

# EDGE International Review

FALL 2006



## MANAGING THE LAW FIRM'S BALANCE SHEET FOR FUTURE PROFIT

by Michael Roch and Friedrich Blase



## STRATEGIC OPTIONS

FALL 2006



## STRATEGIC OPTIONS FOR COMMODITY PRACTICES

by Ed Wesemann

## FIRMS

by Nick Jarrett-Kerr

## DEALING WITH BLIND SPOTS

by Robert Millard

## COMPELLING TESTIMONIALS

by Patrick J. McKenna

## MANAGING OUR FIRM, ONE LAWYER AT A TIME

by Gerry Riskin

## LEADERSHIP IN LAW FIRMS: EDGE WELCOMES MAGGIE CALLICRATE



[www.edge.ai](http://www.edge.ai)

**I**N RESPONSE TO THE REDUCTION OF CORPORATE TRANSACTIONAL WORK AVAILABLE TO LAW FIRMS DURING THE EARLY 2000s, A NUMBER OF GENERAL PRACTICE FIRMS BECAME PROGRESSIVELY DEPENDENT ON OTHER AREAS OF PRACTICE, PARTICULARLY LITIGATION. BUT, THE SLOW DOWN IN CORPORATE PRACTICE REDUCED THE SPIN-OFF OF COMMERCIAL LITIGATION SO LAWYER PLATES WERE OFTEN FILLED WITH DISCOUNTED WORK THAT FIRMS MIGHT OTHERWISE NOT HAVE PURSUED. IN MANY CASES, THESE INVOLVED HIGHER LEVEL INSURANCE DEFENSE WORK. IN SOME FIRMS IT INCLUDED CONSUMER PRACTICES LIKE CRIMINAL DEFENSE AND DOMESTIC RELATIONS. AT THE SAME TIME, NEW AREAS OF INSURANCE COVERAGE, SUCH AS EMPLOYMENT PRACTICES LIABILITY, CAUSED TRADITIONALLY FULL RATE LABOR AND EMPLOYMENT LITIGATION TO BECOME INCREASINGLY COMMODITIZED. THE RESULT IS THAT FIRMS THAT SPENT A DECADE PURSUING STRATEGIES TO RAISE THEIR LITIGATION PRACTICE TO MORE SOPHISTICATED LEVELS FIND THEMSELVES AGAIN DOING SUBSTANTIAL AMOUNTS OF LOW RATE WORK.

# Strategic OPTIONS for Commodity Practices



**T**he question for both general practice firms and boutiques is whether they can strategically position themselves to provide needed revenue streams from commodity level work while viably competing for more sophisticated higher priced matters.

But, beyond the economic pressures, what makes commodity practices tough is that their characteristics become engrained in a firm's culture and become a significant part of the firm's self-image. While the precise impact may differ from firm to firm, most share several specific characteristics that may be difficult for them to admit to, never mind change.

**HIGH SATISFACTION.** Almost uniformly, partners in commoditized practices seem to possess a high level of "job satisfaction" and satisfaction with their firm.

Indeed, for the litigator who wants to spend his life in the courtroom there is probably no better place than in an insurance defense practice where lawyers differentiate themselves as "trial lawyers" compared to "litigators" who may rarely appear in court other than to argue motions. Those underlying skills and characteristics which are needed to meet the firm's outcomes and goals in the principal areas of performance tend to become (for the law firm at least) part of the sub-text. This makes it all the more important for the individual partner to gain a deep understanding of those attributes which he or she needs to develop in order to attain the firm's objectives.

**POOR CLIENT SERVICE ETHIC.** Lawyers who spend much time in commodity practices may have a difficult time serving com-

mercial clients. When lawyers are hired largely on the basis of price, there is often little value placed on the "bedside manner" and responsiveness so important with clients in other commercial matters.

**LACK OF TEAMWORK.** Commodity level cost consciousness leaves little room for teamwork. As a result, lawyers performing commodity level work often take pride in lean staffing of cases, citing the Texas, Ranger motto: "One riot, one ranger."

**HIGH VALUE PLACED ON WORKING ATTORNEY PRODUCTION.** Lawyers with commodity practices typically focus on and encourage their firms to highly value the amount of effort put forth by an individual attorney rather than business produced or non-billable activities. This also bolsters the

lack of teamwork because there is no compensation incentive for giving work to someone else that a lawyer could do himself.

**LACK OF BUSINESS DEVELOPMENT SKILLS.** In commodity practices, young lawyers have often been historically discouraged from attempting to attract new business. Emphasis instead was placed on enhancing specific practice skills. Accordingly, upon becoming

## STRATEGIC OPTIONS

Plotting the future can be a difficult task for law firms that have significant commodity practices. Given the frequently high level of satisfaction among their lawyers, a common theme among them is often the desire to “not see things change.” They enjoy and are accustomed to their practice and the manner in which their firm operates. Yet, at the same

price-sensitive practices (particularly insurance defense work) is to grow their full rate practice and develop new practice areas. The hope is that by capping the amount of low rate work performed and growing the firm with other types of clients, they will eventually reduce their dependence on commodity practices. This is a rational and realistic strategy provided that the firm has the ability to attract new non-commodity work and to manage the current level of low priced work.

