2012
SURVEY OF LAW FIRM ECONOMICS
Executive Summary

ALM Legal Intelligence
The National Law Journal

In 2012, The Managing Partner Forum worked closely with ALM Legal Intelligence and *The National Law Journal* to conduct the most comprehensive survey of mid-size US law firms. 196 firms, with nearly 10,000 lawyers, participated.

The complete 338-page survey was released on August 6, 2012, and this Executive Summary was distributed shortly thereafter. The complete survey contains invaluable benchmarking data, which is broken down by firm size, practice, geography and a variety of other factors.

The survey is available for purchase at www.almlegalintel.com

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Survey of Law Firm Economics, 2012 Edition
Executive Summary

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Overview

The *2012 Survey of Law Firm Economics* survey contains information from 9,970 lawyers including 3,366 associates, 5,775 partners or shareholders (equity and non-equity), 577 active counsel and 179 staff lawyers working in 198 U.S. law firms. The financial and operating statistics provided by this survey cover revenue, expenses, billings, realization, assets, liabilities, billing rates, billable hours, lawyer compensation, and staffing ratios. Additionally, detailed information is provided by law firm size, geographic location, practice area specialty, population size, experience level of lawyers, and lawyer title. In its 40th year, the survey remains an invaluable tool for managers of law firms.

There are many ways to analyze a law firm's financial performance—its results of operations can be compared to the prior year as well as to annual budget, for one. It is more difficult to compare one firm to another because the metrics for any two firms are greatly affected by a number of factors. For example, the financial performance of a 100 lawyer firm cannot easily be compared in a meaningful way to the aggregate amounts of a 6– or 26-lawyer firm. In order to benchmark a firm's performance to other law firms in a meaningful way it is best to convert each firm's data into comparable statistics such as firm size or geographic area. In addition, there are numerous options available for looking at averages on a per attorney basis, including "per lawyer," "per equity partner" and "per fee earner" statistics. Each statistic may be appropriate in certain circumstances, but in general ALM recommends and references "per lawyer" statistics for most comparisons. Finally, it is important to select the correct data *point* for comparison purposes. For example, top tier firms in the New York marketplace should probably compare their performance to the Ninth Decile data point rather than the average of all law firms to facilitate accurate benchmarking.

Revenue Recedes, But Partner Pay Rises

From *The National Law Journal*, August 6, 2012
David Brown

Law firms, particularly midsize and smaller players, continued to face a challenging revenue picture during the last year, our latest survey of firm finances shows. But they appear to have done a better job of managing expenses to keep profitability and partner compensation high.

The Survey of Law Firm Economics, a joint project of *The National Law Journal* and ALM Legal Intelligence, shows that revenue per lawyer (RPL), a key indicator of overall firm health, was down on average among the nearly 200 firms surveyed. In fact, the 4.2 percent decline in RPL was the biggest since we began tracking the metric in 1985[1].

Yet firms reacted by chopping the average expense per lawyer by more than 4 percent. And as a result, equity partner compensation increased by a healthy 7 percent on average, topping $410,000. Non-equity partners weren't so lucky. Overall compensation for them dipped by 4 percent — an indication that firms continued to cut into their salaried ranks to save money. Not that there are many other places to cut: The survey shows that 66 percent of firm expenses come from salaried lawyers, paralegals and staff.

