

THE LAW FIRM OF THE FUTURE

Winning the Law Firm Merger/Acquisition Game

March 15, 2023

by

Corey Castillo

Chief Operating Officer, Lagerlof LLP

Uri Gutfreund

SVP and Managing Principal, Ames & Gough

Roger Hayse

Director, Hayse LLC

Alex Muñoz

Principal and Co-Owner, CSR - Expertise in Results

John Remsen, Jr.

President, TheRemsenGroup

MPF WEBINAR

POWERED BY

TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm

TheRemsenGroup.com

MPF Webinar Series: The Law Firm of the Future



The MPF Webinar Series: Building the Law Firm of the Future
Winning the Law Firm Merger/Acquisition Game
An MPF Webinar with **Corey Castillo, Roger Hayse and Alex Muñoz**
March 15, 2023 – 2:00-3:00pm ET



1



Uri Gutfreund

Senior Vice President and Managing Principal, Ames & Gough



John Remsen, Jr.

President and CEO, Managing Partner Forum
President, TheRemsenGroup



2

MPF Webinar Series: The Law Firm of the Future



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



UPCOMING PROGRAMS IN 2023

- MPF Webinar Series – Third Wednesdays @ 2pm ET
- The MPF 2023 Leadership Conference – May 3-4, 2023, in Atlanta
- The MPF Law Firm Leadership Survey – **coming soon!**
- *The MPF Weekly* – Friday mornings
- MPF Website – www.ManagingPartnerForum.org
- MPF Listserv and Zoom MPIEs



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

3



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



TODAY'S WEBINAR

- Today's Topic: **Winning the Law Firm Merger/Acquisition Game**
- 86 Managing Partners and Law Firm Leaders
- Registrant Survey Results and Audience Polling Questions
- Recording and Handout Materials
- Your Feedback on Today's Session
- Next MPF Webinar – April 19, 2023



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

4

MPF Webinar Series: The Law Firm of the Future



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



Today's Guests



Corey Castillo
Chief Operating Officer - Lagerlof LLP
Pasadena, California



Roger Hayse
Director - Hayse LLC
Dallas, Texas



Alex Muñoz
Principal and Co-Owner - CSR-Expertise in Results
Atlanta, Georgia



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

5

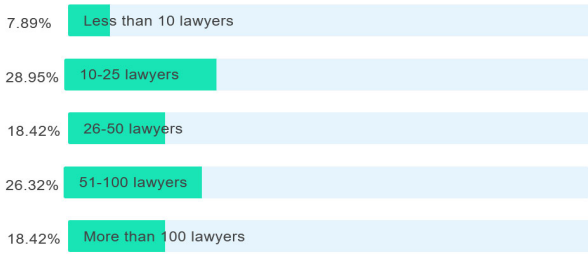


Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



AUDIENCE POLLING QUESTION #1

How many lawyers are with your firm?



Percentage	Number of Lawyers
7.89%	Less than 10 lawyers
28.95%	10-25 lawyers
18.42%	26-50 lawyers
26.32%	51-100 lawyers
18.42%	More than 100 lawyers



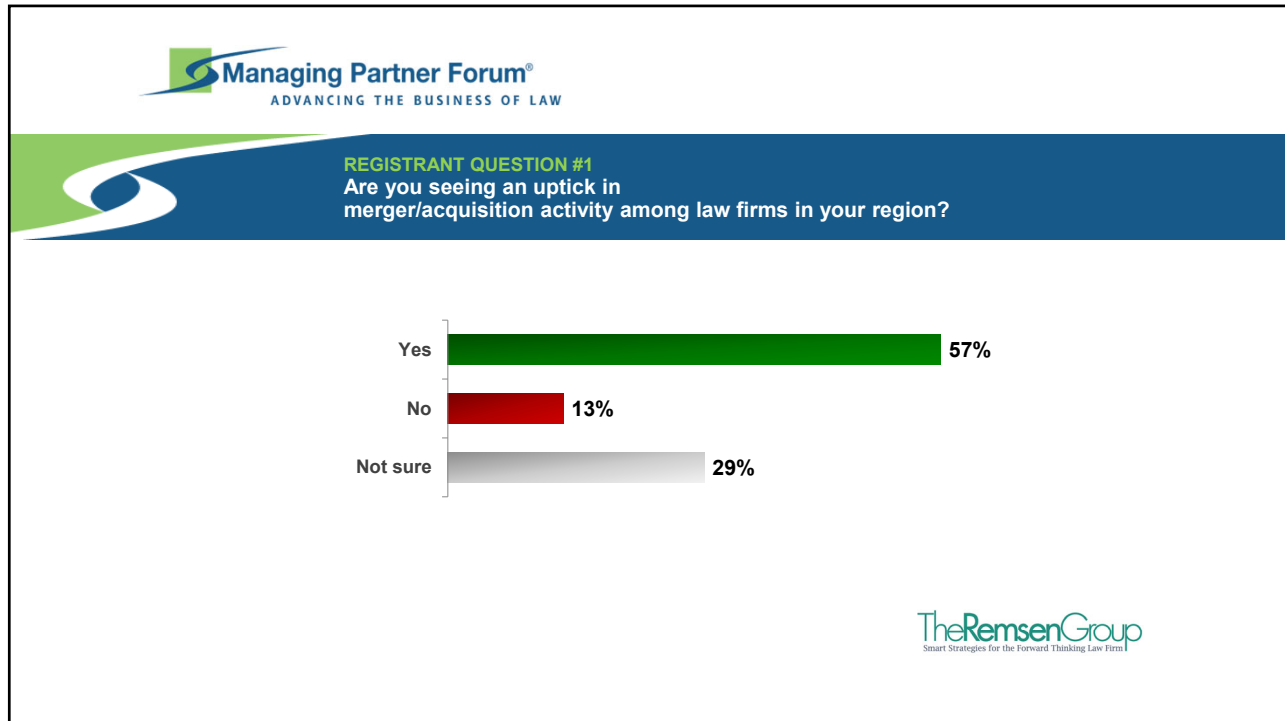
TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



