

Facing facts

Are too many law firms failing to plan effectively because they delude themselves that the challenges of the new market won't affect them? **Nick Jarrett-Kerr** offers potential solutions to the biggest problems facing firms of all sizes over the next few years

One of the biggest challenges facing law firms today is not an external threat, but an internal problem: the capacity which lawyers have for self-delusion. It has often been said that there are three basic types of lawyer – those who make things happen, those who watch things happen and those who ask 'what happened?' Few and far between will be the firms which can say they have no partners in the last category.

This article addresses the biggest problems facing law firms, both large and small, over the next few years, and suggests solutions. It focuses not on the most obvious areas of competitive challenge posed by the Legal Services Act 2007 (LSA 2007), but rather the ideas – the delusions – held dear by many firms which are most likely to mean solicitors bury their heads in the sand, and do not respond effectively to the changes happening around them. Seven of the most common delusions are outlined below.

“WE ONLY DO HIGH-LEVEL WORK”

I hear many mid-sized law firms argue that the LSA 2007 will not affect them, as they focus on 'high-level' work, and think the only major market entrants will be corporate bodies like Co-operative Legal Services, which will only be interested in the bottom end of the market. It is the small high street firms which will be affected, they argue; their own, mid-sized, firms will be immune from such new competition.

In many cases, this is a dangerous fallacy. Informal surveys at many firms reveal that, contrary to partner perception, high-level partner-intensive work is the icing on the revenue cake, and not the cake itself. Some estimates suggest that as much as 70% of the work done by most general firms is either bread-and-butter work or work that can be done by relatively inexperienced staff, albeit under supervision and in accordance with sophisticated systems and matter management processes.

Large firms are finding this out the hard way when their global clients increasingly challenge high charging structures for routine work which could be done in low-cost centres at 20% of the cost of a junior lawyer at a London law firm. The challenge here is, therefore, not just from non-traditional legal service providers following deregulation, but from innovative law firms, some based outside the UK or outsourcing to non-UK suppliers, and from the growth of internet-based DIY legal services.

“WHEN THE RECESSION IS OVER, ALL OUR WORK WILL COME BACK”

I am worried by the number of lawyers who tell me that volumes of work and levels of profitability will normalise once the recession is over. The question is whether a rising economic tide will lift all boats.

Clients can outgrow firms, move away from the locality, or change jobs, so fresh relationships need constantly to be forged

The problem is threefold. First, many law firms have cut their fees in order to keep work levels up, and it will not be easy for them to raise those rates again if and when the tide turns. I hear of commercial property clients who have managed to negotiate fixed-fee decreases of at least 40% over the last two years; those clients will refuse to see those rates go back to 2007 levels.

Second, in many areas of the market, such as conveyancing, there is now a large oversupply of lawyers. This is already giving rise to intense competition for available work. It is likely to be some time before the supply-demand pendulum swings back.

Third, the demand for legal services often lags some way behind any upswing. I fear, therefore, that better economic times – whenever they come – will take a long time to benefit law firms in general, and will come too late to rescue many ailing firms or practice groups

“ALL OUR CLIENTS WILL REMAIN LOYAL”

The maintenance of strong client relationships rightly remains a huge competitive weapon for law firms. The existence of secure personal bonds with leading clients has enabled small and medium-sized firms to retain very significant clients who might normally be expected to use larger or better known firms.

Again, however, I can identify at least three problem areas. First, there is the obvious truth that, although some friendships endure for a long period, many relationships tend to atrophy naturally over time. Clients can outgrow firms, move away from the locality, or change jobs, so fresh relationships need constantly to be forged and new clients sought. Second, some client loyalties are to individual lawyers rather than the firm, so they can be lost if the partner leaves, retires or dies. Third, client loyalties seem to have become somewhat strained during the recession. One reason for this might be that, whilst loyal and long-standing clients are not always as fee-sensitive as new clients, they may still, in some cases, feel that advantage has been taken of them, or that they have been taken for granted. This means that reliance on the loyalty of an existing client base carries enormous risk; key clients, once lost for all these reasons, may become impossible to replace.

