# PETER SCOTT CONSULTING

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## Consolidation without rationalisation does not work!

Any law firm contemplating some form of consolidation (whether you call it a merger or acquisition) should keep in mind two guiding principles:

- *Merger is the beginning, not the end!*
- *It is also a means to an end – to build a more competitive law firm able to take on and beat rivals.*

**Before merging**

An ***integration plan*** should be scoped out and agreed between the parties as part of merger negotiations (it is likely to be too late to try to agree these matters after the merger has happened!).

Identifying the factors that first led to the decision by the parties to seek a merger is a useful way to construct an integration plan for rationalisation of the combined business to make it more efficient and competitive. For example -

- Both parties are likely to have recognised that following detailed reviews of where their markets were going and their competition, they had certain strategic needs and concluded that they needed a means to build a ***stronger platform for focused growth*** to beat larger and more developed competitors. In particular neither firm could see its way on its own to filling the gaps in its expertise or reach, even in its chosen areas of work as driven by the needs of its clients. Such thinking is a very valid driver of consolidation.

- They may have also recognised that each firm on its own had insufficient ***resources*** to enable it to achieve its ambitions. For each firm, consolidation would be a means to harness the combined resources of both to –

    - Grow their ability to attract, retain and develop the best people.

    - Build a management support infrastructure and know how / expertise to underpin the effective and efficient provision of the high quality legal services which the market place now requires.

    - Provide enhanced ability to exploit opportunities which may arise and to provide clients with the services they now need, where they need them and how those services are delivered.

    - Ensure more effective risk and compliance management

    - Build a level of sustainable profitability higher than either firm is achieving at present.

- Many firms embarking on merger also recognise that if they are to compete in the future, then they will need to change the ways in which they operate, and consolidation can be used as a ***catalyst for change***. For example, one question which should always be asked of the other party (and answered for your own firm) is

*"How many of your equity partners will you bring into the new firm as equity partners?"*

The parties should ensure that the new firm starts life lean with no baggage.

- And in the case of those firms which may consider themselves to be 'at risk' from market forces and new competitors with deep pockets which are now threatening to destroy their businesses, ***survival*** is likely to be the decisive factor in deciding to merge.

A comprehensive integration plan to rationalise the combined businesses and to begin to deal with such issues is likely to involve to some degree the ***restructuring*** of the combined businesses. 'Restructuring' can be said to be *"the reorganisation of the legal, ownership, operational or other structures of a business for the purpose of making it more profitable or better organised for its present needs*", which is a good way to view a merger of two law firms. Restructuring should therefore be an integral and critical part of the rationalisation process.

Successfully integrating two law firms into a more profitable and better organised merged business for its present and future needs will require a determined and focused approach, concentrating effort and resources in a prioritised way on those matters which are most likely to achieve agreed objectives within given timescales.

Having a 'focused' approach for the purpose of a rationalisation of the combined firm will require first identifying those critical areas of the business ***where things will need to change*** if the merged firm is to improve its competitiveness and to become more profitable, followed by well - planned and determined steps to implement essential changes. Every aspect of the status quo and planning for the merged firm should be challenged. Very often issues may have already been recognised within each firm but no steps will have been taken to deal with them. Allowing fundamental problems to fester in the newly merged firm by doing nothing is not going to create a sound basis for achieving the agreed vision of the new firm.

A starting point can be to ask the basic question during merger negotiations

*"What will need to change in our merged firm if it is to achieve our vision?"*

If the parties are clearly miles apart on the answer to this question, then that is probably a good reason to end the discussions at that point.

If on the other hand the leaders of each firm are *ad idem* on the essential issues that need to be addressed and how they should be dealt with, then there is probably the basis for going forward. The issues identified will then need to be prioritised and a plan for decision – making and implementation agreed.

However, the first and most important step if effective rationalisation is to succeed is to build consensus within each firm that change will be necessary and this can be built in a number of ways, including for example by –

- Delivering unpalatable 'truths' evidenced by feedback from clients and employees which can be a powerful change agent;

- Carrying out a hearts and minds campaign by each firm's leadership.

If a consensus across both firms can be achieved then it will also be necessary to agree -

- The objectives of the proposed changes as part of developing the vision for the new firm that describes a better future;
- The form the changes should take; and
- An explanation of what the new firm is changing from, and what will need to be changed in detail.

