Recruiting and Retention: A poor ROI for many law firms

In an improved business climate, attorney retention has once again become a priority for law firms, whether the new hires are from incoming classes or lateral moves. Many firms are reportedly facing a shortfall of senior associates, because they either laid off too many attorneys or cut back too much on their hiring goals during the recession – in order to protect short-term profitability.

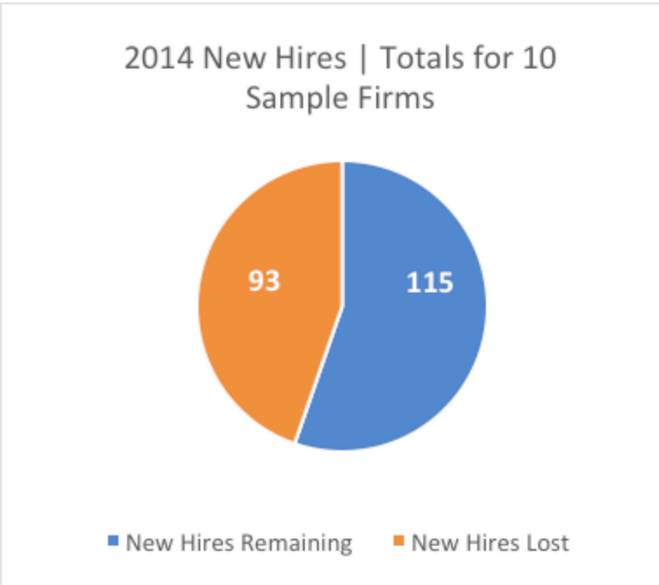
A solid majority of respondents (56%) to a recent Altman Weil survey said that headcount growth was a requirement to ensure their firm's success. In fact, the report goes on to say that virtually all survey participants said their firm had plans to pursue organic growth – entry-level hiring – and the acquisition of attorneys through laterals.

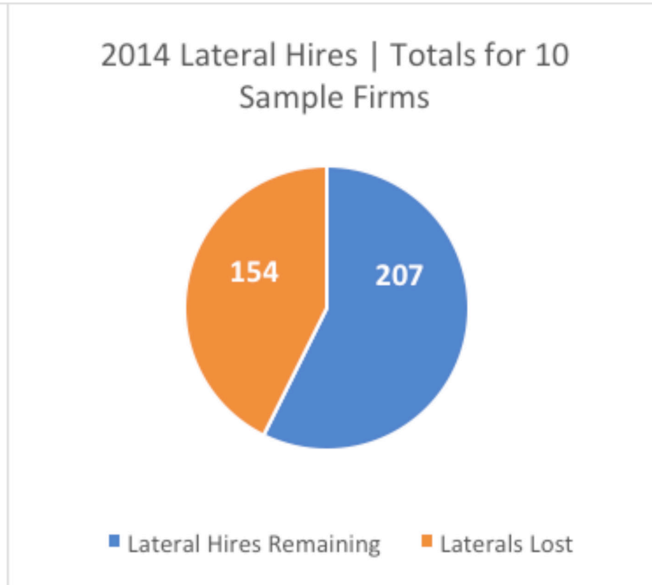
That said, not all hires are equal when it comes to enhancing profitability, and a key factor for profitability is how long an attorney stays at the firm. An analysis of lateral hiring by Hugh Simons, Ph.D., published earlier this year contends that **when lateral hires don't stay more than five full years, the return on investment for the hiring law firm is poor**. Dr. Simons suggests that it takes about two-to-three years for a lateral to get up to speed at a new law firm and another two-to-three years of strong performance. In total it takes four-to-six years – for a law firm to "recoup recruiting costs and compensation-above-contribution through the transition period." But how do individual law firms fare in practice?

Leopard Solutions has been collecting data on attorneys and their careers for over a decade. A recent study among a sample of AmLaw 200 firms revealed that a very high percentage of incoming classes of new and lateral hires leave their firm within three years. In most cases, such an early departure leads to a loss for the firm on the investment made on those individual attorneys. In some cases, the high attrition rate may actually lead to the entire class and/or all lateral hires for that year being unprofitable by year three.

The Data

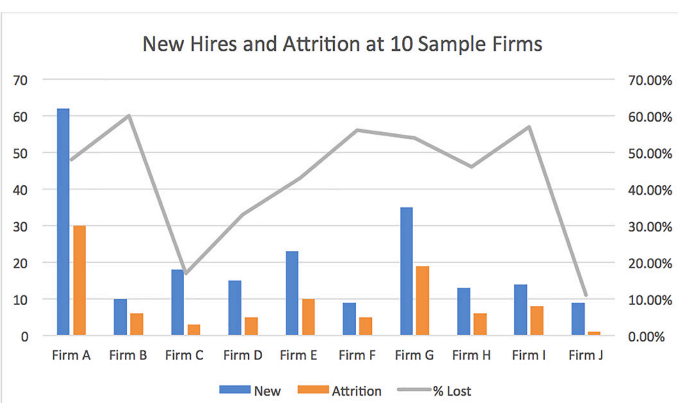
For this study, Leopard Solutions took a random sample of AmLaw 200 firms and tracked the new hires and lateral hires those firms made in 2014 using Leopard Firmscape, our competitive intelligence tool. The review covers the period between January 2014 and September 2017. The firms have been anonymized for this study.

