004) |
| Sue Nelson | (appointed 16 July 2004) |
| Janet Paraskeva* | (Chief Executive) |
| Evlynn Gilvarry* (non-voting) | (Director of Representation and Law Reform) |
| Bruce Minty* (non-voting) | (Director of Finance and Resources) |
| Russell Wallman* (non-voting) | (Director of Strategic Policy/Senior Director Regulation from 28 February 2005) |
| Stuart Bushell* (non-voting) | (Director of Regulation, Standards until 28 February 2005, Chair of Transition Board from 28 February 2005) |
| Alison Crawley* (non-voting) | (Director of Regulation, Compliance) |
| Frances Low* (non-voting) | (Director of Legal Services) |

* denotes members of the Senior Management Team at 31 December 2004.

The membership of the Finance & Resources Board from 1 January 2004 to 31 December 2004 was as follows:

| | |
|---------------------|---------------------------------|
| Geoffrey Sandercock | (Chair) |
| Robin ap Cynan | (re-elected 1 July 2004) |
| Robin Healey | (resigned 15 July 2004) |
| Derek French | (term expired 26 November 2004) |
| Andrew Caplen | (term expired 30 June 2004) |
| John Pickup | |
| Phillip Hamer | |
| Peter Williamson | (appointed 1 July 2004) |
| Bob Heslett | (appointed 16 July 2004) |
| Michael Franks | (appointed 25 November 2004) |

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Council's report and statement of the Council's responsibilities (continued)

The membership of the Audit Committee from 1 January 2004 to 31 December 2004 was as follows:

| | |
|------------------------------|---|
| Stephen Brooker | (Chair from 27 February 2004) |
| Simon Osborne | (Acting Chair until 26 February 2004; retired 26 February 2004) |
| Richard Bagley | (Vice Chair) |
| Peter Davies | (term expired 31 August 2004) |
| Michael Lawson | |
| Huw Thomas [#] | |
| Pauline McBride [#] | (resigned 16 December 2004) |
| Sunil Kambli | (resigned 3 January 2005) |
| Kevin Mortell | |
| Geoffrey Mitchell | (appointed 22 September 2004) |
| Stuart Collins | (appointed 24 February 2005) |
| Sue Carter [#] | (appointed 24 February 2005) |

Simon Osborne assumed the role of acting Chair pending the recruitment and appointment of a permanent Chair.

[#] Council members of the Audit Committee. The remainder are independent members.

The membership of the Remuneration Committee from 1 January 2004 to 31 December 2004 was as follows:

| | |
|----------------------------------|---|
| Sally Irvine ⁺ | (Chair from 24 February 2005) |
| Colin Harris ⁺ | (Chair until 24 February 2005; resigned 24 February 2005) |
| Geoffrey Sandercock ⁺ | |
| Fiona Woolf ⁺ | |
| Richard Bagley | (resigned 6 September 2004) |
| Martyn McCarthy | (resigned 31 March 2005) |

⁺ Council members of the Remuneration Committee. The remainder are independent members.

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Corporate governance

Corporate governance is the system by which companies are directed and controlled. The Cadbury Committee sought to strengthen the financial aspects of corporate governance by reviewing the structure and responsibilities of boards and directors, the role of auditors and the rights and responsibilities of shareholders. This was supplemented by the Greenbury and Hampel Committee reports which, together with the Cadbury guidance, were amalgamated to form the Combined Code (“the Code”).

The Society shares the Code’s aims and has voluntarily decided to comply with its requirements, as indicated by the formal statements elsewhere in these accounts. As the management structures and governance of the Society are not the same as that of a listed company, some of the Code’s provisions are not directly applicable. Full compliance is therefore not possible.

Council Members

The Society has a two-tier governance scheme, with the Council maintaining strategic oversight but delegating most functions to the Main Board. In a wider sense all Council Members can be taken as directors for the purposes of the Code, though for most of the specific functions in the Code the Main Board is the equivalent of a plc Board of Directors. Council members are elected for a fixed term, and the Council has specific responsibilities (governed by statute and the Society’s Charter and Regulations). The Council, the Office Holders and the Chief Executive have separate responsibilities. There is no direct equivalent of non-executive directors, although the Council has five Lay members and, its Remuneration Committee and Audit Committee have two and six Lay members respectively.

Remuneration

The Council Members only receive expenses; they are not remunerated. However, there are schemes in place for compensating the following groups:

- Office Holders or their Firms or employers; and
- the five Lay Members.

These schemes are approved by the Council.

A Remuneration Committee advises on any recompense made to Council Members, and determines and approves the remuneration packages of the Chief Executive and Senior Management Team.

Accountability and Audit

The provisions of this section of the Code are all met where applicable, except that there are no interim or price-sensitive reports to include in the assessment of the Society’s financial position and prospects made in the Financial Statements. There is an organisational structure with defined roles for the Main Board, the Finance & Resources Board, and the Audit Committee. There is also an established Internal Audit unit. For 2004 an annual review of internal control has been undertaken. The Internal Control Statement resulting from this review appears below.

Audit Committee

The members of the Audit Committee are listed on page 2 and 3. The Committee met six times in 2004. Its terms of reference are consistent with the Code, as far as possible, given the Society’s management structure and governance, and include responsibility for the review of internal control and the overseeing of action required as a result of matters raised by the external auditors. The Committee also reviews the plans and monitors the progress of the Internal Audit Unit.

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Corporate governance (continued)

Internal Control

The Society recognises the potential value of the internal control regime in the Combined Code, and decided to adhere voluntarily to all those parts of it which are applicable.

In accordance with this approach the Society reports as follows:-

Although the Council is the Law Society's governing body, it gave specific responsibility for internal control to the Main Board from 1 July 2001. The Main Board is therefore primarily responsible for reviewing the effectiveness of the Society's system of internal control.

The systematic process of identifying, evaluating and managing the Society's significant risks is being thoroughly revised in the light of experience, and will be re-launched in 2005. Meanwhile managing of high-level risks continued under the existing system. The Main Board has twice received the strategic risk register and the updated action plans associated with it. This is in accordance with the prescription in the internal control guidance for directors on the Combined Code.

The Main Board has had throughout the year regular progress reports on the achievement of Strategic Objectives and any related financial implications and control issues. The Audit Committee has monitored risk and control issues, by reviewing

- (i) processes by which internal control and risk management are exercised;
- (ii) action taken in response to the external auditors' management letter for the 2002 Accounts;
- (iii) the work of the Internal Audit Unit.

Following recommendations to the Council, the Remuneration and Scrutiny Committee were established in 2001. The Scrutiny Committee reviews the exercise of delegated powers by the Main Board and its Subsidiary Boards. The Remuneration Committee's terms of reference are to approve the remuneration arrangements for the Chief Executive and Senior Management Team Directors, and advise on all matters relating to compensation to or in respect of Office-holders, Chairs and Members of committees and Council Members.

The sources of assurance available to the Main Board indicate that the system of internal control developed since 2001 accords with the principles of the 'Combined Code' on Corporate Governance. The integration of risk assessment into its control processes has progressed well but was not fully embedded. It was therefore recognised that a revision is needed, in order to re-launch it in 2005. There is further work to do on this. Nevertheless the control framework was sufficient to identify and address the key control and risk issues in volatile circumstances in 2004.

