Law Firm Mergers
Don't Just Get Bigger, Get Better!

By Eric Seeger

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There are many good reasons why law firms should continue to pursue strong growth even in a down economy. There are, however, important differences between good growth — growth that makes good business sense and that matters to clients — and growth for growth's sake. Merely growing in size and scope does not automatically make a law firm better, or even perceptibly different, from a client's perspective.

Some law firms want to expand into a certain geographic market simply because it's a hot market or to merge with Firm X simply because Firm X is a good firm and asked to merge. Proceed with caution: a merger must create a more competitive market position for the firm, or it will drain resources without significantly improving the bottom line.

Most healthy law firms should be actively pursuing some sort of intentional growth plan. Firms that are not trying to grow are likely to begin losing lawyers, recruits, and market share to other firms that are successfully growing in visible, measurable, sensible ways. Talent flows to the winning teams and so do clients.

There are several concerns that law firms should keep squarely in mind as they evaluate their growth options via merger and acquisition.

Define a Growth Strategy First

A merger is a big deal. It is expensive and disruptive. It sends a message outside and inside the firm about what strategic market position the firm intends to achieve. Any merger that fails to communicate that message in clear terms is not likely to advance strategic interests. Too many ill-conceived "me-too" mergers have fallen into this category and had to be undone in full or in part.

A firm should have its growth strategy in place prior to evaluating merger opportunities. If your plan calls for merger as a growth strategy, prepare a prospectus that sets forth the firm's vision as well as the core practice areas and key geographic areas targeted for growth. It should also speak to how your ideal merger partner will contribute to, and benefit from, being a part of your firm's growth plan.

Even if your plan does not call for merger, you should not automatically reject an inquiry. Instead, when presented with any such opportunities, you should consider whether the combination would achieve the strategic goals that you have already identified.

Growing Bigger and Better

Effective growth is about getting better, not just bigger. "Better" means more profitable and more rigorous in dealing with productivity and related issues. Better should be defined both *externally* in terms of benefits to clients and competitive position/market profile and *internally* in terms of improving economic performance and depth of resources. Better also means *substantially* better, not just marginally better.

Before you get too far along in any merger discussions, determine what being better means to your firm and explore the implications in terms of people, strategy, and operations. You will want to assess in advance your organization's willingness to do the things required to become better as a combined firm.

Think about those things that you'll be need to do later, the specific initiatives that will make you better. *Do them now*. The better you can become in the short term, the better merger partners you can attract in due course.

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Achieving Better Economic Performance

Any merger must advance the bottom line, so any firm contemplating merger must be able to answer these two questions in the affirmative.

1. *Will the economics of the combined firm be substantially better than the economics of each firm currently?*
   The firms' combined economics will not improve unless something happens beyond

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merely adding A + B. In most cases, one firm's financial performance will get at least somewhat diluted by the other, and both firms will suffer the inevitable and considerable costs of merger. These costs, and the disruption of a merger, need to be more than offset by the benefits.

2. *Will the firm's financial indicators improve?*
   For better or worse, your firm's AmLaw rankings (or similar performance benchmarks for smaller firms) slot your firm against other firms on such measures as profit per partner (PPP) and revenue per lawyer (RPL). Putting aside the question of whether such figures really do provide the best measures of law firm economics, it is imperative that, simply as a matter of marketplace perception, your firm improve its financial performance indices as a result of the merger.

Firms seeking a "leading" or "dominant" or "preeminent" position in their market must achieve financial performance in the top quarter of the peer group. Even the modest goal of "above average" requires performance in the second quartile. How would your merged firm look against its new peer group in terms of PPP and RPL? What are you prepared to do to improve profitability? Whatever those things are, start doing them now. By improving your own profile, you increase the likelihood of attracting and impressing the best possible merger partner.

To compete for the best work and the best talent, the combined firm will need to improve its revenue per lawyer and profit per partner in the usual ways: (1) by improving rates, hours, realization, and leverage; (2) by making some difficult personnel decisions; and (3) by focusing business development efforts on profitable clients with upside potential.

Most successful mergers include some pruning of underproductive assets (people and clients) and some redirection of the business. Otherwise, you simply get bigger and no one outside the walls really cares. Ask the following questions:

- What needs to occur for the new firm to improve RPL into the first or second quartile?
  - Increase hours?
  - Decrease personnel (without losing volume)?
  - Increase rates?
  - Improve realization?
- What needs to occur in order to improve PPP consistent with peer firms? What are you willing to do?
  - De-equitize underproductive partners?
  - Extend the partnership track?

Practice Group Analysis Is a Must

Mergers succeed when real clients agree that the newly combined firm is better able to handle their work (and more of their work). They then send more work to the firm. Convincing yourselves is important, but the real value comes from getting actual clients to agree with you.

To estimate rationally the legitimate potential for incremental business, it is important to conduct a practice group analysis focused on identifying specific, real benefits to specific existing and potential clients. Identifying and attempting to quantify such a total value package is the best way for you to come to a "go/no go" decision on a potential combination.

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Look for specific opportunities to get new work, more work and better work from existing clients, as well as new work from new clients. Also consider how you will continue to grow practices post-combination. Answer these questions:

- What new access would this combination bring to each side?
- What work will we realistically be able to win away from competitors?
- Which laterals might be attracted to the combined firm?
- Which practice groups can achieve a higher profile via combination?

Be thorough, realistic and specific.

These evaluative steps do not need to be deeply introspective or particularly time-consuming. The process, however, needs to be extremely candid and objective in terms of reviewing the firm's economic potential, as well as its challenges.

The kind of analysis described here, together with a commitment to address whatever concerns may surface, can and should result in making your firm healthier, more productive, a more attractive merger candidate, and better positioned to achieve real market gains from a merger. ◆

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