

LEGAL MANAGEMENT

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LI Feature

LEGAL INDUSTRY/BUSINESS MANAGEMENT

Pondering Profitability

Law firms get innovative to stay ahead

Sustaining long-term growth and profitability requires constant renovation and reimagining.



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Marketing Communications Writer

“I think we, as a profession, need to become much more comprehensive in our outlook about profitability and include more client-focused metrics. For example, metrics related to efficiency and process management or predictable cost/budgeting skills are becoming increasingly important.”

STUART J. T. DODDS
Director, Global Pricing &
Legal Project Management,

CHANGING METRICS AND PROFITABILITY MODELS

To have a workable profitability model, “law firm management — at the highest level — needs to better understand the interconnected behaviors that come into play,” says Stuart J. T. Dodds, Director of Global Pricing and Legal Project Management at Baker & McKenzie Global Services LLC.

Historically, law firm partners haven’t had an overall awareness and understanding of profitability. But that is changing.

“Before, law firm partners didn’t need to know much about what made their business profitable,” says Toby Brown, Chief Practice Officer at Akin Gump Strauss Hauer & Feld LLP. Those days are long gone. “As rate and fee pressures have led to discounts and matter budgets, having a deeper understanding has become an important issue.”

“Peeling back the layers, firms need to understand the impacts of four factors: billing rates, realization (segmented into discounts, write downs and write offs), utilization and leverage,” says Dodds.

According to Brown, the market is pushing down on the first three factors, which leaves leverage as a key tool to enhance profitability. “A significant challenge comes from most law firm compensation systems that actually encourage partners to hold on to work, instead of pushing it down for better leverage.”

ORGANIZING FOR PROFITABILITY

Although value varies by client, Ogletree Deakins’ Managing Shareholder Kim Ebert says they make sure they have the resources needed to respond.

Accordingly, the firm has directed an increasing number of resources into technology to gain greater efficiencies and be more responsive. They’ve invested in extranets so clients can access information 24/7. In the last four years, they’ve also expanded their knowledge management



capabilities. They've added a pricing strategist and focused on analytics by industry and clients.

Additionally, the firm has built a staff of knowledge management researchers, librarians and counsel who have created sample pleadings — nearly 200 different model documents that allow attorneys to save time, work more efficiently and keep a steadier handle on costs. All of these positively affect client relations.

"Price certainty helps expand the relationship," Ebert says.

The task of harnessing information and developing profitability models does vary among law firms.

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TOBY BROWN

Chief Practice Officer,
Akin Gump Strauss Hauer
& Feld LLP



"In prior years, a great deal of responsibility for pricing and profitability modeling fell on the finance department," says Thomas W. Van der Moere, Chief Financial and Information Officer at Neal Gerber & Eisenberg, LLP. With increased demand on alternative fee arrangements (AFAs) and budget planning, the firm created and filled a new position for a Director of Pricing. This role focuses on working one-on-one with the firm's teams to understand, gather facts and develop potential pricing models, including risk-sharing and budgeting factors.

Along with a broad understanding of finance and pricing, this individual is a trained litigator who can speak the language — translating pricing concepts into understandable terms from a practicing lawyer's perspective.

"Because of her training as a lawyer and litigator, the Pricing Director has been a key asset in assisting our teams think strategically through the timing of milestone events, appropriate staffing and deadlines," says Van der Moere.

Mining existing data and developing a historical framework are crucial, time-intensive efforts so the data are as useful as possible, allowing the firm to make the most persuasive argument about approach and budget.

PRICING DIRECTION FROM AN IT PERSPECTIVE

Bryan Cave has a highly sophisticated Practice Economics Group (PEG) that is dialed into nearly every AFA the firm proposes, according to Christopher W. Emerson, Bryan Cave's Director of Practice Economics.

Emerson's background as a pricing director is unique: The firm hired him 18 years ago as a software engineer in the IT department. He focused on financial systems, including developing the firm's first AFA tools in 2014 as part of its financial dashboard.

Today, Emerson's PEG group is outside the normal organization chart — not in finance or IT.

Instead, it reports to a partner/strategic innovation partner, with a dotted line reporting to the chief operating officer and the management committee.

There probably are few (if any) who have reached the position of pricing director with an IT background, but Emerson asserts it has been a decided advantage.

“No way could I do this job without it,” says Emerson. The biggest advantages? “[I] have a deep understanding of the firm’s systems, [which] allows me to cut through the noise. I know the systems inside and out, and know what is doable and how long it will take.”

It also allows Emerson to select staff with the right skills — people with the technical perspective and know-how to retrieve information and automate quickly.

“Working in a law firm environment, speed is a requirement — especially to be responsive to internal and external clients. It’s a real competitive advantage,” he says.