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Corporate governance (continued)

Board Members attendance records

Adherence to the Combined Code requires presentation of the attendance record of the board of directors. Attendance of Council Members at Council meetings is recorded in the Minutes, and available to Members of the Society on request. As a matter of convenience it is not reproduced here. The records for the Main Board, appear below, together with those for Finance and Resources Board, and the Audit Committee.

| | Main Board | F&RB | Audit Committee |
|----------------------|-------------------|-----------------|------------------------|
| Number Held | 10 | 8 | 6 |
| Angus Andrew* | 1 (2) | - | - |
| Robin ap Cynan* | - | 7 | - |
| Richard Bagley | - | - | 3 |
| Stephen Brooker | - | - | 5 (5) |
| Andrew Caplen* | - | 5 (5) | - |
| Helen Davies* | 3 (4) | - | - |
| Peter Davies | - | - | 3 (4) |
| Michael Franks | - | 0 (0) | - |
| Derek French* | - | 2 | - |
| Philip Hamer* | - | 7 | - |
| Robin Healey* | - | 5 (5) | - |
| Richard Hegarty* | 9 | - | - |
| Bob Heslett* | - | 2 (3) | - |
| Andrew Holroyd* | 10 | - | - |
| Sunil Kambli | - | - | 5 |
| Michael Lawson | - | - | 4 |
| Alexandra Marks* | 3 (4) | - | - |
| Kevin Martin* | 10 | - | - |
| Pauline McBride* | - | - | 3 |
| Geoffrey Mitchell | - | - | 1 (1) |
| Kevin Mortell | - | - | 5 |
| Edward Nally* | 10 | - | - |
| Sue Nelson* | 4 (4) | - | - |
| Simon Osborne | - | - | 1 (1) |
| Janet Paraskeva | 10 | - | - |
| John Pickup* | - | 8 | - |
| Geoffrey Sandercock* | 8 | 8 | - |
| Hilary Siddle* | 5 (6) | - | - |
| Huw Thomas* | - | - | 3 |
| Rodney Warren* | 10 | - | - |
| Peter Williamson* | 5 (6) | 3 (3) | - |
| Fiona Woolf* | 9 | - | - |

* denotes Council members.

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Corporate governance (continued)

Board Members attendance records (continued)

The numbers in brackets denote the maximum number of meetings a person could have attended, allowing for the period during which he/she was a Board or Committee member if less than the full year under review.

The Chief Executive has been included in the above table as she is a voting member. Non-voting Senior Management Team members have not been included.

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Statement of Going Concern

In arriving at its decision to prepare financial statements on the going concern basis, the Council has considered a number of matters.

At present the Society has certain powers under the Solicitors Act 1974 (as revised) including the power, under order of the Master of the Rolls with the concurrence of the Lord Chancellor and the Lord Chief Justice, to charge a practising certificate fee. Although the Lord Chancellor has exercised powers under the Access to Justice Act 1999 to restrict the uses to which the practising certificate can be put, the Council of the Society is unaware of any intentions to revoke the Society's Charter or primary statutory powers. It is also unaware of any moves for the practising certificate fee order made by the Master of the Rolls to be rescinded.

The Council approves each year on an annual basis, revenue and capital budgets. The Council, the Main Board and Finance & Resources Board approved the original budgets and forecasts for 2005 and these are subject to continuing review by the Chief Executive in terms of actual performance against plan.

The Council is of the opinion that the Society will have sufficient resources to meet its liabilities as they fall due over the 12 months from the date of signing the accounts.

As a result, the Council has satisfied itself that the Society is a going concern.

Implications of the Clementi Review have been considered and noted in The Office Holders Report.

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Office Holders'

Review of the Regulation of Legal Services

The Government commissioned Sir David Clementi to carry out a review of regulation of legal services aimed at promoting competition and innovation and improving services for the customer. Sir David Clementi published his report in December 2004. The government have yet to issue a white paper indicating how they intend to implement the recommendations.

Sir David Clementi's main recommendations were as follows:

- Legal Services Board (LSB). This new legal regulator will supervise the Law Society, Bar Council and all regulators of legal services. Regulatory functions would be exercised by the front line regulators subject to their competence and governance arrangements, especially in the separation of regulation from representation.
- Office for Legal Complaints. This would be a single independent body to handle consumer complaints against all providers of regulated legal services. Any discipline and conduct issues about solicitors would continue to be dealt with by the Law Society.
- Legal Disciplinary Practices (LDP). Law practices which would enable lawyers from different professional backgrounds, for example solicitors and barristers, to work together, and which would permit non-lawyers to become involved in the management and ownership of legal practices. The Law Society believes that it is well-placed to be front-line regulator of LDPs.

If implemented, these recommendations will have a significant impact on the Society's structure and future role. The Society will have to demonstrate competence and that it can separate its regulatory and representative functions satisfactorily. The Council has taken significant steps to achieve that separation by establishing new governance structures.

A Regulation Board and a Consumer Complaints Board will operate in shadow form from September 2005 and will take on substantive responsibilities from January 2006.

Legal Services Complaints Commissioner

The Government set up the Legal Services Complaints Commissioner in October 2004. The Commissioner has significant powers and is able to make the Society pay a penalty, of up to the lower of £1million or 1% of turnover, if it:

- fails to submit a plan which the Commissioner considers adequate for securing that such complaints are handled effectively and efficiently with it.
- submits such a plan but fails to handle complaints in accordance with it.

The Society has made sustained and significant improvements in 2004 in its complaints handling performance.

Solicitors Indemnity Fund (SIF)

The SIF audited accounts show a surplus of £54m as at 30 September 2004. However the SIF board have been assured the surplus is likely to be in the region of £80m. The bulk of which will be realisable in 2005, as a result of claims being significantly lower than originally anticipated and the under-provision in earlier years being less than anticipated.

The Council on 24 February 2005 agreed in principle:

- 1) a rule change to enable a refund of contributions for the 2002/2003 and 2001/2002 indemnity years (amounting to approximately £50 million) to practices that had made contributions in respect of those indemnity years, and that the balance of the surplus (approximately £30 million) should be released to the Law Society in due course to be applied in accordance with Rule 11 of the Solicitors' Indemnity Rules. Rule 11 deals with the way in which the Society must apply any surplus released to it by SIF;

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Office Holders' (continued)

Solicitors Indemnity Fund (SIF) (continued)

- 2) an amendment of the 'Termination of the Fund' provisions in the Solicitors' Indemnity Fund Rules (Rule 11) to allow a wider range of options to be considered by the Law Society for dealing with the balance of the surplus.

Accounting policy in the Management Accounts

The management accounts are prepared in accordance with applicable accounting standards as set out on page 20 apart from fees received in respect of practising certificate fees (including foreign lawyers and panel fees).

Fees received in respect of practising certificates for the practising year which commences 1 November are accounted for on a cash received basis.

Panel fees covering 3 or 5 years are payable on registration and accounted for in the period in which it is received.

