

A Walker Clark Point Paper

Trends and Strategies in North American Specialty Legal Markets: 2004–2006

This paper summarizes several important trends that have emerged since the late 1990s, and which are likely to continue to shape the specialty legal markets in North America during the next three to five years.

Some of these trends and strategies may appear to be mutually inconsistent or even contradictory. Such is the nature of a mature, rapidly changing market for professional services. Each of these points should therefore be considered in the context of the specific characteristics of each law firm, its clients, its people and their talents, its competitors, and its unique workplace culture.

characteristics of a specialty market

The term *specialty legal market* describes a market for legal services that has several defining characteristics, each of which differentiates it from a more generalized market for the same or similar services.

First of all, a specialty legal market is defined by a relatively narrow range of professional services. These service lines are usually much more specialized than those offered by “full-service” firms with the same general practice areas. For example: tax litigation versus taxation; technology transfers versus trade regulation; infrastructure privatization finance versus project finance.

Second, the most successful specialty law firms tend to further define their markets in terms of a relatively narrow sector of potential clients. Although specialty law firms frequently welcome clients from outside these narrowly defined client base sectors, they concentrate all or substantially all of their investment in marketing, ongoing business development, and internal expertise and capabilities on their target client base.

Trends and strategies to watch

Here are trends that Walker Clark consultants have observed in or pertaining to specialty law firms that have demonstrated consistently strong financial performance and business success in the late 1990s and into the 2001–2003 recession in North America.

The longer term performance of these firms strongly suggest that each of these trends and strategies will continue through 2006, at least, regardless of the length, strength, or depth of any recovery or continued deterioration in the U.S. economy during that period.

1. Countercyclic and counterintuitive responses to economic events

The relative long-term economic stability of specialty legal markets suggests that well-managed specialty law firms produce business performance that is substantially, although not perfectly, insulated from business cycles and performance variation of the economy as a whole. The extent of such insulation varies among practice specialties and target client bases.

Why can the most successful specialty firms absorb the impact of general business cycles and produce consistent business results? Three factors are usually present.

First, the smaller specialty law firms often attain much higher levels of group development than do practice groups in larger firms. This produces higher levels of goal achievement and greater overall effectiveness, efficiency, and profitability in the design and delivery of legal services.

The second factor that is usually present is a balanced offering of diversified, highly valued, legal services. In good times or bad, the firm has a ready market for a range of well-paid services to financially stable clients that is sufficient to ensure strong business performance for the firm.

The third factor is the firm's tolerance for risk and ambiguity. The strategies that are most likely to produce the greatest business benefit to specialty law firms often run contrary to the assumed "best practices" in other general law firms or other professional service businesses. Successful specialty law firms are good at evaluating opportunities, identifying and managing risks, and understanding the factors that are critical to success. They see opportunities and strategies that other firms often assume to be impossible.

2. Leverage becoming less important to profitability

Clients engage specialty law firms to obtain unquestionably high professional quality from experienced, expert lawyers. A high ratio of associates to partners (*i.e.*, leverage) does not have as strong a positive impact on overall law firm profitability in specialty firms as in general practice firms or firms that provide low-margin high-volume services such as insured tort defense.

In fact, as managers in some smaller firms occasionally point out, high associate-to-partner ratios may actually have a negative impact on profitability in specialty firms. In our experience, however, this is an extreme case, usually related to low

levels of associate training, inadequate quality assurance systems, and low productivity.

Leverage may not be as strong a factor on overall profitability in specialty firms as in general practice firms; but it is nonetheless important. A properly leveraged specialty firm, with adequate quality assurance systems to manage delegated legal work, can free at least 10% to 15% of partner time for higher-value legal work and business development activities. The three most important components successful delegation strategies for most specialty law firms are:

1. Realize that adequate leverage will usually be achieved through somewhat smaller associate-to-partner ratios than would be required in general practice firms.
2. Invest significantly greater amounts of time, attention, and resources that would be required in general practice firms for professional development and training in two areas: (1) partner leadership and business skills, especially in the management of delegated legal work; and (2) technical knowledge and professional skills development for associates.
3. Pay close attention to quality assurance systems and procedures to maintain high levels of client confidence.

3. Growing recognition of the competitive advantages of smaller firms

Smaller law firms, with a high concentration of legal expertise and greater perceived attention and responsiveness to individual client needs, are able to compete very effectively against much larger, general practice law firms. They can demonstrate competitive advantages in a number of areas, any of which can be decisive depending on the nature of the specialized services the client requires. For example:

Price

Management of costs and disbursements

Access to partner-level expertise and experience

Quality of service delivery

Subject-matter expertise

Industry knowledge

Ability to achieve high degrees of customization of legal services and products to meet individual client needs and expectations

The critical importance of managed growth

The most important long-term challenge for most specialty law firms is to be able to continue to meet client demand. The complexity and priority of this challenge increases proportionately to the firm's success at building its reputation in the market. Clients want more and the firm must have the internal expertise and delivery capabilities necessary to surpass client expectations at the same or higher levels of quality than before. Otherwise, the specialty law firm risks losing business to larger, general practice firms that do not have the same high levels of reputation and expertise, but do have enough people to get the work done when the client needs it.

The fastest growth strategies, *i.e.*, merger or acquisition, have also proven to be the riskiest for specialty law firms. Increasingly, specialty law firms are shifting their strategic focus away from being an attractive candidate for merger or acquisition, and toward strengthening their service delivery capabilities and market position through well-planned, carefully monitored internal growth. As a result the most successful managed growth strategies for specialty law firms more typically include:

- Planned one-by-one lateral acquisitions of partners or potential partners over a period of one to three years

- Acquisition of highly specialized practice groups from larger firms

- Close strategic alliances with practitioners and firms providing related specialty services to the same target clients

- Investment in professional development of associates to permit more delegation of higher-value legal work, while preserving client confidence in the quality of the work

- Long-term client relationships based on understanding of the client's needs and expectations

Research conducted by Walker Clark, LLC, and other organizations confirm that smaller specialty law firms typically enjoy a better reputation for understanding the client's individual needs and expectations in each matter and in the overall lawyer-client relationship.

Most successful specialty law firms have built their practices on a relatively small but stable foundation of long-term clients. These clients are a strong, but often overlooked, marketing force.

reliance on long-term referral relationships

A substantial portion of the fees received by successful specialty law firms come from referrals from other law firms and other professional service providers such as accountants, architects, and engineers. Although highly beneficial to long-

term financial performance, these relationships can also constrict a firm's options with respect to otherwise appealing opportunities for a merger or strategic alliance. This limiting effect is much greater with specialty firms than with general practice firms.

Leadership in the legal and business communities

Successful specialty law firms usually cast a larger-than-life shadow among other lawyers and business leaders in their market. Carefully designed and targeted activities -- such as active participation in professional and business organizations and sponsoring seminars on complex or more advanced legal topics -- correlate to significantly higher awareness of the firm's services and capabilities, as well as to more favorable perceptions of the firm's expertise.

Walker Clark, LLC, works with small and midsize specialty law firms worldwide to develop and implement strategies such as those discussed in this paper. For more information, contact Norman Clark by e-mail at nkclark@walkerclark.com or by telephone at 1.239.466.8370.