

LEGAL EXECUTIVE
INSTITUTE



2019

State of U.S.
Small Law Firms

“There are risks and costs to action. But they are far less than the long-range risks of comfortable inaction.”

— John F. Kennedy

The words of our 35th president serve as a solid reminder that even choosing the status quo carries with it costs and risks.

Lack of meaningful action can be due to several possible causes: lack of recognition of the problem, lack of knowledge of possible solutions, analysis paralysis, or what is sometimes called “the status quo barrier.”

For today’s smaller law firms, there have been efforts on the part of some firms to move toward possible solutions. But far too many firms remain fixed on the status quo. Why?

It is likely not due to a lack of recognition that there is a problem. This report, the latest edition of the Thomson Reuters State of U.S. Small Law Firms study,¹ highlights that for the third year in a row, the majority of firms surveyed recognize that they face a host of challenges, many of them significant challenges. But in a more disturbing trend, the study also reveals precious few small law firms taking concrete steps to address the challenges they admit they face. In 2019, our rallying cry would be for small law firms to turn that awareness into action.

Small Law Firms Recognize They Have Problems to Confront

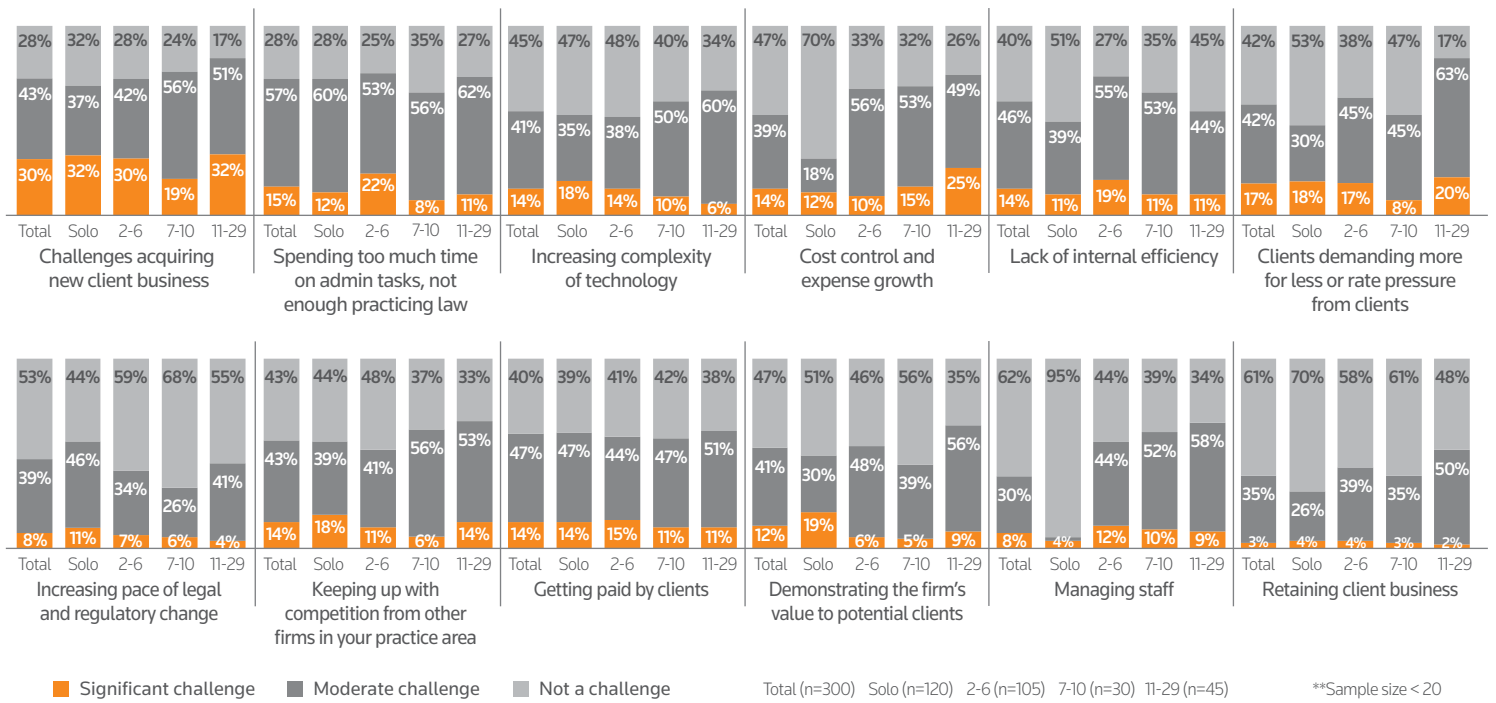
Small law firms realize that they face a significant number of unique challenges.

Chief among these challenges are problems acquiring new client business. Every small law firm segment surveyed, regardless of the number of lawyers, identified this as their primary “significant challenge.” Whether a solo attorney, or the managing partner of a 25-lawyer firm, worries about where your next client will come from likely causes some consternation. Without a steady stream of new business, there wouldn’t be much point in having a firm.

But the worries don’t stop there. A large percentage, if not a majority of respondents in each firm-size classification expressed at least moderate concern about spending too much time on administrative tasks, controlling costs, keeping abreast of new tech, a lack of internal efficiency, keeping up with the competition, getting paid by their clients, and clients demanding “more for less” or pushing back on firm rates.

¹ All findings are derived from an online survey of 300 respondents in law firms from solo attorneys up to 29 lawyers in the firm. The survey was conducted in September and October 2018.

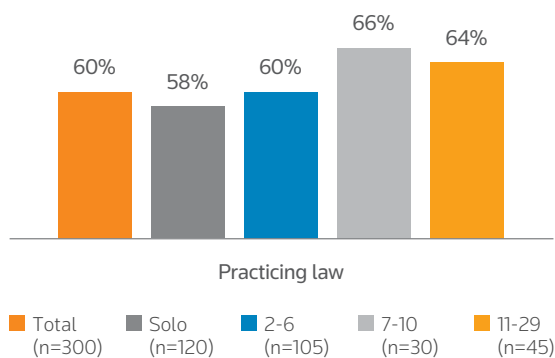
Figure 1 – Firm Challenges 2018



Oh Where Does the Time Go

Another substantial challenge, separate and apart from the plethora already discussed, is how a practicing lawyer allocates his or her time between the actual practice of law and everything it takes to keep the practice running.

Figure 2 – Time Allotment



For most lawyers, nearly 40 percent of their day goes into activities other than the actual practice of law. Much of this is time for which the lawyer will never be paid.

