



## **COST CONTROL STRATEGIES FOR AN IMPROVED BOTTOM LINE**

Ellen Freedman, CLM  
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I must admit that when I was initially approached to write an article on cutting costs, my immediate reaction was to point out that working on increasing revenues was a more effective way to positively impact a firm's bottom line. There is no debate on that issue. Many attorneys seem to concentrate exclusively on cost-cutting strategies, while ignoring the fact that revenues generated are sub par for some or many partners of the firm.

Emphasis should be placed first and foremost on enhancing the revenue stream. Expenses are a target providing lesser opportunity, as often many of the expenses are so locked or beyond the firm's control as to make it difficult to improve the bottom line in any meaningful way. Unfortunately, a firm can cut expenses only so far without destroying morale of staff and/or attorneys, and/or creating a negative impact on client service, which ultimately lowers revenue further and exacerbates the problem.

Nonetheless, I would be remiss if I did not recognize that unnecessary overhead expense eats away at profits. Reducing overhead can effectively and immediately improve a firm's bottom line, and cash position. And whereas it normally requires an investment of both time and money to increase revenues, there is normally no cost to reduce overhead. Therefore, expense control is an important aspect of effective law firm management that cannot be ignored. That being said, however, I also add that it is best left to management at the administrative (staff) level, and should not require significant involvement of attorney time.

The first step in expense control and management is to identify those areas where potential savings exist. But beware the siren's call of short-term savings which wind up sacrificing long-term goals of the firm.

After identifying the areas of expense where savings can be made, prioritize the expenses in descending order, based on the potential magnitude of the savings. Then develop specific strategies and recommendations to achieve the savings. In many cases the firm's management committee—and sometimes even the

partnership-at-large—must approve the changes in order to ensure that the necessary level of commitment is present to achieve the desired goal.

If your firm is typical of most, compensation is the area with the greatest potential for savings. Unfortunately, it is an area where the greatest mistakes can and often are made when making cuts. First, you need to decide whether you will make the cuts quickly by termination and layoff, or slowly through attrition. Attrition is a better method from the perspective of morale. It is not obvious that the firm is making a cutback when attrition is used, and there is no emotional toll on those remaining. It is the method most firms use, because it is easier to implement for those without the intestinal fortitude to implement layoffs or terminations. But it is the least precise method because you can't be guaranteed that the *desired* people will leave, nor can you predict *when* people will leave.

Perhaps the most common mistake made is to terminate those at lower levels, and leave less productive and/or costly employees at higher levels. Let's face it, it's much easier to fire a messenger than the office manager, or a young associate or paralegal rather than an unproductive partner. However, law firms must concentrate on pushing work downward to the least expensive person who can competently complete the task.

The typical firm seeks to achieve downsizing by firing staff at the lowest levels, both from a compensation and hierarchy perspective. The work does not magically disappear just because the people doing it are terminated. Not only does this strategy minimize the compensation cost savings, it also pushes the lower level work upward to more talented employees. This serves to both downgrade the responsibilities of remaining employees, and increase the cost of performing the tasks reassigned. While one can defend this strategy by rationalizing that the firm retains a better talent pool in the process, that rarely turns out to be the case.

Most employees consider opportunity to develop new skills and further advance their careers to be a top priority. When this ceases to be the case, and in fact their responsibilities are downgraded, they will usually seek new and better opportunities. Turnover is expensive, both in terms of out-of-pocket, but also in terms of attorney time, and overall productivity as new people get "up to speed" in the unfamiliar environment.

A better strategy for cutting staff is to look for the highest positions which can be eliminated by reassigning the various responsibilities downward. With some training and education, the firm can push work down to a lower cost level, and



provide growth and advancement opportunities for remaining employees at the same time. This strategy provides greater savings in compensation, is not as deleterious to morale in the long term, and does not produce undesirable turnover.

A similar situation involves layoff or termination of associates and/or paralegals, without regard to partners who may not be producing for any of a variety of reasons. When a partner's productivity slips, he or she begins holding onto work previously delegated downward to more junior partners, associates and/or paralegals. It therefore becomes fairly easy to conclude that the associates or paralegals are the first of the professional staff to cut when trying to achieve a cost savings for the firm. After all, they don't seem to have enough work on their plate to justify their existence.

This is an erroneous but understandable conclusion. It is dangerous in that the responsibility to the client is to push work down to the most cost-effective level. It tends to very quickly destroy the firm's leverage and profitability base. It tends to eliminate the next generation of law firm leaders and rainmakers, as fewer people have an opportunity to rise through the ranks and perpetuate the firm. Hard-working partners may find themselves in a position where their retirement may actually mean an end to the firm itself. That leaves little if any opportunity to salvage their sweat equity.

A wiser strategy is to take a serious look at the firm's "worker bee" partners—that is those who have no book of business of their own, and are fed work by other partners. If a partner is responsible for maintaining key client relationships, takes an active role in firm management, and consistently produces a high level of billable hours, that partner justifies having their plate filled with work. However, if a partner does *not* meet these criteria, the firm should seriously consider whether the talent exists among the associate and paralegal ranks to provide satisfactory quality service to clients, keeping in mind that some training and mentoring may be necessary to effectively move that work downward.

Certainly my perspective will create great discomfort for many attorneys, and some may even react strongly. However, there is no doubt that the earnings of remaining partners will be improved more dramatically by eliminating a partner than by terminating one or more associates or paralegals, especially when the result is less mouths feeding off the profit pie. Of course, associates and paralegals who do not meet billable hour goals and consistently produce high-quality work should be those first targeted for termination when down-sizing is necessary. What the firm should avoid, however, is giving up desirable "next generation" associates because



the work which should go to them is going to higher-paid profit-sharing partners who don't generate sufficient work to fill their own plates, and don't offset this shortcoming with other significant contributions to the firm.

