



“All that Glitters”...may *not* be Lateral Hiring

Lateral hiring has the potential for a huge upside but it also carries with it the potential for any number of downside issues. It's in a way reminiscent of the television reality program, “Storage Wars”. The program centers on the idea of buying a “pig in a poke”. Bidders for storage units place bids without having any idea or very limited information of what they may be buying. Enticingly, they only get a glimpse of the content and then stake their bids on a prospect of success. There are winners and losers. The winners win big, the losers have not even a consolation prize.

Unfortunately, it's actually worse in the context of a law firm and lateral hires. It would be like not only not winning the prize, but also having to replace the storage locker in the same condition in which it was found. Unwinding from an un-successful lateral hire is more difficult than making it work in the first place. The decision to go ahead with a new hire is similar to the choices the contestants would make in their decision to choose a storage locker: “This one looks promising; this one looks like a dud”. Regardless of the level of strategy, however, there is often too little information to accurately gauge what result the firm may be getting. Truly, this is an approach not dissimilar to the way some law firms take on the question of lateral hires.

Some would say that hiring laterals at any level and in *any* context is, at best, a high risk endeavor. Just as it is with management generally, law firms are oftentimes completely unsophisticated in making lateral hire selections for their own office or in trying to establish a branch in which lateral hires are called upon to “carry the flag” in an additional (often a new) location. The question is then called, “Of those factors which play the most prominent role in the success or failure of such a decision, what would be the primary elements involved?”

Visions of Forgotten Treasures

Often, the individual Partners in a law firm who are advocating a merger, an assimilation of a smaller firm or a lateral hiring, tend to exercise their mathematical skills relating to addition but not subtraction (or division for that matter) of the potential hire. They will list their firm's revenue, adding to that the revenue of the lawyer or lawyers to be included and happily arrive at a total of the two. Unfortunately, like choosing the storage container, these circumstances are often hard to read and are generally not nearly so simple. Clients stubbornly have their own ideas about these issues and, of course, various conflicts scenarios are among the many factors which work against the concept

of simple addition. The list would therefore include, first and foremost, careful planning. Like building a house, the plans must be in place before the work begins. Among other things, the firm must be well assured that such a move will not result in the disaffection of an existing client or create competition with another lawyer or law firm which has been a dependable source of new business. (You might be amazed at how often this is the case.) Adding a new practice area (or hiring particular lawyers) may also achieve a greater level of competition with another law firm that has never really attempted to compete for the firm's core business. In some cases, the other, perhaps larger and more powerful entity, has not seen fit to engage in the "piracy" (robbing clients from one firm to another) which is such a constant today. Such a firm may become, when a regional office is established, a formidable competitor. That's one reason that the addition of the law firm or laterals may exercise more of a subtraction than an addition.

Impact on the Existing Firm

Adding lateral hires is also a challenge because of issues involved in partnership standing, compensation and the roles which partners and associates play, within the firm. A common error made by many firms is to hire new lawyers, insinuate them into the partnership "scale" and assume that it will have little or no effect upon existing lawyers. This idea, in fact, vies with "the earth is flat" for being wrong. Experience tells us that hiring laterally impacts every lawyer in the firm in some manner. Associates may see their partnership possibility as taking a step back. Junior Partners may see their opportunities of equity ownership decreased exponentially with the number of hires. The situation is exasperated by the element of a separate office because often a premium is paid to that lawyer or those lawyers to open the office and bonus payments for the office success. All of this means that the firm may make sacrifices they had not intended to make in opening another location. Without careful planning, any or all of these factors may come back to haunt.

Professional Liability Issues

Unless actions are taken to protect the basic entity, a world of trouble can ensue in the hiring of lateral attorneys and/or establishing a branch office. (Unfortunately, there are many law firms that can testify to the acuity of this statement.) Professional liability policies are based upon the coverage at the time the claim is made ("claims made policies"). More often than not, it is the more senior lawyers who are going to be hired and those, often based upon their supposed "book of business" which they are of course encouraged to bring into the firm; often times the reason they are being hired. This may work out very well but the difficulties which the lawyer may have had with their client(s) previously are therefore inherited by the primary firm just as may be the revenue. Professional liability claims made against that lateral (those laterals) become part of the base firm's profile for purposes of acquiring insurance and indeed in reputation. That means that if there have been claims, those claims become part of the primary firm's profile.

In far too many cases, the lateral hire(s) are added without an understanding of the new hire's (or their previous firm's) claim history or of the need for "tail coverage" (coverage associated with the prior firm acts of omission or commission). Part of the planning process should therefore include a vetting process and the subsequent review of any and all malpractice claims or *potential* claims made against any attorney joining the firm for at least the last five years. A negative claim record which is inherited from a new arrival, will most certainly impact renewal pricing and in the extreme, might be the basis for a non-renewal. It turns out that insurers are as stubborn as clients and will want to see what other insurers may have paid toward the settlement of claims (including the defense cost associated with those settlements (termed a "loss run" in the industry). Due diligence in the contemplation of a lateral hire therefore requires a detailed understanding of the professional liability claims history. Since professional liability coverage is almost always limited to claims arising out of work performed on behalf of the named insured, a lateral attorney is only insured for the work performed after the lawyer joins the new firm. (This is a confusing circumstance for many and there are any number of examples where lawyers believed that there was coverage for their past acts, learning to their detriment, only after they have already been sued, that there is no coverage).

In some cases, lawyers left over from a merger situation (those not asked to join the new entity) will practice for the first time on their own and (particularly if there is no on-going firm left behind, often without any professional liability coverage. For what is termed "public policy" rationale, claims which are made against those lawyers, in certain jurisdictions, will often times be made against the on-going firm simply because there is no one else available to make the complainant "whole". The hiring firm is then left holding the bag, as it were, and a substantial (and quite unexpected) expense is added to the cost of the decision to include the lateral or create the branch using a lateral hire approach.

Conclusion

Lawyers and law firms make decisions for all sorts of reasons: some good and some bad. Hiring a lateral partner and/or utilizing a lateral hire to create a regional or branch office does, in fact, work out at least some of the time and if it does so, there may be handsome rewards. It can also be very much like buying the proverbial "pig in a poke" however. To minimize the possibility of finding *your* storage container filled with unwanted and valueless materials, the process of examination must be accomplished with substantial research and analysis in order to at least improve the odds of success. The many pitfalls which may often be attached to this strategy requires partners to keep their eyes wide open and their wits about them.

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Michael Welbel is the founder and President of M.G. Welbel & Associates, Inc. (MGW). His career in professional liability insurance began in 1981 at Shand Morahan & Co during which time his responsibilities included claim management matters effecting architects, engineers, surveyors, insurance companies and law firms. In the late eighties, Welbel was seconded to C.J. Coleman and Co, London where he worked with Lloyd's Underwriters in the resolution of claims insured through various professional liability insurance. Welbel has presented to the

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Before starting the firm of BERMAN & ASSOCIATES in 1991 Mr. Berman had managed and consulted with law firms, corporate law departments, accountancy firms and the Legal Services Corporation for twenty three years. BERMAN & ASSOCIATES began as an independent auditing firm working in conjunction with Lloyd's of London. Its mandate was to assist law firms throughout the United States, Canada and the United Kingdom with professional liability risk issues.

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