That means that a lawyer working a 10-hour day will only have, at best, six hours a day for which they might eventually get paid. And most lawyers will tell you that it is highly unlikely that they will actually collect money from clients for each of those potentially billable hours. By the time the we account for leakage due to poor timekeeping practices, discounts and write-downs offered by the lawyer to address perceived client concerns, and client pushback on the final invoice, the proportion of each working day for which a lawyer will ultimately be paid dwindles quickly.

So with nearly 40 percent of a lawyer’s time disappearing to tasks other than practicing law, what is taking up so much time?

In 2018, Thomson Reuters introduced the “Modern Practice” as a framework to represent all the different functions a modern law firm must undertake to run a successful business. Those activities grouped under “Practice Law” represent those activities for which a lawyer might reasonably expect to be paid, and even there we find some exceptions.

Figure 3 – What Activities Are Taking Up Your Time?

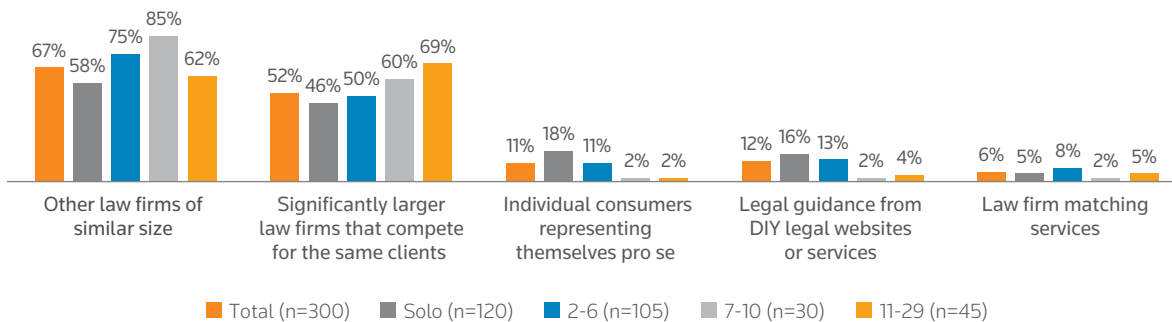
The Modern Practice			
Attract & Retain Clients	Practice Law	Run Your Firm	Manage Finances
Business development	Pre-case consultation & due diligence	Client management	Fee negotiation & structure
Pitch / proposal	Drafting & research	Billing	Write-downs & fee adjustments
Client service	Matter management	Collections	Matter budget
Retention	Discovery & trial prep	Attorney & staff management	Financial metrics & reporting
Referrals	Negotiation, ADR & settlement	Technology & infrastructure	

In short, lawyers in today’s law firms have to wear a lot of hats. This division of attention is the cost of doing business, and it cannot be said that lawyers are unaware of the impacts of these costs. But as we have said before, that awareness must lead to action.

Yet Another Challenge

As if the deck wasn’t stacked heavily enough against small law firms, we must also consider increasing pressure from their competition.

Figure 4 – Sources of Competition



Other law firms of similar size have perpetually been the prime source of perceived competition among respondents to the State of U.S. Small Law Firms survey. As we’ve previously seen, some 53 percent of small firms report keeping up with competition from other firms in their practices areas presents a challenge. And small law firms are increasingly being pressured by larger firms looking to steal client business away to stabilize what has been otherwise lackluster overall demand growth for many midsize and larger firms for the past couple years.

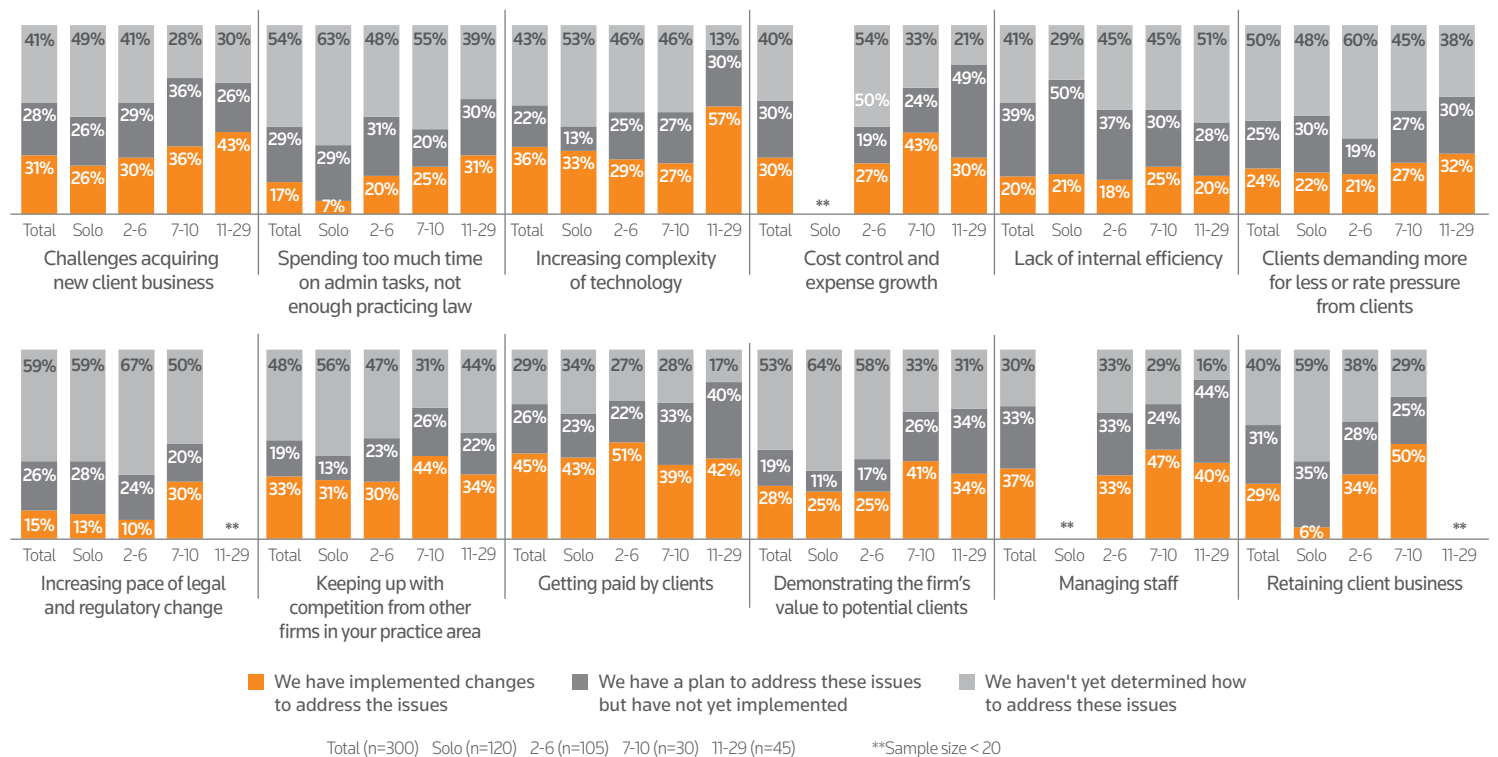
It is surprising to us, though, that individual consumers representing themselves pro se and legal DIY websites are so infrequently identified as sources of competition. In a Thomson Reuters study of how consumers search for legal help, only about six in 10 potential clients even contact a legal professional.² That means 40 percent of a lawyer’s potential client base never even seeks out the lawyer’s help. Instead, they are opting for the pro se or DIY route. That’s a substantial portion of the potential market that is gone before the lawyer ever has a chance.