The attorneys currently with the firm can attract new business. Or, the firm can hire laterals that have clients other than insureds and insurers. These actions may sound easy. “Our firm has a great reputation. We have some of the best standup trial lawyers in the state. Getting commercial litigation should not be hard and laterals should be beating a path to our door.”

But – the firm’s reputation is often based on its lowest common denominator rather than its highest. In today’s legal world, law firms are often judged by how high their billing rates are and how much money their partners earn. Firms with significant commodity practices rarely rank high on either of these criteria. At issue is why a client should take a risk in giving a complex commercial case to a firm with a reputation for doing primarily low rate work. A case in point is the firms to which insurance companies give their major coverage issues, bad faith claims, or large exposure cases. Odds are it is not the firms to which they give their routine claims defense work. Firms that cannot convince their largest clients of their capabilities beyond insurance defense work will have a hard time convincing prospective clients. Telling the marketplace that the firm has great lawyers won’t do it – every good-sized law firm has great lawyers. Attempting to compete on price only solidifies its reputation as a place where routine claims are handled.

It is possible, however, to change a practice and a reputation. Indeed, several AmLaw 100 firms have historically been dependent on insurance



partners, the lawyers have neither the skills nor the interest to develop higher rate work.

**LOW ASSOCIATE TO PARTNER RATIOS.** If lawyers are judged by their production of billable time, then it is appropriate that the standard for partnership would be based on quality as a trial lawyer, history of high hour production and a given number of years of “laboring in the vineyards.” With this relatively liberal screen and, often, a relatively small differentiation between partner and associate bill rates, it is not surprising that associates rise quickly to the partnership.

**LOW HOURLY RATES.** Firms with a mixture of practices often charge lower than market rates for non-commodity matters. Years of having their rates attacked by insurance clients causes exceptional rate sensitivity and some insecurity about a lawyer’s value in the marketplace.

time, they are concerned by the lack of growth of their income in recent years and may be fearful that they have become dependent on work where the rate is difficult to increase.

With an infinite number of variations, there are basically three strategies that a firm with a mixture of full rate and commodity work can pursue. The firm can seek to reduce and eventually eliminate its commodity practices by bringing in other forms of work. It could continue performing the areas of commodity practice by attempting to cordon them off in a separate department or office as an affiliated company. Finally, a firm could use technology and carefully developed practice procedures to make commodity practices highly profitable.

### Strategy 1: Change the Practice

The classic solution of many firms with highly

defense work. Typically, it occurs in one or a combination of three ways

**DILUTION.** Some firms merge or acquire themselves out of commodity work. Essentially, this involves constantly seeking mergers or group lateral acquisitions that do not involve reduced rate work. As the firm grows in new areas of practice, the firm is exposed to clients who may not have known the commodity reputation. At the same time, by bolstering credible practices in other areas, the low rate image is blurred and less dominant in people's minds. Typically, such a strategy requires a long period of time, both to obtain the full rate practice growth to dilute the commodity reputation and because it takes time for the legal market's perceptions to change.

The process of change can be accelerated if the firm is acquired by a larger firm or participates in a merger of equals, provided that the merger partner presents a completely different image to the marketplace. This was certainly the case for many mid-sized firms during the rapid law firm growth years of the middle and late 1980s. In fairness, it must be pointed out that acquisition/merger is a more difficult strategy today because the acquiring firms have become more sophisticated in their selection of merger partners

**LARGE CASE OPPORTUNITIES.** A second tactic (which has primarily been used by firms that have migrated away from an insurance defense practice) is to involve themselves in mass tort and other forms of multi-party litigation. Firms that have been successful in landing clients with major litiga-

tion have been able to provide their insurance defense litigators with other forms of work. For some firms, it was asbestos and other toxic tort matters that gave them the higher rate volume (even though much of it was insured) to move away from their traditional practice. For others, particularly in the Southwest, it was the fail-

**A** firm's reputation is often based on its lowest common denominator rather than its highest.

ing savings and loan work in the late 1980s representing federal agencies (FSLIC, FDIC, RTS, et al). For still others, it was the opportunity to gain work as a national or regional coordinating counsel for products manufacturers. Whatever the opportunity, some firms were able to use large volume cases to convert their practices.

