



Rethinking the Nature of Legal Services: *Challenges for Lawyers in a Time of [R]evolutionary Change*

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Georgetown University Law Center

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OVERVIEW OF PRESENTATION

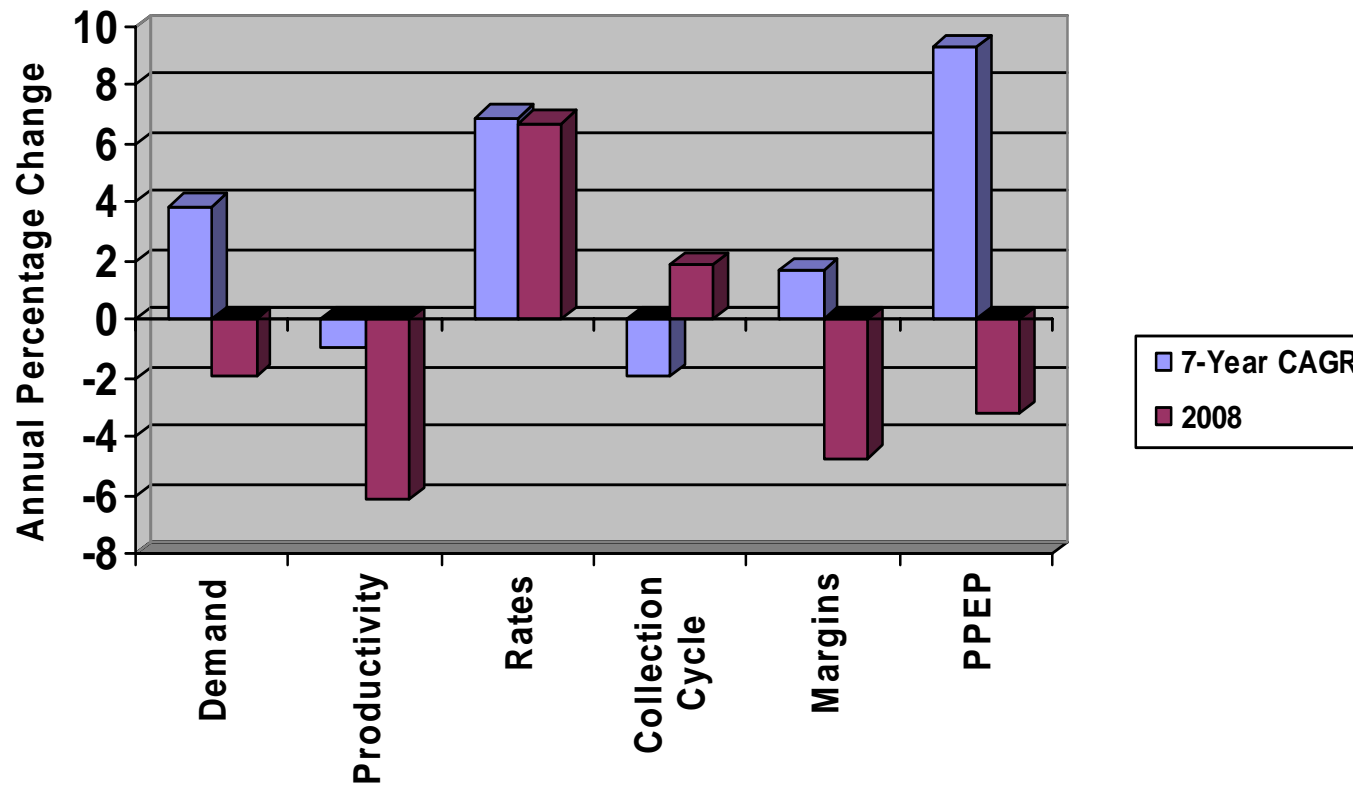
- Current state of the legal economy
- A deeper look – how the current crisis is forcing a shift in economic and practice models
- Emerging new models
- Implications for practitioners
- Implications for new lawyers

CURRENT STATE OF THE LEGAL ECONOMY

- The current downturn is the most serious economic crisis faced by the legal industry in at least half a century.
- It has resulted in dramatic drops in demand, productivity, revenues, and profits for law firms across the market.
- The impact of the downturn has been more dramatic because it followed a prolonged period of growth and profitability.