Having the length of tenure at Bryan Cave and working on the firm’s systems also has translated into having a strong suite of tools, developed in-house. By comparison, many law firms are trying to develop an infrastructure to mine their information.

THE RIGHT STUFF

A big challenge is finding people not only with the right set of skills and an understanding of the legal environment, but who also can apply business analytics to it.

“People with these skills are in short supply,” says Brown. “Firms need to be creative in leveraging existing staff, or looking outside of legal for these skill sets.”

The new roles in pricing require a broad spectrum of interdisciplinary skills. Additionally, they need solid communication and people skills. Sometimes, someone coming in with top-notch IT skills from a nonlegal environment may have a tough time transitioning to the fluid nature of law firms.

Also important is the ability to be assertive when partners push for maintaining unprofitable engagements.

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THE ROLE OF AFAS AND LPM

The demand for AFAs has elevated the importance of new profit models and legal project management (LPM). This raised awareness has expedited the need to have a simple and well understood profit methodology, according to Brown.

“Most often, AFAs are used in situations with rate and fee pressures. So, they also raise the need

for re-evaluating how services are delivered,” he adds.

LPM — the latest addition to the profitability toolkit — is a lever that is within the firm’s control. And in matters with fee caps or fixed fees, staying on budget is crucial.

“LPM plays a big role in profitability,” says Dodds. “It provides a structure that allows a firm to have better control. You can better manage the process and stay on budget, so you can avoid write-downs, manage the scope of your matters more effectively, and be more pragmatic in your advice — which can positively improve client communications.”

MATTER PROFITABILITY

Many firms often have shied away from focusing on matter profitability to avoid pitting practice groups against each other, or having an unclear methodology. But Lisa Smith, a Principal at Fairfax Associates, sees more firms focusing their attention in this area.

“These firms are taking a much more sophisticated approach to evaluating matter profitability to make better informed decisions concerning profit management and pricing — and also so they can set fees and manage engagements more intelligently than on an hourly fee basis,” she says. “More tools are available to do it well, and there is a greater willingness to do it because it will improve overall firm profitability.”

To ease the process, some firms do a rollout on a pilot basis with a group that can most benefit.

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CHRISTOPHER W. EMERSON
*Director of Practice
 Economics, Bryan Cave*



Matter profitability, while important, also needs to be understood in a broader context at the client level. Firms often will have clients with many different types of matters at varying levels of profitability. Matters with lower margins are perfectly acceptable in that situation.

Plus, many clients do want to understand how fixed fees are developed and how they can realize cost savings. So having an understanding of matter profitability and matter budgets can set the stage for having more informed conversations about fees.

Brown advises that attorneys need to understand how pricing and staffing impact the margins on a given piece of work.

“Then they can explore options for improving margins while holding the line on the overall fee at the matter level,” says Brown. “Without this kind of understanding, all an attorney can do is further discount the rates or cut the hours involved. And if you do that blindly, you may drive the matter to negative margins without knowing it.”

CULTURAL CHANGE

Driving a cultural shift about billing and profitability doesn't happen overnight.

Ogletree Deakins has mandatory training for new associates on profitability issues. Bryan Cave's professional development group hosts training for associates, junior partners and equity partners on basics of LPM and demystification of AFAs, as well as training to help attorneys feel more comfortable talking about profitability with clients.

While training is important to ease buy-in about profitability issues, AFAs and LPM, one size doesn't fit all.

"It is important when developing training in these concepts to recognize that, although all attorneys should have a general appreciation of key themes covered, not everyone will need or want high-level, expert training," says Dodds. "Training resources and approaches should be tailored appropriately."

To ease the change, use some basic communication efforts to persuade and educate. Some pricing directors do formal roadshows on a regular basis to local and regional offices, or individual training when onboarding new laterals or associates. The program can provide a basic understanding about profitability at the firm — what are the factors and how profitability is measured.

Brown also says making profitability information more transparent is important. "Once attorneys can plainly see the profitability of their work, the behaviors will change," he says.

Rewarding attorneys for incorporating a mindset about profitability is a longer-term vision.

"I think we, as a profession, need to become much more comprehensive in our outlook about profitability and include more client-focused metrics," says Dodds. "For example, metrics related to efficiency and process management or predictable cost/budgeting skills are becoming increasingly important. Lawyers who have the skills to do these aspects well should be recognized and awarded appropriately."

Dodds also suggests taking into account other skills that are more operational in nature.

"It's not easy to do, but more progressive firms are beginning to include elements such as client team retention, client feedback and so on," he says. "Consulting firms often use such measures, and this might be a model we in legal could learn from."

ABOUT THE AUTHOR

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