Risky Business

Rethinking Lateral Hiring.

February 2019

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Methodology

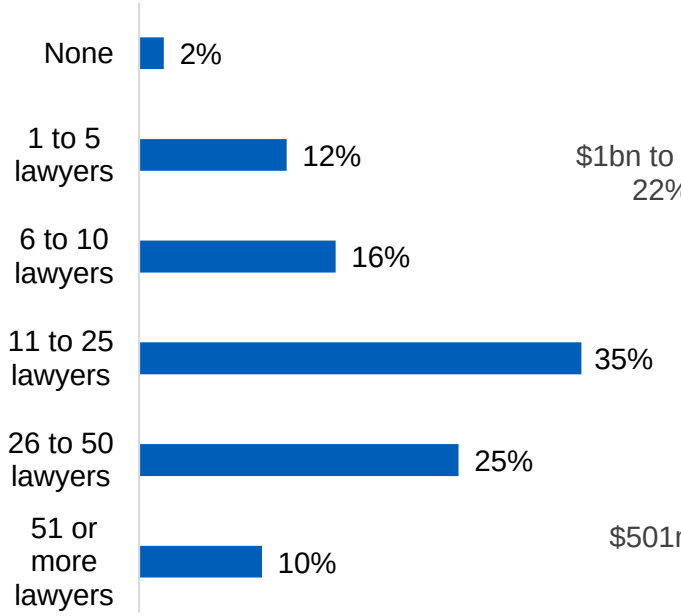
The data for the quantitative portions of this report came from a survey conducted by Decipher and ALM Intelligence as well as data from ALM Intelligence's Legal Compass, which contains information on lateral hiring, law firm financial performance and geographic expansion since 1978.

The ALM Intelligence - Decipher Lateral Partner Hiring Survey gathered data from over a quarter of the Am Law 200. A broad range of firms were represented in terms of size, profitability, and lateral hiring activity (see Figure 1).

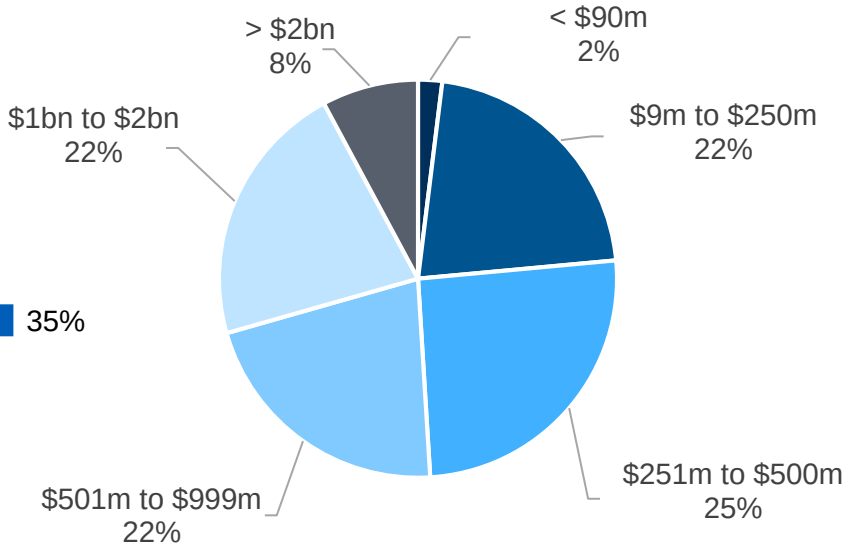
Over 50 one-on-one interviews were held with law firm leaders or other thought leaders with experience in lateral hiring. Interviews were held with over 40 Am Law 200 law firms representing a broad range of global, national, and regional firms. Interviewees typically held leadership positions within the firm holding titles such as managing partner, head of talent or lateral hiring manager. Topics discussed included, but were not limited to, lateral hiring strategies, due diligence, risk mitigation, and lateral partner integration.

Figure 1: The ALM Intelligence - Decipher Lateral Partner Hiring Survey

How many lateral partner hires has your firm made over the past 12 months?
Percentage of firms responding



What was your firm's revenue last year?
Percentage of firms responding



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Introduction

The rewards associated with hiring lateral partners has made the practice an essential part of operating a successful law firm. However, the allure of increased revenue and profitability has dulled firms' senses to the immense risks inherent in the lateral hiring process. To some degree this is understandable. Hiring a lateral partner offers a quick and efficient solution to many of the thorniest challenges facing law firm leaders. For firms struggling with slow growth, lateral hiring offers the tantalizing prospect of new clients and new revenue. For those looking to expand into new markets, hiring provides a way to build scale in new services and new geographies quickly. To law firm leaders who have been struggling against difficult market conditions since the downturn and seek to grow their firm's market share, these opportunities have, seemingly, been too good to pass up.

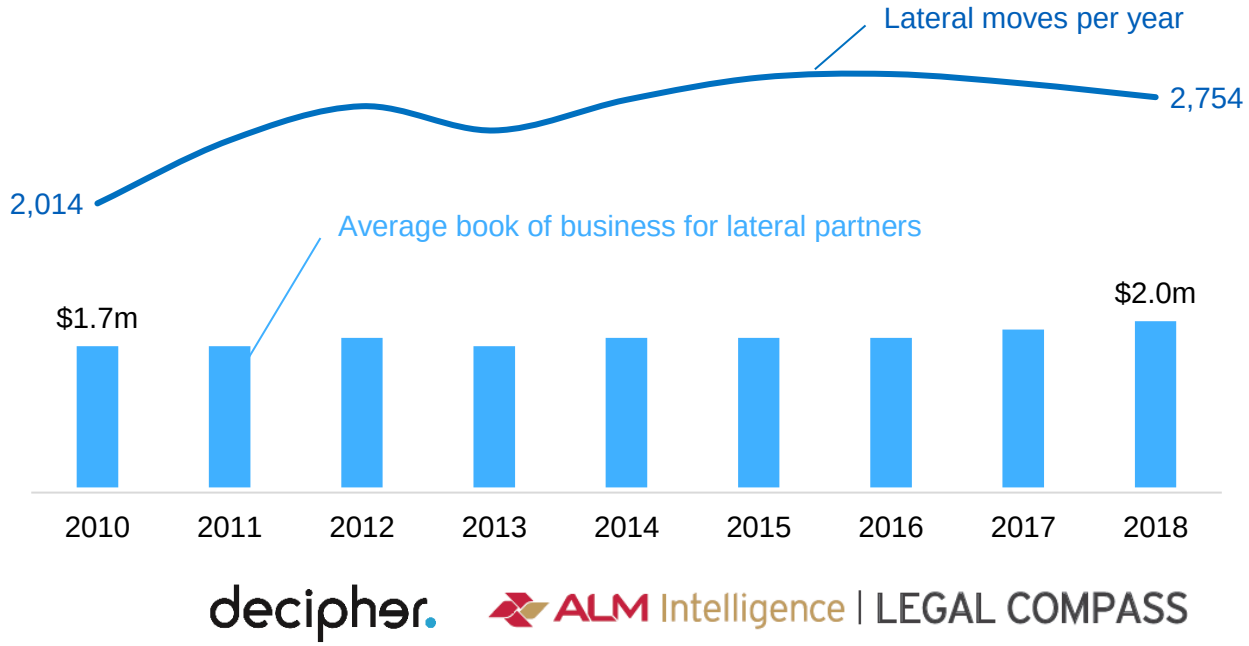
> ***The total book of business moving through the lateral markets, from 2014 to 2018, is estimated to be $17.1 billion for Am law 200 firms.***

Here's the problem. The cost of acquiring lateral partners is incredibly high as are the failure rates. Why have most firms been willing to accept such low returns? Part of the problem is that defining what constitutes a 'failed' lateral hire is extremely difficult. No single study is detailed enough to accurately measure the many ways a lateral hire can 'fail'. Measuring 'failure rates' requires understanding the individual components of 'failure', which are fragmented across many sources. For instance, one study[1] by Hugh Simons, a former chief operating officer of Ropes & Gray, legal market researcher and commentator, and ALM Intelligence Fellow, found that almost half of all laterals do not even last five years at their new firm. The ALM Intelligence - Decipher Lateral Partner Hiring Survey, which features input from a quarter of the Am Law 200 and was part of the research for this report (see the Methodology section for more detail) found that nearly 70% of hires underperform in bringing their expected book of business. Such low success rates are particularly striking given the sky high costs of hiring laterals. ALM Intelligence estimates hiring a lateral partner in today's market averages $2.3 million dollars, with the most coveted partners costing well over $5 million. These figures suggest that the return on investment in the lateral markets is low.

[1] Global Lateral Hiring by The Numbers: A Look Behind the High 5-Year Attrition Rate, Hugh Simons, The American Lawyer, February 2017

Figure 2: The Importance Of The Lateral Partner Hiring Market

Lateral moves and average book of business of lateral hires
For Am Law 200 firms



In addition to poor retention rates and financial considerations, large law firms are more scrutinized than ever before. Firms are being forced to police the behavior of their partners, address the growing cost of staff and associate turnover, and conform to the client's values on issues like diversity and pay equity. Revelations over the past eighteen months connected to partner misbehavior, and the empowered voice of the #MeToo movement have highlighted risks which law firms have, up to now, largely ignored. Law firms face significant risk from issues related to work place harassment and malpractice. Settlements in these types of cases can be enormous. The damage such cases do to a law firm's brand can be even greater. While any partner can commit these actions, there is some evidence to believe lateral partners may be more likely to be "bad actors." This evidence, along with the data presented in this report, suggests law firms should tread very carefully when considering lateral candidates.

