
How the mighty fall

Attorney and author Michael Trotter talks to Lawyers Weekly about why big-firm economics go wrong

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The national media is agog these days over the very public implosion of another high-flying law firm, New York's Dewey & LeBoeuf. At last count, at least 75 of the firm's 300 partners have departed since January. And the firm has now told the rest to start looking for new jobs, while the Manhattan district attorney's office has opened an investigation into the handling of the firm's finances by ousted chairman Steven Davis.

Though uncommon, Dewey's demise is not unprecedented. Those of a certain age remember Finley Kumble, which rose from eight lawyers in 1968 to the second-largest firm in the country in 1985. "Finley rocked the legal world as it signed up high-profile figures and raided other firm's superstars, some of whom earned the then-staggering sum of \$1 million annually," wrote Chicago attorney and law professor Steven Harper on his blog, bellyofthebeast.com. "But Finley grew too fast, assuming debt for office expansions and promising outsized paychecks to big name lateral hires. As revenues dwindled, the firm disintegrated." The firm dissolved in 1987, at a time when it still had 650 attorneys.

Four years later, things likewise fell apart for Boston's Gaston & Snow, an old-line firm which also pursued an aggressive growth strategy in other cities, only to become hostage to the creditors who funded its many new offices. And in 1995, Richard Nixon's old firm Mudge Rose suffered a similar fate when a bunch of partners and associates walked out.

Is the plight of Dewey & Leboeuf any different?

That's a question *Lawyers Weekly* asked Atlanta attorney Michael Trotter, who has himself lived through several law firm iterations, with stints at large firms that were the predecessors of Alston & Bird and Kilpatrick Townsend & Stockton. He is now a partner at Taylor English & Duma in Atlanta, a firm he says is an example of the "new model" likely to thrive going forward.

Trotter has also written frequently on law firm management and economics, and is the author of "Profit and the Practice of Law," which chronicled the growth and change of major business firms from 1960 to 1995. His latest book, "Declining Prospects," to be released in late May, continues that chronicle through today and describes the sea change he sees sweeping through the country's largest firms.

"The strategy pursued by almost all of the major business practice firms over the last three decades has focused more on maximizing the profits of the firms' controlling partners rather than on maximizing the value of service to clients," Trotter writes.

For those firms, the news is not good: "The forces of competition, rising costs and commoditization, coupled with strong corporate law departments inevitably lead to declining prospects."

There's good news, though, for most firms in North and South Carolina, which tend to be smaller, more fiscally conservative, and more attuned to personal client service. They will likely survive unscathed.

"They ought to be pleased with where they are," Trotter says. "While they may not have enjoyed the fruits of climbing up to the top of the tree, they've also avoided the risks. The storm is going to pass by most of the North Carolina and South Carolina firms and leave them in pretty good shape."

What follows is an edited transcript of Trotter's talk with *Lawyers Weekly*.

LW: *In your books “Profit and the Practice of Law” and “Declining Prospects,” you chronicle the profession’s changes since 1960 and make some predictions about its future. And now we’re witnessing yet another large firm meltdown with Dewey & LeBoeuf in New York. But how much different really is all this? We’ve had big failures before.*

Trotter: Well I think the key to all of this, because of Model Rule 5.6 of the Code of Professional Conduct, is that every lawyer is a perpetual, unlimited free agent. The rule, implemented through adoption by the states, says essentially that a lawyer cannot enter into an agreement with his existing firm that would restrict his practice if he left the firm. The theory is to protect the client, so that the client has the right to pick the lawyer he wants to employ regardless of where he is. But the flip side is that the lawyer is free to pick up and move at any time. Of course other factors might keep him at the firm -- if he guaranteed the firm debt, for example -- but even that practice is not as common as it used to be.

LW: *What do you think has gone wrong at Dewey?*

Trotter: I don’t know anything about the situation other than what I’ve read in the newspapers and so on, and that’s quite a bit, but assuming that information is correct, I think Dewey is experiencing a problem that a number of what I would call the major business practice firms or the AmLaw 200 firms are facing. There’s been a fundamental change in the competitiveness of the environment – that has increased extraordinarily so.