In a perhaps surprising turn, small law firms may pose more of a competitive threat to larger firms than they previously believed. According to research from the Thomson Reuters Legal Executive Institute, in 2018, of litigation matters involving the Fortune 50, fully 30% of all matters were handled by law firms with between two and 15 lawyers. That this volume of work from such large companies is being handled by small law firms is a bit remarkable. And it shows that small law firms not only get pressure from larger firms, but they’re capable of exerting it as well.

So Where’s The Action?

It cannot be said that no one is stepping up to address the challenges faced by today’s small law firms. But it is also true that not nearly as many firms have taken steps to address challenges as those who recognize challenges exist.

Figure 5 – Addressing Challenges



For example, across the entire study, 73 percent of small law firms said they faced a challenge acquiring new client business. But only 31 percent said they have implemented changes to address the issue. Regardless of firm size or the nature of the challenge to be confronted, there were only two examples found where better than half of respondents said they’d taken steps to address the challenge; firms of between 11 and 29 lawyers who have taken steps to address the increasing complexity of technology, and firms of two to six lawyers who have taken steps to get paid.

A Persistent Lack of Action

This lack of action has been a trend we’ve noticed each year we’ve conducted this study. For example, in the 2017 version of this study, 71 percent of firms who said acquiring new business was a challenge left that challenge unaddressed. This year, that number sits at 69 percent, a statistically insignificant difference, despite the fact that 34 percent of respondents last year said they had a plan to address the issue, but hadn’t yet implemented that plan.

If they had a plan ready to go, and had finally acted on it, why are we not seeing an improvement in the number of firms reporting having implemented changes?

Now it must be pointed out that we are not surveying the same firms year after year to monitor progress, so it would be unfair to surmise that none of the firms who said they had a plan had put that plan into place.

But it is equally true that in the three years we’ve conducted this study, we’ve consistently seen the same issues identified as the greatest challenges for small law firms, with relatively underwhelming proportions of firms taking proactive steps to address their challenges.

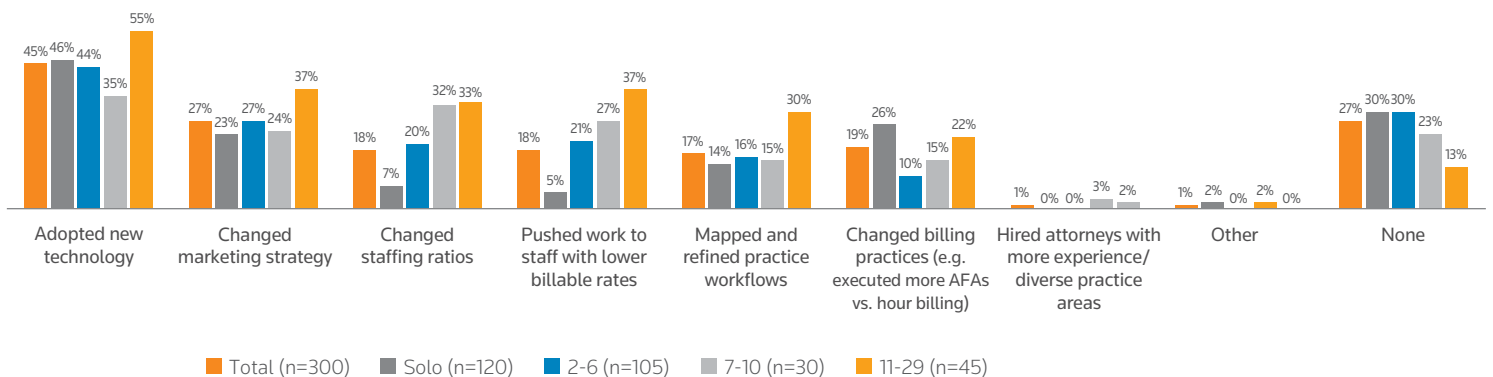
Rather than dwelling on the failure to act, though, it is far more productive to shift focus to what firms can do to address these challenges.

Small law firms clearly recognize the tumultuous landscape before them. Therefore the lack of action is owing to something other than failing to recognize the problem. For those firms who may be stuck in the throes of “analysis paralysis,” who are perhaps too comfortable in their status quo, or who are simply looking for precedents to follow, the study offers plenty of guidance as to what others have done.

The Times They Are A-Changin’

Technology is often the first place many firms are looking as they reexamine their businesses, regardless of the size of the firm.

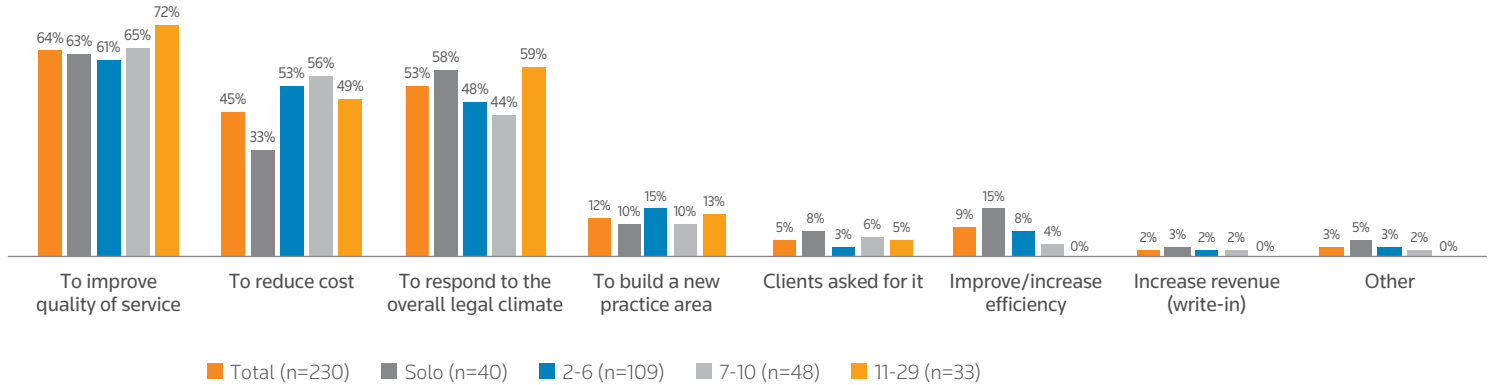
Figure 6 – Firm Changes



This may seem a bit incongruous given that every segment of small law firm saw a majority of respondents identifying increasing complexity of technology as a challenge. But it is, perhaps, viewed as a necessary evil. Technology lies near the heart of nearly any solution to almost every problem in today’s business environment. It is, therefore, encouraging to see so many firms willing to adopt new technology even in the face of concerns over its complexity.