The areas in law firms often identified on merger where change is needed include –

**- Accountability**

One of the most frequent comments I hear is -

*"In the new firm everyone must become accountable"*

by which it is usually meant that if partners agree to do something then they must do it, and if they do not then there should be consequences. Sanctions are too often lacking in many firms but in a newly merged firm they should have real 'teeth'.

**- Leadership and management**

Law firms need to be led and managed as businesses and so governance and management structures need to be streamlined and fit for purpose. There needs to be effective leadership in place at all levels in the new firm to take the merged firm through its first critical stage of life and partners in particular need to become good at business and not just be good lawyers.

**- The way people work and how their performance is managed and rewarded**

Merged firms need to become more efficient and more productive than the two legacy firms and their people need to perform in the manner and to the standards required by clients if they are to achieve the competitive edge to beat their rivals as envisaged by the vision set out for the merger. In return for improved performance, there should be a fair matching of reward to contribution and the overall performance and reward structure should be aligned with and enhance the strategic objectives of the merged firm.

At the same time, it will need to be recognised that the new firm is likely to need to manage its people (its human capital) more effectively than the two legacy firms were doing so that it can create a firm in which its best people *want to work*. Otherwise the 'churn' of good people can become an enormous burden on the new business.

**- The ability to anticipate and respond to clients' needs**

A focus on more effective client relationship management will need to become a top priority in a newly merged firm as the client bases are brought together. Pro-actively understanding what it will take to add value to the merged firm's clients if it is to retain the clients of both firms (not always a given) and develop even more business with them.
The merged firm should be determined to drive out any form of second – rate client service, because it will be the excellence of its people and how they perform for their clients that will ultimately build the merged firm's competitive advantage.

- **Strategic positioning of the new firm and each of its component parts**
Very few, if any law firms can be all things to all men, and so identifying at the outset of the merger the right focus for the new firm in terms of its work types / client types to build its future competitiveness will be vital.

As part of an integration plan, it should be agreed that the parties will 'bite the bullet' and take any long overdue decisions to drop practice areas which will lose money, or will be a drain on cash resources or otherwise serve no useful strategic purpose for the new firm. These issues are likely to involve difficult decisions, particularly regarding people, but such issues need to be faced up to and resolved, **before finalising the merger**.

**Following merger**

The implementation of changes (even agreed changes) to rationalise a merged business is sometimes the most difficult task, often because of fear of change on the part of those within a newly merged firm. This is where having strong communication skills and powers of persuasion are needed to get across the message that there is no alternative but to change. To quote from one of the best books on change I have read, *("A survival guide to the stress of organisational change", Price Pritchett & Ron Pound, 1997 Pritchett & Associates, Inc.)* -

*"The organisation is going to change – it must – if it is to survive and prosper. Rather than banging your head against the wall of hard reality and bruising your spirit, invest your energy in making quick adjustments. Turn when the organisation turns. Practice instant alignment"*

Mergers between law firms are about people and implementing change is about taking people with you on the journey. Here are some thoughts which may help with this task -

**1. Ensure you have the necessary skills**

The task of implementing rationalisation of the merged firm can test to the limit the people skills and change management abilities of even the best and most determined managers. Those who have been given the responsibility of leading the new firm should ask themselves whether they have all the necessary skills (and authority) to successfully carry out the tasks in hand. If not, it would be sensible to bring in external professionals who do have the appropriate knowledge and skills to assist or who can coach those in the firm to acquire the necessary skills.

**2. Prioritise what can be realistically achieved**

It is sometimes said that managing change in a partnership is about *'the art of the possible'.* Notwithstanding that the legal world is changing fast and likely to leave behind those who do not face up to change, some partners, even following a merger when change is expected to happen, simply cannot or do not want to see that they will have to change.

In a newly merged firm, even with the force of an agreed implementation plan behind you, it is still often sensible to implement changes on an *incremental basis* at a pace most partners are prepared to accept. Prioritising those changes which will help to secure the most important objectives of the merger is vital.

**3. Know your partners**

Whenever change is mooted, particularly in a merger situation, can be a time of insecurity for partners for whom professional life may for many years have been a fairly settled existence. Suddenly they are faced with changes which they fear may threaten their cosy way of life. Knowing how to get through to them and to be able to persuade them that there is no alternative to certain changes taking place, is a crucial part of the merger implementation process. Understanding for example -

- *What makes your new partners 'tick'?*
- *What motivates them?*
- *What makes feel them insecure?*
- *How will they react to any specific proposal?*
- *Whether they have strong support across the new firm for their views?*
- *How can we manage any fall-out and limit the damage?*

can be vital when attempting to implement any type of restructuring.

