Your Future; Is There a Merger There?
Are you going to follow the lemmings or setting your own course?

A recent article in the National Law Journal peaked my attention. It hit on a point that many middle market firms must consider too often. The article in the January 10, 2005 issue is titled “Mergers? Not Here Thanks.” Many firms not listed as mega-firms are asking the same questions - should we take an offer to merge with a larger firm? Here are some questions every partner and firm should ask before considering combining with any other firm.

What typically raises the question of possibly merging from inside the firm? Partners see larger firms encroaching on their clients or the firm loses out on new work to a larger firm. The big lease comes up for signature and there doesn’t seem to hold the firm together other than money. A great team player and profitable lawyer leaves for a larger firm. The brightest and best lawyers are beginning to ask how their career will be advanced with the current client mix of the firm. Partners are beginning to ask questions about leadership and the direction of the firm.

Does avoiding a merger buck the trend? It depends upon who you are listening to. Are you listening to the lemmings who believe in the myth of market share - the bigger you are the more profitable the firm will be? Are you listening to partners who want to be part of a bigger firm even though they know that many of their current partners will not be moving? Are you listening to the headhunters who are building corrals of potential candidates they can market to bigger firms for a fee? Or are you looking at the true trends that will drive your practice and your future viability? Here are the true trends and their implications that came from an in-depth assessment of the legal profession at two international conferences on the future of the profession.

Clients are moving toward being Consumers. They are no longer captives. The internet and the marketing activities of other firms are making clients more sophisticated in choosing lawyers that will best meet their needs.

Cases & Matters are moving to Relationships. Clients are more focused on the relationship with their lawyer based up trust and past performance. The name of the firm only applies to past work and where the clients did not feel they had other choices.

Production of Product is moving to the Creation of Solutions. Clients are looking for solutions, not products. Many lawyers think that their primary benefit is in providing a products like a contract but clients want a solution. That will mean that a lawyer must have multi-disciplinary support team to solve a problem. Lawyers who have the trust of a client are perceived to be their outside “general counsel” and perform that way.
Specialty groups are turning into Teams to Support Client Needs. Clients are no longer satisfied at being represented by a single section, like the tax section and then being referred to some unknown in another section. They expect their lawyer to be the leader of a team to solve their problem, regardless of what the problem.

Costs Plus Fee Setting is moving to Value Based Fee Setting. The larger firms and their partners are so entrenched in hourly billing that they cannot respond to client needs for predictability of fees relative the value of the transaction or litigation. Only in strongly lead firms can lawyers be convinced to take the risk of setting fees based upon client expectations.

Personal Profit Centers are moving to Collaborative Teams. In many larger firms compensation is set based upon the size the lawyer’s personal portfolio. But the market is moving to a demand for collaborative support teams which require a lawyer to share work with a team and provide team members with the compensation that will keep them interested in continuing the service to the client.

Avoiding Risks are moving to Building Partnerships. In the past lawyers have used the argument to trust them in their hourly billing. But clients are asking the lawyers to have a “horse in the race” and are asking for more contingency related fees. Who knows more about the risk than a lawyer who is dealing with the client on a continuing basis and is able to estimate those risks.

Capacity Driven to Client Driven. Capacity driven firms create problems by accepting marginal business and seeking volume over profitability which drives irrelevant growth and investment. Client-driven firms are more interested in the success of their clients than in their own profits. That turns the financial planning for many large firms upside down because instead of focusing on the firm profits and hours, the firm must focus on efficiency in delivering services.

So, Is there a Merger in Your Future?
There are three key models that will help you determine whether merger is in your future.

First divide your clients into four quadrants based upon a “y” axis of high and low loyalty to the firm and an “x” axis of high and low profitability to the firm. Those clients that fall in the high-high category are core clients. Those clients that fall in the high profitability and low loyalty are those which the firm must make concerted marketing investments. Those that fall in the other two categories are either question marks (should they be long-term clients) or dogs that need to be managed carefully or moved to other law firms.

The second model is called the Service Investment Model. In this model you are dividing the services the firm delivers into four quadrants again. The quadrants are high versus low depth in the ability to deliver services including people and systems on the “y” axis. And high versus low return on time in the “x” axis. The high and high indicates those services that are core to the firm. The high return on time but low depth are those areas that the firm must invest in and build. When considering a merger, this is a key factor in choosing the possible candidate. The
other two areas fall into the “move people” or “abandon.”

If the firm has good leadership and a plan for bringing in new leaders, then there is a plan for the future and a vision for the future, then there is a focus. Is there a vision for the future? Are there core values that hold the firm together? Is the leadership focused on that?

**FINDING YOUR MERGER SCORE**

There is a scorecard by which any potential merger should be judged.

In the paragraphs below, I have outlined the levels that a firm must progress through to understand what a merger may mean to the future. A firm must start at Level 1 in order to achieve Level 4. Starting at Level 4, focusing on “the numbers,” will produce a long-term disaster. For example, an “eat-what-you-kill” compensation system produces financial results but destroys the focus on the foundational building blocks of Levels 1 through 3. Levels 1 through 3 are what makes a combination successful.