IMPACT OF THE CURRENT CRISIS

Key Economic Indicators 2008 vs. 7-Year CAGR



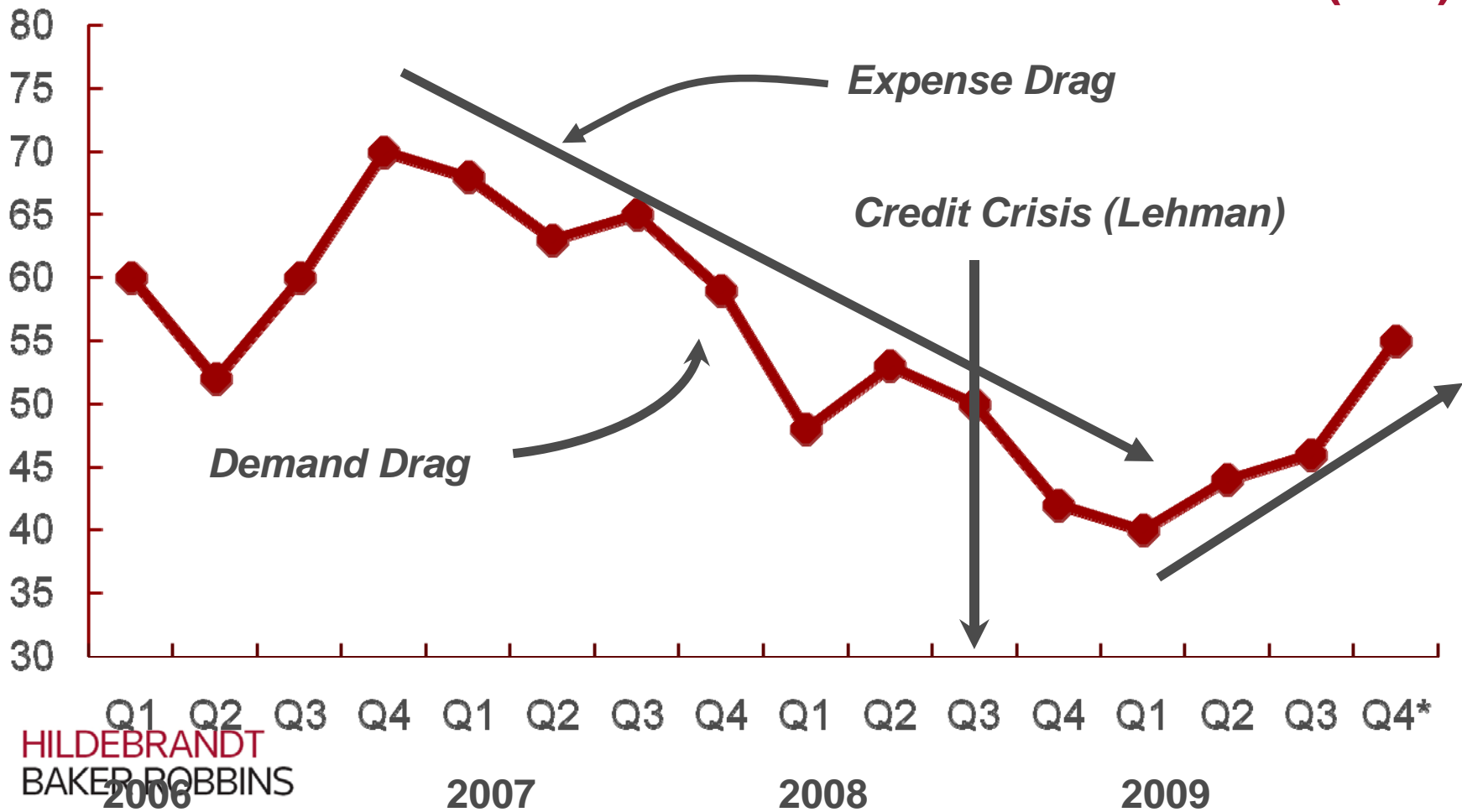
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Source: Citi Private Bank *Law Watch*

