Altman Weil, Inc.

Report to Legal Management

September 2003
Volume 30, Number 12
OUR 29TH YEAR

Are Large Law Firm Mergers Successful?

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At a recent meeting of the executive committee of an AmLaw 100 firm discussing merger as a strategy, one member challenged me to "name one successful merger of large law firms," and then went on to say, "I am not aware of a single success." Taken aback, I cautiously responded that it was my impression that most major law firm mergers would be considered successful, at least in financial terms.

That question resonated with me over subsequent weeks and inspired me to team with Altman Weil consultant Debbie Rhodunda to analyze recent large law firm mergers in terms of the primary objective measure of success, that of profitability as measured by profits per partner. Most mergers contemplate increasing profits per partner, at least over the long term. Few firms would enter a merger that promised to decrease partner incomes.

Our analysis of changes in profits per partner is based mostly on *AmLaw 100/200* figures published by American Lawyer Media, partly on figures from *Legal Business* and *The Lawyer* in London, and partly on our direct knowledge of some of the firms' performances as a result of our work with them as clients. In the few instances of discrepancy between published figures and those provided to us by the firms via their financial statements in the course of consulting engagements, we opted to use the latter. We have not presented any individual firm data here to protect the confidentiality of those figures provided to us by our law firm clients.

We selected 17 law firm mergers involving 300 or more lawyers over the last ten years. The 17 selected mergers involved 33 firms (one firm was involved in two of the mergers). The average size of the "lead" firm (larger of the two) was 441 lawyers at the time of merger. The average "acquiree" was 169 lawyers, for an average total merged firm size of 610. The largest merger, measured by total numbers of lawyers involved, was Clifford Chance/Rogers and Wells. The smallest was Blackwell Sanders/Peper Martin (Kansas City and St. Louis) in 1998. Table 1 on page 12 lists the firms involved in the mergers studied.

Short Term Success

As a baseline, we used the profits per partner of the larger or "lead firm" in the year pre-merger. We compared that number to the profits per partner of the merged firm in each of the first two years, post-merger (for one recent merger, only the first post-merger year figure was available). We did

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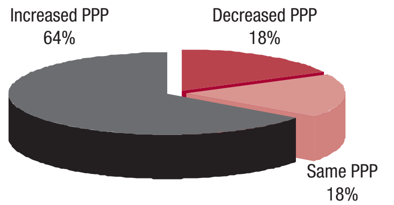
this short term analysis because conventional wisdom suggests that transaction and integration costs would be expected to reduce PPP in the first year or two, whereas longer term PPP would be expected to grow.

The results were revealing. We found that in the first post-merger year:

- Three firms experienced reduced profits per partner.
- Three firms' profits per partner were the same as pre-merger.
- Eleven firms experienced increased profits per partner.

Figure 1

Short Term PPP, Post Merger — Year 1

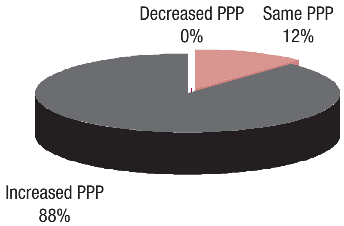


In the second post-merger year:

- Zero firms reported a reduction from first year profits per partner.
- Two firms reported the same profits per partner as in the first year, and
- Fourteen firms reported an increase in profits per partner from the first year.

Figure 2

Year 1 to Year 2

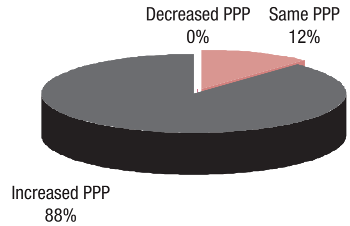


Second year profits per partner compared to starting or "lead" firm profits per partner:

- was the same in two firms; and
- increased in 14 firms.

Figure 3

Pre-Merger "Lead" Firm to Year 2



The results seem to disprove the conventional wisdom that PPP should not be expected to increase in early post-merger years.

Scope or Scale — Does it Matter?

Merger is a strategy, not in itself a goal. It is a means to achieve any number of strategic goals, including diversification, geographic growth, increasing market share, building depth or critical mass, among other possible objectives. Generally, mergers intended to build depth are termed mergers of scale, while those intended to expand product lines or services or to access new geographic markets are referred to as mergers of scope.

