Adapt Or Die: Law Firms In Tomorrow's Economy

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This is a multipart series exploring the metamorphosis that needs to take place in the world of corporate law firms in order for them to survive and thrive in the future. In the first two installments of the series, we discussed the history of the adversarial relationship between corporate clients and their outside counsel and the fate of the billable hour. Here, we address the problem of ad hoc client development and the challenge of associate training.

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Ad Hoc Client Development and the Conflict Conundrum

Many law firms are fighting for their economic lives, and many have already lost the battle. The death of the mid-sized full service firm that was only a scary rumor a decade or so ago has become fact. Firms are merging and acquiring other firms faster than they can print new business cards.

Corporate clients are extracting wider and deeper cuts in the cost of legal services, wreaking havoc on the bottom line of a business model that depends on bringing in more and more business from clients that are willing to pay less and less.

Client development is more important than ever, but gone are the days when a golf date, or an invitation to lunch, or pushing out white papers or bragging announcements will get you business. Gone are the days when belonging to the same club or sorority as the GC will ensure a lengthy or prosperous relationship with a corporate client. And gone are the days that an ad hoc, scattershot, opportunistic approach to client development will sustain a law firm.

Traditional law firm structures that rely on rainmaker partners who support everyone else have resulted in several conditions that are at odds with the current economic reality. Law firms have evolved from businesses with partners and associates and the occasional of counsel thrown in for good measure to equity partners, non-equity partners, of counsel, special counsel, service partners, permanent associates, partner-track associates, non-partner track associates and a partridge in a pear tree.

These endless stratifications of law firm laborers became necessary to do the depth and diversity of work the rainmakers landed from major corporate clients. Similarly, the hurdles erected to equity partnership allowed firms to employ battalions of lawyers but limit access to profits to those whose earnings could support the firm — year after year. Internal competitiveness among rainmakers is encouraged and cooperation is implicitly discouraged under this system.

The frantic race to meet never-ending quotas has yielded a patchwork client portfolio for many firms, restrained only by a conflict of interest policy that is sometimes the subject of creative interpretation. Little or no thought, planning or analysis of market sectors and future trends go into determining which opportunities to pursue and which to forego, because that level of strategic preparation requires cooperation among the rainmakers who have no incentive to do so. Rather, reactive opportunism results in firms chasing big corporations with newsworthy problems or expanding into “new” hot areas of expertise after half the law firm market has already gone there.

Aside from the constant relocation of elite rainmakers from firm to firm that has been going on for many years, one more recent trend serves to underscore one of the many problems with this ad hoc approach. With the proliferation of potential and actual conflicts of interest caused or at least exacerbated by ad hoc client development, many rainmakers have left BigLaw to form boutiques because they cannot practice

their trade and expand their client roster under the current "conflict conundrum."

This conflict conundrum is so widespread that almost all major engagements with BigLaw firms involving large corporations on both sides require the waiver of actual or potential conflicts of interest. Of course, rainmaker musical chairs, with books of business being inserted and extracted from firms on a regular basis, impact the ability of the corporate client to utilize the attorney of its choice and only adds to the inherent difficulty of sustaining a loyal client base.

Portability of client portfolios is a wonderful thing, unless you are the firm left behind. Client development strategies that rely exclusively on the traditional rainmaker model are vulnerable to major upheavals anyway; but having to compete against former partners with lower overhead and client loyalty creates that much more vulnerability.

Firms without a strategic and cohesive client development strategy are at a potentially fatal competitive disadvantage. How do you design such a strategy? Well, it will require some short-term sacrifices in order to reap long-term gains. It will require discipline in establishing a roadmap of market sectors and opportunities to pursue and to avoid. It will require choosing sides when making some of these decisions since firms cannot expect to get corporate client loyalty when they refuse to give it. And it will require a transformation of the current economic model followed by most large firms. It will also require time — but not too much time, since no one can predict with certainty when corporate clients may force the issue.

Training Associates on the Client's Dime

Long before even I started practicing law, a layman used to become a lawyer through apprenticeship. In fact, California and a few other states still allow you to "read for the law" by studying under the tutelage of a licensed lawyer in lieu of attending law school.

