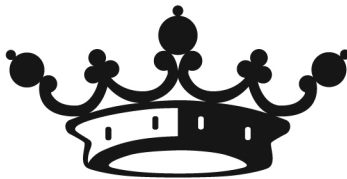


I N S I D E T H E M I N D S

Strategies for Growing a Law Firm

*Managing Partners on Attracting New Clients,
Evaluating Market Potential, and Analyzing a
Firm's Readiness to Grow*

2011 EDITION



ASPATORE

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Quality versus Cost:
An Alternative Growth
Strategy for Today's
Law Firms

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ASPATORE

A Unique Law Firm Growth and Fee Strategy

My view runs contrary to some of the more traditional perspectives in the industry—law firms have grown too large in recent times, and the quality of service has suffered as a result. When a law firm hires thirty, sixty, or eighty new lawyers a year, it is not possible to control quality. It is not possible to provide sufficient training. At some point, clients are going to react to the lower quality of service they receive, and some have begun to do so already.

To know what needs to be done in preparing a case for trial, a lawyer has to have been to trial. There is no chance any cognizable percentage of those scores of new lawyers in large litigation departments are going to see—let alone participate in—a trial for many, many years. In the meantime, they will learn the ways of often ultimately useless discovery—and think they are trial lawyers. They aren't. They are litigators. When they get seniority in their firms, they pass on their bad habits to the next generation. The firm grows, but quality suffers.

One way to combat that cycle is to have a policy of slow growth. Ours is one of the firms that has adopted an anti-growth model; instead of growing in response to increased demand as most businesses and law firms do, we only grow when there is increased supply of top talent. If we do not find a young lawyer who appears to be off the charts in smarts and potential, we do not hire anyone at all. If we do wind up hiring three or four new lawyers, it is only because they are at the very high end of the talent scale.

The second way we control growth is by charging differently for the firm's services. Most firms charge by the hour. The hourly rate model has been the driving force behind the growth of modern law firms, taking size to unprecedented levels. Because the firm makes more money by billing more hours, it has every incentive to hire more and more people to bill those hours to increase revenue. As said above, quality has to suffer at some size point. We have tried to address this by choosing a model wherein we will do no work at all by the hour. We get paid one fixed amount if we lose, another higher amount if we win. Immediately, our incentives change. Rather than making more money by having more people on the case, we make more money by having the most experienced people on the case and winning. We have turned the fee and growth models on their head. Our

view is that if a client pays for hours, they will get hours; if they pay for results, they will get results.

Client Reaction to the Economic Downturn

It has been an interesting time for the legal profession since the economy's reversal in 2007. After the downturn, clients have split into two distinct groups. One group is primarily concerned with cost and tends to put quality second, while the other group is more focused than ever on quality as a way to keep down their overall long-term costs. Some clients are looking to commoditize their work; they are putting out more requests for proposals (RFPs), which means that they are taking bids for legal services and are looking to hire the lowest qualified bidder as the best way to serve their company's needs. The problem with that strategy, of course, is that the lowest bidders are not always the highest quality bidders. A client might wind up being well served, but it also might wind up paying less in actual costs for its legal services but more in settlements and damages.

The second group of clients also believes that money is more precious than ever in the wake of the economic downturn, but they are taking a holistic view with respect to the delivery of legal services. While they are looking at their costs, they are also analyzing the likelihood that the team that they hire is going to keep their company's overall costs down by delivering quality results.

This dichotomy is similar to the situation faced by businesses in other markets. Many markets for products and services contain commodity offerings as well as high-end offerings. Customers have a choice. They can go with a company that produces average product—and doing so can be a good business judgment for their particular enterprise. However, there is also a market for companies whose clients want the highest quality goods, even at a higher price. Therefore, whether you are selling cars, clothes, carpet padding, or legal services, there is room for both the commodity end of the business and the high-quality end of the business. Clients just need to know which one they are buying. They need to make an informed choice and know that when they are saving on costs, they are likely scrimping on quality.