Similarly, it is encouraging to see nearly a quarter or better of each segment of small law firms adapting their marketing strategy. True, if as many firms were acting on their concerns about acquiring new business as have expressed such concerns, this number would be much higher. Nevertheless, any action is better than none at all.

Figure 7 – Reasons for Major Changes



The reasons behind making these changes also show a focus on trying to address recognized challenges. By far, the most popular reason for making change was to improve quality of service. If the key challenge law firms face is acquiring new business, it does them no good to produce a product of inferior quality. The quality of legal work in today's market is essentially table stakes. It is assumed lawyers can produce quality work. But if your competition is investing in improving their quality, the quality of the product you produce may suffer in comparison if you do nothing.

Of note, very few firms said they were making changes because their clients asked for it. Clients do not tend to ask their law firms to change. Instead, they vote with their feet and their dollars. It is important that law firms recognize this and seek to proactively make changes that will better serve their clients without specifically being asked.

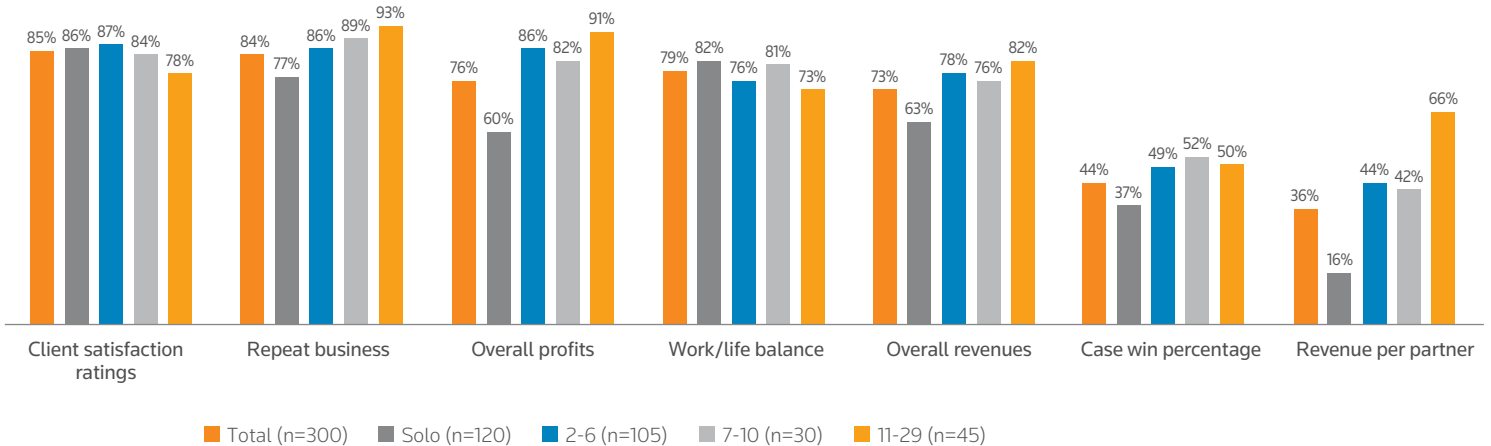
Also notable is the relatively low number of firms who said they were making changes to improve efficiency. Among solo attorneys, 15 percent said this was a motivating reason behind making a change. But for most firms, this was not among the top two reasons for making a shift. This could be because other reasons like improving quality of service or responding to the overall climate took precedence, and not because gaining efficiency is unimportant. But we must also recall that, at best, 25 percent of small law firms had actually implemented changes to make themselves more efficient, despite around 60 percent of firms recognizing that a lack of internal efficiency poses a challenge.

For firms who struggle to generate new business, or are experiencing client pressure around rates, an improvement in efficiency can produce a boost to profit margin, and thereby, boost the lawyer's take-home pay. Indeed, a large proportion of small law firms are paying attention to profit as a key metric, a trend which has stayed strong among small law firms.

Defining and Measuring Success

Small law firms look to a wide variety of factors as they evaluate their success.

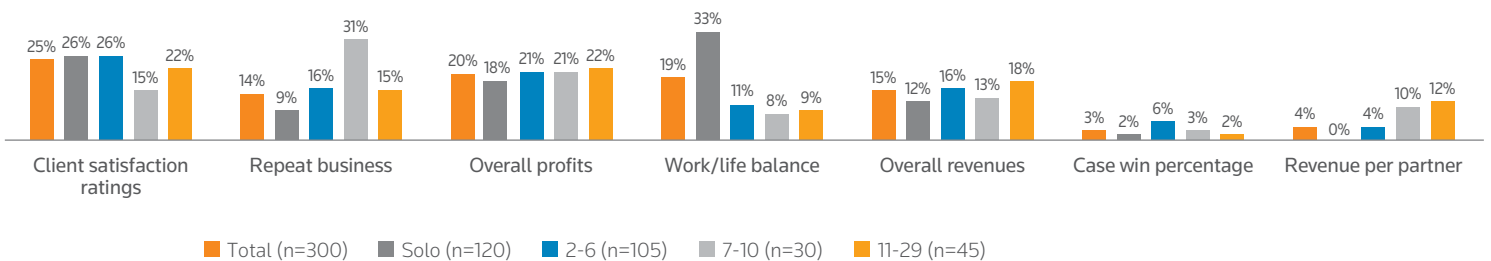
Figure 8 – Measures of Success



Notable here is that more firms look to overall profits as a part of their definition than overall revenues. The same holds true as firms identify their primary definition of success as a firm. But the importance firms place on client satisfaction ratings, repeat business and, particularly among solo lawyers, work/life balance is also of note.

The factors small firms look to as their “primary” definition of success are also instructive.