Consolidated income and expenditure reported under the above method is shown below:

| | 2004 £'000 |
|--|-----------------------------|
| Income – group | |
| Practising certificates and other fees | 81,647 |
| Investment income and interest | 2,022 |
| Other income | 21,648 |
| Grant from the Law Society Charity for educational purposes | 1,143 |
| | <hr/> 106,460 |
| Expenditure | |
| Administration expenses | 100,162 |
| Establishment expenses | 7,367 |
| Donation to the Law Society Charity | 1,000 |
| Donation to the Law Society Bursary Fund | 58 |
| | <hr/> 108,587 |
| (Deficit) for the financial year as per Management Accounts | <hr/> (2,127) <hr/> |
| (Deficit) for the financial year as per Statutory Accounts | <hr/> (5,476) <hr/> |
| Difference due to Income Recognition | <hr/> (3,349) <hr/> |

Independent auditors' report to the members of The Law Society (the 'Society')

We have audited the financial statements of the Society for the year ended 31 December 2004 which comprise the income and expenditure accounts, the balance sheets, the consolidated cash flow statement, the reconciliation of net cash flow to movement in net funds and the notes to the consolidated cash flow statement and related notes 1 to 19. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Society's members as a body, in accordance with the bye-laws of the Society. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Council and auditors

As described in the statement of Council's responsibilities, the Council, through the Main Board and the Finance & Resources Board, is responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibility is to audit the financial statements in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view. We also report if, in our opinion, the Society has not kept proper accounting records or if we have not received all the information and explanations we require for our audit.

We read the Council's report for the above year and consider the implications for our report if we become aware of any apparent misstatements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Finance & Resources Board in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Society and the group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Society and the group as at 31 December 2004 and of its deficit for the year then ended and are properly prepared in accordance with applicable United Kingdom law.



Deloitte & Touche LLP

Chartered Accountants

London

19 May 2005

Neither an audit nor a review provides assurance on the maintenance and integrity of the website, including controls used to achieve this, and in particular whether any changes may have occurred to the financial information since first published. These matters are the responsibility of the directors but no control procedures can provide absolute assurance in this area.

Legislation in the United Kingdom governing the preparation and dissemination of financial information differs from legislation in other jurisdictions.

The Law Society

Consolidated income and expenditure account Year ended 31 December 2004

| | Notes | 2004 £'000 | 2003 £'000 |
|---|-------|----------------|---------------|
| Income – group and joint venture | | | |
| Practising certificates and other fees | 2 | 78,357 | 68,337 |
| Investment income and interest | 3 | 2,022 | 1,913 |
| Other income (including joint venture) | 4 | 21,589 | 24,178 |
| Grant from the Law Society Charity for educational purposes | | 1,143 | 1,048 |
| | | <u>103,111</u> | <u>95,476</u> |
| Less: share of joint venture income | 9 | - | (4,214) |
| | | <u>103,111</u> | <u>91,262</u> |
| Expenditure | | | |
| Administration expenses | 5 | 100,162 | 80,989 |
| Establishment expenses | 5 | 7,367 | 5,978 |
| Donation to the Law Society Charity | 5 | 1,000 | 2,520 |
| Donation to the Law Society Bursary Fund | 5 | 58 | 80 |
| | | <u>108,587</u> | <u>89,567</u> |
| (Deficit)/Surplus for the financial year | 13 | <u>(5,476)</u> | <u>1,695</u> |

All transactions are derived from continuing operations in the United Kingdom.

The Society's share in the operating result of its joint venture (see note 9) results in a nil net position in 2004 (2003 - £nil).

There are no recognised gains and losses for the current financial year and preceding year other than as shown in the consolidated income and expenditure account above.

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Consolidated balance sheet 31 December 2004

| | Notes | 2004 £'000 | 2003 £'000 |
|---|-------|----------------------|----------------------|
| Fixed assets | | | |
| Tangible assets | 7 | 53,216 | 46,545 |
| Investment in joint venture: | 9 | | |
| Share of gross assets | | - | 1,543 |
| Share of gross liabilities | | - | (1,543) |
| | | <u>53,216</u> | <u>46,545</u> |
| Current assets | | | |
| Stocks | | 284 | 268 |
| Debtors | 10 | 8,040 | 7,301 |
| Cash at bank and in hand | | 68,131 | 77,099 |
| | | <u>76,455</u> | <u>84,668</u> |
| Creditors: amounts falling due within one year | 11 | <u>(81,069)</u> | <u>(76,651)</u> |
| Net current (liabilities)/assets | | <u>(4,614)</u> | <u>8,017</u> |
| Total assets less current liabilities | | 48,602 | 54,562 |
| Provisions for liabilities and charges | 12 | <u>(3,075)</u> | <u>(3,559)</u> |
| Total net assets | | <u><u>45,527</u></u> | <u><u>51,003</u></u> |
| Represented by: | | | |
| Accumulated fund | 13 | <u><u>45,527</u></u> | <u><u>51,003</u></u> |

The financial statements were approved by the Council of the Law Society on 12 May 2005.

Signed on behalf of the Council of the Law Society

E Nally

PRESIDENT

G Sandercock

TREASURER

The Law Society

Consolidated cash flow statement Year ended 31 December 2004

| | Notes | 2004 £'000 | 2003 £'000 |
|--|-------|---------------|-----------------|
| Net cash inflow from operating activities | I | 3,909 | 16,695 |
| Returns on investments and servicing of finance | II | 2,022 | 1,913 |
| Taxation | | (791) | (325) |
| Capital expenditure and financial investment | II | (14,108) | (12,104) |
| Cash (outflow)/inflow before management of liquid resources and financing | III | (8,968) | 6,179 |
| Management of liquid resources | IV | 12,200 | (21,500) |
| Increase/(decrease) in cash in the year | | <u>3,232</u> | <u>(15,321)</u> |

Reconciliation of net cash flow to movement in net funds

| | | 2004 £'000 | 2003 £'000 |
|--|-----|---------------|---------------|
| Increase/(decrease) in cash in the year | III | 3,232 | (15,321) |
| Cash used to increase liquid resources | | (12,200) | 21,500 |
| Change in net funds resulting from cash flows | | (8,968) | 6,179 |
| Net funds at 1 January | | <u>77,099</u> | <u>70,920</u> |
| Net funds at 31 December | | <u>68,131</u> | <u>77,099</u> |

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Notes to the consolidated cash flow statement Year ended 31 December 2004

I. RECONCILIATION OF SURPLUS FOR THE YEAR TO NET CASH INFLOW FROM OPERATING ACTIVITIES

| | 2004 | 2003 |
|--|--------------|---------------|
| | £'000 | £'000 |
| (Deficit)/surplus for the year | (5,476) | 1,695 |
| Depreciation charges | 7,383 | 2,990 |
| Loss on disposal of tangible fixed assets | 54 | 1 |
| Bank deposit interest received | (2,022) | (1,913) |
| Tax charge | 975 | 678 |
| (Increase)/decrease in stocks | (16) | 20 |
| (Increase) in debtors | (738) | (449) |
| (Decrease)/increase in creditors | (743) | 2,890 |
| Increase in fees in advance | 4,976 | 8,257 |
| (Increase)/Decrease in provision for liabilities | (484) | 2,526 |
| Net cash inflow from operating activities | 3,909 | 16,695 |