IMPACT OF THE CURRENT CRISIS

Q4 PMI Score: 55

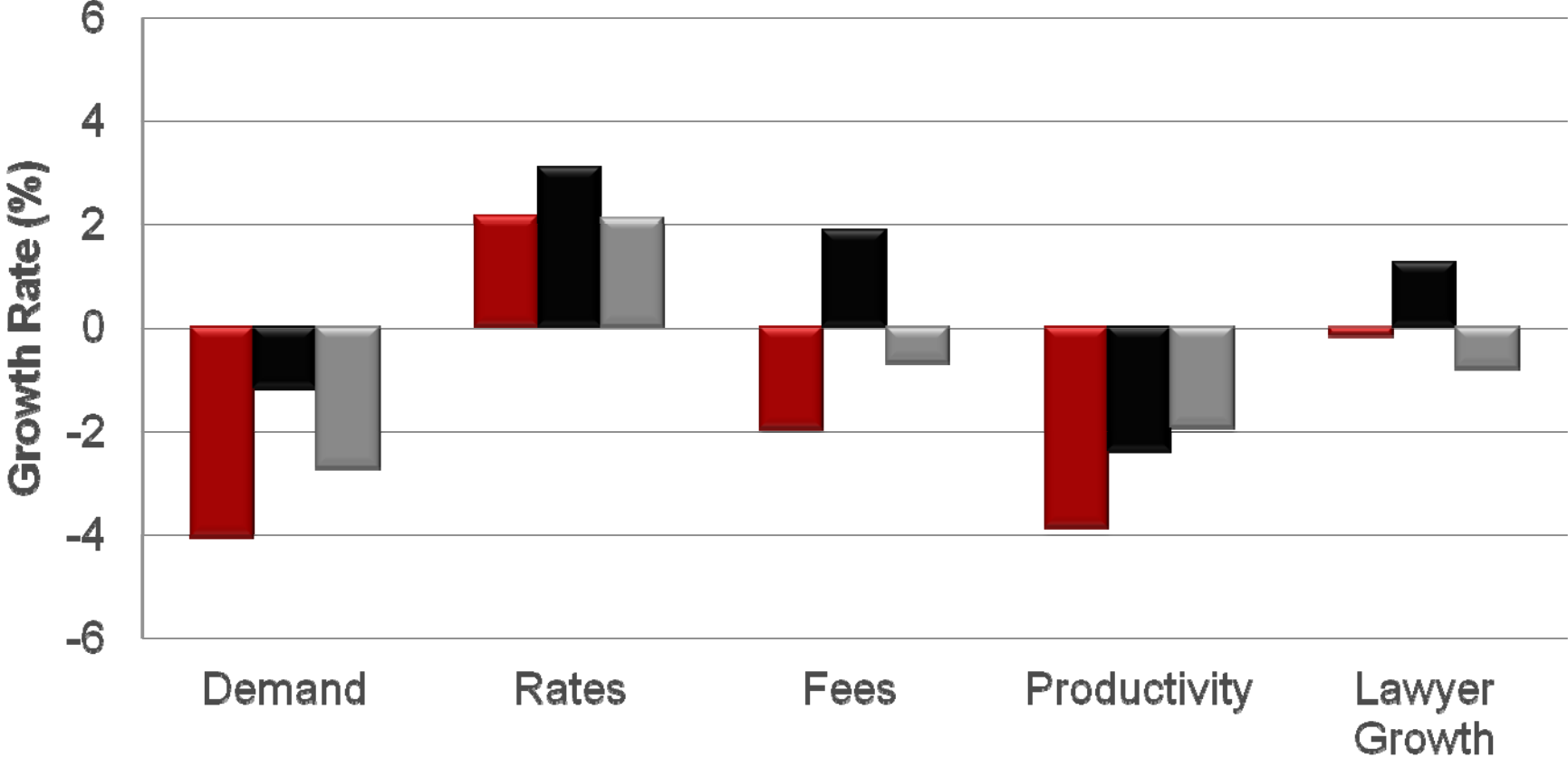
Peer Monitor Economic Index (PMI)