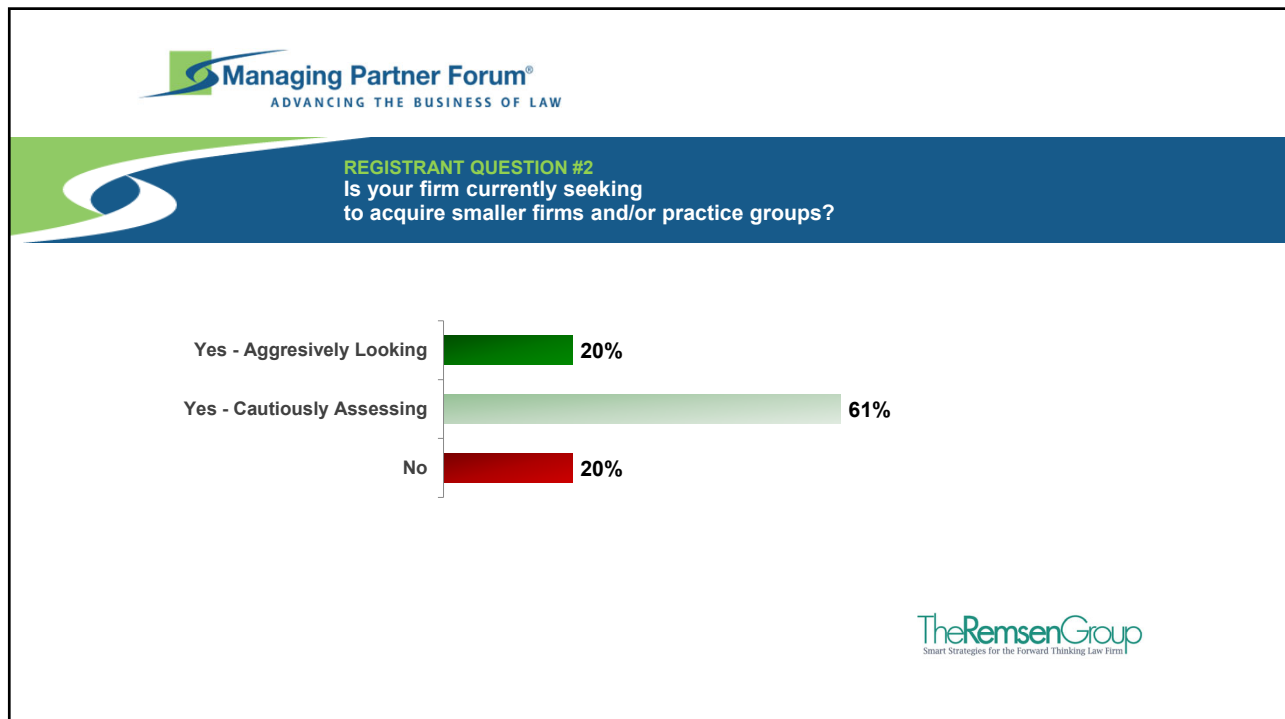
AMES & GOUGH

6

MPF Webinar Series: The Law Firm of the Future

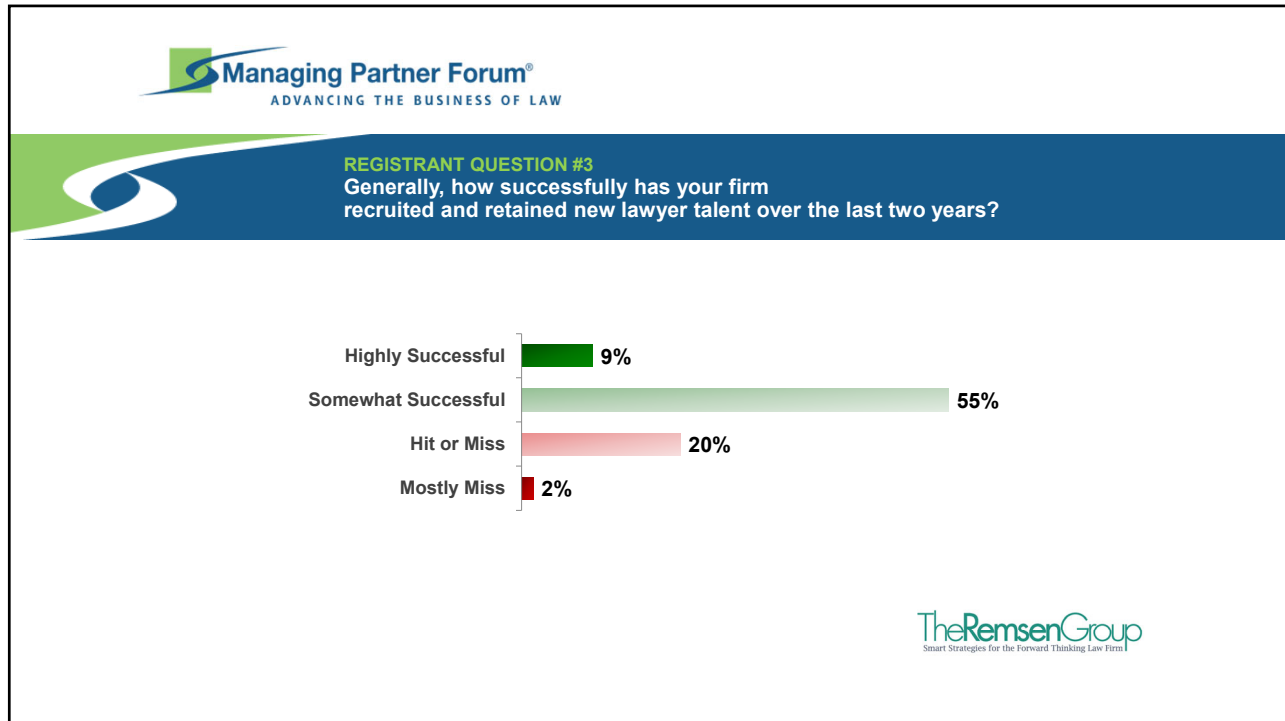


7

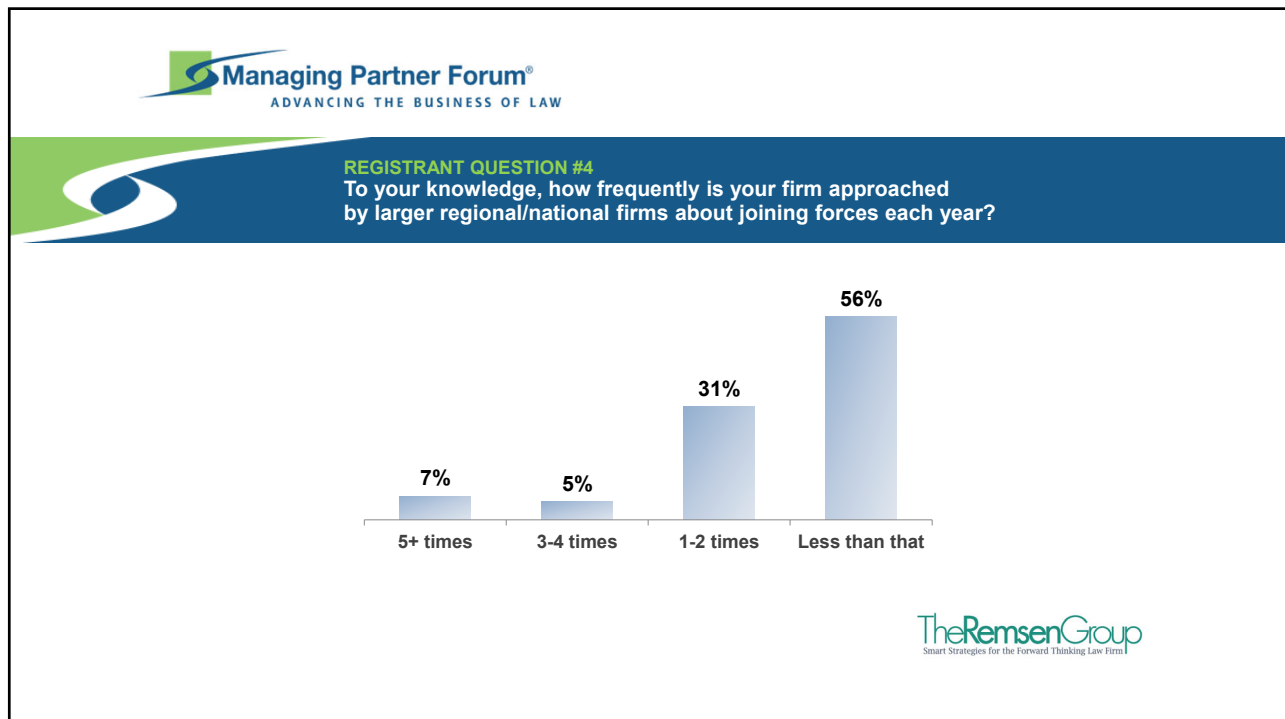


8

MPF Webinar Series: The Law Firm of the Future



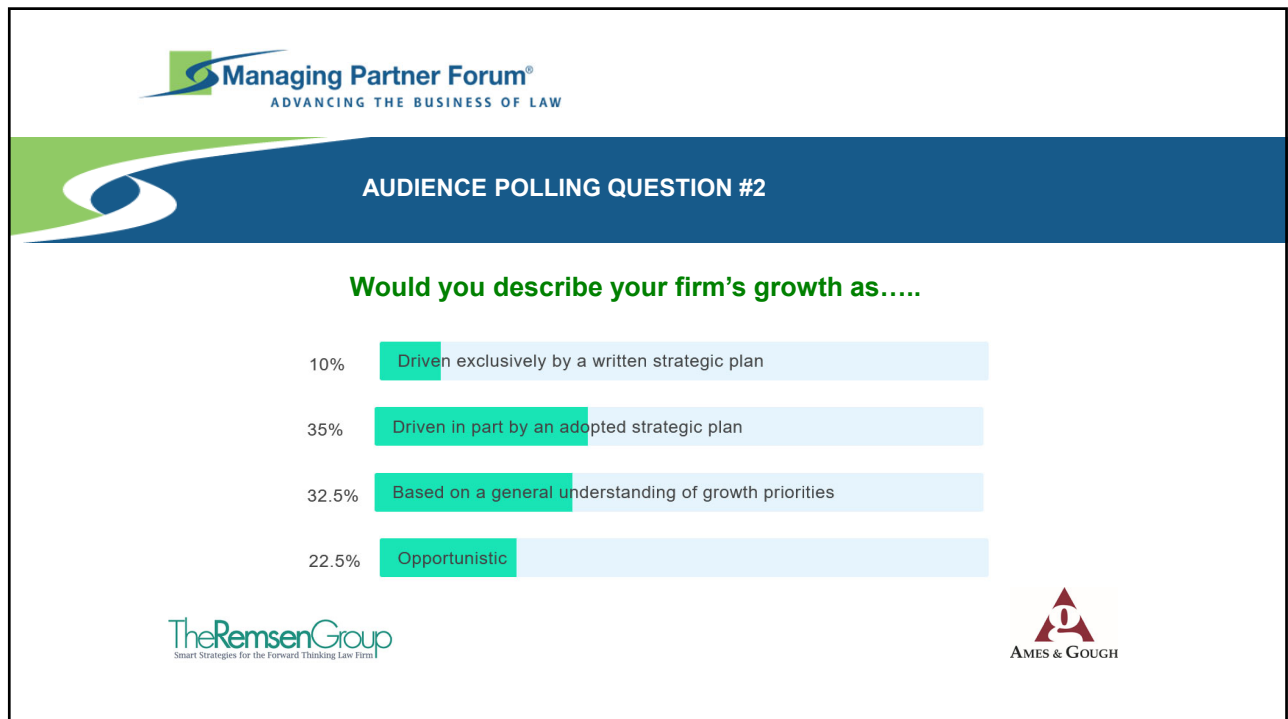
9



10



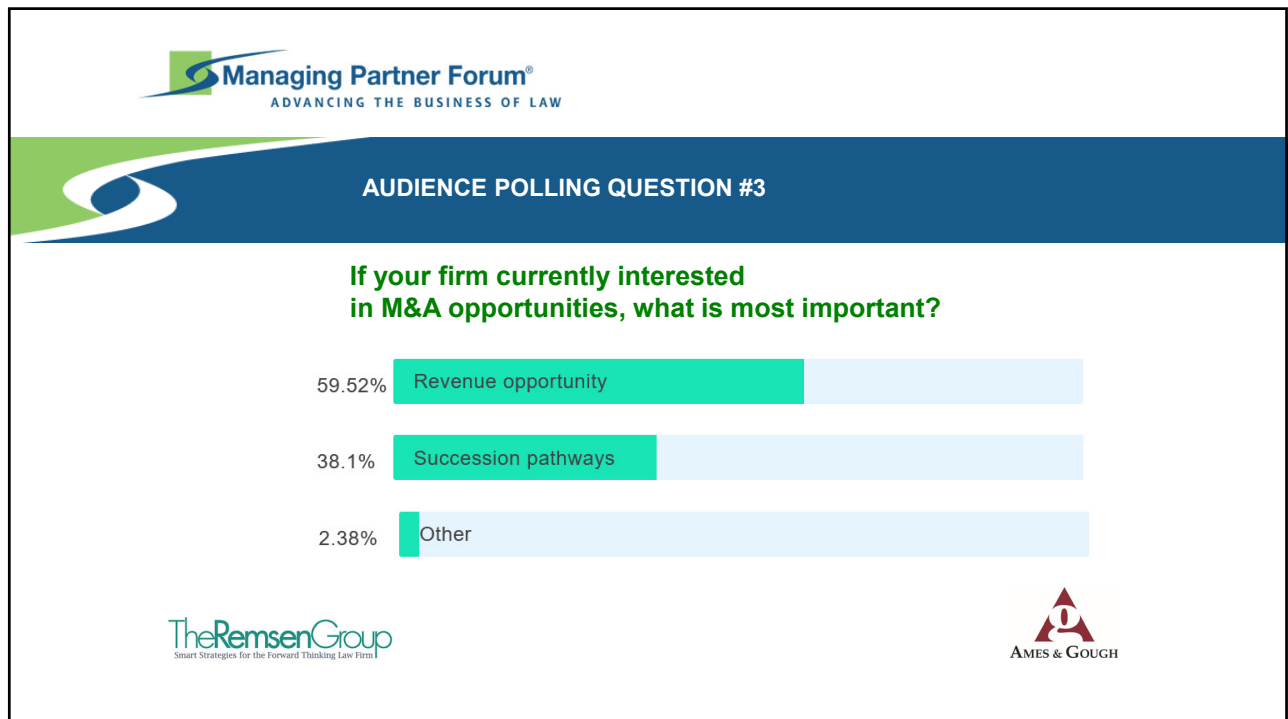
11



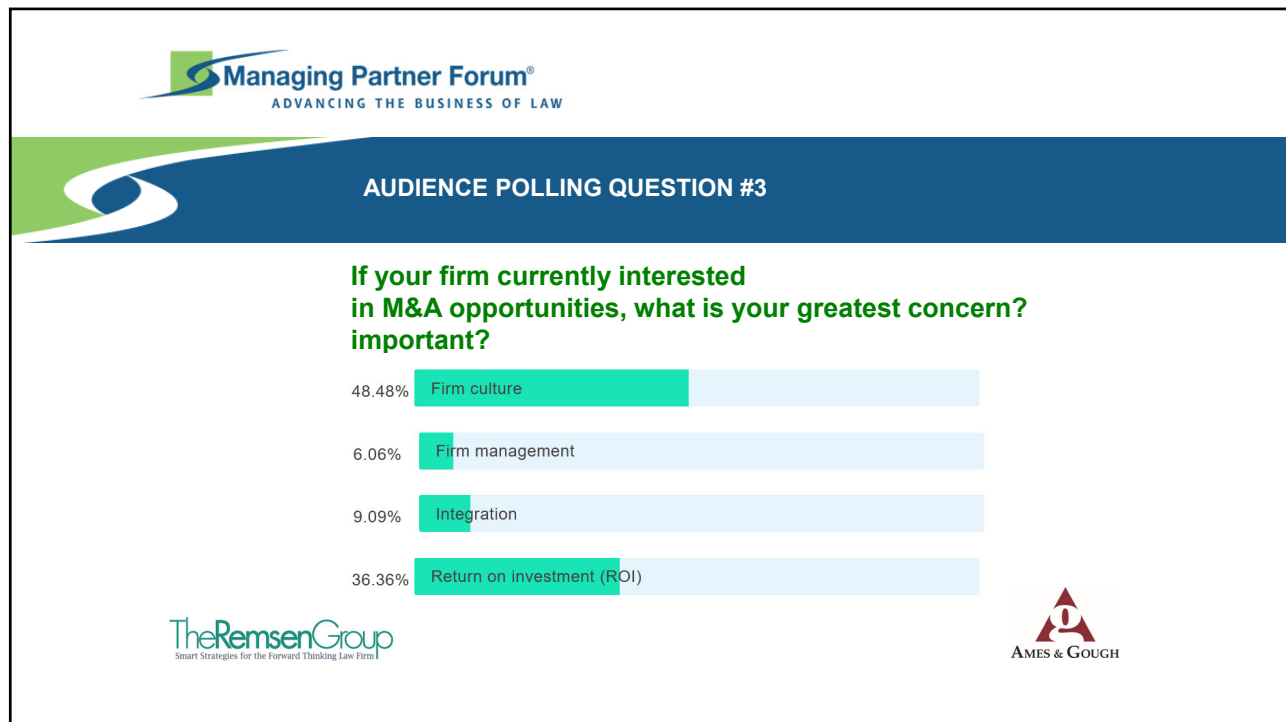
12



13



14



15

 **Managing Partner Forum®**
ADVANCING THE BUSINESS OF LAW

AS THE LARGER (ACQUIRING) FIRM

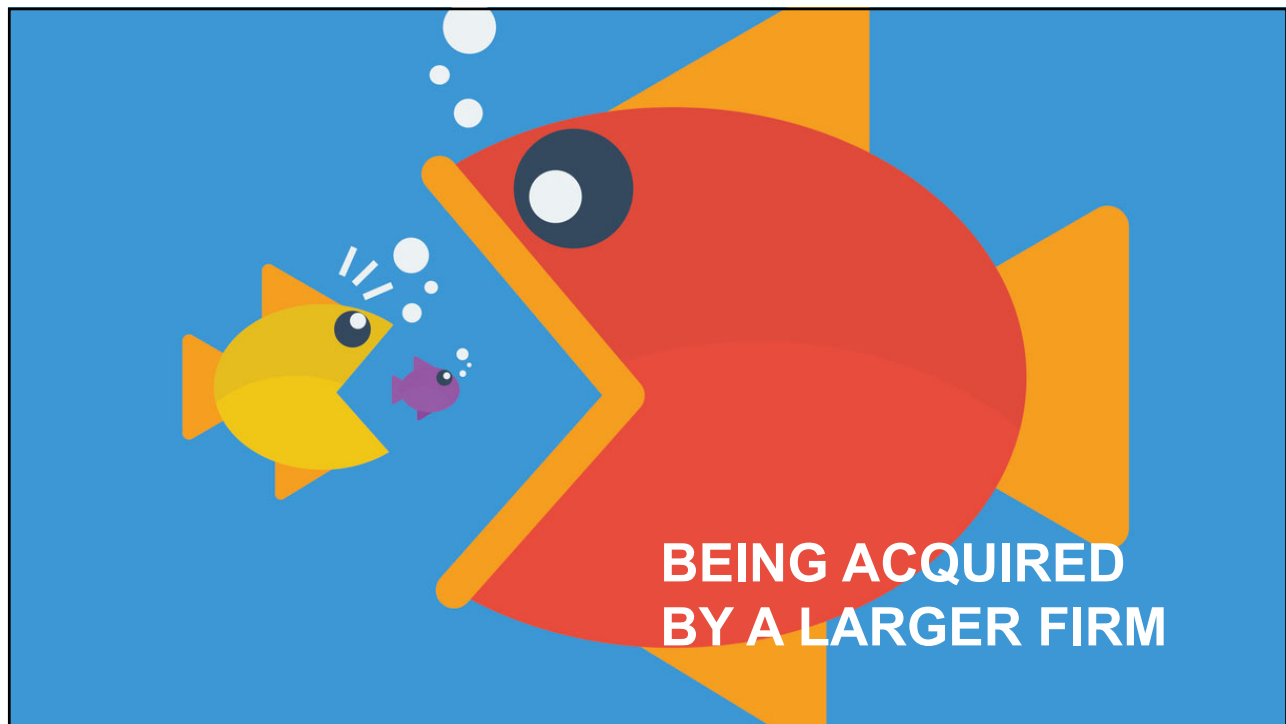
- Strategic Reasons - Clients/Practice Mix/Geography
- Firm Economics – RPL, PEPP, Unfunded Obligations, etc.
- Identify Potential Candidates
- What Are You Selling?
- Conflicts of Interest
- Culture/Core Values
- Compensation and Governance Models
- Remote Work Policies

 **TheRemsenGroup**
Smart Strategies for the Forward Thinking Law Firm

 **AMES & GOUGH**

16

MPF Webinar Series: The Law Firm of the Future



17



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



AS THE SMALLER (ACQUIRED) FIRM

- Why?
- What Are You Selling?
- Firm Valuation
- Process for Handling Inquiries
- All or Part of Us?
- Succession
- Future Leadership
- Headhunters and Brokers



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

18



19



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



DUE DILIGENCE CHECKLIST

- Conflicts
- Clients, Practice Areas, Geography
- Financial Compatibility
- Culture/Core Values
- Compensation, Governance and Ownership Models
- Firm Name
- NDAs
- Deliberate Integration Plans



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

20

MPF Webinar Series: The Law Firm of the Future



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



IMPORTANT REMINDERS

- Your Feedback on Today's Session
- On-Demand Recording and Handout Materials
- The MPF 2023 Leadership Conference – May 3-4, 2023, in Atlanta
- The MPF Law Firm Leadership Survey
- Next MPF Webinar – April 19, 2023



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

21



Managing Partner Forum®
ADVANCING THE BUSINESS OF LAW



CONTACT US

Corey Castillo – 951.231.7521 – ccastillo@lagerlof.com

Uri Gutfreund – 201.430.5827 – ugutfreund@amesgough.com

Roger Hayse – 214.244.1544 – rhayse@haysellc.com

Alex Muñoz – 404.850.7957 – alex@expertiseinresults.com

John Remsen, Jr. – 404.885.9100 – jremsen@theremsengroup.com



TheRemsenGroup
Smart Strategies for the Forward Thinking Law Firm



AMES & GOUGH

22

MPF Webinar Series: The Law Firm of the Future



The MPF Webinar Series: Building the Law Firm of the Future