YEAR	AVERAGE EQUITY PARTNER COMPENSATION	ANNUAL CHANGE
2007	$374,000	+2.5%
2008	$353,000	-5.0%
2009	$358,000	+1.4%
2010	$383,000	+7.0%
2011	**$410,000**	**+7.0%**

Firms on the larger end of the scale took some of the hardest revenue hits. Those with 76 to 150 lawyers saw revenue per lawyer decline by 10 percent. For firms of 150 lawyers or more, the drop was 9 percent. At the other end of the size spectrum, firms of one to nine lawyers experienced a sharp 17 percent drop in RPL. But a caveat is in order: Last year, we didn't include solo practitioners among our smallest firms, and lower averages for solos may have skewed revenue-per-lawyer results for those firms. (The

[1] One caution with year-over-year comparisons: in the latest *Survey of Law Firm Economics*, the composition of the smallest size category now includes single-person law firms, which historically had not been part of this survey. As such, figures from this year's survey will be slightly lower than if single-person firms had not been included.

survey also slightly adjusted the size ranges for two other groups of firms. Firms now are ranked in groups of 10 to 24 lawyers and 25 to 40 lawyers—last year, the equivalent ranges were 9 to 21 lawyers and 21 to 40 lawyers.)

Despite the mixed results, firms still see plenty of sunlight ahead. We asked a series of questions about how firms view the state of the business of law. Seventy-six percent of those surveyed said they were optimistic about the year to come. And with minor variations, the optimism was shared among firms of all sizes.

NUMBER OF LAWYERS	OPTIMISTIC	PESSIMISTIC	UNCERTAIN
1-9	79%	7%	14%
10-24	68%	5%	27%
25-40	72%	2%	26%
41-75	84%	3%	13%
76-150	86%	0%	14%
150+	67%	0%	33%

Perhaps that's because firms expect a surge in litigation-related revenue this year. A strong plurality of firms cited litigation as the practice area that will see the most revenue growth in 2012. Large firms in particular were bullish about the practice. As we note elsewhere in this report, some 75 percent of firms with 150 lawyers or more expect litigation growth.

Corporate work is also looking promising, firms said. About a quarter of firms suggested that they would see the strongest growth in 2012 in their corporate practices. Given the market uncertainty of late, however, that prediction may prove overly sanguine. In a sign of a brighter economic picture, firms were far less likely to say that bankruptcy and restructuring work would grow this year. In our 2011 survey, 7 percent of respondents said they expected a bankruptcy bonanza. This year, it was 3 percent.

And while it's clear that alternative fee arrangements are part of the arsenal for the vast majority of firms (96 percent said 1 percent or more of their billings came from alternative fees), that doesn't mean firms are fast replacing the billable hour. Last year, 33 percent of firms said alternative fees represented more than 10 percent of their billings. This year, 34 percent said so. The needle is moving—but slowly.

Key Findings in 2012

Jennifer Tonti, ALM Legal Intelligence

Financials

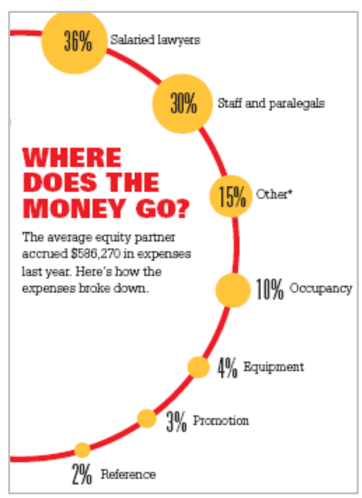
Average receipts per lawyer reported by participating firms totaled $432,242, representing a decrease of 4% from the prior year. Overhead expenses also decreased by 4% from the prior year to $161,904 per lawyer which, when combined with the revenue decrease of 4%, had a net negative effect on law firm profitability. And as go receipts and expenses, thus follows net income, with a 4% drop as well. Not surprising, the survey confirms the continuation of a difficult economic environment.

The following table illustrates the breakout of gross receipts and total expenses by law firm size. Clearly, as firm size increases, revenue, expenses and income increase in direct proportion.

