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**The growth of corporate law firms: Determinants and outcomes
of strategic decisions in New York City firms between 1983 and
1987**

Weisbord, Ellyn Susan, Ph.D.

City University of New York, 1990

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THE GROWTH OF CORPORATE LAW FIRMS:
DETERMINANTS AND OUTCOMES OF STRATEGIC DECISIONS IN
NEW YORK CITY FIRMS BETWEEN 1983 AND 1987

by

ELLYN S. WEISBORD

A dissertation submitted to the Graduate
Faculty in Business in partial fulfillment of
the requirements for the degree of Doctor of
Philosophy, The City University of New York.

1990

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This manuscript has been read and accepted for the Graduate Faculty in Business in satisfaction of the dissertation requirement for the degree of Doctor of Philosophy.

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Abstract

THE GROWTH OF CORPORATE LAW FIRMS:
DETERMINANTS AND OUTCOMES OF STRATEGIC DECISIONS IN
NEW YORK CITY FIRMS BETWEEN 1983 AND 1987

by

Ellyn S. Weisbord

Advisor: Dr. Donald J. Vredenburg

Growth processes in professional firms are not addressed in either the literature on professionals in organizations or the strategy literature and are not well understood. This study investigated strategic growth decisions in general practice corporate law firms. Historically, law firms have been closed internal labor markets, characterized by an up-or-out system of recruitment and promotion. More recently, however, law firms have started to use both lateral entry and merger for expansion.

Growth decisions were analyzed in terms of three strategies and three mechanisms. Strategies include the expansion of existing practice areas, the development of new practice areas, and the development of branch offices. Mechanisms include internal development (promotion and transfer), lateral entry (the recruitment of attorneys at the partnership level), and merger.

Data for the years 1983 through 1987 were obtained from firm records and interviews with managing or senior partners

at sixty-one New York City firms ranging in size from twenty to over two hundred attorneys.

Results of lagged multiple regression analysis demonstrate the influence of organizational conditions on growth strategy decisions. Expansion of the existing practice results from a high associate-to-partner ratio, which induces promotion, as well as from small size and unprofitable areas of practice, which motivate merger and lateral entry respectively. The addition of new fields of practice is related to the breadth of the practice and also to the firm's reliance on a limited number of rainmakers, and is accomplished by lateral entry. Branch offices are opened by internal development in firms with a strong policy of promotion-from-within, though larger firms open more branch offices by merger.

Results also show that profit increases are not related to the expansion of the existing practice but are associated with the development of new practice areas and branch offices. Profit is positively related to practice development when it is undertaken by lateral entry. However, branch office development is positively related to profitability only when clients use more than one of the firm's offices.

A low R-square in many of the analyses indicates the need to identify additional variables that will more comprehensively specify the model. Additional research is also needed to extend generalizability to specialist law firms, and to other types of professional service firms.

For my father, Wallace W. Weisbord

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CHAPTER I INTRODUCTION

The past century has witnessed an evolution in United States society from the dominance of manufacturing and agriculture to that of service. In 1870 just over 20% of the work force was employed in the service sector, compared to three out of every four workers today (Cohen & Zysman, 1987; Fuchs, 1968). There has also been a trend toward an increasing number of professional workers, inspiring at least one author to speak of "the professionalization of everyone" (Wilensky, 1964). Moreover, professional work is becoming increasingly organizationally based (Hall, 1968; Blankenship, 1977; Mills, 1986). It is estimated that by the 1990s 20% of the labor force will be professionals and that three-fourths of the professional workforce will be organizationally salaried (Raelin, 1987).

Most organization researchers agree that there are marked differences between service and manufacturing organizations (e.g., Normann, 1984). Drucker (1973) warns that caution should be exercised in applying models derived from and for manufacturing to service organizations. Nonetheless, the growth of theoretical and applied knowledge specifically pertaining to service entities has not kept pace with their rapidly expanding place in the U. S. (and worldwide) economy. Professional service firms (PSFs), have received even less attention by organization theorists than have service organizations generally. The PSF is a model of organization which

is, in effect, a synthesis of professional and bureaucratic models (Litwak, 1961; Smigel, 1964; Mintzberg, 1979). Scott defines professional organizations as "organizations in which members of one or more professional groups play the central role in the achievement of the primary organizational objectives" (1965, p.65). Scott further differentiates between autonomous and heteronomous professional organizations. In the former, professionals not only provide services but also manage the organization, i.e., they set organizational goals, coordinate activities, evaluate performance, and determine compensation. Examples of autonomous PSFs include law firms, accounting firms, and consulting firms. In heteronomous PSFs, professionals "are clearly subordinated to an administrative framework, and the amount of autonomy granted professional employees is relatively small" (Scott, 1965, p. 67). Examples include public health agencies, universities, and libraries. In the present study, all reference to professional organizations will implicitly be to autonomous PSFs.

In addition to the tendency in the organization literature to focus on manufacturing organizations, there is a dearth of extant research on firms that are neither large nor mature (Quinn & Cameron, 1983). An identifying characteristic of service organizations, and particularly of PSFs, is the tendency to be small in comparison to manufacturing organizations. This is not to suggest that all PSFs are small. Indeed, several of the Big Eight accounting firms have over 1,200 partners and more than 20,000 employees (Maister, 1982)

and the largest law firms are approaching the 1000 lawyer mark (Glaberson, 1986). Universities and public health agencies are also often large. Still, whereas 50% of manufacturing sector workers are in organizations of 250 employees or more, almost 75% of service sector workers are employed in organizations with fewer than 250 employees (1982 Bureau of Census; Mills, 1986). Much of the organization literature is thus questionable when applied to PSFs.

Research on professional organizations suffers from two additional limitations. First, the breadth of the literature is limited. Researchers addressing the interaction of professionals and organizations have produced three major research streams: the effects of bureaucratic organizations on professionals' behavior and attitudes (e.g., Sorensen & Sorensen, 1971); the determinants of organizational structure (e.g., Hall, 1968; Nelson, 1988); and the career mobility of professionals (e.g., Wholey, 1985). Topics concerning PSF administration have received some but limited attention (e.g., Sibson, 1971). However, little research on organizational processes in these firms has been generated. Second, the majority of the work that has been done concerns heteronomous PSFs; there has been very little research on autonomous PSFs. Theoretical and empirical attention to autonomous PSFs would both contribute to the organization literature by generating knowledge about increasingly important organizational forms and develop information useful to PSF management.

The intent of this dissertation is to contribute to the understanding of professional service firms by studying the determinants and outcomes of growth strategy in law firms. The study has two major objectives. The first objective is to identify antecedent firm conditions that influence the direction of growth, i.e., existing and new products and markets, and the means of growth, i.e., internal versus external development; the latter includes both lateral entry and merger. Included in this part of the investigation is an examination of the differential use of internal and external growth mechanisms for implementing particular strategies. The second objective is to analyze the economic impact of these strategic choices on the firm.

The comparison of internal development, lateral entry, and merger within one study is new. Research on the use of internal versus external growth mechanisms is found in two distinct bodies of research. The use of promotion and lateral entry has been studied by organization and management researchers investigating intraorganizational and interorganizational mobility, including internal labor markets. The focus of this research is environmental and organizational influences on the movement of personnel within and between organizations. Most studies treat only one of the mechanisms rather than comparing the two. Research on the mergers and acquisition process is primarily found in the strategy literature. Merger and acquisition is assumed to be the primary means for diversification (Porter, 1987) and scant attention

has been paid to organization level reasons for growing by merger beside the diversification motive. Moreover, the focus on merger to effect diversification has meant that little attention is paid to internal diversification.

Unlike other types of organizations, the service and the service-provider are not readily separated in the professional service firm. In a law firm, an individual attorney can open a new practice area or branch office. Internal development (which, in addition to promotion, includes the retraining or transfer to new locations of existing firm members) is therefore a viable mechanism for implementing a product or market diversification strategy. Indeed, law firms have historically grown almost exclusively by internal development. By the same reasoning, diversification can occur by the lateral acquisition of one or a small number of attorneys. Conversely, merger is not necessarily used exclusively for diversification but rather is also a mechanism for enlarging the size of the existing practice. In sum, law firms (and other professional firms) are better able than firms more commonly studied by strategy researchers to use all three mechanisms for all types of growth. However, because the literature on professional organizations does not address strategic growth, and the literature on growth strategies and mechanisms fails to adequately represent the professional service firm, these processes are currently not well understood.

Growth in Professional Service Firms

A unique characteristic of the professional service firm is its internal promotional structure, which creates the need for continual growth. "The archetypal structure of the professional service firm is an organization containing three professional levels which serve as a normal or expected career path" (Maister, 1982, p.15). (An exception is the law firm, which tends to have only two levels, associate and partner.) In the "up or out" world of such firms, the failure to promote deserving juniors within normative time limits will erode the promotion incentive central to the recruitment and motivation of junior members. This promotional structure creates a need for growth due to the practice of leveraging the skills of senior professionals with efforts of junior members, i.e., billing out more fees in junior hours than they earn in salary so that partners may share in resulting profits. Leveraging pushes firms to grow because once juniors become seniors, moving from salaried to profit-sharing positions, new juniors are needed or the rewards of top professionals will shrink. Thus, growth is needed in order to maintain desired ratios. Specific growth rates vary based on the interaction of leverage, i.e., the ratio of junior to senior firm members, and promotion policies, i.e., the target rate of promotion, but all PSFs will experience some amount of ongoing internal pressure for growth. Given the primacy of this growth objective, an understanding of strategic growth

issues is especially germane to theoretical and applied knowledge of this type of organization.

Professional service firms grow by pursuing three growth strategies through three growth mechanisms. One growth strategy is the expansion of existing practice areas through market penetration, i.e., increasing business opportunities within existing practice areas. A second strategy is the development of new practice areas for existing client markets (this growth strategy is commonly called product development but in the case of PSFs products are practice areas, and thus reference within this paper will be to practice development). The third strategy is market development, i.e., to expand geographically by opening branch offices. PSFs may engage in one, two or all of these growth strategies over time, and may alternate among them. Each of these strategies may be accomplished by any of three growth mechanisms: internal development, lateral entry, or merger. The first, internal development, involves the promotion of junior members through the PSF hierarchy. Lateral entry, the addition of members at a senior level, and merger, the formation of one partnership from two or more previous partnerships, are similar in that both create growth by adding to the firm from the external labor market. As a result of their particular advantages and disadvantages, each of the growth mechanisms is suitable under different PSF conditions. Broadly considered, the internal development mechanism will result in slow, steady growth. Conversely, both external mechanisms will achieve more rapid

growth. Pairing the three growth strategies with the three growth mechanisms results in nine strategy/mechanism combinations that are growth options for professional service firms, as shown in Figure 1.

Figure 1
PSF Strategic Growth Options

		G R O W T H S T R A T E G I E S		
		Practice Area Expansion	Practice Development	Market Development
G R O W T H M E C H A N I S M S	Internal Development	S L O W G R O W T H		
	Lateral Entry	M O R E R A P I D G R O W T H		
	Merger	M O S T R A P I D G R O W T H		

Growth in Law Firms

The present research investigates the topic of PSF growth strategy within a population of general practice corporate law firms. This description identifies the type of firm chosen for study in two ways. First, the "corporate" designation indicates that the firm's client is the business organization, though corporate firms also represent wealthy individuals. Second, the "general practice" firm provides those clients a full array of legal services, in contrast to the specialist firm which offers expertise in one or a small number of legal fields.

The legitimacy of categorizing legal practice by client type has been forcefully argued by Heinz and Laumann (Heinz & Laumann, 1982; Laumann & Heinz, 1979). In their study of the social structure of the Chicago Bar Association, Heinz and Laumann demonstrate that "...though there is some clustering of fields [of legal practice] according to their cognitive similarities, the primary structure of co-practice appears to be client centered" (1982, p.52). The authors advance the thesis that there is a fundamental distinction within the legal profession between lawyers who represent large organizations and those who represent individuals, and that these two "hemispheres" are largely separate. Indeed, their analysis reveals differences among the sectors so profound, including, in addition to different clients, different lawyers, law school origins, office environments, social networks, and

more, as to provoke their conclusion that "only in the most formal of senses do the two types of lawyers constitute one profession" (1982, p.384).

The general practice corporate law firm provides an appropriate setting for the study of PSF growth and development for several reasons. For one, law firms very much reflect the previously discussed trends toward increasing numbers of professionals and professional organizations. To wit, in 1960 one in every 632 Americans was a lawyer; in 1970 that figure rose to one in every 572 and in 1980 it was one in every 418 (Bradlow, 1986). By 1985 there was one lawyer for every 360 Americans (Glasser & Glasser, 1987). Moreover, as indicated in Table 1, private practitioners have steadily shifted from solo to firm practice within that same time period.

Table 1
Lawyer Employment

Year	Number of Lawyers	Number in Private Practice	% Solo Practice	% Firm Practice	Number of Firms*
1960	285,933	206,000	64	36	
1970	355,242	240,000	52	48	
1980	542,205	370,111	49	51	38,482
1985	655,191	460,206	47	53	42,318

*Not available before 1980

Sources: Curran (1985); Glasser & Glasser (1987)

Corporate law firms in particular are proliferating not only in number but in size. A review of law firm growth over the past decade corroborates the oft-cited development of legal "megafirms". The largest law firm in 1975 had 326 members; in 1986 that same firm (still the largest) had 808 members (Glaberson, 1986). In 1978 there were 79 firms that contained more than 100 lawyers; by 1985 this number had increased to 219 (O'Connor, 1985). From 1978 to 1986 the cut-off point for the top ten largest law firms in the country grew more than 100% from 208 to 422 (Miskiewicz, 1986; O'Connor, 1985). Manhattan Lawyer, the newest publication of Steven Brill's American Lawyer Newspaper Group, categorizes midsize firms as those with 35 to 75 lawyers (Goldner, 1987) and Mark Stevens, in his recent book The Power of Attorney, refers to 50 to 200 member firms as "second tier" (1987). In short, the large firm of ten years ago is today's midsize firm.

In addition to reasons of increasing number and size of law firms, the legal profession has particular appeal for management research as a result of fundamental changes in its competitive environment. In his September, 1986 speech at the Indiana University School of Law, Chief Justice William Rehnquist noted the trend over the past twenty-five years, "to make the practice of law more like a business" (Rehnquist, 1987). This frequently heard charge refers to a profusion of changes in the conduct of providing legal services, changes that range from the adoption of business procedures for more

efficient firm administration to more volatile changes surrounding compensation, loyalty, and delivery of service.

A major cause of the metamorphosis of this sector of the legal profession is increased competition resulting from the changing nature of the client/law firm relationship. Corporate consumers of legal services have increasingly been using in-house legal staff for routine legal services (Agrest, Clausen, & Camper, 1981; Bradlow, 1986). This development has changed the role of outside counsel in two ways. First, since much of the general corporate work once done by outside firms is now often performed by in-house staff, the work of outside counsel has shifted toward legal matters that cannot be efficiently handled internally, such as large scale litigation or highly specialized legal matters. Second, the primacy of the relationship between external corporate counsel and top corporate management has changed to one where outside counsel's primary link is to corporate general counsel. In effect, corporate general counsel -- not senior management -- is the outside law firm's client. As clients, internal general counsel are sophisticated and powerful buyers of legal services who know what legal services should cost and have the authority to choose which firms will provide those services. Those general counsel are increasingly spreading work among several law firms rather than conducting long-term exclusive relationships with one or two firms.

One result of client movement toward in-house legal services and away from loyalty to any particular firm is the

greater need to develop "rainmakers" (business-generators) throughout the firm. Consequently, the basis of law firm partner compensation is shifting from seniority to a merit-based system with business-getting as a primary criterion (Heintz, 1981), a shift which is increasing insecurity and decreasing the loyalty of firm members. Lateral movement of individual partners and occasionally whole departments is becoming ubiquitous (Brill, 1985). This phenomenon is particularly disruptive because raided firms often lose not only their best business producers but the clients of those lawyers as well. These changes have contributed to an increasingly competitive law firm environment.

Further exacerbating competition is increasing firm size. The practice of leveraging the work of law firm associates creates an imperative for law firm growth. But this growth cannot happen without an increase in the amount of business conducted. Indeed, financial writer Mark Stevens asserts that the biggest megafirms must increase billings by at least twenty million dollars annually just to sustain modest growth (Glaberson, 1986). Though the megafirm is an extreme example, it serves to demonstrate that the amount of new business that must be generated annually in order for law firms to maintain their promotional and economic structures as they grow is considerable. This situation has contributed to competition for business and for those lawyers who bring business to the firm. Size increases are due as well to the

attempt to increase prestige, of which size is an important symbol (Abel, 1986).

The competitive structure of the industry has also been altered by efforts to become transnational and highly specialized, as the desire to attain competitive advantage leads firms to develop multi-site, as well as multi-specialty, capability. A growing number of firms have opened branch offices, resulting in an increase in the number of large, national firms capable of serving corporate clients (Reed, 1983). These firms compete not only for national clients but for a place in the local market, to the detriment of firms already practicing there. The creation of practice "boutiques", or narrow specialty area departments, within large firms is another phenomenon intensifying competition and also increasing raiding; expanding firms compete for talent, attempting to garner expertise and rainmaking ability by the more expeditious route of importing expertise into the firm, rather than developing it internally.

Clearly, law firms face a more competitive environment than ever before. An emphasis on growth and an increasingly competitive environment are related because size as a goal is linked to industry competition through perceptions of the advantages inherent in being large. Large firms are more profitable than small ones (Brill, 1985, 1986, 1987, 1988), and widespread acceptance of the perceived advantages of size, including status and recognition, lead many firms to actively pursue growth well beyond that needed to satisfy internal

structural imperatives. The result of these changes in the competitive environment is the erosion of professional traditions and the development of an increasing business orientation. Law firm management has experienced a marked shift toward concern with the bottom line. Profit has always been a concern, of course, but the explicit discussion of profit and changes in structure and processes to accommodate that emphasis is new. Compensation, once almost exclusively based on a lock-step seniority system, is now based on business generation to a least some degree in most firms. Legal practice areas or departments are frequently treated as profit centers.

Perhaps most profound is the changing structure of professional staffing. Law firms have long been firm internal labor markets, recruiting attorneys out of law school, providing further training within the firm, and making partners almost exclusively from the ranks of associates (junior lawyers). Recently, however, there has been a movement toward the addition of partners by external growth mechanisms, i.e., lateral entry and merger. Lateral movement to new firms by individual partners and even whole departments is now common, and law firms are more frequently considering and engaging in merger activity (Goldner, 1987).

Weakening of the law firm internal labor market can be understood in terms of the relative advantages of internal and external staffing methods for the current law firm environment. An important benefit of promotion and internal

mobility is training. Internal labor market theorists argue that firm specific skills lead to promotion ladders and block lateral entry (Wholey, 1984). This was important to law firms when institutional clients, i.e., those who used the services of one firm for virtually all their legal needs, were the norm. Recently, however, due to the increasing use of corporate in-house legal counsel for general work and concomitant use of outside firms for more complex and specialized matters, as well as the practice by corporate clients of acquiring legal services from several firms, legal work has become more transactional, specialized by field of law rather than by client. At the same time, a major reason for recruiting senior positions externally is the lack of available expertise within the organization. In the case of law firms, such expertise may be both the legal or business-generating capabilities of attorneys. Therefore, growth by external mechanisms may be better suited to the current law firm environment than the older policy of promotion-from-within. Under these circumstances, the ability to attract and keep attorneys with valuable expertise and rainmaking ability is critical, and compensation is a primary factor in a firm's ability to do so. Thus the profit advantage of large size constitutes an additional imperative for growth, helping firms adapt and survive in the competitive environment.

Concurrent with the increasing emphasis on growth, there is an increasing awareness among lawyers and law firm management professionals that, in order to be successful, the

growth process must be managed. One need only review recent issues of legal periodicals such as The American Lawyer, The National Law Journal and others to observe the escalating recognition of and attention to this issue. Perhaps the most basic issue in managing the growth process is the determination of how to grow, that is, in what directions and by what means. Thus, efforts to formulate successful growth strategies should be enhanced by consideration of the conditions under which various growth mechanisms are most effective in pursuing different growth strategies.

The present research is directed toward that end. The study first addresses determinants of the choice between internal and external growth mechanisms for pursuing the three growth strategies. The question of why, i.e., under what conditions, firms choose to grow by external rather than internal mechanisms is particularly important in light of the tradition of law firm internal labor markets. Next, based on the assumption that the combined influence of the proposed determinants as well as the advantages and disadvantages of the three growth mechanisms will result in tendencies among firms toward specific mechanisms for each growth strategy, hypotheses predicting patterns in the frequency with which law firms grow by each of the nine strategy-mechanism combinations are tested. Finally, the outcomes of growth decisions are considered by examining the effects of strategic decisions on firm profitability and partner departures.

CHAPTER 2 RESEARCH CONTEXT

Growth Strategies

Organizational growth strategy is typically characterized in terms of the direction in which a firm is moving with respect to its current product-market position (Ansoff, 1965). Growth decisions involve choices regarding existing versus new products and existing versus new markets. These choices create four possible growth strategies, as depicted in Figure 2.

Figure 2
Product-Market Matrix

Products Markets	Existing Products	New Products
Existing Markets	Market Penetration	Product Development
New Markets	Market Development	Diversification

The market penetration strategy focuses on increasing the sale of existing products to existing customers. Product development refers to the development of new products for existing customers. Market development is finding new

customers for existing products. Finally, an organization diversifies when it seeks to provide new products to new customers. When applying this typology to professional service firms, products are referred to as services and customers as clients.

Of the four growth strategies, it is the first three that are central to the present study. Diversification in its purest sense "takes place when the firm expands to make and sell products or a product line having no market interaction (technically, having zero cross price-elasticity) with each of the firm's other products" (Rumelt, 1982, p.363); the prototype of the pure unrelated diversified firm is the conglomerate. In addition to market considerations, diversification is also characterized by the extent to which necessary resources for the production and distribution of one product cannot be shifted to the other (Gort, 1962).

As defined above, diversification by law firms, though no longer completely unheard of (Lewin, 1987), remains anomalous. However, the concept of diversification is ambiguous. Penrose (1959) has pointed out that it is neither possible nor desirable to establish an absolute meaning of diversification, as such meaning "will depend on the grouping of commodities...that is significant for the analysis at hand" (p.107). Diversification in the PSF needs to be considered within the unique structure of this type of organization, i.e., the equivalence between functional and market bases for grouping. As Mintzberg (1979) points out, "Because clients

are categorized...in terms of the functional specialists who serve them, the structure of the Professional Bureaucracy becomes at the same time both a functional and a market-based one...Thus, the distinction between functional and market bases for grouping breaks down in the special case of the Professional Bureaucracy" (p.354).

The structural implications of this characteristic cause the PSF to have certain parallels with the multi-divisional form of organization. In the M-form, divisions are separated on the basis of product, market, or region and all resources necessary to manufacture and sell the product are under the control of the division. In the autonomous PSF, functional/market-based departments act much like M-form divisions, insofar as they are basically self-contained, relatively autonomous units that operate essentially as mini-companies; the services are produced and delivered concurrently (Sasser, 1976). The functional/market based unit of the PSF may be limited to one professional or a team of professionals. Hence, product development and market development are also considered to be diversification (Penrose, 1959; Pitts, 1977), and motives for diversification provide some direction for developing an understanding of the use of the product and market development strategies by law firms. In the case of law firms, product development is the development of new practice areas or legal specialties, and market development is considered in geographic terms, i.e., the opening of branch offices (Montgomery & Wilson, 1986).

Commonly held reasons for diversification vary in applicability to law firms. Financial economies like risk-pooling (Lewellen, 1971) and portfolio management, i.e., pooling of cash flows, are generally associated exclusively with unrelated diversification (Hill & Hoskisson, 1987). The concept of risk-spreading as it applies to conglomerate diversification, i.e., the spreading of resources and concomitant reduction in investment risk (variability of returns over time) does not apply to PSFs, which are neither highly diversified nor publicly held. Some of the advantages often realized by related diversifiers, such as economies of scale or vertical integration (Harrigan, 1985), also do not have applicability to law firms. Law firms are limitedly able to realize economies of scale due to the knowledge-intensive nature of legal work; similarly, the unique nature of professional work precludes ownership of sources of raw materials or outlets for the sale and distribution of services.

Two other motives for diversification do obtain in the case of the law firm. First, diversification provides a defense from potential decline in product demand (Ansoff, 1965; Galbraith et al., 1986; McNichols, 1977; Penrose, 1959). Diversification spreads risk by reducing vulnerability to exogenous changes in supply or demand (Penrose, 1959; Salter & Weinhold, 1979) stemming from reliance on an overly narrow range of services. This motive is a consideration for firms that specialize in very narrow practice areas. For example,

the October, 1987 stock market debacle was potentially threatening to the mergers and acquisitions specialty and hence to the firm of Wachtell, Lipton, Rosen & Katz, which relies almost exclusively on a mergers and acquisitions practice. Frequently, however, legal specialties enjoy a large measure of security, as practice areas emerge largely in response to regulatory policy and there is rarely a decrease in regulation (with notable exceptions, such as anti-trust).

A second and more widespread motive for law firm diversification is the pursuit of practice area breadth in order to effectively compete (Penrose, 1959). The argument has already been made that law firms need to develop expertise in specialty areas in order to compete more effectively as a result of conditions imposed by the burgeoning use of in-house counsel for routine corporate work.¹ In addition, the increasing complexity and interdependence of legal fields have contributed to the trend by large firms toward becoming a collection of specialty "boutiques" ("Lawyers Catch Merger Fever," 1987), allowing them to create multi-specialty teams. For example, large firms which once disdained bankruptcy matters have been developing bankruptcy practices (Rosenwein, 1988) as a result of the increasing amount of corporate restructuring brought about by events in the business environment. Bringing this practice to large firms allows them to call on lawyers with expertise in tax

¹A more complete discussion of the law firm competitive environment is contained in the section on Law Firms in Chapter 1.

law, real estate law, etc. for restructuring work. As the number of legal fields increases and the ability for interdependence becomes more critical, multi-specialty firms face pressures to offer an increasing number of legal services in order to compete as "full service" firms.

