

# LEGAL MANAGEMENT

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## FM Feature

FINANCIAL MANAGEMENT

# Your Clients' Surprising Effect on Firm Profitability

If your firm doesn't know how clients are affecting the bottom line, you may be missing out on potential revenue

Until the recession hit, many law firms' business models were fairly simple — and successful.



**ERIN BRERETON**  
Owner, Chicago Journalist Media

*“Law firms can generate profit by being able to figure out how to leverage that middle opportunity. One hour of standard attorney work could cost \$600. If 90 percent of that quality could be gotten from a \$325-an-hour lawyer, that’s a decision the client will always make.”*

**NATHANIEL SLAVIN**

Clients, and profits, seemed to be in endless supply, according to Jim Hassett, Founder of law firm consultancy LegalBizDev.

“Up until 2008, in the 10 years or so preceding, almost no matter what you did, you made money in the legal world because the market was expanding so rapidly,” Hassett says. “Clients were not resisting higher hourly rates.”

In the years since, as many organizations reduced their legal and other expenses, a number of firms have vastly underbid on work, says Hassett.

In some instances, clients have tried to negotiate lower rates. (Sixty percent of Am Law 200 firms said they were discounting rates for a portion or all of their top 50 clients, according to a recent survey from *The American Lawyer*.)

With clients urging firms to provide more value for less money, the way some firms assess profitability is changing.

If your firm has been trying — with mixed success — to increase its earnings, consider the following client relationship suggestions.

### **DETERMINE THE RIGHT METRICS**

According to *The American Lawyer*, firms on average showed the lowest revenue per lawyer last year since the publication began tracking 200 firms in 1998.

However, before firms can try to start increasing returns, their partnership needs to agree how profit will be measured, says Hassett, who questioned 50 AmLaw 200 chairs and managing partners

for his 2014 *Client Value and Law Firm Profitability* study.



"It sounds so basic," Hassett says. "But firms don't have that information, for the most part. They need to look around and see who is making money and who isn't."

Some firms struggle to identify criteria to determine financial success.

"One firm, for example, talked about bringing in \$10 million of business that cost \$11 million a year to produce," Hassett says. "You'd be better off bringing in \$5 million in business that costs \$4 million to produce, but that's not the way lawyers have traditionally thought."

To help them fully understand how profitability opportunities could be improved, some firms are employing outside assistance, says Nathaniel Slavin, former *InsideCounsel* Publisher and current Partner and Founder of the Wicker Park Group, an international consultancy that conducts law firm client feedback interviews.

"We've seen more and more firms in the past year or so using financial analysts and other non-lawyer specialists to help them put a value on their current and future work — and figure out how to maximize utility and efficiency," Slavin says.

## QUICK HIT 1

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*"If there are 300 partners and they're all owners and extremely smart people who may have their own agenda and clients, it can be very difficult to figure out as a business which clients you really want to go out on a limb for — and which you want to break up with."*

**JIM HASSETT**

Founder, LegalBizDev

### MARKET TO POTENTIALLY PROFITABLE CLIENTS

To present its services to a specific client base, Criminal Defense and Traffic Violation Attorney Benjamin Luftman's Columbus, Ohio-based firm, Luftman, Heck & Associates, added pages to its website that explain how a driving under the influence (DUI) charge could potentially impact people in various careers, such as medicine.

"In this particular area, a lot of lawyers just hustle to get as many clients in the door as possible," Luftman says. "Some are savvier and try to micro-target clients with web [and other] advertising."

The site also features information about its attorneys' track record and professional designations.

"Our business perspective is that our level of service and the results we've achieved [enables us] to charge a premium," he says.

### MAXIMIZE MIDDLE-GROUND RESOURCES

The pressure to correctly estimate how much time certain tasks take is obviously a concern in fixed-fee matters.

"I've had conversations with my business partner about, if you know how many cases you can do in a day, how much do you charge, relative to other firms in your market?" Luftman says. "Does it



make sense to say I'd rather do two \$5,000 cases instead of having to do [several] at \$1,000?"

Luftman's firm generally operates on a flat-fee system — making time tracking a crucial part of the pricing process.

"We charge accordingly for time-intensive cases because we know the effort and time it takes to do it," Luftman says. "Just like any other business, you try to maximize the resources you have and your profit."

Hourly rate work can also affect a firm's profitability.

Traditionally, clients may not have minded if firms assigned less experienced attorneys to work on fairly common tasks. Now, as clients grow more budget-conscious, some are allowing — or even encouraging — firms to assign work that falls in between high-stakes and more common matters to junior attorneys.

"Law firms can generate profit by being able to figure out how to leverage that middle opportunity," Slavin says. "One hour of standard attorney work could cost \$600. If 90 percent of that quality could be gotten from a \$325-an-hour lawyer, that's a decision the client will always make."

### ENCOURAGE LONG-TERM PLANNING

At firms where the billable hour requirements reset each January 1, attorneys often aren't being encouraged to truly develop client relationships.

"The greatest fault with law firms is that they start every year at zero," Slavin says. "It creates a culture of playing a relative short game."

Potential profit is sometimes also weighted too heavily. Firms need to keep a careful eye on receivables to ensure attorneys' work is earning actual money — and contributing toward the firm's big-picture profitability goals.

"Very often, lawyers are rewarded for signing bigger deals, not whether they're profitable or clients pay their bills or not," Hassett says. "Somebody who has a \$5 million client who pays \$5 million for its work earns less than a lawyer with a \$10 million client who pays \$5 million for its work."

## QUICK HIT 2

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### LET GO OF UNPROFITABLE CLIENTS

"It's a tough thing to walk away from that potential, but if it's not there, it's not there," Luftman says. "The business partners have to ask themselves: Are there other cases I can be involved in that

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**BENJAMIN LUFTMAN**

*Founding Partner, Luftman, Heck & Associates*



are less time- and labor-intensive and would pay better for that time?"

The decision, however, isn't always an easy one to make.

"If there are 300 partners and they're all owners and extremely smart people who may have their own agenda and clients, it can be very difficult to figure out as a business which clients you really want to go out on a limb for — and which you want to break up with," Hasset says.

A firm may choose to end client relationships in an indirect way to improve operations, particularly if it's dealing with an underperforming office or practice group.

"Sometimes, it's easier to let the lawyers go and take the clients that no longer have potential with them than to directly say to the client, 'We can't make the economics work,'" Slavin says. "Getting rid of clients doesn't answer the lack of profitability questions."

**STRENGTHEN COMMUNICATION**

Slavin says a number of firms are investing in training to help attorneys learn to communicate with clients effectively and truly understand how each defines service.

"What works for one client doesn't necessarily work for another," he says. "Personalities are different. One individual at the same company might value project planning skills, and another might prioritize the total spent."

Talking to clients about their needs can help firms deliver the best possible service. However, once you initiate the conversation, you'll need to keep it going — and have the discipline to act on the input clients provide.

"[Many] law firms have learned the only way to truly know what clients think is to ask," Slavin says. "But the single worst thing you can do is talk to clients about how they define value, and then ignore what they say."

**ABOUT THE AUTHOR**

Erin Brereton is a Chicago-based freelance writer, editor and marketing consultant who has written about the legal industry, finance, business and other topics for the *Chicago Tribune*, *Legal Management*, *Commercial Law World* and other publications.

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