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*THE AMERICAN LAWYER'S*  
**13<sup>TH</sup> ANNUAL LAW FIRM LEADERS SURVEY**  
**LAW FIRM LEADERS ARE OPTIMISTIC GOING INTO 2016**

*by*

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# THE AMERICAN LAWYER

Law Firm Leaders Survey

## Survey: Firm Leaders Are Optimistic Going Into 2016

Our annual Law Firm Leaders Survey finds managing partners hopeful, if uncertain, about their firms' prospects for next year.

November 30, 2015

Approaching the end of 2015, law firm leaders are positive about the coming year, but uncertainty is rising, results of The American Lawyer's 13th Annual Law Firm Leaders Survey suggest.

While hopeful, managing partners and chief executives are increasingly wary of economic and legal industry trends, including moderating economic growth, slowing demand for legal services and discounting pressure from clients. Thirteen percent of respondents said that they were "very" optimistic about 2016 with respect to their firms, the highest percentage in years, and 68 percent said that they were "somewhat" optimistic. But the percentage of leaders who said that they were uncertain about the year ahead jumped to 13 percent from 2 percent a year ago, and another 5 percent said that they were pessimistic. The growing uncertainty could be at least partly the result of volatile financial markets this summer. Respondents filled out the survey in early September.

Most respondents, 68 percent, said that they expected the U.S. economic recovery to maintain its current pace, but the next largest group, 21 percent, said that they were expecting slower growth. Only 11 percent thought that the economy would gain speed. In that, they resemble many business leaders who also were concerned about growth in the third quarter: U.S. real gross domestic product slowed to 1.5 percent from a 3.9 percent seasonally adjusted annual rate in the second quarter, according to the U.S. Bureau of Economic Analysis.

A large majority of respondents said that they didn't expect to be able to raise billing rates much next year, however, citing intensifying competition as a price constraint in follow-up interviews. Ten percent, the lowest percentage since 2009, said that they expected profits per partner (PPP) to grow more than 5 percent in 2016. By contrast, 24 percent of respondents in last year's survey said that they expected PPP growth in 2015 to exceed 5 percent. More partners than last year also said that they were considering asking partners to contribute additional capital in 2016.

As for head count, a majority of leaders (88 percent) expected at least a modest increase at their own firms next year, but they still planned on thinning the herd of partners: More than three-quarters said that they anticipated asking from one to 10 partners to leave in 2016, and another 6 percent said that they'd ask 11 or more partners to depart. Most said that they didn't expect to have to lay off associates or staff, although several firms already had some staff layoffs or buyouts this year, including Dentons and Latham & Watkins. "This year and the end of last year was the first steadily positive momentum for the legal industry in a long time," says Katten Muchin Rosenman chief executive officer Noah Heller. "We have seen some steady growth in demand, and it is staying that way

**EXECUTIVE SUMMARY**  
*Takeaways from the  
 latest Law Firm Leaders Survey.*



month after month." At his own firm, Heller says, 2015 has been "a slightly better year than we anticipated at the beginning."

But like other firm leaders, Heller says he's less confident about 2016. "The one big unknown that would impact a lot of transactional work and insolvency would be the Fed embarking on a series of interest rate increases," he says. "For me, the Fed and interest rates are the big unknowns."

Indeed, Citi Private Bank Law Firm Group's report, released in early November, found that demand growth for legal services slowed in the third quarter of this year, in contrast to the uptick that occurred in the same quarter of 2014 and third-quarter expense growth. The bank projects law firms' full-year revenues and profits for 2015 to be positive but lower than 2014 results. An Altman Weil Inc. annual survey of chief legal officers released around the same time found that 40 percent of law departments plan to decrease their spending on outside counsel in the next 12 months in response to "internal and external cost pressures."

#### GOING CORPORATE

Firm leaders are bullish on their corporate and IP practices for 2016. Asked which groups would increase revenue most, 36 percent of leaders surveyed cited their corporate practices, followed by intellectual property (21 percent), litigation (18 percent), real estate (16 percent, double last year's percentage) and bankruptcy and restructuring (4 percent, up from 1 percent a year ago).

Leaders' higher expectations for their corporate practices is a change from previous years. From 2009 through 2013, with the exception of 2010, only about 20 percent of firm leaders said that corporate would be their fastest-growing practice group by revenue in the coming year. Intellectual property gained ground in that period, though, surging to 21 percent this year from 9 percent in 2009. Litigation, on the other hand, dropped to 18 percent from the 42 percent of firm leaders who expected that practice group to bring in the most revenue in 2009.

Roughly 40 percent of firm leaders surveyed said that they thought that bankruptcy and restructuring would be the most financially challenged practice group in 2016. Jenner & Block managing partner Terrence Truax suspects that "some of the negativity is a result of people having expected [bankruptcy and restructuring] to turn around six months ago."

