



MANAGEMENT

Your Firm's Place in the Legal Market

How should you grow? Analyzing the future needs of your clients is key.

By William Henderson and Evan Parker

GROWTH IS THE LINCHPIN OF THE TRADITIONAL LAW FIRM model, as it creates an aura of confidence for partner/owners and the resources and opportunities necessary to reward junior lawyers for their hard work. For decades, growth occurred organically; as clients grew, so did the firm.

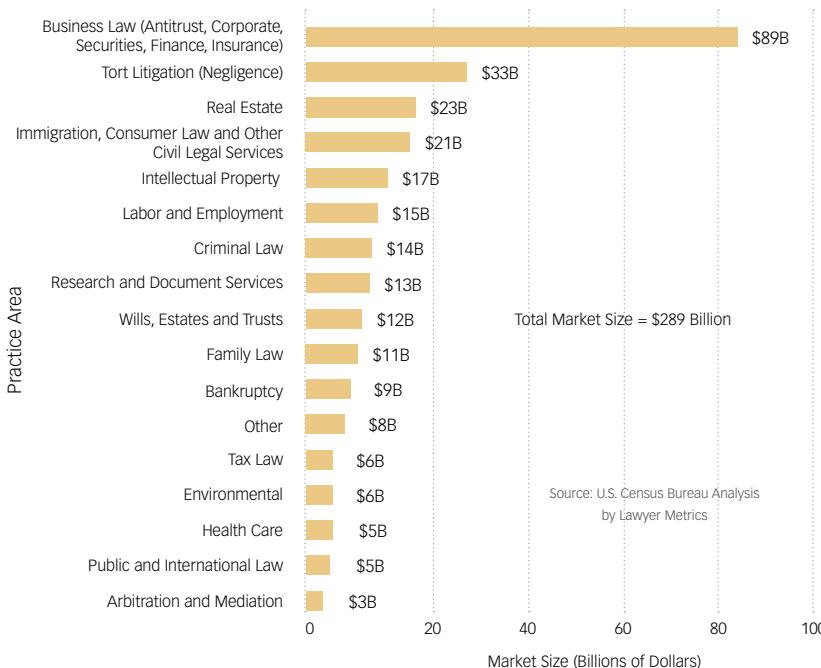
But every market has a saturation point. For the corporate legal market, the rise of The Am Law 200 ended comfortable regional oligarchies. Regional firms became national firms by moving into each other's backyards and poaching each other's talent. An unintended consequence

of all this growth is that the supply of capable outside counsel exceeds demand.

For the foreseeable future, most of The Am Law 200 will only be able to grow by taking market share. Yet this business challenge is no more formidable than the one confronted by Steve Jobs upon his return to Apple in 1997 ["How to Take Market Share," November]. For the better part of a decade, the company had been losing market share to Microsoft. For Jobs, focus was the key—create a handful of new products that were "much better" than anything else in the market. To achieve this goal, Apple would "start with the customer experience and work backward to the technology." That singular focus can help large law firms take market share.

MARKET SIZE BY PRACTICE AREA

Business law is the focus of Big Law. But there's money to be made in other practice areas.



SIZING THE U.S. LEGAL MARKET

Standard questions in any focused planning process are, "What is the size of the addressable market?" and "Why are the customers in this market going to buy from us and not our competitors?" The answers provide the basis for strategic focus.

Here is some data to begin formulating an answer to the first question. The market for U.S. legal services totals roughly \$289 billion. We calculated this number directly from the 2012 Economic Census, the census of U.S. business that takes place once every five years. In 2012, the Census Bureau reported that the dollars spent in the U.S. legal services market totaled \$263 billion (NAICS code 5411). These are the gross receipts of organizations that are in the business of providing legal services. We then adjust upward to \$289 billion to ac-



count for upward growth in GDP between 2012 and 2015.

One of the implications immediately evident in this analysis is that the U.S. legal market is highly fragmented. Latham & Watkins, the firm at the very top of the Am Law 200 league table (\$2.6 billion in annual revenue), has less than 1 percent of the total market. At the same time, the combined annual revenues of the 2015 Am Law 200 totaled \$100.4 billion, which reveals the enormous economic sway of the large law firm sector.

WHICH PRACTICE AREAS?

The Economic Census disaggregates the gross receipts of legal service organizations into so-called product lines. With a little work, these product lines can be grouped into a set of submarkets that break down annual sales into prac-

tice areas familiar to most big-firm lawyers (see the graph on the facing page).

Sizing the market in this way, we see the relative importance of certain legal work and the wide variation by practice area. The largest market is the one most synonymous with large-firm practice: antitrust, corporate, securities, finance and insurance. Although some of the market is focused on retail clientele (wills, estates and trust, \$12 billion; family law, \$11 billion), most specialties bear on the commercial world.

Returning to the focus principle, the \$15 billion labor and employment (L&E) market offers a good case study.

For large corporate clients, labor and employment legal fees are a cost of doing business—a cost they want to minimize while also reducing settlement costs, court and arbitration awards, and the risk of future litigation. Yet, for at



least the last 15 years, firms toward the top of The Am Law 200 have had little interest in solving those problems, instead responding to client rate pressures by shedding L&E lawyers ("Playing Not to Lose," February 2013).