The solutions to these problems are relatively straightforward. This report argues that law firms must start treating lateral hires as their own clients treat the hire of senior executives. Firms must see lateral partner hires as significant investments that will shape the future of the firm. Candidates must be consistently and thoroughly vetted from all angles. The business case for each hire must be examined and quantified. The risks related to these prized individuals must be investigated, understood, and, when possible, mitigated. Many firms may argue they are already

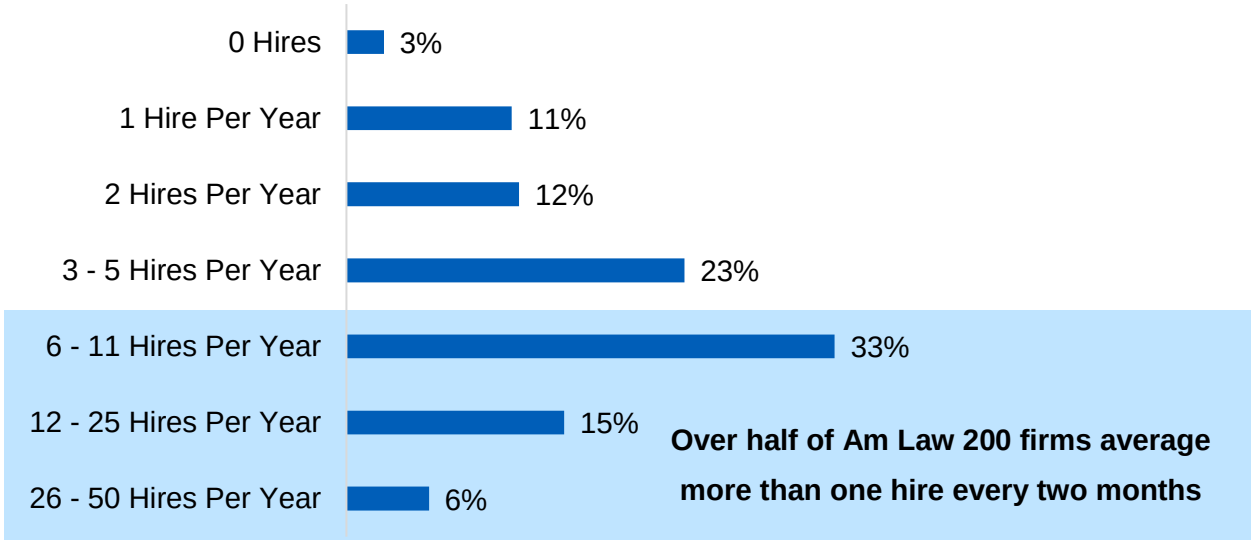
doing such investigations. Interviews with dozens of managing partners and heads of talent from Am Law 200 firms, which were held as part of the research process for this report, suggests some firms are following best practices. Those interviews also reveal that the due diligence process at most firms leaves much to be desired. Law firms vetting processes are uneven, incomplete, and, in most cases, merely skim the surface

> ***"It takes leaders with a certain maturity and self-confidence to have their instincts tested with third party data about a candidate. Facts are our friends even if, or perhaps especially when, they are counter to our expectations"***
>
> *- Hugh Simons, former COO of Ropes & Gray*

To assist law firms in the process of overhauling their lateral hiring programs to improve success rates and reduce risk, this report examines the opportunities and the challenges law firms face in lateral hiring. The ultimate goal is to assist law firms with the evolution of their lateral hiring programs to a point where the risks and opportunities of each hire are fully understood and incorporated into the business plan, maximizing the chances of success, not only for the firm and the lateral, but for all stakeholders – staff, associates, clients, and leadership.

Figure 3: Almost All Firms Hire Lateral Partners

Percentage of law firms by number of lateral hires per year
Average of moves for Am Law 200 firms between 2014 and 2018



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Status Quo: Big Hires, Big Opportunities

The opportunities created by lateral hiring are relatively clear. The market for laterals offers law firms the ability to gain access to top quality talent (and their books of business) which, under the best circumstances, would have taken them years to develop internally. As cultivating talent is at the heart of most law firms' business models, the opportunity to attract gifted lawyers is critically important to the long term success of the firm, both from a cultural and financial standpoint. Lateral hiring can help firms meet short term goals – such as filling revenue gaps created by departing partners or lost clients – as well as help firms achieve long term strategic initiatives such as expanding into new markets, building new client relationships, or solidifying their all-important succession strategy.

Everyone Hires

In the five years from 2014 through 2018, there were almost 9,000 lateral partner moves from one Am Law 200 firm to another. While some firms do more hiring than others, no single firm accounts for more than three percent of the total moves among the Am Law 200. In fact, lateral partner hiring is much more common than most appreciate. Data from ALM Intelligence's Legal Compass shows that ninety-seven percent of Am Law 200 firms made a lateral partner hire in the past five years (see Figure 3). Data from The ALM Intelligence - Decipher Lateral Hiring Survey sheds even greater light on these statistics. Seventy percent of firms surveyed have made at least 10 partner hires over the past 12 months, and 10% have hired 50 or more partners during the same time period. This dispels an important myth – that lateral hiring is only important to a subset of large law firms.

One of the most interesting trends over the past several years is the increasing use of lateral hiring among "elite", or high profitability, firms. This trend, which is most evident when looking at the lateral hiring track record of Kirkland & Ellis, is new. James Jones, a Senior Fellow at the Center on Ethics and the Legal Profession at Georgetown University Law Center, notes that "high profitability firms are more active in the lateral markets than ever." Jones believes these firms have moved into the lateral markets because they see talent which will ultimately help their value proposition with clients. He also believes elite firms have increased their use of lateral hiring "because they can" adding "these firms have outpaced the rest of the market in terms of profitability growth, they are using their profit per equity partner as a weapon to attract talent and gain market share."

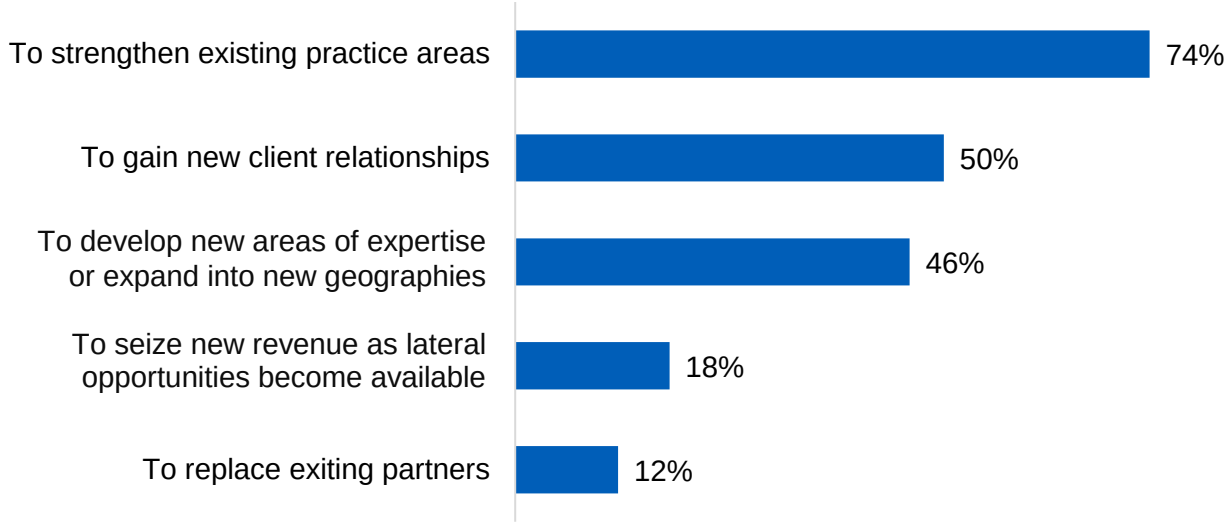
The data is clear: all firms, regardless of size, financial metrics, or geographic footprint, are actively and aggressively hiring lateral talent. Firms are competing in a lateral partner arms race. Against this backdrop, it is critical to understand the motivations behind why firms hire lateral partners.

Hiring Laterally to Strengthen Existing Practice Areas

According to the ALM Intelligence / Decipher Survey, the most cited reason Am Law 200 firms gave for hiring lateral partners is to strengthen the firm's existing range of services. Three-fourths of law firms reported that strengthening existing practices was one of their top two motivations for hiring lateral partners (see Figure 4). Research on lateral hiring provides some useful clues as to why law firms are using lateral hiring in this way.

Figure 4: Why Law Firms Hire Lateral Partners

Law firm's motivation for hiring lateral partners
Percentage of law firms reporting



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Studies on both the legal industry[2] and other professional services industries[3] consistently report that lateral hires aimed at bolstering existing strengths have significantly higher success rates than other types of hires. Heidi Gardner, a Distinguished Fellow at the Harvard Center on the Legal Procession and the author of a book on lateral hiring titled Smart Collaboration for Lateral Hiring, argues these types of hires are more successful for several reasons. Gardner reports that

[2] Surmounting the Lateral Partner Hiring Challenge: Lessons Learned, Best Practices, and Tools for Success, ALM Intelligence
[3] The Risky Business of Hiring Stars, Harvard Business Review

her empirical research “shows that lateral hires who engage in collaborative work with their new colleagues are about sixteen times more likely to stay longer with their firm, to hit or exceed their targets, and to thrive professionally”. The logic behind this is fairly straightforward. She argues that joining an established group allows laterals to plug into existing networks and business development activities without needing to educate the firm about the value of what they bring. A firm already engaged the lateral’s area of expertise also has client relationships that require that sort of expertise, making it more likely that the newcomer would benefit from the firm’s reputation in that area. Lastly Gardner argues that “laterals who join an existing group have an instant community that they can turn to for help, advice on the unwritten rules of their new firm’s culture, and so on—provided, of course, that their new peers welcome them as enhancements rather than competitors.”