Financials: Averages per Lawyer		Firms	Average Gross Receipts $	Average Total Expense $	Average Total Expense %*	Average Firm Income $	Average Firm Income %*
Size of Firm	1 to 9 Lawyers	14	532,717	282,378	53.0	250,338	47.0
	10 to 24 Lawyers	40	828,913	489,984	59.1	338,929	40.9
	25 to 40 Lawyers	41	744,161	393,015	52.8	351,146	47.2
	41 to 75 Lawyers	37	859,058	486,466	56.6	372,592	43.4
	76 to 150 Lawyers	27	1,020,140	609,176	59.7	410,964	40.3
	Over 150 Lawyers	11	1,345,038	821,844	61.1	523,195	38.9

**Percentage of Gross Receipts*

The relative magnitude of each individual expense is clearly apparent from the neighboring graph, which indicates that staff expense is the largest single overhead expense item for all categories of law firms, followed by occupancy expense (excluding the "other" category which is a catch-all expense comprised of malpractice insurance premiums and settlements, payments to retired partners and miscellaneous expenses).

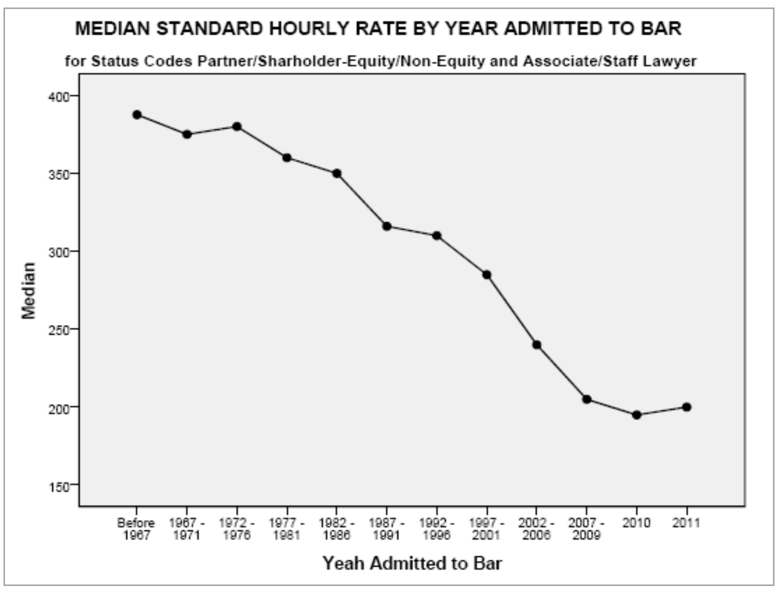


Billing Rates and Realization

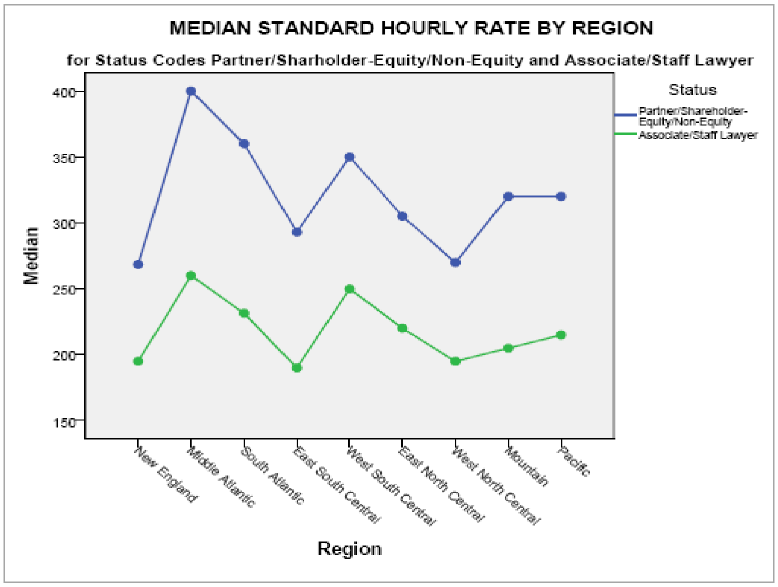
The flow of financial activity in a law firm involves the recording of billable time (by all law firm timekeepers, including lawyers and paralegals), the conversion of that asset, "unbilled time," to accounts receivable via the billing process, and ultimately the collection of fees when the client pays the invoice, or "realization."