Winning the Law Firm Merger/Acquisition Game
An MPF Webinar with **Corey Castillo, Roger Hayse and Alex Muñoz**
March 15, 2023 – 2:00-3:00pm ET



FIRMS MUST BE INTEGRATED FOR MERGERS TO BE SUCCESSFUL

by Robert W. Denney

As discussed in our April Communique, many mergers fail because there were red flag issues evident beforehand which the firms either ignored or failed to resolve. However, even if the firms resolve these issues beforehand, some mergers still fail. Why? Because management did not address the integration of the firms after they were officially merged. Here is a list of things that management should do in order to integrate the firms so that the merger is successful.

- **Give priority to human due diligence.** People issues are often at the root of failed mergers. The best way to address these issues – and to prevent a “we” and “they” attitude – is to . . .
- **Communicate, communicate, communicate.** During pre-merger due diligence, both firms generally take great pains to communicate to their partners – and eventually everyone in the firm – the status of the possible merger. After they merge, however, there is often a big drop-off in communication. This is the opposite of what should happen. More communication is needed after the merger than before. Firms that have successfully integrated do some or all of the following to maintain communication throughout the merged firm.
 - One of the most important steps is for the Managing Partner/CEO and others in senior management to be visible and available. They should walk the halls, talk to the people – staff as well as lawyers – and visit the offices, particularly if they are located in other parts of the country or even in other countries. The objective is to answer questions and provide information.
 - Distribute a daily newsletter with updates on what’s going on and what will be going on.
 - Set up a merger “hot line” to answer questions and obtain feedback. This is often best handled by senior members of the administrative staff.
 - Publish a directory of all personnel, administrative and support staff as well as lawyers. Include position or title if appropriate, practice group, office, phone number and e mail address. Plan to update the directory after a few months.

FIRMS MUST BE INTEGRATED FOR MERGERS TO BE SUCCESSFUL

Page Two

- Draft a temporary Procedures Guide and distribute it to everyone, lawyers and staff.