> ***Studies on both the legal industry and other professional services industries consistently report that lateral hires aimed at bolstering existing strengths have significantly higher success rates than other types of hires.***

There are also strategic reasons for focusing on building practice area depth. A recent study[4] on Chambers & Partners practice area rankings by Hugh Simons, shows that stronger practice areas are more sustainable. Firms with established practice areas have a significant competitive advantage when it comes to attracting, hiring, and retaining talent. This hiring advantage has a direct effect on a firm’s revenue and profitability.

Lateral Hiring as a Way to Bring in New Clients and Support Growth

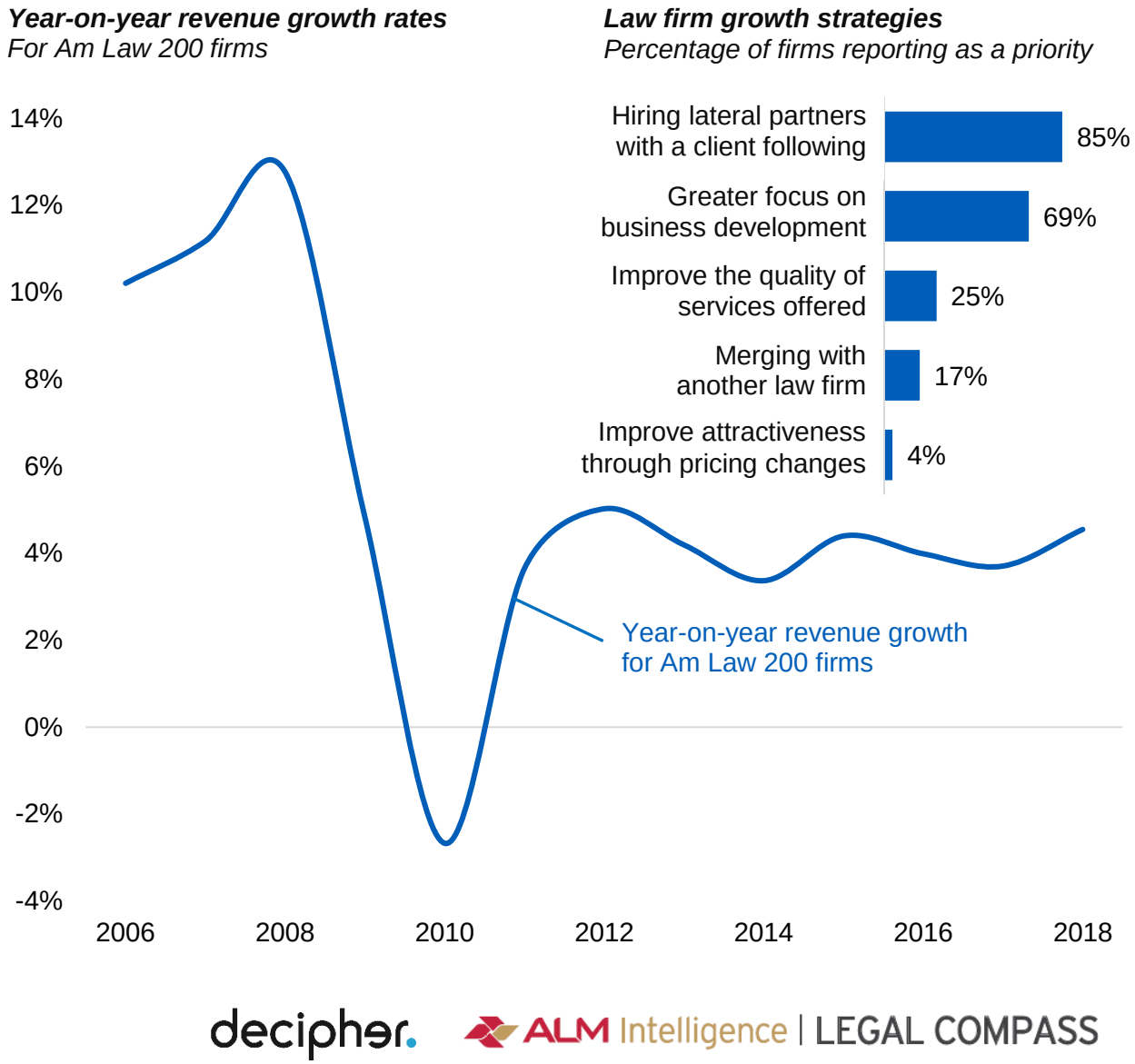
The survey’s second-most cited reason why firms hire laterally is to gain new client relationships. Half of the surveyed firms reported this as one of their top two motivations for hiring lateral partners. Given the sluggish, slow-growth environment over the past several years, this should come as no surprise.

Growth has slowed significantly since the pre-downturn era. Reports out of Citi and Wells Fargo, banks that service law firms and have access to their most intimate financial details, consistently reveal demand growth is slow by historical terms. ALM Intelligence’s revenue data reveals a similar trend (see Figure 5). Revenue growth for the past five years has averaged 4.0% per year, far less than the 10.7% average in the five years that preceded the downturn. Despite this, the appetite for growth has not subsided, causing firm leaders to look for new sources of growth,

[4] The Power of Just Getting Better at What You Already Do, by Hugh Simons, January 2019, Law.com

often in the form of hiring partners with existing client relationships. Eighty-five percent of law firms report that hiring laterals with a book of business is a high priority in their revenue growth strategies (see Figure 5).

Figure 5: Declining Growth Rates Have Increased The Importance Of Lateral Hiring



Given the enormous amount of revenue moving through the lateral partner markets, law firms' focus on lateral hiring is understandable. ALM Intelligence estimates that between 2014 and 2018, the total book of business moving between Am Law 200 firms due to lateral movement

was $17.1 billion. If lateral hires from smaller firms were included[5] that estimate increases to $20.5 billion. This is significantly higher than alternative means of growing law firm revenue. Revenue growth tied to increases in hourly rates only accounts for $9.7 billion; less than half the amount of the lateral market over the same time period. Given these extraordinary figures, it's no surprise that many law firms have turned to hiring laterals with a client following as a means to grow quickly and efficiently.

> ***The total book of business moving through the lateral markets, from 2014 to 2018, is estimated to be $17.1 billion for Am law 200 firms.***

The opportunity for growth through lateral hires comes with a caveat: hiring and integrating successful laterals is not an easy endeavor, and often ends in failure. Shockingly, the majority of lateral hires fail at their new firm, either by not delivering their advertised book of business or by leaving within five years (see section below titled "Retention Rates and Book of Business Conversions"). Interviews with law firm leaders reveal consistent disappointment with laterals' ability to port clients and revenue from their previous firms.

Lateral Hiring to Support Expansion

The survey's third-most cited reason why Am Law 200 firms hire lateral partners is to develop new areas of expertise or expand into new geographies. Again, this motivation has strong ties to wider legal market trends. Am Law 200 firms have opened over 1,000 new offices in the past decade and half (see Figure 6). Kent Zimmermann, a principal at Zeughauser Group who advises law firms on strategy and growth, notes that "while some offices have been opened via internal transfers of trusted partners from other offices, most of the growth has been with lateral hires". Zimmermann argues the logic behind this strategy is fairly straightforward and is akin to a buy versus build decision. Building an office with internal transfers can take a long time and organically building a new sought-after mix of clients and work is an uncertain path. The transferred partners typically would need to develop new relationships and establish himself or herself as a "go to" lawyer in the new market. Buying in to a new market, with lateral hires and groups of lawyers may offer firms a short cut. "Instead of building a new office over time, law firms often choose to acquire an existing reputation and established book of business through lateral growth" Zimmermann notes.

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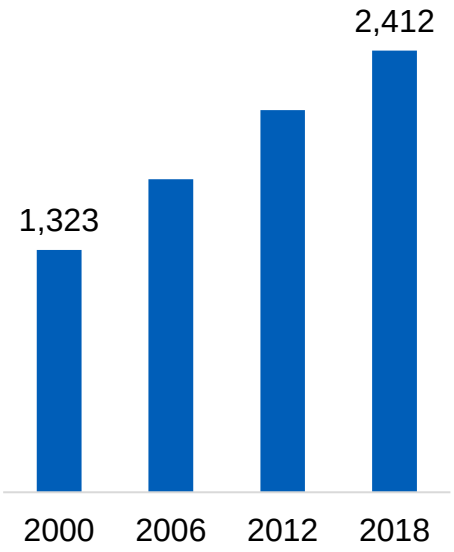
[5] Lateral moves from smaller firms are defined as a lateral partner move where the partner joined an Am Law 200 firms and departed a firm outside the Am Law 200.