As of January 1, 2012, the average hourly billing rate for equity partners or shareholders was $355. The average rate for associates was significantly lower, at $232 per hour. When looking at billing rates by gender, male equity partners bill more than female equity partners by about $14 ($342 vs. $356). Non-equity partners and associate billing rates are generally on par for both male and female attorneys.

Billing rates increase in direct proportion to experience practicing law, as the following chart illustrates:



And the same principle applies to hourly rates by firm size (as firm size increases, so does billing rate). Rates are also very contingent on geographic area as well; the median billing rate for an equity partner in Omaha, Nebraska ($300) will not be the same rate for an equity partner in a New York Metro-area firm ($400), for example.



According to the 2012 report, it takes the average law firm 2.2 months to realize accounts receivable. The billing and collecting process of every law firm is fundamental to the firm's financial success. One measure of a law firm's efficiency in this regard is the balance of unbilled time—or work-in-progress—the firm carries at any point in time. The larger the balance of unbilled time, as computed on a per lawyer basis, the less efficient the firm is in billing its clients. That is, the firm takes longer to prepare its billings to clients, slowing down cash flow. The following table provides selected unbilled time statistics from the survey about various categories of firms.

Value of Unbilled Time at Year End (Non-Contingent Fee Matters), Average per Lawyer		Firms	Average $	Lower Quartile $	Median $	Upper Quartile $	Ninth Decile $
Size of Firm	1 to 9 Lawyers	9	23,883	--	--	--	--
	10 to 24 Lawyers	34	45,986	22,322	37,731	66,803	86,290
	25 to 40 Lawyers	36	59,117	29,503	46,384	60,029	86,945
	41 to 75 Lawyers	35	53,370	42,893	54,674	62,438	78,809
	76 to 150 Lawyers	27	64,840	43,986	54,671	72,983	85,099
	Over 150 Lawyers	11	67,650	--	57,182	--	--

**Missing data indicates not enough respondents to analyze in that cell*

The average amount of unbilled time for non-contingent fee matters per lawyer for all participating law firms is $54,404, and the average for all size law firms fluctuates in a narrow range between $46,000 and $68,000. The small law firm category (firms with between 1 to 9 lawyers) should be treated separately from the other size firms in the group, as the value of their unbilled time is significantly lower than the other categories. This may be attributable to small firms managing their unbilled time more effectively than larger law firms, a function of the size of overall receipts the firms realize, or it may be an aberration since only nine law firms are included in this category.

Another means of measuring the efficiency and effectiveness of a law firm's revenue generating policies, systems and procedures entails the firm's realization statistic, which can be measured both in terms of billing and collecting. The table below provides information on these measures for law firms of varying size categories:

Average Realization Data (Standard Rates)		Firms	Billing Realization %	Collection Realization %	Overall Realization %
Size of Firm	1 to 9 Lawyers	1	--	--	--
	10 to 24 Lawyers	17	99.9	95.9	95.8
	25 to 40 Lawyers	28	91.0	95.4	86.9
	41 to 75 Lawyers	27	92.4	97.2	89.8
	76 to 150 Lawyers	15	87.4	95.6	83.5
	150 Lawyers or more	7	87.0	97.2	84.6

**Missing data indicates not enough respondents to analyze in that cell*

All size firms are generally about the same in terms of converting their unbilled time into client billings and then such billings into receipts. Firms in the 10 to 24 lawyer category are slightly more effective across all facets of realization, and it is interesting to note that the higher billing realization statistics reported by these firms is consistent with the notably lower balance of unbilled time reported in the prior graph. That is, small firms apparently billed as many clients as possible at the end of the year, which reduced their investment in unbilled time and increased their billing realization statistics. Conversely, law firms with over 150 lawyers carried a higher investment in unbilled time and were not as effective in converting that value into billings. Some portion of the larger balance of unbilled time maintained by these large law firms relates to the fact that they typically charge higher billing rates to their clients. Even if they carried the same number of billable hours as the smaller law firms they would report higher balances of unbilled time solely because of this rate differential. This rate differential at least partially explains the higher balance of unbilled time carried by larger law firms but it does not explain the lower billing realization reported by these firms.