The Role of Geography in Law Firm Growth

In the high-end litigation market, which involves major business litigation and intellectual property (IP) disputes, clients are essentially dealing with a national legal market. Simply put, in these “bet the company” cases there is very little parochialism. There is little demand that the person in charge of the litigation be local. Rather, in high exposure cases companies will be searching for the best trial lawyers available, wherever they happen to be.

That does not mean that a company that is involved in high-end litigation will not have a local lawyer on their team, because they may be required to do so under local rules. A client may also want to have someone on their team who understands the local legal practices, the community, and the jury pool. However, high-end/high-dollar cases generally draw from those with a national practice, particularly with the technology and the high speed of communication available today. Our Chicago and Denver based firm tries five to ten big cases a year and 90 percent of them are not in our home cities.

Legal Issues Driving Growth in Key Practice Areas

Back in the 1890s, someone in England suggested that the British Patent Office ought to be closed “because there was nothing left to invent.” He turned out to be rather wrong. Patent applications have been issued in ever-increasing numbers, particularly over the past twenty years.

The IP litigation area has been hot for some time, and it seems to be getting even hotter. There are two primary reasons for this. First, patents that once languished in drawers are now getting monetized, both by companies looking for new revenue sources and by individual inventors drawn in by well-publicized success stories. Huge damages and license revenues won by the Lemelson team in the '80s and the Katz patent team in the '90s have led to a gold-rush environment for inventors.

Further fueling the fire is the fact that a number of private equity firms have determined that it is a good idea to invest in patents that once sat around gathering dust in the Patent Office, and have funded litigation with the goal of extracting license fees from a wide variety of large companies. The

telecommunications and other high-technology fields in particular have hundreds if not thousands of patents that overlap and could be said to cover some recent inventions, and those patents are increasingly the subject of litigation. Consequently, there is more patent litigation than ever before.

Patent litigation is now an incredible growth area for general practice law firms, both on the plaintiff's side and the defense side. That trend was triggered by a decision some years ago to allow patent cases to be tried by juries. Instead of more technically oriented patent lawyers handling the litigation within the patent bar, all of a sudden there was a market for jury trial lawyers in patent cases.

The percentage of patent cases that were tried to a jury¹:

1975 – 11.9%

1985 – 23.5%

1995 – 52.8%

2005 – 73.5%

All these factors have driven huge growth in the IP practice areas.

Growth

The most important consideration for a law firm when setting growth goals should be whether the firm can truly maintain quality as it grows. A firm should grow only as fast as it can maintain the skill level of its lawyers; otherwise, the quality of service the firm is providing to its clients, by definition, has to go down.

An alternative model for firms that want to do big case work without quality-stifling growth is to be open to partnering with a second, larger firm for those matters that need more bodies. Our firm has used this barrister-solicitor approach on numerous occasions, and our experienced and well-trained trial lawyers have brought in great results on huge cases by associating with one or more of the biggest firms in the country for the case

¹ Statistics compiled from Dir. Of Admin. Office of U.S. Courts, Table C-4, Ann. Repo. 1975-2004.

at hand. The big firm supplies the discovery and document reviews person power and we provide the strategic direction and trial skills. It is a form of outsourcing that allows us to stay small and control our quality while the big firm happily bills its hours.

A law firm should be up front with its clients about its growth plans. If the firm's plan is to be all things for all people, to provide one-stop nationwide and sometimes worldwide service, you need to tell your clients about that plan—that may well be what they are seeking. If, on the other hand, a firm is not of sufficient size to be able to handle large cases, clients have to be told. But the small, elite firm will still find it is in the market for that big case if it is open to working with big firms as co-counsel.