Figure 9 – Primary Measures of Success



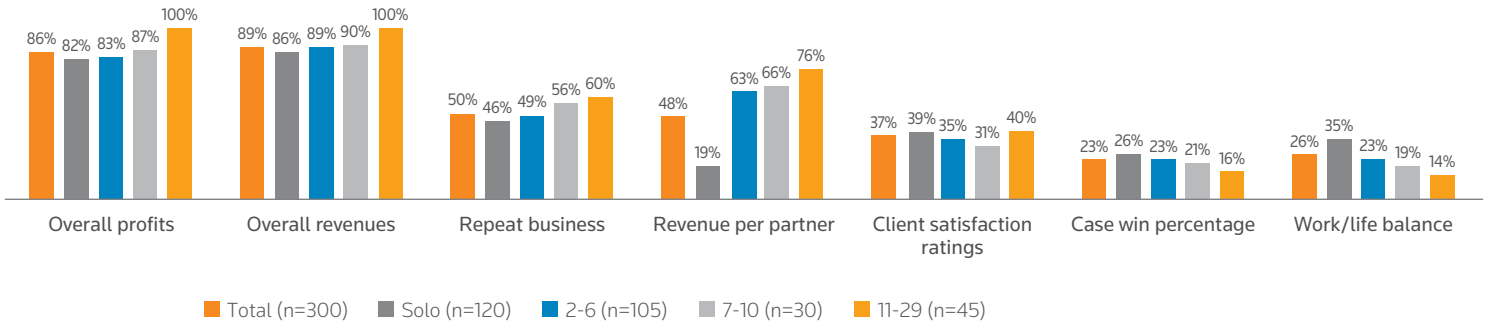
Among most small law firm segments, client satisfaction ratings and overall profits are in a near dead heat. Firms with between seven and 10 lawyers tended to place a bit more emphasis on repeat business. And among solos, they tended to be far more concerned with work/life balance than any of their peers.

These firms have identified what matters to them in terms of determining the success of their practice. For those firms struggling with how to move from awareness to action, an understanding of how they define what they want to achieve may serve as a useful starting point.

Measuring What Matters

What is a bit puzzling, though, is the seeming disconnect between what some firms said matters to them, and what they measure.

Figure 10 – Metric Tracking



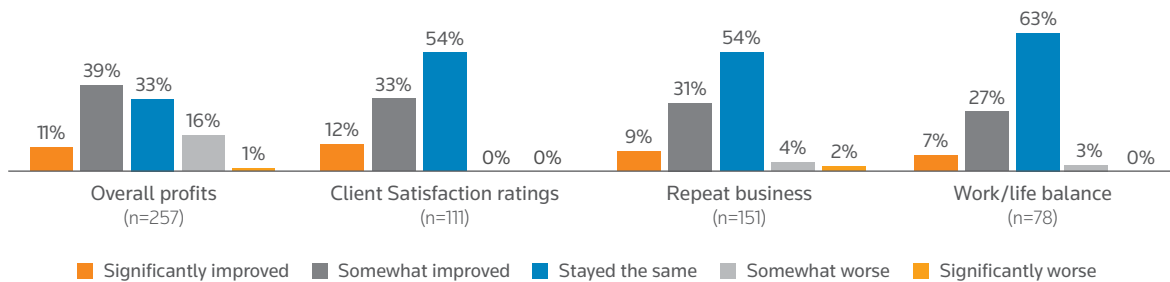
You'll recall, nearly 80 percent or better of every segment of small law firms said client satisfaction ratings were at least a part of how they define success. And around a quarter of almost every segment said it was the "primary" way they define success. If this is the case, though, why are 40 percent or fewer of these firms actually tracking that metric?

The old cliché holds that you can't manage what you don't measure. But it is equally true that you should measure what matters to you.

And in this case, measuring makes a difference.

Among those firms who said they measure their client satisfaction ratings, none reported a decline in that metric compared to 12 months before. The same holds true for the other top primary definitions of success: If a firm measured that metric, they were far more likely to see those metrics improve than decline.