Diversification is also a response to client need. For law firms, a primary source of growth opportunity derives from client need for legal services. Such opportunities frequently come from clients which have extended lateral and longitudinal relationships with the firm (Lefton and Rosengren, 1966), so-called institutional clients, who use the firm for a large proportion of their legal needs over an extended period of time. One way that law firms increase the scope of their practice is to follow these clients into new practice areas. For example, a firm might decide to begin a mergers and acquisitions practice if its clients are going elsewhere for such services. Parallel market considerations, i.e., frequent client need for legal services in another city, may induce law firms to open branch offices.

Starbuck (1965) maintains that growth is either a means of attaining other goals or the side effect of such attainment. In other words, size as an operational goal is correlated with the attainment of goals that have a more basic relevance to the organizations's purpose. Like other organizations, law firms grow both to reduce the risks of small size and increase the rewards of large size.

Liabilities of smallness have been recognized by both economists and organization theorists (Aldrich & Auster, 1986; Penrose, 1959; Starbuck, 1965). Of the liabilities commonly identified by such researchers, those most pertinent to law firms include the difficulty of raising capital, a weak position in the competition for labor, and instability due to variation (e.g., unbalanced work loads). Besides reducing these difficulties, larger size has other advantages. These include geographical comprehensiveness, flexibility of operation, a wide range of specialties, the ability to attract the highest quality professionals, and confidence-inspiring prestige (Montagna, 1974). For law firms, the advantages of large size (e.g., the ability to create multi-specialty teams, the ability to put large numbers of lawyers on a matter on short notice) help to attract large clients, whence large fees are most readily generated. Moreover, though there are exceptions, the relationship between large size and large per-partner profits (Brill, 1985, 1986, 1987, 1988) contributes to the large firm's ability to attract and keep top lawyers. Additionally, large firms are less susceptible to endangerment through the loss of clients (Pfeffer & Salancik, 1978; Thompson, 1967) and are buffered also against the departure of partners insofar as sheer numbers limit the effect of departures on the ability of firms to keep doing business.

Cross-selling and the Relationship of Practice and Market
Development to Profitability

The relationship of diversification to performance has been investigated primarily in terms of the relative success of related and unrelated diversifiers in achieving profitability increases (Bettis, 1981; Christensen & Montgomery, 1981; Montgomery, 1985; Rumelt, 1974, 1982), with relatedness defined as similarity of markets, distribution systems, or production technologies, or the exploitation of similar science-based research (Rumelt, 1974). Results of these studies have been inconclusive and contradictory and have failed to establish a clear relationship between diversification and profitability, though on balance there is some evidence of better performance by related than by unrelated diversifiers. Findings concerning related diversification are of interest here because PSF practice area and market diversification can be considered as related diversification, i.e., product/market extensions within the same industry (McNichols, 1977).

Despite weak and inconclusive empirical evidence, prevailing wisdom holds that related diversification has the potential to be successful, i.e., to increase earnings, when diversification exploits synergies or scope economies (Kazanjian & Drazin, 1987; Porter, 1985; Salter & Weinhold, 1979). According to Porter (1985), while the creation of value through synergy was widely used as a justification for the extensive diversification that took place in the United States in the 1960s and early 1970s, that synergy rarely

occurred in practice. Porter explains the failure of synergy as management's failure to understand and implement it, rather than as a flaw in the concept itself, and asserts that the potential for effecting interrelationships, or shared activities, among business units is an important source of competitive advantage.

Both tangible and intangible interrelationships are possible. Intangible interrelationships involve the transference of management capability or "know-how" from one business unit to another. Opportunities for tangible interrelationships arise from the presence of common buyers, channels, technologies, and other factors, and include such shared activities as raw materials procurement, development of technological or production processes, and sales and distribution (Porter, 1987). Ansoff (1965) makes a point similar to Porter's in suggesting that a complete line of related products provides the opportunity for tie-in sales. The implication of these arguments is that product line development should result in increased profits because of the opportunities a diversified product line affords for cross-selling. However, the effect of cross-selling on the relationship between diversification and profitability has not been addressed empirically by organization researchers.

Despite the absence of empirical investigation, cross-selling is considered to be a potential benefit of related diversification. In his treatment of that subject, Porter (1985) suggests that cross-selling lowers the cost of finding

new buyers. He also suggests a number of impediments to achieving the potential benefits of diversification, some of which have applicability to law firms. For example, business units may resist cross-selling due to fears that their relations with clients will be damaged by the poor performance of other units within their firm. Also, incentive systems typically fail to reward this contribution to overall firm performance, though this situation is diminished in firms that consider business-getting as a primary criterion of compensation decisions.

Cross-selling has received attention in recent years by management writers in connection with service industries such as banking and insurance (Costigan, 1987; Fitzgerald, 1986; Sippel & Gouthro, 1987; Smith, 1986; Spooner, 1985; Thomsett, 1987; Turk, 1981; Watne, 1979). Building multiple relationships with clients is believed to improve competitive advantage by strengthening client loyalty (Sippel & Gouthro, 1987). Client loyalty is strengthened because additional business with a single provider can work to increase efficiency and accuracy (Costigan, 1987), and because of the disadvantage to the client of increased switching costs.

Applied to law firms, business unit cross-selling refers to multiple practice area use and multiple branch office use by existing clients that results from intrafirm referrals. Firms with diversified practice areas have the opportunity to cross-sell services, and firms that have undertaken geographic expansion have the opportunity to cross-sell branch offices.

The advantages of cross-selling have a direct impact on two variables critical to law firm profitability: billing rate and utilization. The basic measure of business success in law firms (indeed, in all professional service firms) is net income per partner (NIPP). NIPP is calculated by a multiplicative relationship of five variables: leverage, utilization, billing rate, realization, and margin (Maister, 1984a).² These variables are defined in Table 2.

Table 2
Net Income Per Partner: Key Variables

Leverage:	ratio of associates (and other non-partner professionals) to partners
Utilization:	weighted annual average number of billable hours per lawyer
Billing rate:	weighted average hourly fee
Realization:	percentage of work performed that is billed and collected
Margin:	ratio of net income to gross fees

Leverage is an important route to increasing profitability, as it involves billing out more fees in junior hours than juniors earn in salary, allowing partners to enjoy profits beyond those resulting from their own billings. However, the ability to leverage is limited by the degree to which work can be routinized. Limits on routinization are set both by the nature of the legal work performed (Maister, 1986) and the increasing corporate trend toward bringing

²Much of the following description of law firm economics is drawn from the cited article and from a personal communication with D. H. Maister, October 29, 1987.

routine legal matters in-house. In a similar vein, increasing costs and client resistance to excesses in the legal process, e.g., time spent training junior members, limit the ability to manipulate margin and realization respectively. Utilization and billing rate are also limitedly open to manipulation, the former because there is a limit to the number of work hours (even for associates, whose grueling work routine has become legendary), the latter because clients are increasingly balking at fees perceived to be extraordinary.

Nonetheless, cross-selling can contribute to the improvement of both utilization and billing rate. Utilization should be improved by cross-selling to the extent that intrafirm referrals lower the cost of finding new buyers. This is particularly important in light of the increasingly competitive environment of the legal profession and resultant emphasis, and therefore time spent, on business-getting. Billing rates are dependent on the value of the firm to the client. Cross-selling has the potential to increase this value by increasing client reliance on the firm, which it does by increasing familiarity with the client's business, hence increasing efficiency and accuracy and raising switching costs.

Growth Mechanisms

It is the nature of professional service firms that the ability to expand service -- whether within existing practice areas, in new ones, or in new locations -- is largely dependent upon the addition of service providers. Law firms pursuing the three growth strategies of market penetration, practice development, and market development may increase the size of their professional membership using any one of the three growth mechanisms described earlier: internal development, lateral entry, or merger.

Traditionally, law firms have been firm internal labor markets (ILMs) (Wholey, 1985), hence favoring growth by internal development. Althauser and Kalleberg (1981, p.130) define ILMs in terms of three basic structural features: "(a) a job ladder, with (b) entry only at the bottom and (c) movement up this ladder, which is associated with a progressive development of knowledge or skill". In keeping with these criteria, law firms recruit law school graduates who enter the firm as associates and progress through levels of increasing seniority until a partnership decision is made, a process which generally takes between six and ten years (Nelson, 1983). In his empirical examination of law firm career patterns, Wholey (1984) found internal development (promotion) to be the dominant mechanism for staffing senior positions in the law firms he studied.

Several reasons have been offered for the existence of ILMs. These include motivation through the hope of promotion (Slichter, 1919), retention of workers with firm-specific skills (Becker, 1962), the need for senior people to train juniors (and hence for those seniors to have positions protected from competition) (Doeringer & Piore, 1971), greater consonance between employee goals and organizational goals (Wholey, 1985), scarcity of labor (Pfeffer & Cohen, 1984), and institutionalization (Tolbert & Zucker, 1983), i.e., the acceptance of promotion-from-within as appropriate and necessary.

Applicability of these motives to law firms is considerable. The "up-or-out" system (Meyer & Rowan, 1977) is highly motivational to associates, as performance is the route to partnership (Maister, 1985a). Law firms also provide associates with postgraduate training (Smigel, 1969). Moreover, while there is no shortage of lawyers, there is nonetheless a limited number of graduates of top quality law schools, and competition for those is fierce.

Finally, and perhaps most importantly, the institutionalization of promotion practices is a hallmark of the legal profession. The practice of promotion-from-within began at the start of this century with Paul Cravath. The founder of Cravath, Swaine & Moore insisted that the firm's legal staff be recruited exclusively from law schools, both to assure a Cravath-trained staff and because he believed that the best service would come "from men confident of unimpeded opportunity for advancement" (Stewart, 1983, p.370).

(Training of junior members by seniors is another part of the Cravath legacy.) More recently, the legal profession has been marked by conflict and disparate orientations toward the traditional professional norms of internal development. The profession has increasingly assumed a business orientation and concomitant focus on rapid expansion. Nonetheless, many law firms remain committed to promotion as the primary route to growth.

Despite the aforementioned inducements to maintain a closed ILM, law firms are increasingly engaging in development through external mechanisms, i.e., lateral entry and merger. Where studies of large manufacturing firms lump merger and acquisition together as a single strategy, merger is distinct from acquisition for the professional firm. The former is the amalgamation of all or most of two firms into a new firm which is fully integrated and in which neither original firm clearly dominates. Unlike many other types of organizations, professional firms do not maintain functional autonomy subsequent to merger.

Acquisition, or lateral entry, is the addition of one or a group attorneys into the firm at a senior level. Again, the intent is full integration. The lateral movement of partners between firms, once shunned by the legal profession, is currently widespread. In Spangler's (1986) recent study of lawyers in organizations, fully one-third of her respondents were lateral entrants. Reflecting this change, the weekly legal periodical Manhattan Lawyer reports "Lateral Moves" as

part of its regular column on new hires, promotions, and office changes.

Research on lateral entry is addressed primarily within the literature on internal labor markets (ILMs). ILM literature focuses on issues of career movement within firms and lateral entry is the alternative to internal development (Baron, Davis-Blake, & Bielby, 1986). That is, an either-or decision is assumed, such that the focus of the literature is on the determinants of firm choice between staffing by lateral entry and the ILM policy of promotion-from-within. The motivation most often assumed to explain lateral hiring is the need for instant expertise (Spangler, 1986; Wholey, 1985). In order to reduce the likelihood of failure associated with the liability of newness (Stinchcombe, 1965) and to save costs incurred by retraining (Doeringer, 1967), firms recruit personnel who do not require training. These arguments are supported by findings that specialists have greater interorganizational mobility than others (Leggatt, 1979). However, research has paid most attention to the benefits of internal promotion; reasons for the use of lateral entry in a predominantly closed ILM have not been empirically examined.

Though not as pervasive as lateral entry, merger has also become a common occurrence among law firms. Like other professional service firms, law firms pursue merger in order to rapidly attain greater practice area breadth, a broader client base, and a greater number of business-getters, toward the overarching goals of reduced vulnerability and increased

profitability (Graves, 1981). The use of merger to achieve rapid growth is well documented (Finkelstein, 1986; Mueller, 1980; Penrose, 1959). Indeed, when growth is defined, as it is in this study, as an increase in the number of employees, practice areas, and branch offices, then the relationship between merger and growth is tautological.

Merger has received considerable attention in the strategic management literature. A variety of motives to explain merger activity have been proposed (Lubatkin, 1983; Mueller, 1980; Pfeffer, 1972; Shepherd, 1979; Steiner, 1975). Lubatkin (1983) suggests that these motives can be understood as an attempt to attain three types of synergies: technical economies, which are largely economies of scale; pecuniary economies, which extend market power by increasing size, i.e., the attempt to approach monopoly and monopsony; and diversification economies, which spread and reduce risk, i.e., conglomerate mergers.

It has also been frequently suggested by organization and strategy researchers that mergers take place as a result of the desire of managers to pursue growth for its own sake. This argument is predicated on advantages of size for organizational managers. For example, evidence of the positive relationship between organizational size and executive salary is consistently reported (Galbraith & Stiles, 1984; Lubatkin, 1983; Meeks, 1977; Roberts, 1956; Shepherd, 1979; Simon, 1957; Williamson, 1963). Other, more intangible advantages of

size such as status and prestige (Starbuck, 1965; Reid, 1968) also accrue to members of large organizations.

Two major problems exist in understanding PSF use of merger from this research. First, the literature is inconclusive. Data for proposed relationships are relatively limited (Shepherd, 1979) and results are often contradictory (Steiner, 1975). This research largely overlaps with the diversification literature, as merger is most often considered to represent a diversification act (Lubatkin, 1983; McNichols, 1977). Thus, it suffers from the same weaknesses in applicability to professional service firms as does the diversification literature, including no clear findings regarding its relationship to profitability (Finkelstein, 1986).

Second, and perhaps more pertinent, research has been conducted virtually exclusively on large corporations, frequently on publicly held corporations, and often on highly unrelated-diversified companies. Hence, generalizing findings to mostly small, private, single business professional organizations yields limited descriptive or predictive power. For example, the labor intensiveness and knowledge based work of the PSF largely precludes efficiencies attained through economies of scale (Maister, 1984a). Pecuniary economies or market power are similarly limited due to the need to avoid professional conflict of interest, e.g., law firms can not represent both parties in an adversarial matter. This is one

reason for the fragmented nature of most professional industries (Porter, 1980)³.

Issues concerning the use of internal versus external development by professional service firms remain largely unexplored. In Reid's (1968) study of bank mergers, those banks using merger as a growth mechanism enlarged themselves considerably more than banks that depended upon pure internal growth. However, in the nonmerger banks, growth was on the average more profitable and, Reid surmised, more orderly. Though not empirically determined, Maister (1985b, p.3) has identified slow growth, minimal use of lateral entry, and avoidance of merger as being characteristic of the "one-firm firm", a model he describes as being marked by "a remarkable degree of institutional loyalty and group effort that is clearly a critical ingredient in their success". Examples of such firms are the investment banking firm of Goldman Sachs, the management consultanting firm McKinsey, the accounting firm of Arthur Anderson, and the law firm of Latham & Watkins, all of which are among the most profitable in their fields, and all of which, by industry standards, are large.

Organization and strategy literature addressing the internal versus external development decision focuses on two primary factors widely assumed to influence this choice: start-up costs and time.

³An exception to this statement is the accounting industry, which is dominated by eight megafirms commonly referred to as The Big Eight.

Start-up Costs

Start-up costs take two forms, tangible and intangible. Tangible costs include expenditures for product development and introduction and for new facilities. Intangible costs include such considerations as patents, trademarks, exclusive distribution channels, product image, and specialized skills.

Tangible costs: Internal Development. In his examination of internal corporate venturing, Biggadike (1979) found that, on average, corporate ventures suffer severe losses the first four years, and that new ventures take eight years before reaching profitability and ten to twelve years before the ROI of those ventures will equal that of mature businesses. These figures are unlikely to have correspondence to law firms. Tangible costs for law firm internal development need to be considered separately for practice development and market development. For the former, start-up cost may be minimal. Because the practice and the person are in a real sense synonymous, development costs may be limited to the cost of providing training to one individual, with no cost at all incurred for physical plant. In addition, profitability is largely a function of efficiency. That is, a transaction would fail to be profitable only if professional time could not be billed to the client, i.e., if inexperience resulted in lost time. While such a situation may occur early on, it is unlikely that the eight year figure has meaning in this case. Moreover, professional time can be devoted to matters other than the new practice as demand warrants, though some billable

time will be lost to activities devoted to providing client exposure to the new practice area.

Market development, in which firm members are transferred to a new location to open a branch office, presents a different and opposite set of conditions. Under these circumstances, costs would be incurred for physical facilities but not for development, as firm professionals already have the necessary knowledge technology. Branch offices, however, may well require time to reach profitability. Here it is the time necessary to build up the practice, i.e., procure clients, that is at issue. However this situation too is mitigated, since market development is often undertaken in response to existing client need.

Tangible costs: Lateral Entry and Merger: The cost of diversification by external mechanisms is different for lateral entry and merger, as well as for practice and market development. In the case of lateral entry, the cost of practice development is equal to the lateral entrant's negotiated draw, i.e., the amount of annual compensation from partnership profits promised to the incoming partner. The value of a lateral is weighed against that lawyer's revenue generating potential. In hiring a lateral entrant, the firm is paying for that potential, i.e., for experience and business-getting ability, in the expectation that the lateral entrant will generate sufficient revenue to cover and exceed the negotiated draw. Indeed, the promise of additional revenues brought to a firm by the business that accompanies acquired

attorneys may itself provide a rationale for external growth. Of course, when expected revenues are not forthcoming the firm incurs the costs of supporting acquired partners. An extreme example is the late 1987 collapse of Finley, Kumble, Wagner, Underberg, Manley, Myerson & Casey, the nation's fourth largest law firm, which was due in large part to excessive debt incurred for high profile lawyers hired laterally who failed to produce expected revenues (Shipp, 1987). When a branch is opened with lateral entrants (or with some mix of lateral entrants and existing firm members, as is often the case), costs also include office space.

Merger for practice development generally imposes costs for a new physical plant, which expense is generally contributed to proportionally by the merging firms, whereas merger for market development avoids those additional costs, as branch offices are already established. In the case of market development costs will also be incurred, as with lateral entry, for the branch partners, since as a general rule lawyers in the firm becoming the branch generally negotiate upward their draw. There are, of course, also costs attached to the merger process itself, such as search and closing costs (Reid, 1968).

Tangible costs of practice and market development are presented in Table 3.

Table 3
Tangible Costs of Practice and Market Development

	<u>Practice Development</u>	<u>Market Development</u>
<u>Internal Development</u>	• Training • Unbillable time	• Space • Unbillable time
<u>Lateral Entry</u>	• Negotiated draws	• Space • Negotiated draws • Unbillable time
<u>Merger</u>	• Space • Cost of process	• Negotiated draws • Cost of process

Intangible costs. Intangible costs create barriers to entry due to the difficulty (if not impossibility) of duplicating the favorable conditions represented by the costs internally within reasonable cost and time limits (Porter, 1980). Intangible costs applicable to law firms include specialized skills and, broadly conceived, product image. The former may include expertise in a highly specialized area of practice, e.g., products liabilities, expertise in regional law, or even a network of important contacts. Product image applied to legal services can be thought of as the reputation of the firm or of the individual practitioner. Intangibles are thus equally important to law firm product and market development. Indeed, intangibles are also a factor in the choice of growth mechanism for the expansion of existing practice areas, insofar as the reputation of a lawyer is a factor in considering lateral entry for that growth strategy.

Time

The time factor is commonly argued to influence the choice between internal and external diversification. As a general rule, diversification by acquisition is considered appropriate when quick entry is important (Fray, Gaylin & Down, 1984). The perception that time is important to law firm growth may be related to several threats and opportunities faced by law firms.

One condition that may create a perceived threat to firm survival and the concomitant desire to grow quickly is size. Small and midsize firms face many of the obstacles of smallness previously discussed. Firms in the midsize category often have additional problems germane to being midsize, such as cash flow problems due to overhead costs such as space and computer systems (particularly when these are not yet fully utilized), as well as high associate salaries (Hildebrandt, 1987). In short, midsize firms have often reached a transition point where they have "big firm" expenses while still doing "small firm" business. Compared to small and midsize firms, large firms realize greater profits due to higher fees (large firms attract more profitable work), higher leverage, and slightly higher utilization (since firms with many small clients must spend a higher proportion of partner time on business-getting) (Maister, 1984a). The result of these conditions is that small and midsize firms may feel pressured to accomplish the transition to large size quickly.

While growth is often conducive to planned internal

development, whereby practice area departments anticipate their professional needs and numbers of associates are hired accordingly, the slow growth available through the internal development mechanism may not be adequate to reduce the risks attendant to small size or to allow timely response to emerging business opportunities. The perception that rapid growth is necessary to attain or enhance a competitive position is therefore likely to contribute to the use of external mechanisms for expansion.

A more germane condition than size per se to firm vulnerability may be the number of the firm's practice areas that are not profitable. Firms often have one or more practice areas that exist to support others, such as a trusts and estates department that primarily provides service to clients who use the services of the corporate department. Thus, the unprofitable practice area contributes to the firm only indirectly. To the extent that a firm's practice areas are profit-generating, members may be less likely to perceive size as constituting a threat to survival. On the other hand, when a firm's profit-generating departments financially carry many non-profitable departments, dissatisfaction among members of the profit-generating departments may result, leaving the firm vulnerable to the departure of critical members or the splitting off of whole departments. Hence limitations in both size and number of profit-generating practice areas may lead to the use of external mechanisms for rapid growth.

A related and critical threat facing law firms is that weakened partnership bonds (Goldner, 1987) have increased the difficulty of holding on to key partners who are solicited to join other firms that can offer them higher incomes and/or other advantages. Opening up of the market has allowed some firms to successfully divest others of experts in specialist fields and of other major business-getters or "rainmakers". The loss of rainmakers has often meant dissolution, even for firms which were economically sound (Goldner, 1987). Frequently, this threat is more problematic for small and midsize firms than for large ones. Again, however, it is not size per se that creates the vulnerability but reliance on a small number of members to bring in business. Hence, firms that rely on a small number of rainmakers to bring in a large proportion of the firm's business may perceive a need to grow by using the external mechanisms in order to increase the number of rainmakers in the firm.

Growth Mechanisms and Profitability

Attention paid to the relationship between internal and external growth mechanisms and firm profitability outcomes has been directed toward the relative performance of merger versus non-merger firms. Because merger and acquisition are treated virtually synonymously in the strategy literature, no empirical investigation has been conducted assessing the differences between the two external mechanisms in affecting profitability. However, numerous studies by strategy and finance researchers have been undertaken in an attempt to discern the merger-profitability relationship.

Results of these studies are contradictory and inconclusive. On the one hand, researchers report that a wealth gain does accrue to shareholders as a result of merger (Chatterjee, 1986; Lev & Mandelker, 1972; Weston & Mansinghka, 1971), while other results show the effect of merger on profitability to be neutral or negative (Davidson, 1985; Hogarty, 1970; Meeks, 1977; Melicher & Rush, 1974; Singh, 1971). Perhaps the largest study of merger determinants and effects is reported by Mueller (1980), whose international study demonstrated no consistent pattern of improved or deteriorated profitability across countries studied.

The lack of success of recent mergers is reflected in estimates which indicate that half to two-thirds of all mergers don't work (Business Week, 1985). In searching for an explanation for unsuccessful mergers, i.e., neutral or

negative profitability outcomes, organization researchers have recently begun to look beyond the question of strategic fit. One area of investigation has been a consideration of the influence of a poorly conducted pre-acquisition analysis and negotiation process. McCarthy (1963) points out that the pre-acquisition process frequently focuses on strategic fit and largely excludes consideration of organizational fit, i.e., fit of structure, systems, and processes. Haspeslagh & Jemison (1987) provide one explanation for such exclusion; they suggest that key issues are left unresolved because dissimilar interests combine with pressure to reach agreement, causing parties to "agree to disagree". Other dysfunctional characteristics of the pre-merger process include the independent goals of specialists and analysts and escalating commitment toward closing a deal that can force premature closure and limit consideration of critical issues (Jemison & Sitkin, 1986). More generally, the pre-acquisition process is hindered by the difficulty of making sound decisions under the uncertainty, fast pace, and high pressure inherent in that process (Fray, Gaylin, & Down, 1984).

Other interpretations have focused on the adequacy of the post-acquisition integration process (Finkelstein, 1986; Kitching, 1967; Marks & Mirvis, 1985; Mirvis & Marks, 1986; Shrivastava, 1986). According to Shrivastava (1986), integration must occur at three levels: the initial integration of procedures, i.e., the combining of accounting systems and creation of a single legal entity; the integration of physical

assets, product lines, production systems, and technologies; and, finally, cultural integration. While threats to merger success may stem from any level, the latter is considered by some to be most difficult and most critical of the three to merger success (Buono, Bowditch, & Lewis, 1985; Shrivastava, 1986). As such, it has become a subject of recent interest (Marks, 1982; Malekzadeh & Nahavandi, 1987; Sales & Mirvis, 1984).