Another 28 percent of respondents said they expected litigation to come under pressure next year, and 21 percent said that corporate practice groups would be financially challenged. Intellectual property was cited by 6 percent and real estate by 2 percent.

Firm leaders also seem to be lowering their expectations for improved deal flow next year. About 65 percent of respondents said that they expected it to improve moderately, and 29 percent predicted that it would remain flat. Five percent expected a moderate decline in the number of deals. This was the lowest expectation for improvement in about four years. Last year, 73 percent of firm leaders said that they expected an increase and 25 percent expected no change; 2 percent expected a decrease.

68%

of respondents expect

34%

expect their firms to raise billing rates by 5 percent or less in 2016; 6 percent said the increase would be more than 5 percent.

73%

said they expect profits per partner at their firms to rise by 5 percent or less in 2016.

36%

expect to see the most revenue growth in corporate practices; bankruptcy and restructuring is forecast to be the most challenged area.

66%

said they expect their firm's head count to grow by 1-5 percent in 2016.

Of respondents expect the economy to recover at its current pace;

**21%**

expect slower growth.

Despite their overall optimism, leaders said that they didn't expect to be able to raise billing rates much: Ninety-four percent said that they expected to raise them by 5 percent or less, and 6 percent said that they would raise them more than 5 percent. That is the highest share to say their firms would be holding rate increases below 5 percent since 2009.

Perhaps because of the rate pressure, expectations for PPP growth were restrained. Seventy-three percent of respondents said that PPP would grow 5 percent or less in 2016, and another 13 percent said that profits would be flat. Ten percent expected growth of 5 percent or more, with the rest expecting a decrease.

Alan Waldenberg, chairman of Schulte, Roth & Zabel's executive committee and co-head of its tax group, says that "demand is not growing significantly, so to grow revenue you are competing against other firms for even the business you [already] have, which makes it tough."

The majority of respondents said that they expected the same or improving business conditions in Europe next year; just 17 percent said conditions in Europe would worsen. Firms had an average of nine foreign offices.

Latham & Watkins chair and managing partner William Voge said in an emailed statement that his firm "had another strong year, and we expect the tempo to continue," including growth in corporate, litigation, transactional and regulatory practices. "The combined impacts of globalization, disruptive technologies and industry consolidation are driving demand for legal services," he wrote.

Voge predicts that Asia will play a larger, more critical role in global transactions and multijurisdictional disputes next year. "Fifteen years ago, we saw strong growth in private equity and related finance in London and Europe. We're seeing the same patterns in Asia today, in particular where high-yield has grown to become a significant part of leveraged finance. For these reasons, we are optimistic about prospects in the region and our position to capitalize on the trends," he wrote.

#### ADDING BODIES

Two-thirds of leaders said that they expected overall head count to rise modestly at their firms next year, by 1-5 percent. The next largest group, 19 percent, said that they expected an increase of 6-10 percent, while 2 percent said that they expected to reduce personnel by 11 percent or more next year.

The overwhelming majority of leaders (96 percent) said that they didn't anticipate laying off associates in the remainder of 2015; 87 percent said that it was unlikely that they would lay off staff. Most leaders said that the size of their associate classes next year would be the same (53 percent) or larger (29 percent) than this year's. Eighteen percent anticipated a smaller class next year.

Despite reduced hiring of first-year associates during the recession, just 44 percent of respondents said they were worried about having enough midlevel associates in a few years. Last year, 52 percent of leaders said that they were concerned about a midlevel shortage.

Lateral partner hiring predictions followed the money, that is, the revenue: Eighty percent of law firm leaders said that they anticipated making lateral hires in their corporate group, followed by IP with 61 percent, litigation with 57 percent and real estate with 43 percent. (Multiple responses were allowed.)

At international firms, the largest group of respondents, 38 percent, said that they anticipated adding lawyers in London; 13 percent said that they expected to staff up in Tokyo. Twenty-one percent of respondents said that their firms were likely to venture into Latin America. (Again, multiple responses were allowed.)



A view from the top:  
Jenner & Block's  
Terrence Truax;  
Schulte Roth & Zabel's  
Alan Waldenberg;  
Katten Muchin  
Rosenman's Noah Heller

## PRESSURING THE PARTNERS

Despite the heated lateral market, few respondents—9 percent—said that they were worried about losing partners to rival firms. In fact, a majority of respondents said that they planned to thin their ranks of partners. About 67 percent said that they planned to ask from one to five partners to leave next year, up from 56 percent a year ago. But 17 percent said that they didn't plan to ask any partners to leave in 2016, which is more than last year's 13 percent.

Managing partners were anxious that their partners were not billing enough hours, however. About 71 percent of respondents said that they were somewhat worried about this, and 15 percent said that they were very worried. Perhaps because of those concerns, 54 percent of respondents said that they had de-equitized partners in the past year, and 56 percent said that they had plans to do the same next year. A little less than half of respondents (43 percent) said that they were worried about partners hoarding business that could be performed by more junior lawyers.

