

THE
AMERICAN LAWYERClients or Partners? Who Does a Big Law
Merger Have to Please More?

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December 4, 2023

Editor's Note: This is the third in a series by Hugh Simons on law firm mergers. The first piece on how mergers succeed can be found [here](#) and the second piece on turning a firm with declining profits into an accretive acquisition can be found [here](#).

A merger is not a strategy; rather, a merger can be a means for a firm to drive forward its strategy. This truism warrants some unpacking. What exactly is a strategy? In theory, how might a merger move one forward? In practice, what tends to happen?

Strategy and Mergers: Theory

In a business context, strategy has a very specific meaning: it is the conceptual basis by which a firm intends to realize above-normal profitability on a long-term basis. Commodity chemical companies pursue a cogent strategy: they accept that there is an exogenously-set market price that they can get for their product, and they then build plants larger than those of their competitors so that, through economies of scale, they can operate at lower costs, and hence enjoy higher profits, than the competition. Pharma companies pursue a simple strategy: they develop drugs for which people are prepared to pay handsomely and then prevent would-be competitors coming into the market and undercutting them on price through patent



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Panorama top view diverse corporate officer worker collaborate in office connect puzzle piece as partnership and teamwork concept. Unity and synergy in business success with jigsaw puzzle. Concord

protection; high prices and no price erosion deliver long-term strong profitability.

Strategy at high-performing law firms is different from that at traditional businesses in that law firms operate in two markets simultaneously—that for clients and that for lawyer talent, particularly partners. However, all firms pursue the same core strategy: they seek to attract and retain compelling clients by having great lawyers, and to attract and retain great lawyers by having compelling clients. It's the eBay strategy: eBay is the place buyers know to go to in order to find

sellers, and the place sellers know to go to in order to find buyers. Once a leadership position is established in such a two-sided marketplace, it is extraordinarily difficult for would-be competitors to break in: without great lawyers they can't attract the compelling clients; without compelling clients they can't attract great lawyers. With competitors thus effectively locked out, the firm that is the marketplace provider can realize strong pricing, and hence above-normal profitability, indefinitely.

Of course, the realization of a concrete lock on a marketplace is an idealized outcome (in the same way that 'perfect competition' and 'monopoly' are idealized conditions in Econ 101). However, by developing market leadership in specific areas (typically combinations of industry sector, practice area, and geography) firms build the renown that has mutually-reinforcing attraction to great lawyers and great clients, and thus attain elements of the advantages relative to the competition.

Bringing this back to mergers, the implication is that for a merger to advance a firm's strategy, it must enhance the firm's appeal to compelling clients and/or to great partners.

Strategy and Mergers: In Practice

Recent Big Law mergers have shown how mergers are used to enhance a firm's appeal to great partners. Essentially, they enable a step change in the composition of the equity partner ranks and, by extension, the firm's renown as a leader in the sectors, practices and geographies it serves. Merging firms take this step change while cognizant of the need to balance the imperative to grow their profitability relative to competitors with the obligations to maintain the highest quality of service, to protect the best of the firm's culture, and to sustain and build morale.

The data show that when healthy firms combine there is on average a 13% decline in the number of equity partners between a proforma combination of the firms pre-merger and the new entity in

its first year, and that this decline is accompanied by a 10-place rise in rank by revenue per equity partner. This reflects a transitioning out or de-equitizing of equity partners who undercut the achievement of a firm's revenue and profitability goals, often because they do not commit the hours, develop the volume of business or operate at the leverage that is consistent with being a partner at a high-performing firm. It reflects, too, that the continuing core group has greater depth in their chosen areas, that they're more typically seen as market leaders and that they appeal to clients as being the safe choice. Importantly, this group has the kind of high-performance culture that great partners look for in their peers: intensely-committed, business-savvy and strongly dedicated to personal development. Together, these attributes enable the continuing partners to command higher rates and thus have practices whose profitability can keep pace with rising market expectations for partner compensation.

How can a merger enhance a firm's appeal on the "compelling clients" side of the strategy? There are two broad options: enhance the breadth of services offered or enhance their depth, i.e., add new 'complementary' practices or 'double down' on current practices.

The strategy implicit in the former is that of the one-stop shop, i.e., the notion that clients will shift business to, and pay a higher price for a bundle of services from, a single firm than they would for individual offerings from separate firms; the higher prices naturally lead to higher profits. The strategy implicit in the latter is the best-of-breed rationale, i.e., the notion that clients will shift their business to, and pay a premium for services from, firms with the deepest expertise (manifested in deeper benches, longer deal lists, more relevant litigation wins, and so forth); the more partners a firm has practicing within a particular area, the greater will be their visibility, the deeper will be their expertise, and the greater will be demand for their services, thus enabling higher price realization and above-normal profitability.

In principle, both these merger strategies are valid because clients differ in their preferences. Many clients with large and sophisticated in-house legal departments look to best-of-breed providers; others with smaller in-house departments or simpler needs lean toward the one-stop-shops; and still others look for elements of both, wanting both best-of-breed expertise while also containing the number of firms with which they work.

The data show that in practice ‘double down’ mergers tend to outperform their ‘complementary’ practice counterparts. From 2000 to 2020 there were 30 mergers between Am Law 200 firms. Of these, 16 had relatively high practice area overlap. Although there are many drivers of profitability, of these 16, 11 were ranked higher by profit per equity partner (PEP) five years after the combination than the larger firm was ranked pre-combination, i.e., 11 of 16, or 69%, were accretive. The comparable success rate for complementary practice area mergers is 54%, or 15 percentage points lower.

That said, complementary practice mergers comprise notable successes. Some are bolt-on acquisitions, e.g., Piper Rudnick’s 2002 acquisition of government affairs boutique Verner, Liipfert, Bernhard, McPherson and Hand, or Squire Sanders’ 2014 acquisition of Patton Boggs. But they also include mergers of comparably sized firms, e.g., the 2007 merger that created Locke Lord: Lock Liddell & Sapp specialized in commercial litigation, real estate, and energy; Lord Bissell & Brook was renowned for its insurance and reinsurance practices. Five years post-merger, the new entity’s PEP ranked eight places higher than the larger and more profitable Lock Liddell & Sapp did pre-merger. Restructuring the equity ranks played a key role: Locke Lord’s number of equity partners five years post-merger was 14% below

that of a proforma combination of the two firms pre-merger, and its rank by revenue per equity partner was 23 places higher.

So much good planning work has been done under the name of strategy that the critical concept of building practices where “great lawyers attract compelling clients and compelling clients attract great lawyers” gets overlooked.

When it comes to mergers, this pertains particularly to the ‘great lawyers’—particularly ‘great partners’—side of the dynamic. Most firms are held back from realizing their full potential less by the sectors, practices and geographies in which they compete (the ‘compelling client’ side of strategy) and more by allowing partners who don’t commit the hours, build great client relationships or operate at strong leverage to remain in the equity ranks (the ‘great partner’ side).

Restructuring the equity partner ranks can be an intractable challenge for a firm in steady state, with a large group of firm leaders believing they’ve made too little progress over too long a period of time. In contrast, a merger creates the opportunity to make quantum strides forward. Thus, while it would be ideal to find a merger partner with all the desired attributes (e.g., comparable profitability, overlapping practices, strong profit momentum, etc.) a combination focused on a resolute restructuring of the equity partner ranks can accelerate the achievement of a firm’s strategy and prove strongly accretive to PEP.

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