**DEFLECTIONS.** A third common route by which firms have moved away from a commodity emphasis has been the attrition of their lawyers with the least profitable practices. Although counter-intuitive, this sometimes occurs in mixed practice firms because, regardless of the type of compensation system, over time, partners with practices generating higher gross revenues on a per lawyer basis tend to be paid increasingly higher compensation. As a result, a gap in pay occurs between partners with full rate practices and those with commodity practices. Even though this difference may be justified, it becomes both an economic and ego issue for the partners doing lower rate work. Since the barriers to starting a new law firm or moving laterally to a firm

that focuses on a commodity practice are not high, leaving can be an attractive option, particularly if a group of lawyers has the promise of business from a number of clients whose attachment to the lawyers is stronger than the firm. While these departures may have been traumatic for everyone involved, in retrospect they were quite successful, with the departing lawyers being able to operate more profitably with a lower overhead cost, and the remainder of the original firm being able to dramatically increase its average revenue per attorney literally overnight.

It is unlikely that any firm would or could strategically plot a wholesale change away from insurance defense using one of the above scenarios. For most firms, these were historic anomalies. But they do demonstrate that firms can change their image, operations, and profitability.

#### **Strategy 2: Establish a Subsidiary**

**F**or some law firms it is extremely difficult to maintain a mixture of commodity work with other types of law practice. Attempting to operate side-by-side practices with dramatically different forms and levels of profitability constrains both sides of the firm from achieving their objectives. The business lawyers, whose practices spin off commercial litigation, complain that insurance defense and workers compensation litigators don't provide the level of responsiveness that business clients demand. They are concerned that the low priced reputation makes the firm appear less capable of performing complex transactional work. The commodity practice lawyers, on the other hand, complain that the business lawyers don't bill enough

hours and are extravagant in their expenditures for marketing.

A number of law firms have responded to these concerns by splitting the firm. One way of doing this is to make a functional division – an active and visible separation between those involved in insurance defense or consumer litigation work, and those in other practices. This often includes differentiated locations within the firm's office space, offices on different floors, or even locating in a completely separate building. The two divisions may operate differently to reflect the unique needs of each type of practice, with separate recruitment programs, different pay scales for associates, and different levels of office support. One firm went so far as to hire commodity associates as staff attorneys at starting salaries 40 percent below their partnership track counterparts, housed the staff associates in cubicles, and provided only word-processing secretarial support.

The primary difficulty with attempting to operate a firm-within-a-firm – especially if one is in effect a “second class citizen” – is that it is contrary to the culture of most law firms. Whenever one attempts to create a subdivision within a social or business unit, some level of negative results will occur. This is particularly true when the basis of the division is that one practice is seen as being more profitable, sophisticated, or intellectually demanding than the other. The most common deterioration results from commercial litigation partners “borrowing” insurance defense associates to work on a large case, and eventually the line between the two sides of the firm become blurred once again. Experience has indicated that, while a firm-within-a-firm has been tried on numerous occasions over the past 20 years, it simply does not work as a long-term operating strategy.

### Strategy 3: Reorganize as a Specialized Low Priced Firm

Some highly successful firms have embraced commodity practices and made them profitable by strategically positioning themselves in the marketplace. The core of this strategy involves having a clear understanding of the basic actions which must be taken, and iden-

**P**artners in commoditized practices seem to possess a high level of “job satisfaction”

tifying the most efficient means of completing the engagement.

Most of the actions necessary to operate as a specialized low price firm are obvious to any business observer, but they can be summarized in three simple yet powerful objectives:

1. **Specialization.** The more a firm specializes in a single area of practice (e.g., medical malpractice defense, workers compensation, residential real estate closings, slip and fall defense for mass retailers) the greater the focus and efficiency of its operations.

2. **Convergence.** The operation of the firm must, in every detail, match the needs of the practice. Office space must be what is most effective and efficient - open plan offices close to the court house probably make sense. Staffing must be appropriate to needs, including strong reliance on non-lawyers for case intake and preparation, and lawyers recruited from lower wage employers such as the prosecutor's office, insurance companies, and other commodity practice firms.

3. **Management.** Actively manage all aspects of the relationship with clients and the performance of legal work. Let the lawyers do what they like to do: go to court.

### NO EASY ANSWERS

There is a folktale about how to cook a frog. If you try to throw the frog into a pot of boiling water it will hop out and run away. But, if you put it in tepid water and then put the pot on the flame, the frog will sit peacefully in the water until it is too late to escape. For many firms, none of these strategic options may appear attractive. Because the impact of commodity practices in a full service firm increases incrementally, maintaining status quo is, of course, always the most attractive option. Some firms will address the issues strategically, others will not.

One final issue – many firms attempt to deal with these issues in secret, often without involving the affected lawyers who work in the commodity areas. In every firm that has successfully dealt with a low rate or inconsistent practice, the success has been based on open communication among all of the lawyers involved and a clear recognition and understanding of everyone's objectives and best interests.



**Ed Wesemann** is a Principal with Edge International. He works with law firms around the world on strategic issues. His blog site is [www.edwesemann.com](http://www.edwesemann.com) or he can be contacted by email at [wesemann@edge.ai](mailto:wesemann@edge.ai) or by phone at 1-912-598-2040.