- **Form an Integration Task Force.** This is a group comprised of lawyers, administrative personnel and support staff from various practice areas and offices. Their charter is to provide feedback on how integration is progressing. This task force can also serve as a sounding board to test potential announcements, policies and plans.
- **Hold a partners' retreat three or four months after the merger.** Include senior administrative personnel. The objectives of the retreat should be:
 - To enable the partners from each prior firm to get to know each other.
 - To begin to get them working together.
 - To develop or confirm the direction or focus for the firm.

Agenda items could include:

- Define or reaffirm the firm's Vision.
- Develop or confirm principles about matters such as governance, client relations, internal communications and community involvement.
- Cross-marketing.
- Begin development of a Strategic Plan if none exists.
- **Schedule a separate meeting or retreat for key administrative personnel.** This should occur shortly after the partners' retreat.
- **Communicate with clients.** Everyone's focus and action must be client-driven. Major clients (largest fees) and key clients (potential for large fees) must see the benefits of the merger if it is to be successful.
- **Initiate cross-marketing.** Begin scheduling meetings of partners, associates and key firm managers, in-person or by conference call. Agenda items should include:
 - Presentations by each practice group
 - Presentations on industry expertise including specific clients
 - Identification of target clients who could use services from the "other" firm
 - Development of action plans to initiate cross-marketing opportunities
 - Setting dates to review progress and to track new work resulting from cross-marketing

FIRMS MUST BE INTEGRATED FOR MERGERS TO BE SUCCESSFUL

Page Three

- **Hold a firm retreat for all lawyers.** This should be scheduled for a year after the merger.
- **Establish criteria to measure the success of the merger – and track them.** These should include more than just increased revenues and profits/partner (PPP). Also include:
 - Progress in understanding and fulfilling the firm's Vision
 - Improvement in providing value to clients as measured by client feedback
 - Improvement in other key areas including:
 - case and project management
 - internal communications
 - development of practice and industry groups
 - additional work from existing clients
 - community involvement
 - reduced lawyer and staff turnover

Successfully integrating the firms after a merger requires a lot of extra work and can take as long as two years. But the only alternative – a merger that subsequently fails – is not acceptable.

