Law Firm Rate Increases for 2010

Okay, I have to vent a bit: I just got a call from an NLJ reporter asking about how much firms will be raising rates in 2010 and whether I was surprised that rates only went up about 2% overall in 2009 - that's so low compared to previous years, the reporter said. For those of you who know me, just try for a minute to imagine me speechless. Okay, it didn't last. And now you're the beneficiaries of the rant that follows.

I understand that most firms employ the business model of selling rates and hours, and thus the only way to make more money for them is to raise rates or increase hours. Since many are still struggling to secure the hours (even tho the billable "expectations" have not decreased), they'll seek to raise rates for the lawyers who remain working. But are they really that tone deaf? Do they really believe that the path to profitability requires increasing rates in 2010? Do they really not see not only the imperative (for their own survival and for longer-term-profit sustainability), as well as the opportunity, to start moving toward another business model of valuing their legal services based on the worth of what they sell and the efficiency with which they provide their services?

While my info is anecdotal, everything I have heard from firms I'm talking to as a result of the ACC Value Challenge and from clients who have been whacking back their budgets is that a firm would have to be crazy to announce any kind of increase right now. Do they believe that the markets rebounding means that they'll be able to return to the "Golden Age of Profitability" that all the consultants use to describe the last 10 years?

Sure, many firms will engage in a "paper" exercise of increasing rates so that when they were asked to provide a discount they will be at least somewhat ahead of the game, but surely, they can't really believe there will be an resulting rise in the amount of money that clients will pay for work overall?

Here's the scenario: the CLO goes down the hall to the CFO's budget meeting for 2010. The CFO says to all the leaders present: "It's been a hard year for us, and you've all done a great job in driving down costs to keep this company afloat. I'd like to especially recognize the law department, which after years of uncontrollable cost-overruns and a 75% increase in legal services costs to the company over the last ten years (a stat he has retrieved from the Conference Board), succeeded in bringing home a 25% decrease in legal costs in 2009. We knew you could do it! Congratulations and Welcome to the team! You've done so well, that this year, we're only looking for another 10% reduction in your budget while everyone else will have to cut 15%!"

What will the CLO say? Is her answer is going to be: "Well, actually folks, our firms were so great about discounting their fees last year, that we wanted to repay them for their investment in us during our hardest moment, and so we're looking for our budget to be back up to what it was in 2008, plus a 5% increase for the firms for 2010! Those poor guys saw a decrease in their profit per partner last year from 1.8 million per partner to about 1.6 mil after they fired 1/3 of their support staff, de-equitized our best servicing partners, and deferred the starting date for their incoming class of 38 new associates."

If you're the CLO who responds like that, it's you who'll be looking for a new way to fill your hours this coming year.

Any firm watching the market and their clients this last year should have engaged in some kind of cost-cutting or efficiency exercise that did more than cut dead weight or marginalize those who actually do the work, but that fundamentally addressed inefficiencies in the firm's business model. And that, hard as it will be to take, begins the process of re-setting the compensation expectations of some of their highest paid lawyers. Many of the larger firms are simply going to have to tell people at the top that their take-home expectations are simply going to have to change IF THE FIRM IS TO REMAIN PROFITABLE. Lawyer comp in many firms is not realistic, not supportable, and has to go down because the bubble has burst. So it's time for them to ante up to the discussion of what it's all about - will they choose the firm's sustainable path to shared profitability, or an attribution system that often puts individual partner comp ahead of the firm's best interests. Either all boats will rise, or all may sink.

The idea that firms should look to maintain their stature as a top player by raising their prices is based on old thinking. Value firms will proudly strut their increasing portfolio and profitability by pointing to an increase in client satisfaction with the value of their services, or an improvement in their efficiency, or a reduction of their costs because of an innovative new way they're working in this environment; raising rates to "assure" profitability is a failing strategy. As this becomes increasingly apparent in the coming months, I hope that more firms will join the ranks of those who've already begun to think about new ways to value their services that don't rely on rate x hours at all.

Get with the program, law firms: just because many of you sell an overpriced inventory of hours doesn't mean that that's what clients are going to purchase in the new paradigm, and raising rates is going to make your pitch to sell all those hours even more unattractive. Further, it will evidence your lack of alignment with the clients you serve. And hand your current clients the permission slip to visit other firms that will provide the services you've always provided, but for less, or better, or for a more predictable cost.

Perhaps the silver lining for firms that haven't figured this out in the short term is that clients are increasingly uninterested in rates at all; they are increasingly focused on the all-in cost of the work. Rates are becoming irrelevant to many clients who say: "I really don't care what your rates are - that's not my problem; this is what I'm willing to pay for the work, since this is what it's worth, and you figure it out from there."

But the merry-go-round of "firms-raise-rates-so-clients-will-demand-discounts" is no way to sustainable profitability or support strong, institutionalized, trusted relationships over the long-term. Hopefully, 2010 will be the year NOT of the rate increase, but of the movement of firms toward other options for valuing the services they provide, while there's still an opportunity to experiment with new models and adjust to the new order without as great a penalty - indeed, with a distinct upside for early adapters. The window of this opportunity will begin to close soon as some folks get it and others don't: those who haven't been moving to accommodate new client expectations will find themselves keeping company with their newly hiked rate structures on the sidelines. Seated right next to -- as Mike Dillon so aptly put it – the Mastodons [http://blogs.sun.com/dillon/entry/the_way_of_the_mastodon].

Poor NLJ reporter: I think she was hoping for a one-line, pithy comment. But what firms raising their rates (without any corresponding showing of increased value in the service they're providing) need is an earful. And the same goes for clients who enable and reward such behavior by paying higher rates as if they have no other choice.