**Level 1, The Vision Perspective - the soul of the firm.** There must be a vision for the combined firm supported by a set of core values that will support the vision. The key success factor for the combination will be a collaborative firm where every person is accountable to one another for the accomplishment of the vision and will operate within the core values. With a strong vision for the direction for the Firm, there will be a constant effort to seek new ways of delivering legal services and organizational learning to achieve the vision. Elements include but are not limited the following:

- Innovations in service to clients and to client relationship lawyers in the Firm. Constant develop of new ideas from diversified interests in the Firm who feel tied into the vision by the Firm’s leadership.
- Continuous improvement in service quality to understand and meet the needs of the clients.
- Continuous improvement in the ways services are delivered to cut cycle time of matters and costs for the clients of the Firm.
- Continuous improvement in the effective and efficient use of the intellectual assets and the accumulated experience of the Firm.

*Level 1 leads to Level 2*

**Level 2, The Internal Perspective.** These are the benefits perceived by the owners and employees of the firm and includes:

- Increases in the return on the time of professionals and the utilization of talent.
- Improved depth in the core competencies of the Firm.
- Continually improving standards of performance for both technical and service quality.
- Investment capital (emotional and dollar) for emerging needs of clients and those areas where the Firm must invest to sustain its relationship with core clients and enable the professionals who will be providing the core services.
Level 2 leads to Level 3

Level 3, The Client Perspective. This level includes:

- Improved cycle time on effort.
- Reduction in the number of issues moving into the legal pipeline.
- Efficiency in the use of client and Firm resources.
- Improved technical quality.
- Improved service quality.
- Fees are decreasing while service quality improves.

Level 3 leads to level 4

Level 4, The Financial Perspective. This level includes:

- Profits per partner go up.
- Growth in market share of desired matters.
- Financial and emotional equity value in the Firm on a per partner basis including:
  - Return on the time invested in the Firm’s efforts to serve clients.
  - Improvement of the franchise of the Firm and the probability of a continued flow of high quality business to the Firm.
  - Improvement in the probability of a stable revenue stream.

Many lawyers have some pre-conceived notions of what makes a merger successful or unsuccessful. Here are some of the discussion points.

- Mergers tend to work best when there is a strong assimilation process that brings the best core values from each.
- Mergers are too often based upon some faulted assumptions including:
  - Size equals quality and a strong competitive position.
  - Billable hours *times* Billing Rate equals value added.
  - Leverage equals profitability (even though the capacity of a law firm may have outpaced the demand for legal services).
  - Portfolio control is what drives firm profitability.
  - Any work is better than no work.
  - Pushing legal product (as opposed to client service) is what drives firm profitability. This leads to assumption that the firm can acquire hot practices and that they will naturally assimilate into the Firm’s mix.
  - These assumptions create the impression that:
    - A firm can provide any practice and make money.
    - All work is the same and can be serviced the same.
    - All clients have the same needs.
A successful merger of practices will require a strong vision of what the combination is supposed to accomplish. The combined firm must make choices about where it will invest to sustain and build core clients and core competencies (the core bundles of services). Those choices will drive the allocation of resources in:

- Marketing and client development.
- Developing services for clients.
- Building the depth of experience to serve the clients by staffing and training.
- Building substantive and expert systems manage the knowledge of the firm.

The Firms must develop and experience mix based upon the substantive areas of experience and the skills necessary to serve the core clients in the in the core competencies of the Firm. Those additional skills should include:

- The ability to understand the needs of clients and provide/sell the services that will meet their needs. The Firm is not selling legal product but a bundle of services that specifically respond to the goals and objectives of the client. Typical, but not inclusive, bundles of services may include:
  - Reduction in legal fees through more effective planning of projects and more efficient delegation of work.
  - Reduction in the cycle time for work performed when the client wants the issue resolved quickly.
  - Reduction in business risk of clients.
- The ability to effectively define, organize and efficiently direct the projects for clients.
- The ability to communicate the scope of work with the client and explain the costs and benefits of the work.
- The ability to build a strong and loyal relationship with a core clients and capture a large percentage of their work.
- The ability to effectively negotiate the legal work with the client to insure the client understands the value added by the Firm and understands and conforms to the financial obligations to the Firm.
- The ability to build a strong client support team within the Firm and delegate effectively.
- The ability to recognize the changes affecting core clients and structure a response that will put the Firm in a stronger competitive position with the core clients.

In summary the needs of the clients and the core services and values of the law firm should rule decisions on the direction of the law firm. If the considerations do not meet the criteria above, the firm should not consider the merger. Remember, if the core values do not fit, there is no merger. If the needs of the clients are not met, there is no merger. Be careful and vigilant - market share is not the key and sacrificing values for volume and compensation will be destructive.

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