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PERFORMANCE BY SEGMENT

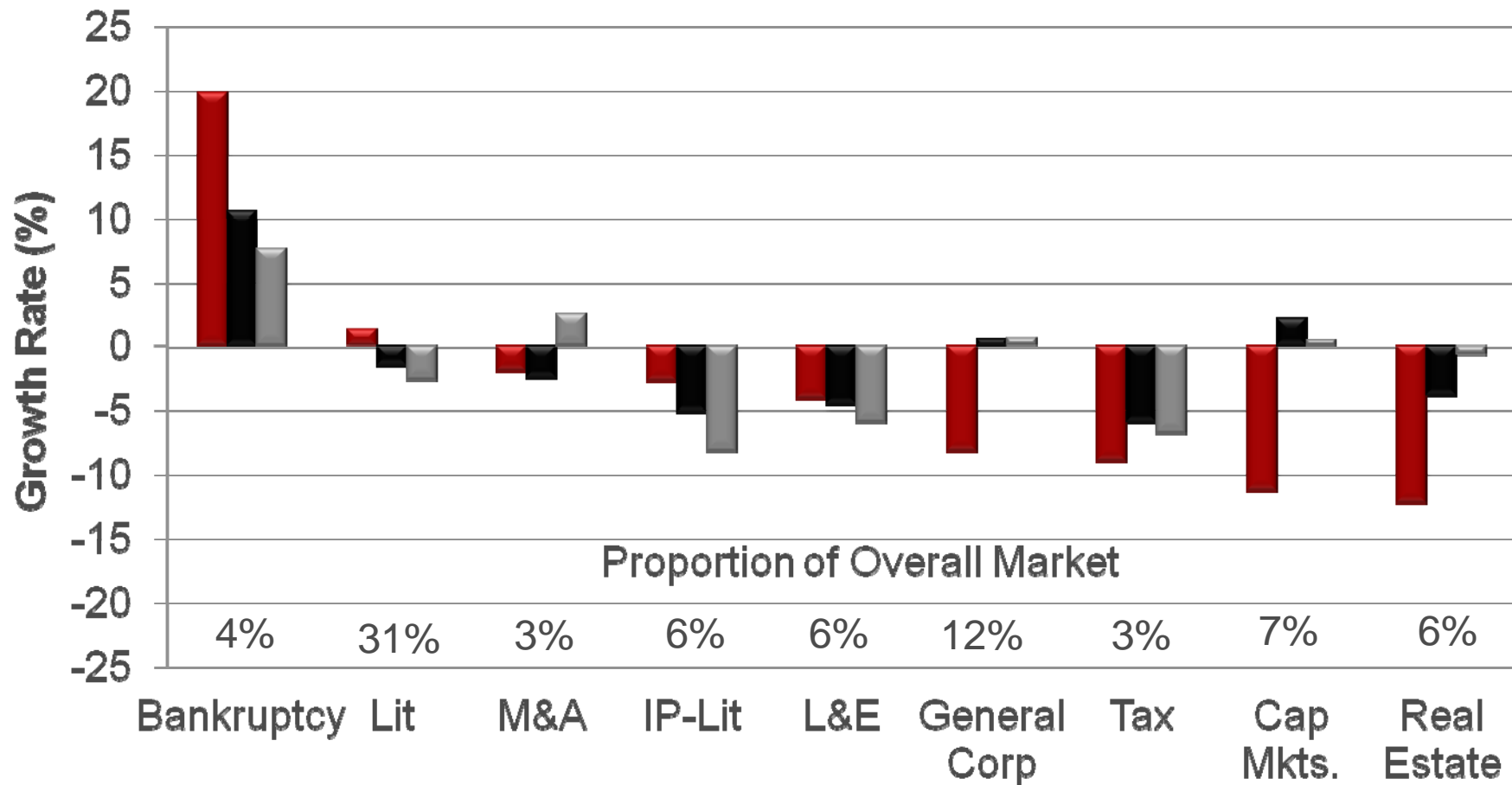
PERCENT CHANGE 2009 OVER 2008



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■ AmLaw 100 ■ AmLaw 200 ■ Mid-size

