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Firm Leader Forecast: Mostly Sunny

In annual survey, heads of Am Law 200 firms say they expect great things in 2007 -- but some anxiety lurks below the surface

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Count on the leaders of America's biggest law firms to lead the pep rally. The heads of Am Law 200 firms have been bullish about the year ahead since we began surveying them annually in 2003. This time, they are even more so: Ninety-one percent of respondents say they are optimistic about their firms' future. It's the first time more than 90 percent of those surveyed gave that response. Firm leaders also say they expect growth in most of the leading indicators -- firm revenues, profits per partner, billing rates and head count.

Enthusiasm about the economy as a whole was a little more muted. The largest group of respondents -- about 77 percent -- predict that the U.S. economy will grow only slightly in 2007, and 71 percent say they expect deal flow to increase only moderately.

In fact, in interviews, firm leaders expressed an undercurrent of doubt about how long the good times will last. "I'm bullish, but I'm also worried," admits one. Another says that the economy must be good because "most experts are positive," but he hedges his bets by adding that his firm is "also strong in restructuring, [so] we'll be fine" in a recession. A third passes the buck: "I'll let you call the guy at 1600 Pennsylvania Avenue."

We conducted the Leaders Survey in October, asking the heads of Am Law 200 firms to complete a confidential online questionnaire. This year we received 143 responses. Some highlights from the survey:

- Profits per partner will continue to rise. Sixty-six percent of respondents predicted that profits will grow by more than 5 percent; 31 percent say they will increase 5 percent or less; and the remaining 3 percent say they will be flat.
- Billing rates will increase. Fifty-three percent say rates will rise by more than 5 percent; 46 percent say they will increase by 5 percent or less. Only 2 percent say they'll keep rates steady.
- Litigation is expected to see the greatest revenue growth, according to 35 percent of the respondents. Corporate activity runs a close second -- 32 percent say that will be their area of greatest growth in 2007, followed by intellectual property, which was named by 20 percent.
- Mass tort and securities litigation will stay in the picture. Despite studies forecasting a decrease in these areas, 45 percent of respondents say that the practices have remained stable this past year, and 31 percent report an increase. Twenty-three percent report a decrease.
- Firm leaders are not fretting about associate retention. More than 67 percent say that associate retention is a minor problem or no problem at all.
- There is no collections slowdown. About 64 percent of respondents say clients are paying their bills at the same pace as the year before. Twenty-two percent say clients are paying more promptly, and 15 percent say they are taking longer to pay.
- Respondents' top disappointments include the failure to attract major lateral partners, a lack of collaboration among partners for

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Despite the mostly rosy outlook, firm leaders say that trying to figure out what clients want has become a major preoccupation. "The thing that haunts me the most is the future -- what clients need, how we can anticipate those needs, how we get talent," says Hughes Hubbard & Reed chair Candace Beinecke. Morgan, Lewis & Bockius chairman Francis Milone says that "more and more clients are interviewing more firms. I worry all the time whether clients are satisfied."

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Adding to the uncertainty is clients' increasing use of requests for proposals, in which firms must bid for jobs, rather than rest on their laurels (or perhaps a preexisting relationship). "We do more RFPs these days -- that's the world we're in," says Covington & Burling managing partner Stuart Stock. Another reason for worry: convergence -- the increasingly popular practice among clients of building short lists of approved outside counsel by winnowing down the number of outside firms they use.

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In such an atmosphere, some firms are being proactive about client retention.

Milone says Morgan Lewis now hires coaches to help lawyers "enhance their interpersonal skills." White & Case managing partner Duane Wall says his firm "ask[s] our clients all the time what they think of us. ... We run statistics; we have a client-calling program." Wall estimates that his partners and the firm's marketing team will have visited 50 to 60 clients by the end of 2006. "I've done six or seven myself," he says.

Nonetheless, that kind of approach is still the exception, not the rule. For all the griping about the competitive marketplace, most firms seem passive about client satisfaction. About 46 percent of respondents to our survey say they visited with five or fewer major clients in 2006; 8 percent didn't meet with any. (In 2005's survey, 48 percent of respondents said they visited with five or fewer clients, and 6 percent met with none.)

Nearly all of the Am Law 200 leaders we spoke with insisted that their firms are not threatened by the convergence movement. Marianne Short, managing partner-elect of Dorsey & Whitney, says that "convergence works for us, [because] we have very close relationships with our clients," who include Wal-Mart Stores Inc., Supervalu Inc. and UnitedHealth Group Inc. "We welcome convergence," says Kaye Scholer's Barry Willner, citing demand for the firm's intellectual property, product liability, antitrust, commercial litigation and private equity practices. Willner says that his 500-lawyer firm has nothing to fear from thousand-lawyer-plus shops: "We don't see clients going to megafirms," he says. "They are not going to firms based on size."

Despite the view that convergence is the other guy's problem, some Am Law 200 firms are trying new strategies to stay competitive. One method is to scrap the hourly fee structure. "Clients are looking for discounts and want a little skin here and there," says Short. "Flexibility is key." White & Case's Wall says that his firm is more willing than some of its clients on this issue: "Clients still believe in the hourly rate; they feel [it gives them] more control." Rather than agreeing to a fixed fee -- which Wall argues is more efficient and cost-effective for all concerned -- clients prefer getting a discount on the hourly billings, he says. So for now, Wall says, discounts are "very common" -- from all firms.

Some firms peg their fees to the outcome of a litigation or transaction. "There's more risk-sharing between a law firm and the client," says Matthew Larrabee, the managing partner of Heller Ehrman. "Most Am Law 100 firms outside of Wall Street will do this kind of partnership-building with clients. This can be a huge advantage over the Wall Street firms."

Although firms may say they are on the cutting edge when it comes to fee arrangements, they're conservative about the bottom line. About 89 percent of respondents say that their firms will carry the same or less debt as the year before; only 11 percent plan on borrowing more.

Firms are also cautious about overseas expansion. Less than one quarter of respondents -- 22 percent -- say their firms are considering opening new offices abroad. Heads of such global firms as White & Case (36 offices) and Hogan & Hartson (23 offices) say they're maxed out on the international front. Hogan's managing partner, J. Warren Gorrell Jr., answers a definitive "no" to the question of new offices, and wouldn't say whether the firm will close existing offices, although he acknowledges that "Central Europe has been challenging for us." White & Case's Wall says, "We finished our geographic build-out." The firm closed offices in San Francisco and Ho Chi Minh City in 2006.

But one firm that's seriously looking into opening an office abroad is Houston's Bracewell & Giuliani, which competes against oil and energy firms that already have a substantial overseas presence. "There is so much capital" in the Persian Gulf, says managing partner Patrick Oxford. "We are very optimistic [about business there]." Despite what Oxford sees as exceptional opportunities in that region, he's not rushing in. "It's difficult to read about the strife [in the Middle East] and not be cautious about putting people there," he says. "I'd be lying if I said we didn't look at world events."

So does Hughes Hubbard's Beinecke. "I wonder about our economy, and where the world is going," she says. "But maybe that's just me."

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