Increasing Firm Revenues by Increasing Risk

For many years, lawyers felt they deserved to make money no matter the quality of service they provided. For example, when a firm's fees were based on an hourly rate, those firms got paid the same money whether they won or lost cases. However, many believe that in this new world economy, we ought to be paid more if we win and less if we lose. For most of the world's biggest firms, that is a revolutionary concept. Plaintiffs' contingency firms have long had the philosophy that they only make money when they succeed; defense firms can adopt it as well. Lawyers should have something at risk, just as their clients do. Clients have something at risk when they go into a big piece of litigation, and there is no reason lawyers should not have some risk as well. One way for lawyers to take on risk in litigation is to allow their ultimate fee to be set pending the outcome of the case. The plus side for the law firm is that if you put some aspect of your fee at risk, you should get paid more if you win than you would have been paid if you had lost. For instance, if you have a case with \$100 million at stake and you can resolve the case for under \$5 million, you should get paid more than you would have been paid if your client ended up paying \$70 million. Fortunately, it is very easy to set up fee structures to reward you for a good result on the defense side, just as it is easy to set up a fee for rewarding a good result on the plaintiff's side. Therefore, one way to grow law firm revenue without attorney headcount growth is to put more at stake in fee agreements that give you an opportunity to earn higher fees for good results.

Modern Marketing

The best way to acquire new clients is by achieving high-quality results. With little effort, word gets around fast.

Up until the 1980s, lawyers often found promotion to be distasteful; in fact, our own professional rules prohibited it for many years. However, those promotional rules have now been loosened up sufficiently so that if there is a good story to tell, there are many ways to get it out there. Websites are of course a must, and most big firms now have full-size professional marketing departments.

The advent of professional marketing departments has led to a proliferation of books, directories, magazines, and websites that purport to rate the best lawyers in a particular practice or geographic area. (No longer is it Martindale-Hubbell or bust.)

Marketing departments are quick to purchase ad space or to show their bosses how good a job the marketing department is doing. (Get your senior partner's picture in the magazine, keep your job.) Some of this comes close to pay-for-ranking. But clients have quickly learned that there are only a few publishers that have true quality rankings. The rest are simply paid advertisements, the existence of which unfortunately brings down the credibility of the entire industry. The fact is that good results in a big case will bring you sufficient publicity to last for many years. With a good website as your assistance, a firm's work and record speak for itself.

The Experience Model: Recruiting and Retaining Top Talent

I previously served as hiring partner at one of the major national firms. We went to every major law school and invested a lot of money interviewing and entertaining new recruits. The vast majority of lawyers hired out of school or clerkships left the firm before they were equity partners. That approach certainly works well for the mass hire large firm pyramid model. That model has large numbers of young, inexperienced lawyers billing hours, with a fewer number of experienced partners at the top.

The firm I manage now only hires one to three lawyers a year, and we retain 90 percent of the lawyers that we hire. We do not hire laterally, ever. Our

pyramid is inverted—that means we have far more experienced lawyers than new ones.

We do not need to go to law schools to get the word out about our firm. Lawyers come to us. About 20 percent of our lawyers are former US Supreme Court clerks, who are the most valued hires in our profession. We have been able to do that type of hiring with very minimal spending on recruiting. Word has gotten out about our hour-free and trial-oriented environment, leading young lawyers to our door.

Turnover is a killer in a fixed-fee environment. When you put a premium on experience, the last thing you want is high turnover. Turnover makes much less difference in the traditional hourly model, as inexperienced lawyers can take longer to do the work—and more money is made when things take longer to do. The impact on quality is obvious. The firm that is incentivized through its fee arrangements to use small teams of highly experienced lawyers has a clear advantage over the firm that is incentivized to operate with a large team of inexperienced lawyers.

Investing in Technology

A successful law firm cannot avoid making investments in technology. Clients as well as young lawyers are demanding the investment. There was a time as recently as ten years ago when senior lawyers were not embracing technology; they were not brought up with it and they did not feel it was necessary. There were also economic disincentives to the investment—when you are paid by the hour, the idea of being able to do things much faster is not necessarily a good thing.

With today's computer technology, you can search your depositions for a particular phrase in just two seconds, unlike the old days when it used to take a lawyer or legal assistant three to four hours looking for that phrase at a full billing rate. Those days are over, and now all lawyers are expected to have and utilize every possible search engine—both the public ones and internal ones—to look for materials that have been generated in the course of a lawsuit or that are available to the public. A full technology budget is mandatory for all of today's top law firms.