Billable Hours and Alternative Fee Arrangements

The average partner (non-equity and equity alike) worked 1,642 billable hours. Associates recorded about 150 more billable hours (1,794) per annum. As with billing rates, there is a significant difference between the numbers of hours worked by lawyers in different size firms and types of markets as defined by the size of an area's population. Specifically, partners and associates in a "metropolitan division" (i.e., within a city's core area) tend to work more hours than do those located in a "metropolitan" area (in essence, an area within the boundaries of a major city but outside the core city itself) and significantly more than those in a "micropolitan", or rural area.

Though still the primary indicator of a firm's gross receipts, the billable hour has started to make way for approaches to billing that are not based on traditional hourly rates. Historically, firms had always talked about alternative fee arrangements, but until recently very little action followed. Then, with the economic collapse of 2008, corporations needed to cut expenses and nothing was left off the table, including outside legal costs. Alternative fee arrangements (or AFAs) obtained a new urgency[2], and firms have responded.

For the past two editions of the Survey of Law Firm Economics, we asked firms a few questions about AFAs, including to what degree the firms use them, and how the AFA volume has changed over the past year.

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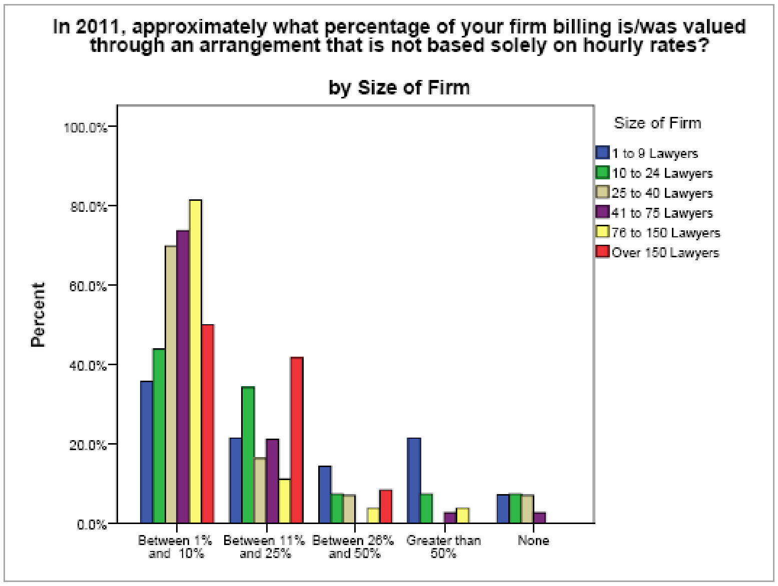
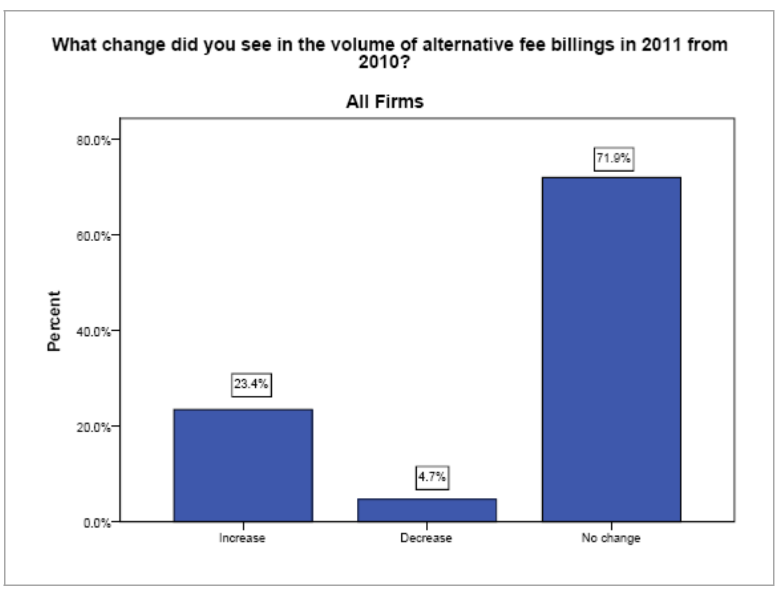
[2] For more information, please refer to ALM Legal Intelligence & Lexis CounselLink's 2012 report, "*Speaking Different Languages: Alternative Fee Arrangements for Law Firms and Legal Departments.*"



