BCG ATTORNEY SEARCH

Avoiding Merger Minefields

It's no secret that there is an intensifying rush to consolidate within the legal profession. And of course, we expect the future to bring larger and increasingly complex mergers to the legal profession. Those are likely to include transatlantic combinations—and even multidisciplinary ones.

But most merger talks do not result in a combination. Our experience is that for every proposed law firm merger that results in a union, seven to ten do not. Naturally, the specific reasons that merger discussions dissolve are unique to each situation. But there are often a few common pitfalls that doom mergers. Knowing what they are and taking steps to avoid them can save time and help ensure success.

Know why you're merging. Like corporate mergers, law firm mergers succeed when the merger partners have thought out their business plans and clearly defined their strategic goals. Too often, firms focus on the numbers and specific deal points without stepping back to think about what is to be gained through the combination. Will the merged firm cross-sell **legal services** more effectively? Will it become a major service provider for joint clients of the two merger partners? Do the firms have similar practices that will achieve critical mass when merged, or will the merger enhance the ability of complementary practices to serve clients? Is a merger the best way to realize each firm's goals, or is there a better alternative?

Usually merger discussions will reveal early on whether there is enough synergy to make a combination worthwhile. But when discussions focus on issues other than synergy and long-term strategy, these fundamentals can be overlooked until late in the game.

Take an expansive view of conflicts. Client conflicts, which are classic deal-breakers, are usually uncovered early in the process, because they are relatively easy to identify through each firm's conflict system. But conflicts can also exist when the merging firms have major clients in the same industry. These types of conflicts are a particular problem in competitive, consolidating industries like banking, telecommunications, and energy. Firms also should find and resolve conflicts that may arise when combining different types of practice areas, such as a banking practice and a bankruptcy practice.

Firms in merger discussions often make two key mistakes in dealing with conflicts. The first is the tendency to focus on the top 20 or 30 clients when identifying possible conflicts. Many conflicts do not occur at this level. Conflict checks should include a more in-depth comparison of clients before merger discussions advance too far. The second mistake is to dismiss potential conflicts cavalierly, with a "we can deal with that later" attitude. Lawyers take conflicts very personally, especially when they perceive that their clients or practices may be at risk. If merging firms make no attempt to resolve such conflicts, the affected lawyers will develop a negative attitude toward the merger that can spread throughout the firms.

Steer clear of culture clashes. Contrary to the conventional wisdom, governance issues are seldom the real reason law firm merger talks fail. Firms usually manage to work out leadership issues, even if it means creating cochair positions for a while. More often, it's the clash of firm cultures that derails a deal. A heavy-handed approach to merger discussions, where one firm dominates, can be a killer. This is especially true in discussions between two large firms. Usually firm culture is evident early on, but sometimes the true culture is not revealed until later, when both firms have had exposure to lawyers outside of the small group of partners who are involved in the bulk of the discussions.

Work out money matters. Like it or not, merger discussions often focus on financial issues—such as capital programs, use of debt, retirement plans, and profitability levels—because they can be the most divisive. Here, law firm mergers differ dramatically from corporate mergers. In the corporate world, companies are willing to make short-term sacrifices for long-term gain. In a law firm merger, there is more emphasis on short-term results and less on long-term returns. Unlike business executives, lawyers focus on the impact that a merger will have on their own compensation in the year or two after the merger. Senior partners nearing retirement may fear making a sacrifice without reaping the rewards down the road. Even younger partners who may benefit in the long run are unwilling to give up income in the short term.

Disparities in partner compensation levels (or in approaches to partner compensation) can be a major hurdle in merger discussions. These issues take on a whole new dimension in merger discussions between American firms and those in the United Kingdom or Europe. There are misconceptions on both sides of the Atlantic regarding work ethic, style and philosophy, among other things. Many corporations, banks, and insurance companies have overcome such cultural issues. The law firms that can follow the lead of these multinational organizations will be enormous winners.

Don't structure your own deal. While few lawyers would admit this, one of the biggest problems in law firm merger discussions is that the lawyers try to construct their own deals, and every detail of the deal becomes personal. Ironically, M&A lawyers can be the biggest hindrances to closing a deal because they are trained to pick deals apart. This approach leads many firms to focus on details rather than their strategic vision or the business rationale for the merger.

Details are important, certainly. But we've seen too many firms start an initial merger meeting discussing associate salaries, technology, unfunded retirement benefits, or whatever else comes to mind without first talking about why a merger makes sense for the market, the clients, and each firm's lawyers. Remember: If there is a clear business rationale for the merger, almost any deal point can be resolved.

Finally, be sure that you have a process and timetable in place in any merger discussions. This will help ensure that all potential issues are addressed—but addressed in order of importance.

When a merger is a good one, it is **an opportunity** for both firms to expand their practices, serve their clients better, and set the stage for dynamic long-term growth. By approaching mergers in a haphazard, ill-advised manner, too many firms miss these opportunities.