A few law firms, however, decided to make L&E their singular focus. Three examples are Oglethorpe Deakins, Jackson Lewis and Littler Mendelsohn. In the 2005 Am Law 200 rankings, these firms ranked No. 195, No. 128 and No. 108, respectively. Their combined revenues were \$433 million. A decade later, all three had significantly grown their topline and entered The Am Law 100 (No. 84, No. 79 and No. 62). Their current combined revenue is \$1.3 billion, or nearly 10 percent of the total U.S. labor and employment legal market.

Law firm leaders may scoff at the low revenue per lawyer (RPL) figures generated by these three firms (between \$500,000 and \$530,000, compared with an average \$882,000 for The Am Law 100 and \$643,000 for Second Hundred firms.) Yet alternative staffing, use of technology and better practice management enhances the profitability of this lower RPL work, particularly if work is performed using AFAs. Ac-

ark that won't sink. This stability and prosperity was created by working backward from the needs of the client.

WHICH INDUSTRIES?

One of the most common laments from corporate clients is the failure of outside counsel to understand their business. A law firm can solve this problem by focusing its resources on clients in a handful of industries, thus creating the economies of scale and scope to master its clients' mix of business and legal issues.

Some industries spend more money on legal fees than others. Working with Rees Morrison, a principal of Altman Weil, who has collected data on law department spending since 2010, we constructed a statistical model (see graph at left) to estimate differences in external legal spending across 11 industries. External spending is based on percentage of company revenue; 0.3 percent is the average across 2,500 corporate clients in the sample.

One obvious takeaway is that legal problems (and legal bills) vary widely by industry, with companies in finance, technology and energy sectors tending to spend the most. Yet law firms often draw the wrong inferences, focusing on marquee clients and lateral partners on Wall Street, Silicon Valley or the Houston Energy Corridor. Rather than envy someone else's client base, a better path is to know your market and pursue focused opportunities.

Among firms serving the finance sector, Skadden, Arps, Slate, Meagher & Flom is one firm to envy. In the 1960s, the New York City-based firm had fewer than 20 lawyers and was an outsider. The firm got its start on Wall Street by representing shareholders in proxy battles because white-shoe firms turned down the work, lest they be seen as anti-management by their investment banking clients. With the rise of the hostile takeover era, Skadden rose to prominence along with another outsider firm, Wachtell, Lipton, Rosen

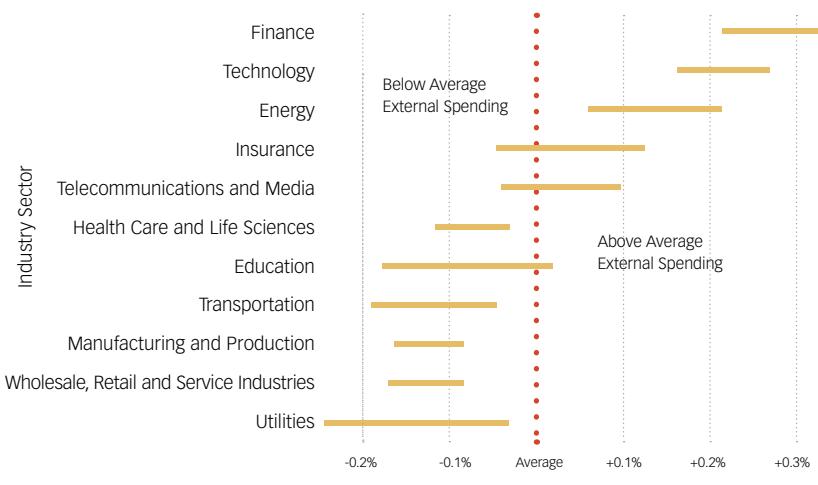
& Katz. Because the work paid well, the white-shoe Wall Street firms eventually followed.

Skadden and Wachtell entered a lucrative Wall Street niche by focusing on the needs of clients no one else particularly envied. When it comes to industry focus, study the industry concentrations that, through accidents of geography, history and relationships, already exist within your firm. What are those clients' most pressing business and legal problems? Answer that, and you'll provide better solutions than your competitors. In turn, you'll take market share.

William Henderson is a professor at Indiana University Maurer School of Law and co-founder of Lawyer Metrics. Evan Parker PhD is the director of analytics at Lawyer Metrics.

OUTSIDE LEGAL SPENDING BY SECTOR

Finance, tech and energy sectors spend a greater share of revenue on external legal work than do other industries. (The average is 0.3 percent of revenue.)



Source: General Counsel Metrics

cording to our research, all three of these firms appears to be pursuing this strategy, each with its own areas of emphasis.

One of the more surprising metrics on L&E firms comes from ALM's Corporate Representations scorecard. Based on our analysis of 2008-2012 data, Littler, Oglethorpe Deakins and Jackson Lewis are in the top five firms for having the most relationships with Fortune 500 companies. Furthermore, the No. 1 slot for Fortune 500 relationships went to general practice firm Morgan, Lewis & Bockius for the strength of its labor and employment work, which accounted for over 40 percent of its Fortune 500 representations.

Labor and employment may be a \$15 billion "commodity" legal market, but when diversified across a broad swath of corporate America, L&E firms appear to be building an