Figure 6: Lateral Hiring Has Been Used To Support Geographic Expansion

Number of law firm offices
For Am Law 200 firms



Top 10 domestic markets for lateral hires
For US metro areas since 2001

Metro Area	Lateral Partner Moves	Office Openings
New York	6,634	38
Washington D.C.	5,606	16
Chicago	2,854	41
Los Angeles	2,175	41
San Francisco	1,648	47
Boston	1,351	26
Houston	1,254	46
Dallas	1,160	29
Atlanta	1,000	24
Philadelphia	917	25

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The strategy of using lateral hires to break into new markets is not without risk. Zimmermann notes that many firms find that hiring individual laterals can be a slow, error-prone and expensive way to grow. In addition, Zimmermann notes that "Law firms that aspire to grow into a new market sometimes compromise on reputation, quality or practice mix in the hopes of gaining a toehold to build from" adding "when this happens, firms generally end up regretting that approach later". Research on the legal market backs up Zimmerman's observations. As noted previously, studies on lateral hiring have consistently shown that hires focused on supporting existing strengths have higher success rates. These same studies have shown that lateral hires used to break into new service areas or new geographies are among the most risky. A 2015 study by ALM Intelligence[6], for example, revealed that law firms who believed lateral hires focused on "adding new skills to the firm" were the most challenging types of lateral hires. Interviews with law firm leaders for this report suggest the findings from 2015 continue to hold up. Firms consistently reported, in interviews, that their hiring success rates are lower when using lateral

[6] Surmounting the Lateral Partner Hiring Challenge: Lessons Learned, Best Practices, and Tools for Success, ALM Intelligence

hiring to break into new markets. Despite this, firm leaders believed they had few other options. Most firms felt lateral hiring was the only way to build local offices to a sustainable size.

Succession Planning

While supporting existing practice areas, acquiring new clients, boosting growth, and facilitating expansion all provide compelling reasons for firms to hire laterally, there are additional reasons for firms to look to the lateral markets for help. Among the most compelling is to replace exiting partners. Succession planning is an ongoing problem at most law firms. Even the most prepared firms suffer from unexpected vacancies. In situations where a partner departs for another firm or unexpectedly stops practicing, the lateral markets can help fill a much-needed skills gap. Given this dynamic, it is somewhat surprising that only 12% of firms reported “replacing exiting partners” as a primary motivation for lateral hiring. In interviews with law firm leaders, many reported that the lateral markets were vital in cases of unexpected vacancies. One way to understand the inconsistency between law firms’ reported motivations and their comments in interviews is that most firms view hiring laterals for succession planning as ad-hoc cases rather than strategic moves. This may help explain why firms did not report succession planning as a primary motivation for lateral hiring programs.

Key Takeaways: Lateral Hiring Supports a Range of Goals for Law Firms

- **All firms hire:** Ninety-seven percent of Am Law 200 firms made a lateral partner hire in the past five years. Slightly more than half averaged at least one lateral every two months over that period, and one-quarter averaged at least one lateral per month.
- **Least risky forms of lateral hiring:** Studies show that hires focused on reinforcing a firm’s existing strengths are significantly more successful than other types of lateral hires.
- **Firms are hiring to facilitate faster growth:** Roughly $20.4 billion of client revenue has moved firms due to laterals between 2014 and 2018. Lateral partner hires represent the single largest source of revenue growth potential for law firms.
- **Lateral hiring is being used to support geographic expansion:** Firms have relied heavily on lateral hiring as the most efficient way to support their aggressive geographic expansion goals over the past decade.
- **Firms are undervaluing the importance of succession planning:** Hiring laterals in an attempt to replace lost revenue from departing partners is an underrated reason for why firms hire. This is particularly true in cases where the firm did not have a succession plan in place for exiting partners.

Risk, Reward, and Failure

While the opportunities available to law firms in the lateral partner market are large, so are the risks. Firms are exposed to an enormous amount of risk when it comes to lateral hiring. Often law firms overlook or misunderstand these risks, which go well beyond just the financial aspect of a lateral hire.

The Cost of Acquiring Lateral Partners

Before looking at rates of success and failure it's important to acknowledge that acquisition costs in the lateral partner market are extremely high and firms put significant capital on the line with each hire. Most firms carry many hundreds of thousands of dollars in cost related to staff who are required to screen, interview, and integrate lateral hires. Additionally, firm partners spend a significant amount of time recruiting and interviewing candidates. This time should be considered as cost as it would have otherwise be spent billing or developing new business. Recruiter's fees, another key cost component, typically costs the hiring firm between 20-25% of the lateral's first year salary. This typically adds up to hundreds of thousands of dollars. All of this precedes the largest cost figure: the lateral partner's often guaranteed salary costs.

> ***ALM Intelligence's analysis reveals that the average cost of acquiring a lateral partner was $2.3 million in 2018, including one year of compensation, recruiter's fees and other internal costs associated with the acquisition. If two years of compensation is included, which nearly every lateral receives, then the average cost increases to $4.2 million.***

Convincing a partner to move their practice and client relationships to a new firm requires, in most cases, some form of guaranteed salary. In the post-Dewey environment, most firms won't admit to utilizing guaranteed salaries, however it still happens regularly (for those who do not remember Dewey & Leboeuf's demise is partially blamed on their use of lateral guarantees). Most firms give partners a two, or sometimes three-year grace period to port their clients and establish their practice. Firm leaders may not like to call these grace periods 'guarantees,' but on the balance sheet they look the same. They amount to millions of dollars in payouts to lateral partners, regardless of performance.

ALM Intelligence estimates the cost of acquiring lateral partners ranged from $525k to $8.7 million in 2018[7]. ALM Intelligence's analysis reveals that the average cost of acquiring a lateral partner was $2.3 million in 2018, including one year of compensation, recruiter's fees and other internal costs associated with the acquisition. If two years of compensation is included, which nearly every lateral receives, then the average cost increases to $4.2 million.

James Jones, a Senior Fellow at the Center on Ethics and the Legal Profession at Georgetown University Law Center, argues law firms have not done enough to manage the costs associated with lateral hiring. The data suggests law firms have, for the most part, have done a fairly good job of managing cost in the post downturn era. Lateral hiring stands out as an exception. James believes that "firms have not done enough to ensure they are getting good returns on their investments in the lateral hiring space."

What Is The Lateral Failure Rate?

Sky-high acquisition costs combined with low success rates are what makes lateral hiring such a risky endeavor. As firms hire laterals for a wide range of reasons, defining what constitutes a "failure" can be extremely difficult. Many factors can contribute to a lateral partner's failure. Some of these factors may become apparent immediately, while others may only be realized years later. For most firms, however, failure should be defined through a combination of: (1) the hire's longevity (or lack thereof) at their new firm; (2) the amount of realized revenue which they assisted in bringing in; (3) their integration into the firm's culture, and, perhaps most importantly (4) their impact on the firm's profitability.

Figure 7: Defining success and failure in lateral partner hiring

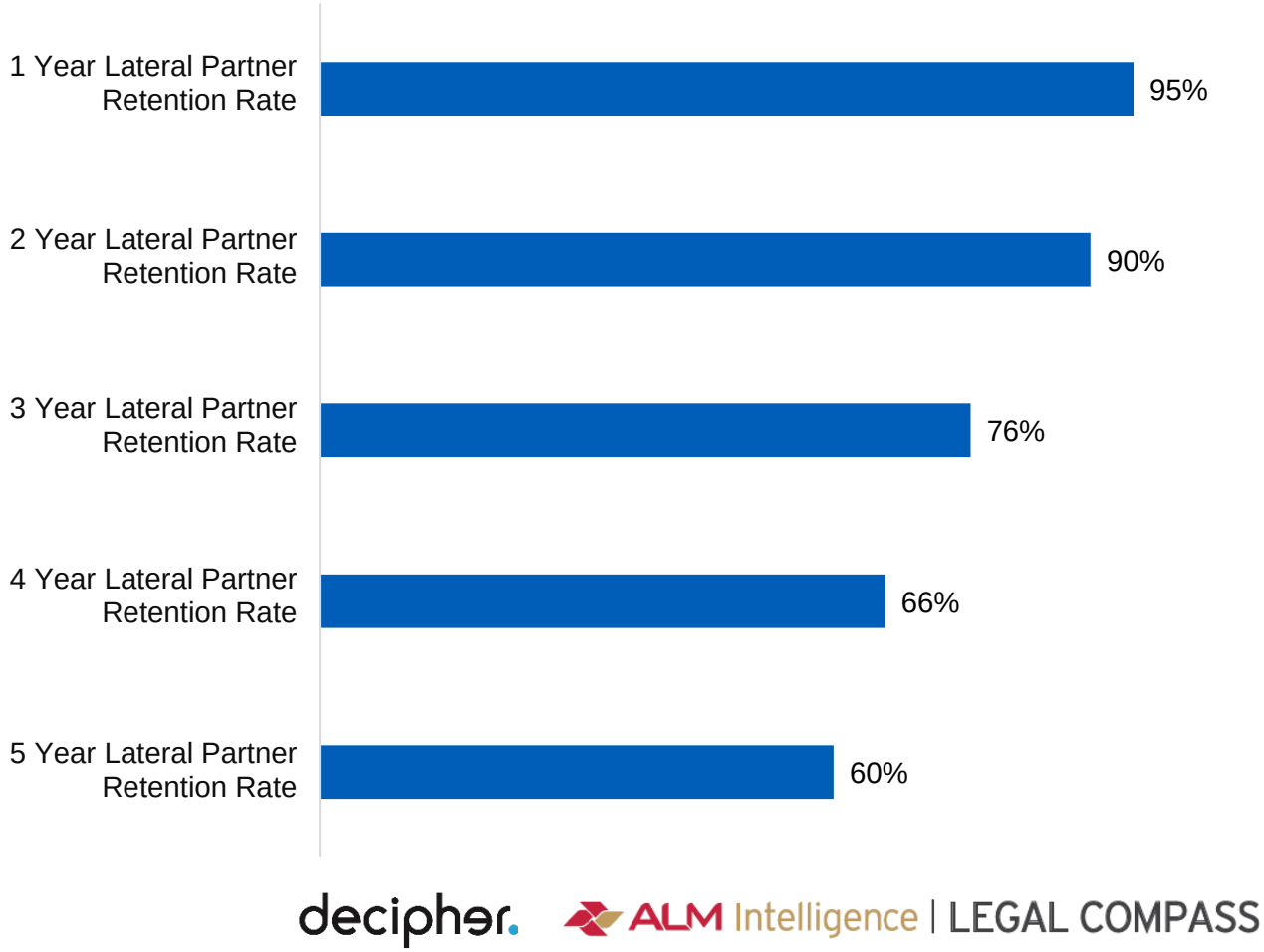
1. **Longevity:** The hire's longevity (or lack thereof) at their new firm.
2. **Revenue:** The realized revenue which the partner assisted bringing to the firm.
3. **Culture:** The partner's interactions with partners and staff.
4. **Profitability:** The partner's impact on the firm's profitability.