In general, just about all firms are turning to variations on the billable hour (not including discounting). Some of the most popular methods are flat fees, blended rates and capped fees. And although the billable hour still drives the boat, the pervasiveness of AFAs is growing: between 2010 and 2011, almost one quarter of respondent firms reported an *increase* in AFA billing.



Compensation

In 2011, the average equity partner/shareholder earned $409,624. The following table provides an overview of national data, although with more detail than just the averages for various classifications of lawyers. Where data was provided, we show the breakout of male and female attorneys at each lawyer status level and the differential between compensation for either group.

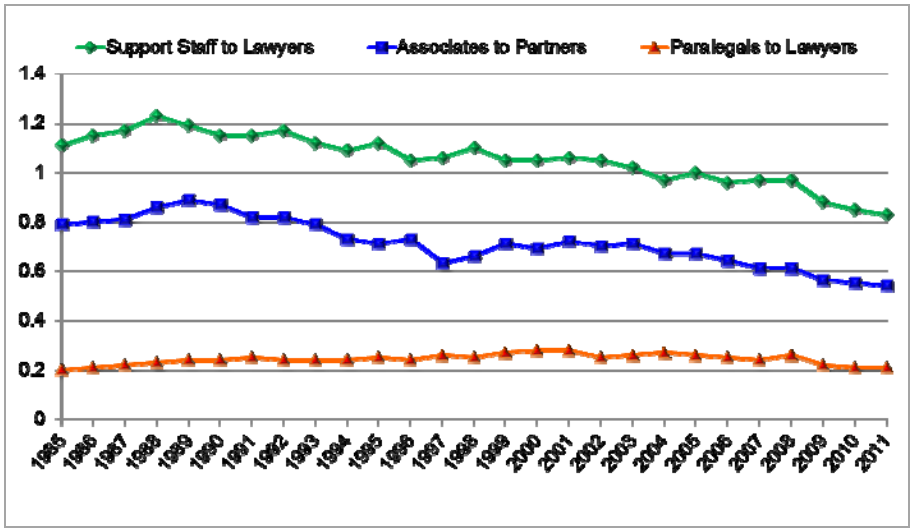
Total Compensation by Lawyer Status and Gender		Number of Offices	TOTAL COMPENSATION Number of Lawyers	Average $	Lower Quartile $	Median $	Upper Quartile $	Ninth Decile $
Female	Equity Partner/Shareholder	189	601	369,639	203,370	283,456	420,519	664,127
	Non-Equity Partner	126	362	222,578	162,892	200,000	260,434	349,235
	Associate/Staff Lawyer	207	774	137,861	111,822	132,625	158,496	188,626
Male	Equity Partner/Shareholder	295	2,647	399,876	241,771	337,990	469,704	665,068
	Non-Equity Partner	205	860	232,664	172,546	212,177	267,886	344,950
	Associate/Staff Lawyer	228	1,152	142,646	113,203	137,786	166,400	195,429

As with billing rates and hours, compensation levels will differ when looking deeper at size of firm, geographic area, metropolitan region and years of service.