*Your business
needs you*



NOW

“WE ARE EFFICIENT AT USING TECHNOLOGY”

There may be some firms which have managed to achieve optimal use of technology, but many are way behind the curve – much further than they might think. High secretarial ratios in the legal profession still reflect a somewhat inefficient use of technology – there are still many partners who have one-to-one secretaries. Anybody starting a law firm from scratch would staff the firm as leanly as possible, relying instead on heavy investments in systems, technology and sufficient knowledge management to enable menial and administrative tasks to be carried out by lower paid (and less qualified) staff rather than expensive lawyers. Working practices are hard to alter in existing law firms.

Incremental improvements have proven to be slow, and can easily stall at an intermediate plateau of efficiency.

“WE ARE WELL MANAGED AND DISCIPLINED”

It is fair to say that, over the last decade, I have observed a steady improvement in law firm management and in partner behaviour and discipline. Nevertheless, there is huge room for efficiency gains in just about every law firm in the UK. In addition, the way in which partners manage their people, their time and their priorities is, in some cases, embarrassingly poor. There are a few private equity houses which are interested in investing in the legal sector, and most of them see the imposition of strong management and appropriate accountabilities and discipline to be one of the key areas where they can add value, with a view to gaining a return on investment. For the last 50 years or more, lawyers have led a fairly cosy existence, with high profits continuing to accrue from traditional working practices and comfortable work ethics. The brutal truth is that these comfort zones are shrinking fast, and the firms which have acted quickly to bring about efficiencies and accountabilities are steadily gaining ground, in both profitability and the ability to compete.

“COMMERCIAL LAW IS OUR ROUTE TO SUCCESS”

It is good to see private client law coming back into fashion after some years of disfavour. Even so, I still encounter many medium-sized, and even quite large, firms which think that they can and should field impressive teams in a wide-ranging portfolio of commercial legal services. This is by no means easy. Larger commercial clients are looking for depth in both expertise and resources. A single partner or small team in the heavy-lifting areas of commercial and corporate law does little to impress corporations. Clients and potential recruits both ask similar questions of firms: “Why should I choose you, when I have a bewildering choice of leading firms in your area?” Of course, there has been room for some firms in cities and regions to have established a competitive position in many areas of commercial law, and those firms may well be able to continue to develop and prosper. But firms with only the beginnings of a commercial offering may find it more and more difficult to gain traction in this market, unless they have a very strong sense of ambition and vision, accompanied by the appetite and ability to invest heavily in the long term.

“WE ARE WELL KNOWN AND HIGHLY REGARDED”

It is very easy to get carried away by one’s own propaganda. Firms which carry out independent name recognition surveys amongst their client bases and communities often find this a chastening experience. The legal sector remains very fragmented, and there are very few well known law firm brands. Good branding enables potential clients to know who you are, what you do and how to get hold of you. However good their lawyers, a majority of firms in every region continue to be well kept secrets. Again, investment in branding can be a heavy cost which firms find hard to resource, even where the case for investment has been agreed. But firms which proactively manage to make their voices heard in a noisy marketplace will continue to stand out in the crowd. One way for smaller firms to achieve this might be to join one of the growing numbers of umbrella organisations which provide branding, training and quality support.

Continued on page 24

Continued from page 23

WHAT CAN BE DONE?

Despite the obvious problems, there are still huge opportunities for law firms and new entrants alike to take advantage of a fragmented and incoherent service sector. Now is a time when the fast will overtake the slow. New entrants have the advantage of being able to start with a blank piece of paper to construct structure systems and brand, and they may come to the sector with deep investment pockets to kickstart their operations. But they have no clients, no reputation and no people. Innovative and assertive law firms, on the other hand, have the huge advantage of an existing client base and established teams of talented people.

To make sure you make the most of this advantage and don't get left behind those revered solicitors who 'make things happen', you could start by conducting an honest self-appraisal of your firm, ascertaining which of the delusions above are present in your firm, and ensuring those myths are debunked where necessary.