[7] This range represents the 10% percentile to the 90% percentile.

Longevity. An analysis of ALM Intelligence's Legal Compass data, which includes information on +20,000 lateral moves over the past decade, suggests that 40% of Am Law 200 partners leave the hiring firm within five years. Other studies suggest the figure is even higher. A study[8] by Hugh Simons suggested that nearly half (47%) of all Am Law 200 lateral partners leave their new firm within five years. If these trends hold, in three years' time, almost a quarter of last year's crop of lateral partner hires will have already left the firm that hired them this year (see Figure 8). The implications of this data are distressing. Even before factoring in financial metrics into the lateral "failure equation", nearly half of all lateral partners fail simply because they leave their new firm within five years.

Figure 8: Retention Rates For Lateral Hires

Retention rates for lateral partner hires
For Am Law 200 firms



[8] Global Lateral Hiring by The Numbers: A Look Behind the High 5-Year Attrition Rate, Hugh Simons, The American Lawyer, February 2017

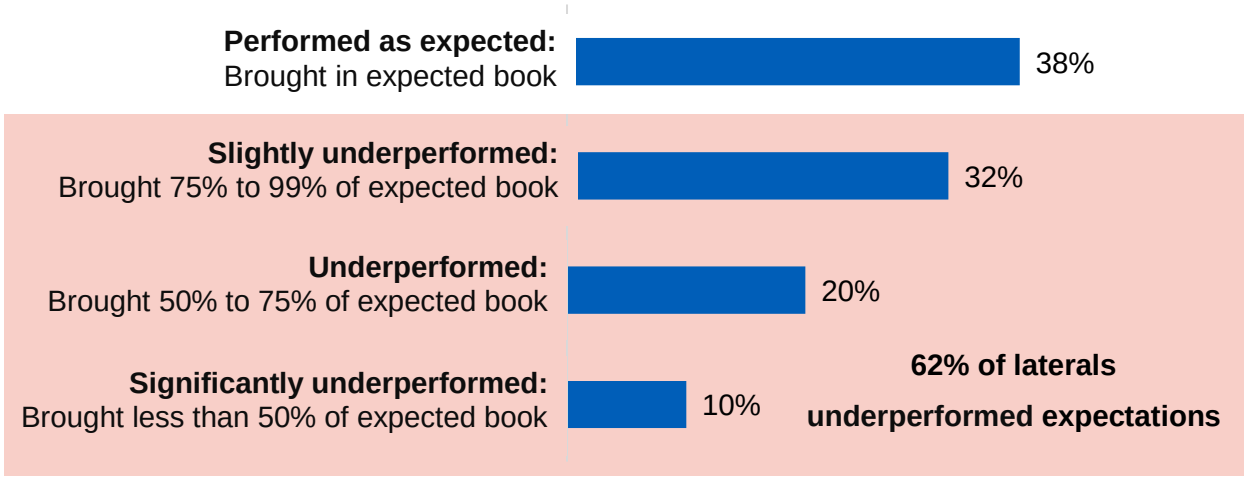
Book of Business. Another key component in the "failure equation" of lateral hires is the revenue which the new hire assisted in bringing into the firm. In this case, "book of business" means more than just revenue brought from existing clients. While a candidate's book of business is important, their ability to build new relationships and generate new revenue within the new firm's platform is also critically important.

The data makes a compelling case that most lateral hires don't bring their expected book of business. The ALM Intelligence - Decipher Lateral Hiring Survey reveals that 62% of lateral partner hires underperform the revenue expectations of their new firm. Thirty-two percent 'slightly underperformed', bringing in somewhere between 75% and 99% of the expected business, while a shocking 30% of partners 'underperformed' or 'significantly underperformed' expectations.

One important question to consider when looking at this data is what the law firm's expectations were. One head of talent at an Am Law 25 firm told ALM Intelligence "our experience is that almost no lateral partner brings everything they promise" adding "we typically discount a lateral's promised book of business by 30% to 50%". Interviews with several industry professionals suggest this level of discounting is standard. This suggests law firm's expectations have been adjusted downward from the lateral's initial promises. The fact that most partners are not meeting expectations, even after significant downward adjustments, should be concerning. These data points highlight the importance of understanding a lateral's client relationships and business development skills *prior to* the hire.

Figure 9: Retention Rates For Lateral Hires

Retention rates for lateral partner hires
For Am Law 200 firms



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Cultural Fit. Beyond lateral retention rates and the financial risks inherent in lateral hiring, another group of risks are arguably even more important. The "personality risk" of a lateral hire can, in some cases, be much more costly to the hiring firm than a lateral's financial risk. "Personality risk" encapsulates a broad range of issues. It includes ethical issues such as malpractice, sexual harassment or issues related to work place harassment. It can also relate to issues connected to work style, communication style, and "fit" within the organization. Many interviewed law firms told ALM intelligence they had faced issues of "fit" with lateral hires. In some cases a lack of fit resulted in the lateral leaving. In the worst cases it had spillover effects on the morale of partners, associates, or staff at the firm - resulting in departures.

> ***74% of firms had a lateral partner leave within the past 5 years due to personality or cultural issues.***

The results of the ALM Intelligence / Decipher Survey, suggest a lateral's personality and behavior is at the forefront of firm leaders' minds. Forty percent of surveyed firms ranked cultural and personality fit as being the most desired quality in a lateral hire. Furthermore, 74% of firms had a lateral partner leave within the past five years due to personality or cultural issues.

Malpractice. It is difficult to assess how often lateral hires commit malpractice due to the fact that most firms won't openly discuss the issue. To fill the gaps, ALM Intelligence interviewed several major insurance companies which underwrite law firms in this areas to see if lateral hires posed an above average risk. Insurance providers are, arguably, the best source for this type of information because they aggregate claim data from the majority of Am Law 200 firms.

> ***"Almost everyone in the insurance industry believes laterals represent a disproportionate number of claims."***

In interviews, insurers admitted that the way they collect and measure claims made it difficult to statistically link lateral hires with increases in malpractice. However, a majority of insurers reported that there is some evidence to suggest that lateral hires are more likely to be "bad actors." Dan Donnelly, the head of claims at ALAS, a malpractice insurer to large law firms, summarized this point of view when speaking with Scott Flaherty for a 2018 piece[9] in The American Lawyer noting "In the professional liability space there has been, for a long time, a conventional wisdom that laterals present significant risk." Insurers reported to ALM Intelligence

[9] In the MeToo Era, Lateral Candidates Are Going Under the Microscope, February 2018, The American Lawyer

there are many reasons for laterals' higher risk profile. One insurer noted that "there are inherent risks related to moving a book a business. If a client's files get lost or do not get processed correctly, the firm could open itself up to a malpractice claim".

Harassment. Data suggests that we have only begun to see the full extent of the #MeToo movement in the legal sector. A 2018 FTI Consulting Group study[10] concluded that 27% of women in the legal industry had experienced firsthand or witnessed unwanted touching in the workplace.

> ***27% of women in the legal industry had experienced firsthand or witnessed unwanted touching in the workplace.***

As with cases of malpractice, it is difficult to conclusively prove that laterals represent above average risk in these areas. The insurance companies interviewed by ALM Intelligence, who also underwrite law firms in areas of harassment, held similar views on harassment and malpractice. They admitted there was little hard data proving laterals posed above average risk. That said, they admitted that anecdotal stories suggested a link. In a conversation with one insurer they noted that in many cases a lateral partner is moving because things didn't work out at the last firm. The insurer noted that "in some cases it just wasn't a good business fit at the previous firm, in other cases it's because the partner is a bad actor." This point, that some partners move laterally to escape problems they created at a previous firm, was made clearly in a 2018 Wall Street Journal piece titled "*At Law Firms, Rainmakers Accused of Harassment Can Switch Jobs With Ease*." In the article, authors Sara Randazzo and Nicole Hong, make the argument that some "rainmakers accused of bad behavior often receive second and third chances."

Cases of malpractice, sexual harassment and workplace harassment carry significant risks. Settlements in these types of cases can be enormous, and the damage such cases do to law firm's brand – particularly in the #MeToo era – can be even larger. The implications of hiring a partner with a history of this type of behavior are staggering. In addition to the financial risks associated with claims resulting from bad behavior, should allegations against a firm become widely known, it will face intense public backlash, brand degradation, hiring troubles, and potentially a talent drain.