Figure 11 – Metric Changes

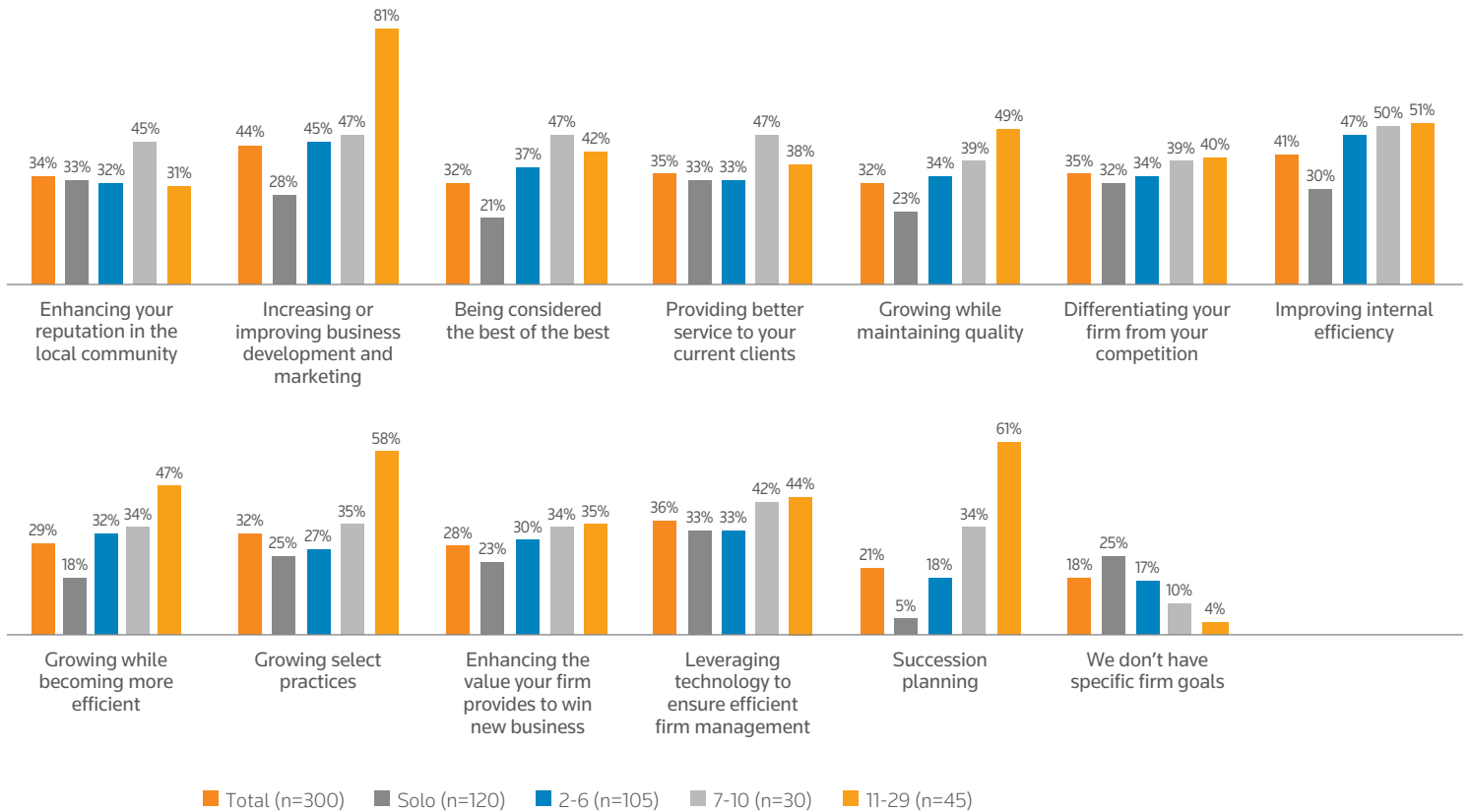


Some of these metrics, such as overall profits and repeat business are subject to external influences which will never be fully under the firm's control. But the fact remains that those firms who measured these key metrics were far more likely to enjoy positive results.

The Importance of Setting a Goal

If you don't set a goal, how will you know when you've achieved it? Small law firms appear to be pursuing a wide number of goals, but there are some consistent themes.

Figure 12 – Goals and Priorities



First, for those firms with between 11 and 29 attorneys, a large majority have stated a goal of improving their marketing and business development. This is commendable. We should note that only 69 percent of these firms said that they had taken steps to address their challenges in acquiring new business, or have at least formulated a plan, but setting the goal is an important first step.

And other segments of the small law firm market also showed a strong level of desire to place a greater focus on their marketing. Coincident to this goal would also be a desire to enhance the firm's reputation, provide better service to clients, and enhance the value clients receive, all of which enjoy strong recognition as stated goals for small law firms of all sizes.

But we would be remiss if we didn't address the 25 percent of solo lawyers, 17 percent of firms between two and six lawyers, and 10 percent of firms with between seven and 10 lawyers who say they don't have specific firm goals. While their candor is commendable, such a response begs the question: so how are you going to prepare for the future?

While widely varied in their approach to the future business environment, each of these goals is forward looking in the sense that whichever ones a firm decides to pursue, the firm is trying to prepare for what the future may bring. Without specific goals, a firm is much more likely to rest on the status quo and be caught off guard as the business environment changes.

What's Driving Success?

Perhaps as important as understanding the goals small law firms are pursuing is understanding what they have done that has led to positive outcomes. After all, law firms are run by lawyers, and lawyers value few things more than precedent. So what factors have contributed to positive performance among law firms?

Overall, a focus on becoming more efficient led to positive outcomes for many small law firms. Forty-four percent of solo lawyers pointed to increased efficiency as an important factor in their performance in the past 12 months, along with an equal number of firms with between 11 and 29 attorneys. For firms with between two and six lawyers, 40 percent said this focus helped their performance, and for firms with seven to 10 lawyers, that number was 39 percent.

Figure 13 – Performance Factors

Positive Performance Factor	Solo	2-6 Lawyers	7-10 Lawyers	11-29 Lawyers
Focused on becoming more efficient	44%	43%	42%	57%
Increased client referrals	37	40	42	48
Invested in technology/infrastructure	33	35	40	45
Enhanced reputation	32	34	39	45
Grew relationships with existing clients	30	29	39	44

Although each segment has them in a slightly different order and to slightly varying degrees, there is surprising uniformity among the segments as to what is driving positive outcomes.

And when these firms were asked what was the single most important factor driving positive outcomes for each segment?

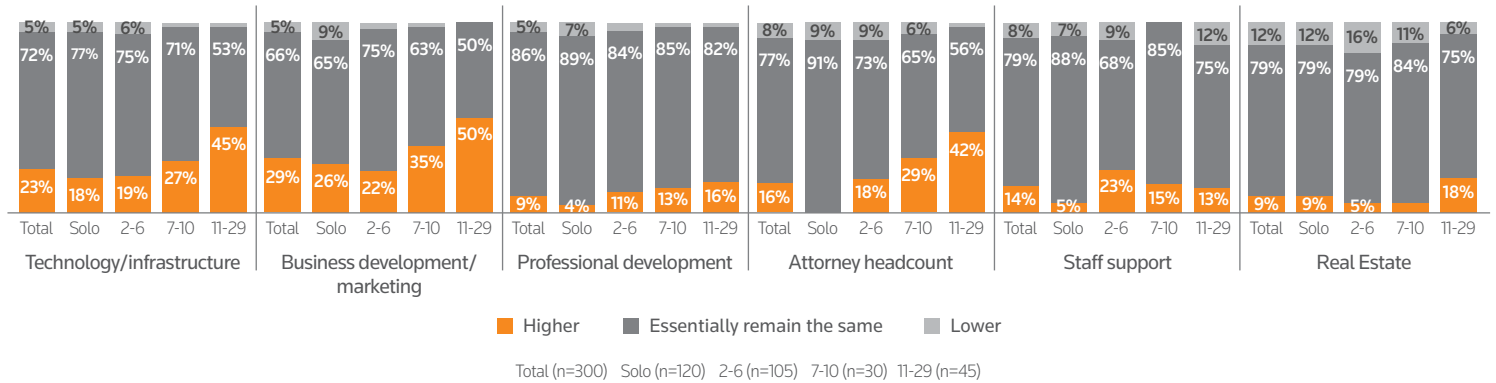
- **Solo:** Focus on becoming more efficient
- **2-6 lawyers:** Grew relationships with existing clients
- **7-10 lawyers:** Grew relationships with existing clients
- **11-29 lawyers:** Improved business development efforts

This is great news for small law firms. Acquiring new client business was routinely cited as the most significant challenge faced by these firms, and for nearly every segment, focusing on client relationships and business development was identified as the single most important factor driving positive outcomes. This focus has not fully abated the challenge, but such is the nature of the challenge: it will likely never fully subside. But firms have chosen to confront this head-on and it appears to be paying dividends for them.

Speaking of Paying Dividends...

For firms of any size, capital is a precious resource and must be spent wisely. How an organization chooses to invest its money is a pretty direct demonstration of its priorities.

Figure 14 – Investment areas



Here again we see a demonstrated focus on improving business development with the goal of confronting the challenge of acquiring new client business. Across the board, firms were nearly unanimous in their commitment to either hold their marketing spend constant or grow in this important area.

Running a close second was investment in technology and infrastructure. As we’ve discussed, a key component to serving clients is the ability to stay at the forefront of how services are delivered and to be constantly evaluating the service model to look for better ways to deliver outcomes for clients. This requires a focus on technology.