And way back when the majority of lawyers practiced solo or in small firms, it was possible to work under an attorney's direction with the discipline and focus required to learn the law. Apprentice training was the responsibility of the lawyer the apprentice shadowed for several years in order to master the craft.

Enter the large law firm, along with the proliferation of law schools that populated them, and it was no longer possible for the apprenticeship system to function. The rise of the law firm as the favored form of private practice brought with it the advent of the associate attorney. It was not economically optimal to divert senior attorneys' time from making money to train associates under the law firm system while that new associate was unable to generate profits on their own.

As a consequence, law firms of yesteryear had new associates occupy their time with mundane but necessary learning tasks like reviewing documents, researching arcane points of law and performing work that was probably better suited to secretaries or law clerks. Those same firms, however, recognized that these associates were unable to deliver value to clients, and so didn't bill clients for these fledglings' work, or billed them at substantially reduced non-lawyer rates.

When associate salaries in large law firms precipitously rose in the mid-eighties, many firms chose to defray the cost of carrying higher associate salaries by using associates' least profitable years (typically the first two years of practice) to train them by doing billable work for clients.

Not only did these associates lack the legal skills to provide real value, their inexperience meant that they performed tasks inefficiently. Associate billing rates have continued to climb, while the inexperience and inefficiency that typifies new lawyers obviously remains unchanged.

For many years corporate clients did little more than grumble about the unfairness of being charged ever-increasing hourly rates to train new associates. Eventually, a few companies took the bold step of disallowing first-year, and later second-year associates from working on their matters. That trickle has become a flood and now that prohibition has become a standard part of many corporate billing rules.

Even in the absence of explicit bans, many corporate clients select or approve the teams doing their work and do not choose new associates as team members. The problem has become so sufficiently widespread and acute that many law firms struggle with what to do with new associates whose work cannot be billed to corporate clients.

Although summer associate programs have been slashed and entering classes of associates winnowed significantly, firms still must hire new associates to ensure longevity. To attract the most desirable law students to their firms, they need to offer competitive compensation.

After nearly 10 years of new associate salary stagnation, BigLaw has raised the bar on first-year salary to $180,000. Of course, they have compressed mid and senior associate salaries to compensate for this increase — a fact that shouldn't be lost on any first-year who has aspirations to advancement.

For now, it seems BigLaw has decided to err on the side of keeping the associate funnel flowing; but as in-house salaries fall, particularly in relation to associate salaries, corporate clients will continue to pressure BigLaw to cut costs.

Without the ability to reliably pass the cost of new associate salaries on to corporate clients, firms will be forced to choose between shifting their priorities away from hiring new associate to lateral hires who can be immediately profitable, or eating the cost of keeping new associates and thus reducing firm profits.

Unrelenting competition, corporate budget cutting and departing rainmakers are already attacking firm profit margins, so there is probably little appetite for further diminishing profits by assuming the full burden of associate compensation.

Limiting hiring to lateral associates is a short-term solution, since those same laterals must be trained somewhere. If enough firms cease hiring new associates, the source for lateral hires will dry up, particularly as BigLaw firms typically require a certain pedigree from their laterals that, in their assessment, usually means coming from other BigLaw firms.

There are alternatives to these two harsh prospects. Firms could invest in intensive training programs, much like bar review courses but tailored to their client portfolio and decrease associate compensation to lessen the impact of idle employees. Many graduating law students, who 10 years ago would have been first-tier picks, are not able to find large law firm employment. A rigorous training program could become an enticement sufficient to outweigh the loss of compensation.

After the requisite training period, new associates could rotate between firm departments and shadow selected attorneys after an appropriate orientation. Secondment could be the next phase, to permit the associate to gain experience of the corporate client's culture and priorities and develop relationships that can be leveraged by the firm.

Any of these options require law firms to revamp their compensation structures, trim their overhead, and lower their profit expectations. Associate training then becomes yet another arrow pointing to the inescapable conclusion that BigLaw structure must change, rather significantly, to survive.

Tune in tomorrow for part 4 of this series: "Compensation Just Ain't What it Used to Be … And Never Will Be Again."

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