[10] #MeeToo At Work, FTI Consulting Group, 2018

Key Takeaways: Lateral Hiring Success Rates and Risks

- **The cost of acquiring lateral partners is sky high:** After including all relevant factors, firms on average, spend between $2.3 million dollars per lateral hire. If two years of compensation is included, which nearly every lateral receives, then the average cost increases to $4.2 million.
- **Low rate of retention**: between 40% and 50% of lateral hires don't last 5 years at their new firm.
- **A majority of lateral hires are not bringing their expected book of business:** 62% of lateral partners underperform in delivering their stated book of business.
- **Cultural fit**: 40% of surveyed firms listed cultural fit as the most desired quality in a lateral hire. Additionally, 74% of law firms have cited 'cultural fit issues' as a reason why a lateral partner has the left firm over the past five years.
- **Insurance companies believe lateral hires pose unique risks:** Insurance companies told ALM Intelligence that they believe lateral hires represent a disproportionate percentage of malpractice and work place harassment claims**.**
- **Malpractice and workplace harassment:** Given the current climate, the threat of malpractice and workplace harassment claims related to hiring laterals has increased significantly and pose significant financial and brand risk to law firms.

Improving Lateral Hire Success Rates

Law firms face an unenviable challenge. On the one hand, lateral partner hiring comes with significant risk. On the other hand, the opportunities in the lateral market are too large for many firms to ignore. Some of the challenges in the lateral hiring space will take time to address. Firms need to think more strategically, and less opportunistically, about hiring. If they are clear why they are hiring and what they expect the candidate to deliver then they will have an appropriate filter through which to evaluate the candidate. They also need to increase the amount of support their, often understaffed, hiring and integration programs receive. Addressing these challenges will take time and buy-in from the partnership. Tony Williams of Jomati Consultants, an advisor to law firms and the former Global Managing Partner of Clifford Chance believes “law firms should be more strategic and business focused to lateral hiring. Inevitably some laterals will not realize their potential and will need to be addressed but with rigor both as to the reason for hiring and in the hiring process these expensive failures can be significantly reduced”. He argues that “partner hires must be thoroughly examined. The business case for each hire must be strategically focused and reasonably quantifiable. If the risks inherent in any particular hire are fully understood then they can to a large extent be mitigated.”

> ***“It takes leaders with a certain maturity and self-confidence to have their instincts tested with third party data about a candidate. Facts are our friends even if, or perhaps especially when, they are counter to our expectations”***
>
> *- Hugh Simons, former COO of Ropes & Gray*

Four key tactics are at play in getting the most out of a firm’s lateral hire program: (1) Fine-tuning the Lateral Partner Questionnaire (LPQ); (2) Embracing consistency in the vetting process; (3) Utilizing competitive intelligence to achieve the transparency firms need; and (4) Building a business case that is honest about a candidate’s strength and weaknesses. This new standard of due diligence can be instrumental in discovering the warning signs and “red flags” before the hire, which will likely yield significantly higher success rates.

The Importance of the Lateral Partner Questionnaire (LPQ)

The Lateral Partner Questionnaire (LPQ) is, for most firms, the primary method of gathering information on potential lateral candidates. There is no industry standard for LPQs, leaving each law firm to design their own questionnaire. That said, LPQs share some similarities in the types of questions they ask and, more importantly, the questions they don’t ask.

LPQs are the first, and for many firms the primary, method of gathering information on candidates. It is therefore essential that they ask the right questions. For most firms, there is significant room for improvement in this area. Typically, the first section of an LPQ contains basic information such as (1) biographical data (2) financial data and (3) client data. The next section contains more detailed information such as (4) conflicts and (5) professional and personal references. While there is room for improvement in the questions firms typically ask in these sections, it is the final section of the LPQ where firms need to focus their immediate efforts.

The final section of the LPQ, often entitled “Other Information”, typically includes questions which, in most industries, are relatively standard due diligence inquiries. These will include personal legal history, malpractice claims, and outside activities and interests. Asking the right questions in this section is vital to the due diligence process as these areas of investigation represent the greatest risk to a law firm.

> ***Questions were rarely asked in black and white terms. Instead LPQs are often written in a way that creates ‘wiggle room’ for the candidate to reinterpret them question asked.***

ALM Intelligence and Decipher have reviewed dozens of LPQs as part of the research for this report, and reached two primary conclusions: First, most firms are not asking enough questions to appropriately identify and assess the legal and reputational risks that lateral candidates pose. Second and equally important, was a lack of specificity in the questions that were asked. Questions were rarely asked in black and white terms. Instead LPQs are often written in a way that creates ‘wiggle room’ for the candidate to reinterpret the question asked. This is a mistake. Law firms need to review their LPQ process with the goal of (1) ensuring all of the key topics are covered (see next page for a list of questions which law firms should consider adding to their LPQs) and (2) tightening-up the language used within the questionnaire to give “teeth” to the signed disclosures.

Questions All Law Firms Should Be Asking In Their LPQs

Below are a list of questions which should help law firms identify and assess the risk a lateral candidate poses to the firm in areas related to malpractice claims, law suits, conflicts, reputational issues, and outside interests.

1. **Reputational Risks to the Firm**

   Are you aware of any facts or circumstances that would result in damage or embarrassment to FIRM or to you if you join FIRM as a partner? (If yes, please elaborate).

2. **Malpractice**

   Have you ever been involved in a matter that resulted in a malpractice claim or allegation against you (whether or not an action was actually filed and whether or not you were individually named as a defendant)? (If yes, please describe and state the status and outcome of each).

3. **Sexual Harassment**

   Have you ever been the subject of a claim of sexual harassment, unlawful discrimination, or other claim or allegation made in the context of the workplace (whether or not any formal action was taken)? (If yes, please describe and state the status and outcome of each).

4. **Problems with Past Employers**

   Have you ever been asked (explicitly or implicitly) to leave a legal employer or partnership?

5. **Crimes and Investigations**

   Are you now, or have you ever been, a party (plaintiff or defendant) in any pending administrative or employment proceedings, arbitrations, or criminal or civil court actions (exclusive of routine, non-alcohol-related or non-drug-related motor vehicle offences)? Have you ever been charged or convicted of a felony or misdemeanor, the penalty for which could be incarceration? (If yes, please describe and state the status and outcome of each).

6. **Additional Conflicts**

   Are you aware of any other matters that may create a conflict with FIRM? (If yes, please describe the matter(s)).

7. **Professional Standing:**
   Have you ever been disciplined by any Bar or equivalent professional licensing body, or, to your knowledge, have there ever been any complaints lodged against you with any such body (if yes, please describe and state the status and outcome of each).

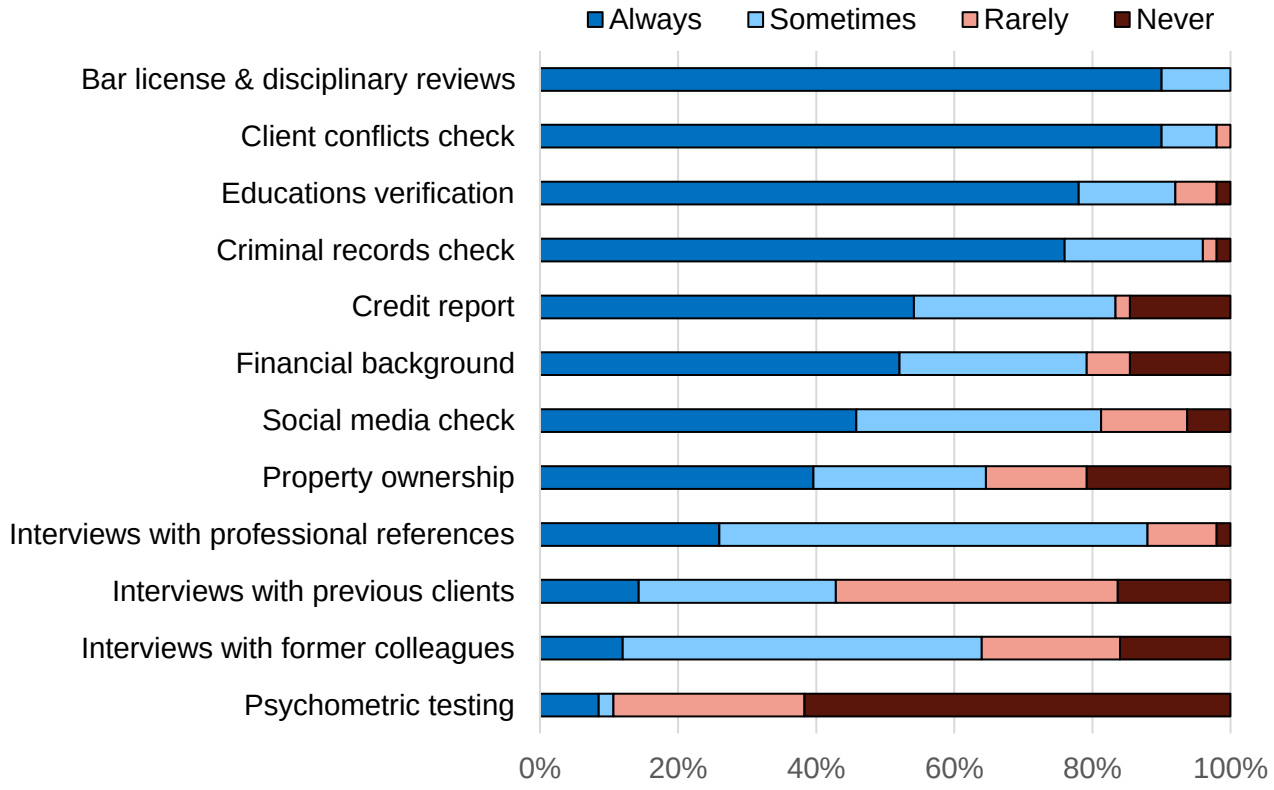
Implementing a Consistent Due Diligence Program

Among the biggest challenges law firms face is a lack of consistency in how they vet candidates. While 78% percent of firms reported, in the ALM Intelligence / Decipher Survey, that they perform some basic due diligence on all candidates, 22% reported that they only investigate candidates “some of the time”. This lack of consistency in partner hiring is alarming. A partner’s role combines many key functions - co-owner of the firm, key account manager, business developer, subject matter expert, and supervisor of junior staff. Each of these roles require different capabilities. They also pose unique risks. If firms are not vetting candidates to ensure they can fulfil the requirements of those varied and diverse duties they open themselves up to significant risk.

