Law Firm Merger Business Case Development: The 'Script' is Evolving with the Times

By Michael D. Short on December 6, 2022

Something interesting is happening in the world of law firm merger matchmaking and due diligence. Specifically, the order of importance for the key components of the vitally important *compelling business case* is shifting for some (typically larger) firms. These clients are focused on their number one need for expanding their excellent client service capabilities – finding a critical mass of excellent talent. With this shift comes a new *primary* merger-search criterion that has been assumed to be either aligned or fixable for many years – culture.

"Find us talented lawyers who are like us and share our values via similar cultures. Then, if the goals and economics are reasonably close, we can figure the rest out."

No sound law firm merger comes together without a compelling, exciting, and energizing business case. Each business case has three universal elements – financials, strategic goals, and culture – along with any number of supporting areas of focus, depending on the needs of the transaction at hand. These elements coalesce into a storyline that is the framework for the first 'go/no-go' decision as each party determines if the business case is strong enough to justify additional (and perhaps significant) time, money, and stress in evaluating the opportunity at hand. A sound, win-win business case is the basis for creating the vision of what the two firms can do together that neither can do alone. It is also the key message used to sell the deal to each partnership and, ultimately, get the appropriate level of official support come voting time.

The business cases for potential mergers in the 90s were fairly easy to identify and develop. Back then there were *many* more candidate firms of enviable size and sophistication of practice because industry consolidation was just starting to really take off. A few firms were leading the way toward regional or national platforms and the recession of 1990-1991 shook the confidence of some law firm leaders in their ability to continue independently.

From a merger consultant's perspective, these were the very easy years. In those days, if the Key Performance Metrics (e.g., revenue per lawyer; profits per equity partner) were within a 5%-7% range, you had the foundation of a "great" business case. The strategic alignment wasn't a major consideration because, back then, the industry was quite homogeneous. Many firms were more focused on doing what their competitors were doing and racing to the middle rather than differentiating from them, which comes later (in history and in this piece).

As for culture at that time…well, it was a minor consideration because offering something different here was still years away. The industry was transitioning away from the apprentice model but that type of thinking was still pervasive. All firms said they were "collegial" and "professional" and that was about the extent of any due diligence exploration of the cultures…and it worked.

Recall that the 2000s started off with a recession as well (in 2001). The impact of this recession on the legal industry was that it became time to strategically differentiate and find sophisticated means to beat the competition and take market share. This shift had a material impact on the law firm merger world wherein criterion #1 shifted from economics as the "lead punch" to strategic alignment.

How do any two law firms super-charge the implementation of both firms' strategies? Where do they supplement and complement each other? How does the potential new firm take market share from competitors by offering something unique and different?

Financials shifted into the #2 spot and the range of acceptable variances around the Key Performance Metrics stretched into the low double-digits. Law firm leaders needed more wiggle room to close the deals because a) the industry was consolidating and the pool of ideal economic matches had dwindled and b) the compensation spreads of most firms were widening with the rapidly improving economics of all law firms. Expanding compensation spreads facilitated the "slotting" of most/all Partners from a slightly less profitable firm into an acquiring entity.

Meanwhile, culture held strong in position #3 but the focus on talent attraction and retention was building steam, often as part of the implementation of the sophisticated strategic plans being developed. Experts were starting to evaluate and measure cultures, which were becoming points of differentiation for young lawyers in particular.

Then, several events over time aligned to elevate the focus on talent and flip the priorities in the corresponding business case script. Those events included:

1. The big recession of 2007-2009, during which the demand for legal services slipped dramatically (in Q4 of 2008) and law firm leaders had to learn how to operate in an environment wherein the supply of talent exceeded the demand for services (for a short period of time). Suddenly, retaining the *right* people and managing the talent pool became an existential challenge and talent strategies developed in earnest. Then, as the economy healed and demand for legal services recovered, attracting and retaining the right people moved to a featured position in many strategic plans.
2. A global pandemic, which thrust the law firm business model (including the corresponding talent strategies) a decade into the future. We all went home and the geographic component of the practice of law came under serious scrutiny. People were working from all sorts of interesting locations while the development of firmwide talent strategies lagged.
3. The subsequent, insatiable, and frenetic demand for Associate talent (that is now ebbing…perhaps equally dramatically) that could only be met by incredible – some would say irrational – increases in compensation levels combined with promises for many to work from "wherever you are." This "geography-free" approach to recruiting was a true paradigm shift.

Now, talent strategies have become featured components of law firm strategies and, by extension, the mergers used to implement the strategies. Only a handful of firms can compete for talent on money/compensation without limitation. The rest must differentiate via their core values, mission statements, work environments, philosophies toward professional development, work from home policies, dedication to pro bono, and their communities…all elements of the broad umbrella known as "culture." For firms with this type of focus, strategic alignment is now criterion #2 and financial fit is criterion #3…with an even wider range of tolerance around the numbers. Misalignment across any of these core business case elements can still kill a deal, but the ability to bend/give more on strategic and financial alignments is greater for firms who truly seek a critical mass of "good lawyers who are like us and share our values via similar cultures."

This shift makes "matchmaking" very interesting. We cannot rely on the descriptors most lawyers use because few can move beyond "collegial" and "no jerks" to any meaningful degree. There is no large database of trusted cultural evaluations to draw upon, although the measurement tools exist, but have not yet achieved broad-based acceptance in the law firm world. Since the featured elements of "culture" vary from firm to firm, alignment here starts with comparing behavioral norms, philosophies, management styles, work ethics, expectations of lawyers, and any other soft measures to see if a potential spark exists. Then, the key people need to get to know each other. If a mutual trust level starts to develop, followed by a combined focus on what the parties can do together, then we can get serious about the process.

One could argue that culture has always been the critical criterion in the law firm merger business case because no one wants to practice with people who don't fit into their professional community/family. That is probably true but, over time, events in and around the marketplace have forced "culture" to evolve from an assumed similarity to a tangible and describable differentiator that is critical for strategic success. Therefore, we should not be surprised when we increasingly hear law firm leaders say, first and foremost, "we are looking for people like us."