The importance of firm culture and identity (Albert & Whetten, 1985) is of particular significance in the legal profession, where the related (albeit changing) traditions of promotion-from-within, one-firm careers, and owner (partner) management have resulted in the pronounced unity of and commitment to firm ideology, management philosophy, ritual, etc. The dilution of identity by merger is often anathema to law firm professionals. Moreover, in addition to the integration problems inherent in any corporate merger, law firms must attend to concerns specific to professional organizations, such as client conflict of interest. A summary of potential sources of merger trouble for law firms catalogued by Africa (1987, p.50) includes "increased risk brought on by the assumption of unwieldy debt, loss of autonomy, increased bureaucracy and accountability, increased overhead for the smaller of the two entities, higher billing rates, incompatibility of firm cultures and/or of client-attorney mixes, incompatible management styles and/or working styles, lack of sufficient monetary benefit, and firm

chemistry not 'rich' enough to help the new entity overcome start-up problems".

As with the diversification literature, the main body of this research makes a limited contribution to an understanding of the outcomes of law firm merger activity. For one reason, studies have focused on large acquisitions, i.e., \$10 million in assets or more (Steiner, 1975). At an even more basic level, these studies do not apply to law firm mergers because they do not investigate mergers at all, i.e., they investigate acquisitions. This circumstance is quite understandable in light of the rarity of what Boisi and O'Toole (1987) refer to as "mergers of equals". These writers characterize such mergers as being

those combinations or amalgamations of two business entities in which neither side "purchases" the other, entities of approximately equal "size" (defined primarily in terms of relative contribution to sales, earnings, book value, market value, and dividend yield) join to form a larger organization governed by a management team representative of the two firms' former managements, and neither side receives an acquisition premium...Each company is contributing its assets, both financial and human, to create a new enterprise that will, in the longer term, benefit each...in a more assured manner and with greater return potential than each enjoys as an independent entity. Neither company is "selling" control: each is seeking to build on the other's strengths without losing its own identity (p.360).

The introduction of new products to existing markets and the expansion of geographic markets are explicitly recognized as motivations for such mergers. Thus, except that law firm mergers usually involve firms of unequal size, this

description adequately represents virtually all law firm mergers. However, mergers of equals comprise a very small component of contemporary mergers and acquisitions activity (Boisi and O'Toole, 1987).

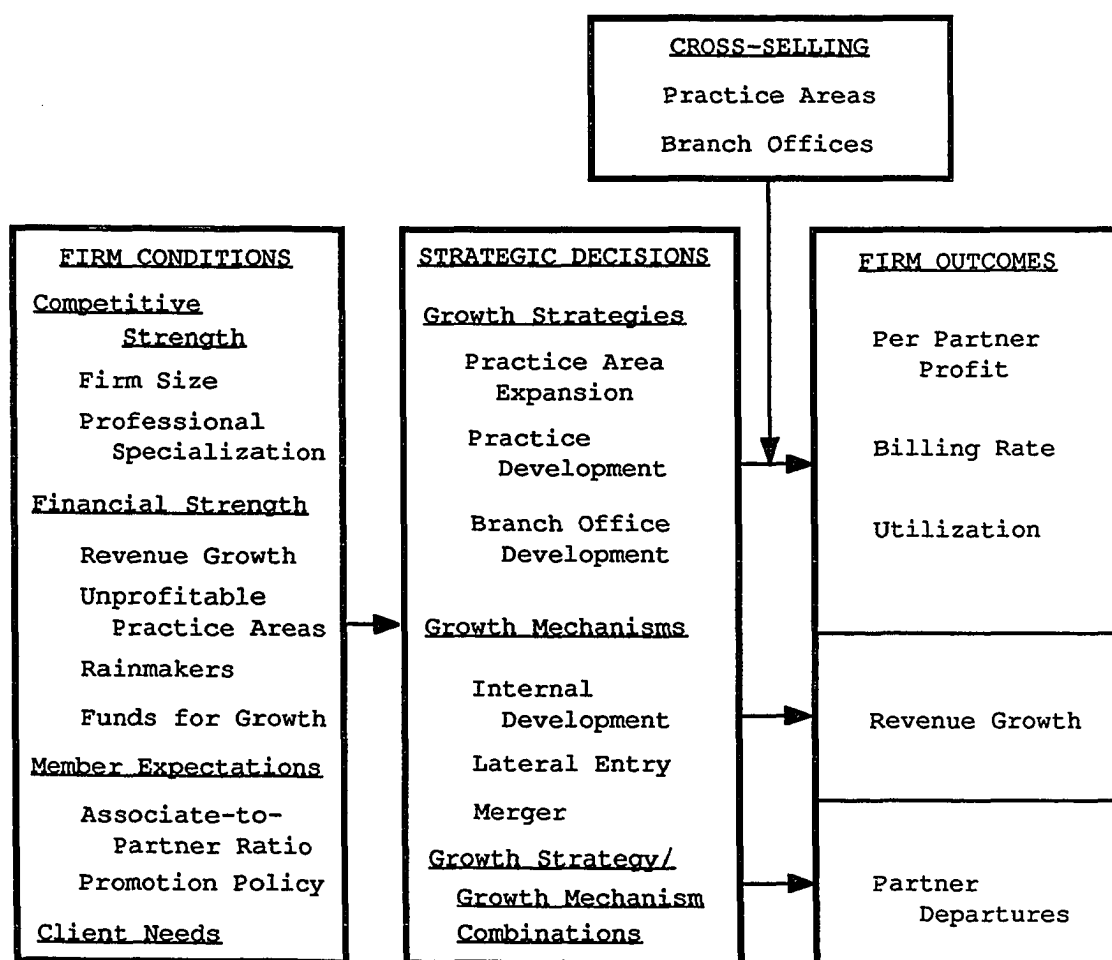
CHAPTER 3 RESEARCH MODEL AND HYPOTHESES

The previous chapters have developed the conceptual and theoretical underpinnings for the proposed model and hypotheses. In this chapter, three sets of hypotheses are presented concerning the effect of firm conditions on growth decisions, relationships between growth strategies and growth mechanisms, and the effect of strategic decisions on profitability and partner departure outcomes.

Set 1 addresses the influence of determinant organizational conditions on law firm growth decisions. Hypotheses predict the relationship of firm conditions in the areas of competitive strength, financial strength, member expectations, and client needs, to choices among growth strategies, among growth mechanisms, and among strategy/mechanism combinations. Set 2 investigates patterns of growth by the nine strategy/mechanism combinations. Here, it is assumed that the advantages and disadvantages of the growth mechanisms result in the greater usage of some mechanisms than others in implementing each strategy. Hypotheses predict the mechanisms expected to be dominant for each strategy. The final set of hypotheses, Set 3, concerns the consequences of strategic decisions. The majority of hypotheses predict the effects of strategic decisions on economic outcomes, including annual growth in revenue and longer run effects on per partner profit. In addressing long run profitability, the moderating influence of cross-selling on practice and branch office

development is posited. Hypotheses are also developed for the relationship between strategic decisions and partner departures. Figure 3 depicts the hypothesized relationships.

Figure 3
Strategic Decision Model



The remainder of this section presents the three sets of hypotheses.

Firm Condition - Strategic Decision Relationships

In this set, relationships are hypothesized between the law firm conditions and strategic behaviors. Determinant conditions are categorized as competitive strengths, financial strengths, member expectations, and client needs. The general form of the hypotheses is to predict the relationship of the determinants to strategies, to mechanisms, and then to the strategy/mechanism combinations. However, adherence to this form is restricted by substantive considerations which have limited the number of hypotheses developed for each determinant in two ways. First, most firm conditions are considered to influence either the undertaking of a strategy or the choice of a mechanism, but not both. Therefore, for most predictors, hypotheses are developed for either strategy or mechanism criterion variables, not both. Second, hypotheses developed for the relationship of firm conditions to strategy/mechanism combinations are similarly limited by substantive considerations, such that all nine possible combinations are not tested for each predictor variable. For example, where firm characteristics concern only the principal office, hypotheses are not developed for strategic options that include the development of branch offices.

Competitive Strength

One reason why law firms grow is to improve competitive position. General practice corporate firms need adequate

size and breadth in order to compete effectively in the current legal environment.

Size. Law firms attempt to become large in order to increase advantages and decrease disadvantages associated with size. Smaller firms may be particularly vulnerable to such threats, and hence may choose to engage in lateral entry and merger in order to achieve rapid and substantial increases in the size of the existing practice.

Large firms face their own pressures to expand. In order to become more "full service", large firms add practice areas. Since experienced attorneys offer immediate legitimacy in the new field, as well as existing clients, it is expected that expertise will be developed laterally and by merger. Large firms also add branch offices in order to have a presence in all major business markets. Branch offices developed by lateral entry and merger are immediately operational and provide the additional advantage of local expertise. On the other hand, concern with quality control and firm culture motivates some firms to develop branch office by transferring existing partners to new locations. Therefore, large firms are expected to open branch offices by all three mechanisms. In sum, it is predicted that:

- Size is negatively related to the expansion of existing practice areas and positively related to the development of new practice areas and branch offices.

- Size is negatively related to lateral entry and merger and not significantly related to internal development.

- Size is negatively related to the expansion of existing practice areas by lateral entry and merger; positively related to the development of practice areas by lateral entry and merger; and positively related to the development of branch offices by all mechanisms.

Professional specialization. Legal practice areas have become increasingly complex and interdependent. Hence, many specializations that were once the exclusive domain of small specialist firms, e.g., divorce law and environmental law, are being practiced in large firms as well. In addition, the sheer number of fields of law has greatly increased. As a result of the redistribution and profusion of practice areas within the legal profession, the general practice firm needs to substantially increase the breadth of its practice in order to stay competitive. Therefore, we can expect the firm with a narrow range of practice areas to develop new fields of practice. Lateral entry and merger should be preferred mechanisms for developing new practice areas when immediate expertise and established clients are important. However, practice development by current attorneys, who move incrementally into new areas of expertise while maintaining their existing practice, is also expected. Since the scope of a firm's practice should have a bearing only on the practice development strategy, it is hypothesized that:

- Professional specialization is negatively related to the development of practice areas and not significantly related to the expansion of existing practice areas or to the development of branch offices.

- Professional specialization is negatively related to the development of practice areas by internal development, lateral entry and merger.

Financial Strength

Financial considerations both impel and impede growth decisions. Growth may be a means to increase firm revenues, to improve the profitability of practice areas, or to develop rainmakers, i.e., attorneys who generate and sustain client business for the firm. At the same time, the unavailability of sufficient funding can inhibit growth choices.

Revenue Growth. A potential advantage of growth by the external mechanisms is that acquired attorneys bring new client business to the firm. Firms seeking to increase revenue growth may thus use the lateral entry or merger mechanisms as a means of generating income. New attorneys may have either existing or new areas of expertise, and therefore contribute to the expansion of existing practice areas or the development of new ones. This suggests the following hypotheses:

- Revenue growth is negatively related to lateral entry and merger and not significantly related to internal development.

- Revenue growth is negatively related to the expansion of existing practice areas and the development of practice areas by lateral entry and merger and not significantly related to the expansion of existing practice areas or the development of practice areas by internal development.

Unprofitable practice areas. Law firms often have practice areas that are minimally or not at all profitable. The need for profit-generating departments to carry practice areas that do not generate profits may cause dissatisfaction among members in the profit-generating departments, leaving the firm vulnerable to the departure of critical members or of whole departments. Acquiring lateral partners or merging may be perceived as necessary to strengthen the firm's practice and reduce vulnerability. New partners may be brought into existing unprofitable areas in order to improve their economic performance, or new areas may be entered in order to strengthen the firm's practice. Therefore, the following hypotheses are proposed:

- Percentage of unprofitable practice areas is positively related to lateral entry and merger and not significantly related to internal development.

- Percentage of unprofitable practice areas is positively related to the expansion of existing practice

areas, and the development of practice areas by lateral entry and merger and not significantly related to the expansion of existing practice areas and the development of practice areas by internal development.

Rainmakers. Dependence on a limited number of rainmakers makes a firm vulnerable to the loss of a small number of critical members. Firms in this position can be expected to attempt to decrease vulnerability by bringing in rainmakers through external mechanisms. Since each office of a multi-branch firm competes in its own geographical market, the addition of rainmakers in one office does not reduce the vulnerability of any other. Thus, relevant growth is that within a single location, and the following hypotheses concern the principal office:

- Reliance on rainmakers is positively related to lateral entry and merger and not significantly related to internal development.

- Reliance on rainmakers is positively related to the expansion of existing practice areas and the development of practice areas by lateral entry and merger and not significantly related to the expansion of existing practice areas and the development of practice areas by internal development.

Funds for Growth. Costs attached to growth mechanisms can be expected to influence choices among them for implementing the

growth strategies. The acquisition of lateral partners with valuable expertise and/or a strong client base can require the firm to provide a sizable partnership draw, such that both practice area expansion and practice development are less costly through internal development. Merger, too, is expensive, making financial capability a factor for firms seeking to merge in order to reduce vulnerability stemming from small size. Branch office development has considerable cost attached to both internal and external mechanisms, and is therefore unlikely to be undertaken at all by firms with financial constraints.

For any strategy, the ready availability of funds for growth is not expected to limit the use of internal development where it is desired, especially insofar as internal development is necessary to satisfy career expectations of junior members. Therefore, it is predicted that:

- Financial constraints are negatively related to lateral entry and merger, and not significantly related to internal development.

- Financial constraints are negatively related to the expansion of existing practice areas and the development of practice areas by lateral entry and merger; negatively related to the development of branch offices by all mechanisms; and not significantly related to the expansion of existing practice areas or the development of practice areas by internal development.

Member Expectations

The way in which law firms grow is also a function of the preferences and expectations of firm members. Pressures imposed by the career expectations of associates, and the degree to which partners commit the firm to a policy of making partners from within will influence growth decisions.

Associate-to-partner ratio. The tradition of promotion-from-within creates an imperative for law firms to promote associates to partnership positions at a competitive rate or risk reducing the commitment and motivation of existing associates and jeopardizing the recruitment of new ones. However, the pressure for growth by internal development resulting from the internal labor market career structure is mitigated by factors that make the external mechanisms preferable to internal development, under some conditions, for practice development and branch office development strategies. Therefore, it is expected that associate-to-partner ratio will influence internal development and not lateral entry or merger, and that such influence will be limited to promotions within existing practice areas, and it is proposed that:

- Associate-to-partner ratio is positively related to internal development and not significantly related to lateral entry or merger.
- Associate-to-partner ratio is positively related to the expansion of existing practice areas by internal develop-

ment and not significantly related to the development of new practice areas and the development of branch offices by internal development.

Promotion policy. Longstanding norms governing law firm partnership have weakened considerably, and the degree to which firms conform to the tradition of making partners by promotion varies widely. It is expected that firms with a commitment to traditional practices will make new partners by promotion, enter new fields by developing new legal skills, and transfer attorneys to open new offices. Conversely, firms that do not value such policies concerning growth are expected to pursue expansion with more lateral entry and merger. Consequently, it is hypothesized that:

- Commitment to promotion is positively related to internal development and negatively related to lateral entry and merger.

- Commitment to promotion is positively related to the expansion of existing practice areas and the development of practice areas and branch offices by internal development; and is negatively related to the expansion of existing practice areas and the development of practice areas and branch offices by lateral entry and merger.

Client Demand

Clients propel growth as they develop legal needs for services in practice areas or geographic markets the firm has

not yet entered. Historically, law firms had monogamous relationships with clients, and grew concomitantly with clients in response to demand for additional services. More recently, bonds between law firms and their corporate clients are weakened, and law firms increasingly enter new practice areas and open branch offices in order to be competitive. Nonetheless, opportunities resulting from client needs are more certain, and therefore more likely to be compelling, than perceived market opportunities. Therefore, it is expected that client demand remains the primary source of growth opportunity for law firms and it is hypothesized that:

- Client need for services in legal fields in which the firm does not practice influences the development of practice areas.
- Client need for legal services in cities where the firm does not practice influences the development of branch offices.

Set 1 hypotheses are listed below by growth strategy, growth mechanism and strategy/mechanism combination.

Hyp. 1. Organizational conditions are significantly related to the expansion of existing practice areas, the development of practice areas, and the development of branch offices.

- Hyp. 1A. The expansion of existing practice areas is negatively related to firm size
- Hyp. 1B. The development of practice areas is
- (a) positively related to firm size
 - (b) negatively related to number of practice areas
- Hyp. 1C. The development of branch offices is positively related to firm size
- Hyp. 1D. The amount of development of practice areas and branch offices due to client demand is significantly greater than the amount of development of practice areas and branch offices due to practice demands or other demands.
- Hyp. 2. Organizational conditions are significantly related to internal development, lateral entry and merger.
- Hyp. 2A. Internal development is
- (a) positively related to associate-to-partner ratio
 - (b) positively related to commitment to promotion
- Hyp. 2B. Lateral entry is
- (a) negatively related to size
 - (b) positively related to reliance on rainmakers
 - (c) negatively related to revenue growth
 - (d) positively related to unprofitable practice areas
 - (e) negatively related to financial constraints
 - (f) negatively related to commitment to promotion

Hyp. 2C. Merger is

- (a) negatively related to size
- (b) positively related to reliance on rainmakers
- (c) negatively related to revenue growth
- (d) positively related to unprofitable practice areas
- (e) negatively related to financial constraints
- (f) negatively related to commitment to promotion

Hyp. 3. Organizational conditions are significantly related to strategy/mechanism combinations.

Hyp. 3A. The expansion of existing practice areas by internal development is

- (a) positively related to associate-to-partner ratio
- (b) positively related to commitment to promotion

Hyp. 3B. The expansion of existing practice areas by lateral entry is

- (a) negatively related to size
- (b) positively related to reliance on rainmakers
- (c) negatively related to revenue growth
- (d) positively related to unprofitable practice areas
- (e) negatively related to financial constraints
- (f) negatively related to commitment to promotion

Hyp. 3C. The expansion of existing practice areas by merger is

- (a) negatively related to size

- (b) positively related to reliance on rainmakers
 - (c) negatively related to revenue growth
 - (d) positively related to unprofitable practice areas
 - (e) negatively related to financial constraints
 - (f) negatively related to commitment to promotion
- Hyp. 3D. The development of practice areas by internal development is
- (a) negatively related to professional specialization
 - (b) positively related to commitment to promotion
- Hyp. 3E. The development of practice areas by lateral entry is
- (a) positively related to firm size
 - (b) negatively related to professional specialization
 - (c) positively related to reliance on rainmakers
 - (d) negatively related to revenue growth
 - (e) positively related to unprofitable practice areas
 - (f) negatively related to financial constraints
 - (g) negatively related to commitment to promotion
- Hyp. 3F. The development of practice areas by merger is
- (a) positively related to firm size
 - (b) negatively related to professional specialization
 - (c) positively related to reliance on rainmakers

- (d) negatively related to revenue growth
 - (e) positively related to unprofitable practice areas
 - (f) negatively related to financial constraints
 - (g) negatively related to commitment to promotion
- Hyp. 3G. The development of branch offices by internal development is
- (a) positively related to size
 - (b) positively related to firm commitment to promotion
 - (c) negatively related to financial constraints
- Hyp. 3H. The development of branch offices by lateral entry is
- (a) positively related to size
 - (b) negatively related to firm commitment to promotion
 - (c) negatively related to financial constraints
- Hyp. 3I. The development of branch offices by merger is
- (a) positively related to size
 - (b) negatively related to firm commitment to promotion
 - (c) negatively related to financial constraints

Growth Strategy - Growth Mechanism Relationships

The following hypotheses concern the relationship of growth strategies to growth mechanisms. In the previous set, hypotheses were developed to examine the influence of individual determinant conditions on firm growth. The objective of this set is to discern patterns of growth that emerge as a result of the advantages and disadvantages of particular growth mechanisms for enacting each growth strategy. Hypotheses predict the growth mechanism expected to be used most frequently to accomplish each growth strategy.

Practice Area Expansion.

The strong tradition in the legal profession of promotion-from-within suggests that, in the absence of mitigating factors such as the need or desire for rapid expansion, the preferred mechanism for growth is internal development. Routine growth of the existing practice is incremental; expansion does not need to be rapid and growth related to the practice area expansion strategy is likely to occur through internal development. Under certain circumstances lateral entry may also be used to expand existing practice area departments, such as when the firm has an insufficient number of partners to handle increasing business and no one to promote or when there is an opportunity to acquire a good rainmaker. To the extent that an increase in

size alone is perceived to be beneficial, the use of merger to enlarge existing practice areas may also be considered appropriate; however the difficulties of integration make merger less desirable than the acquisition of lateral partners. Based on these arguments the following hypotheses are proposed:

- The expansion of existing practice areas is more often accomplished by internal development than by lateral entry or merger.
- The expansion of existing practice areas is more often accomplished by lateral entry than by merger.

Practice Development

Practice development can be achieved through internal development when timeliness is not a critical consideration, or more quickly through lateral entry or merger when speed is perceived to be necessary or desirable. Both lateral entry and merger, but particularly merger, have costs attached. These include not only the operating and capital costs of negotiated salaries and new office space, but the dysfunctional negative influence on the motivation of existing associates and potential pitfalls of the integration process as well. In addition, the option for merger depends in part on the availability of merger candidates (Yip, 1982). Taking into consideration the ease and rapidity of acquiring expertise as opposed to developing it, and the various costs

and integration problems of the merger mechanism, it is hypothesized that:

- The development of practice areas is more often accomplished by lateral entry than by internal development or merger.
- The development of practice areas is more often accomplished by internal development than by merger.

Branch Office Development

Branch offices are opened in response to a perceived need or desire to achieve competitive advantage by being in key business markets or key client locations. A quick start-up time may be important in responding to such opportunities, and the external mechanisms offer the advantages of an up and running operation and existing client base. However, integration difficulties associated with merger, and to a lesser extent with lateral entry, make it difficult to maintain control of acquired branches, i.e., to assure uniformity of the practice across offices and to maintain firm culture. Because of the importance of these professional issues, it is predicted that:

- The development of branch offices is more often accomplished by internal development than by lateral entry or merger.
- The development of branch offices is more often accomplished by lateral entry than by merger.

Set 2 hypotheses are listed below.

Hyp. 4 Growth strategies are significantly related to growth mechanisms.

Hyp. 4A. The expansion of practice areas is

- (a) significantly greater by internal development than by lateral entry or merger, and
- (b) significantly greater by lateral entry than by merger

Hyp. 4B. The development of practice areas is

- (a) significantly greater by lateral entry than by internal development or merger, and
- (b) significantly greater by internal development than by merger

Hyp. 4C. The development of branch offices is

- (a) significantly greater by internal development than by lateral entry or merger, and
- (b) significantly greater by lateral entry than by merger

Strategic Decision - Firm Outcome Relationships

The final set of hypotheses addresses the outcomes of growth decisions. The primary focus of investigation is the influence of growth strategy on short and long run economic consequences; annual changes in revenue and increases in per partner profitability over the full five year period of the study are examined. The influence of growth mechanisms on the rate of partner departures from the firm is also considered.

Revenue Outcomes

Like other professional service firms, law firms compete on the basis of quality; therefore their emphasis is on producing revenue rather than cutting costs. Revenue is thus an important factor in law firm economics. Indeed, firms that generate the most revenue are also among the most profitable (Brill, 1985, 1986, 1987, 1988).

Perhaps even more directly, revenue is indicator of firm size; as in other industries, larger law firms have higher gross revenues. It follows from this that revenue growth should be related to firm growth. Indeed, the relationship between revenue growth and growth that accrues from increases in the number of attorneys generating revenue for the firm is tautological. However, there is no a priori reason to assume that the same result will obtain as an outcome of increased practice area or geographical breadth. Rather, the economic

contribution of practice and branch office development will depend on the value added to the firm by diversifying into new legal fields and cities. Applied to the growth strategies, this means that an increase in revenue is expected to result from practice area expansion, i.e. from increasing the size of the partnership, but not necessarily from practice or branch office development, i.e., from increasing the scope of the practice. Following the same reasoning, revenue growth should also result from growth by any mechanism, given that all serve to increase the size of the membership, albeit by different means. Consequently, the following relationships between revenue growth and firm growth are expected:

- Revenue growth is positively related to practice area expansion and not significantly related to the development of practice areas or branch offices.
- Revenue growth is positively related to internal development, lateral entry, and merger.

Profitability Outcomes

Conventionally, the basic measure of profitability in law firms, as in professional service firms generally, has been net income per partner. Because profitability includes expenses as well as revenues, per partner profit is a more accurate reflection of the economic benefits of the strategic growth options than is revenue. Moreover, the longer measurement period used to examine the growth-profit relationships reduces the degree to which the adjustment period of new

partners and the start-up phase of new practice areas and branch offices distort the extent of their economic contribution. In the preceding hypotheses, increases in revenue were proposed to result largely from increasing size; therefore, the growth mechanisms were posited to play a major role in influencing revenue. Given the differences between the two economic measures, it is expected that, in contrast to revenue, per partner profitability will be influenced primarily by growth strategies.

Practice Area Expansion. Key factors that comprise per partner profitability include leverage, utilization, billing rate, realization, and margin (Maister, 1984a). Growth alone is not expected to affect this profitability measure. As the amount of business conducted by a firm increases, additional lawyers are needed to handle that work. In this way, an increased work load allows associates to become partners and more associates to be hired. However, while this growth supports the promotional structure of the law firm, and thus is a valid organizational goal, it has no effect on any of the five components of per partner profit. That is, additional revenues are generated, but additional professionals are then needed who will share in those revenues. Hence, per partner profit will not change. Based on this reasoning, it is predicted that:

- The expansion of existing practice areas is not significantly related to per partner profit.

Cross-selling. The cross-selling of services, i.e., multiple practice area use and multi-site use by clients, has the potential for increasing profitability in two ways. First, by creating greater client dependence on the firm, cross-selling increases the value of the firm to the client and allows the firm to increase billing rates. Second, cross-selling has the potential to improve utilization by reducing time spent on business-getting, hence increasing available billable hours. Therefore, cross-selling is hypothesized to moderate the relationships between practice development and branch office development and per partner profit, billing rate, and attorney utilization. Hypotheses are presented below.