The second stage would be a thorough appraisal and assessment of the strategic options and choices available to your firm to make sure it gains a decent competitive position. These options fall into three distinctive areas.

1. THE FOUNDATIONS FOR COMPETITIVE STRATEGY

Firstly, the firm should consider exactly what it is that makes it, or is likely to make it, competitive, such as a focus on a particular sector or a full range, strong client relationships, or a price-based strategy.

Analyse the types of client you work with, and in what sectors; what the range of your service portfolio is or should be; consider differentiation strategies based on positioning, such as a sector or specialist focus, local dominance, or client relationships; and address the potential for price-based strategies.

Where the building and maintenance of strong relationships with clients and referrers is seen as a vital part of the firm's recipe for success, those relationships must be nurtured and renewed, not only through your people being nice to clients, but also by the firm providing them with services that they will continue to find valuable. The basis for a firm's competitive strategy is largely client-oriented and externally focused. If the clients can see no added benefit or advantage from selecting a particular firm, then that firm is not likely to develop a winning competitive edge. What is clear is that the firm must decide how it wants to be seen in its market, what position in this market it wishes to occupy, and what type of client will provide its core custom in future.

2. STRATEGIC DIRECTION

Secondly, consider the overall strategic direction the firm needs to take in order to build the competitive position which it has, at step one, established that it needs.

Now is when the firm needs to consider consolidation and growth; the rationalisation of the business model; development of service range, technical expertise or overall capabilities; increasing its market share and market development; geographical expansion; and diversification, which could include becoming an alternative business structure.

Do we need to grow in order to have the depth of specialism that we need to provide a compelling client proposition, and if so, by how much? Do we need to develop our resources and capabilities in order to service the clients for whom we aspire to

Firms must recognise that a compelling competitive strategy will require risk-taking and a huge degree of change in attitudes

act, and the required depth in each practice area? Do we need to expand into other towns or regions or do we still have ample opportunities to build market share in existing areas?

As for diversification, the new regime heralded by the LSA 2007 will, of course, give both existing law firms and new entrants to the market the opportunity to pursue a strategy of unrelated or partially related diversification into the legal services market. But there is no one-size-fits-all approach, and firms need to consider carefully what might work for them. What, if any, are the synergies with what we do? What are the entry barriers? What is the likely cost of the investment and what is the likely return? How difficult will it be to acquire the people and build the systems, processes and infrastructure? How easy will it be to build the brand and successfully take our offerings to the market?

3. METHODS OF PURSUING STRATEGY

Once a firm has established its basis for competitive differentiation and has decided its overall strategic directions, it can then turn to the final of the three areas – how best to pursue the firm's strategy. Methods might include organic development; internal efficiency; the drive of high-performing people; merger; team acquisition; alliances; brand investment; or external investment to fuel expansion. This part of the strategic thinking will necessitate a thorough appraisal of the firm's existing resources and momentum to reveal whether a combination of organic growth and operational improvements will suffice to carry the firm forward. In some cases, if the firm wants to expand, heavy investment capability will be needed. In many areas of private client and consumer law, for instance, firms are seeing the benefits of persistent and well thought-out advertising campaigns, but the heavy cost of a long-term marketing budget needs both resolve and access to funds.

MAKING IT COUNT

Fortune favours the bold. If firms are to fight off their existing and threatened challengers and beat their rivals, they need to start by honestly and openly assessing their strategies and making sure that they are not lulling themselves into a false sense of security. They must recognise that a compelling competitive strategy will require risk-taking and a huge degree of change in attitudes, behaviours and working practices amongst partners, who will be required to experiment and learn new ways of doing things.

And if they don't, some firms and partners will discover, too late in the day, that they are left asking ruefully, "what happened to our practice?". ■

Nick Jarrett-Kerr (nick@jarrett-kerr.com) is one of the UK's leading advisers to firms on strategy and governance. He was a founder member of the Law Management Section and author of *Strategy for Law Firms – After the Legal Services Act* (Law Society Publishing, 2009).