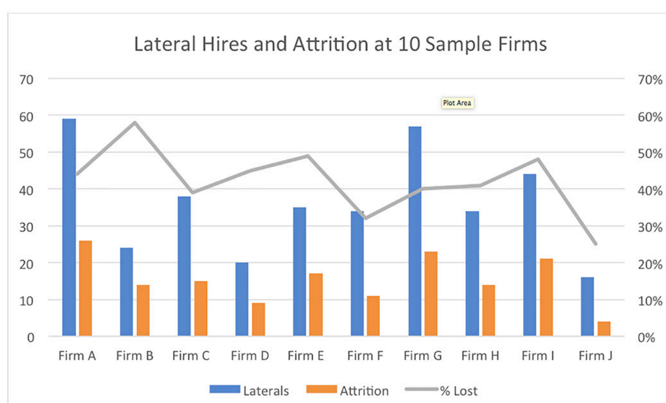




Overall, the number of departures within the first three years after hiring is astonishingly high. Across the entire sample group, the average attrition rate for new hires was 45%, and for laterals it was only marginally better at 43%. Of course, the rates varied by firm – for first year hires, the loss rate ranged between 11% on the low end to 60% for the firm with the largest attorney losses. In the lateral category, the range was narrower, starting at 25% and reaching as high as 58% in one case.

Digging more deeply into the individual firm results, all but two of the firms saw more than one third of their new hires leave within three years. Taking out the best two performing firms (Firm C and Firm J), the average of new hires that left the hiring firm within three years reaches 49%. With respect to lateral hires the results are slightly better. Taking out the two best performers, (Firms F and J), **the average of lateral hires that leave the firm reaches 44.7%.**





To be clear, this is a random sample and, as such, may not be fully representative of what is happening at every AmLaw200 firm. That said, the fact remains that the performance of the sample group raises serious questions regarding the recruiting and retention practices of the firms. It also exposes the poor ROI that some firms are realizing on their recruits and lateral hires.

A closer look at ROI

To fully understand the financial impact of law firm retention rates, it's essential to understand the basic arithmetic that determines profitability rates for each new or lateral hire. Based on an estimate of cost and yield for average associates (first year and laterals), as depicted below, and with the increasing refusal of clients to pay for first years and sometimes second years, a ramp up for laterals and write offs means:

- Associates that leave in their first or second year create a loss for the firm;
- Associates that leave in their third year may break even, but more likely create a loss;
- Lateral hires that leave in the first year after hiring create a loss for the firm;
- Lateral hires that leave in the second or third year may be profitable for the firm overall, but it varies significantly case by case. Most often the people that leave within three years are the ones that don't work out, which often means they don't bill enough.

	First Year	Second Year	Third Year	Lateral
Base Salary	$170,000[1]	$190,000	$210,000	$240,000[2]
Bonus	$15,000	$25,000	$30,000	$60,000
Payroll Taxes & Benefits	$40,000	$45,000	$55,000	$60,000
Recruitment Cost	$50,000	-	-	$60,000
Office, Shared personal assistant, subscriptions, CLE, etc.	$40,000	$40,000	$40,000	$40,000
Total Annual Cost	$315,000	$300,000	$335,000	$460,000

[1] In 2016 the average associate salary for first year hires went from $160,000 to $170,000.
[2] This is an estimate and is based on the salary of a 5th year.

A thorough look at individual firms' hiring patterns could help firms to predict factors that drive success and failure. For example, among the external factors that may play a role, the Leopard data suggested that for some of the firms analyzed above, certain schools created better results than others. For laterals, in some instances there was better success when laterals came from a particular firm. Internal factors are important as well – and the Leopard data indicated that within each firm, certain departments fared better than others in retaining their laterals and first year hires.

What other steps should firms consider to retain newly hired talent? First, let's consider what attracts associates to particular firms. Research from Cushman & Wakefield shows that most associates are attracted by a firm's reputation (75%), areas of practice (66%), compensation (58%), diversity and complexity of work (39%) and partnership track (35%). While the same top factors come up when asked about what would get them to stay with their current firms, i.e. areas of practice (57%), firm reputation (56%) and compensation (55%), the other top factors following these are mentoring (48%) and collaborative culture (43%). The notable difference in the retention list is the absence of partnership track. Millennials became the highest percentage of the workforce in 2015, and as Cushman & Wakefield executive managing director Sherry Cushman explains, "Today's young lawyers have far different career goals and objectives than their predecessors. Understanding what drives them is key to associate recruitment and retention. Mentorship, collaboration, and feeling like they have some skin in the game have become critically important."

Of course, compensation is a top factor for attorneys when it comes to both recruitment and retention, and some firms are reportedly throwing money at associates in a bid to retain their services. Some firms have started to pass out bonuses to high-performing associates who have remained loyal to the firm, a strategy that "reflects and exemplifies a changing legal marketplace where mid-level attorneys are increasingly difficult to retain and the goals of young lawyers are in flux." While the prospect of partnership is not the motivating tool it used to be, associates still want to have an understanding of their current, and future, compensation; the potential for further increases and bonuses.

In sum, there's a range of factors that determine whether an attorney will stay with or leave a firm within a few years of being hired. Before moving forward with the next hire, whether a new recruit coming out of law school or a lateral, law firms should take the steps necessary to ensure they are most likely to achieve a positive return on their investment in their human capital. That can and should include understanding the internal and external factors that can influence the longevity of those new hires.

Knowledge is Power.

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