II. ANALYSIS OF CASH FLOWS FOR HEADINGS NETTED IN THE CASH FLOW STATEMENT

| | 2004 | 2003 |
|---|-----------------|-----------------|
| | £'000 | £'000 |
| Returns on investments and servicing of finance | | |
| Bank deposit interest received | 2,022 | 1,913 |
| Net cash inflow from returns on investments and servicing of finance | 2,022 | 1,913 |
| Capital expenditure and financial investment | | |
| Purchase of tangible fixed assets | (14,108) | (12,104) |
| Net cash outflow from capital expenditure and financial investment | (14,108) | (12,104) |

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Notes to the consolidated cash flow statement Year ended 31 December 2004

III. ANALYSIS OF NET FUNDS

| | At 1 January 2004 £'000 | Cash flow £'000 | At 31 December 2004 £'000 |
|--------------------------|--|--------------------------------|--|
| Cash in hand and at bank | 2,099 | 3,232 | 5,331 |
| Cash held in deposit | 75,000 | (12,200) | 62,800 |
| | <u>77,099</u> | <u>(8,968)</u> | <u>68,131</u> |

IV. MANAGEMENT OF LIQUID RESOURCES

| | 2004 £'000 | 2003 £'000 |
|--------------------------------------|-----------------------|-----------------------|
| Cash withdrawn from deposit accounts | <u>12,200</u> | <u>(21,500)</u> |

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Income and expenditure account Year ended 31 December 2004

| | Notes | 2004 £'000 | 2003 £'000 |
|---|-------|----------------|---------------|
| Income | | | |
| Practising certificates and other fees | 2 | 78,357 | 68,337 |
| Investment income and interest | 3 | 2,022 | 1,910 |
| Other income | 4 | 5,062 | 4,615 |
| Grant from The Law Society Charity for educational purposes | | 1,143 | 1,048 |
| | | <u>86,584</u> | <u>75,910</u> |
| Expenditure | | | |
| Administration expenses | | 84,601 | 67,404 |
| Establishment expenses | | 7,341 | 6,204 |
| Donation to The Law Society Charity | 5 | 1,000 | 1,000 |
| Donation to The Law Society Bursary Fund | 5 | 58 | 80 |
| | | <u>93,000</u> | <u>74,688</u> |
| (Deficit)/Surplus for the financial year | 13 | <u>(6,416)</u> | <u>1,222</u> |

All transactions are derived from continuing operations in the United Kingdom.

There are no recognised gains and losses for the current financial year and the preceding year other than as shown in the consolidated income and expenditure account above.


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Balance sheet Year ended 31 December 2004

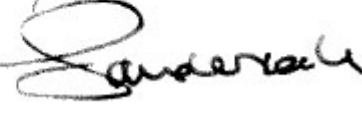
| | Notes | 2004 £'000 | 2003 £'000 |
|---|-------|----------------------|----------------------|
| Fixed assets | | | |
| Tangible assets | 7 | 50,655 | 43,839 |
| Investments | 8 | 74 | 2,495 |
| | | <u>50,729</u> | <u>46,334</u> |
| Current assets | | | |
| Debtors | 10 | 6,027 | 4,211 |
| Cash at bank and in hand | | 68,131 | 77,099 |
| | | <u>74,158</u> | <u>81,310</u> |
| Creditors: amounts falling due within one year | 11 | <u>(79,812)</u> | <u>(75,669)</u> |
| Net current (liabilities)/assets | | <u>(5,654)</u> | <u>5,641</u> |
| Total assets less current liabilities | | 45,075 | 51,975 |
| Provisions for liabilities and charges | 12 | <u>(3,075)</u> | <u>(3,559)</u> |
| Total net assets | | <u><u>42,000</u></u> | <u><u>48,416</u></u> |
| Represented by: | | | |
| Accumulated fund | 13 | <u><u>42,000</u></u> | <u><u>48,416</u></u> |

The financial statements were approved by the Council of the Law Society on 12 May 2005.

Signed on behalf of the Council of the Law Society

E Nally  PRESIDENT

G Sandercock  TREASURER



The Law Society

Notes to the accounts Year ended 31 December 2004

1. Accounting policies

The financial statements are prepared in accordance with applicable United Kingdom accounting standards. The particular accounting policies adopted are described below and these have been applied consistently in the current and prior year.

Accounting convention

The financial statements are prepared under the historical cost convention.

Basis of consolidation

Consolidated entities

The consolidated financial statements include the financial statements of the Law Society, together with those of The Law Society Services Limited, The Law Society Property Services Limited, The Law Society Pension Scheme Limited, Law Society (Hardware Rental Services) Limited and Law Society (Software Licensing Services) Limited, which are wholly owned by the Law Society.

The Society's 51% holding in Solicitors Professional Indemnity Limited (SPIL #2) – a dormant company is included in the consolidated accounts of the Society.

Non-consolidated entities

The following entities are not consolidated into the financial statements of The Law Society: Solicitors Indemnity Fund (SIF), Compensation Fund, Stannard Bequest Fund, The Law Society Retirement Benefits Scheme, The Cheviot Trust, The Law Society Trustees Limited, The Law Society Charity, The Law Society Pension Scheme and the Assigned Risks Pool.

These entities are not consolidated in the consolidated Society financial statements for a number of reasons, including: no beneficial interest in the assets of these entities, the Law Society does not exercise control over these entities or does not bear the risks and rewards of ownership. In addition, a number of these entities are set up by statute outside the control of the Society and there are, therefore, significant restrictions in the ability of the Society to utilise the funds of these entities.

Practising Certificates

Fees received in respect of practising certificates for the practising year which commences on 1 November are apportioned on a time basis. No credit has been taken for fees due but not received at the balance sheet date.

Examination fees and Legal Practice Course fees

Examination fees are accounted for in the year in which the examination is held. Legal Practice Course fees are apportioned over the period of the course to which they relate.

Admission, annual enrolment, registration and transfer of articles fees

These fees are accounted for on a cash received basis.

Students' enrolment fees

These fees are payable on registration and are apportioned over the period to which they relate.

The Law Society

Notes to the accounts Year ended 31 December 2004

1. Accounting policies (continued)

Taxation

Full provision is made for taxation payable on activities during the year. The society is only liable for taxation on its investment income and gains and obtains no tax relief for its overhead expenditure, which is regarded as being incurred for the benefit of members whose fees are correspondingly not taxed. Tax relief is obtained on annual payments made under deed of covenant and Gift Aid. Its subsidiaries, The Law Society Services Limited and The Law Society Property Services Limited, are liable for corporation tax on their profits.

Depreciation of fixed assets

Tangible fixed assets are stated at cost net of depreciation.

Depreciation is provided on a straight line basis over the periods indicated below:

- (i) In respect of freehold property which has been split into various component parts with each category being depreciated over its useful economic life:

| | |
|-----------------------|----------|
| Building structure | 50 years |
| Internal finishes | 15 years |
| Services and fittings | 25 years |
| External works | 35 years |

Costs of repairs and maintenance are charged against revenue in the year in which they are incurred.

- (ii) In respect of leasehold property and improvements:

Premiums paid - over the period to the next open market rent review.

Improvements - over 10 years or the period of the lease if shorter.

- (iii) In respect of equipment and furniture:

Motor vehicles: over five years.

Equipment and furniture: over ten years

- (iv) In respect of computers and hardware:

Main frame, mini computers, servers and operating software: over five years.