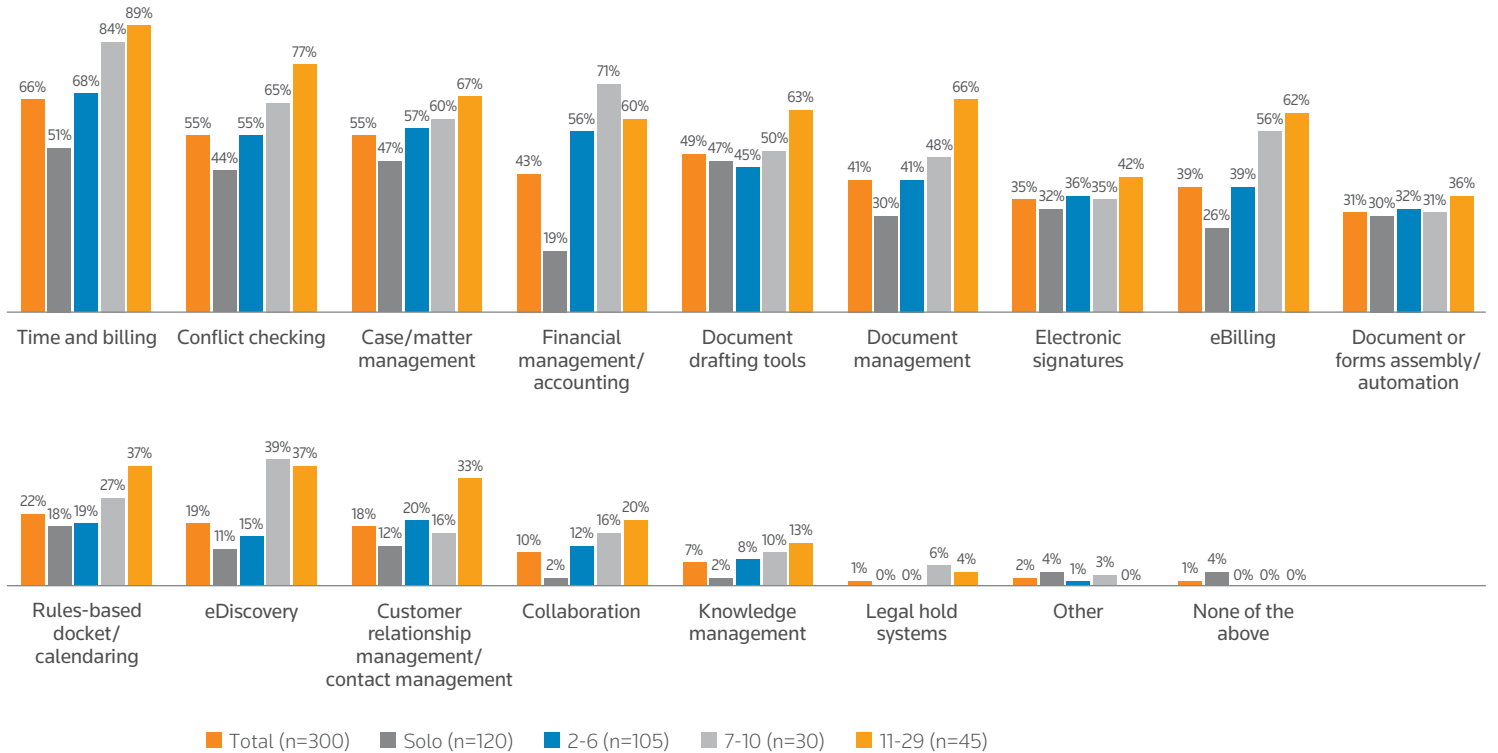
In fact, improvements in technology can help to address many of the areas small firms identified as presenting challenges. For firms struggling to acquire new business, improvements in tech can enable the firm to provide better, more efficient service, leaving existing clients with a better impression and making them more likely to return or refer. Struggles with administrative tasks can be obviated by automating processes where possible. Improved technology should almost be a guarantee of better efficiency because no one invests in better technology in the hopes of doing things worse. And in turn, this will ultimately allow the firm to deliver more for the client without having to incur additional costs, meeting the client’s desire for better value.

On the whole, it is quite encouraging to see technology and business development as the two areas most ripe for investment growth in the next 12 months.

So What Kind of Tech is Hot?

Saying that investment in technology is set to increase is informative, but technology is also a wide umbrella. It is helpful to understand what types of tech small law firms are using today, what they've adopted recently, and where they plan to grow in the near future.