Practice Development. New practice areas can be developed through any of the internal or external growth mechanisms, each with its own advantages and disadvantages. While the disadvantage of a greater initial cost of the external mechanisms has been argued to be a factor in the choice of mechanism, the impact of cost on profitability factors should be eliminated once the start-up period has passed. At that point, it can be expected that the firm that has moved into new practice areas, and has increased the number of services used by clients by cross-selling old and new practice areas, has increased the value of the firm to its clients. Thus, it is predicted that:

- In the presence of cross-selling, the development of practice areas is positively related to utilization, billing rate, and per partner profit.

- In the presence of cross-selling, the development of practice areas by internal development, by lateral entry, and by merger are positively related to utilization, billing rate, and per partner profit.

Branch Office Development. Like the practice development-profitability relationship, the market development-profitability relationship is proposed to be moderated by cross-selling. Though the initial costs of the external mechanisms may influence choices about their use, profitability is not expected to be affected following start-up. As with practice development, the advantages that accrue from the cross-selling of branches should enhance the value of the firm to the client. However, given that the cross-selling of firm offices is usually from the principal office to the branches, increased utilization is not expected to result. Hence, the following relationships are predicted:

- In the presence of cross-selling, the development of branch offices is positively related to billing rate and per partner profit.

- In the presence of cross-selling, the development of branch offices by internal development, by lateral entry, and by merger are positively related to billing rate and per partner profit.

Departure Outcomes

Law firm culture has traditionally been characterized by the lifetime commitment of partners to the firm. The movement away from promotion-from-within and toward growth through the external mechanisms has served to diminish those bonds. Law firms that embrace norms which accept lateral movement by attorneys should also be expected to experience partner departures. Where firm loyalty is less valued, partners will be more likely to leave for more lucrative or otherwise rewarding practice opportunities. This reasoning suggests that:

- Growth by internal development is negatively related to partner departure.
- Growth by lateral entry is positively related to partner departure.
- Growth by merger is positively related to partner departure.

Set 3 hypotheses are listed below.

Hyp. 5. Revenue growth is significantly related to growth strategies and growth mechanisms.

Hyp. 5A. Revenue growth is positively related to practice area expansion and not significantly related to practice development or branch office development

Hyp. 5B. Revenue growth is positively related to internal development, lateral entry, and merger

Hyp. 6. The expansion of existing practice areas is not significantly related to per partner profit.

Hyp. 7. Cross-selling moderates the relationship between practice development and profitability.

Hyp. 7A. In the presence of cross-selling, the development of practice areas is positively related to utilization, billing rate, and per partner profit

Hyp. 7B. In the presence of cross-selling, the development of practice areas by internal development, by lateral entry and by merger are positively related to utilization, billing rate, and per partner profit

- Hyp. 8. Cross-selling moderates the relationship between market development and profitability.
- Hyp. 8A. In the presence of cross-selling, the development of branch offices is positively related to billing rate and per partner profit
- Hyp. 8B. In the presence of cross-selling, the development of branch offices by internal development, by lateral entry, and by merger are positively related to billing rate and per partner profit
- Hyp. 9. Growth mechanisms are not significantly related to per partner profitability
- Hyp. 10. Growth mechanisms are significantly related to partner departures.
- Hyp. 10A. Internal development is negatively related to partner departures
- Hyp. 10B. Lateral entry is positively related to partner departures
- Hyp. 10C. Merger is positively related to partner departures

CHAPTER 4 SAMPLE, MEASUREMENT AND DATA ANALYSIS

Sample

The focus and time frame of this research require that law firms included in the study meet several criteria. First, the study excludes firms that are specialty "boutiques", i.e., firms that limit their practice to one primary specialty area (e.g., products liabilities work). Such firms do not add practice areas and generally do not have branch offices. Second, the study excludes firms whose income derives primarily from contingency fee work. This type of firm, e.g., negligence firms, is not subject to the imperative for growth that results from the practice of leveraging, since contingency billing by definition precludes the ability to bill out the time of junior members for the economic benefit of seniors. In addition, firms that rely on contingency billing are frequently also specialist firms. The study therefore includes only firms that bill on a time basis. Third, the study has been limited to firms that are at least ten years old in order that they will have been in existence throughout the time frame measured, as discussed below.

Data were collected through structured interviews in a sample of New York City firms. The decision to use a limited local sample rather than a comprehensive national one was based on requirements imposed by the detailed, sensitive, and time lagged nature of the research data. The study attempts

an intensive investigation into the growth processes of law firms. As such, the research analyzes the contribution of certain organizational conditions to strategic growth decisions, the pattern of those decisions over time, and their profit-related outcomes. Gathering the data required first hand interaction with key people in the firms as well as access to financial records. The greater depth of understanding about law firm growth processes resulting from a smaller, concentrated study is more desirable than that which could be learned from a larger but necessarily more superficial study. Hence, the sample was drawn from the population of New York City law firms meeting the research criteria.

The study population was identified through listings in the 1988 New York volume of the Martindale-Hubbell Law Directory. The Martindale-Hubbell Law Directory is a directory of all lawyers practicing in the United States and has been published annually since 1931. The current eight volume directory lists individual lawyers and law firms by geographic region (city and state). Firm information includes firm name and address, members (the majority of listings specify whether members are partners or associates), fields of practice and branch offices. The principal source of information for the directory is a questionnaire completed by thousands of members of the legal profession. Other sources include reports from field representatives, newspaper clippings, bar association rosters and publications, correspondence, and reports by the National Conference of Bar

Examiners (Curran, 1971). Given the uniqueness and prestige of the directory and concomitant motivation for firms to respond to the Martindale-Hubbell, Inc. questionnaire, as well as the absence of any fee for inclusion in the directory,¹ the Martindale-Hubbell Law Directory can confidently be assumed to include virtually all firms of interest to this study.

A preliminary step in eliminating firms not meeting the research criteria from the study population was to exclude firms of fewer than twenty members. The rationale for this decision is the overwhelming presence of young, specialist and contingency firms in that size category. In addition, the 1978 Martindale-Hubbell was consulted to verify that firms had existed for at least ten years. These steps resulted in identifying a pool of one hundred thirty-eight firms. The sample was then drawn from those firms in the targeted population that agreed to participate in the study. Three attempts to elicit participation were made. An initial letter of introduction and summary of the research were sent to the managing or senior partner in each firm. The attorneys were then contacted by phone to request participation in the study. Two additional mailings were sent to firms not responding to the earlier communications, and follow-up calls were made to those firms. The final sample included sixty-one firms, a forty-four percent response rate.

¹The directory also contains a firm biographical section for which a fee is charged. Subscriber information includes individual lawyer biographies and a list of representative clients in addition to the information contained in the free line listings.

The vast majority of interview respondents were managing or senior partners; in a small number of cases the interviewee was the firm's director of administration. Data were gathered using an interview questionnaire designed for the research study. Data collection occurred in two or three steps, depending upon the accessibility of financial data during the interview. A set of preliminary questions was sent to the respondent prior to the interview. These queried the amount and type of growth, e.g., the number of lateral partners, elected partners, new practice fields, and new branch offices, between 1983 and 1987. At the interview, questions focused on organizational conditions posited in the research model to influence growth decisions, such as rainmaking strength and client need for new services. Profit data were requested during the interview as well. In some cases, respondents had the necessary data available immediately. In other cases, information was requested by the respondent from accounting personnel and were forwarded to the researcher subsequent to the interview.

Strategic growth decisions were tracked over the five year period from 1983 through 1987. Reasons for the choice of this time period are threefold. First, the years from 1983 through 1987 are within the time period posited to reflect changes in the legal profession that have been argued to result from the changing competitive conditions discussed in Chapter 1. Hence, it was felt that there was likely to be adequate variability in the use of internal and external

growth mechanisms within this period. Second, given that the law firms investigated in this study, i.e., multi-practice, time billing firms using associates for leverage, can be expected to increase in size annually, a five year time period could provide the opportunity to observe an adequate number of strategic growth decisions.

Finally, a five year period appropriately circumscribes the amount of time within which organizational conditions can be expected to influence strategy decisions and those decisions can be expected to make and sustain a profit impact on the firm. The governance structure of law firms, i.e., partnership decision-making, allows resources to be channelled and implementation to occur quickly. Moreover, since service is provided by trained professionals, little start-up time is needed and profit results can also be expected quickly.² When new business is brought into the firm by lateral entrants or through merger, as is often the case when those mechanisms are employed, the economic impact is likely to be even more immediate, as the firm recognizes a sudden large increment of revenue from an influx of new clients. However, those increases stabilize and are subsequently diluted over time as the bonus from new partners is absorbed and future contributions occur incrementally. In order to maximize the explanatory value of results, variables were measured for different time spans within the five year period: data on

²A more detailed discussion of this issue can be found in the section on start-up costs in Chapter 2.

determinant organizational conditions, growth decisions, and revenue change were all collected annually; one profitability measure was obtained for the years 1983 - 1987 inclusive; and two other profit-related variables were measured at the end of the decision period, 1987. Triangulating the time span in this way allowed both short and longer term effects of strategic decisions to be examined.

The decision to limit the sample to a local metropolitan law firm population limits the generalizability of the study. The primary bias in a New York City population is the over-sampling of larger law firms. In Table 4, city and national figures representing the number and per cent of law firms in the size categories of interest to this study are compared.

Table 4
Size Distribution of Law Firms: New York City and the Nation

<u>Size Range</u>	<u>Number/Percent of Law Firms in Category</u>	
<u>Number of Lawyers</u>	<u>New York</u>	<u>National</u>
20 - 49	90/53.6	1322/71.3
50 - 124	41/24.4	423/22.8
125 +	37/22.0	109/5.9
TOTAL	168/100	1854/100

Source: Martindale-Hubbell Law Directory (1988)

While the overemphasis on larger firms is apparent, the choice of New York City law firms is nonetheless an appropriate one for the study of law firm strategic growth. For one reason, though New York City has a disproportionate

number of large and small firms, there is still substantial variation in size in the sample. Moreover, the emphasis on larger firms represents a concentration on law firms with corporate clients. These firms represent a subset of law firms that has a disproportionate impact on the practice of civil law and the functioning of law firms in this country (Wholey, 1984). Also, to the extent that the larger size of the firms in this population is indicative of an emphasis on growth, the appropriateness of the population for studying law firm growth is increased. Finally, given the prominence of New York City as a major center of business and home to leading law firms, it is reasonable to expect that the competitive environment and resultant growth patterns that currently exist in that city are indicative of conditions that have and will continue to emerge in other metropolitan cities across the nation. Thus, given that data acquisition demands, i.e., interviews, preclude a national sample, a data set based on New York City firms provides an effective way to conduct this study.

In order to establish the representativeness of the sample, sampled and non-sampled firms have been compared along pertinent demographic characteristics. Data are presented in Table 5. The initial comparison of the two groups indicated a possible pattern of differences between sampled and non-sampled firms, with the non-sampled firms consistently larger than the sampled firms. Therefore, T-tests were conducted to test for differences between the means of the two groups for

each indicator of firm size and tests of differences between binomial proportions were used to test differences in the percentage of firms in each size category. The analyses revealed no significant differences between the two groups for any of the indicators. Results are presented in Table 6.

Table 5
Demographic Profile of Sampled and Non-sampled Population

	Population Firms (N=138)	Sampled Firms (n=61)	Non-sampled Firms (n=76)
Average Firm Size			
Number of Attorneys	81.5 (SD=74.5)	74.0 (SD=63.3)	87.5 (SD=82.2)
Number of Partners	32.9 (SD=24.2)	30.5 (SD=21.5)	34.4 (SD=26.2)
Number of Associates	48.6 (SD=51.3)	43.4 (SD=43.5)	52.7 (SD=56.7)
Average Number of Fields of Practice	9.7 (SD=3.8)	9.1 (SD=3.9)	10.1 (SD=3.7)
Average Number of Branch Offices	2.0 (SD=2.8)	1.7 (SD=2.1)	2.3 (SD=3.2)
Percent of Firms With			
Less than 50 Attorneys	48%	44%	51%
50 to 124 Attorneys	29%	36%	22%
125 + Attorneys	23%	20%	25%

Source: Martindale-Hubbell Law Directory (1988)

Table 6
Results of Tests of Differences Between Sampled and Non-Sampled Firm
Groups on the Demographic Indicators

<u>Demographic Indicators</u>	<u>T or Z Value^a</u>	<u>Probability</u>
<u>Average Number of:</u>		
ATTORNEYS	1.091	0.277
PARTNERS	1.012	0.314
ASSOCIATES	1.086	0.280
FIELDS OF PRACTICE	1.034	0.305
BRANCH OFFICES	1.337	0.184
<u>Percent of Firms With:</u>		
LESS THAN 50 ATTORNEYS	0.816	0.412
50 - 125 ATTORNEYS	1.813	0.070
125+ ATTORNEYS	-0.695	0.487

^a A T value is provided for the T-tests (the number of attorneys, partners, associates, fields, and branch offices); a Z value is provided for the tests of binomial proportions (the size categories).

N = 138

Measurement

Size

Firm size is operationalized as the total number of partners and associates in the New York City office. Data on firm size were obtained from firm information in the Martindale-Hubbell Law Directory. Accuracy of the data was confirmed during the firm interview.

Professional Specialization

Professional specialization refers to the number of distinct legal fields in which the firm practices. Information about practice areas was requested prior to the interview. Respondents were provided with a comprehensive list of practice areas culled from the Martindale-Hubbell Law Directory and asked to indicate all fields of the firm's practice.

Rainmakers

Firm rainmakers are considered to be those partners responsible for substantial amounts of firm business. Reliance on rainmakers was determined by calculating the ratio of "percentage of firm business attributable to rainmakers" to "number of rainmakers in the firm". Data were collected with an interview questionnaire item that asked for the number of major rainmakers for each year from 1983

through 1987 and the percentage of client business for which they were responsible.

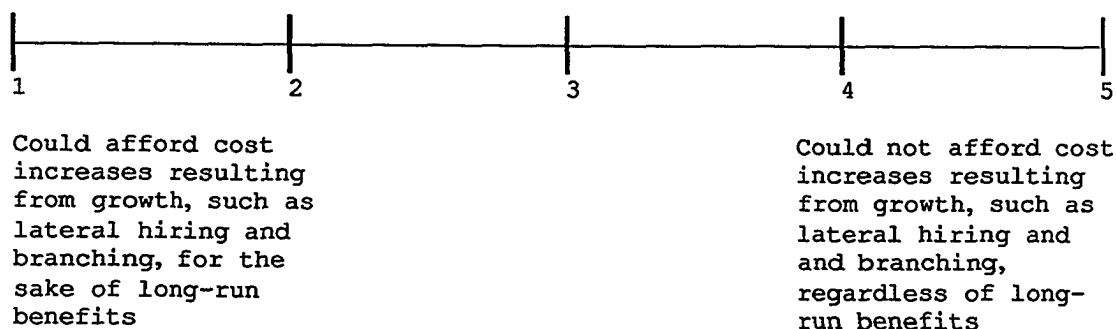
Revenue Growth

Revenue growth is operationalized as the percentage change in fee income from the previous year, e.g., the change from 1982 to 1983, from 1983 to 1984 and so forth. Data were requested during the interview.

Funds for Growth

The availability of funds for growth is operationalized as the degree to which a firm had sufficient funds to implement desired growth decisions, e.g., lateral hiring, branching. During the interview, the respondent was asked for the firm's situation with respect to funds available for growth for each year from 1983 through 1987. The questionnaire item reads:

In each of the years we are discussing, what was the firm's situation with respect to funds available for growth?



Unprofitable Practice Areas

Unprofitable practice areas refers to the percentage of the firm's practice that is not profitable. This percentage has been calculated by comparing the number of unprofitable practice areas to the total number of practice areas for each year from 1983 through 1987. Information was obtained during the interview.

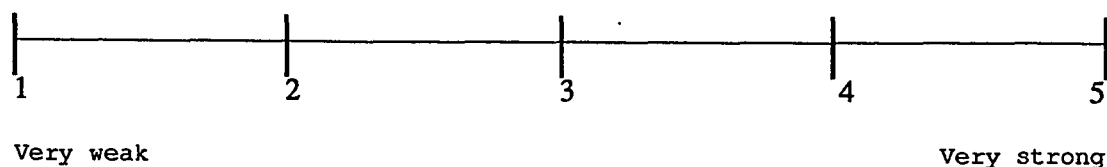
Associate-to-Partner Ratio

Associate-to-partner ratio has been calculated from data collected on the number of partners and number of associates for each year from 1983 through 1987.

Promotion Policy

The firm's promotion policy is its policy regarding making partners by promotion versus making partners by lateral entry and merger. During the interview, respondents were asked the following question:

Firms differ in their commitment to "growing their own" partners versus bringing in lawyers at a partnership level. For each of the years 1983 through 1987, where would you place your firm on a continuum where 1 represents a weak commitment to promotion from within, and 5 represents a strong commitment to promotion from within?



Client Demand

Client demand is the need by clients for services in legal fields and in cities where the firm does not practice. The measurement of client demand was problematic, in that no measure was found or could be constructed of client demand per se. As a result, client demand is operationalized in terms of its strategic results, i.e., as the percentage of firm practice areas and branch offices started in response to client demand for services. Interview respondents were asked the reasons for entering new practice areas and cities during the period 1983 through 1987. Responses were categorized as "client demand", i.e., client need in legal fields or in cities where the firm did not practice; "practice need", i.e., firm partners' perception of the need for capabilities in particular legal fields or cities; and "other" reasons.

Expansion of Existing Practice Areas

Practice area expansion is the percentage increase in the number of partners in existing practice areas. The number of partners added to the firm's existing practice areas for each year from 1983 through 1987 was queried in preliminary interview questions and compared to partner information culled from the Martindale-Hubbell Law Directory.

Practice Development

Practice development is the addition of new practice areas, calculated as the ratio of new practice areas to total

number of practice areas. Data concerning practice development from 1983 through 1987 were requested in the set of questions completed by the firm prior to the interview.

Branch Office Development

Branch office development is the addition of branch offices, calculated as the ratio of new offices to total number of offices, including the principal office. Data concerning branch office development from 1983 through 1987 were requested in the set of questions completed by the firm prior to the interview.

Internal Development

Internal development is operationalized as the promotion of associates to partnership, and the utilization of current firm partners to begin new practice areas and open branch offices. The measure was calculated as the ratio of that total to the full partnership.

Lateral Entry

Lateral entry is operationalized as growth in the number of partners as a result of bringing lawyers into the firm at the level of partner. Preliminary interview questions asked for the number of lateral entrants each year from 1983 through 1987. This number was calculated as a percentage of the total number of partners.

Merger

Merger is operationalized as growth by the formation of one partnership from two previous partnerships. Merger was measured as the percentage increase in the number of partners who have entered the firm through merger. Preliminary interview questions asked for the number of partners who entered the firm by merger each year from 1983 through 1987. This number was calculated as a percentage of the total number of partners.

Strategy - Mechanism Combinations

The combination of growth strategies and growth mechanisms results in nine strategy-mechanism combinations. The three combinations in which the strategy is practice area expansion are operationalized as the percentage of partners added to a firm via each mechanism. Thus, practice area expansion by internal development is the percentage increase in total partners resulting from the election of associates to partnership; practice area expansion by lateral entry is the percentage increase in total partners resulting from the addition of lateral partners; and practice area expansion by merger is the percentage increase in total partners resulting from the addition of partners by merger.

For the practice development and market development strategies, combinations are operationalized as the percentage change in practice areas or firm offices through a given mechanism. For example, practice development by lateral entry

is the percentage increase in new practice areas started by lateral partners; market development by merger is the percentage increase in number of offices opened by merging with another firm.

Per Partner Profit

Per partner profit is reported as the percentage change in average per partner profits from 1983 to 1987. Average per partner profit is calculated by dividing net income (total revenues minus overhead) by the number of full equity partners. This figure was requested during the interview.

Billing Rate

Billing rate is operationalized as the firm's weighted average hourly fee for professional members. The 1987 weighted rate for partners and associates was requested during the interview. The questionnaire asked for the number of lawyers billed out at each billing rate. From this information, the firm's weighted average billing rate was calculated by multiplying each billing rate by the number of lawyers who were billed out at that rate, adding results, and dividing by the total number of lawyers.

Utilization

Utilization is the weighted average number of billable hours per lawyer per year. It was requested for 1987 during the interview. The questionnaire requested the total number

of billable hours for firm partners and associates. From this information, utilization was calculated by dividing the total number of billable hours by the total number of lawyers.

Cross-selling

Cross-selling is operationalized as the percentage of firm revenues that have come from multi-service clients and multi-site clients in 1987. This information was requested during the interview. The questionnaire items read:

- For 1987, what was the percentage of firm revenue that came from multi-service clients, i.e., from clients who used more than one of the firm's practice areas?

- Also for 1987, what was the percentage of firm revenue that came from multi-site clients, i.e., from clients who used more than one of the firm's offices?

Partner Departures

Partner departures is operationalized as the proportion of partners who left the firm between 1985 and 1988. At the interview, respondents were asked to indicate the number of partners who left the firm from 1985 through 1988 for reasons other than retirement or death. This number was calculated as a percentage of the total number of partners that year.

Data Analysis Methods

The first task of data analysis was to calculate summary statistics, including means, standard deviations, and minimum and maximum values, for all variables. Preliminary analysis also included examination of variable sets to check for multicollinearity. Pearson product-moment correlations were computed for relationships among organizational level predictors, among growth strategies, i.e., expansion of existing practice areas, practice development and branch office development, and among growth mechanisms, i.e., internal development, lateral entry and merger. Though the preliminary analysis did not indicate a problem, the absence of multicollinearity among variables was confirmed for each subsequent analysis by examining variance inflation scores. The majority of hypothesis tests were conducted using multiple regression.

In order to capture the causal dynamics of growth in law firms, lagged multiple regression analysis was used to test the effect of firm conditions on growth decisions. Strategic growth behavior is assumed to be based on information from the past; therefore, values of the independent variables should have a lagged effect on the dependent variable. Given the expectancy of relatively quick implementation of strategic decisions, discussed earlier in this chapter, a one year lag was chosen. To determine that the degree of the lag structure was sufficient, initial analyses were conducted using both one and two year lags. The two year lags were

found to be insignificant. Using a one year lag allowed for four waves of the pooled 1983 - 1987 data to be used in the analyses.

A lagged effect may not be felt all at once, but instead may be distributed over a number of future points in time, i.e., the process of adjustment may be gradual (Judge et al., 1980). This is an apt description of the phenomenon of law firm growth, since growth is constrained by the availability of attorneys who fit the firm's needs, as well as by other considerations. Researchers have used partial adjustment models to analyze dynamic relationships such as changes in firm structure (e.g., Hummon, Doreian, & Teuter, 1975) and the growth of populations of organizations (Nielsen & Hannan, 1977). In such models, a lagged value of the dependent variable is included as an independent variable in the regression equation in order to control for the portion of the adjustment that has already occurred. In this study, the dependent growth variable is the amount of growth during year T, and firm conditions are measured at the beginning of year T-1; therefore the lagged models used to analyze the relationships between firm characteristics and growth decisions control for growth occurring during year T-1 by including lagged values of the growth variables as additional independent variables. The form of the regression model used for those hypotheses is:

$$Y_t = \beta_0 + \beta_1 Y_{t-1} + \beta_2 x_{1_{t-1}} + \beta_3 x_{2_{t-1}} + \dots + e$$

Lagged models were also used for testing the effect of strategic growth decisions on revenue growth. Clients are billed and can be expected to pay those bills within a year. Therefore, the one year lag was also appropriate to test these hypotheses. However, since firm growth was measured for the entire year T-1, and since revenue generation is not immediate, i.e., at least a few months will pass before billing and payment occur, revenue growth for year T was regressed onto firm growth for year T-1 without controlling for revenue change in year T-1. The regression equation used in testing those hypotheses is:

$$Y_t = \beta_0 + \beta_1 X_{1_{t-1}} + \beta_2 X_{2_{t-1}} + \dots + e$$

Finally, hypotheses that predict the influence of growth on per partner profitability and partner departure outcomes were also tested by multiple regression analysis. For these analyses, however, growth data over the five year period of the study were combined and compared to changes in profit and partner departure outcomes over the same period. Therefore, data were essentially cross-sectional and non-lagged multiple regression analysis was used to test hypotheses. The form of the equation used for these regressions is:

$$Y_t = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \dots + e$$

CHAPTER 5 RESULTS

Set 1 Hypotheses

The first set of hypotheses predicts the influence of firm characteristics on growth decisions. Table 7 contains descriptive statistics for firm characteristics for each of the years included in the analysis. These include firm size (SIZE), firm rainmakers (RAIN), associate-to-partner ratio (RATIO), promotion policy (PROMOTE), availability of funds for growth (FUNDS), revenue growth (REVENUE), professional specialization (FIELDS), unprofitable practice areas (UNPROFIT), and the client demand variables, including client need for new practice areas (CLIENTPD), practice need for new practice areas (PRACPD), and other reasons for new practice areas (OTHERPD), client need for new branch offices (CLIENTBO), practice need for new branch offices (PRACBO), and other reasons for new branch offices (OTHERBO).