Software associated with the Society's Customer Relationship Management and web systems is being written off over five years from the point at which the relevant software is first used.

All other computing equipment and software: over three years.

All additions to the library are now written off in the year of purchase.

No depreciation is charged on freehold land.

The Law Society

Notes to the accounts Year ended 31 December 2004

1. Accounting policies (continued)

Investments

Fixed asset investments are shown at cost less provision for impairment.

Stocks

Stocks are valued at the lower of cost and net realisable value.

Lease transactions

Rentals under operating leases are charged to the income and expenditure account in equal annual amounts over the lease term.

Development costs

Software development expenditure is capitalised if it is separately identifiable, it is reasonably certain that the development will be successful and, on completion, it will provide a material benefit to the Society.

Pension costs

The expected cost of pensions in respect of the Law Society Pension Scheme is charged to the income and expenditure account so as to spread the cost of pensions over the service lives of employees. Variations from the regular cost are spread over the expected service lives of current employees in the scheme.

The discounted value of ex-gratia pensions is charged to the income and expenditure account in the year in which they are granted.

The Council of the Law Society decided to close the existing Law Society Pension scheme to new members from 1 January 2005. From that date, a new Pension scheme has been set up whereby new or current staff who have not joined the existing scheme within 12 months of commencing employment are now eligible to join this new scheme, which will be a Defined Contribution (Money Purchase) scheme. The Law Society will also contribute towards this new scheme, which will be double the individual employees' contribution up to a maximum of 7% of basic salary.

On 27 January 2005 the Finance & Resources Board made the decision to appoint Zurich Assurance Ltd as the provider of the Law Society Stakeholder pension scheme.

2. Practising certificates and other fees

| Consolidated and the Law Society | 2004 £'000 | 2003 £'000 |
|--|-----------------------|-----------------------|
| Practising certificates | 73,817 | 63,899 |
| Examination and Legal Practice Course Fees | 1,962 | 1,970 |
| Admission fees | 715 | 717 |
| Student enrolment fees | 828 | 730 |
| Annual enrolment fees | 407 | 406 |
| Registration and transfer of articles | 628 | 615 |
| | <u>78,357</u> | <u>68,337</u> |

3. Bank deposit interest

| | Consolidated | | The Law Society | |
|-----------------------|-----------------------|-----------------------|------------------------|-----------------------|
| | 2004 £'000 | 2003 £'000 | 2004 £'000 | 2003 £'000 |
| Bank deposit interest | 2,022 | 1,913 | 2,022 | 1,910 |
| | <u>2,022</u> | <u>1,913</u> | <u>2,022</u> | <u>1,910</u> |

The Law Society

Notes to the accounts Year ended 31 December 2004

4. Other income

| | Consolidated | | The Law Society | |
|--|---------------------|---------------|------------------------|--------------|
| | 2004 | 2003 | 2004 | 2003 |
| | £'000 | £'000 | £'000 | £'000 |
| Gazette income from advertisements | 9,508 | 8,869 | - | - |
| Publications and products | 1,875 | 1,442 | - | - |
| Courses and functions | 519 | 529 | 2 | 3 |
| National conference | 270 | 398 | 2 | - |
| Recruitment service | 136 | 270 | - | - |
| Library | 175 | 181 | 1 | - |
| Rents receivable | 327 | 378 | 6 | - |
| Royalty income | 802 | 756 | - | - |
| Grant income | 972 | 897 | 972 | 897 |
| Catering | 455 | 190 | 6 | 5 |
| Foreign lawyer registration | 1,558 | 1,428 | 1,558 | 1,428 |
| Special interest sections income | 619 | 570 | - | 3 |
| Family Law Panel fees | 218 | 240 | 218 | 240 |
| Countrywide legal indemnity | 401 | 296 | - | - |
| Personal Injury Panel | 162 | 171 | 162 | 171 |
| Authorisation of Course Providers | 729 | 490 | 729 | 490 |
| Subscription to Solicitors' Financial Services | 21 | 101 | - | - |
| Business services to solicitors | 818 | 830 | - | - |
| Other subscriptions | 121 | 222 | 121 | 222 |
| Sundry income | 1,903 | 1,706 | 1,285 | 1,156 |
| | <u>21,589</u> | <u>19,964</u> | <u>5,062</u> | <u>4,615</u> |
| Joint venture income | - | 4,214 | - | - |
| | <u>21,589</u> | <u>24,178</u> | <u>5,062</u> | <u>4,615</u> |

Grant income includes £10,963 (2003: £23,654) from Westminster foundation for Democracy, £349,677 from the Department for Constitutional Affairs and £25,740 from the European Commission.

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Notes to the accounts Year ended 31 December 2004

5. Analysis of expenditure (continued)

In addition to their remuneration as auditors, as set out above, Deloitte & Touche LLP were also paid £3,355,000 (2003: £1,069,000) in respect of the following matters:

| Non audit fees | 2004 £'000 | 2003 £'000 |
|--|-----------------------|-----------------------|
| Tax services | | |
| - compliance services | 22 | 16 |
| - advisory services | 24 | 97 |
| Other services | | |
| - litigation assistance | 60 | 214 |
| - Programme Engineer assurance services | - | 101 |
| - Project management and implementation services | 2,918 | 454 |
| - IT Outsourcing | 185 | - |
| - other services not covered above | 146 | 187 |
| | <u>3,355</u> | <u>1,069</u> |

Tax advisory services include work in relation to VAT advice and assistance, and income tax advice and assistance given during the year.

During the year Deloitte & Touche LLP continued their work in relation to the ongoing assessment of Programme Engineer, as well as the project management of Programme Engineer. It is expected that Deloitte & Touche LLP will continue with the project management of Programme Engineer in 2005 for phase 2.

Other services include work in relation to the operating model project.

Of the £3,355,000 fees shown above, £62,000 (2003: £214,000) was recharged to the Compensation Fund, and £2,918,000 (2003: £605,000) capitalised.

This additional remuneration is included in other professional fees and legal fees.

Ernst & Young continued their Programme Engineer assurance work in 2004.

Donation to the Law Society Charity

The donation to the Law Society Charity for 2004 was £1,000,000 (2003: £2,520,000). No donation for 2004 was made from the Law Society Services Limited (2003: £1,520,000) under Gift Aid.

Donation to the Law Society Bursary Fund

The Law Society-Education and Training Department made a gift aid donation of £58,288 (2003: £80,000) to the Law Society Bursary Fund for the benefit of students.

The Law Society

Notes to the accounts Year ended 31 December 2004

6. Compensation, remuneration and staff numbers

Office holders

Compensation for the year was payable in respect of the office holders as follows:

| | 2004 £ | 2003 £ |
|-----------------------|-----------|-----------|
| President | 89,284 | 84,608 |
| Vice-President | 44,642 | 42,304 |
| Deputy Vice-President | 22,321 | 21,176 |

From 1 September 2004, the annual compensation payable was increased in respect of office holders as follows:

| | £ |
|-----------------------|--------|
| President | 90,760 |
| Vice-President | 45,380 |
| Deputy Vice-President | 22,690 |

The Lay Commissioner received total emoluments of £114,637 during the year ended 31 December 2004 (2003: £107,210).

Compensation in respect of lay members serving on the Adjudication Panel is £4,000 per annum, in respect of those serving on the Compliance Board is £3,000 per annum and in respect of those serving on the Council is £3,000 per annum.

