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Is Your Firm Leveraging Its Leverage?

Declining leverage is not a new problem for law firms. Over the past 10+ years, partner leverage has declined, and many firms have gradually, and sometimes unintentionally, shifted to a partner-heavy model. With the advance of non-traditional providers who often have a highly leveraged model, and intensifying client pressure for firms to improve efficiency, the time is ripe for firms to rethink and better organize their leverage model.

A Problem Years in the Making

In the aftermath of the 2008 recession and in the face of a material decline in demand, law firms conducted widespread associate layoffs. This start of the 'de-leveraging' of law firms began a shift from what were historically pyramid-shaped law firm staffing models, to diamonds or columns, and in some firms today, inverse pyramids.

At the same time, law firms also began to experience a swelling of the non-equity partner ranks. Non-equity partnership models were widely adopted in the early to mid-2000s, often without specific criteria for promotion beyond years of experience. This led to a proliferation of non-equity partner promotions over a number of years, and relatively unfettered promotion to non-equity still continues in some firms today. The combination of these two factors led to a reduction in the average associate to partner leverage among AmLaw 200 firms from 1.5 in 2005 to 1.4 in 2010, in spite of a 21% increase in lawyer headcount during this time period.

While these staffing decisions were likely necessary for some firms, particularly those most dramatically impacted by the financial crisis, other firms later regretted the material associate reductions. Once demand began to rebound post-recession, firms were hard pressed to find the talent needed to take on additional work. Competition for mid-level and senior associates skyrocketed, leading to even higher pay levels for the best talent. The reduced associate ranks also placed pressure on firms' talent pipelines, resulting in fewer high caliber candidates prepared to become future partners. In hindsight, many firms would say that the associate cuts may have been too deep, and the deleveraging created longer term opportunity costs associated with lost revenue, market share and potential future partner talent.

Where are Firms Today?

Fast forward to 2021. Law firms appeared to have learned from the past. The vast majority of law firms decided against mass associate layoffs in 2020 – in spite of extreme uncertainty in the early months of the pandemic. While some firms made this decision based in part on the nature of the crisis and the broader societal impact of the pandemic, others made this decision based on a desire to preserve leverage and retain the investments associated with recruiting and developing their hard-won associate talent.

Nonetheless, while firms avoided mass layoffs in 2020, firms still experienced natural attrition. Associate headcount was down 1.6% on average in U.S. based firms by the end of 2020.

So, where does that leave firms today? A majority of firms today have lower partner leverage than they did 15 years ago, and in many cases, firms are not effectively or efficiently deploying the leverage that they have available. Clearly, there are opportunities for firms to take on more non-partner leverage and to do more with the leverage they already have available within the firm.

Partner vs. Non-Partner Leverage

On average, income partners represent a large percentage of the lawyers within many mid-size and large firms –43% of the partnership and 21% of the total number of lawyers among the AmLaw 200.

While a partner-heavy model offers some advantages, particularly for firms focused on complex advisory matters, it can present challenges for firms handling a broader range of work. For the majority of firms, leverage is critical to managing the total cost of a matter. This is particularly true for large scale matters involving a range of tasks, price sensitive matters, or high-volume routine matters.

We often hear partner-heavy firms bemoan their lack of associate talent. The reality that these firms must confront is that their income partners are their leverage. While this may work just fine for some firms, it is an expensive form of leverage for many others, particularly those with mid-value and/or routine work.

To compound this challenge, in addition to large income partner classes, a number of firms are freely moving lawyers into a mix of counsel titles without first defining roles or expectations. In these firms, 'counsel' include a broad mix of lawyers - laterals seeking partnership, former partners transitioning to retirement, former associates who may or may not be considered for partnership, and off-track mid-career lawyers. It is important to note that a counsel model with clearly defined roles and performance expectations can create opportunities for firms to leverage experienced, off-track attorneys, often at a lower cost than on-track associates. However, when these roles are poorly defined, the counsel title can also become a 'dumping ground for underperformers,' where lawyers go to languish in their careers. In these instances, firms experience a range of challenges, including a high degree of variability in performance and productivity, compensation creep, and weak profitability.

Organizing Leverage for the Future

Looking ahead, firms seeking to make better use of leverage will need to rethink the value proposition around leverage. With clients keenly focused on efficiency and a growing number of alternative providers entering the legal market, law firms are under pressure. Increasingly, clients are requiring law firms to move lower value and routine tasks down to the lowest cost resources. They are also insisting, as an overall principle, that firms direct work to the most appropriate level resource for each specific task, which in some cases does not require lawyers, or even humans.

To respond to client expectations around staffing and efficiency, firms will need to not only take a hard look at old forms of leverage (whether it is a partner-heavy model or the undisciplined application of counsel roles, or both), but also creatively and strategically evaluate new sources of leverage.

A number of firms are fairly far down the path building a leverage model more heavily comprised of lower-cost lawyer and non-lawyer roles, including: Staff Attorneys (typically salaried lawyers paid at a significantly lower level than traditional associates), Contract Attorneys (typically hourly lawyers, hired for specific matters or outsourced through a contract attorney service), and Other Professionals (including economists, technical specialists, nurses/doctors, consultants, project managers, etc.).

While firms are already using these roles and building leverage through them, they are often doing so without a clear strategy around how the firm will maximize the benefit of this emerging form of leverage. Often, these resources are simply folded into the practice groups and treated as 'other timekeepers' handling legal or quasi-legal work in the same way traditional paralegals, associates, and counsel handle their work. When this occurs, firms often find that these lower cost resources go underutilized or mis-utilized – from a staffing perspective (e.g., level of work or volume of work), a talent management perspective (e.g., getting lost in the shuffle), and/or compensation perspective (e.g., relativity problems driving morale challenges or compensation creep driving profitability challenges).

In order to maximize the benefits of lower cost, non-traditional resources, firms must take a more strategic approach to the organization, management, and staffing of these roles.

One of the most critical, gating questions firms must confront is around the organization of these roles. Increasingly, we see firms making more strategic use of these roles by moving them into formal, organizational models outside of traditional practice groups. This focused organizational model built around emerging leverage enables firms to develop a more defined and consistent approach to how these resources will be staffed. Dedicating management to these functions also helps ensure that firms develop answers to the following critical questions:

- What types of tasks will these roles perform? What types of tasks will they not perform?
- What are the performance expectations for these roles?

- What career progression opportunities will be available for these roles?
- Who will manage them?
- How will these resources be trained?
- What types of workflow processes and technologies will be applied to help manage their more routine tasks?

In addition to tackling the key questions above, a structured organizational model and dedicated leadership also helps ensure that firms are managing – across practice groups – how these resources are applied within the firm's overall client service model. It ensures non-traditional staffing resources are used for the most appropriate tasks and at a sufficient rate to create profitability. Also, the cross-practice centralization of these resources enables firms to more fluidly move resources into support areas experiencing surges in demand, and away from areas bottoming out.

Of course, there is also the opportunity for firms to leverage technology more effectively in the delivery of legal services, and to factor technology into the design of leverage models and the mix of talent required. We are still in the early stages of the application of AI in the practice of law and the automation of routine tasks – technologies which are already reshaping leverage models. We also see increasing use of predictive algorithms, which necessitate more senior level insight (e.g. litigation case outcomes), as yet another consideration in establishing a leverage model for the future.

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Now is the time for firms to rethink how to best leverage their leverage. In addition to evaluating the advantages and disadvantages of existing forms of leverage, firms should look to the future, by creatively and strategically exploring the adoption of new staffing models, the related technologies, and approaches to service delivery, and ensuring those models are structured for success.

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