Staffing and Personnel Ratios

The expense analysis referred to earlier in the Executive Summary highlights the fact that the largest single overhead expense for law firms relates to people costs. Accordingly, a law firm should strive to keep its ratio of support staff to lawyers as low as possible while ensuring that all client work gets performed on a timely basis and in a quality manner. The ratio of all administrative and secretarial support staff to lawyers is a comprehensive statistic that allows a firm to measure its operational efficiency. This statistic hovered around a 1.1 ratio for many years, but during the past five or six years this statistic has shown a modest but steady decline to the point where the ratio is now below 1 for many categories of firms. This has undoubtedly helped boost the profit level of those firms since small reductions in this ratio can have a significant impact on a firm’s profitability.

Leverage Ratios Over Time



In 2012, per 100 partners, firms are averaging:

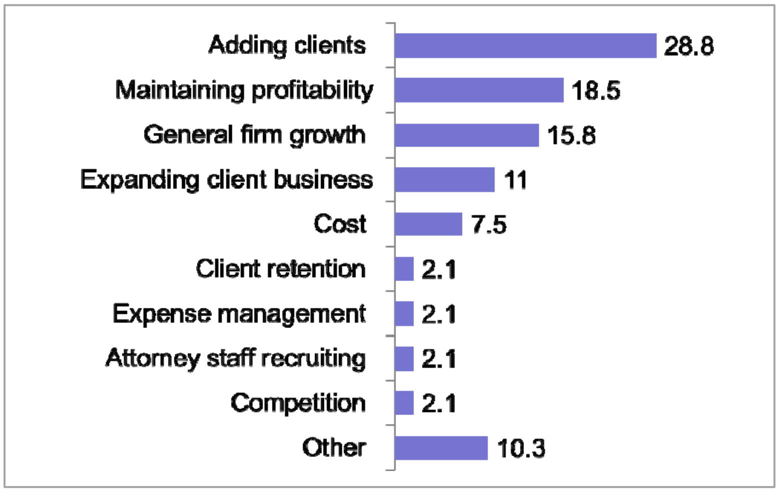
- 83 support staff
- 54 associates
- 43 legal secretaries
- 21 paralegals
- 20 administrative/clerical staff

And this downward trend appears to be continuing. When asked about how firms have staffed over the past year, the majority said that increases happened at positions with billable hour requirements (particularly at the partner level), and less so with non-attorney staff:

Percent Change in Staffing Levels, 2010 to 2011		Firms	%
Partners	Increase	74	37.9%
	Decrease	37	19.0%
	No Change	84	43.1%
Associates	Increase	72	37.1%
	Decrease	69	35.6%
	No Change	53	27.3%
Non-Attorneys	Increase	56	29.0%
	Decrease	71	36.8%
	No Change	66	34.2%

Biggest Concerns in the Year Ahead

As part of the Outlook questions we have charted for the past two editions, firms were asked about what issues were topmost in mind as they entered into the first few months of 2012. With no surprise, most firms chose issues that centered on positive indicators of firm health, such as obtaining additional clients and maintaining profitability.



General firm growth is third in priority, and can indicate either financial growth, acquiring clients or expanding staff, which firms can realize via a few key means, one of which is merging with other firms. Thus, a follow up question was asked regarding whether firms intend embark on a merger the next 5 years. Although the majority said no, 30-50% said that they were open to the possibility, and just under 10% were actively seeking merger partners. When looking at responses by firm size, it appears that midlevel firms are more likely to be open to mergers than their larger or smaller brethren.

We hope this summary is informative, but please note that it is only a fraction of the breadth of information and data points available in the *Survey of Law Firm Economics*. To inquire about purchasing a copy of this year's or previous year's editions, please call ALM Legal Intelligence at (888) 770-5647 or visit us online at www.almlegalintel.com.