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O U R 2 8 T H Y E A R

Branch Offices: Risky Business Or Significant Opportunity?



Thomas S. Clay

By Thomas S. Clay

“We are losing our shirt in the Washington, D.C. office and I don't understand why we don't close it and close it now.”

“John said that he had a \$1.2 million book of business when we started this office. He only produces about \$750,000 and now wants us to spend more money adding laterals to the office.”

“I don't even know why we have the Florida office. Why are we there?”

I heard these comments during the past year while attending various law firm management committee meetings.

“Those guys in the home office don't understand our marketplace at all.”

“We thought they were going to help us generate business in order to make this office successful, but we never see them.”

“The only time we get any attention here is when we try to hire a lateral. They keep telling us to increase the business but they don't let us do the things we need to do to get people with business.”

These are things that I heard leaders of branch offices of law firms say over the last year.

It is no surprise that management of branch offices is a challenge. Just ask any law firm managing partner whose firm has branch offices, or ask any managing partner of a branch office. Is all this effort and investment worthwhile? According to the 2001 *Altman Weil Survey of Law Firm Economics*, overhead per lawyer in multi-office firms was \$149,944 versus \$144,568 for all law firms. That is an

additional cost of \$5,376 per lawyer. The survey, however, shows that multi-office law firms produced \$348,191 per lawyer in fee receipts while all firms produced on average \$338,167, a \$10,024 differential. This results in multi-office firms producing \$4,648 more in net income per lawyer than single-office firms. This relative relationship has held for the last several years according to survey data.

Clearly, branching can be risky because of the hard dollar cost and managerial energy required. But there can be significant benefit and strategic benefits as well. Following the advice herein can help you make better business decisions about adding branch offices. It can also be useful in helping to rethink or evaluate current branches.

The Business Case

My observation, in almost 25 years of working with law firms, is that firms spend too little time evaluating the business rationale for proposed branch offices. Too often, firms are like the cobbler's children, not taking the time to make as well-considered decisions for themselves as they would for clients. Often, when they do have a good business rationale, they lose sight of the objective in the quest to open an office.

I was asked to help evaluate a group of lawyers in New York for a firm seeking to open an office there. It took only a short conversation with the New York group to find that the lawyers being considered, although good people (and probably good lawyers), did not meet the stated objective of the proposed office.

When I commented on this, members of the search committee said, "We've been looking for a long time and these are good guys. They don't really meet our criteria but we need to be in New York City and this gives us a platform."

Not very sound business reasoning in my judgment. I suggested that the firm ask a representative group of clients, financial service firms, what they thought of the move. After only three meetings with clients, it was clear that the proposed platform of lawyers was irrelevant to these clients. Establishing a base from which to acquire more work from the financial service clients was the objective of the proposed New York office. The clients were unimpressed. The search committee lost sight of the objective in favor of just getting someone on the ground.

Be clear about the objectives to be achieved by establishing a branch office and be rigorous in staying with them. Following are legitimate reasons for establishing a branch office:

- ***It fits the firm's (or practice group's) strategic plan:*** If the firm's strategic plan or practice group plans show that branching meets strategic needs, this may be the best reason to pursue it. The existence of firm-wide and practice area plans are prerequisites for this rationale to exist.
- ***Geographic market penetration:*** Branching is an effective means of penetrating geographic markets in those instances where a physical presence is required by (target) clients.
- ***Client service requirement:*** From time to time current clients will require that a branch be opened in order to service them appropriately or improve service. Where you can demonstrate that the economics make sense, then branching is rational.
- ***Escaping the home market:*** Branching is a feasible means by which to pursue growth when there are few opportunities for growth locally.
- ***Capital branching:*** Opening an office in a state capitol or Washington,

D.C. has been a frequent strategy. Typically firms pursue opportunities to represent current clients requiring representation in the capital.

- ***National or regional client opportunities:*** A few firms perceive that clients with national or regional representation needs will be attracted to a firm with offices in many locations. This is true for a *limited* number of clients. Firms should avoid what I call the "pins in the map strategy," hoping clients will be attracted. Few clients are impressed or care about such a strategy.
- ***Defensive measures:*** Some firms find it necessary to open a branch from a defensive standpoint. Competitors will target another firm's clients and tout being local as a differentiating service factor
- ***Office of convenience:*** Firms open offices of convenience, especially for work such as trust and estates, real estate closings and the like. Typically, these branches are sub-urban and focused on achieving improved client service and possibly increased market share.

Once you have determined the business reasons for a branch office, use this checklist as a guide for setting objectives. This makes decisions regarding staffing, marketing, and economic consideration easier to make. It also provides a means by which to evaluate the performance of the branch office over the next several years.

Develop Empirical Data

I am reminded of the well-known line from the movie *The Treasure of the Sierra Madre*, "Badges? We don't need no stinking badges." When I ask what data firms have developed to help with the business case evaluation, I often hear, "Data? We don't need no..." Well, you *do* need data to make good business judgments.