Senior Management Team ("SMT")

The SMT of the Society received total emoluments, including pension contributions, of £1,259,000 for the year to 31 December 2004 (2003 - £1,069,000).

The majority of the increase is due to the full year effect of the Director of Legal Services.

The highest paid member, being the Chief Executive, received emoluments including pension contributions of £297,000 (2003: £279,000). This figure includes basic salary of £190,000, bonus of £28,000 and pension contribution of £72,000 including employer's contributions.

All SMT members are members of the Law Society Pension Scheme.

Staff numbers (full time equivalents at year end)

The number of persons employed by the Society at 31 December 2004 was 1,297 (2003: 1,265).

The Law Society

Notes to the accounts Year ended 31 December 2004

7. Tangible assets

| Consolidated | Freehold land and buildings £'000 | Leasehold property and imp- rovements £'000 | Equipment and furniture £'000 | Computers and hardware £'000 | Total £'000 |
|-------------------------------------|--|--|--|---|------------------------|
| Cost | | | | | |
| At 1 January 2004 | 30,523 | 1,311 | 17,445 | 40,897 | 90,176 |
| Additions | 19 | 112 | 2,572 | 11,405 | 14,108 |
| Reclassification | - | - | (2,732) | 2,732 | - |
| Disposals | - | (1,011) | (315) | (933) | (2,259) |
| At 31 December 2004 | 30,542 | 412 | 16,970 | 54,101 | 102,025 |
| Accumulated depreciation | | | | | |
| At 1 January 2004 | 8,212 | 1,037 | 8,891 | 25,491 | 43,631 |
| Charge for the year | 927 | 51 | 1,148 | 5,257 | 7,383 |
| Reclassification | - | - | (2,477) | 2,477 | - |
| Disposals | - | (942) | (330) | (933) | (2,205) |
| At 31 December 2004 | 9,139 | 146 | 7,232 | 32,292 | 48,809 |
| Net book value | | | | | |
| At 31 December 2004 | 21,403 | 266 | 9,738 | 21,809 | 53,216 |
| At 31 December 2003 | 22,311 | 274 | 8,554 | 15,406 | 46,545 |
| The Law Society | | | | | |
| Cost | | | | | |
| At 1 January 2004 | 26,490 | 1,311 | 16,415 | 40,833 | 85,049 |
| Additions | 19 | 112 | 2,572 | 11,405 | 14,108 |
| Reclassification | - | - | (2,732) | 2,732 | - |
| Disposals | - | (1,011) | (311) | (933) | (2,255) |
| At 31 December 2004 | 26,509 | 412 | 15,944 | 54,037 | 96,902 |
| Accumulated depreciation | | | | | |
| At 1 January 2004 | 6,865 | 1,037 | 7,881 | 25,427 | 41,210 |
| Charge for the year | 795 | 51 | 1,134 | 5,256 | 7,236 |
| Reclassification | - | - | (2,477) | 2,477 | - |
| Disposals | - | (942) | (324) | (933) | (2,199) |
| At 31 December 2004 | 7,660 | 146 | 6,214 | 32,227 | 46,248 |
| Net book value | | | | | |
| At 31 December 2004 | 18,849 | 266 | 9,730 | 21,810 | 50,655 |
| At 31 December 2003 | 19,625 | 274 | 8,534 | 15,406 | 43,839 |

The Law Society

Notes to the accounts Year ended 31 December 2004

7. Tangible assets (continued)

Freehold land and buildings are periodically valued. The total open market value at the last valuation in 2004 was £20,100,000.

The Library collection, which has a net book value of £nil (2003: £nil) is shown within equipment and furniture. It is periodically valued for insurance purposes. The last valuation in 2004 totalled £3,297,000.

8. Fixed asset investments

| | The Law Society | |
|-------------------------------------|------------------------|--------------|
| | 2004 | 2003 |
| | £'000 | £'000 |
| Advances to subsidiary undertakings | 74 | 2,495 |

Subsidiary and other undertakings

The Society has the following wholly-owned subsidiary undertakings. They are all incorporated in Great Britain and operate in England and Wales.

| | Nature of business | Issued share capital |
|---|---------------------------|-----------------------------|
| The Law Society Services Limited | Trade and services | £100 |
| The Law Society Property Services Limited | Property holding company | £100 |
| The Law Society Trustees Limited | Charity trustee | Limited by guarantee |
| The Law Society Pension Scheme Limited | Pension Trustee | Limited by guarantee |
| Law Society (Hardware Rental Services) Limited | Lease rental (dormant) | |
| Law Society (Software Licensing Services) Limited | Lease rental (dormant) | |

The Law Society Pension Scheme Limited, Law Society (Hardware Rental Services) and Law Society (Software Licensing Services) have no, or minimal, assets or liabilities.

9. Joint venture

On 25 April 2000 the Society entered into a joint venture agreement with St. Paul Holdings Limited. In accordance with this agreement, a joint venture company, Solicitors Professional Indemnity Limited – SPIL#1 (the 'joint venture Company'), was set up for the following purposes: to arrange the provision of compulsory professional indemnity insurance to solicitors in private practice in England and Wales under the new open market arrangements; to act as marketing, claims handling and underwriting agent of St. Paul International Insurance Company Limited in respect of solicitors' professional indemnity insurance; and to provide run-off and related services to the Solicitors Indemnity Fund.

During the year ended 31 December 2002, St. Paul Holdings Limited transferred its shareholding to St. Paul Co. Inc who subsequently transferred it to St. Paul London Limited.

The Law Society owned 51 'A' shares and St Paul owned 49 'B' shares in SPIL#1. Under the terms of the agency agreement, St Paul agreed to pay agents commission to SPIL#1 at the rate of 5% of gross premiums. If income exceeded expenditure, the commission payable to St Paul International Insurance Company Limited was reduced to offset any commission previously paid. This ensured there was no financial risk being borne by the Law Society, other than the share capital.

The agreement with St Paul was terminated on 30 September 2004.

The Law Society

Notes to the accounts

Year ended 31 December 2004

9. Joint venture (continued)

The Law Society was approached by St Paul with an offer to enter a new joint venture agreement but under this agreement St Paul would not manage and administer the run-off of SIF.

The carve-out of the management of the run off of SIF was achieved by the shares in SPIL#1 being transferred from each of the Law Society and St Pauls to Solicitors Indemnity Fund Limited on 1 October 2004. The Law Society gave no warranties or indemnities in respect of the 'A' shares and received £51 from SIF Limited in consideration for the transfer.

SPIL#2 was set up and the share capital is allocated to both St Paul London Limited and the Law Society resulting in an ownership structure which is identical to that of SPIL#1.

The Law Society entered into a number of agreements relating to SPIL#2 on 1 October 2004. The arrangements largely mirror the agreements which were in place on the previous joint venture, but crucially, the difference between SPIL#1 and SPIL#2 is that SPIL#2 will not operate and will remain effectively dormant unless and until St Paul group fails to offer quotations for compulsory professional indemnity insurance to the profession (trigger event).