#

Robert Denney Associates Inc. has provided strategic management and marketing counsel to law firms, companies and non-profit organizations throughout the United States and parts of Canada for over 30 years.

ROBERT DENNEY Associates, Inc.

P.O. Box 551, Wayne, PA 19087-0551 • 610-644-7020 • fax: 610-296-8726
email: bob@robertdenney.com • website: www.robertdenney.com



BEFORE THE MERGER – DUE DILIGENCE

Ellen Freedman, CLM
© 2005 Freedman Consulting, Inc.

I approach mergers like any other project. I use an organized methodology and checklist to help ensure nothing is overlooked in the process. And it is a process, folks, not an event. It is something to be approached with care and caution. I have witnessed too many mergers over the years which have evaporated before the ink was dry on the new letterhead. In most instances I'd shrug and think to myself that anyone could have seen it was never going to work. Well, except for those involved, of course. I've seen mergers which remain in effect, but one or two years later there are none of the attorneys of the merged-in firm remaining. Isn't this usually the way it goes? Well it doesn't have to be.

I've previously written about the fact that there are right reasons and wrong reasons to merge. [See *Merger Mania* originally published in the 10/8/01 issue of the PA Bar News.] I will therefore assume that you have already done some soul-searching to determine that the reasons for wanting to merge are valid. So now what? Well, 80% of attempted mergers don't come about. Mostly that's because firms don't go about the process properly. But fortunately it's sometimes because when the process is handled correctly, impossible obstacles are uncovered *before* the merger; not after, and one or both firms wisely withdraw from the process.

First a word of caution. As you make the preliminary steps to explore the feasibility of a merger, the utmost confidentiality should apply to the process. During the first part of the process — what I refer to as the due diligence phase — or the second part of the process — what I refer to as the compatibility assessment — there is a high likelihood that information will be revealed which will terminate the process. Under public scrutiny, one or both firms can be viewed as “damaged goods” if the merger fails to proceed. Outsiders will speculate and often make false assumptions about what was uncovered about one or the other firm which ultimately made them an unacceptable merger candidate. So you must really stress to involved partners how important it is that this exploration be strictly confidential.

The first step in the process involves performance of due diligence. If you don't get through this process relatively unscathed, there is no point in proceeding further, because you have virtually no likelihood of success. This article will focus on some of the most important aspects of due diligence. In its most basic terms, merger due diligence is about enabling both firms to really know what they're getting or becoming part of. It's about avoiding misperceptions and misconceptions, bait and switch tactics, or creating problems for a firm where there were none before.

Let's begin first, however, with a moment of candor. Realistically, in most merger instances one firm is being absorbed or acquired by another, larger or stronger—e.g. more profitable—firm. When that happens, the smaller or weaker firm is often reticent to perform its own due diligence, and defers to the information requests of the larger, acquiring firm. That's a mistake. It is important for *both* firms to clearly know what they're getting into. Ok, that being said, let's take a look at some of the most important aspects of due diligence.

1. **CONFLICTS OF INTEREST** must be explored. It is unusual if there are none uncovered here and there. But in most cases they can be dealt with by obtaining waivers, or resigning in a professional manner which does not prejudice the client. What you need to determine is whether there are any major clients or prospects who will be conflicted out as a result of the merger, and whether there are in fact any conflicting practice areas.

For example, a thriving insurance defense practice would suffer immeasurably by merging with a firm which did any significant amount of PI work. Even if there were not direct conflicts, the chances are that many of the insurance defense clients would not want to be represented by the firm any longer, due to the perceived positional conflict.

2. **VULNERABLE CLIENTS** should be revealed. An analysis of each firm's client roster should be made to determine where each firm's vulnerable clients are, and what impact on the firm's profitability the loss of the client(s) would make. Failure to disclose this is like selling a car and failing to disclose it was parked in a lake for a month. It can take some time and thought to do this. But from a marketing perspective, you should be doing it on a regular basis anyway.

For example, if one of the firms does a significant amount of business law and a major client is thinking of merging into an entity whose GC works primarily with a different firm in another city, this vulnerability should be disclosed up



front. If you are not comfortable disclosing specifics about the client, even with a mutual confidentiality agreement in place with the merger candidate, then you should disclose it in terms of dollars “at risk”.

Once this disclosure is made, the potential attractiveness of each candidate to the other under the “worst case” scenario must be considered. If there is truly synergy as a result of the merger, chances are the vulnerabilities won’t blow the deal. But if one firm is seeking a financial savior, knowing that the other firm may in fact be in a significantly different financial condition itself if certain events unfold may just change their decision. Better to find out beforehand.

3. What are the **PERCEPTIONS OF KEY CLIENTS** of each firm about the prospect of the merged firm? Prepare your “elevator speech” about the merger candidate and what you believe will be the benefits for clients. And then meet with a few in confidence to see how they react. Do they see it having positive or negative impact on their relationship with the firm? No matter how positive your firms view the merger, it counts for nothing if your clients view it otherwise.

For example, if one of the firms is a boutique, their clients may be drawn to them because they perceive that they will get more immediate and personal attention. Clients may believe that if the firm becomes part of a large firm it will result in a decline in service, and a degrading of the perceived importance of their work. It may just drive them away. So unless the merger simultaneously opens the door to bigger and better clients, you might wind up merging your firm out of its client roster.

As another example, in the course of this aspect of due diligence one firm uncovered bad feelings toward the merger candidate on the part of a key client. It turns out that the client had past experience with a few lawyers who subsequently became part of the merger candidate’s firm. The client had such ill will that he stated that he would “never do business with [the firm] again if you become part of that firm.” And of course, we know that the result would not be the resulting loss of just the one client. It would be that client, some other clients the client spoke to about the past experience with particular lawyers, and future prospects who would then be referred elsewhere by the lost client, instead of to your firm.



4. What are the **BILLING METHODS** of each firm? There are a number of variables here to consider. Just one of those is a need to explore on what basis firms bill. Flat fee? Hourly? Contingent? Firms that do some of everything can fit well with firms that bill on any basis or combination. But a merger between a firm which is strictly hourly with another which is contingent-based will often lead to strong conflicts and misunderstandings.

Typically, contingent-basis firms live in a roller-coaster financial environment. Budgeting is difficult. Cash flow can be feast or famine. Lines of credit are utilized regularly to fund on-going matters. When a big case results in a favorable verdict or settlement, it's a temporarily life-altering event. Payables are cleared, lines are temporarily retired, bonuses are given, capital investments in technology and other areas are quickly spent, and meaty distributions are made. For firms which bill on an hourly or flat-fee basis, this roller coaster is disconcerting, and often produces an unacceptable level of stress.

Typically, those who bill hourly are particularly disdainful of contingent-fee work when the result is unfavorable and write-offs must occur. They simply don't "get it" that not every case will be a winner. However, if a contingent-basis firm is diligent in the intake process and carefully screens incoming matters for quality, the "hits" will greatly outweigh the "dogs" and the firm will ultimately be profitable. The contrasting perspective from the contingent-basis attorneys is a recognition of the fact that hourly work will only generate excess revenues if production increases per lawyer. And there are only so many hours in a day, and you can only push people so hard. Therefore, a good stream of contingent-fee cases has a greater probability of creating excess value than a good stream of hourly cases.

Bottom line? Make sure differences in this area don't spell doom post-merger.

5. **PROFITABILITY AND OVERHEAD** are factors which relate to billing realization, but we're instead exploring the actual overhead cost spent to produce revenues, both including and excluding partner salary.

There are some attorneys who consistently consume more than \$1 in overhead (including salary) to produce \$1 in revenue. As a consequence, the more revenue dollars the attorney produces, the worse the financial condition of the firm. So while it may sound impressive that a partner in the firm generates one or even ten million in revenue receipts each year, you would not be happy to find out after the merger that it cost more than that to produce the revenues, because that would result in a reduction in income for yourself and other partners.