Branch offices are often opened based upon anecdote, intuition, a need to follow the Joneses, and other poor

reasons. Gut business judgment can be useful, but it should be supported with good data. This could include:

- Client information developed through meetings and surveys;
- Referral source data;
- Competitor analysis; and
- Market research regarding expected business growth, demographic projections and related data.

The more solid the research that supports assumptions, the better the decisions and the easier it will be to convince partners that a branch is a rational business initiative.

Barriers to Entry

Pursuing opportunity should be at the heart of branching, but not in the face of barriers that increase the risk of success to unacceptable levels. Barriers must be rigorously and candidly examined. Some of these might include:

- ***Excessive competition:*** Even when it would seem rational to expand out of one's marketplace, excessive competition in the target market can foul the plan. A thorough evaluation of existing competitors should be made.
- ***Limited number of target clients:*** Too often, firms branch with the expectation that they can expand their client base. This often is in the face of hard data which reflect a small target group. Great care should be taken to ensure that the level of potential clients and targets actually exist that would meet the firm's objectives.
- ***Large differentials in lawyer compensation:*** Extreme pay differentials often make what would otherwise seem to be a rational branching policy a managerial nightmare. If professional staff in a branch will be paid differently, a rational needs to be developed or problems will arise.

The People

Professional staffing, in the short term and the medium term (three to five years), will play the greatest role in achieving the objectives of the branch. Consider the following:

- Based upon the objectives to be achieved, what specific expertise must be resident in the office initially? What level of expertise (experience)?
- What additional capabilities are needed within the first two years?
- What professional staff levels are needed initially and within the next two years to achieve the objectives set forth?
- What *profile* is required of professional staff, i.e., describe the best candidates, partners, associates, paraprofessionals, considering the objectives of the branching exercise? These might include management capabilities, marketing ability, community image and contacts.

Staffing Strategies

Once a decision has been made regarding the profiles of desired staff, selection strategies for both short and medium term should be evaluated. These will be affected by availability of appropriate lawyers in the local market and willingness to move. Following are options that should be considered:

- **Acquire a firm or part of a firm:** For a sprig of a branch to take root, some firms acquire an existing tree — another firm or a portion of a firm. The search strategies for such a move can vary including contacting lawyers known to members of the firm, or using head-hunters, consultants and the like.
- **Send lawyers to the locale:** Sending lawyers to the locale, if consistent with the branch objectives, may well be a rational move. But firms would be wise to consider the carpetbagger effect that can occur if only firm lawyers from a distant place open the office.

- **Combination:** Acquiring local lawyers and sending firm lawyers to the locale is often the best strategy. If local lawyers are employed and firm lawyers are sent to the office, integration will occur more quickly.

Don't lose sight of the objectives by adding non-strategic personnel simply to obtain mass. Too many firms have been strategically and economically disappointed when they have lost sight of the branch office objectives.

Budgeting and Forecasting

Branch offices should increase profits, not dilute them. Often they do not because poor budgeting occurred initially. Most firms will develop a rudimentary budget when considering a branch operation. Although budgets are often only "educated forecasts," as much or more care should be put into the budgeting effort for the branch office than for the home office. Preparing sound operating and capital budgets with detailed assumptions will be one of your best tools in terms of developing a sound business case.

Marketing and Promotion

Promotion of a branch office is critical to its success. Promotion must occur with firm lawyers, clients, potential clients and media. Identify the minimum activities required to fulfill the office's objectives in the first year. Early consideration of marketing needs will point out the resources and effort required to meet the objectives and may affect the decision-making process. It may sharpen your business case focus. You should consider:

- Written promotional literature required;
- Client or perspective client meetings and presentations required in the first six months;
- Public relations efforts;
- Website enhancements; and
- Seminars and receptions.

Time budgets as well as dollar budgets should be carefully developed for these things.

International Branch Issues

There are special issues to consider when evaluating international branching opportunities. If the firm is not experienced in international branching, it should employ consulting expertise, as there are pitfalls that do not exist with domestic branches. Some of these would include:

- management
- communications
- different ethical issues
- cultural and operating issues
- compensation differentials
- language problems
- taxation issues

As the market moves increasingly toward a more global economy, more law firms will be opening or will consider opening branch offices in other countries. Following the same basic protocol in terms of making the evaluation will benefit the firm.

Summary

Of the 250 largest US firms, only six do not have one or more branch offices. As geographic markets become overly competitive, as larger clients consolidate the numbers of firms they use and as law firms seek markets to penetrate, branch offices will proliferate. Following the suggestions above will save enormous amounts of time, energy and cost on the front end. It will also save greatly post-implementation by ensuring that firms make better business decisions and are not burdened with the cost of unfocused, unproductive, unprofitable branch offices. ♦

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