Even among those firms which performed due diligence “all of the time”, there is significant variability in the types of due diligence performed on each candidate. For example, while 90% of law firms reported that they perform criminal background checks all the time, only 46% said they perform social media checks all of the time (see Figure 10). Given the increasing occurrences of social media-related controversies, such variability is worrisome.

Figure 10: Inconsistency In Law Firm Due Diligence On Lateral Hires

Frequency of due diligence checks performed by law firms
Percentage of firms reporting



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In interviews, most firms admitted that they do not have a consistent approach to due diligence across the entire firm. There were two primary reasons for this inconsistency – differences in the information available on candidates across markets and a belief the firm had all the necessary information. A head of human resources at a global Am Law 20 firm told ALM Intelligence "our due diligence process in the United States is very thorough, but internationally it's a very different story. We don't have access to the same kinds of information in emerging markets as we do in the United States." Inconsistency in these cases is understandable. The approaches used by law firms to gather information will vary based on the information available. In cases where basic background and credit checks are not available more thorough interviews with references, colleagues and clients become even more necessary. The difficulty is that firms don't appear to be using these readily available sources of intelligence. When faced with information gaps most firms are not shifting their approach. Instead, they are simply moving on without the necessary information. In these cases, they are relying more heavily on information gathered through candidate interviews, possibly, or the lateral partner questionnaire.

In interviews most firms admitted that they do not have a consistent approach to due diligence across the entire firm. There were two primary reasons for this inconsistency – differences in the information available on candidates across markets and a belief the firm had all the necessary information.

The second driver of inconsistency in law firms' due diligence process is more concerning. Many firms reported that they do not believe due diligence is needed in cases where they "know the candidate". In an interview with an Am Law 100 firm, the head of lateral recruitment reported that "we do a lot of due diligence in markets that we are trying to expand into. In our home market there isn't much need for us to do background checks on partners. It's a small market. We know everyone." This approach is surprisingly common and should cause law firm leaders great concern. The legal community in many markets can feel particularly insulated. Senior partners within niche practice area specialties or in smaller geographic markets may have collaborated with, or sat across the table from, many of the individuals who the firm is considering, or has considered, hiring. The information gathered from these interactions can be useful in identifying and vetting candidates. This information does not, however, replace a thorough vetting. Many aspects of a partner's personal and professional life that will directly impact their risk profile and ability to succeed at their new firm, cannot be gleaned from social and professional interactions between partners. These risk issues (claims, personal conflicts, personal litigation history,

cultural issues, etc.) are also unlikely to be common knowledge within the legal community. Put simply, much can be missed by relying on partners interactions with potential laterals.

The value of consistency goes well beyond ensuring all necessary information is gathered and assessed. Greater consistency should enhance firms' ability to investigate hires and triangulate data points. One Am Law 200 firm told ALM Intelligence, "once we started collecting more information on potential hires we started to see how different data points connected." This is an important point. Due diligence sometimes reveals major "red flag" issues. More often than not however it reveals areas of concern which require more investigation or some form of risk mitigation. Collecting more data more consistently should allow firms to understand how to spot these areas of concern and put plans in place to mitigate the risks they create.

One strategy to increase the consistency of due diligence on lateral candidates is to separate diligence from recruitment. Stephen Poor, the chair emeritus of Seyfarth Shaw, believes "recruitment teams sometimes struggle to do due diligence effectively." There is a natural conflict between recruitment and due diligence. Recruitment teams are tasked with bringing in partners. Due diligence requires a different mindset. Poor argues that most firms "should separate these tasks or, potentially, outsource diligence to a third party provider."

Increasing the Use of Human Intelligence (Source Interviews)

Human Intelligence is the least common form of research used in due diligence investigations on lateral hires. This is a missed opportunity. There is much that can be gained from talking to a lateral partner candidate's colleagues, market peers, and clients. Gretta Rusanow, the Managing Director and Head of Advisory Services at Citi Private Bank's Law Firm Group, says "our research shows that most lateral candidates fail because they don't bring their expected book of business." This suggests firms need to do more digging into the candidate's relationships with clients.

Firm's need to get a better understanding of candidate's practices so that can understand what portion of their promised book of business will actually show up. Interviews with a candidate's colleagues or past clients can help accomplish this. It can also allow firms to get a better understanding of the candidate's "cultural fit," their ability to develop emerging talent, and, most importantly, help identify "red flags" in their behavior that pose an immediate risk to the firm.

Utilizing Human Intelligence as Part of the Due Diligence Process

Conducting what is commonly known as an “investigative consumer report” (ICR) on lateral candidates requires legal permission to do so. This consent is straight-forward and can be incorporated into a firm package of materials including the LPQ, other disclosures, business plans, etc. The ICR empowers the firm to conduct deep dive market intelligence, including source interviews via a qualified third-party, to determine their true market reputation as well as their legal ability, the way they work with others, and their business and client skills.

A thorough investigation will involve discussions with twenty to thirty individuals including:

1. Clients
2. Former colleagues
3. Market peers; and
4. Opposing counsel

The goal of these inquiries is to assess the candidate’s “true” market reputation in three key areas:

1. Legal skills;
2. Personality and ability to work with others; as well as
3. Business development and client skills.

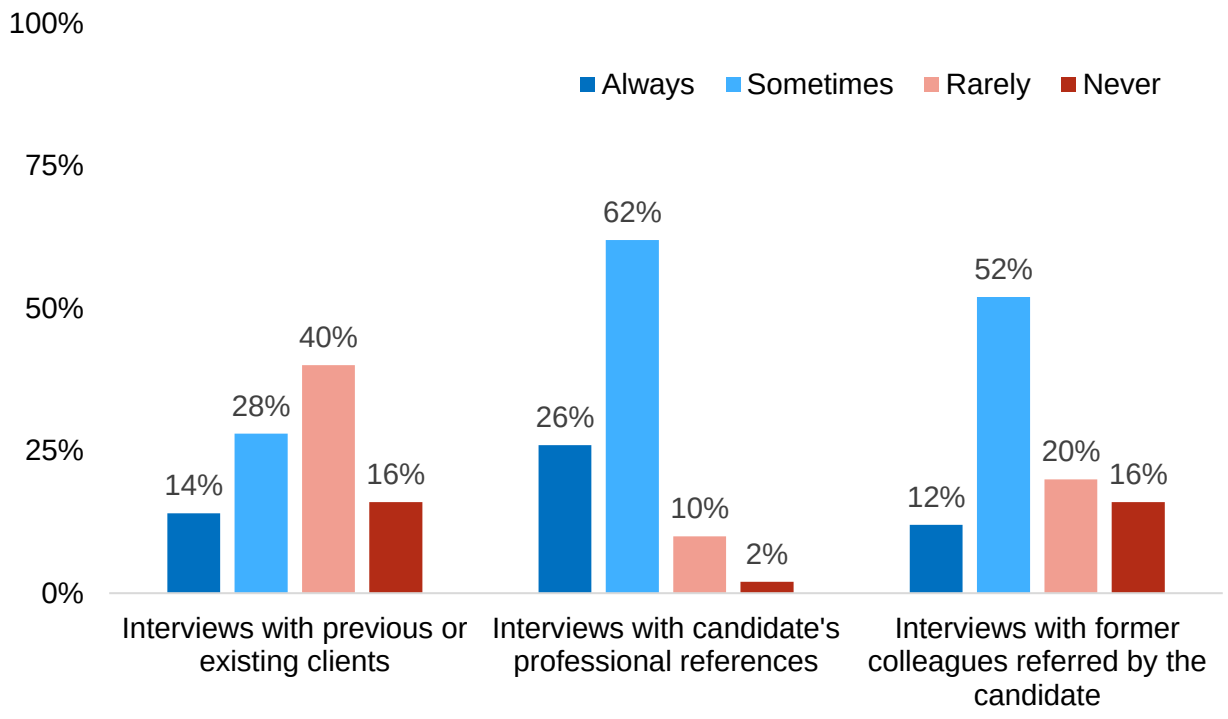
These candid and confidential inquiries give the firm a much better feel for not only a candidate’s potential “fit” but can also reveal the “red flags” that can save a firm great expense, embarrassment, and heartache.

Source interviews are typically conducted by a qualified third-party, skilled in these types of investigations to preserve the anonymity of the candidate and confidentiality of the client.

In interviews, many heads of talent reported interest in using source interviews to vet lateral candidates. They also reported that many of their partners felt uneasy with this new tactic. This is understandable. Law firms are often slow to embrace new methods. Partners reported they were concerned that utilizing human intelligence tactics could compromise the confidentiality of their discussions with the candidate. They also felt that performing this level of due diligence doesn't "strike the right tone" with a potential hire.

Figure 11: Inconsistency In The Use Of Interviews In Lateral Partner Due Diligence

The use of interviews in due diligence
Percentage of firms reporting



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Issue of confidentially can be managed. A qualified, third-party with an established track-record with this type of due diligence will conduct human intelligence-based investigations utilizing a sensitive and secure methodology which will not compromise the security of the firm or the candidate.