10. Debtors

| | Consolidated | | The Law Society | |
|---|---------------------|--------------|------------------------|--------------|
| | 2004 | 2003 | 2004 | 2003 |
| | £'000 | £'000 | £'000 | £'000 |
| Trade debtors | 3,076 | 2,595 | 1,362 | - |
| Grant receivable from The Law Society Charity | 1,143 | 1,048 | 1,143 | 1,048 |
| Compensation Fund | 685 | - | 685 | - |
| Other Law Society affiliated entities | 306 | 363 | 306 | 363 |
| Other debtors | 955 | 1,592 | 619 | 1,008 |
| Prepayments | 1,875 | 1,697 | 1,912 | 1,792 |
| Corporation tax recoverable | - | 6 | - | - |
| | <u>8,040</u> | <u>7,301</u> | <u>6,027</u> | <u>4,211</u> |

11. Creditors: amounts falling due within one year

| | Consolidated | | The Law Society | |
|--|---------------------|---------------|------------------------|---------------|
| | 2004 | 2003 | 2004 | 2003 |
| | £'000 | £'000 | £'000 | £'000 |
| Amounts due to suppliers | 11,322 | 7,932 | 10,575 | 7,483 |
| Other creditors including taxation and social security | 1,807 | 1,622 | 1,450 | 1,302 |
| Fees received in advance | 67,940 | 62,964 | 67,787 | 62,751 |
| Compensation Fund | - | 4,132 | - | 4,132 |
| Other Law Society affiliated entities | - | 1 | - | 1 |
| | <u>81,069</u> | <u>76,651</u> | <u>79,812</u> | <u>75,669</u> |

Included in other creditors are balances of £1,147,000 (2003: £1,044,000) in respect of PAYE and National Insurance.

The Law Society

Notes to the accounts Year ended 31 December 2004

12. Provisions for liabilities and charges

| | 2004 £'000 | 2003 £'000 |
|--|--------------------------|--------------------------|
| Pension costs - unfunded | | |
| At 1 January | 965 | 1,015 |
| Charge for the year | 30 | 84 |
| Utilised in the year | (130) | (134) |
| | <hr/> | <hr/> |
| At 31 December | 865 | 965 |
| | <hr/> | <hr/> |
| Pension costs - funded | | |
| At 1 January | 1,994 | 18 |
| Charge for the year | 7,842 | 6,963 |
| Utilised in the year | (7,626) | (4,987) |
| | <hr/> | <hr/> |
| At 31 December | 2,210 | 1,994 |
| | <hr/> | <hr/> |
| Other provisions | | |
| At 1 January | 600 | - |
| Reduction in year | (600) | |
| Charge for the year | - | 600 |
| | <hr/> | <hr/> |
| At 31 December | - | 600 |
| | <hr/> | <hr/> |
| Total provisions at 31 December | <hr/> 3,075 <hr/> | <hr/> 3,559 <hr/> |

The provision for the pension costs unfunded is in respect of the estimated present value of additional pension payments that have been granted to former members of staff beyond the pension scheme contractual obligation. Payments are made monthly in arrears.

13. Movement on reserves

| | Accumulated fund £'000 |
|------------------------|---------------------------------------|
| Consolidated | |
| At 1 January 2004 | 51,003 |
| Deficit for the year | (5,476) |
| | <hr/> |
| At 31 December 2004 | 45,527 |
| | <hr/> |
| The Law Society | |
| At 1 January 2004 | 48,416 |
| Deficit for the year | (6,416) |
| | <hr/> |
| At 31 December 2004 | 42,000 |
| | <hr/> |

The Law Society

Notes to the accounts Year ended 31 December 2004

14. Operating lease commitments

The Society's commitments for rental payments under operating leases payable during the year to 31 December 2004 are as follows:

| | Land and buildings | | Other operating leases | |
|--|--------------------|-------|------------------------|-------|
| | 2004 | 2003 | 2004 | 2003 |
| | £'000 | £'000 | £'000 | £'000 |
| Leases expiring between two and five years | 534 | 481 | 821 | 1,211 |

15. Capital commitments

The Main Board has agreed Programme Engineer (mostly Customer Relations Management system and WEB) capital expenditure of £8,648,000 of which £5,816,000 has been spent on the Programme up to the end of December 2004, leaving a capital commitment of £2,551,000. Programme Engineer for 2005 (including the brought forward balance from 2004) is £3,500,000 including VAT at 17.5% for revenue and 14.35% for capital.

The Core Programme (mostly information technology projects) for 2005 (including the brought forward balance from 2004) is £3,578,000 (including capitalised irrecoverable VAT at 14.35%).

The Transition Programme (relates to the costs of taking IT service delivery in-house) for 2005 is £731,000 (including capitalised irrecoverable VAT at 14.35%).

The Law Society

Notes to the accounts Year ended 31 December 2004

16. Pension commitments

The Society operates a pension scheme (the 'Scheme') providing benefits based upon final pensionable salary. The assets of the Scheme are held separately from those of the Society in a trustee administered scheme, The Law Society Pension Scheme. These assets are invested mainly in quoted securities and are managed by Merrill Lynch Investment Managers Limited, Barclays Global Investors Limited and Bank of Ireland Asset Management UK Limited.

The total pension cost for the year was £7,873,000.

There is a provision for pension costs of £3,075,000 in the balance sheet as at 31 December 2004 arising from the accumulated difference between contributions paid and the corresponding pension costs, including the estimated present value of unfunded pension payments that have been granted to former members of staff beyond the pension scheme contractual arrangements. These payments are payable monthly by direct debit from the Society's bank account.

The Society currently accounts for pensions under SSAP24. Under the transitional arrangements for FRS17, the Society is required to provide additional disclosures relating to its pension scheme. These are provided below.

SSAP24 Accounting for pension costs

Contributions to the Scheme are charged to the profit and loss account so as to spread the cost of pensions over employees' working lives with the group. The Scheme is subject to triennial valuation by a qualified independent actuary. The last valuation was carried out as at 31 December 2002, using the projected unit method. It was assumed that the investment returns would be 6.0% a year, salary increases would average 3.4% a year and pension increases would average 2.4% for LPI pension increases or the fixed rates specified by the scheme. The joint contribution rate payable by the Society and its employees to meet the cost of accruing liabilities was increased from 23% to 32% of earnings from 1 August 2004. An additional 9% of pensionable salaries was also paid by the Society in August 2004, for July 2004.

At the actuarial valuation date, the market value of the assets of the Scheme was £57,729,000 and, in the opinion of the actuary, this value represented 70% of the value of the benefits which had accrued to members, after allowing for expected future increases in earnings. The employer's contribution rate takes account of the deficit disclosed by the valuation. The regular cost is 20.6% of pensionable salaries, less members own contributions of 5% of pensionable salaries.

FRS17 Retirement benefits

Under the transitional arrangements of FRS 17, the Society is required to disclose the following information about the Scheme and the figures that would have been shown in the Society's balance sheet if FRS 17 applied in full today.

The full actuarial valuation of the Scheme was carried out as at 31 December 2004 by a qualified, independent actuary.

Disclosures for 2005

Under UKGAAP FRS 17 will be fully adopted in the financial statements of the society for 2005. The effect of full adoption are that the pension cost (i.e. service cost plus interest cost less expected return on assets) will be charged to the profit and loss account.

Also an additional amount will pass through the statement of recognised gains and losses (STRGL) account.