Along the same vein, some firms operate more efficiently than others. Overhead may consume just 40 cents of each revenue dollar. By today's standards, that's pretty frugal. But there are firms out there operating at the other extreme with an overhead cost at 60 or more cents of each revenue dollar. So it's important to compare how efficiently each firm is operating.

Don't assume that there will automatically be economy-of-scale efficiencies post-merger which will make one or both firms more profitable. Depending on where the overhead drain is, actual savings may or may not materialize. It is a common mistake to make this erroneous assumption about savings without doing a sufficiently in-depth analysis.

6. **BALANCE SHEET** items are often ignored. I tend to believe it's because most attorneys just aren't as versed in business accounting, and typically don't understand the significance of balance sheet items. But this is where due diligence exposes debts and other obligations of the firm. There may also be items which need to be disclosed or uncovered because they do not appear on the balance sheet, even as a footnote. For example, the existence of open or pending lawsuits, such as employment discrimination or wrongful discharge, can ultimately result in a huge payout. Unfunded retirement obligations, or buyout obligations for departed partners can come as a nasty surprise post-merger. Even a significant account payable in dispute with a vendor, and therefore not reflected on the books, can become an unpleasant surprise post-merger. If you're from a large firm, you are probably wondering how significant a factor a payable dispute can be. Keep in mind that a lot of mergers happen between relatively small firms, making the significance much greater. But even for a large firm, depending on the vendor and disputed purchase or service, the dollars can still be significant. (Think computer network, telephone system, software, custom animation, litigation support or any of a dozen other items or services which I can think of off the top of my head what can involve very significant amounts.)
7. **MALPRACTICE HISTORIES** of both firms must be compared, and the possibility of future claims must be examined and disclosed. One firm I know acquired not just a small practice, but an unpleasant surprise in the accompanying cancellation of its professional liability policy post-merger because of the claim history of the acquired practice. This was followed by several malpractice law suits. Every firm's worst nightmare, for sure.



Space precludes me from continuing, and there are certainly more areas which bear careful scrutiny during the pre-merger due diligence phase. Hopefully, this article has raised your awareness that the process may be more involved than you thought. Well, unless of course you want to do what a lot of firms do, which is a) decide that the other firm consists of “good guys” based on having gone to the same college, law school, church, etc, and just do the deal based on a lunch conversation and handshake; or b) decide that the other firm or group won’t be around long, contains sufficient “heavy hitters” to benefit your firm, and you’d better move fast and not stop to ask too many questions before the opportunity is lost.

I’m not suggesting that you take forever in this process. In fact, the simple fact is that on average law firms take a lot longer—too long— to complete a merger than any other industry. What I am suggesting is that you be thorough, don’t skip important steps, and don’t fail to utilize the services of a qualified consultant to assist you if you believe you can’t do this properly yourself. Often due diligence is better accomplished by a neutral third party. A separate article will focus on the many factors to explore during the pre-merger compatibility assessment phase.

*A version of this article originally appeared in the October 3, 2005
issue of the Pennsylvania Bar News*

©2005 Freedman Consulting, Inc. The information in this article is protected by U.S. copyright. Visitors may print and download one copy of this article solely for personal and noncommercial use, provided that all hard copies contain all copyright and other applicable notices contained in the article. You may not modify, distribute, copy, broadcast, transmit, publish, transfer or otherwise use any article or material obtained from this site in any other manner except with written permission of the author. The article is for informational use only, and does not constitute legal advice or endorsement of any particular product or vendor.





Law Firm Mergers and Acquisitions
Checklist of items for transition planning

General

- Identify critical issues for due diligence work
- Identify short term transition solution
- Determine long term goals
- Across all areas – personnel consolidation; specialty applications

Firm executives

- Legal form of new entity
- Firm management structure
- Management philosophy
- Practice area management and integration
- Staff management structure
- Workforce consolidation
- Firm-wide communications
- Facility location
- New partnership agreement
- Restrict use of predecessor firm name(s)
- Liability insurance
 - Outstanding malpractice issues
- Partner compensation
 - Partner guarantees
- Associate compensation
- Evaluation of skills, retention policy for valued associates, dismissal strategy for non-performers
 - Promotion policies
 - Recruiting strategies
 - Rotation, transfers and assignment
 - Continuing education

Administration

- Secretarial Services
- Purchasing and inventory management
- Office Services
 - Paper files
 - Records, closed files consolidation
 - Reproduction

- Deliveries
- Training
 - Policies and practices
 - Technical
- Human Resources
 - Policies
 - Compensation programs
 - Equalization program
 - Exempt/Non-exempt distinctions
 - Pay ranges
 - Skills
 - Promotion policies
 - Recruiting strategies
 - Overtime
 - Benefits
 - For various groups (Partner v. Associate v. Staff, etc.)
 - Vacation
 - Personal days
 - Meals
 - Medical plans
 - Retirement plans
 - Personal computers
 - STD, LTD
 - Life
 - Parking
 - Tuition reimbursement
 - Leave of absence policies
 - Loans
 - Employee subsidies, purchase programs
 - HR management system consolidation
- Facilities
 - Office Space
 - Integration of practice areas
 - Staff department consolidation
 - Moving expenses
 - Construction
 - Abandonment of leasehold expenses
 - Lease terminations
 - Commissions
- Accounting
 - Changes in accounting methods
 - Change in year-end
 - Capital structure – permanent capital, how paid in, debt
 - Key management statistics
 - Comparability of Financial Data
 - Value of WIP and A/R
 - Client Disbursements – balance sheet methodology, hard, soft

- Reserves
- Prepaid assets
- Cash v accrual
- Investments
- Accounting methods for software development costs
- Unrecorded assets
- Contingent liabilities
- Contingent tax matters
- Lease commitments – space, equipment
- Unrecorded liabilities
- Unfunded employee retirement plans
- Unfunded deferred compensation partner plans
- Accounting for retainers
- Unamortized opening adjustments from accounting method changes
- Operating leases
- Letter of credit
- Financial Analysis
 - Analysis of earnings, expenses, etc on an FTE basis
 - Difference in chargeable hour expectations
 - Proformas developed
 - Partners v Of Counsel – how paid? Share of NI or expense
 - Fee income eliminated due to conflicts, attorneys leaving firm
 - Benefit plans – funded, unfunded
 - Comparability of accounting policies for wip, a/r, client disbursements, prepaid assets, investments, goodwill, retainers, accrued liabilities, contingencies, operating leases, capital leases, partner loans, guaranteed payments, capital accounts
- Tax issues
 - Tax changes when merger consummated
 - Tax changes as result of operating as one firm
 - Depreciation methods
 - Tax accounting methods (cash v accrual, accelerated vs. straight-line depreciation)
 - Tax accounting periods (calendar vs. fiscal)
 - Tax accounting entities (partnership vs. PC)
 - Differences to be established between financial reporting policies and tax accounting policies for new firm
 - State and local tax issues positions
 - IRC Section 704(c) theoretical
 - Outstanding tax claims
- Accounting software
- Asset management
- Billing practices
- Billing rates
- Branch offices: access to data, reports, data entry, roles
- Budgets
- Collections
- Conflicts
- Contingent matters

- Disbursement recovery consolidation
- Executive information systems
- Financial Statements, internal & audited
- General Ledger integration
- Leases
- New accounting controls, data security controls and internal controls
- One time costs of merger
- Partner accounts
- Partnership and other Employment Agreements
- Payables
- Payroll
- Pensions
- Time Entry
- Standardization and integration of various codes
 - Clients' numbers, areas of law, etc.
 - Strategy for dealing with duplicates

Client Relations

- Visual identity, signage
- Letterhead, envelopes, business cards
- Client communications re merger
 - Announcement
 - Changes in policy or practice
- Media communications re merger
 - Announcement
- Firm-logo merchandise, gifts
- Client relationship software, address list consolidation
- Web site consolidation

Information Technology

- Phase 1 core application access
 - Network integration
 - Network user accounts
 - Electronic mail and calendar
 - Time Entry and Edit
 - File Opening
- Equipment consolidation
 - Inventory
 - Communications Infrastructure
 - Server
 - Workstation computers: configuration, operating system
 - Redundancy, disaster recovery
 - Special equipment: cameras, projectors, scanners, courtroom A/V
- General office application consolidation
 - Word processing
 - Macros and forms
 - Related document processing applications (redline, metadata scrub, PDF conversion)
 - Document management
 - Electronic mail and calendar