Slightly less than half of the respondents (47 percent) said that they did not have a formal plan for electing or appointing the managing partner or chairperson. "They are ignoring the whole situation," says Patrick McKenna, a legal consultant based in Edmonton, Canada. "It is a testy, sensitive subject matter."

Seventy percent of respondents said that they were concerned about partners staying on too long. In this year's survey, 29 percent of firm leaders said that their firms have a mandatory retirement policy. Among the firms that have a mandatory retirement age, it was an average 68.3, but 93 percent of leaders said that their firm makes exceptions. Twenty-seven percent of respondents said that their firm has an unfunded retirement plan, compared with 41 percent last year.

On average, respondents say that slightly more than 20 percent of matters on average were billed under alternative fee arrangements, up from 18 percent a couple of years ago. An average 14 percent of the firms' work was on a nonbillable-hour basis, little changed from the previous few years. Discounting is common: An average 60 percent of Top 50 clients receive rate discounts, respondents said.

Most leaders said that their firms use alternate staffing arrangements. Eighty-two percent said that they employ contract lawyers; 78 percent utilize secondments; 28 percent outsource to third-party nonlawyers; and 22 percent outsource to third-party lawyers. Another 14 percent said that their firms use shared staffing. (Multiple responses were allowed.)

## CUTTING BACK ON CREDIT

Despite low interest rates, firms are continuing to cut back on credit use. Though 61 percent of leaders said that their firms were carrying bank or other third-party debt, 39 percent said that they had no debt as of Sept. 2, the date when the survey was distributed, an increase from last year's 35 percent.

Fifty-three percent of respondents said that the amount of debt their firms were carrying was about the same as last year, and 34 percent said they borrowed less. The rest said they borrowed more. Seventy-four percent of respondents said that their firms' total debt amounted to 0-5 percent of net income, and 73 percent of firm leaders said that their firm's debt was 0-5 percent of assets. Eight percent said that their firms carried debt totaling more than 15 percent of assets.

"We have seen a gradual deleveraging over time," says Michael McKenney, head of credit origination for Citi Private Bank Law Firm Group, adding that the bank's internal surveys also have noted the same trend since 2010. He says that firms, especially the largest ones, increasingly use paid-in capital instead to finance large investments "typically matched to their long-lived assets," such as new offices and equipment. Gretta Rusanow, head of advisory services at Citi, says the shift to paid-in capital means that "there is still borrowing going on, but it has shifted somewhat institutionally to partner capital loans in some instances."



Law firm management consultant Edwin Reeser contends that the low debt figures cited by leaders therefore could be misleading. If the partners themselves are taking out full-recourse personal loans to contribute capital, the firm is still carrying debt, he says, just not at the enterprise level. It is typical of Am Law 100 firms to require equity partners to contribute 35 percent of projected income for a year, but the amounts are rising, he says.

For instance, in August 2012, Greenberg Traurig raised \$24 million from shareholders in its first capital call in a decade, requiring them to contribute from 1 to 5 percent more of compensation, which worked out to an average \$77,000 per partner. Over time, increasing capital requirements such as this can help destabilize a firm by making it difficult to attract new partners and retain existing ones, who may leave and demand return of their capital, Reeser says.

Twenty-one percent of this year's respondents said that they had made a capital call this year, compared with 24 percent last year and 18 percent in 2013. Twenty-seven percent said that they expected to make a capital call next year. Rusanow says that signaling capital calls in advance is good planning and "is a kinder and gentler way to treat partners."

But Reeser warns that "if the purpose of raising money is to maintain partner distribution levels, while at the same time grow, you have to be very cautious that you are not distributing more money than you can afford. That is what killed Dewey [ & LeBoeuf]. They simply distributed too much cash," Reeser says. "Law firms don't fail for lack of profits, but lack of cash."

#### **ABOUT THE SURVEY**

Each year, The American Lawyer sends managing partners in The Am Law 200 confidential surveys meant to assess their views on legal industry conditions and their firms' outlook. This year, 104 leaders responded. Seventeen percent headed firms of 1,000 lawyers or more; 6 percent firms of 800-999 lawyers; 14 percent, 600-799 lawyers; 23 percent, 400-599 lawyers; 34 percent, 200-399 lawyers; and 6 percent, fewer than 200 lawyers. Ninety-one percent of respondents said they had been on the job more than 10 years. None had been there less than four years.

Fifty-nine percent of respondents were from firms with more than 10 offices, and nearly a third were at firms with six to 10 offices. More than a fifth of the respondents' offices were in New York, 9 percent were in Chicago, and about 67 percent were in other major U.S. cities. Respondents said that their firms had an average of 9.1 overseas offices; the median number of offices was 4.5.

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