

Mitch Kowalski

Dewey LeBoeuf: Taking the short view

*It could never happen
to us, right?*

By Mitch Kowalski



To those of us with practices outside of global law firms, the meltdown of Dewey LeBoeuf seems unreal; the supposed “smartest guys in the room” managed to blow themselves up. For we regular lawyers, the destruction of a world built on hubris, greed and entitlement was, and is still, riveting. Dewey has become our own reality TV show, our own *Keeping up with the Kardashians*. Secretly we all want to be like them, but we so love to see them fail.

So we turn back to our practices and slap ourselves on the back with a smug, “It could never happen here.”

After all, we tell ourselves, law firms in Canada would never negotiate multi-year guarantees (payable no matter how the firm performs financially) for a third of their partners.

Nor, we say, would Canadian firms create Ponzi-like schemes of requiring such “guaranteed-income partners” to pay a percentage of their annual draw as a capital contribution in return for those guaranteed returns. (Ironically, banks who lent money to guaranteed income partners to cover their capital contributions are unwilling to take any haircut on these loans. And why should they?



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These partners are now earning major incomes at other firms and are perfectly capable of paying them back.)

And certainly, we sniff, Canadian firms facing a budget shortfall, would never compound such a financial mess by drawing heavily on lines of credit while also issuing IOUs to the “guaranteed-income partners.”

Or would we?

There are many lessons for Canadian firms in the Dewey disaster. Here are just a few:

A fragile structure

First and foremost the Dewey debacle reveals how fragile the partnership structure of law firms can be when competition among partners is unhealthy; many Dewey partners clearly saw the firm as nothing more than a place to make fast money before the next career move. Many of you are already saying, “So what? That’s the essence of law’s entrepreneurial spirit; each lawyer *building his or her own practice*.”

Partnerships have traditionally operated on the basis that collecting a number of profitable practices will automatically lead to a profitable firm. But what Dewey shows us — not that this is by any stretch of the imagination new information — is that the short-term goals of individual lawyers do not automatically lead to the long-term viability of a firm.

At too many partnerships, lawyers tend to be loyal only to themselves. Noted U.K. legal commentator, Stephen Allen, poses a valid question for those who are concerned about their own firm’s survival: “Do your partners value your partnership over their own personal aims and agendas?” In other words, is your partnership the sum of its parts, or greater than the sum of its parts? If it’s the former, then the only incentive for partners to remain at the firm is the continual granting of massive draws — and we saw how that turned out for Dewey. Money alone is not sufficient to keep a partnership successful and solvent for the long term.

In the aftermath of Dewey, I hope that we will see, as

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professor Stephen Mayson of the U.K.-based Legal Services Institute says, a shift away from concepts of ownership and rights, and a move toward concepts of custodianship, stewardship, responsibility and accountability in law firms; a shift away from building a lawyer's own practice to building the firm's practice; the creation of a firm that is greater than the sum of its parts; a firm that will be difficult for lawyers to leave because of what they give up by leaving. Perhaps we will see a move to a corporate model of organization, with an independent board of directors, and a strong CEO who makes decisions based on the long-term interests of the firm, rather than being forced to engage in the bargaining and horse-trading that is endemic in partnership decision-making.

Financial transparency

Also at the core of Dewey's failure was a lack of financial transparency. Firm financials are notoriously secret, as is the determination of partner compensation. But at Dewey this secrecy was compounded by allegations that the firm misrepresented its (secret and unsubstantiated) financials to lateral partners in order to entice them to join. One wonders how many lateral partners in Canada join firms without a detailed review of the firm's financial data, but I digress.

Given that the failure of any large firm is as traumatic for its clients and staff, as it is for its lawyers, perhaps it's time for law societies to mandate publicly available, audited financial statements for firms of a certain size.

Such disclosure would not only protect clients from disruption of their files, but also give lawyers the ability to conduct better due diligence before moving their careers to such firms.

Drastic response you may say?

Perhaps, but if lawyers and law firms have a special (and even noble) role to play in society, aren't solvent, well-managed law firms in the public interest?

Where was the risk manager?

Dewey's demise raises another issue that is relevant to Canadian firms — the lack of risk management.

I know of no law firm that has a full-time senior risk manager tasked with providing a contrary perspective on firm strategy, practices or policy. Yet most, if not all, well-managed and good-sized corporations have such a person of influence, who, in the Dewey scenario, would have asked several basic questions:

Isn't it possible that the economy will not stay strong for the length of the partner guarantee? How do we pay if the economy deteriorates?

Is that a risk worth taking?

And, is that risk worth taking with so many partners?

It seems that no one at Dewey asked these questions or if they did, these questions weren't given much thought. The result was a wilful exchange of long-term risk for short-term benefit.

While it's easy to criticize Dewey for its mismanagement, perhaps the most important take-away from this disaster is that it signals the initial death throes of an old world order. Dewey tells us that the current model of legal services providers is nearing the end of its natural life cycle and that it's time for new models to be created because the old way of doing things no longer works. ■

Mitch Kowalski is the author of the critically acclaimed, American Bar Association best-seller, "*Avoiding Extinction: Reimagining Legal Services for the 21st Century*," which will be widely available in Canada in December. He speaks, writes and advises on innovation in legal practice, and blogs for the *Legal Post* and *Slaw.ca*. Follow him on *twitter* @mekowalski or contact him at www.kowalski.ca.