Table 7
Demographics for Firm Conditions

VARIABLE	N	MEAN	STD	MIN	MAX
----- YEAR=1983 -----					
SIZE	61	67.361	57.351	6.000	248.000
RAIN	59	19.608	18.365	2.286	90.000
RATIO	61	1.647	0.965	0.000	6.500
PROMOTE	61	3.602	0.955	1.000	5.000
FUNDS	61	1.000	0.000	1.000	1.000
REVENUE	49	18.393	13.886	-23.000	70.000
FIELDS	60	9.967	2.980	5.000	18.000
UNPROFIT	59	6.683	8.229	0.000	33.333
CLIENTPD	60	1.533	5.248	0.000	28.571
PRACPD	60	0.432	1.631	0.000	7.143
OTHERPD	60	0.167	1.291	0.000	10.000
CLIENTBO	61	2.131	13.053	0.000	100.000
PRACBO	61	0.574	3.428	0.000	25.000
OTHERBO	61	0.410	3.201	0.000	25.000

Table 7: Demographics for Firm Conditions
(continued)

VARIABLE	N	MEAN	STD	MIN	MAX
----- YEAR=1984 -----					
SIZE	61	70.639	59.734	9.000	261.000
RAIN	59	17.844	15.682	2.424	80.000
RATIO	61	1.608	0.903	0.286	6.000
PROMOTE	61	3.488	0.846	1.000	5.000
FUNDS	61	1.000	0.000	1.000	1.000
REVENUE	52	16.891	13.302	-3.000	58.000
FIELDS	60	10.133	2.977	5.000	18.000
UNPROFIT	59	6.782	8.723	0.000	33.333
CLIENTPD	60	0.727	3.152	0.000	20.000
PRACPD	60	0.917	3.509	0.000	21.429
OTHERPD	60	0.671	2.594	0.000	12.500
CLIENTBO	61	0.091	0.711	0.000	5.556
PRACBO	61	0.911	6.429	0.000	50.000
OTHERBO	61	0.000	0.000	0.000	0.000
----- YEAR=1985 -----					
SIZE	61	74.393	61.807	10.000	259.000
RAIN	59	15.464	12.045	2.162	80.000
RATIO	61	1.615	0.715	0.400	4.000
PROMOTE	61	3.365	0.836	1.000	5.000
FUNDS	61	1.000	0.000	1.000	1.000
REVENUE	54	17.911	14.715	-15.300	75.000
FIELDS	60	10.350	3.030	5.000	18.000
UNPROFIT	59	6.108	7.913	0.000	33.333
CLIENTPD	60	0.180	0.990	0.000	6.250
PRACPD	60	0.653	2.347	0.000	12.500
OTHERPD	60	0.715	2.855	0.000	16.667
CLIENTBO	61	5.082	16.762	0.000	100.000
PRACBO	61	0.984	4.882	0.000	33.333
OTHERBO	61	0.000	0.000	0.000	0.000
----- YEAR=1986 -----					
SIZE	61	80.131	67.629	18.000	280.000
RAIN	59	14.251	11.588	2.286	80.000
RATIO	61	1.620	0.752	0.308	4.667
PROMOTE	61	3.164	0.872	1.000	5.000
FUNDS	61	1.000	0.000	1.000	1.000
REVENUE	55	19.218	19.034	-22.000	100.000
FIELDS	60	10.500	3.067	5.000	18.000
UNPROFIT	59	6.486	7.625	0.000	28.571
CLIENTPD	60	1.683	4.335	0.000	21.429
PRACPD	60	1.170	3.654	0.000	18.182
OTHERPD	60	0.513	2.310	0.000	12.500
CLIENTBO	61	0.533	2.997	0.000	20.000
PRACBO	61	0.915	4.684	0.000	33.333
OTHERBO	61	1.366	7.635	0.000	50.000

Examination of the descriptive statistics indicated a problem with the predictor variable "funds", i.e., the degree to which firms have economic resources available for growth. No variability was found in the measurement of this variable. In no case did a firm report that a decision not to pursue a growth strategy, e.g., to acquire lateral partners or open a branch office, was due to insufficient resources. All firms reported that funds were available to pursue growth strategies considered important. Therefore, this variable was dropped from the analysis.

Table 8 contains summary statistics for the growth variables. Growth strategies include expansion of existing practice areas (EXISTING), practice development (PRACTICE), and branch office development (BRANCH). Growth mechanisms are internal development (INTERNAL), lateral entry (LATERAL), and merger (MERGER). Strategy/mechanism combinations include practice areas expansion by internal development (EXINT), by lateral entry (EXLAT), and by merger (EXMER); practice development by internal development (PDINT), by lateral entry (PDLAT), and by merger (PDMER); and branch office development by internal development (BOINT), by lateral entry (BOLAT), and by merger (BOMER).

Table 8
Demographics for Growth Variables

VARIABLE	MEAN	STD	MIN	MAX
----- YEAR=1984 -----				
INTERNAL	6.876	10.028	0.000	66.667
LATERAL	4.930	6.850	0.000	33.333
MERGER	0.851	4.271	0.000	28.571
EXISTING	11.289	11.202	0.000	66.667
PRACTICE	2.315	5.242	0.000	21.429
BRANCH	1.002	6.535	0.000	50.000
EXINT	6.551	9.944	0.000	66.667
EXLAT	3.996	5.974	0.000	33.333
EXMER	0.742	4.204	0.000	28.571
PDINT	0.238	1.844	0.000	14.286
PDLAT	2.077	4.650	0.000	20.000
PDMER	0.000	0.000	0.000	0.000
BOINT	0.000	0.000	0.000	0.000
BOLAT	0.820	6.402	0.000	50.000
BOMER	0.182	1.423	0.000	11.111
----- YEAR=1985 -----				
INTERNAL	7.380	7.685	0.000	37.500
LATERAL	4.164	7.360	0.000	30.770
MERGER	0.574	3.968	0.000	30.769
EXISTING	9.414	8.307	0.000	38.462
PRACTICE	1.548	4.313	0.000	20.000
BRANCH	6.885	18.134	0.000	100.000
EXINT	5.907	5.973	0.000	20.000
EXLAT	3.248	6.530	0.000	30.770
EXMER	0.259	1.565	0.000	11.538
PDINT	0.152	1.174	0.000	9.091
PDLAT	1.245	4.082	0.000	20.000
PDMER	0.152	1.174	0.000	9.091
BOINT	6.066	17.262	0.000	100.000
BOLAT	0.820	6.402	0.000	50.000
BOMER	0.000	0.000	0.000	0.000
----- YEAR=1986 -----				
INTERNAL	8.693	9.079	0.000	50.000
LATERAL	3.721	5.060	0.000	16.667
MERGER	1.294	6.470	0.000	46.154
EXISTING	10.645	8.682	0.000	46.154
PRACTICE	3.030	6.050	0.000	28.572
BRANCH	3.224	9.864	0.000	50.000
EXINT	7.249	6.776	0.000	33.333
EXLAT	2.341	3.835	0.000	13.333
EXMER	1.055	6.315	0.000	46.154
PDINT	0.701	3.124	0.000	16.667
PDLAT	2.177	4.748	0.000	20.000
PDMER	0.000	0.000	0.000	0.000
BOINT	1.448	5.928	0.000	33.333
BOLAT	1.230	7.110	0.000	50.000
BOMER	0.546	4.268	0.000	33.333

Table 8: Demographics for Growth Variables
(continued)

VARIABLE	MEAN	STD	MIN	MAX
----- YEAR=1987 -----				
INTERNAL	6.718	6.326	0.000	23.077
LATERAL	6.038	8.087	0.000	45.455
MERGER	2.553	8.996	0.000	52.632
EXISTING	11.540	8.832	0.000	40.000
PRACTICE	4.643	8.841	0.000	37.500
BRANCH	8.349	21.836	0.000	100.000
EXINT	6.006	5.814	0.000	22.222
EXLAT	4.252	4.965	0.000	18.182
EXMER	1.282	5.527	0.000	36.000
PDINT	0.590	2.625	0.000	14.286
PDLAT	3.735	8.692	0.000	37.500
PDMER	0.318	1.730	0.000	10.000
BOINT	3.704	14.971	0.000	100.000
BOLAT	1.571	7.764	0.000	50.000
BOMER	3.074	15.326	0.000	100.000

The descriptive statistics for the growth variables are presented in terms of percentage increases in the number of partners, practice areas, and branch offices. For example, in a firm with thirty partners, promoting three associates to partner would represent a ten percent increase in the size of the existing practice through promotion, i.e., practice area expansion by internal development. While it is that percentage which is used in hypothesis testing, the number of occurrences of each type of growth is also pertinent in assessing the value of the research data for statistical analysis. Continuing the example used above, since promotions are made annually, the promotion decision would represent one occurrence of practice area expansion by internal development. Similarly, acquiring two partners to begin a new legal specialization is one occurrence of practice development by

lateral entry. Table 9 contains frequencies of the number of occurrences of the growth variables between 1983 and 1987.

Table 9
Frequencies for Growth Variables: 1983-1987

<u>Growth Variables</u>	<u>Occurrences</u>
EXISTING	341
EXINT	200
EXLAT	130
EXMER	11
PRACTICE	79
PDINT	13
PDLAT	62
PDMER	4
BRANCH	40
BOINT	24
BOLAT	9
BOMER	7

Viewing the data in this way provides greater clarity than the descriptive statistics for assessing the adequacy of the variance of the growth variables. For example, there were only four occurrences of practice development by merger. Thus, despite a sufficient N, the preponderance of zero occurrences in the data rendered this variable unfit for meaningful analysis. Consequently, this growth variable was excluded from regression analyses.

In the following section, results of analyses conducted to test hypotheses concerning the predictor-growth relationships are presented. Most variables were entered into the regression equations simultaneously. The simultaneous model is appropriate when there is "no logical or theoretical basis for considering any variable to be prior to any other, either in terms of a hypothetical causal structure of the data or in terms of its relevance to the research goals" (Cohen & Cohen, 1975, p.98). Given the absence of research using the majority of independent variables investigated in this study, and as influences on growth in particular, there was no compelling causal priority for ordering them, with two exceptions: size and associate-to-partner ratio. The effects of size are generally considered to be pervasive in influencing organizational strategy, structure, and processes, and size is certainly expected to influence growth (Starbuck, 1965). Associate-to-partner ratio is more specifically pertinent to professional service firms, and has been found to influence growth in law firms (Wholey, 1984). Thus, where size and ratio are included in analyses they were entered hierarchically, first size and then ratio, into equations. Because size is potentially so potent, it was introduced as a control variable even in equations for hypotheses that did not directly posit its influence. When it did not prove to be significant, as was true in all cases, it was removed and the equations were tested as hypothesized.

The number of firms included in the multiple regression analyses is sixty-one and the number of years of observation for each is four. A total N of 244 is thus possible for each analysis; the number of cases differs because of missing values. In this section and throughout the reporting of results, statistics for related analyses, e.g., for the regression of each of the three growth strategies on firm condition predictors, are tabled together. Tables therefore contain blanks where relationships for particular independent variables were not hypothesized.

Hypothesis 1. This hypothesis predicts the relationship of client demand, firm size and professional specialization to the growth strategies, i.e., expansion of existing practice areas (EXISTING), practice development (PRACTICE) and branch office development (BRANCH). The growth strategies are ratio level variables. The size (SIZE) and professional specialization (FIELDS) variables are also measured at the ratio level. Hypotheses concerning relationships between these two variables and the growth strategies were analyzed by lagged multiple regression analysis controlling for prior growth, i.e., all independent variables are lagged one year. Table 10 presents the results of this analysis.

Table 10
Regression Results for Growth Strategies

<u>Firm Conditions</u>	<u>Growth Strategies</u>		
	EXISTING	PRACTICE	BRANCH
EXISTING (LAG)	0.256***		
PRACTICE (LAG)		0.073	
BRANCH (LAG)			-0.284***
SIZE	-0.028	0.163*	0.033
FIELDS		-0.276***	
F	8.707***	4.988**	11.515***
CONSTANT	8.637	7.490	3.358
R-SQUARE	0.060	0.048	0.081
N	240	240	240

Standardized regression coefficients are reported

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

The hypotheses for the influence of firm size and professional specialization on law firm growth strategy are partially, though weakly, supported. As regards practice area expansion, smaller firms were expected to increase the size of their existing practice more than larger firms. Results indicate that no significant relationship exists between size and practice area expansion. Only prior practice area expansion is a significant predictor of practice area expansion. Similarly, the hypothesized relationship between size and branch office development is not significant. Again, only prior branch office development is a significant predictor.

Hypotheses for practice development are supported. Increasing development of legal fields is associated with increasing size. Also as expected, a significant negative relationship was found between practice development and professional specialization. The narrower the breadth of a firm's practice, the more practice development is undertaken. It is notable that when size was entered into the regression equation hierarchically, with only the lagged practice development variable, it did not achieve significance, but only became significant once fields was entered. This finding suggests the presence of suppression among these variables and speaks for examining them in interaction in future analysis.

The influence of client demand on the development of new practice areas and branch offices was treated separately due to the measurement constraints discussed in Chapter 4, i.e., the inability to measure demand separately from the growth strategies. Lacking a measure of client demand per se, data were gathered on the number of practice areas and the number of branch offices developed in response to three categories of demand: client demand, i.e., client need in legal fields or in cities where the firm does not practice; practice demand, i.e., firm partners' perception that the practice should include certain legal fields or that the firm should have a presence in particular cities; and "other" reasons, such as the availability of a desirable attorney, or opening a small branch office outside the metropolitan area to accommodate

semi-retired partners. For each strategy, differences in group means were tested by an analysis of variance.

For the most part, tests fail to support predictions that client demand more strongly influences the development of new practice areas and branch offices than does practice demand or other demands. The null hypothesis of no significant difference among group means was rejected in the practice development analysis. A significant difference was found between the "client demand" and "other demand" categories. The significantly greater mean value of the "client" category versus the "other" category supports the hypothesis of greater practice development in response to client demand than other demand. However no significant difference was found between the "client" and "practice" categories or between "practice" and "other" categories. In sum, client need is more likely to result in the development of new practice areas than "other" reasons, but client need for new legal services is not more significant than practice need in influencing the development of new practice areas.

The null hypothesis of no differences between category means was not rejected in the branch office development strategy analysis. There are no significant differences between means of "client" and "practice", "client" and "other", or "practice" and "other" demand categories. These results indicate that no one demand type is more influential than another for the opening new branch offices.

Results of the analyses are presented in Table 11.

Table 11
Mean Practice and Branch Office Development by Demand Category

<u>Development of</u>	Demand Categories			F	Means Test
	CLIENT	PRACTICE	OTHER		
PRACTICE AREAS	1.362	0.907	0.507	4.208*	CL > PR CL > OTH** PR > OTH
BRANCH OFFICES	2.010	1.125	1.052	1.153	CL > PR CL > OTH PR > OTH

N = 305

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Hypothesis 2. This hypothesis predicts a relationship between certain organizational characteristics and firm growth mechanisms. Predictor variables, i.e., the organizational conditions, are measured at the interval or ratio level. Growth mechanisms are measured as the percentage increase in partners added to the firm by each mechanism, and so are also measured at the ratio level. For example, lateral entry is the proportion of lateral partners hired across strategies.

The initial regression analysis of the hypothesis concerning the relationship between firm characteristics and the merger growth mechanism did not achieve statistical significance. Therefore, a stepwise analysis was conducted to eliminate variables that were detracting from the specification of the model. That analysis resulted in removing the lagged merger and promotion variables from the regression equation. Having omitted these variables, the new regression

equation was tested and found to be significant. The removed variables are noted in the results table.

Regression results for tests of relationships between each growth mechanism, i.e., internal development (INTERNAL), lateral entry (LATERAL) and merger (MERGER), and part of the set of organizational variables including size (SIZE), rainmakers (RAIN), revenues (REVENUE), unprofitable practice areas (UNPROFIT), associate-to-partner ratio (RATIO), and promotion policy (PROMOTE), are presented in Table 12.

Table 12
Regression Results for Growth Mechanisms

	<u>Growth Mechanisms</u>		
<u>Firm Conditions</u>	INTERNAL	LATERAL	MERGER
INTERNAL (LAG)	0.127*		
LATERAL (LAG)		0.158*	
MERGER (LAG)			removed
RATIO	0.314***		
PROMOTE	0.119*	-0.218**	removed
SIZE		0.100	-7.083**
RAIN		0.155*	-2.45**
REVENUE		-0.028	0.479
UNPROFIT		0.174**	-4.546**
F	17.090***	5.077***	2.136*
CONSTANT	-2.465	6.486	1.358
R-SQUARE	0.167	0.110	0.023
N	241	200	200

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Findings support the hypothesized relationship between associate-to-partner ratio and internal development. Firms with a higher ratio of associate attorneys make more partners from the associate ranks and undertake more development of practice areas and branch offices with their own attorneys. Further, a significant positive relationship exists between internal development and commitment to promotion. There is more internal development in firms that express a commitment to "growing their own", implying that these firms resist growth by external mechanisms.

Of the five variables posited to influence lateral entry, three were found to be significant predictors. In contrast to firms committed to the traditional professional norms of promotion from within, those firms without such commitment do indeed undertake more expansion with lateral partners. A positive relationship between lateral entry and reliance on rainmakers is also significant, suggesting that firms which are dependent on a small number of rainmakers for a large proportion of their business seek to reduce that reliance through the acquisition of additional rainmaking partners. The significant positive relationship found between lateral entry and percentage of unprofitable practice areas suggests a similar attempt to increase the profitability in departments that are being supported by the rest of the firm. The inverse relationship predicted between revenue growth and lateral entry is not significant. The influence of size on lateral entry is also insignificant.

Despite support of some hypotheses, results of tests of firm influences on growth by merger are weak, with an explained variance of only 2.3%. As predicted, size is inversely related to merger. Reliance on rainmakers and percentage of unprofitable practice areas were also found to be negatively related to merger, in contrast to the direction hypothesized. And revenue was found to have an insignificant relationship to merger, as opposed to the negative relationship predicted. One possible explanation for these findings is that firms with few rainmakers, unprofitable practice areas, and a poor revenue history are avoided as merger partners.

Hypothesis 3. This hypothesis predicts a significant relationship between organizational conditions and the strategy/mechanism combinations. The variables are measured at the interval or ratio level. Multiple regression analyses tested relationships between each of the nine strategy/mechanism combinations and the following organizational conditions: size (SIZE), professional specialization (FIELDS), rainmakers (RAIN), revenues (REVENUE), unprofitable practice areas (UNPROFIT), associate-to-partner ratio (RATIO), and promotion policy, i.e., degree of commitment to making partners from within (PROMOTE).

The initial analyses of hypotheses concerning practice area expansion by merger and practice development by merger did not achieve significance. Stepwise analyses were again

conducted to eliminate variables and more accurately specify the regression equation. The stepwise procedure was successful in developing a significant model for practice area expansion by merger; the removed variables are noted in the regression table. However, the equation for practice development by merger was not improved by the elimination of variables. This is understandable in light of the minimal use of this strategy/mechanism combination by the law firms sampled. As noted earlier, there were only four occurrences of practice development by merger, and therefore the failure to adequately specify a significant model is very likely a result of too little variance. Therefore, this regression analysis was eliminated.

Table 13 reports findings for practice area expansion by the growth mechanisms, i.e., internal development (EXINT), lateral entry (EXLAT), and merger (EXMER).

Table 13
Regression Results for
Practice Area Expansion/Growth Mechanism Analyses

<u>Practice Area Expansion by Each Growth Mechanism</u>			
<u>Firm Conditions</u>	EXINT	EXLAT	EXMER
EXINT (LAG)	0.095		
EXLAT (LAG)		0.277***	
EXMER (LAG)			removed
RATIO	0.269***		
PROMOTE	0.096	-0.209**	-0.171*
SIZE		0.074	0.132
RAIN		0.118	removed
REVENUE		-0.066	removed
UNPROFIT		0.195**	removed
F	10.495***	7.287***	9.351***
CONSTANT	-0.009	5.279	1.951
R-SQUARE	0.105	0.159	0.065
N	244	200	244

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

As predicted, a significant positive relationship was found between ratio and practice area expansion by internal development. The earlier reported finding of more internal development in firms with a higher associate-to-partner ratio supports the argument that law firms need to respond to the promotion expectations of junior attorneys. The current finding suggests that, not surprisingly, promotion occurs within existing practice areas.

Hypotheses predicting negative relationships between commitment to promotion and practice area expansion by both lateral entry and merger are also supported. However, the positive relationship predicted between the promotion variable and practice area expansion by internal development is not significant. A possible explanation is that, given expectations for promotion as discussed above, all firms experience some amount of pressure for internal development. If so, firms with a lesser commitment to promotion may be more likely to add lateral and merger partners to existing areas, but all firms will need to promote some percentage of associates to partnership, expanding existing areas of practice. In the case of merger, results of the hierarchical analysis may also be relevant. Though size was not found to be significant through the stepwise procedure, it was significant when introduced initially with only the lagged practice area expansion by merger variable. Therefore, the interaction between size and promotion policy may warrant further investigation.

Practice area expansion by lateral entry is significantly positively related to having unprofitable practice areas. Considered together with the previously reported relationship between unprofitable practice areas and lateral entry, this finding suggests that firms bring lateral partners into unprofitable areas to improve their economic performance.

Table 14 reports results of the analysis of the relationship between firm characteristics and practice

development by internal development (PDINT) and practice development by lateral entry (PDLAT). Since the low incidence of practice development by merger precluded analysis of this growth variable, it does not appear in the table.

Table 14
Regression Results for Practice Development/Growth Mechanism Analyses

<u>Practice Development by Each Growth Mechanism</u>		
<u>Firm Conditions</u>	PDINT	PDLAT
PDINT (LAG)	0.319***	
PDLAT (LAG)		-.000
FIELDS	-0.096	-0.608*
PROMOTE	0.056	-0.045
SIZE		0.637*
RAIN		0.531**
REVENUE		-0.171
UNPROFIT		-0.183*
F	9.991***	4.046***
CONSTANT	0.335	3.576
R-SQUARE	0.103	0.098
N	234	234

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Results for tests of these hypotheses are mixed. The relationships of practice development by internal development to firm promotion policy and to professional specialization did not achieve statistical significance. Practice

development by internal development is predicted only by its lag variable.

The analysis supports the predicted inverse relationship between professional specialization and practice development by lateral entry. Firms with more limited breadth of legal fields expand by bringing in lateral partners with existing expertise. A significant positive relationship was also found between practice development by lateral entry and reliance on a small number of rainmakers, suggesting that the desirability of bringing into the firm attorneys with an existing client base is a reason for choosing lateral entry to develop new legal fields. This supposition is further supported by findings for the predicted negative relationship between revenue growth and PDLAT, which achieved a significance of $p = .06$.

A significant positive relationship was found for the influence of size on practice development by lateral entry. This finding suggests that larger firms respond to increasing competition to expand the breadth of their services by acquiring expertise, rather than by developing it from within. Finally, contrary to prediction, a negative relationship between practice area expansion by lateral entry and unprofitable practice areas was found to be significant.

Results for branch office development by the growth mechanisms, presented in Table 15, are weak. The regression model for branch office development by lateral entry did not achieve statistical significance. Moreover, the variance

explained by the model, as indicated by the R-square statistic, is minimal for both equations. The low variance of branch office development by both lateral entry (nine occurrences) and merger (seven occurrences) further limits confidence in the strength of these findings.

Two hypotheses were supported. Commitment to promotion was found to predict branch office development by internal development, i.e., by staffing the new branch fully or primarily with partners from the principal office. Also, larger firms are more likely to add branch offices by merger.

Table 15
Regression Results for Branch Office Development/Growth Mechanism Analyses

	<u>Branch Office Development by Each Growth Mechanism</u>		
<u>Firm Conditions</u>	BOINT	BOLAT	BOMER
BOINT (LAG)	-0.071		
BOLAT (LAG)		-0.015	
BOMER (LAG)			-0.036
PROMOTE	0.158*	-0.018	-0.056
SIZE	0.058	0.058	0.228***
F	2.661*	0.277	4.150**
CONSTANT	-3.303	0.306	0.066
R-SQUARE	0.020	-0.009	0.038
N	244	244	244

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Set 2 Hypotheses

These hypotheses concern the degree to which law firms favor particular growth mechanisms for undertaking the three growth strategies. Descriptive statistics for the growth strategy/growth mechanism combinations have been reported in Table 8. Differences in the use of the strategy/mechanism combinations, all of which are ratio level variables, were tested by analysis of variance.

Results of the analyses for each strategy/mechanism combination are presented below in Table 16, following which each is discussed.

Table 16
Mean Growth Strategy by Growth Mechanism

<u>Growth Strategies</u>	Growth Mechanisms			F	Means Test
	INTERNAL	LATERAL	MERGER		
EXISTING	6.629	3.208	0.667	39.865***	INT > LAT*** INT > MER*** LAT > MER***
PRACTICE	0.461	2.148	0.124	21.763***	LAT > INT*** LAT > MER*** INT > MER
BRANCH	2.473	1.281	0.761	3.018*	INT > LAT INT > MER* LAT > MER

N = 61

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Hypothesis 4A. This hypothesis predicts differences in the use of the internal development, lateral entry, and merger growth mechanisms for practice area expansion, i.e., for increasing the size of existing practice areas. Significant differences were found among the three types of growth. The mean for practice area expansion by internal development is significantly greater than the mean for practice area expansion by lateral entry and by merger, supporting the hypothesis that a greater amount of growth in existing practice areas occurs by internal development than by lateral entry or merger. A significant difference was also found between lateral entry and merger for practice area expansion. More growth in existing practice areas occurs by lateral entry than by merger.

Hypothesis 4B. A second analysis was conducted for practice development by the three mechanisms. The null hypothesis was again rejected and significant differences found among the three types of growth. As hypothesized, the mean for practice development by lateral entry is significantly greater than the mean for practice development by internal development and by merger, indicating that lateral entry is more frequently used for developing new practice areas than either internal development or merger. However, no significant difference was found between the the internal development and merger categories.

Hypothesis 4C. The final analysis in the growth strategy/growth mechanism hypothesis set tested for differences in the means of branch office development by internal development, lateral entry, and merger. The results of this analysis partially support the hypothesis. A significant difference was found between branch office development by internal development and branch office development by merger. As predicted, the mean of the internal development category is significantly greater, indicating greater use of internal development than merger for opening branch offices. However, no significant difference was found between branch office development by internal development and branch office development by lateral entry. Moreover, analysis of differences between branch office development by lateral entry and by merger showed that those categories are also not significantly different.