It should be noted that the balance sheet, profit and loss account and the STRGL figures will be volatile from 2005 onwards as a result of the full adoption of FRS 17.

The Law Society

Notes to the accounts Year ended 31 December 2004

16. Pension commitments (continued)

The assets in the scheme and the expected rates of return at 31 December were:

| | 2004 | | 2003 | | 2002 | |
|---|--|----------------|--|----------------|--|----------------|
| | Long term rate of return expected | Value £'000 | Long term rate of return expected | Value £'000 | Long term rate of return expected | Value £'000 |
| Equities | 7.8% | 44,188 | 7.8% | 35,908 | 7.5% | 26,575 |
| Bonds | 4.8% | 40,327 | 4.8% | 33,345 | 4.8% | 31,176 |
| Total market value of assets | | 84,515 | | 69,253 | | 57,751 |
| Present value of Scheme liabilities | | (129,356) | | (112,308) | | (93,281) |
| Deficit in the scheme and net pension liability | | (44,841) | | (43,055) | | (35,530) |

If the above net pension liability were recognised in the financial statements at 31 December, the Society's consolidated Accumulated Fund would be as follows:

| | 2004 £'000 | 2003 £'000 |
|---|---------------|---------------|
| Accumulated Fund as at 31 December | 45,527 | 51,003 |
| Pension cost provision included in Accumulated Fund (note 12) | 3,075 | 2,959 |
| Pension cost provision in relation to unfunded scheme | (900) | (1,001) |
| Deficit in the scheme and net pension liability | (44,841) | (43,055) |
| Accumulated Fund | 2,861 | 9,906 |

The figures shown above were calculated on the basis of the following assumptions:

| | 2004 | 2003 | 2002 |
|---|-------|-------|------|
| Discount rate | 5.3% | 5.4% | 5.6% |
| Rate of increase in salaries | 4.85% | 4.75% | 3.4% |
| Rate of increase in deferred pensions | 2.85% | 2.75% | 2.4% |
| Rate of increase in pensions in payment (for pensions accrued before 1 November 2002) | 5.0% | 5.0% | 5.0% |
| Rate of increase in pensions in payment (for pensions accrued after 1 November 2002) | 2.85% | 2.75% | 2.4% |
| Inflation assumption | 2.85% | 2.75% | 2.4% |

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Notes to the accounts Year ended 31 December 2004

16. Pension commitments (continued)

Analysis of the movements in the scheme deficit during the year

| | 2004 £'000 | 2003 £'000 |
|---|-----------------------|-----------------------|
| Opening deficit in the scheme and net pension liability | (43,055) | (35,530) |
| Current service cost | (7,293) | (4,698) |
| Contributions | 7,626 | 4,987 |
| Past service cost | (1,018) | - |
| Other finance income | (1,648) | (1,716) |
| Actuarial gain/(loss) | 547 | (6,098) |
| | <hr/> | <hr/> |
| Closing deficit in the scheme and net pension liability | (44,841) | (43,055) |
| | <hr/> | <hr/> |

Amounts that would have been included within the financial statements for the year ended 31 December 2004 had FRS 17 been applied are as follows:

Amounts included within operating profit:

| | 2004 £'000 | 2003 £'000 |
|---|-----------------------|-----------------------|
| Current service cost and past service cost included within operating profit | 8,311 | 4,698 |
| | <hr/> | <hr/> |

Amounts included as net finance return:

| | 2004 £'000 | 2003 £'000 |
|----------------------------------|-----------------------|-----------------------|
| Expected return on scheme assets | 4,627 | 3,630 |
| Interest on scheme liabilities | (6,275) | (5,346) |
| | <hr/> | <hr/> |
| Other finance costs | (1,648) | (1,716) |
| | <hr/> | <hr/> |

Analysis of the actuarial gain in the statement of total recognised gains and losses:

| | 2004 £'000 | 2003 £'000 |
|---|-----------------------|-----------------------|
| Actual return less expected return on pension scheme assets | 3,524 | 3,221 |
| Experience gains arising on the scheme liabilities | 1,184 | 3,065 |
| Changes in assumptions underlying the present value of the scheme liabilities | (4,161) | (12,384) |
| | <hr/> | <hr/> |
| Total actuarial gains/(losses) recognised in the statement of total recognised gains and losses | 547 | (6,098) |
| | <hr/> | <hr/> |

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Notes to the accounts Year ended 31 December 2004

16. Pension commitments (continued)

History of experience gains and losses:

| | 2004 | 2003 | 2002 |
|--|-------|---------|----------|
| Difference between the expected and actual return on scheme assets: | | | |
| Amount (£'000) | 3,524 | 3,221 | (10,315) |
| Percentage of scheme assets | 4% | 5% | (18%) |
| Experience gains/(losses) on scheme liabilities: | | | |
| Amount (£'000) | 1,184 | 3,065 | (4,383) |
| Percentage of the net present value of scheme liabilities | 1% | 3% | (5%) |
| Total actuarial gain/(loss) in the statement of total recognised gains and losses: | | | |
| Amount (£'000) | 547 | (6,098) | (26,974) |
| Percentage of the present value of scheme liabilities | 0% | (5%) | (29%) |

17. Monies held as a consequence of the intervention process

At 31 December 2004, monies held by the Society, in Statutory Trust Accounts ("STA") as a consequence of intervention in the practices of solicitors amounted to £44,633,000 (2003: £37,924,000). The increase has occurred due to the reinstatement of certain Statutory Trust Accounts and the embargo on distributions from non-intact accounts whilst the Legal Trustee's responsibilities are determined. The Society has no beneficial interest in these monies and accordingly they are not included in the balance sheet. In addition, the Society, as sole trustee, has made no provision for potential losses or costs relating to the identification of the beneficial owners of these monies.

These balances were held by the Law Society as statutory trustee. The rightful beneficiary of these monies is not always known. The Compensation Fund may have a legal entitlement to some of these monies and this may be clarified by the courts. This unknown amount that the Court may direct should be remitted from the STAs to the Compensation Fund.

18. Related party transactions

Five lay members of the Council received payments of £3,000 each in 2004 and 2003. The Lay Commissioner's emoluments are set out in note 6.

The Law Society paid £195,228 excluding VAT to Council members £169,850 related to fees for handling complaints. The remainder related to other professional fees.

There are no other related party transactions, except for expenses, allowances and fees paid by the Society to Council members and their firms, which have been disclosed.

19. Contingent asset

A significant surplus of £54 million has arisen in the Solicitors Indemnity Fund (SIF), the bulk of which will be realisable in 2005, as a result of claims being significantly lower than originally anticipated and the under-provision in earlier years being less than anticipated.

The Council on 24 February 2005 agreed in principle:

- (1) a rule change to enable a refund of contributions for the 2002/2003 and 2001/2002 indemnity years to practices that had made contributions in respect of those indemnity years, and that the balance of the surplus should be released to the Law Society in due course to be applied in accordance with Rule 11 of the Solicitors' Indemnity Rules;

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Notes to the accounts

Year ended 31 December 2004

19. Contingent asset (continued)

- (2) an amendment of the 'Termination of the Fund' provisions in the Solicitors' Indemnity Fund Rules (Rule 11) to allow a wider range of options to be considered by the Law Society for dealing with the balance of the surplus.