Employee benefits is probably the next area to offer significant opportunity for cost savings. It is an area of expense which has been growing rapidly for all employers, including law firms. Health and disability insurance premiums in particular have been experiencing large percentage cost increases.

Law firms have historically provided generous benefit packages, as part of their recruiting effort to attract associate talent. Plus, partners want to have generous benefits for themselves, often including the highest-cost indemnity medical plan. The majority of firms still offer full family medical coverage to attorneys, and individual coverage for staff. When premiums increase, employees get the equivalent of a compensation increase, but the firm gets no "bang for the buck" for the additional expense.

Firms often offer a multitude of other benefits including various retirement plans, long term care insurance, and long and short-term disability insurance. Many of these types of benefits have value for professionals, but may not provide the same perceived benefit to staff members. For example, if you asked your staff the majority would probably tell you that they'd much rather have a child care allowance or additional paid time off rather than life insurance.

The first step to cost savings, then, is to assess where the firm will gain the greatest benefit in terms of loyalty and retention of employees. Eliminate those benefits which do not provide the desired return, and replace them with those which do. You may be surprised to find that savings can be had from that simple change.

With respect to health insurance, consider offering more than one plan. Pay for the premium for the lowest cost plan, and allow employees to "buy up" to the better plan. Other ways to lower premium include incorporating higher deductibles, or eliminating prescription coverage. You can also consider capping your premium contribution, and requiring employees to pay for future premium increases. Just keep in mind that you need to remain competitive with employers in your area or this type of change can contribute to costly turnover.

In addition, consider offering an "opt out" dollar reward to any employee who has valid group coverage elsewhere and waives your coverage. Typically the "share" ranges anywhere from 60% premium savings to the firm and 40% to the employee, to 60% to the employee and 40% to the firm. At one firm, a partner who for years



had fully paid family medical coverage, elected to waive coverage for only a \$1,000 opt-out reimbursement. The firm had been paying over \$6,000 annually to provide full family medical coverage in spite of the fact that the partner's spouse had full family coverage as well. He rationalized that giving up his benefit was tantamount to taking a cut in pay.

At another firm an attorney health care policy was implemented which began with an annual survey form completed by each attorney, which required attorneys to state in writing whether they had no or low-cost health insurance available through their spouse's employer, and disclose deductibles. For those not sure, the firm required the employer's name and phone number, and the employee's agreement to release information, so that the firm could check. The firm's policy was to require opt-out in the case of duplicate insurance, even if it meant that the firm had to reimburse the employee for an additional premium for full family coverage on the spouse's policy, or for a higher deductible on the other plan to make the employee "whole" under firm's policy. The 36-attorney firm achieved savings in excess of \$20,000 per year by implementing this simple policy, even after paying the opt-out fees. Moreover, the firm was startled to find out how many partners and associates were taking medical insurance without ever disclosing that they had quality insurance available at little or no cost elsewhere.

Other expense categories may provide some opportunity for savings, but the firm may have to be more creative in its targeting. For example, if the firm has not taken a hard look at the rate tariff applied to its local and long distance telephone rates in the past couple of years, it may find considerable savings by doing so. Most firms do not realize that the telecommunications industry has been "soft" for the past few years, and there are many opportunities to negotiate better rates, particularly by consolidating several types of service with one vendor.

Another example of creative savings can be had simply by printing in duplex if your printer can do so, or by recycling used drafts and printing the next draft on the other side. Worried about confusion? Include the filename and date/time stamp in a footer on each draft page. Law firms are still paper-intensive, so don't underestimate the accumulated savings from reducing your paper consumption over the course of a year.

At most firms I find that there are some "sacred cow" expenses in the marketing area. For example, one law firm had a large yellow pages advertisement, and another had a general TV commercial which was not practice-specific. Each was an expensive marketing strategy, and at each firm dominant partners were promoting the strategy. But neither firm could point to a single matter which had ever resulted from their expense. Each firm saved significant dollars by eliminating



the “feel good” item from the budget, and neither noted any drop in revenues or matter intake as a result.

Take a good look at each of your marketing expenditures. I’m a strong supporter of marketing in law firms. I can assure you that those firms which market in a “down” economy will recover quicker than those who don’t when the market rebounds. And in today’s competitive climate, a firm must invest a significant percentage of it’s revenues—at least 5% in my estimation—on marketing strategies and activities. But, the firm must implement a strategy to track where its business comes from. And it must attempt to find a way to measure the efficacy of each expensive marketing strategies. Those which don’t produce results within a reasonable time limit should be eliminated.

There are lots of other opportunities to save cost dollars, from recapturing client costs more effectively, to eliminating unnecessary service contracts, to utilizing encrypted email to exchange documents with clients, rather than more expensive express mail carriers. Look at every line item on your financial statement for opportunity to target more savings. For example, when looking at your occupancy costs, ask yourself if they’re as low as possible. Does the firm use all available space to generate revenue? Are you using spare attorney offices to store junk? If so, clean them out and bring aboard an attorney sub-tenant in a non-competitive area of law. (Contact me to discuss the R.P.C. and malpractice issues which are relevant to an office sharing arrangement.)

Achieving meaningful savings requires careful analysis and planning. You want to reduce fat, not muscle. You want to achieve your savings without sacrificing long-term goals of the firm. You want to “right-size” your staff without negatively impacting client service. You probably have to be courageous and face some difficult issues, rather than take the easy path, in order to achieve significant savings. Don’t be penny-wise and dollar-foolish. And don’t neglect to invest the significant portion of your available time and energy into developing solid strategies to maximize revenues.

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