What a Difference a Decade Makes for Law Firms…

By Joseph B. Altonji on August 9, 2017

It's hard to believe the inflection point that marked the beginning of so much change in the legal world occurred ten years ago today on August 9, 2007. That was the day BNP Paribas closed withdrawals from three funds citing an inability to value them, marking the beginning of what was to become the global credit crisis. Adam Applegarth, then CEO of Northern Rock (one of the first bank victims of the crisis) ultimately called August 9th "the Day the World Changed." He was referring to the financial world (and maybe the world in general), but it applied equally to law. The markets froze up that day and transactional legal practices everywhere went from 120% capacity utilization to just about 0%, almost overnight. Things loosened up a bit within a few weeks, but those events were the first shot across the bow for lawyers and everyone else. Between that day and the collapse of Lehman Brothers 13 months later, the world was clearly on a major slide toward and ultimately into, crisis. We all remember how that played out.

Enough time has gone by that we tend to forget how the legal industry worked back then (and many of today's young law firm partners were still in school), but consider the following:

- In early summer 2007, the talk in New York was about *which* law firm would be the first to increase law firm associate starting salaries to $200,000 (not $180,000). Not *if*, but *who*. Because of August 9th, it never happened. Most firms froze (and some cut) associate salaries, stopped all hiring, and started reducing head counts a short time later. There wasn't a generalized raise in the industry until 2016, almost a decade after the last raise.
- Prior to August 9th, there was a simple 3-variable formula for making money in large firms: 1) Engage as many smart new law firm associates as possible, billing them out full time at whatever the market would bear; 2) Raise lawyer billable rates regularly at a much higher rate than inflation; and 3) Get the client's work done on time (usually). Most of that is gone for good, though not the "on time" part.
- Clients started demanding, and getting, pricing cuts in the wake of the crisis. Before August 9th, they asked but didn't make demands.
- Technology was a necessary cost center but could be ignored by some senior partners who had their secretaries print their e-mails for their handwritten markups and responses.
- The average law firm secretary supported at most two lawyers and sometimes only one. Powerful partners got whatever they wanted by way of support and often that meant dedicated resources.
- Alternative Fee Arrangements (AFAs) were commonly discussed but rarely used. Legal Project Management (LPM) had barely gotten started and was not widely known, and the term "process improvement" likely recalled *Cheaper by the Dozen* (the *original* book and movie) rather than anything in the legal world. As a rule, partners were left to manage matters as they saw fit.
- Artificial Intelligence (AI) was a thing for movies and techies but not on the minds of most lawyers.
- "Competency Models" were barely recognized and lockstep dominated.
- And generally, law was a supply-driven industry where law firms could drive ever-increasing law firm profitability with limited effort.

What a difference a decade makes. In the depths of the crisis, the Chair of one global law firm told me, "If we don't change the way we do everything, in five years we'll be dead." Driven by economic crisis and a simultaneous client "awakening," law firms have pushed for and driven change to meet ever-increasing client pressures and demands. Along the way, the best firms have found new formulas to drive their own success while still meeting and exceeding client expectations. The biggest have grown much larger, more profitable and more global, while great law firms of all sizes have opened gaps with their local peers. They have found a way to thrive even while benchmarking data shows the demand for commercial law firm *time* has flat-lined for almost a decade. That Chair's law firm? Far larger and more profitable today than it was back then.

Clients want, *and are willing to pay for,* solutions to their consistently growing legal challenges. They just want them handled efficiently, and they discriminate far more between routine and truly important matters. The legal world has gone a long way toward remaking itself to deliver on this. Consider:

- The use of alternative fees for legal services has at least tripled in the last decade and continues to grow (even while some firms say their clients just aren't interested). Microsoft's new Strategic Partner program is just one of the latest moves which will drive up AFA usage, with a goal of getting to 90% AFAs within 2 years (from 55% today.)
- Legal project management and legal process improvement have become widespread and even law firms that have not fully embraced them pay lip service to efficiency and the need to deliver cost-effective solutions.
- As an industry, we have cut back tremendously on "traditional" resources such as secretarial support and law firm office space but have diverted those resources to develop new capabilities in pricing, legal technology support, LPM, law practice management, and other critical skills.
- Artificial intelligencce solutions are driving time and cost out of legal processes. Once common law firm revenue drivers, such as discovery, research, and other time (read: law firm associate) intensive tasks may soon no longer be done by law firms – or at least by *people* at law firms. Many (including me) worry how we will ever train the next generation of partners.
- Venture capital is pouring into the legal space, recognizing that opportunities exist to drive real value from legal innovation and change. The world has come to realize that law really is a business.
- Increasingly, technology is changing the basis of competition among law firms, making it possible for smaller law firms to compete effectively for more sophisticated assignments.
- Clients have disaggregated their legal spend, hiring lawyers, law firms and mixed teams, using alternative legal service providers, and bringing work in-house, all to find the best value mix for achieving their legal goals.
- Demands on law firm partners have never been higher, as law firms force the issues of performance, law firm culture management and accountability. Partnership is no longer a tenured position, and "culture" is no longer a good excuse for not making tough decisions. (Though culture remains a challenge in many firms – See Mike Short: *"Is Your Culture Putting Your Firm At Risk."*)

It simply isn't true, as I've noted elsewhere *("Is Disruptive Innovation in Law Even Possible?")*, that law firms are bad at innovation. Aided by outside investment, client demands and internal pressures, law firms consistently drive sustaining innovation. And while we have not yet seen the formula that completely disrupts the legal industry, this does not mean that real change hasn't occurred. Law firms everywhere will continue to respond by driving changes demanded by their clients.

The legal industry is not the same as it was ten years ago when the global crisis began. The pace of change right now is dramatic, but we often don't realize that as it happens in real time and around us. We are all playing a part in the re-make of the legal industry. It will be interesting to see what the *next* decade brings and what I will say in my update on August 9, 2027!