## 4. Let your partners take ‘ownership’ of the restructuring

It is often the case that if partners believe they have themselves originated ideas then they are likely to be more willing to take those ideas to heart and agree to changes which implement those ideas. On the other hand, if they feel that someone is trying to foist on them changes which they have not had an opportunity to fully digest then they may well just pull up the drawbridge and fight against such changes, even though those changes may be for their benefit.

An illustration of how this can work in practice is in relation to one of the currently topical areas of law firm restructuring – ***performance management and profit sharing***, which will inevitably need to be discussed and agreed on a merger.

Developing broadly – based key performance criteria aligned with the newly merged firm’s strategic objectives will be fundamental to developing an effective performance management and reward system. Appropriate performance criteria should ideally cover both activities that are an investment in longer term competitiveness and short term profitability. However some partners may feel threatened by a new system which measures their performance and so it is important that all partners are closely involved in establishing these criteria, rather than letting them feel that these changes are being forced on them. In this way partners will more likely feel they ‘own’ the process and are more likely to work to make it a success.

There was a good example recently of a firm using performance and reward as a tool to help the integration process between two merged firms. The new firm has built into its performance and reward criteria the requirement that partners operate and behave in ways to further the integration of the two legacy firms and their ‘good’ behaviour will be rewarded appropriately.

## 5. Tame your ‘big gorillas’

Many law firms have what I tend to describe as ‘big gorillas’ – partners who are not prepared to be managed and who will typically say things such as

*“You can’t manage me – I am a big biller!”*

*“This compliance nonsense is alright for the rest of you – but not for me!”*

*“You can’t tell me what to do – I am as much an owner of this firm as you!”*

It is often the ‘big gorillas’ who are greatest hurdles to change on a merger. They tend to be partners who are often ‘big billers’ (although they are not necessarily very profitable) and see themselves as ‘untouchable’. Firms do not confront them for fear of losing their turnover, but unless these partners are dealt with, it is unlikely a newly merged firm will make progress.

These are sometimes the same people who at partners' meetings will appear to approve of decisions (including merger) but who have no intention of ever complying or permitting successful implementation of those decisions. How can the leadership of a newly merged firm improve its chances of obtaining 'partner buy-in' to effectively implement restructuring plans in the face of opposition from such partners?

There can be several ways to approach big gorillas, including the following –

**- Use compliance as a tool to manage change**

‘Zero tolerance’ is becoming in some firms the new mantra as far as compliance is concerned and it can be applied to situations where changes must be made to the way partners operate and behave otherwise a firm will not be compliant. As a result some firms are turning compliance to their advantage and using the introduction of COLPs and COFAs as a means to deal with the lack of accountability on the part of some partners. As one experienced managing partner said to me before he agreed to become a COLP –

*"I have told my partners that if I have to do the job, then we are first going to have a very serious debate within the partnership as to how this firm will be managed in the future!"*

I would firmly advocate that approach to a merger situation.

**- Develop partner accountability**

As mentioned earlier this is something which is often discussed within partnerships, although the meaning of the term is rarely defined, and accountability is even less frequently put into practice. When we talk about accountability we are referring to the idea that within a partnership each individual partner should accept the obligation to be accountable to every other partner for his or her actions and behaviour.

Acceptance of the principle of having to 'stand up and be counted' before one's partners is central to the well-being of any law firm and even more important in the case of a merger.

A useful tool to adopt is an 'accountability statement' as part of the new firm's governance arrangements, to create a culture that is supportive of the idea of partners being managed, and embodying one of the principles set out by David Maister in *Practice what you Preach (Free Press 2001)* when describing firms that will succeed by behaving in certain ways:

*'We have no room for those who put their personal agenda ahead of the interests of the clients or the office'*

That approach should be a key aspect of the successful implementation by a merged law firm of a restructuring exercise because the management of many firms would be more effective if the signed buy-in of all partners to this principle was obtained. Peer pressure may well persuade them to sign but if they refuse then at least the issue is out in the open and can be faced up to.

**6. Use the 'power of the team'**

Having a loyal and able team to handle merger integration and the implementation of a restructuring can mean the difference between successfully implementing your changes or not. Your 'team' may in reality consist of most of the other partners who by peer pressure force a minority to accept that certain changes need to be made.