At the same time, managers of law firms have a decision to make about how they are going to handle technology within their firm. The primary and threshold issue is whether they are going to have a static system or an inclusive, dynamic system. For example, when you issue a computer to a lawyer that is loaded with the firm's basic software, do you allow the lawyer to put their own favorite programs on the firm-issued laptop, or do you keep it a static system? If you decide to have a static system, you are going to be able to get away with having a much smaller management information system (MIS) staff, because you will have more stable systems. On the other hand, if you allow your lawyers to have a dynamic system where they can install any software that they want to add on top of the firm's core software bundles, you are going to have a much more unstable system, and more problems in maintaining your firm's core technology. Consequently, you will need to make a much greater investment in MIS personnel to keep things running.

Some people may feel that the static system is the obvious way to go, but I disagree. I believe that if you are going to get the most out of your lawyers, then you want them to use the software systems that work best and fastest for them. Most often, they are better at choosing such a system than a tech department or a managing partner. Therefore, whatever extra money you have to put out for MIS people will be more than returned to you by allowing lawyers to have the software on their system that makes them the most productive.

Final Thoughts

Litigation itself remains a large and stable practice area. Many companies are looking at their legal spending and deciding that litigation is quite expensive, and perhaps they should do more arbitration or other forms of alternate dispute resolution (ADR) in order to save on legal costs. Despite this, litigation is the biggest growth driver for any high-end firm.

Again, a primary challenge for many law firms at this time is the fact that clients are demanding—whether they realize it or not—either low costs or high quality. If a client is going for the low cost/commoditization approach and is putting pressure on their law firm to reduce their fees at all costs, this most likely means that in the long run their firm's quality will be reduced.

However, if a client believes that the highest quality legal services will bring the best results for their company—and ultimately, the lowest total costs for their company—then they are going to be looking for law firms that have the highest quality people, and should be willing to reward success.

Consequently, my advice to other law firm managers is not to grow for growth's sake—grow only if that growth means that you can deliver a better service and better quality to your clients. Allow your firm to take financial risks in return for higher rewards for successful results. You can have happier clients and happier lawyers, and still make money.

Key Takeaways

- In sum, a growth model is one that encourages smaller, highly experienced teams aimed at delivering great quality. Over time, that is another way to improve your bottom line; don't assume that can only be done by hiring large, inexperienced teams that try to bill the most hours. Growth should only come about when you have a supply of smart people who are there to deliver good results.
- One way for lawyers to take on some risk in litigation is to put a portion of their fee at risk pending the outcome of the case. Again, the plus side for the law firm is that if you put some aspect of your fee at risk then you should get paid more if you win than you would have been paid if you had lost.
- If firms are going to get the most out of its lawyers, you want them to use the software systems that work best and fastest for them. Most often, they are better at choosing such a system than a tech department or a managing partner. Therefore, whatever extra money you have to put out for MIS people will be more than returned to you by allowing lawyers to have the software on their system that makes them the most productive.

Sidney N. (Skip) Herman has been the managing partner of Bartlit Beck Herman Palenchar & Scott LLP since he helped found the firm in 1993. Bartlit Beck is recognized as one of the leading big case trial firms in the nation, and was named the American Lawyer's Litigation Boutique of the year in 2009. Mr. Herman received his JD from Northwestern University School of Law and BA from Haverford College. He is a member of the board of directors of The Chicago Lawyers' Committee for Civil Rights Under Law, Inc. and the Law Board of Northwestern University School of Law. His practice has included representation of such companies as United Technologies and their Pratt & Whitney division; DuPont; Bayer Corporation; Tyco International; and Dun & Bradstreet. Prior to starting Bartlit Beck, Mr. Herman was a share partner at Kirkland & Ellis. As managing partner of Bartlit Beck, Mr. Herman counsels on all alternative fee arrangements with clients, assists in strategy on primary firm matters, and is a featured speaker on matters of law firm economics, particularly the insidious impact of hourly billing on the modern practice of law.



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