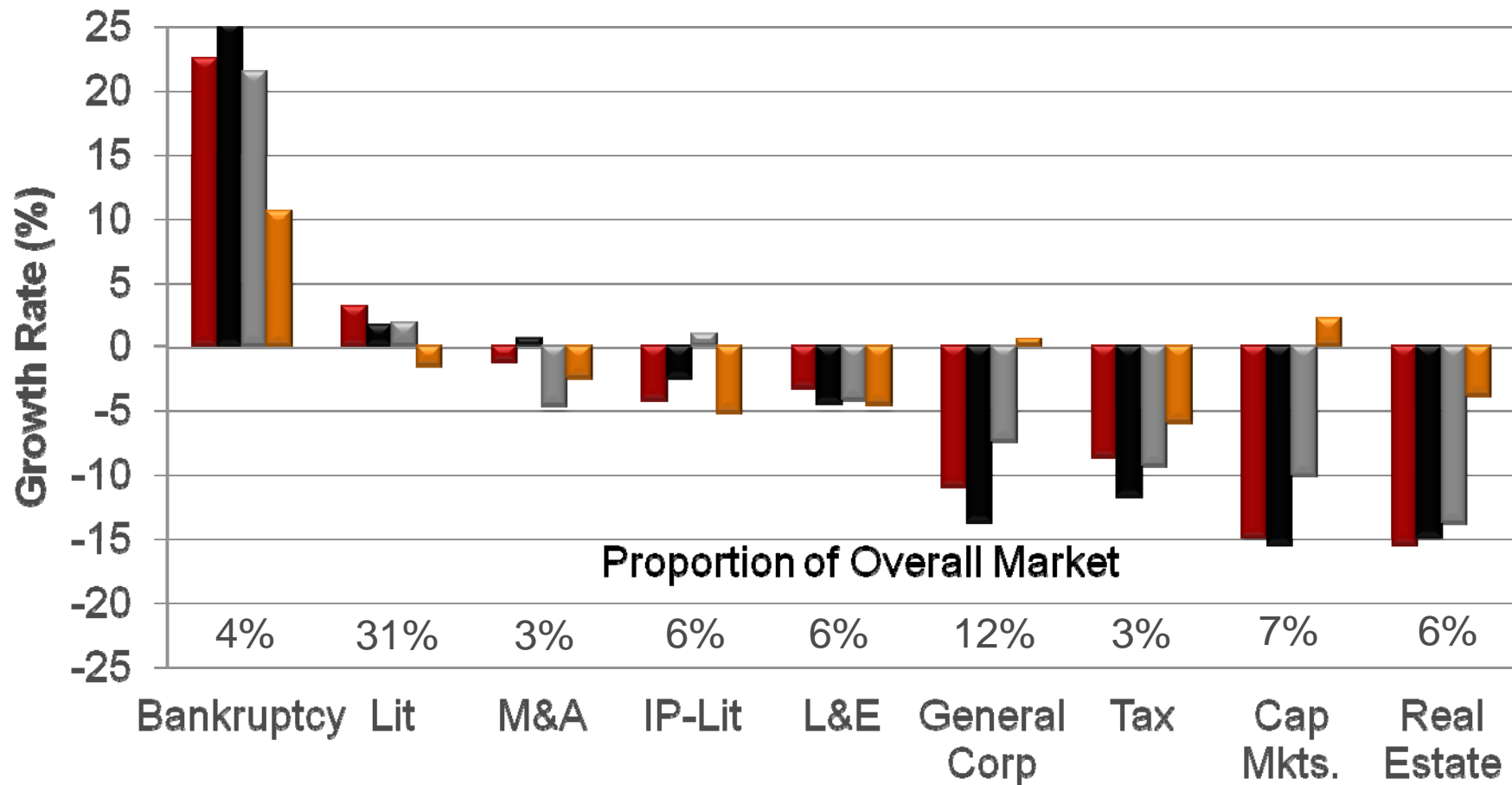
DEMAND GROWTH BY PRACTICE



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■ 2009 v 2008 ■ Q4'09 v Q4'08 ■ Dec '09 v Dec '08

DEMAND GROWTH BY PRACTICE (2009)



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■ Q1 ■ Q2 ■ Q3 ■ Q4

IMPACT OF THE CURRENT CRISIS

- Firms responded to the dramatic downturn in demand by slashing expenses – including particularly personnel costs.
- Collectively, in 2009, NLJ 250 firms laid off 5,259 lawyers – a decline of 4% in total lawyer population (compared to a 4.3% *increase* in 2008).
 - Associates were hardest hit, with an 8.7% reduction.
 - Number of equity partners remained fairly flat.
- Many firms also deferred starting dates for new hires, and a few even rescinded offers.

KEY QUESTION FROM CURRENT CRISIS

- Whether the current downturn is a cyclical “blip” or a harbinger of more fundamental and long lasting changes in the legal market?
 - Recent survey of leaders of AmLaw 100 firms showed many believe the latter is the case.
 - Hildebrandt survey of LEB Pebble Beach attendees supports the same conclusion. Percent of leaders expecting significant change in next 5 years:
 - Pricing models – 67%
 - Staffing of legal matters – 58%
 - Recruiting – 58%
 - Management of legal matters – 55%
 - Associate evaluation and advancement – 55%
 - Associate compensation – 55%

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**Even before the current downturn, the “old”
economic model for law firm structure and
management was under serious stress.**

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A DEEPER LOOK – THE “OLD” MODEL

- Key features –
 - Highly leveraged, premised on using *relatively* low-paid associates who could be billed out at *relatively* high hourly rates.
 - Pricing based essentially on the billable hour, a system that rewarded lawyers for the amount of time spent on a matter regardless of the profitability of the matter to the firm.
 - Heavy dependence on significant (6-8 percent) annual rate increases to sustain growth.
 - No significant incentives to drive efficiencies in the delivery of legal services.

A DEEPER LOOK – THE “OLD” MODEL

- A talent management system premised on high turnover.
 - An “up or out” approach that recognized value only in partners and “partners in waiting”.
 - Essentially a “sink or swim” mentality.
- Work process and support systems that were almost completely lawyer centric.
 - Deep suspicion of value of non-lawyer professionals.
 - Reluctance to partner with other professionals in multi-disciplinary approaches to client problems.