Some firms adopt the 'task force' approach, putting together a handpicked team from across a wide spectrum of the firm under a strong and purposeful leader, which is given the mandate to 'go do', which is likely to be particularly effective in a restructuring exercise following merger.

**7. Strike while the iron is hot**

Once a decision has been made then it can be important to set about the task of turning that decision into action quickly. This is not to say you should rush into things with undue haste, but beginning the job of implementing your restructuring plans should start as soon as possible before others have second thoughts. In particular, responsibilities for particular tasks should as soon as possible be assigned to and accepted by appropriate individuals or groups of partners capable of implementing particular changes.

**8. Just do it**

Sometimes, in difficult situations just getting on with it without further reference to those persons who, if asked, would only say *'no'* can be an effective way of making progress. However, it can take a brave management to do this but if management feels it is strong enough and that there is enough support across the firm (remember the 80/20 rule), this can be effective, particularly when it would be difficult to gain agreement from everyone to a proposed course of action.

For example, it is often very difficult to convince every partner of the need to manage out an underperforming or badly behaving partner because some partners (particularly in merger situations) may never be able to bring themselves to assent to such a course of action. If on the other hand the partner's exit is just dealt with, backed by the support of the majority and negotiated, without having to have recourse to a partnership agreement, LLP members agreement or other governance document, then those recalcitrant partners are likely to accept the fait accompli because they will then be able to say they played no part in it.

However, *'just doing it'* needs a robust approach from management and putting your head above the parapet can be dangerous and so is not advisable for every situation, although sometimes it is the only way to get things done.

**9. Use sanctions**

What can be done if a partner refuses to comply with what has already been agreed? Is there a need for sanctions if firms are to implement their restructuring plans fully and successfully? However, many managing partners are provided with no formal authority to manage or impose sanctions.

Sanctions will need to be appropriate to meet the particular type of problem encountered and each individual firm (particularly in a merger situation) will need to consider, given the culture it is trying to create in the new firm, what type of sanction should be applied. A firm may need appropriate sanctions even for minor transgressions, because if partners know they can get away with small things, they are more likely to believe they can get away with more serious refusals to 'obey the rules'.

**10. Bank progress and move on**

Leading a law firm is rarely about making quantum leaps. It is often said that change should be implemented by 'evolution not revolution' (although in a crisis, revolution is sometimes the only thing that works) More often than not it is about working steadily every day, making incremental progress here and there towards achieving your plan. Sometimes it can be frustrating, taking two steps forward and one back, but if whatever progress is achieved can be *'banked'*, then you can move on to the next issue and over a period of time it is possible to look back at the sum of all the incremental changes made and say -

*'Look how far we have come'*

Success tends to breed success and partners like winners but often find it difficult to tolerate failure. However, because managing change is a continuous process there will inevitably be some failures from time to time and so limiting fall-out from any failures when they do occur also needs to be planned for and made a priority if the process is to continue.

*'Banking progress and moving on'* using incremental change can be a very effective means of putting restructuring plans into action. It will, however, be a matter of judgment in any particular situation as to whether it is best to make progress by incremental changes or to 'go for broke' and seek major changes quickly. Those trying to implement changes will often be faced with a crucial decision;

*'Is this a battle worth fighting now or do we wait for another day?'*

Choosing the most appropriate battle can be one of the keys to success in restructuring. Avoid battles you know you are unlikely to win.

Sometimes events take over and a crisis (such as a cash flow crisis following merger because partners have taken their eye off the cash management ball during the merger discussions) can occur forcing changes to be accepted even by unwilling partners. However, even as partners may be looking into the abyss, it can still take a long time for some people to understand their predicament. Crisis management is not the ideal way to restructure a law firm but knowing how to use a crisis can be very effective to implement change.

**A few final thoughts**

Those who have the responsibility to lead a merged firm may also like to consider the following –

- Think bigger and adapt to the enlarged size of the new firm by growing with it.
- If a managing partner, rethink how you operate personally and in particular delegate more – you cannot in a larger organisation do it all yourself.
- Put a lot of effort into managing performance issues in the new firm.
- Quickly enhance the quality of the management capability if necessary
- Upgrade systems and people and do not avoid taking tough decisions.
- Harness all the energy and ambitions which are released by the merger; and
- Above all, get your people working together.