

"High Overhead Costs- Reason #1 Why the Traditional Law Firm Business Model is Broken"

Many traditional law firms are bound by various constraints, limitations, and restrictions based upon their operating business models which are driven by high overhead, profits per equity partner, and billable hours; and not by providing the best possible legal solution alternatives available to clients. In these firms, expansion over the last few years has included law firm consolidation and the opening of multiple offices in multiple locations. While this was done to better service the client, it has also led to large commitments to high fixed overhead leases and properties. Because of this business model and high fixed costs, many of these firms are struggling and unable to adjust to the current economic crisis without raising their billing rates.

The Cost of Offices and Office Improvements

While the drive to service multi-location clients has led to law firms establishing multi-location offices, it has also led to long term leases that are now a drain on firm expenses that cannot be lowered without breaching the firm's contractual commitments. In order to create an image and impress clients, many firms have also upgraded their offices by having spectacular views, marble, glass, and other image conscious amenities. In this new age of frugality, many of these upgrades now seem foolish as the clients are unwilling to pay for these excesses.

The Cost of Associates

Over the last few years, starting salaries for 1st year associates have risen considerably. In some parts of the country, 1st year lawyers are earning \$160,000 in base pay. In the Midwest, the starting pay is a bit lower; although if clients were aware that the starting pay often exceeds \$100,000, they would not be pleased. While law firms have wanted to keep up with the salary metrics of other similar firms, the end result is that the clients are paying for these high salaries.

The Cost of Perks

As many of you know, typically the best seats at the ballpark, hockey rink, or basketball court are controlled by the law firms. While these were secured for "client development", many law firm partners attend many games and events and like to be seen in these prime seats. When I served as an in house counsel, I had my share of law firm partners that thought I would provide business based upon going to a game. This never happened and in fact many companies have instituted policies that prohibit the use of these law firm perks. It is time for the law firms to reconsider this practice as clients in this economy are likely not willing "to pay" for these perks.

What can you do if you feel you are funding increased hourly rates to cover overhead cost excesses?

Here are a few of my suggestions:

1. Check your invoices for increases in the billing rate- Many lawyers do not broadcast rate increases if you agreed to increases in the Engagement Letter. Many lawyers raise their rates early each year by changing invoice rates without notice. Check your invoices; if rates are increasing, ask your lawyer why?
2. Ask your lawyer how they are compensated- While this is not a comfortable conversation, in this tough economic time, there must be transparency and you need to understand the economic incentives that drive the law firm business model.
3. Ask your lawyer what billing alternatives are offered- The hourly rate billing model is still the norm and favored by many clients and lawyers. However, if you feel that you are funding high overhead expenses that do not benefit you as the client, ask what billing alternatives your lawyer or law firm offers. You should not be paying for high overhead expense excesses that bring you no benefit.