LW: *Law firms have always been competitive, though. How is this different?*

Trotter: We’ve got very many able lawyers and law firms – more than we need. Law schools are currently producing about twice as many graduates as there are jobs available. And the quality of the students is very high – probably the highest we’ve ever had, which is the result of the fact that at the top level it’s paying so well, it’s attracted a lot of people who are interested in a profitable career. And until now it was probably something you could do with less risk and no capital.

LW: *Is it only competition that’s driving transformation?*

Trotter: In the book I talk about five factors – starting with the increased supply of capable lawyers and law firms. In addition to that, though, the costs of legal services have been driven to the point that companies are now focusing on how to control them. And on the other side of the table, there are some very smart, able people negotiating on behalf of the businesses. Corporate counsel knows that an awful lot of the work they give to outside lawyers is probably a commodity

(financial) product that a large number of law firms are capable of providing. They can bid that out and perhaps in more subtle ways place pressure on firms to reduce those costs. And of course the changes in communications technology have made it possible for attorneys in Seattle or New York to compete with lawyers in Atlanta or Charleston or Charlotte.

LW: Has there been a pushback on costs?

Trotter: Corporate counsel has the charge from their client companies to reduce the cost of their legal operations. I think we're going to see a return somewhat to the retainer system of the '50s and '60s. Pfizer for example has done that. They've identified a group of law firms that they are going to use for specific things – intellectual property, corporate, litigation, and so forth – and they have a budget. They allocate 80 percent of that budget amongst those firms that they've designated to be their counsel, and those firms agree to do whatever it is they need in their area of practice that's been allocated to them at a fixed price. Pfizer then holds back 20 percent of the budget, which they allocate at the end of the year based on criteria that they've created – for example, one firm may have had extra work to do, or obtained a notable result. But at the end of the year, the amount that Pfizer has spent is the amount that they budgeted for at the beginning of the year. That's the way it used to be.

LW: How might these changes affect firms in North and South Carolina?

Trotter: I think the major business practice firms are at the greatest risk. And we can't lose sight of the fact that about 50 percent of the lawyers in America are sole practitioners, and a total of 70 percent are in firms with fewer than 20 lawyers. The last time I checked, I think there were only a few Carolina firms in the AmLaw 200 – Womble Carlyle, Nelson Mullins, Moore & Van Allen.

LW: In our recent ranking of firms, we saw that some of the larger, out-of-state firms like Alston & Bird, Hunton & Williams, for example, that opened offices in North Carolina have suffered the largest drops in number of attorneys. Why do you think that is?

Trotter: I think the North Carolina market historically was a lower-priced market - - lawyers didn't earn as much and they didn't charge as much, and these firms from maybe Atlanta and other places that had grown accustomed to a certain level of profitability I think were frustrated that N.C. firms were not operating at the same level of profitability.

LW: *And yet we see other firms making the same move -- K&L Gates opening in Charleston is an example.*

Trotter: I think it's very misguided. You're trying to be both a major business practice firm, competing with the likes of Cravath and Sullivan Cromwell on one hand, and a local firm competing at the level of a Nelson Mullins, for example -- which has some very competent, talented lawyers and I suspect is charging at lower levels. So how do they compete?

LW: *Tell us about the "new model firms" you discuss in your book -- why you think they'll thrive and fill a niche. Your firm, for example, mostly hires only experienced attorneys.*

Trotter: Leverage has been a big factor in large firm profitability. When companies brought work, they typically wanted you to handle the entire project. And firms grew to having more associates than partners [to handle different levels of a project]. Now, corporate counsel will say "I've got a hundred lawyers on my staff, and we can do this part or that part, the document review we can farm out to someone at a much lower cost, but we want you because of your expertise and experience, maybe for strategy, or we'll draft a basic document and you'll review it for us." The effect of that is to reduce the need for leverage.

A firm like ours can handle the upper level work that a client might need us to do, and we charge less to do that. So generally we're each paid for what we do. Some derisively refer to that as eating what you kill. But if you're not paid for what do you do, what are you paid for? How do you measure it? That brings politics into the legal environment. We have a more comfortable environment.