Set 3 Hypotheses

The final set of hypotheses posit relationships between growth decisions and firm outcomes. Multiple regression equations were used to test the influence of growth strategy on four profit measures, i.e., per partner profit, revenues, billing rate, and utilization, and on partner departures from the firm. Short-run effects of strategic growth decisions on profitability were examined by investigating their influence on annual percentage change in firm revenues. Hypotheses were tested using lagged multiple regression, with annual percentage change in revenue regressed onto growth strategies and growth mechanisms lagged one year. The effects of strategic growth decisions on profit were further evaluated by testing the effects of growth decisions on per partner profitability over the full period of the study. Hypotheses were tested using multiple regression analysis in which percentage change in per partner profitability over the five year period of the study was regressed onto the various growth strategies and strategy/mechanism combinations.

Hypothesis 5. This hypothesis predicts relationships between growth strategies and growth mechanisms and revenue growth, i.e., annual percentage change in firm revenues. Descriptive statistics for revenue and growth have been presented earlier in Tables 7 and 8 respectively.

The first regression tested the effect of growth strategy (EXISTING, PRACTICE, and BRANCH) on revenue growth

(REVENUE). Since only practice area expansion was posited to have a significant effect on revenue, it was entered into the equation first, followed by the other two strategy variables. Findings are presented below in Table 17.

Table 17
Regression Results for Analyses of Relationships Between Growth
Strategies and Firm Revenue

<u>Dependent Variable</u>	
REVENUE	
<u>Strategy Variables</u>	
EXISTING	0.323**
PRACTICE	0.091
BRANCH	-0.142*
F	11.014***
CONSTANT	13.828
R-SQUARE	0.125
N	212

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Results of the regression support the hypothesis of a significant positive relationship between practice area expansion and revenue growth. Increasing the size of the partnership results in greater gross revenues. The prediction of a non-significant relationship between practice development and revenue growth is also supported. However, though a non-significant relationship was predicted between branch office development and revenue, findings show a significant and negative relationship between those variables.

This unexpected finding may be explained by the earlier finding that most branch office development is undertaken by internal development, i.e., by transferring partners to new locations. Thus, smaller revenue growth may be a result of partners leaving the principal office, and thereby reducing gross revenue, to open a new office that may not immediately generate revenue sufficient to compensate for that reduction. This is particularly likely given that revenue change was measured annually.

Revenue growth was also predicted to be positively related to all three growth mechanisms. Since some evidence exists that merger and acquisition increase profitability, and since earlier hypotheses posited that the two external mechanisms would be used to increase revenue and bring rainmakers into the firm, hierarchical models were appropriate for testing these hypotheses. Of the two external mechanisms, lateral entry occurred far more frequently than merger. Consequently, hypotheses were tested entering first lateral entry and then merger into the equation before internal development. Results of the analysis are presented in Table 18 below.

Table 18
Regression Results for Analyses of Relationships Between Growth
Mechanisms and Firm Revenue

<u>Dependent Variable</u>	
REVENUE	
<u>Mechanism Variables</u>	
LATERAL	0.203**
MERGER	0.089
INTERNAL	0.208**
F	7.011***
CONSTANT	13.728
R-SQUARE	0.077
N	216

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

The analysis supports the hypothesis for two of the three growth mechanisms. Both internal development and lateral entry were found to be significantly positively related to revenue growth. Increasing the size of the firm through either mechanism results in greater revenues. The relationship of merger to revenue growth was not found to be significant.

Longer term effects of growth were captured by analyzing the effect of strategic decisions on percentage change in per partner profitability (PROFIT) over a five year period. It was hypothesized that practice area expansion would not influence per partner profitability. The relationships of practice development and branch office development to profitability were predicted to be moderated by the cross-

selling of practice areas (CSPA) and branch offices (CSBO). The moderating effect of cross-selling was posited to be due to its effect on firm billing rates (BILLRATE) and weighted partners' billable hours (WTHOURS). Hence, the relationship between those variables and growth was also tested. Descriptive statistics for the cross-selling and firm outcome variables are presented in Table 19.

Table 19
Descriptive Statistics for Criterion Variables

VARIABLE	N	MEAN	STD	MIN	MAX
PROFIT 1983-7	54	50.12	48.39	-50.00	241.00
BILLRATE 1987	55	172.28	20.68	110.00	203.00
WTHOURS 1987	58	1808.78	196.51	1250.00	2300.00
DEPARTS 1987	61	2.95	3.02	0.00	18.13
CSPA 1987	57	46.03	27.21	0.00	100.00
CSBO 1987	30	16.10	14.71	0.00	55.00

Hypothesis 6. This hypothesis predicts that increasing the size of the existing practice will not increase per partner profitability, i.e., that there is a non-significant relationship between practice area expansion and percentage change in per partner profit. In order to control for the effects of the other growth strategies, the per partner profitability variable (PROFIT) was regressed first onto practice area expansion (EXISTING) alone, and then onto all three growth strategies: practice area expansion, practice development (PRACTICE), and branch office development (BRANCH). Results of the regression analysis are presented in Table 20.

Table 20
Regression Results for Growth Strategy and Profit Analysis

<u>Dependent Variable</u>	
PROFIT	
<u>Growth Strategies</u>	
EXISTING	0.093
PRACTICE	0.380**
BRANCH	0.149
F	3.167*
CONSTANT	20.422
R-SQUARE	0.111
N	53

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

The analysis found no significant relationship between change in size of the existing practice and change in per partner profit over a five year period, supporting the hypothesis of no significant relationship between practice area expansion and per partner profitability. In addition to the hypothesized finding, the regression analysis found a positive significant relationship between practice development and per partner profit and a non-significant relationship between branch office development and per partner profit. Both the latter relationships were posited to be moderated by cross-selling and are further evaluated below.

Hypothesis 7. This hypothesis predicts the moderating effect of cross-selling of practice areas on the relationship

between practice development and profitability. Variables are measured at the ratio level. Hypotheses were tested through cross-sectional moderated multiple regression analysis in each case, testing first for the effect of the predictor variable on profit variables, then for the additive effect of the predictor and moderator variables on profit variables, and then for the interactive effect of the predictor and moderator variables on profit variables.

Cross-selling was posited to increase profitability by increasing the value of the firm to the client, and by decreasing the amount of time partners needed to devote to business generation. Therefore, in addition to per partner profitability, the influence of cross-selling of practice areas on billing rate (BILLRATE) and attorney utilization, or weighted billable hours (WTHOURS), was tested. However, tests of those relationships did not achieve significance. Results for the two latter analyses are presented in Table 21.

Table 21
Regression Results for Analyses of Relationships Between Practice
Development and Billrate and Utilization

	<u>Profit Variables</u>	
<u>Strategy Variables</u>	BILLRATE	WTHOURS
<u>Predictor</u>		
PRACTICE	-0.081	0.179
F	0.345	1.818
CONSTANT	173.775	1777.907
R-SQUARE	-0.013	0.014
N	54	57
<u>Predictor/Moderator</u>		
PRACTICE	-0.067	0.194
CSPA	0.196	0.079
F	1.147	1.145
CONSTANT	166.235	1754.315
R-SQUARE	0.006	0.005
Δ R-SQUARE	0.018	-0.009
N	51	54
<u>Predictor/Moderator</u> <u>/Interaction</u>		
PRACTICE	-0.074	0.242
CSPA	0.191	0.114
PDCS	0.011	-0.071
F	0.749	0.777
CONSTANT	166.367	1745.829
R-SQUARE	-0.015	-0.013
Δ R-SQUARE	-0.021	-0.018
N	51	54

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Table 22 presents the results of the moderated regression analyses for the relationship of practice development (PRACTICE) to per partner profit (PROFIT).

Table 22
Regression Results for Practice Development and Per Partner Profit Analyses

<u>Profit Variable</u>	
PER PARTNER PROFIT	
<u>Strategy Variables</u>	
<u>Predictor</u>	
PRACTICE	0.369**
F	8.023**
CONSTANT	33.680
R-SQUARE	0.119
N	53
<u>Predictor/Moderator</u>	
PRACTICE	0.377**
CSPA	0.223
F	5.565**
CONSTANT	14.418
R-SQUARE	0.157
Δ R-SQUARE	0.038
N	50
<u>Predictor/Moderator /Interaction</u>	
PRACTICE	0.164
CSPA	0.105
PDCS	0.280
F	4.088*
CONSTANT	22.621
R-SQUARE	0.159
Δ R-SQUARE	0.002
N	50

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Results of the first two regression analyses indicate a significant positive relationship between practice area development and per partner profit. However, contrary to prediction, the cross-selling of practice areas does not contribute to profitability. These analyses suggest that the development of practice areas increases per partner profitability irrespective of the cross-selling of those practice areas.

The relationship was evaluated further by including the practice development/cross-selling interaction term. The introduction of the interaction term rendered all the variables insignificant. In order to ascertain if those results were due to multicollinearity between the interaction term and the independent variables, Pearson product-moment correlations were calculated for the interaction term (PDCS) with the practice development strategy alone (PRACTICE) and in combination with growth mechanisms (PDINT, PDLAT, AND PDMER). The correlations are presented in Table 23.

Table 23
Practice Development
Independent, Moderator, and Interaction Variable Intercorrelations

Moderator Variable	Independent Variables					Interaction Terms		
1	2	3	4	5	6	7	8	
<u>Moderator Variable</u>								
1. CSPA								
<u>Independent Variables</u>								
2. PRACTICE	-0.049							
3. PDINT	0.207	0.366**						
4. PDLAT	-0.127	0.896***	-0.054					
5. PDMER	-0.127	0.046	-0.096	-0.074				
<u>Interaction Terms</u>								
6. PDCS	0.453***	0.665***	0.522***	0.487***	-0.068			
7. PDINTCS	0.282*	0.281*	0.955***	-0.125	-0.088	0.531***		
8. PDLATCS	0.323*	0.572***	-0.073	0.676***	-0.148	0.782***	-0.097	
9. PDMERCS	-0.004	-0.014	-0.081	-0.122	0.852***	-0.024	-0.074	-0.130
* Significant at $\leq .05$ level								
** Significant at $\leq .01$ level								
*** Significant at $\leq .001$ level								
N = 56								

Multicollinearity among the variables is evidenced by the large size of the correlation between the interaction term and practice development by internal development and practice development by merger. Therefore, the contribution of the interaction term cannot be evaluated.

Table 24 reports findings of the moderated regression analysis of the relationship between per partner profitability and the practice development/growth mechanism combinations. For reasons cited earlier, practice development by lateral entry was entered in order ahead of practice development by internal development. Also, practice development by merger was excluded from the analysis based on an insufficient number of occurrences for adequate analysis. Results of the regression of per partner profitability onto the other strategy/mechanism combinations (PDINT, PDLAT), the combinations plus the cross-selling moderator (CSPA), and the combinations, moderator, and interaction term (PDCS) are presented below.

Table 24
Regression Results for Practice Development/Growth Mechanism and Profit Analyses

<u>Dependent Variable</u>	
PROFIT	
<u>Strategy Variables</u>	
<u>Predictor</u>	
PDLAT	0.318*
PDINT	0.226
F	4.362*
CONSTANT	34.126
R-SQUARE	0.115
N	53

Table 24
Regression Results for Practice Development/Growth Mechanism and Profit
Analyses (continued)

<u>Dependent Variable</u>	
PROFIT	
<u>Strategy Variables</u>	
<u>Predictor/Moderator</u>	
PDLAT	0.343**
PDINT	0.188
CSPA	0.215
F	3.828*
CONSTANT	15.463
R-SQUARE	0.148
Δ R-SQUARE	0.033
N	50
<u>Predictor/Moderator</u> <u>/Interaction</u>	
PDLAT	0.395
PDINT	-0.572
CSPA	0.133
PDLATCS	0.039
PDINTCS	0.820
F	2.908*
CONSTANT	19.550
R-SQUARE	0.163
Δ R-SQUARE	0.015
N	50

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Results of these analyses produce much the same results as the previous one; however, in this analysis it is only practice development by lateral entry that has a significant effect on profit. Specifically, the development of practice areas with lateral partners improves per partner profit irrespective of the cross-selling of those practice areas. As in the previous analysis, all the variables were rendered insignificant with the addition of the interaction term.

Hypothesis 8. This hypothesis predicts the moderating effect of cross-selling of branch offices on the relationship between branch office development and profitability. The influence of branch office development and branch office development by the three growth mechanisms on percentage change in per partner profit and on billing rate was examined. Improved utilization across offices was not expected and was not included in the analysis. As in the preceding analysis, variables are measured at the ratio level and moderated multiple regression analysis was used to test the relationships. Analyses were conducted on the subset of firms with branch offices, hence the lower N for these tests.

Branch office development was not found to influence billrate. Results of the moderated regression for that analysis appear in Table 25.

Table 25
Regression Results for Analyses of Branch Office Development and
Billrate

<u>Profit Variable</u>	
<u>Strategy Variables</u>	BILLRATE
<u>Predictor</u>	
BRANCH	0.090
F	0.213
CONSTANT	172.817
R-SQUARE	-0.030
N	28
<u>Predictor/Moderator</u>	
BRANCH	0.786
CSBO	-0.092
F	0.210
CONSTANT	174.400
R-SQUARE	-0.062
Δ R-SQUARE	-0.032
N	28
<u>Predictor/Moderator</u> <u>/Interaction</u>	
BRANCH	0.079
CSBO	-0.092
BOCS	-0.000
F	0.135
CONSTANT	174.398
R-SQUARE	-0.106
Δ R-SQUARE	-0.044
N	28

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Findings of the per partner profit analyses are quite different from those of the analogous practice development tests. For branch office development, neither the equation that regressed per partner profit (PROFIT) onto the growth predictor (BRANCH) alone, nor onto the growth predictor with the cross-selling variable (CSBO), achieved significance. However, the moderated regression including the multiplicative interaction term of branch office development by cross-selling (BOCS) was significant. Examination of the significant coefficients indicates that the effect of branch office development on per partner profitability is dependent on the interaction between cross-selling and branch office development, supporting the hypothesis of a moderated relationship. Furthermore, Pearson product-moment correlation analysis indicated no serious multicollinearity problem among the variables. The simple correlations appear below in Table 26. Following that, results of the branch office strategy and per partner profit relationship are presented in Table 27.

Table 26
Branch Office Development
Independent, Moderator, and Interaction Variable Intercorrelations

	Independent Variables					Interaction Terms		
	1	2	3	4	5	6	7	8
<u>Moderator Variable</u>								
1. CSBO								
<u>Independent Variables</u>								
2. BRANCH	-0.108							
3. BOINT	-0.002	0.692***						
4. BOLAT	-0.056	0.507***	-0.025					
5. BOMER	-0.162	0.375**	-0.101	-0.085				
<u>Interaction Terms</u>								
6. BOCS	0.541**	0.528**	0.406*	0.294	-0.067			
7. BOINTCS	0.520**	0.373*	0.577***	-0.094	-0.169	0.821***		
8. BOLATCS	0.189	0.366*	-0.076	0.708***	-0.106	0.561***	0.025	
9. BOMERCS	-0.011	0.053	-0.191	-0.127	0.716***	-0.016	-0.172	-0.105
* Significant at $\leq .05$ level								
** Significant at $\leq .01$ level								
*** Significant at $\leq .001$ level								
N = 30								

Table 27
Regression Results for Analyses of Branch Office Development and Per
Partner Profit

<u>Profit Variable</u>	
PROFIT	
<u>Strategy Variables</u>	
<u>Predictor</u>	
BRANCH	-0.069
F	0.134
CONSTANT	62.002
R-SQUARE	-0.031
N	30
<u>Predictor/Moderator</u>	
BRANCH	-0.034
CSBO	0.326
F	1.661
CONSTANT	40.923
R-SQUARE	0.044
Δ R-SQUARE	0.075
N	30
<u>Predictor/Moderator /Interaction</u>	
BRANCH	-0.661**
CSBO	-0.314
BOCS	1.057***
F	9.043***
CONSTANT	72.052
R-SQUARE	0.454
Δ R-SQUARE	0.411
N	30

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

As the table indicates, having controlled for the interaction term, branch office development is found to have a negative effect on profit. Given the positive and significant interaction term, findings at first appear to suggest that the development of new branch offices contributes to profitability when those offices are cross-sold and detracts from profits when they are not.

In order to better understand the nature of the interaction between branch office development and the cross-selling of branch offices vis-à-vis profit, the sample was divided into four groups on the basis of high and low scores on the measure of the two interaction term variables and mean scores for percentage change in per partner profits were calculated for the four resulting subgroups. Firms in the top and bottom third of each variable were included. As depicted in the matrix in Figure 4 below, the mean scores suggest that the branching/cross-selling relationship may have a curvilinear relationship with profit. A similar percentage change in profitability is found when low branch office development is coupled with low cross-selling and with high cross-selling. Profit increases are different and considerably lower for firms in the condition of high branch office development and low cross-selling. The high cross-selling/high branch office development cell is a null set. These results suggest a curvilinear relationship between the interaction term and profit change, with profit increase greatest in the conditions of very low and very high cross-

selling of branches. However, given the low N and empty set in both the high cross-selling/low branch office development and high cross-selling/high branch office development cells respectively, caution needs to be exercised in speculating about these results. The apparant implication that law firms do not engage in much cross-selling of their branch offices is also important to note in considering the future use of this variable.

Figure 4
Mean Change in Profit for Branch Office Development/Cross-selling Subgroups

Cross-Selling	High	60.8% N = 3	N = 0
	Low	64% N = 13	40.9% N = 7
		Low	High
		Branch Office Development	

The next results reported are analyses of the relationships of profit to branch office development by the three growth mechanisms (BOINT, BOLAT, BOMER). As with the practice development analyses, results for the branch office development/growth mechanism combinations were much the same as

those for branch office development strategy. Equations including the branch office development/growth mechanism predictors alone did not achieve significance, nor did the additive equation including the combinations and the cross-selling moderator. However, the equation with the interaction terms for each strategy/mechanism combination (BOINTCS, BOLATCS and BOMERCS) was significant. Table 28 presents the results of the analyses.

Table 28
Regression Results for Branch Office Development/Growth Mechanism and Profit Analyses

<u>Dependent Variable</u>	
PROFIT	
<u>Strategy Variables</u>	
<u>Predictor</u>	
BOLAT	-0.118
BOMER	-0.121
BOINT	0.013
F	0.234
CONSTANT	62.422
R-SQUARE	-0.086
N	30
<u>Predictor/Moderator</u>	
BOLAT	-0.090
BOMER	-0.064
BOINT	0.028
CSBO	0.314
F	0.864
CONSTANT	41.817
R-SQUARE	-0.019
Δ R-SQUARE	0.067
N	30

Table 28
Regression Results for Branch Office Development/Growth Mechanism and
Profit Analyses (continued)

<u>Dependent Variable</u>	
	PROFIT
<u>Strategy Variables</u>	
<u>Predictor/Moderator</u> <u>/Interaction</u>	
BOLAT	-0.449*
BOMER	0.021
BOINT	-0.640**
CSBO	-0.328
BOLATCS	0.411*
BOMERCS	-0.178
BOINTCS	1.066***
F	5.442***
CONSTANT	73.967
R-SQUARE	0.517
Δ R-SQUARE	0.537
N	30

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Results support the hypothesis of a moderated relationship. In keeping with the previous findings for branch office development, the effect of branch office development/growth mechanism combinations on per partner profitability is dependent on the level of cross-selling. However, the analysis does not confirm the moderated relationship for all three strategy/mechanism combinations; findings for branch office development by merger are insignificant. As with

practice development by merger, the relatively low occurrence of branch office development by merger should be considered in assessing the reliability of this finding.

Hypothesis 9. This hypothesis predicts a non-significant relationship between growth mechanisms and per partner profitability over the five year period of the study. The hypothesis was tested by regressing the three growth strategies (INTERNAL, LATERAL, and MERGER) onto the per partner profit variable. Findings of a non-significant R square supporting the hypothesis are presented in Table 29.

Table 29
Regression Results for Growth Mechanism and Profit Analysis

<u>Dependent Variable</u>	
PROFIT	
<u>Growth Mechanisms</u>	
LATERAL	0.150
MERGER	-0.025
INTERNAL	0.034
F	0.428
CONSTANT	39.119
R-SQUARE	-0.034
N	54

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Hypothesis 10. In addition to profit outcomes, the effect of growth strategy on partner departures from law firms was

investigated. Regression analysis was used to test the relationships between internal development, lateral entry and merger respectively and the percentage of partner departures from the firm. Variables are measured at the ratio level of measurement. There was no theoretical or logical basis upon which to assign priority to the variables and the hypothesis was tested using a simultaneous equation. The results of this final analysis are presented in Table 30.

Table 30
Regression Results for Growth Mechanism and Partner Departures Analysis

<u>Dependent Variable</u>	
DEPARTS	
<u>Growth Mechanisms</u>	
INTERNAL	-0.268
LATERAL	0.318*
MERGER	0.170
CONSTANT	2.494
R-SQUARE	0.044
N	61

Standardized regression coefficients are reported.

* Significant at $\leq .05$ level.

** Significant at $\leq .01$ level

*** Significant at $\leq .001$ level

Results of the analysis provide some support for the hypothesized relationships. As predicted, lateral entry was found to be significantly and positively related to partner departure. Firms that increase their partnership by lateral entry also have higher levels of partner departures.

Conversely, the inverse relationship found between internal development and partner depatures is in the direction hypothesized and is significant at the .07 level, providing some support for a relationship between growth by internal development and lower levels of partner departure. However, the hypothesized negative relationship between merger and partner departure is not supported. Further, the amount of variance explained by the regression model is minimal.

CHAPTER 6 CONCLUSION

In the preceding chapters, an analysis was conducted of the organizational influences and outcomes of strategic growth decisions in law firms. In the next section the results of this analysis are reviewed and discussed. Following that, the contribution of the research to existing organization literature is noted and implications of the findings for law firm growth and growth strategy are drawn. Finally, limitations of the research are assessed, and suggestions for addressing those limitations and extending the analysis in future research are made.

Summary of Research Findings

Organizational Influences on Growth Strategy

The analysis began with an investigation of the influence of firm conditions on growth strategy, i.e., expansion of the existing practice, diversification into new practice areas, and the addition of branch offices. The expectation that smaller firms increase the size of existing practice areas more than larger firms was not confirmed. Rather, the only predictor of practice area expansion is its lag variable, i.e., the amount of practice area expansion the previous year.

In interpreting this unexpected result, it is necessary to recapitulate the purpose for the lagged dependent variable in the regression analysis. In modeling the regression

equations, independent variables were lagged one year in order to increase the opportunity for causal inference. Then, since the dependent growth strategy and mechanism variables were measured over the full year, and the independent variables were measured at the start of the prior year, one year growth lags were included as independent variables in order to determine whether some partial adjustment, i.e., some amount of growth, had already occurred during the prior year. Thus, it was expected that where the lagged dependent variable was significant, some amount of growth caused by the independent variables had already occurred; where it was not significant, it would imply that the adjustment took the full year (or somewhat more than a year) to occur.

The most straightforward interpretation of the singular significance of the lagged practice area expansion variable is that practice area expansion in one year is predicted only by practice area expansion the prior year, regardless of the size of the firm, i.e., there is strategic continuity within firms. The reason for the finding of strategic variety across firms despite differences in size is less obvious. If some firms choose to enlarge the size of their existing practice irrespective of their current size, it may mean that strategic decision makers enact different environments (Weick, 1979) or various interpretations of environments (Starbuck, 1982). That is, some but not all small and midsize firms may perceive no need to become large, and some but not all of the large and largest firms may perceive a need to be megafirms.

This explanation is in keeping with the perspective that strategies of firms in a strategic group are not necessarily identical (Mascarenhas, 1989).

In contrast to findings about practice area expansion, hypotheses concerning practice development were supported: larger firms and firms with fewer practice areas undertake more practice development. These results, which emphasize the importance of practice breadth as an organizational condition influencing growth strategy, are even more material given the lack of support for size as a condition for practice area expansion. Extending the argument raised earlier regarding the effect of firm members' perceptions of the environment on strategic choice, these findings would indicate that little dissensus exists concerning the need for practice breadth in order to be competitive. As regards the time necessary for strategic response, the lagged growth variable was not significant in this analysis, indicating that adjustment is not immediate; some time is needed to add new practice areas.

Finally, the prediction of a positive relationship between size and branch office development was not supported. However, though size does not predict the degree of branch office development, a review of the cities where branch offices were opened reveals that firms of different sizes differ in the location of their branch offices. Larger firms are more likely to expand internationally or to Los Angeles, often to position themselves for Pacific Rim business, while small and midsize firms are more likely to open offices in

New Jersey or in Washington, D.C.. To some degree these differences reflect the type of client served, e.g., the closely held corporate client of the smaller firm versus the international conglomerate client of the larger firm; however, they do not bespeak less necessity for being responsive to those clients. In this analysis, the lagged growth variable was again significant; however, an inverse relationship was found. This result supports the earlier (Chapter 2) discussion of costs associated with branch office development. Given high start-up costs as well as the tangible and intangible costs of maintaining control and preserving firm culture, one would expect branch offices to be opened infrequently and not in consecutive years.

A second analysis concerning the growth strategies investigated the influence of "client" and "practice" and "other" demands on the development of new practice areas and branch offices. Results of this analysis did not support the prediction that more development would be due to client need for services the firm did not offer than to gaps in the practice limiting a firm's ability to respond to market opportunities, or to miscellaneous other needs. Though no empirical evidence exists, it is widely accepted that law firms historically have had institutional relationships with clients, and have grown along with those clients. The present findings reflect changes in the firm-client relationship, whereby corporate clients have reduced their reliance on outside law firms by using in-house lawyers for more of their

legal needs and hiring more than one firm to handle matters that require outside counsel. These phenomena seem to have influenced law firms to alter their own behavior, defining practice needs and making growth decisions in response to perceived market needs and opportunities as well as to client needs.