Figure 15 – Technology Systems: Used

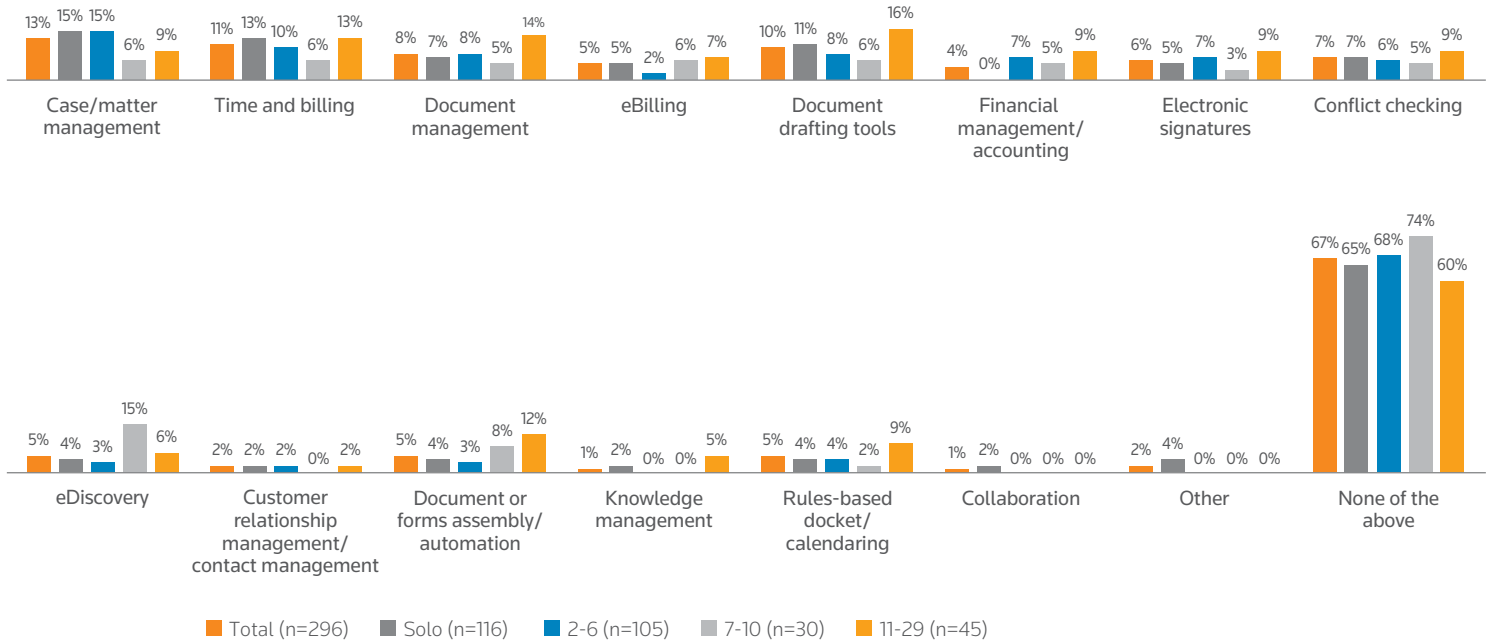


Across the board, staple technologies like time and billing, conflict checking, case/matter management, and financial/accounting tools are the most common. As we look at technologies like document drafting or document management tools, those become much less common in firms with fewer than 11 attorneys. But these are technologies that would go a long way to accomplishing some of the goals discussed above like improving internal efficiency and client service delivery.

Much of the time spent reviewing documents or correcting mistakes goes unbilled by attorneys. *Legal Executive Institute* research indicates that the average partner at a law firm may lose 32 hours or more every year to write-downs due simply to extra time spent correcting or revising an associate's work. Document management and drafting tools help to eliminate much of this time because associates can find better examples of previous work product and catch more of their mistakes before the partner even sees them.

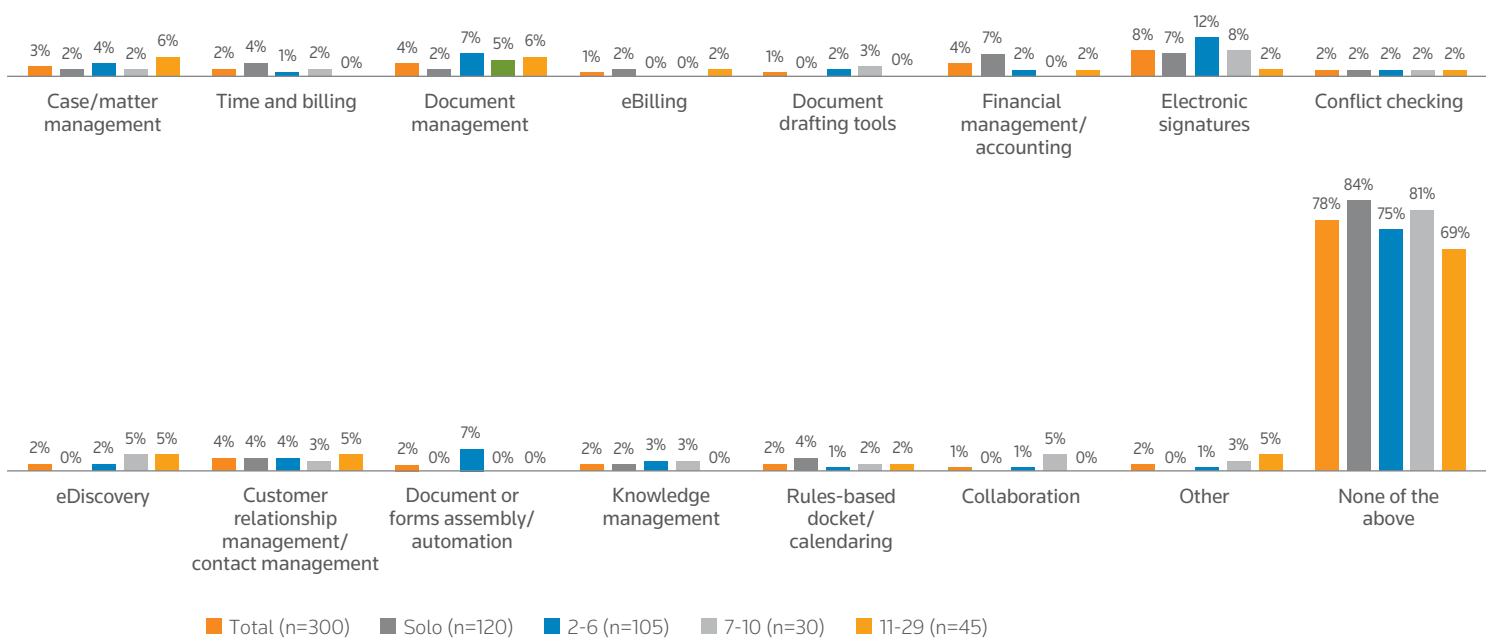
And it appears that at least some small law firms are looking to make just such improvements.

Figure 16 – Technology Systems: Implemented in Past 12 Months



About 11 percent of solo attorneys have implemented a drafting tool in the past 12 months, with another seven percent of solos adopting document management.

Figure 17 – Technology Systems: Plan to Implement in the Next 12 Months



Moving forward, though, it appears that while a good number of firms are planning an increase in tech investment, they are not quite sure where that investment will land. Very few firms report a plan to implement document drafting or management tools, despite the fact that we are still far from 100 percent adoption. Across all segments of small law firms, it appears that the plan for the next year will be to adopt electronic signature tools. Certainly, these are important efficiency tools. But firms would be wise to consider what sorts of technology will most directly help them to address the challenges they've identified in their own practices.

Conclusion

John F. Kennedy provided the opening framework for this report with his exhortation to not overlook the risks of inaction. This same sentiment is, perhaps, captured in another quote: “If you choose not to decide, you still have made a choice.” Those lyrics from the Rush song *Free Will* remind us in a different way that there really is no such thing as status quo. The legal economy is an ever-shifting environment where any attempt to stand still can leave a firm vulnerable to falling behind.

It is our hope that the findings in this report will spur attorneys who are increasingly cognizant of the challenges they face to consider actions they can take to address those challenges. If you’re unsure how, we would offer the following.

- **Start with your end goal in mind.** Pick the two or three things you want to accomplish this year and focus on that.
- **Conduct an honest evaluation of where you are now.** It’s acceptable, even encouraged, to be critical at this phase; you can’t understand how to get where you’re going if you don’t know where you are.
- **Evaluate what you need to get from here to there.** There is no single answer to any of these challenges. Each firm will find different paths to success. But once you know where you are and where you want to be, you can plan the steps needed to get you there.

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