

## **The New World Order:**

### **A handful of firms are on the brink of global domination—but they didn't get there through get-big-quick schemes.**

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1. In 1989, *The American Lawyer* predicted the emergence of a tiny group of super-firms, which it dubbed the Am Law 20. Since then, the legal business has gone global at a then-unforeseen rate, and Am Law 200 firms are consolidating at a rapid clip. What are the characteristics of the firms that will come to dominate global legal practice?

I do buy the premise that 20 or so firms—let's call them the Global 20—will emerge as dominant worldwide players. Sorting out the firms that will be in that elite isn't easy, but it's likely that they will have some attributes in common. They certainly will have had a succession of leaders who shared a vision of global dominance with their partners. Such firms will be highly profitable, either through thoroughly dominating a lucrative niche practice, as Wachtell, Lipton, Rosen & Katz foes, or through building countercyclical finance and dispute resolution practices that are strong enough to support a global infrastructure. (Skadden, Arps, Slate, Meagher & Flom is an example of such a firm.) They also will probably have highly constricted equity partner ranks, with lawyer-to-equity-partner ratios that could run as high as 50 associates per equity partner.

It's a safe bet that at least two or three of the twenty-off slots will be filled by British firms. Four of the five Magic Circle firms have built global infrastructures of 25 or more offices—and those infrastructures continue to expand. Another eight to ten Global 20 firms will be top New York firms: At least three Wall Street firms have built significant international practices while maintaining top-tier net income per partner. One or two Global 20 firms will likely come from the Big Five accounting firms. Not only are they among the world's largest legal organizations, they dominate certain key markets, and each of them has hundreds of offices spread over a hundred countries, give or take a dozen.

That leaves five to nine slots. Among U.S. firms there are some obvious contenders—large firms that dominate crucial geographic markets and important practice areas. Such firms are Kirkland & Ellis; Brobeck, Phleger & Harrison; Latham & Watkins; and Gibson Dunn & Crutcher. All are highly profitable firms with tightly controlled equity partnership admission standards leading to favorable equity partner ratios.

Leaving aside for a moment the question of where Global 20 firms will have offices, what are the lessons in this for the scores of other American law firms aspiring to join the elite? The first is that size is important, because big firms can generate huge net operating incomes to invest in global infrastructure. Second, relatively small equity partner ranks allow for nimble decision making and a greater pool of earnings for investment. A third is the importance of building highly profitable core practice areas. There may be room for a couple of commodity-based corporate players in the Global 20, but they will have to be structured in a way that enables them to obtain top-tier profits from their commodity practices—and the business model for that has yet to emerge.

A larger question involves offices, both their number and their location. Many U.S. firms fixate on creating a local presence in an endless number of markets, both domestically and abroad. A look at the Global 20 contenders, though, shows that the emphasis should be on the quality of the practice (as measured by the client base and the type of work undertaken), not by the mere number of offices. Too many U.S. firms have networks of offices pocked with only marginally profitable offices. Sure some firms have begun closing their less profitable outposts lately, but for every Am Law 200 firm closing a nonperformer, there seem to be ten opening them. If firms are serious about contending for the elite, they are going to have to either eat crow and close their marginal offices or make them profitable quickly. Most firms say they are pursuing the latter strategy, but that's a delusion, because their already low profitability renders them impotent in attracting the kind of talent it takes to make the offices profitable. To contend, they need to put profitability growth ahead of growth in head count.

For foreign firms looking to expand into the U.S., there are probably only two must-have markets. The most obvious is New York: It is, after all, the world's biggest and most lucrative legal market. But I believe that non-U.S. firms will also need a presence in the San Francisco Bay Area, whether in Palo Alto or in downtown San Francisco. Despite the slowdown in the technology sector, the Bay Area has clearly emerged as the West Coast's business and financial center.

Merely maintaining token offices in these locations will not be enough. Conventional wisdom is that a firm needs 150 attorneys in a major market to achieve critical mass there. This means that Magic Circle firms looking to move into the United States still have to pull off mergers both in New York and on the West Coast. In their search for West Coast partners, they will be looking at firms a notch below those they have been examining as New York merger mates. This will probably cause them to reconsider their current strategy, which is to merge only with top-tier New York firms.

So where does that leave mid-tier U.S. firms seeking elite status? They should not construe this advice as a recommendation that they should move to New York pronto. The basic lesson is to open and build only where core practice areas can be highly profitable in short order. If an office doesn't achieve profitability on schedule, the firm should have the stomach to close it.

A final note: One has to wonder when the inexorable march of technology will affect expansion strategy. One would think that it will, and that someday soon, geography will matter less than technological brains and brawn.

2. We are a full-service intellectual property firm that now finds itself competing against big general practice firms for high-stakes IP litigation. How do we compete with such firms, many of which are known for their litigation practices?

I get this question from nearly every IP boutique I speak with. I also hear the converse, from general practice firms: To obtain high-stakes IP litigation must we develop full-service IP practices?

Clients seek out big general practice firms for two reasons. First, their name brand offers reassurance, or "insurance value," to the general counsel in a high-stakes dispute (and when the stakes are high, the general counsel is usually the decision maker). Second, general counsel have the perception that trial specialists can sell a case to a jury better than a lawyer with a technical background. On the other hand, full-service IP firms are perceived as offering deeper technical and legal expertise in the IP area.

To remain competitive with the big litigation shops, full-service IP firms are going to have to improve their profitability. That will allow them to ward off cherry-picking and continue to attract and retain top IP trial lawyers. Such firms have two mutually exclusive alternatives: to de-emphasize their prosecution practices, which typically are a drag on profitability, or to adjust their pricing and structures to enhance the profitability of prosecution work. Prosecution practices are somewhat like estate planning and immigration practices, in that the work is often done on a flat fee and must be pushed way down on the leverage ladder to be accomplished profitably. If full-service IP firms do not succeed in enhancing their prosecution practices, we will likely see those practices go the way of estate planning and immigration work: Either they will become small, noncore service practices in large firms or they will spin off and become highly leveraged prosecution boutiques.

What about the perceived lack of technical expertise at the big litigation shops? Although these firms sometimes go after high-end prosecution work, limited as it is, even that work will likely dilute their profitability and breed more conflicts of interest than it is worth. A better strategy may be to bring on a patent prosecution boutique as co-counsel, to the extent that technical is needed. This avoids the conflicts and the dilution, and allows the litigation firm to shop for the best expertise for the matter at hand.