- Contacts
- Case management and docket
- Intranet systems
- Internet access
 - Domain names
- Electronic fax
- Remote access
- Various Administrative area specific software (legal recruiting, etc)
- Legal practice applications
 - Docket calendar
 - Case management
 - Client matter databases
 - Litigation support capabilities
 - Practice area specific applications
- Voice communications
 - Phone system integration
 - Switchboard consolidation
 - Call routing
 - Voicemail consolidation
 - Cellular phone program

Library

- Resource consolidation; paper and electronic
- System consolidation
- Westlaw, Lexis access

Other

- Time zone considerations
- Business climate (casual vs. suits), lifestyle issues
- International aspects

SMOCK♦STERLING

Strategic Management Consultants

THE SEVEN DEADLY SINS OF LAW FIRM MERGERS AND COMBINATIONS

By John S. Smock, Partner

Dante Alighieri's epic poem *The Divine Comedy* (and earlier theological/biblical references) listed the seven deadly sins of pride, envy, anger, sloth, greed, gluttony, and lust. In coming across this listing while doing some recent research, I clearly had an "*I could have had a V-8*" experience. These seven deadly sins – with a little bit of adjustment and redefinition – can clearly illustrate the problems many law firm managements have in successfully carrying out meaningful mergers and combinations. Thus, the following offers our take on these seven deadly sins of law firm mergers and combinations and what a firm interested in strategically growing can do about them.

Absence of an Articulated, Agreed Upon Growth Strategy

Growth is a capitalistic imperative – businesses have to successfully grow to respond to the dynamics of the marketplace. Law firms have to grow to survive (but, growth is defined by more than simply the number of attorneys).

- Certainly by now, most law firms of any size have had serious or semi-serious discussions regarding merger or combination with other firms.
- Yet, many of these firms have not considered or articulated why they want to grow, whether they want to merge or not (and many firms do not need to merge in order to grow), and, if they do, what they want in a merger partner (i.e. – criteria).
- And, even if firms have articulated a growth strategy, it is not understood, not reinforced, and often not supported within the partnership.

The remedy or antidote for this sin is clear – the development (and regular updating) of a clear straightforward growth strategy (that reflects the Firm's vision) that is shared with and understood by the Firm's partners and can be easily shared with any merger/combination candidate.

Laissez-Faire Approach to Merger Consideration and Execution

Many law firms have an unstructured approach to identifying candidates, determining the viability of a merger, and, ultimately negotiating and executing it. They lurch from step to step (a series of steps, rather than a parallel approach) and this often takes forever. As a result, even well thought out mergers/combinations die of their own weight. Often no one has responsibility other than the CEO/Managing Partner – but often he/she has little help and gets bogged down in the details. Scheduling meetings with key people in the two firms becomes an administrative impossibility or close to it.

If firms have decided they want to grow through merger or combination, then there must be a corresponding process, discipline, and schedule – and adherence to all three. Firms must decide who fits their criteria, who should be contacted, what happens in the initial and following meetings, and when each step has to be completed. Good mergers/combinations do not happen by accident.

Irrational Attachment to the Legacy Firm and an Inability to Focus on the New Firm

In spite of the fact that, intellectually, most law firm managers understand that the value of a merger or combination comes in what is created, not either firm's historical position – many cannot emotionally cope with that fact. We are continually amazed in seeing the representatives of both parties in an apparently solid strategic merger trying to ensure that everything will be done the way their legacy firm did it. Both firms try to duplicate what they had in their legacy firms and very little time and effort is placed on thinking about and planning for *new firm* (i.e. – thinking of a better way to do things).

Even in an acquisition of one firm by another, doing it the way the larger firms does is not necessarily the right answer. There is usually little attempt to take advantage of what the acquired firm brings to the table.

The antidote to this sin is very simple – get to thinking about and planning for new firm as soon as possible – regardless of the size differences of the two firms. *New firm* strategic plan should be developed early in the discussions, as should *new firm's* name.

The Fatal Need to One-Up Potential Partners, As If You Are Representing a Client

This corollary of the above sin is a particularly difficult one to deal with. Law firms, their managements, and, all too often, their non-lawyer management tend to enter merger negotiations looking for negotiation victories over their potential partner (e.g. – a larger number of people than logical on the Management Committee, control of the major practices, etc.). In fact, one of the biggest problems we have as consultants is to get both parties recognizing that they have to be negotiating relative to the needs of *new firm*, not to one-up the other. Simply put, if you win a victory in negotiating a law firm merger, you create an enemy. That will come back to haunt most firms and is not the way to begin a relationship.

The answer is to be fully transparent in a negotiation process and make a good faith effort to ensure that both firms are fairly represented in *new firm*. Remember, these people are going to be your partners – the golden rule applies.

Selfish Obstructionism

We see selfish obstructionism in virtually every merger we work on. This is where individual partners, small groups of partners, or non-attorney managers clearly get in the way of what the clear majorities in both firms are trying to do.

- That may come from an individual partner or a practice that does not feel the merger materially benefits them – so, rather than having their cheese moved, they put obstacles in the way of the overall merger.
- Often, small groups can have tremendous impact on decisions to merge or combine. Most firms have a super majority regarding merger decisions defined in their partnership agreement – usually 67% or 75%, while others have severely limiting super majorities, as much as 80% or 90%. It does not take much to create a roadblock that severely hurts the best strategic interests of both firms.

We have found that self obstructionism comes from two camps – the highly productive partners (one end of the bell curve) and the underproductive partners (the opposite end of the bell curve). Both see a merger or a combination as a direct threat to their present existence.

Addressing selfish obstructionism requires continuing communications by managements at both firms, isolating the obstructionists and dealing with them (more often than not diplomatically, but less than diplomatically if it is called for), and continuing, as discussed above, to focus on the advantages of *new firm*.

Avoiding Deal Breaking Issues

Another merger capital sin involves both firms avoiding difficult issues that often can be deal breakers. For instance, if the name (which is always an emotional issue) cannot be resolved, firms will put it on the back burner, but it always comes back to bite them when agreement is not achieved early on. Other potential issues that need to be addressed early are the philosophy of partner compensation, major conflicts (client and practice), organizational responsibilities, and major financial issues. Financial issues deserve a comment – often lurking in the firms' respective balance sheets are problems for both the legacy firms and/or for *new firm* (examples include such items as capital accounts, unfunded pension liabilities, etc.).

The appropriate way to deal with the avoidance of deal breaking issues is obvious – deal with them early in the process (as soon as possible). Most of these potential issues can be dealt with rationally early in the process – as time marches on they fester and become emotional issues and are much more difficult to deal with. And, if they cannot be resolved, better to know that before significant time and resources have been poured into merger discussions.

Inability to Integrate

The last deadly sin is a real killer. Even if firms have done everything the way it should be up to the closing of the merger, the combination can fall well short of expectations if there is an inability to integrate and execute against the idea of *new firm* and its strategy. Even though every law firm manager knows this to be true, actual integration performance can be very spotty. For example firms often make critical mistakes to avoid controversy – naming co-chairs for all of the practices, leaving practices and offices in one firm independent of the other, creating a management structure where each legacy firm is generally independently managed by its own people, etc.

Other manifestations of this final sin include poor marketing and missing the opportunity to tell the marketplace who *new firm* is and why the two firms have merged, inability to communicate effectively with clients about why the merger is being done and why it is in the clients' best interests, and an "*us versus them*" mentality among the administrative and support staffs of the two legacy firms. We have seen attorneys come together and merge effectively, yet years later there are examples of where the administrative staffs never merged or integrated.

The answers are straightforward and simple. First, a merger needs to be integrated as totally as humanly possible on the first day – no excuses. *New firm* begins on the first day of the merger, it does not slowly but surely emerge over the first year or two. Also, a detailed integration plan with tasks, responsibilities, and timing is essential to get the integration right.

* * * * *

We hope the above seven deadly sins of law firm mergers and combinations provided some insight to your own consideration of potential strategic growth moves. Our intent was not to be definitive or comprehensive, but to provide some insight to the major pitfalls.