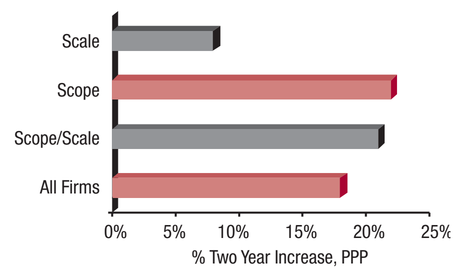
We further examined the 17 major law firm mergers and concluded that although most could be considered as some combination of scale and scope, the primary objective of three of the mergers was scale, as they were basically expanding in existing geographic markets in existing practice areas or specialties. Nine of the mergers appeared to be primarily mergers of scope to pursue geographical expansion (five), practice area expansion (two) or a combination of geographic and practice area growth (two). The remaining five mergers appear to be equally both of scale and scope, involving substantial growth in an existing or new location with significant strengthening of one ore more existing practice areas. We have not identified which mergers fall into these categories, as some are so small that it could compromise confidential Altman Weil client information.

The following chart indicates year one, year two and cumulative growth in profits per partner organized by type of merger.

Primary Strategy	Year One	Year Two	Two Year Cumulative
Scale	-2%	+10%	+8%
Scope	+9%	+11%	+22%
Scope/Scale	+13%	+7%	+21%
All Firms	+9%	+8%	+18%

Figure 4

Short Term (Two Year) PPP by Type of Merger



Thus it appears that scope or combined scope and scale mergers generally produced greater short-term economic improvement in profitability than pure scale mergers. In a sense, that is understandable, as scale mergers require greater integration of cultures earlier, and thereby could be expected to be more disruptive.

Scope merger successes were comparable whether the objective was either geographic or practice area expansion, but less so where the objective appeared to be both geographic *and* practice area expansion. Strategic focus thus appears to add value.

Scope Merger Purpose	Year One	Year Two	Two Year Cumulative
Geographic	+10%	+13%	+26%
Practice Area	+14%	+11%	+24%
Both Geographic and Practice Area	0%	+8%	+9%

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Long-Term Experience

Finally we looked at those seven mergers that occurred over four years ago (1999 or before). Since 1999, PPP has increased 21% in those firms, on average. The AmLaw 100 PPP figures since 1999 have increased 13%. (See Figure 6) By this standard, large law firm mergers seem to have achieved their financial objective over the longer term, as well.

Conclusion

Who says large law firm mergers don't work? From a profit perspective, it appears they generally do, both in the short and longer term. It also appears that scope mergers pay off better and sooner than scale mergers and furthermore that either geographic or practice area scope mergers are initially more successful than those intended to achieve both. ◆

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Figure 5
Short Term Scope Merger PPP, by Purpose

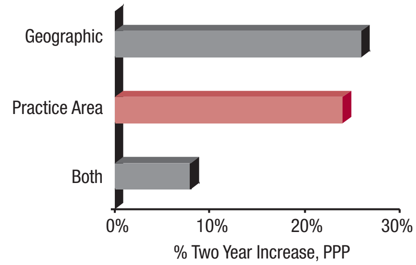

Figure 6
Long Term PPP Growth Since 1999

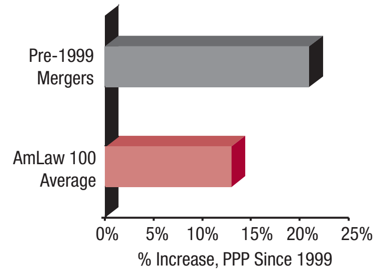

Table 1: The Mergers Studied

Baker Botts/Brumbaugh, Graves, Donohue & Raymond	1997
Bingham Dana/McCutcheon, Doyle, Brown & Enersen	2002
Blackwell Sanders Matheny Weary & Lombardi/Peper, Martin, Jensen, Maichel and Hetlage	1998
Blank Rome Comisky & McCauley /Tenzer Greenblatt	2000
Clifford Chance/Rogers Wells	2000
Dibb Lupton Broomhead/Alsop Wilkinson (UK)	1996
Foley & Lardner/Hopkins & Sutter	2001
Holland & Knight/Dunnells & Duvall	1994
Holland & Knight/Haight, Gardner, Poor & Havens	1997
Howrey & Simon/Arnold White & Durkee	2000
Nixon, Hargrave, Devans & Doyle/Peabody & Brown	1999
Paul, Hastings, Janofsky & Walker /Battle Fowler	2000
Pillsbury, Madison & Sutro/ Winthrop, Stimson, Putnam & Roberts	2001
Piper & Marbury/Rudnick & Wolfe	1999
Sidley & Austin/Brown & Wood	2001
Swidler & Berlin/Shereff, Friedman, Hoffman & Goodman	1998
Thelen, Marrin, Johnson & Bridges/Reid & Priest	1998