Organizational Influences on Growth Mechanisms

In addition to assessing the effect of firm conditions on strategic direction, the study undertook to analyze the influence of firm conditions on the choice of mechanisms by which to grow, i.e., on internal development, lateral entry, and merger. As was discussed in earlier chapters, diversification has been assumed to be the primary motivation for merger and merger has been assumed to be the primary means by which firms diversify. Because the providers of legal and other professional services can individually constitute an area of practice, application of these assumptions to professional firms is questionable. In law firms, diversification can be achieved by internal development or lateral entry, as well as by merger. Moreover, reasons other than diversification can provoke the decision to bring outside lawyers into the firm, whether through lateral entry or merger. Consequently, an important objective of the study was to gain a better understanding of reasons for the use of the three mechanisms.

In investigating the influence of firm conditions on the use of the three growth mechanisms, one expectation was that member demands would play a significant role. Demands were operationalized in terms of both structure and policy; it was posited that a high associate-to-partner ratio and a strong firm commitment to promotion would be positively associated with internal development. These hypotheses were supported. The relationship of ratio to internal development reflects the need for law firms to be responsive to the promotion expectations of associate attorneys in order to attract and motivate junior members. The relationship of promotion policy to internal development suggests further that decisions about how to build the practice are influenced by the degree of commitment to traditional law firm norms. Since in addition to promotion, internal development includes the development of new practice areas and branch offices by current attorneys, that commitment will affect decisions concerning internal versus external diversification. The nature of that influence is more precisely specified by analyzing firm influences on strategy/mechanism combinations, and is therefore discussed further in the next section.

Predictions about the decision to engage in lateral entry and merger were predicated on the time advantage that accrues from both. It was expected that firms would use the external mechanisms in order to quickly improve a weak competitive position due to small size. Similarly, lateral entry and merger were predicted to be influenced by financial

weakness as indicated by low revenue growth and by the need to support practice areas that were minimally profitability or unprofitable, and by reliance on a small number of major rainmakers. Consideration was also given to membership influences, such that firm commitment to promotion was expected to be inversely related to both external mechanisms.

Analyses indicated that greater use of lateral entry occurs in firms where a small number of rainmakers is responsible for generating a large amount of business, and which have a larger percentage of minimally profitable or unprofitable practice areas. In similar ways, these conditions place the firm in a weak financial position. Findings suggest that firms seek to remedy this situation by bringing in lateral partners. The objective in using this mechanism is thus not growth per se but rather the correction of identified weaknesses through strategic acquisitions. Notwithstanding the utility of the mechanisms for this purpose, the inverse relationship found between lateral entry and commitment to promotion suggests that its use depends upon the firm's promotion policy. Finally, there is a significant relationship between the amount of lateral entry one year and the next. This indicates that lateral partners can be found in a relatively short time period, allowing some portion of desired growth by lateral entry to occur quickly.

Merger is motivated by different firm conditions than those which influence lateral entry. Growth by merger is inversely related to firm size. Much more than lateral entry,

merger can accomplish substantial growth in a discrete occurrence, making it attractive to those small firms seeking strength in size. However in contrast to lateral entry, and contrary to prediction as well, merger is negatively related to both the rainmaker and unprofitable practice areas variables. That is, firms are more apt to merge when they are less reliant on a limited number of rainmakers and have a smaller percentage of practice areas that require support. As has been surmised previously in discussing results, a possible explanation for these findings is that firms with few rainmakers and a greater number of unprofitable practice areas are avoided as merger partners. Because the amount of variance in merger explained by the firm condition variables is minimal, caution should be exercised in drawing conclusions. Bearing this caveat in mind, it appears that, for the firm that does not have a strong policy of commitment to promotion from within, lateral entry is the preferred mechanism for focused growth objectives such as the acquisition of attorneys who can generate business, whereas merger is preferred for the general improvement of competitive position that derives from larger size.

Organization Influences on Strategy/Mechanism Combinations

Given nine possible strategy/mechanism options, greater explanatory power is achieved by looking specifically at the use of particular mechanisms for implementing particular strategies. The influence of firm conditions on the choice

of mechanism for expanding the size of the existing practice and for diversifying into new fields and geographic markets is therefore a primary focus of the study.

Practice Area Expansion. Firm conditions influencing the choice of mechanism for expanding the firm's existing practice areas include associate-to-partner ratio, promotion policy, and the percentage of unprofitable practice areas. A high associate-to-partner ratio increases the promotion of associates to partnership. This finding supports the argument made in the introductory description of law firms, that law firm growth is a result not only of demand for services but is due as well to the need to offer partnership opportunities to associates while maintaining stability in leverage, i.e., in associate-to-partner ratio. Promotion rates nonetheless vary from year to year, such that the level of promotion in one year does not predict the level the following year. A possible reason for this finding is variance in the quality of associates up for promotion in any particular year. Most full service corporate firms, particularly midsize and large ones, regularly have some number of associates in each "class" from one year to eight, nine, or ten years out of law school, depending on the number of years before partnership decisions are made. The performance of associates in each class is likely to vary, affecting partnership decisions accordingly.

Firms that increase the size of their existing practice by bringing in lateral partners and by merging are, not

surprisingly, those with a weak commitment to promotion. What makes this finding interesting is that the opposite condition does not obtain; no relationship exists between promotion policy and practice area expansion by internal development. It appears that firms with a weak commitment to promotion bring lateral partners into existing practice areas along with, not in place of, promoting associates in those areas. This again underscores the importance of associate expectations as an influence for growth.

Lateral entry is also used for practice area expansion in firms having unprofitable practice areas. Lateral growth may be one way to strengthen those departments. Though law firms frequently support minimally profitable areas which exist primarily to service other, profitable departments, this finding suggests that this practice is becoming less acceptable as the legal profession assumes an increasing "bottom line" orientation. As one lawyer said, "You eat what you kill." Insufficient data prevent matching lateral partners to the existing fields they entered, precluding definitive determination of this supposition.

Practice Development. Examination of the determinants of growth strategies identified insufficient breadth of professional specialization and large firm size as conditions leading to practice development. Analysis of strategy/mechanism combinations indicates that law firms responding to these conditions enter new fields by acquiring expertise through lateral entry, rather than by developing it internally. The

use of lateral entry for practice development is notable in its contrast to the internal expansion of existing practice areas resulting from high associate-to-partner ratio. Where the latter demonstrates that law firms grow, at least in part, in response to internal demands (in effect to supply as opposed to demand), the former reveals that growth is also pursued in response to existing or anticipated external demand. Further, the two conditions influence different strategic directions. Briefly expressed, results of this study indicate that law firms seek practice depth in response to internal demands and practice breadth in response to external demands.

Heavy reliance on a limited number of rainmakers is another condition leading firms to bring in lateral partners who take the firm into new fields. This is in contrast with practice area expansion by lateral entry, which has no relationship to reliance on rainmakers. Newly acquired rainmakers are apparently more likely to begin new legal specialties than to enter existing ones. Evaluation of the role of the lateral partner suggests that a possible explanation for this is the benefit to both firm and rainmaking partner of joining the firm in a new rather than existing field. From the firm's perspective, the rainmaker who brings to the firm a new expertise adds not only a new source of clients but a new service to be sold to existing clients. Moreover, the integration of a new partner into the firm, especially one with the status and power that accrue to major

rainmakers, is likely to be easier when that person enters a new domain, rather than threatening the balance of existing ones. For the same reasons, joining the firm in a new field is likewise likely to be preferred by the rainmaker.

Branch Office Development. Results of the analysis of branch office development were weak and, overall, inconclusive in providing an understanding of that process. Branch office development is substantially different than development of the principal office, whether in depth or breadth. For one thing, while all general practice firms increase in size (number of attorneys) and, over time, add new areas of practice, no similar imperative exists to have multiple offices. In the current sample of sixty-one firms, just thirty had one or more branch offices. For those firms that do expand geographically, the difficulties of maintaining control and sustaining firm culture inherent in external expansion are exacerbated by the distance factor introduced in branch office development. This is important, since firm reputation rests on client perception of consistency in service quality among offices. On the other hand, acquiring or merging with attorneys having a strong local market position increases the likelihood that the branch will be economically viable. Therefore a tension exists between the desire for control and the advantages of local client support.

Study results indicate that larger law firms are more likely than smaller ones to add branch offices by merger.

More than smaller firms, larger ones open offices in major business capitals nationally and internationally, so as to be competitively positioned to serve existing and prospective clients. Large offices may therefore choose to merge with existing local firms in order to reduce the costs of carrying what would otherwise be money-losing offices. Another explanation for this finding is the tendency for smaller firms to open branch offices closer to the principal office, such that lawyers are more easily transferred and, not infrequently, can maintain a practice in both principal and branch offices.

Findings additionally show that law firms are more likely to open branch offices with partners transferred from the principal office when the firm has a policy of commitment to promotion. This finding, in keeping with the concept of the "one-firm firm" (Maister, 1985b), indicates that commitment to firm unity extends to branch offices.

Variance in Use of the Strategy/Mechanism Combinations

Additional understanding of the growth process was gleaned through a comparison of the frequency of use of each of the mechanisms for each of the strategies. To a considerable degree, the findings from this part of the study extend and add statistical support to the trends that emerged from the prior analysis.

When increasing the size of the existing practice, law firms are twice as likely to grow through promotion as

lateral entry, and almost ten times as likely to grow by promotion as by merger. The implication of this discovery in light of the potent influence of associate-to-partner ratio on practice area expansion is considerable. These findings clearly support the argument made repeatedly in this paper, that the promotional structure of law firms impels growth beyond that attributable to market demand for legal services.

Lateral entry plays the major role in practice development. The finding that lateral entry, and not merger, is the primary route to practice diversification is particularly interesting in light of assumptions about merger made in the strategy literature. As was argued earlier, the unique structure of the professional firm, in which the service and service provider are relatively synonymous, makes it possible to employ lateral entry as a means for diversification. Given the difficulties inherent in merger, the preference for lateral entry is understandable. Acquiring expertise in this way allows the firm to "cherry pick" attorneys with preferred legal and business skills and avoids the disruption, threats to firm culture, and other risks of failure associated with merger. These issues are especially ponderous in a professional firm, where merger means full integration of people and systems and where the psychological investment of firm members in the culture and processes of their organization is considerable. This finding reinforces the warning for caution in applying research paradigms based

on manufacturing type organizations to service firms, and certainly to professional service firms.

Patterns of branch office development are less marked than those of the other two growth strategies. While branch office development is more likely to occur by transferring partners to the new office than by merging with a local firm, other differences are not found. The failure to find any preference between internal development and lateral entry confirms the salience of the dilemma posed by distance that was discussed earlier, i.e., the tension between the desire for control and the advantage of a local presence. Firms are likely to make this decision at least in part based on their ability to support the branch for the period of time until it achieves profitability.

Effect of Strategic Decisions on Firm Economic Outcomes

The economic rewards of increasing organizational size have been widely studied. In the legal profession, the advantage of large firm size has been clearly demonstrated in recent surveys of law firm profitability; with few exceptions, the richest firms are the largest firms (e.g., Brill, 1985, 1986, 1987, 1988). However, such data do not allow one to break out the effect of increasing numbers from that of diversification into new legal areas and geographic locations. More meaningful information is generated by probing the differential effects on profitability of depth and breadth.

The economic advantage of increasing the size of the professional membership was demonstrated by this study's findings that annual revenue increases are realized by enlarging the size of the existing practice and by adding partners to new and existing practice areas by both promotion and lateral entry. Such a result is expected for law firms, where, as in other professional firms, revenues are primarily generated by hourly charges to clients¹. More interesting perhaps, given the seemingly tautological relationship between number of people and number of dollars in this type of firm, is the finding that size increases resulting from firm mergers do not have a significant effect on revenue. An apparant conundrum, this result seems to suggest that merger reduces lawyer productivity, measured in terms of billable hours, in the period immediately following the merger, perhaps as a result of the demands of the merger process itself. Anecdotal information obtained during the firm interviews supports this supposition. In each of the firms that had grown by merger, managing partners spoke of the hours devoted to reorganization, and to time "lost" to the need for acclimation to new people and ways of doing things. Additional longitudinal study incorporating longer lead times is needed to gain a fuller understanding of the effect of merger on revenue.

¹Hourly fees are often supplemented by premium billing, i.e., additional fees for exceptionally successful resolution of client matters.

In contrast to increases in the size of the professional membership, annual change in revenue is not related to practice development and, unexpectedly, is inversely related to branch office development. To repeat a point made earlier, the negative impact of branch office development on the following year's revenues may be a result of the tendency for firms to open branch offices with partners transferred from the principal office to the new one. To the extent that a branch office is not immediately fully productive, the result of this approach to branch office development would be to reduce revenues by reducing the number of producers in the principal offices without compensation for that loss by the branch office. Again, anecdotal information about the frequent need for branch office support for one or more years following inception supports this suggestion.

Longer term per partner profit outcomes of expansion are related not to increases in number of attorneys, but to product and market diversification. The economic structure of law firms is designed to increase the return to equity partners above that which would be realized in solo practice. Therefore, the incremental increases in revenue contributed by additional partners are returned to them in their share of the partnership profits. To improve profitability requires not that the number of partners is increased but that value is added to the firm such that more and better, i.e., higher paying, business results. Results of this study indicate that

both practice development and branch office development add value to the firm, albeit apparently in different ways.

Firm profitability increases with the addition of practice areas. Moreover, this effect on profitability is unrelated to the cross-selling of the firm's services. Apparently, the capability to provide full service adds value to the firm irrespective of whether clients benefit directly from the firm's greater breadth by using the firm's services in more than one legal field.

One possible explanation for this phenomenon is that reputation and perceived value by the client result from the firm's ability, utilized or not, to provide service. It may well be, for example, that the corporate client attaches some significance to knowing that a law firm has the capability to handle unexpected legal complications. However, an additional dimension, revealed in further analysis, is that the effect of practice development on profitability is limited to growth by lateral entry. Since typically there is a primacy of the client-attorney relationship over the client-firm relationship, it may be the particular attorneys brought in laterally who add to the firm's reputation and increase its value to clients.

Adding branch offices also increases profitability. However, the manner in which branch office development interacts with the cross-selling of branch offices to affect profit is somewhat more complex than the analogous development of practice areas. Unlike practice development, branch

office development without the multiple use of those offices by clients has a negative impact on profit. However, also in contrast to practice development, partner profitability increases for firms that mix branch office development with the cross-selling of their newly developed offices. However, though any amount of cross-selling appears to contribute to profitability, the relationships do not appear to obtain under conditions of high branch office development. In other words, high levels of branch office development may inhibit profit regardless of the amount of cross-selling of those offices. Though interesting, these conclusions must be considered speculative given the weaknesses of the statistical findings supporting them, specifically the low N of firms engaging in a high level of cross-selling.

Finally, it is notable that the effect on profit of branch office development occurs when branch offices are opened by internal development and by lateral entry but not by merger. From one perspective this result is surprising, since it would seem that branch offices opened by merger, which have a client base different from that of the principal office, provide more opportunity for cross-selling than would branch offices opened by internal development. In searching for an explanation, it may be instructive to again examine the particular nature of professional organizations. Though merger would not occur without considerable consonance by both parties as regards the quality and delivery of services, the sense of unity prerequisite to the proactive attempt to

convince clients of the merits of relatively unknown colleagues may be missing. In this sense, perhaps the "real" integration of firms across what are often large geographic distances simply does not occur between two formerly independent professional entities. Again, however, it is important to focus attention on the statistical explanation of low variance in the branch office development by merger variable that is a likely alternative to this speculation.

Effects of Strategic Decisions on Partner Departures

Norms dictating the rules for partnership in law firms have changed considerably in response to changes in the legal profession over the past decade. These changes have provided the impetus for this study and have informed much of the theorizing. Granted that economic results are correctly emphasized as important consequences of strategic action, a broader perspective is gained by looking at the effect of strategic decisions on firm cohesiveness. This is a particularly salient issue in law firms, which are professional organizations historically characterized by the lifetime commitment of their partners.

It was expected that the effects of disparities among firms in their policies about making partners would not be limited to partner entry but would also affect partner departures from the firm. Contrary to prediction, an inverse relationship between internal development and partner departures was not found; the firm that makes more partners

does not necessarily lose less. The logic behind this finding follows from earlier analysis which indicated that the degree to which law firms undertake internal development is influenced by associate-to-partner ratios, and not by promotion policies. However, results also reveal that firms which bring in more partners laterally do suffer more to leave, most often to accept positions at other firms or as general counsel to clients². The same is not true for merger. Apparently, the consequences of the two external mechanisms for law firms are different. This makes sense when one considers their different purposes. Merger is essentially a vehicle for rapidly effecting substantial size increases, an objective it can achieve in one occurrence. As regards the principal office, merger is therefore likely to be a unique event in the firm's life. Conversely, lateral entry is used to acquire one or a few specialists or rainmakers, such that growth by lateral entry signifies repeated occurrences of that mechanism. Greater growth by lateral entry is therefore likely to reflect firm norms that stress opportunity over stability.

²Data were not collected on attorneys who retired or passed away. A small number of departing partners went into solo practice, became judges, or left the practice of law. This category was not included in the analysis.

Theoretical and Applied Value of the Study

The results of this study point to new perspectives and conceptual refinements within three bodies of organization literature, including research on professional service firms, on organizational mobility, and on merger and diversification.

First, this study is contributory in developing knowledge about professional organizations. Little theoretical literature exists to guide research concerned with the strategic behavior of professional service firms, and this study represents the first investigation into the process of PSF growth. Two antecedent conditions commonly considered to influence organizational growth were found to be applicable to professional firms. These are the liabilities of small size (Aldrich & Auster, 1986; Penrose, 1959; Starbuck, 1965) and the benefits of a diversified product line (Ansoff, 1965; Galbraith et al., 1986; McNichols, 1977; Penrose, 1959). Other findings support the view that growth processes in PSFs are unique to this type of organization, such that findings from research conducted primarily on non-service firms are not readily transferable to PSFs (Drucker, 1973; Normann, 1984).

Of particular importance is the influence of associate-to-partner ratio on the promotion of associates to partnership. Promotion induces growth by impelling the concomitant addition of new associates so as to maintain stable ratio levels. Hence, having a high proportion of associates results in a high level of promotion, and promotions result in increasing size in response to the need for structural

stability. In order to accommodate this growth, additional business needs to be generated. This process is contrary to the usual principle that "the demand for labor...is...derived from the demand for the final product or service" (Rees, 1979, p.54). In PSFs, growth appears to be a response to supply as well as to demand.

One implication of this model of PSF growth is that there is an imperative for growth that would prevent the firm from effecting a firm/environment fit. For example, despite arguments that there is nothing in principle to inhibit indefinite expansion as long as a firm can elicit resources by satisfying some needs of society (Haire, 1959; Penrose, 1959; Starbuck, 1965), life cycle literature shows firms shifting between highly innovative birth, growth, and revival phases, and more conservative maturity and decline stages. An emphasis on efficiency, marked by price cutting and retrenchment of product/market scope, is widely agreed to characterize the latter phases (Miller & Friesen, 1984). The internal promotional and economic structures of the PSF may separate it from the set of organizations appropriately depicted by such growth patterns by creating the need for continual growth, thereby precluding such retrenchment.

In this study, law firms were shown to respond to a weak financial position by further growth, i.e., by bringing lateral partners into the firm to increase revenue through the introduction of new clients. This response is especially interesting in light of research suggesting that that power

in the law firm is inextricably tied to control of clients, and that it is the attorneys with client control who are responsible for the development of organizational policies (Nelson, 1988). Given the authority of rainmaking partners, their entrance into the firm during periods of economic uncertainty is particularly significant. A comprehensive model of PSF growth strategy should more fully demonstrate how professional service firms handle the process of decline. Moreover, in addition to organizational level influences on growth strategy, the present argument suggests that environmental influences, such as a flat or declining demand for services, should also be examined.

In the literature addressing organizational mobility, little attention has been paid to organizational factors that influence decisions to staff senior positions by lateral entry, which is attributed generally to the need for expertise not available within the organization. Analyses of the determinants of being closed versus open internal labor markets are comprehensive in ascribing reasons for the former (staffing senior positions by promotion) while largely neglecting the latter (individuals can enter any position); promotion is emphasized as the dependent variable (Baron, Davis-Blake, & Bielby, 1986; Doeringer & Piore, 1971; Osterman, 1984; Wholey, 1985).

This emphasis seems to presume that vertical intraorganizational mobility is more beneficial to the organization than horizontal interorganizational mobility. While outcomes

of a closed internal labor market, e.g., employee motivation and the development of firm specific skills, may indeed be functional, the results of this investigation indicate that equally important benefits accrue from lateral entry. Findings of this study indicate that lateral entrants are sought out for their client contacts and concomitant ability to generate revenues. Client control is one way in which laterals may help to control the organization's relations with its environment.

These results have important implications for the research in this area. Firms are rarely totally open or totally closed internal labor markets but rather fall somewhere inbetween. Therefore, rather than treating the two as a dichotomy, fuller understanding may result from investigations that seek out reasons for using both types of staffing patterns and ways in which firms integrate them into the same system. It may be that while closed ILMs facilitate internal processes such as employee evaluation, motivation and the development of firm specific skills, open ILMs serve the purpose of better managing relationships with the environment through the lateral introduction into the firm of individuals who can control resource dependencies. A model for analyzing this process should also account for how firms accommodate both types of staffing within one organization. For example, conflict might be reduced by using lateral entry and promotion for filling different types of positions, such as new versus existing positions, as evidenced in the law firms

in this study. Open and closed ILMs might also exist within one firm in different departments, depending upon the degree to which the management of internal processes or external relations is primary.

Study results are also pertinent to research on merger and on diversification. The salient issue is the joint discussion of merger and diversification, ubiquitous in organizational literature. Diversification is assumed to be the motive for merger, and merger is assumed to be the means to diversify (Lubatkin, 1983; Porter, 1987). The present study has demonstrated that, at least for professional service firms, this assumption is invalid. The law firms studied used merger as a mechanism for increasing the size of the existing practice, rather than for diversifying into new legal fields. On the other hand, diversification into new legal fields was most often -- and most successfully -- accomplished by the lateral acquisition of one or a small number of professionals, i.e., lateral entry. Thus merger and acquisition serve different purposes for law firm growth.

Though this distinction between merger and acquisition may be most meaningful within a discussion of professional service firms, a consideration of merger objectives, i.e., the reduction of risks caused by a lack of diversity versus the reduction of vulnerability due to small size, may provide some insight into the inconclusive body of research examining the performance outcomes of merger and diversification. Typically, the strategy literature makes no distinction between these

merger motives, but simply compares the performance of merger versus non-merger firms (Lev & Mankelker, 1972; Meeks, 1977; Mueller, 1980; Weston & Mansingka, 1971), despite the discussion of both size and diversity as motives for growth. Also, research on diversification has focused on performance outcomes of related versus non-related diversifiers (Bettis, 1981; Christensen & Montgomery, 1981; Rumelt, 1982), but limited empirical research has been conducted on the relationship between diversification strategy and performance (Lamont & Anderson, 1985). The failure of the research to adequately assess performance outcomes may be a result of the failure to identify relevant contingencies. Greater clarity may result from conducting research that examines the performance outcomes of all these possibilities: merger/acquisition of same business firms to effect size increases, merger/acquisition of related and unrelated firms to effect diversification, and merger/acquisition versus internal development to effect diversification.

From an applied perspective, the objective of a study on law firm growth is to provide guidance to managing partners and firm administrators responsible for making growth decisions. The findings of this study suggest a number of salient issues to consider in determining how to grow. Though statistics confirm the trend toward larger firm size, results demonstrate that increasing the size of the existing practice is not in itself the key to increased profitability. Rather, that benefit appears to derive from increasing the

value of the practice to the client. While a larger number of attorneys may serve that purpose for some types of practices, e.g., for mergers and acquisitions work requiring the ability to put a large number of attorneys to work on a matter on short notice, most firms will add value through the breadth of services offered and the stature of particular attorneys. Concerning practice development, findings have indicated that a broad complement of practice areas is important to profitability. Moreover, profitability accrues from entering new fields by bringing in lateral partners with established legal and client-management skills. Conversely, advantages to be gained from opening branch offices appear to be dependent on whether firm clients will make multi-site use of those offices. In addition, either internal development or lateral entry are appropriate for implementing the branch office development strategy, depending on particular firm objectives.

Results also have implications for firm structure. In determining optimum levels of associate-to-partner ratio, it appears important to consider the tendency for higher leverage to impel growth based on the exigencies of supply, such that projections about future demand for services should be an important factor in planning. This finding is especially salient in the face of an environment characterized by cost conscious clients, expensive associate salaries, and no room to increase the billable hours needed to leverage those salaries. Structural innovations such as permanent associate

positions and non-equity partnership arrangements are already being tested.

An overarching issue for law firm management growing out of this study is that law firms need to plan their growth. Throughout the planning and conducting of this research, I have spoken with many lawyers. Their responses to the concept of law firms as a subject for organization theory research were often funny and, in that humor, instructive. More than one lawyer expressed the thought that the notion of law firm strategic planning is an oxymoron, that law firms don't plan but rather grow by serendipity. Despite the drastic changes that have taken place in the environment for legal services, there is probably great truth in that statement. Most law firms don't plan, or at least don't engage in formal, long range planning. The results of this study suggest that this approach is becoming increasingly less viable. Law firms need to be responsive to the ebb and flow of corporate business activity. For instance, the enormous amount of business generated in recent years by leveraged buyouts and other merger activity is likely to subside, while new areas like environmental work and intellectual property matters are burgeoning. Though it is difficult to plan for this type of change, the structure of the professional firm is well suited to small scale entry into new fields, and even into new cities (though at a greater cost), allowing for flexible reactivity to environmental change. As the legal profession becomes, for better or worse, more imbued with the

conventional concerns of running a business, those firms behaving like businesses are more likely to survive and prosper.