Partner's second concern – on striking the right "tone" - is also important. Hiring of any kind – not just at the partnership level - involves active recruitment and vetting. Both parties are evaluating each other. The hiring firm needs to assess if the candidate can perform the duties of the role. The candidate, on the other hand, wants to feel as though they are being courted, and that their career is safe at their prospective new firm. Firm leaders need to balance these competing goals while also fulfilling their responsibilities to their partners and staff. Stephen Poor, the chair emeritus of Seyfarth Shaw, believes these competing goals can be balanced. "Law firm leaders have responsibilities to their fellow partners, associates, and staff to do thorough due diligence". Poor believes "most lateral partner candidates understand their hire is a business decision and there is a need for serious vetting". To their fellow partners, firm leaders have a fiduciary responsibility to thoroughly vet lateral partner candidates not only from a perspective of "brand risk" but in business and financial terms as well. An unsuccessful hire, as noted earlier in this report, is likely to cost the firm's partners hundreds of thousands or even millions of dollars. A malpractice claim will cost them even more. To associates and staff, firm leaders have a responsibility to ensure that candidates will create a safe work environment. To shirk these responsibilities out of a desire to maintain a sense of collegiality is irresponsible and unethical.

> ***"Law firm leaders have responsibilities to their fellow partners, associates, and staff to do thorough due diligence. Most lateral partner candidates understand their hire is a business decision and there is a need for serious vetting"***
>
> *- Stephen Poor, the chair emeritus of Seyfarth Shaw*

Firm leaders should be transparent about the need for holistic due diligence, including human intelligence with their lateral candidates. They should explain that they take their responsibilities seriously and that they guard the doors of partnership closely. Some lateral partner candidates may be turned off by this approach. Others will see this as a sign of good governance and solid management.

A Look Behind the Curtain: Responses Heard in Lateral Partner Interviews

Below are quotes heard, by Decipher, during due diligence investigations into lateral partner candidates on behalf of law firm clients. These responses have been altered slightly to preserve the anonymity of the candidates and law firms involved.

Quote 1: The law firm had concerns about a candidate's cultural fit within an office setting.

> *"As far as her overall skills, she knows the law very well (pause). She just has issues with boundaries. She becomes 'bff's' with clients on social media and then things go wrong. She does the same thing with junior partners and associates. Sometimes it gets ugly."*

Quote 2: The firm wanted the candidate to open an international office, but they felt that something was not entirely right about their background.

> *"He is a felon. He is a criminal. He hacked into the firm's computer system when he was an associate. He then was found to have stolen confidential information from a prior firm. He was removed from that firm and he should have been disbarred, but he was not."*

Quote 3: The firm was looking for a high profile litigator with a great reputation.

> *"He's super smart. I'm positive he's a good lawyer. He can be astoundingly rude though, at times really disrespectful. Once he insulted someone based on their race. It was so bad the client dropped their relationship with him and went with another firm."*

Quote 4: The firm was looking for a corporate partner in Asia, but was concerned about his ability to work with others.

> *"He's an okay lawyer, he can do the work (pause). I have observed that he is very bad with stress. He is very demanding, which can be fine for a lawyer, but he is known to take it out on his team."*

Building a Business Case for Each Hire

In some cases, due diligence reveals “red flags” which cause a firm to reconsider a hire. In most cases however, the information gathered will not change the firm’s decision to move forward with the candidate, but will highlight certain performance and risk issues which should be incorporated into the overall business case for hire.

Information on the partner’s relationships with clients, which are gathered via interviews with the candidate, information provided on the lateral partner questionnaire, and through proper, responsible, and secure human intelligence sourced from the candidate’s colleagues and clients, should help create a more realistic view of the book of business which is likely to move with the partner to the new firm. This should inform compensation discussions and help set targets for

> ***To associates and staff, firm leaders have a responsibility to ensure that candidates will create a safe work environment. To shirk these responsibilities out of a desire to maintain a sense of collegiality is irresponsible and unethical.***

originations and billings for the coming year. It may also inform conversations with clients on pricing and the manner in which matters are staffed.

Information collected on a partner’s work style should also be incorporated into the business plan. One key question to answer is if other partners, associates, or staff need to be moved with the candidate. In many cases, partners rely on an individual or group of individuals to make their practices work. In some cases, it is a senior associate with whom the partner has a strong relationship. In others, it’s a personal assistant who helps balance the partner’s practice and personal life. It is vital to identify which individuals are the key to the partner’s success. The information required to answer these questions can often be found in the lateral partner questionnaire or be gleaned through interviews.

Cultural fit is another key aspect of making a lateral move successful. Firm leaders should identify, via interviews and due diligence, which partners with whom the candidate is likely to work best, and worst. This information should be incorporated into the partner’s business plan for the first year. Any issues of concern in the partner’s work style should also be anticipated and addressed so that the new partner has the greatest chance for success at the lowest possible risk to the firm and its stakeholders.

Key Takeaways: Improving Success Rates

- **Revamping the firm's LPQ:** A lack of specificity and direct questions aimed at identifying and assessing the legal and reputational risks that laterals pose creates significant risk.
- **Consistent due diligence**: The scope of what constitutes due diligence varies widely from firm to firm and candidate to candidate. Erroneously, many firms feel that if they "know the candidate," due diligence isn't necessary. These consistency "gaps" create significant risks.
- **Use human intelligence:** Confidential third-party source interviews can shed light on a candidate's personality, potential cultural fit, and business development skills, and can catch serious "red flags," all of which would otherwise not be accessible to the hiring firm.
- **The business case**: Intelligence collected throughout the due diligence process can inform compensation discussions with the candidate, as well as give the hiring firm a solid understanding of the candidate's business development skills, the strength of their client relationships, and work style, and can dramatically improve integration and chance for sustained success.

Conclusion

Lateral partner hiring offers enormous rewards but also involves significant risk. The research presented in this paper argues greater due diligence on lateral candidates is a key ingredient in balancing these risks and potential rewards. Interviews with law firm leaders suggest that, from a financial perspective, implementing a consistent due diligence program is cost effective. Even if performing due diligence 'only' saves a firm from hiring one partner, it represents millions of dollars in savings. The cost of due diligence is only a fraction of such savings. Furthermore, the peace of mind, for leadership and other firm stakeholders, knowing that each and every lateral hire is being carefully vetted, is invaluable.

The status quo is not sustainable. The data makes a compelling case that lateral hires fail more often than they succeed, whether by leaving the hiring firm within five years, underperforming their promised book of business, bringing excess reputational baggage, engaging in "bad behavior", or merely by failing to fit in culturally. The end goal of implementing a consistent and effective due diligence program is simply to increase the success rate of a law firms' lateral hires. In most cases, this is accomplished by identifying risky hires before commitments are made. Due diligence can also help improve a law firm's integration plans and help the new partner succeed. Lateral hires pose unique risks. Rigorous and straight-forward due diligence can properly equip law firms to realize the great strategic promise of their lateral growth programs.

About Decipher

For law firms who plan to grow with lateral hires, Decipher (decipherglobal.com) is the corporate intelligence provider that lowers risk and empowers better decision making. Unlike basic screening services, we combine quantitative data with human intelligence to accurately access candidates' business, legal skills, work style and character. Armed with this information, our clients grow safely and more efficiently, with success rates four times the industry average.

What we do

We reduce law firms" lateral risk and cost by providing deep-dive intelligence about prospective partners – before they are hired. We help our clients grow safely and more efficiently.

How we do it

We combine qualitative and quantitative research to build custom in-depth profiles that accurately assess a candidate's book of business, legal skills, work style and character.

Our confidential double-blind process delivers actionable data in 10 days.

Why we do it

While 96 percent of law firms say lateral growth is part of their strategy, less than 10 percent of laterals currently recoup their cost of acquisition. Half will fail in five years.

As legal-industry veterans, we believe law firms and their partners deserve better. We take pride in helping hem make better decisions, avoid financial losses and prevent reputational harm

About ALM Intelligence

ALM Intelligence, a division of ALM Media LLC, provides the proprietary data, analysis, tools and knowledge that empower our clients to succeed. Our products are built to arm you with the critical business information you need to make the most impactful and informed decisions possible. Meet competitive challenges head on and be confident that you are taking the correct steps to remain ahead of the field. Leverage the depth of our industry experience and expertise across the benefits, consulting and legal industries.

ALM Legal Intelligence

Servicing the Legal Industry offers a distinct set of challenges. Law firms are not like other companies, and lawyers are not like other professionals. ALM Intelligence understands the unique needs of the legal industry and offers a variety of tools, reports, and services that are specifically tailored to our profession. We work with hundreds of law firms and thousands of lawyers from across the Am Law 200 and beyond, providing the game-changing data that legal professionals need. Whether it's benchmarking a verdict, finding the right partner to hire, or simply keeping up on industry trends, ALM Intelligence gives you the tools and information you need to stay ahead of the curve.

ALM's industry-leading rankings, surveys, reports and databases are all designed with one purpose in mind: giving our clients an edge. Our intelligence suite comprises a dynamic combination of products that empower case preparation and management, offer razor-sharp industry and trend analysis and fuel better competitive intelligence. We also offer custom advisory services tailored to clients' exacting needs. With ALM's intelligence in hand, surmounting business challenges and keeping ahead of the competition have never been easier.

ALM's suite of business of law intelligence databases, research and solutions grants you the deepest insights on the legal industry and its biggest firms. We're well-known and respected for our Am Law and NLJ rankings, but the bedrock of data they are founded on runs far deeper. We bring you more than just the best law firm data. Our rigorously researched reports provide context around the numbers, analyzing across data sets and elucidating key insights, and our custom advisory services are bolstered by 40 years of industry knowledge and experience, and a team of our sharpest analysts and researchers.