A DEEPER LOOK – THE “OLD” MODEL

- Overall, model premised and focused far more on growth and expansion than on efficiency and cost effectiveness in the delivery of legal services.
- The “old” model worked fine, as long as –
 - Associates were in ample supply, would work hard, and could be paid less, and
 - Clients tolerated constantly escalating rates and did not question efficiencies in service delivery.

It produced a 20-year run of extraordinary growth.

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**While the “old” model produced
extraordinary results, ultimately
it proved unsustainable.**

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DRIVERS OF LAW FIRM PROFITABILITY

Leverage

Productivity

Rates

Realization

Expense Management



Profitability

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DRIVERS OF LAW FIRM PRODUCTIVITY

Level

Productivity:

- Declining steadily since the late 1990's.
- Driven by associate pushback to unsustainable billable hour requirements.
- Aggravated by a "seller's market" for talent that drove up salaries as productivity declined.

bility

Expense

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DRIVERS OF LAW FIRM PROFITABILITY

Leverage

Leverage:

- Struggle to maintain leverage as:
 - Firms hired more associates to make up for declining productivity and
 - Firms made partners at a faster pace than the firms were growing.
- Most firms sustained or grew their leverage but at a very high cost.

ility

Expense

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DRIVERS OF LAW FIRM PROFITABILITY

Leverage

Realization:

- Dropping fairly steadily in years just prior to downturn.
- Reflected increasing client demands for discounts and resistance to “premium” arrangements.

Ability

Expense m

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DRIVERS OF LAW FIRM PROFITABILITY

Leverage

Expenses:

- During years prior to downturn, expenses grew at a much faster rate than inflation.
- Principal driver was rapidly escalating associate salaries – followed by space and technology costs.

Profitability

Expenses

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DRIVERS OF LAW FIRM PROFITABILITY

Leve~~X~~age

Pro~~X~~ductivity

Rates

Real~~X~~ation

Expense ~~X~~management

Profitability

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LOSS OF RATES AS A RELIABLE DRIVER OF PROFITABILITY

- Prior to the recession, firms were raising rates at a clip of 6-8% per year – well ahead of annual inflation rates.
- Partly as a result, the overall costs of legal services grew exponentially – ultimately to a point that strong client resistance became inevitable.

LOSS OF RATES AS A RELIABLE DRIVER OF PROFITABILITY



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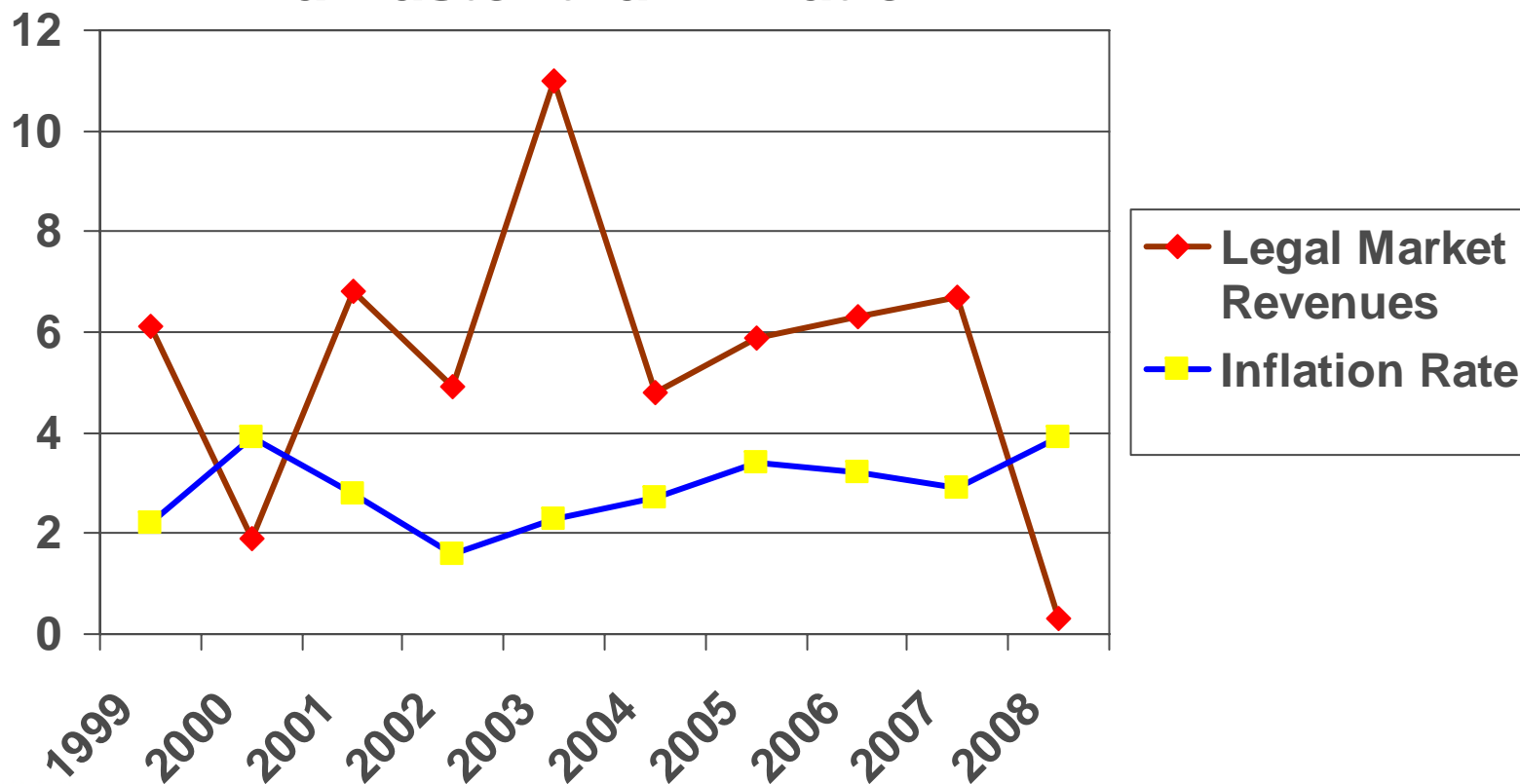
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■ Revenue in \$Millions