Limitations of the Study

Implications for further research are related to two important methodological limitations: degree of generalizability and strength of explanatory power.

Constraints on generalizability result from several factors. The first derives from the primary criterion for inclusion of firms into the study population: that firms engage in a general corporate practice. This criterion precludes the generalizability of study findings to law firms that grow without expanding their fields of practice, i.e., specialist firms. Specialist firms practice in one or a small number of fields of law rather than offering general legal services (Nelson, 1981). Such firms would thus be limitedly expected to pursue practice and market development strategies. The growth process of specialist firms may be quite different from the general practice firms investigated in the current research. For example, do specialists engage in lateral entry; if so, under what conditions? Also, specialist firms tend to remain small, and may offer valuable insights into how firms manage the internal pressure for expansion. That is, how do they limit their size, given the internal push for growth created by the career expectations of firm associates?

The study design also precludes inference to firms in the earliest stages of development. The study sample includes only firms that are ten or more years of age. Hence, further research is needed to ascertain what factors are pertinent to the formulation of growth strategy in the start-up period of firm development. Conditions perceived as problematic by more mature firms, such as reliance on a small number of rainmakers, may be acceptable at early stages of development.

Another methodological issue is the strength of the data analysis for certain of the strategy/mechanism combinations. Specifically, the value of the analysis of hypotheses about practice development by merger and branch office development by merger is questionable as a result of the limited number of occurrences of those combinations. The low incidence of such growth is informative in revealing patterns in the way law firms grow, but does not provide adequate variability to conduct meaningful tests of hypotheses including these variables. This problem needs to be addressed by increasing the size of the sample of law firms studied, in order to increase the number, if not the proportion, of mergers.

Finally, the current study is constrained by its limited geographic scope. The sensitive financial and longitudinal data needed to test the research model necessitated collecting data through in-depth interviews. A local, New York City, rather than national population of law firms was thus sampled. Though the New York City population has merit for a

study of law firm growth, the generalizability of study findings is nonetheless limited by the restricted geographical breadth, i.e., by the want of empirical support for the assumption that the dynamics of law firm growth in the New York City metropolitan area are representative of law firm growth nationally. Research directed at a national sample of law firms, or in other metropolitan areas, is necessary in order to assess the applicability of findings to the larger law firm population. Indeed, an equally important avenue of research is to investigate other types of professional service firms, such as consulting and accounting firms, so that it can be learned to what degree the findings of this study inform us about growth processes in those organizations.

In addition to issues of generalizability, the limited strength of the predictor variables in the majority of regression models suggests the need to evaluate the analytical approach taken in this study. In most cases the amount of variance explained by the independent variables is less than twenty percent. Given study objectives of understanding determinants and outcomes of strategic growth decisions, this figure is of less concern for hypotheses predicting profit from growth strategy than for those predicting growth strategy from firm conditions. In the former case, the low R-square is informative in suggesting that law firm profitability is only partly a result of growth behavior; within that part, results permit comparison of

profit outcomes of the various growth options. The more serious issue is the limited amount of variance explained by the firm condition variables posited to influence growth decisions, which inhibits the descriptive and predictive utility of the models and indicates the need for a more fully specified growth model or for a different analytical approach to the study of law firm growth.

One explanation for the lack of robustness of the model may be the operationalization of client demand. In the absence of a direct measure, client demand was measured for this study in terms of the number of practice areas and branch offices opened as a result of client need; its influence in comparison to two other demand categories, market demand and "other", was determined by analysis of variance. This approach did not allow client demand to be included as an independent variable in any of the hypotheses tested by regression analysis. Consequently, its explanatory value could not be determined and its potential contribution to the strength of the model is unknown. The development of a more useful measure of client demand is thus desirable. However, the ANOVA results produced a potentially more important finding, i.e., that the perception that the firm should be in certain fields and certain cities in response to market needs is no less influential on practice and branch office development than is client demand. The implication of this result is that firms may enter new fields and cities, and do so through specific mechanisms, as a result of the beliefs of

key decision-makers. This suggests that a greater understanding of strategic growth in law firms may be found in an analysis of the decision-making process. One such approach to the study of law firm growth is presented in the following section.

A Suggested Approach to the Study of Strategic Growth in Law Firms

The present study hypothesized the choice of growth strategy as a function of internal firm conditions, most of which were highly quantifiable, e.g., firm size and number of practice areas. This analytical approach is based on a rational choice model of decision-making which assumes that decision-making is directed toward the maximization of consistent and congruent organizational goals. A more useful analytical framework for explaining strategic growth decisions in law firms may be a power or force model that explains strategic behavior in terms of the preferences of the power-holders who make key decisions (Pfeffer, 1981).

The influence of key decision-makers on corporate strategy has been the subject of considerable attention. The Carnegie School theorists argued that complex decisions are largely the result of behavioral factors, with decision makers bringing different sets of assumptions and knowledge to situations (Cyert & March, 1963; March & Simon, 1958). This view is in keeping with the strategic choice (Child, 1972) perspective which emphasizes the dominant coalition's

perception of environmental conditions and the decisions it makes about how to cope with those conditions. Given that strategic choices are decisions made under conditions of uncertainty, attention to the beliefs of key decision-makers should provide an important perspective in developing theories of strategic choice.

The specification of a model of law firm growth strategy based on the preferences and influence of key decision-makers assumes that authority for growth decisions is relatively centralized. At first blush, such an assumption appears minimally applicable to law firms, which are generally assumed to have a highly participative form of governance. However, though professional firms are characterized by decentralization (Mintzberg, 1979), some types of decision are made more democratically than others. In their study of corporate law firms, Tolbert & Stern (1989) found that decisions related to professional standards, such as promotion decisions based on colleagues' competence, are likely to be marked by greater participation than decisions linked to financial issues, such as compensation; the latter are more likely to be made by a smaller, more centralized body of partners such as an Executive Committee. The authors argue that only a small number of decision making areas are tied to professional authority. Indeed, Brill has suggested that the emphasis on law as a business has served to create near autocracy in law firm governance (1982). Decisions concerning business strategy would thus be expected to be decided by the subset

of partners who control resource dependencies (Pfeffer, 1981), such as major rainmakers.

To explain strategic decision-making within a power framework, it is necessary to identify the major coalition members for a particular decision or for a certain class of decisions (Cyert & March, 1963) and to specify their preferences (Pfeffer, 1981). Such a perspective implies that the interpretation of the environment by key decision-makers (Daft & Weick, 1984) is an important component of a model that attempts to explain and predict strategic decisions. Consequently, it is proposed that elements of a model of strategic growth decisions in law firms should include key partners' (power-holders) beliefs about practice and market development and about the firm's competitive strength, and the determinants of those beliefs. These elements are discussed below.

One primary influence on the choice of growth strategy is the strategic orientation of key decision-makers. The study of strategic types has assumed a prominent position in the strategic management literature (Brittain & Freeman, 1980; Miles & Snow, 1978; Porter, 1980). Strategic typologies typically include the generalist/specialist dichotomy. Generalists attempt to acquire market share across multiple segments of a market domain, while specialists focus on a particular buyer group, product line segment, or geographic market. Given the present emphasis on generalist corporate law firms, a more useful typology of strategic types is the

more fully differentiated one suggested by Miles and Snow (1978). In addition to specialists (Defenders), their typology includes Prospectors and Analyzers. These strategic types are defined by Miles and Snow (1978, p.29) as follows:

Prospectors are organizations which almost continually search for market opportunities, and regularly experiment with potential responses to emerging environmental trends. Thus, these organizations often are the creators of change and uncertainty to which their competitors must respond.

Analyzers are organizations which operate in two types of product-market domains, one relatively stable, the other changing...top managers watch their competitors closely for new ideas, and then they rapidly adopt those which appear to be the most promising...

The two types are distinguished from one another by the degree to which the entrepreneurial focus is on the development of new products versus maintaining a strong base of traditional products and customers. Hence, we would expect key decision-makers with a Prospector orientation to attempt to focus firm resources on readiness to meet changing market demand, with growth resulting primarily from the location of new markets and the development of new products. In contrast, key decision-makers with an Analyzer orientation would be those whose priority is to focus resources on the ability to meet the needs of existing clients, such that growth would result largely from market penetration, though with a meaningful amount of growth occurring through product and

market development in order to exploit proven practice and market opportunities.

Given that strategic types differ with respect to the degree of caution versus aggressiveness they exercise in defining their product/market domains, and given the differential effects of internal and external development on rate of expansion, decision-maker strategic orientation should also be expected to influence choice of growth mechanism. External development is better suited to the more aggressive expansion objectives of Prospectors. Analyzers should be expected to grow more cautiously and incrementally, using more internal development than acquisition.

A second major influence on growth strategy decisions is the firm's competitive strength in its chosen domain. Results of the present study indicate that this category should include size, as measured by number of attorneys, and client-getting or rainmaking strength. The importance of each of these has been discussed in Chapter 3 of this dissertation. To briefly review, liabilities associated with small size may affect a firm's desired growth rate, and hence its choice of growth mechanisms. Moreover, the ability to draw and keep clients is particularly important in an environment characterized by the declining institutionalization of law firm/client relationships. A different perspective from that proposed in the study is proffered here, however, i.e., the perceived firm strength in each of these areas as opposed to the objective measurement of the variables. In other words,

critical factors leading to growth decisions are posited to be: 1) the decision-maker's perception of the adequacy of the firm's size compared to the size perceived to be competitively viable for the firm's market, and 2) the decision-maker's perception of the firm's rainmaking strength, based on the percentage of rainmakers considered sufficient to generate revenues and to guard against threats of rainmaker departure. In contrast to the influence of strategic orientation, perceived competitive strength is proposed to affect the decision-maker's interest in engaging in lateral entry and merger/acquisition in order to increase size and bring rainmaking partners into the firm.

Decision-maker beliefs about strategic orientation and perceived competitive strengths are expected to derive from the belief structures they hold about the attributes that characterize a successful organization (Walsh, 1988). DiMaggio and Powell (1983) have proposed that, under certain conditions, decision-makers may model their own organizations after organizations in their field that they perceive to be successful. According to the authors, such mimetic isomorphism is more likely to result the more uncertain the relationship between means and ends, the more ambiguous or disputed the organization's goals, the greater the academic credentials of managers, and the greater the participation of managers in trade and professional organizations. These conditions are descriptive of the context of law firm growth strategy decisions: outcomes of strategic choices are uncertain; member,

client, and professional constituencies have expectations about firm structure and strategic behavior that need to be considered; and decisions are made by lawyers serving as managers. Consequently, decision-maker role models of successful firms are posited to be one influence on their growth strategy preferences.

Linking DiMaggio and Powell's thesis to a network analysis view of decision-making under conditions of uncertainty, Galaskiewicz and Wasserman (1989) suggest that managers are particularly likely to mimic the behavior of organizations to which they have some type of network tie. Citing a "network effect", the authors posit that network ties provide decision makers with models for behavior by allowing them to view how other organizations cope with environments similar to their own. The authors argue that "decision makers are more likely to mimic those whom they know and trust, and it's through the networks of boundary-spanning personnel that they come to know and trust one another" (p.456). The influence of network ties on law firm decision-maker preferences is particularly important in light of the current professional environment, i.e., the increasing acceptance of the view that law firms should be managed like a business, and the concomitant emphasis on the benefits of size, specialization, and multi-city capabilities. As a result of these changes, norms concerning the explicit attention to profit and, relatedly, practice and market expansion and the use of external growth mechanisms, have become inconsistent

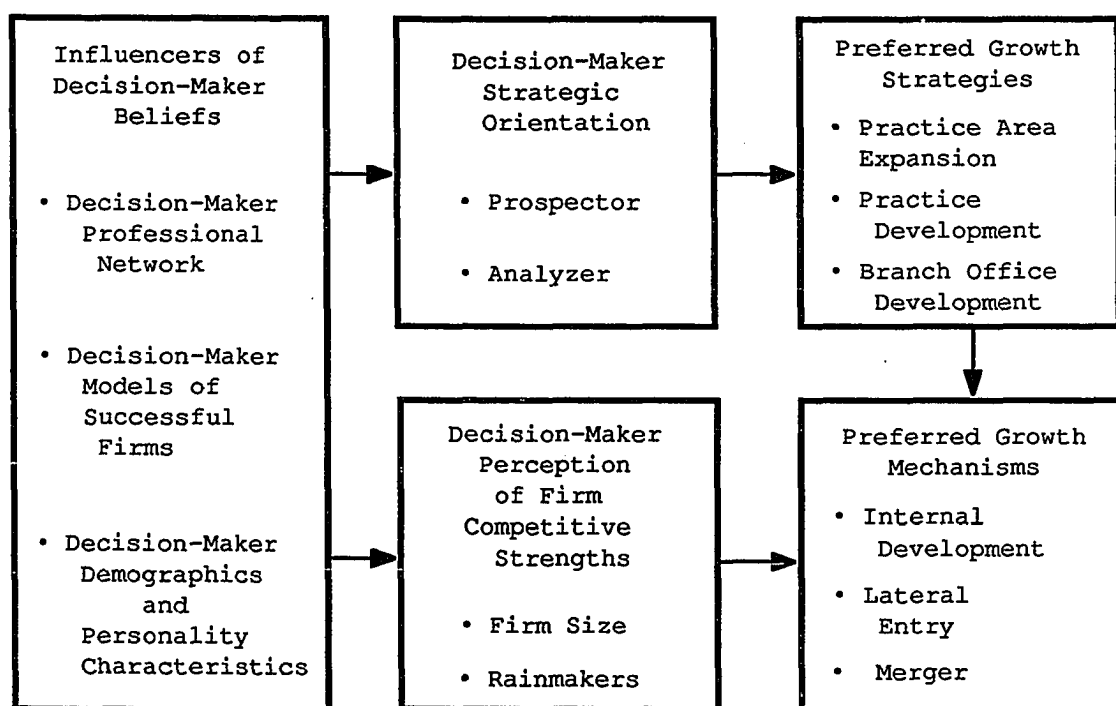
within the profession. Hence, decision-maker beliefs about how to grow are posited to be further influenced by personal contacts from within a professional network that holds a shared view of success and of appropriate standards of behavior.

Strategic preferences are also expected to be influenced by certain demographic and personality characteristics of key decision-makers. Hambrick and Mason (1984) have proposed that, given the complexity of strategic decisions, strategic choices are partially predicted by managerial background characteristics, such as age, functional background, education, and socioeconomic roots. Managers' values, needs, attitudes, and personality predispositions have also been proposed to be associated with political behavior (Vredenburg & Maurer, 1984) and with strategic and organizational orientations (Kets de Vries & Miller, 1986). Thus individual attributes of firm power holders are also posited to account for growth strategy preferences.

To summarize, the analytical approach being suggested views growth strategy as the outcome of the subjective process of enactment (Weick, 1979), which occurs as key decision-makers define a preferred strategic orientation and assess the firm's competitive strengths. Influencers of critical perceptions and beliefs include the decision-makers' professional network, models of successful law firms, and demographic and personality characteristics. The resulting preferred product/market orientation is expected to influence

choice of growth strategy, which in turn is expected to influence choice of growth mechanism. Additionally, resulting perceptions about competitive strength are expected to directly influence the choice of growth mechanisms. These relationships are depicted in Figure 5 below.

Figure 5
Decision-Maker Preference Model of Strategic Growth



Insofar as research methodologies are concerned, the analytical approach suggested here calls for a study design based on an interpretive research paradigm, i.e., a focus on understanding the strategists' thoughts and actions at a personal level (Smircich & Stubbart, 1985). Qualitative

studies using techniques such as participant observation, which are argued to be necessary for building theory from abstract phenomena under conditions characterized by problematic meaning, conflict, and social complexity (Douglas, 1976; Glaser & Straus, 1967), would thus seem to be appropriate. Key decision-makers could be identified by managing partners, members of the management committee, and other relevant firm members. Data on those partners identified as the primary formulators of growth strategy could then be gathered using semi-structured in-depth interviews.

The decision-maker preference approach to understanding law firm growth strategy has been presented as an addition to the firm conditions approach taken in the dissertation research. Rational choice models focus on the development and evaluation of alternative ways to achieve goals such as profit or efficiency. The origin of these objectives is not the primary concern of rational models, but is the focus of behavioral approaches, e.g., of power models. Thus, a behavioral approach should serve to increase understanding of the strategic growth process by considering key decision-maker perception of firm conditions criteria contributing to objectives.

Little is known about strategic growth processes in law firms, and in professional service firms more generally. At this stage of research, more can be gained from investigating strategic processes using a variety of models than by attempting to choose among analytical frameworks. It is in

this spirit that suggestions for future research include both efforts to improve the robustness of the firm conditions model through better operationalization of certain variables, and analysis of the role of decision-maker preferences. Eventually it may be possible to integrate findings from multiple analytical approaches toward a more comprehensive understanding of the growth behavior of professional organizations.

Appendix A: Pre-Interview Questions

1. In what year was the firm founded? _____

2. What is the current size of the firm's professional membership?

Partners _____

Associates _____

3. Which fields of law does the firm practice in? How much of the firm's total practice does each practice area represent? (Worksheet enclosed.)

4. For each year between 1983 and 1987, how many partners joined the firm's principal office? This would include associates who made partner each year, partners brought in laterally, and partners brought in through merger. Please exclude those partners brought in to begin new practice areas. (Worksheet enclosed.)

5. Which practice areas, if any, did the firm get into between 1983 and 1987? For each, please indicate the year that the practice area was started, and the number of partners and associates involved in the start-up who were current members, brought in laterally, or brought in by merger. (Worksheet enclosed.)

6. Which branch offices, if any, were opened between 1983 and 1987? For each, please indicate the year that the branch was opened, and the number of partners and associates involved in the start-up who were current members, brought in laterally, or brought in by merger. (Worksheet enclosed.)

7. How many partners left the firm between 1985 and 1988, excluding those who retired or passed away?

1985 _____

1986 _____

1987 _____

1988 _____

Fields of Practice*

Please indicate percentage of firm's practice represented by each field.

___ Admiralty	___ Housing/Urban Dev.	___ Trade Regulation
___ Administrative	___ Immigration	___ Transportation
___ Antitrust	___ Import/Export	___ Trust & Estates
___ Aviation	___ Insurance	___ Trademarks
___ Banking	___ International	___ Unfair Competition
___ Bankruptcy	___ Labor	___ Worker's Comp.
___ Business	___ Legislation	___ Zoning
___ Commercial	___ Litigation	
___ Communications	___ Literary Property	OTHER:
___ Construction	___ Malpractice	_____
___ Corporate	___ Maritime	_____
___ Criminal	___ Matrimonial	_____
___ Civil Rights	___ Mining	_____
___ Defamation	___ Municipal	_____
___ Eminent Domain	___ Negligence	_____
___ Employment Law	___ Oil & Gas	_____
___ Employee Benefits	___ Patents	_____
___ Energy	___ Personal Injury	_____
___ Entertainment	___ Probate	_____
___ Environmental	___ Product Liability	_____
___ Family	___ Property	_____
___ Finance	___ Public Utilities	_____
___ General Practice	___ Real Estate	_____
___ Gov't. Contracts	___ Securities	_____
___ Health Law	___ Tax	_____

* These practice areas have been culled from Martindale-Hubbell and are consequently somewhat artificial. Please feel free to combine or change them as necessary to accurately profile your firm.

Growth of Principal Office: 1983 - 1987

Number of New Attorneys

	Partners promoted from Associate	Partners added by Lateral Entry	Partners added by Merger
1983	_____	_____	_____
1984	_____	_____	_____
1985	_____	_____	_____
1986	_____	_____	_____
1987	_____	_____	_____

New Practice Areas: 1983 - 1987

Number of Start-up Attorneys

		Current Attys		Lateral Attys		Merger Attys	
		Partners	Assocs	Partners	Assocs	Partners	Assocs
<u>New Fields</u>							
Field _____		_____	_____	_____	_____	_____	_____
Year _____		_____	_____	_____	_____	_____	_____
Field _____		_____	_____	_____	_____	_____	_____
Year _____		_____	_____	_____	_____	_____	_____

New Branch Offices: 1983 - 1987

Number of Start-up Attorneys

		Transfer Attys		Lateral Attys		Merger Attys	
		Partners	Assocs	Partners	Assocs	Partners	Assocs
<u>New Branches</u>							
City _____		_____	_____	_____	_____	_____	_____
Year _____		_____	_____	_____	_____	_____	_____
City _____		_____	_____	_____	_____	_____	_____
Year _____		_____	_____	_____	_____	_____	_____

Appendix B

Interview Questionnaire

1. Respondent's Position: _____
2. Respondent's Gender: _____
3. Respondent's Age: _____ [From Martindale-Hubbell]
4. Respondent's Years with Firm: _____
5. I consulted Martindale-Hubbell for the number of partners and attorneys in your firm for the years 1983 - 1987. Could you confirm their accuracy for me? [Showed respondent firm size data; sample appears below.]

Firm Size: 1983 - 1988

	1983	1984	1985	1986	1987	1988
Partners	_____	_____	_____	_____	_____	_____
Associates	_____	_____	_____	_____	_____	_____

6. I also looked at Martindale-Hubbell for your branch offices. Do I have an accurate list?

[Referred to list culled from Martindale-Hubbell.]

7. What were the reasons for opening the practice areas new to the firm between 1983 and 1987?

[Referred to Pre-interview Practice Area worksheet and recorded responses on the New Practice Areas: Reasons worksheet.]

8. What were the reasons for opening the branch offices new to the firm between 1983 and 1987?

[Referred to Pre-interview Branch Office worksheet and recorded responses on the New Branch Offices: Reasons worksheet.]

Sample Worksheets

New Practice Areas: Reasons

Field: _____

Reason: _____

_____.
.
.

New Branch Offices: Reasons

City: _____

Reason: _____

_____.
.
.

9. As you know, some of my questions request financial data and this information is strictly confidential. Could we get figures on the percentage change in firm revenues for each of the years we're discussing?

% Change in Revenues from previous year

1983

.

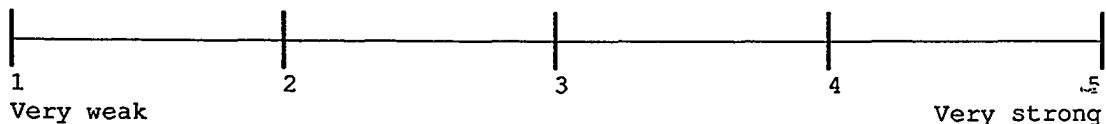
.

.

1987

10. In the firms I've visited, I've found a lot of disparity in firm policy toward making partners, with some firms being very committed to the traditional Cravath model of promoting from within, and others aggressively seeking growth through lateral partners and mergers. For the years 1983 through 1987, where would you place your firm on a continuum where 1 represents a weak commitment to growing by promotion from within and 5 represents a strong commitment to growing by promotion from within? For example, a "5" firm would be committed to never hiring a partner laterally. Conversely, a "1" firm could be characterized as actively looking for the kind of quick growth that lateral hiring brings regardless of immediate needs. In the middle, a "3" firm can be thought of as having a preference for promotion-from-within but willing to take in lateral partners when necessities or opportunities arise.

1983



.

.

.

1987

11. I've also observed that firms have varying amounts of funds available to invest in expansion objectives at any particular time. For example, sometimes a lateral partner will come with clients, but other times a firm brings in a lateral attorney specifically for some particular expertise and must wait for a period of time until that attorney begins to generate revenue. On this continuum, where would you place your firm with respect to funds available for growth in each of the years we are investigating?

1983

Could afford cost increases resulting from growth, such as lateral hiring and branching, for the sake of long-run benefits

Could not afford cost increases resulting from growth, such as lateral hiring and branching, regardless of long-run benefits

.
.
.

1987

12. Firms often practice in areas that do not recognize a large profit. This may be because the firm wants to maintain an area that will support other, more profitable areas, such as a trusts and estates department that serves corporate clients. There are other reasons, too, such as a department which is not currently profitable but is expected to be in the future. For the period we have been discussing, can you tell me which of the fields your firm practiced in that were minimally profitable?

1983?

.
.
.

1987?

13. Historically it was common for a firm to have a small number of rainmakers, say three or so, bringing in most of the firm's business. More recently, there seems to be an increasing interest in developing rainmakers throughout the firm. Whether or not records are kept on this, most attorneys in your position, indeed most partners in a firm, can identify the major rainmakers. Could you tell me how many major rainmakers there are in this firm? What per cent of the firm's business are they responsible for? How would those numbers have looked for the period we are investigating?

Number of RainmakersPercentage of Business

1983

.
.
.

1987

The next several questions concern financial and other data. In most cases, I need information only as of the end of 1987.

14. What percentage of firm revenues came from multi-service clients, i.e., from clients who use more than one of the firm's practice areas?
15. What percentage of firm revenues came from multi-site clients, i.e., from clients who use more than one of the firm's offices?
16. What was the average number of billable hours for partners?
17. What was the average number of billable hours for associates?
18. I'd like to know what your 1987 blended billing rate was. Some firms calculate this rate and can provide it to me. However, if your firm doesn't do this, I can calculate it myself if you would provide me with the range of rates for professionals and the number of lawyers who billed out at each rate.
19. Could you tell me the percentage change in average per partner profits from 1983 to 1987? For example, if the average in 1983 was \$100,000 and that had increased to \$150,000, the change would be in increase of 50%.
20. Finally, you have already provided me with figures on the number of partners who have left the firm each year between 1985 and 1988, excluding those who have retired or passed away. Could we discuss the reasons for their departures?

1985	
.	
.	
.	
1988	

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