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Right-sizing your merged law firm

A merger provides a host of opportunities to right-size. Some arise directly from the merger itself. Others will be realised because 'all bets are off' in a newly-merged firm, providing a window to implement efficiencies that were previously denied.

Right-sizing is generally assumed to mean moves to reduce costs and therefore increase operational efficiency in order to improve profitability. However, right-sizing should also consider the introduction of new structures, modern practices and innovative approaches. Through this combination of sustainable structural and operational efficiency improvements, net profitability can be boosted further.

Staffing costs

Headcount reduction is a necessary part of any merger process. Every opportunity must be taken to eliminate unnecessary duplication of roles and to ensure production capacity is aligned with future revenue expectations. Given the proportion of fixed overheads represented by a traditional law firm's salary bill and the ability to shift these quickly following a merger, this is the area in which the most impact can be made most quickly.

It may also be where more flexible staffing arrangements can be introduced to reduce fixed costs even further. It seems inevitable that the market more generally will move (either through desire or economic pressure) to a staffing model which builds a temporary and flexible workforce around a permanent and stable core. A merger allows this process to be accelerated.

Paradoxically, HR reshaping is also an area in which right-sizing may lead to an increase in average salaries paid to personnel in equivalent positions; there will always be a mismatch between the pay scales at each firm.

Converging salaries will be necessary over the integration period and there will generally be a gravitational pull towards the higher position in each case. While some of this will be ameliorated by headcount reductions, it is still likely that the average cost per retained individual will be higher than the combined average pre-merger. These people need to be more productive in order to make the economic model work.

Premises costs

The market is replete with stories of potential mergers that had a strong long-term strategic logic but were scuppered by immovable property commitments. While regrettable, this is not as concerning as mergers that appear to proceed purely on the basis of an excellent property outcome, even though the strategic logic of the union is flimsy. Premises are a key component of the cost base and, as a corollary, an area in which substantial opportunities for right-sizing may be sought.

A merger should be an opportunity to look at premises strategy with a fresh perspective, introducing remote working where appropriate, along with hot-desking and other modern practices (supported of course by IT infrastructure and training) that allow for optimal real estate commitments.

Supplier costs

It is also important to reshape the supplier base, taking every opportunity to consolidate and negotiate more favourable terms for the enlarged business. For firms without the expertise to undertake such large-scale exercises in-house, the services of freelance procurement professionals are available. They will ensure that a rigorous process is followed and that the best possible terms and service level agreements are secured across the supplier base.

Insurance costs

Insurance at all levels is an area in which significant savings can be made. Given the magnitude of the numbers at play, even a modest percentage change will translate into meaningful sums.

Client response

On the negative side of the equation, savvy clients may also see the merger as an opportunity to right-size their law firm supplier relationships. This will be especially true when the antecedent firms both acted for the same client – not an uncommon occurrence given the predominantly consolidatory mergers that we are witnessing.

In the same way that salaries will tend to drift upwards towards the higher end of a particular band, in the case of shared clients, fee rates will tend to migrate in the other direction.

Other clients may seek to use the uncertainty and nervousness that follows a merger to renegotiate more advantageous terms, using the implied threat of re-tender or the increased interest of competitors seeking to capitalise on any instability as a way to improve their own commercial position.

Incredibly, a merged firm may even cannibalise its own revenue streams through cross-selling activities and pricing strategies that are neither well thought through nor based on sound arithmetic.

A holistic approach

Moves to reduce costs or improve efficiency need to be thought of in a holistic way, since each will have knock-on effects (perhaps unanticipated) on other parts of the business. By taking this rounded approach, a firm gives itself the best opportunity of achieving both reductions in overheads and sustainable improvements in profitability.

Just as importantly, success also breeds a changed mindset and a belief that seeking out better and more innovative ways of doing business is the best way to ensure future success. mp

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