Smock♦Sterling Strategic Management Consultants is a focused strategic management consulting firm with a primary industry focus on the legal marketplace. We serve our law firm clients in five areas – overall firm and practice strategy, mergers and combinations, practice group management, firm financial management, and strategic issue resolution.

SMOCK♦STERLING

Strategic Management Consultants

900 North Shore Drive, Suite 256 • Lake Bluff • IL • 60044 • (847) 615-8833

6430 N. Central Avenue, Suite 207 • Chicago • IL • 60646 • (773) 763-6353

29 Weston Rd. • Weston • CT • 06883 • (203) 341-0601

www.smocksterling.com

Merger Checklist

- Determine compatibility of Mission/Vision/Goals
- Analyze and resolve differences in
 - Net equity
 - Performance (hours originations etc.)
 - Billing rates
 - Clients
 - High end/commodity
 - Plaintiff/defense
 - Company/Individual
 - Conflicts
 - Open or threatened litigation
 - Debt
 - Compensation systems
 - Leverage
 - Cost
 - Staffing
 - Capitalization
 - Policies and procedures
- Deal structure
 - Name
 - Entity type
 - Decision making
 - Roles/titles
- Integration plan
- Announcement/Marketing plan



Law Firm Mergers and Acquisitions
Checklist of items for transition planning

General

- Identify critical issues for due diligence work
- Identify short term transition solution
- Determine long term goals
- Across all areas – personnel consolidation; specialty applications

Firm executives

- Legal form of new entity
- Firm management structure
- Management philosophy
- Practice area management and integration
- Staff management structure
- Workforce consolidation
- Firm-wide communications
- Facility location
- New partnership agreement
- Restrict use of predecessor firm name(s)
- Liability insurance
 - Outstanding malpractice issues
- Partner compensation
 - Partner guarantees
- Associate compensation
- Evaluation of skills, retention policy for valued associates, dismissal strategy for non-performers
 - Promotion policies
 - Recruiting strategies
 - Rotation, transfers and assignment
 - Continuing education

Administration

- Secretarial Services
- Purchasing and inventory management
- Office Services
 - Paper files
 - Records, closed files consolidation
 - Reproduction

- Deliveries
- Training
 - Policies and practices
 - Technical
- Human Resources
 - Policies
 - Compensation programs
 - Equalization program
 - Exempt/Non-exempt distinctions
 - Pay ranges
 - Skills
 - Promotion policies
 - Recruiting strategies
 - Overtime
 - Benefits
 - For various groups (Partner v. Associate v. Staff, etc.)
 - Vacation
 - Personal days
 - Meals
 - Medical plans
 - Retirement plans
 - Personal computers
 - STD, LTD
 - Life
 - Parking
 - Tuition reimbursement
 - Leave of absence policies
 - Loans
 - Employee subsidies, purchase programs
- HR management system consolidation
- Facilities
 - Office Space
 - Integration of practice areas
 - Staff department consolidation
 - Moving expenses
 - Construction
 - Abandonment of leasehold expenses
 - Lease terminations
 - Commissions
- Accounting
 - Changes in accounting methods
 - Change in year-end
 - Capital structure – permanent capital, how paid in, debt
 - Key management statistics
 - Comparability of Financial Data
 - Value of WIP and A/R
 - Client Disbursements – balance sheet methodology, hard, soft

- Reserves
- Prepaid assets
- Cash v accrual
- Investments
- Accounting methods for software development costs
- Unrecorded assets
- Contingent liabilities
- Contingent tax matters
- Lease commitments – space, equipment
- Unrecorded liabilities
- Unfunded employee retirement plans
- Unfunded deferred compensation partner plans
- Accounting for retainers
- Unamortized opening adjustments from accounting method changes
- Operating leases
- Letter of credit
- Financial Analysis
 - Analysis of earnings, expenses, etc on an FTE basis
 - Difference in chargeable hour expectations
 - Proformas developed
 - Partners v Of Counsel – how paid? Share of NI or expense
 - Fee income eliminated due to conflicts, attorneys leaving firm
 - Benefit plans – funded, unfunded
 - Comparability of accounting policies for wip, a/r, client disbursements, prepaid assets, investments, goodwill, retainers, accrued liabilities, contingencies, operating leases, capital leases, partner loans, guaranteed payments, capital accounts
- Tax issues
 - Tax changes when merger consummated
 - Tax changes as result of operating as one firm
 - Depreciation methods
 - Tax accounting methods (cash v accrual, accelerated vs. straight-line depreciation)
 - Tax accounting periods (calendar vs. fiscal)
 - Tax accounting entities (partnership vs. PC)
 - Differences to be established between financial reporting policies and tax accounting policies for new firm
 - State and local tax issues positions
 - IRC Section 704(c) theoretical
 - Outstanding tax claims
- Accounting software
- Asset management
- Billing practices
- Billing rates
- Branch offices: access to data, reports, data entry, roles
- Budgets
- Collections
- Conflicts
- Contingent matters

- Disbursement recovery consolidation
- Executive information systems
- Financial Statements, internal & audited
- General Ledger integration
- Leases
- New accounting controls, data security controls and internal controls
- One time costs of merger
- Partner accounts
- Partnership and other Employment Agreements
- Payables
- Payroll
- Pensions
- Time Entry
- Standardization and integration of various codes
 - Clients' numbers, areas of law, etc.
 - Strategy for dealing with duplicates

Client Relations

- Visual identity, signage
- Letterhead, envelopes, business cards
- Client communications re merger
 - Announcement
 - Changes in policy or practice
- Media communications re merger
 - Announcement
- Firm-logo merchandise, gifts
- Client relationship software, address list consolidation
- Web site consolidation

Information Technology

- Phase 1 core application access
 - Network integration
 - Network user accounts
 - Electronic mail and calendar
 - Time Entry and Edit
 - File Opening
- Equipment consolidation
 - Inventory
 - Communications Infrastructure
 - Server
 - Workstation computers: configuration, operating system
 - Redundancy, disaster recovery
 - Special equipment: cameras, projectors, scanners, courtroom A/V
- General office application consolidation
 - Word processing
 - Macros and forms
 - Related document processing applications (redline, metadata scrub, PDF conversion)
 - Document management
 - Electronic mail and calendar

- Contacts
- Case management and docket
- Intranet systems
- Internet access
 - Domain names
- Electronic fax
- Remote access
- Various Administrative area specific software (legal recruiting, etc)
- Legal practice applications
 - Docket calendar
 - Case management
 - Client matter databases
 - Litigation support capabilities
 - Practice area specific applications
- Voice communications
 - Phone system integration
 - Switchboard consolidation
 - Call routing
 - Voicemail consolidation
 - Cellular phone program

Library

- Resource consolidation; paper and electronic
- System consolidation
- Westlaw, Lexis access

Other

- Time zone considerations
- Business climate (casual vs. suits), lifestyle issues
- International aspects

Firm Scorecard - Strategic Planning

Scoring System

10 Points	8 Points	6 Points	4 Points	2 Points
This area has been <i>fully addressed</i>	This needs <i>minimal improvement</i>	This needs <i>some improvement</i>	This needs <i>serious improvement</i>	This area has <i>barely been addressed</i>
Item	Description			Score
1	We have a precise, well-articulated mission or purpose statement that we actively use to make key decisions.			
2	We have a clear, aspirational vision statement that guides long-term goals.			
3	We have identified 3-5 values that constitute the fundamental basis of our culture.			
4	We have completed a SWOT analysis (or a similar exercise).			
5	We have developed an Ideal Client Profile(s) and use it consistently in our marketing and business development efforts.			
6	We have a 3-5-year pro forma to project our financial state.			
7	We have well-developed 5-10 year goals and a well-defined plan to accomplish those goals.			
8	We have defined strategic objectives for the current year in each functional area.			
9	We have a detailed project plan for the current year based on the strategic objectives.			
10	We have a 90-day plan based on the strategic plan & have quarterly meetings to review progress and plan for the following quarter.			



Total:

Scoring Analysis

100	99 - 80	79 - 60	59 - 40	39 - Below
Overall, strategic planning is sound.	A limited number of areas need to be addressed.	Some areas need important improvements.	Some steps have been taken, but significant areas need attention.	Current status jeopardizes company goals.