Source: U.S Census Bureau: Service Annual Survey.

LOSS OF RATES AS A RELIABLE DRIVER OF PROFITABILITY

Legal market revenues have generally risen far faster than inflation.



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Sources: U.S. Census Bureau: Service Annual Survey and
U.S. Bureau of Labor Statistics.

BREAKDOWN OF “OLD” MODEL

- Rapid escalation in cost of legal services over past 10 years, coupled with the current downturn, has produced sharp client “push back” --
 - Little tolerance for “routine” rate increases;
 - Expanding use of competitive proposal processes;
 - For billable hour based matters, continuing demands for discounts, blended hourly rates, capped fees, multi-year fee arrangements, etc.;
 - Expanding use of alternative (non-hourly based) pricing arrangements;
 - Growing determination to bring economic interests of client and law firm into alignment.

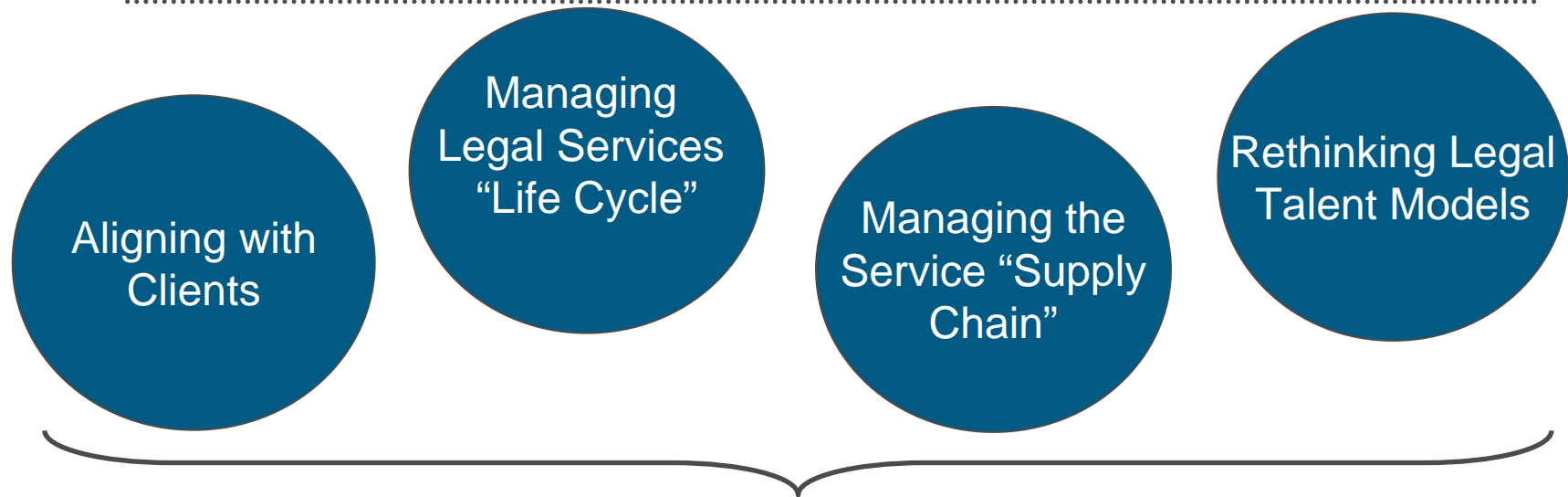
BREAKDOWN OF “OLD” MODEL

- There is increasing evidence of shifting client focus to overall “value” in purchase of legal services.
 - Continuing demand for predictability.
 - More emphasis on efficiency and cost effectiveness in service delivery.
 - More willingness to disaggregate services to achieve efficiency and cost savings.
 - More willingness to change law firms.
 - Less willingness to pay for the training of new lawyers.
 - Growing sense of client empowerment to control the lawyer-client relationship.

For the foreseeable future, we are likely to be dealing with a “buyer’s market” for legal services.

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TOWARD NEW ECONOMIC MODELS



Law firms that are considerably more creative and flexible in:

- Pricing legal services
- Designing and managing legal work processes
- Recruiting, managing, and retaining talent
- Partnering with other service providers to achieve efficiencies
- Engaging in creative problem solving with clients

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**All of these changes in the economic models
of law practice will be enhanced and accelerated
by pervasive – indeed, disruptive -- changes
in legal technology.**

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DISRUPTIVE TECHNOLOGIES

- “Disruptive technologies” are new, innovative technologies that periodically emerge and fundamentally transform companies, industries, and markets. They are distinct from “sustaining technologies” that simply support or improve the way a business or sector already operates.*
- Within the next few years, we will likely see such rapid and fundamental changes in technology impacting legal practice that all such changes to date will seem almost insignificant by comparison.

DISRUPTIVE TECHNOLOGIES




On-Line Legal Guidance
and Services



On-Line Sharing of Legal
Knowledge



E-Learning



Work Flow and Project
Management



Embedded Legal Knowledge



Electronic Legal Marketplace

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TOWARD NEW PRACTICE MODELS



Disruptive Technologies

Practice models characterized by:

- Continuous emergence of new methods, systems, and processes to reduce the cost of undertaking “routine” legal work
- Growing pressure to “routinize” even complex legal matters
- Increased sharing of costs by clients through recycling of work
- Shift in role of lawyers from “gate keepers” to “facilitators”

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IMPLICATIONS FOR PRACTITIONERS

- Combination of market forces and rapidly changing technology will drive subtle but very significant shifts in the way lawyers work and relate to their clients in the future.
- **View of Client**
 - Shift from normative view of lawyer as keeper of unique knowledge advising a client who has no access to such knowledge.
 - Shift from lawyer as “gate keeper” to lawyer as “facilitator.”
 - Significant economic implications – as disintermediation expands.

IMPLICATIONS FOR PRACTITIONERS

- **View of Client Relationship**

- Shift from norm of customized, one-on-one relationships to a model of one-to-many knowledge sharing.
- Significant ethical implications under a system that views one-on-one representation in litigation as the normative environment for legal practice.

- **Mode of Working**

- Shift from lawyer as independent “guru” to lawyer as collaborative partner – both with clients and with other professionals.
- Recognition that legal issues always arise in broader contexts.

IMPLICATIONS FOR PRACTITIONERS

- View of Client Interests

- Shift away from assumption that clients are *only* interested in maximizing their legal rights.
- Recognition that client may define “value” very differently from the lawyer.

- Focus on Prevention

- Shift from “pathology” to “preventive care.”
- Understanding that an important part of the lawyer’s role in the future will be to help clients prevent problems *before* they arise.

So . . . what does all this mean for you?

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IMPLICATIONS FOR NEW LAWYERS

- In the short-term, the hiring market will remain depressed.
 - While there are preliminary signs of a bottoming out and slight upturn in demand, the recovery is not likely to be robust.
 - Most firms will continue to be very cautious in 2010.
 - Hiring quotas are likely to remain well below normal for another year or so.
- Students in elite law schools may not feel the effects quite as much as others, but no one is completely immune.

IMPLICATIONS FOR NEW LAWYERS

- From a longer term perspective, this is a good time to be starting a legal career.
 - Demographics are on your side.
 - You will have a wider range of options – both within law firms and elsewhere – than ever before.
 - You will be entering a profession where innovation and creativity will be rewarded as never before – creating whole new models of competitive services.
 - You will be part of the generation of lawyers that, in all likelihood, will have the chance to re-define the practice of law and the fundamentally re-shape the way lawyers relate to their clients.



Questions and Discussion

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Thank you.

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