

The “Associate Recruitment Conundrum”

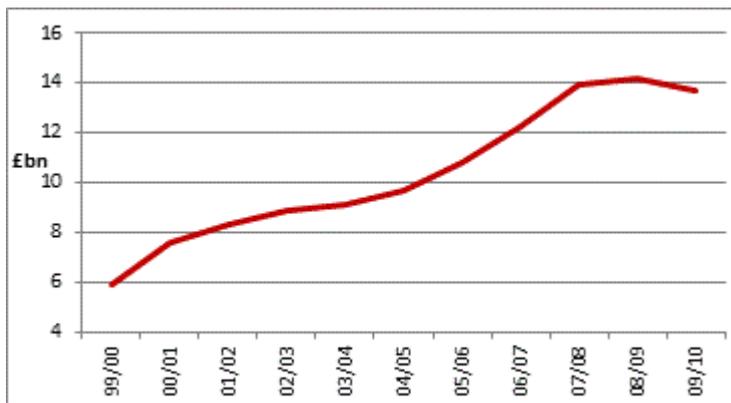
Why some firms are struggling to find the right people in a candidate rich market.

To answer this question (and to have any hope of at least addressing the situation) we need to look at the dynamics of law firm hiring over the last decade. This can roughly be broken down into four phases:

- The Market Rise
- The Market Fall
- The Current Market
- Prognosis for the Future

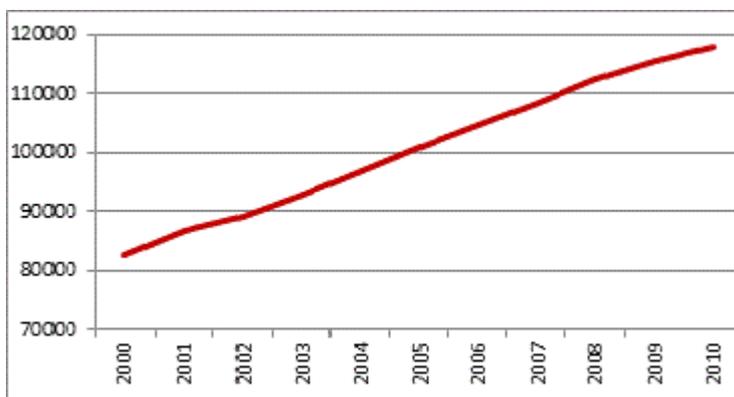
The Market Rise

Over the past ten years, the “value” of legal services produced by the top 100 UK headquartered law firms has increased by 133% (see graph). This represents a real term increase of about 94%.



Turnover of top 100 UK law firms. Source : Legal Business September 2010

Not surprisingly this is consistent with a rise in the number of solicitors with practising certificates over the same period.



Number of solicitors with practising certificates. Source: Law Society's Annual Statistical Report

From 2006 to 2008 (the “good old days”) we experienced frenetic activity in City law firm recruitment, characterised by:

- Law firm demand for candidates in virtually all practice areas;
- Multiple roles of similar types in law firms – for example most firms always had a requirement for assistants at all levels in corporate and finance departments;
- A real demand for commercial lawyers by in-house organisations (see below);
- A shortage of good UK qualified candidates for law firms;
- Large numbers of experienced lawyers being imported into the market from Australia, New Zealand, South Africa and Canada, as well as India in certain “hot areas”. We estimate in excess of 500 lawyers per year were transferring to law firms in the UK from overseas.

The market was such that there was a strong demand and poor supply of good candidates which resulted in:

- Sharp rises in compensation – there were large, across the board salary hikes in most City firms. For example magic circle newly qualified (NQ) salaries between 2005 and 2007 increased from c. £52,000 to c.£64,000 – an increase of about 23% over that two year period. Sign on bonuses were common and retention bonuses were near universal;
- Flexibility and a willingness to compromise on new hires in relation to their post qualification experience (pqe) level, pedigree, specific experience and the necessity for UK experience;
- High attrition rates – 2006, 2007 and 2008 saw attrition rates of 27%, 29% and 27% respectively in top 10 law firms (see below).

The above held true even after the collapse of Northern Rock in the summer of 2007 when the banking system started to fail. For law firms, this period was characterised by a “defiance of gravity” predicated on naivety and a belief that improvement was just around the corner and that departments needed to be staffed up to cope with an expected upsurge. There was some slowing of recruitment in areas such as structured products and real estate, but in the main up to, and throughout most of 2008, the legal recruitment market was reasonably active.

The Market Fall

The financial year ending 2010 saw the first fall in combined revenue at the UK’s top 100 law firms in over 10 years. Although only slight, when taking into account inflation, this had real implications for the UK legal market.

From the last quarter of 2008 and throughout 2009, the market was characterised by:

- A sharp fall in assistant utilisation rates: according to the PricewaterhouseCoopers (PwC) 2010 law firm report, in 2009 the top 25 firms saw a 20% reduction in chargeable hours for all levels of lawyer;
- An immediate and drastic headcount reduction of around 10% of commercial lawyers in City law firms (either by redundancy or “performance management”). Redundant lawyers generally fell into three categories:
 - I. the “fat” – generally underperforming lawyers who the firm might secretly be happy to be rid of, but also lawyers who were “nice to haves” such as professional support lawyers which firms couldn’t necessarily justify keeping in the prevailing economic environment;
 - II. the “newbies” – these included lateral assistant hires who had been employed for less than 12 months and so were more vulnerable to the “last in first out” syndrome. Unfortunately some excellent quality lawyers fell victim to this;
 - III. the “muscle” – after the fat and the newbies had been removed, many firms still had to reduce headcount and were forced to cut into their ranks of experienced, quality and loyal lawyers.

- The virtual collapse in assistant level recruitment at law firms - even “necessary” hires into crucial areas (such as finance litigation and restructuring) were halted as widespread redundancies in other departments made hiring a politically thorny issue. By the first quarter of 2009, we estimated that assistant lawyer level vacancies in City law firms had fallen by about 95% from the first quarter of 2007.

The result was that, for the first time in 10 years, there was an across the board surplus of very good lawyers in areas which were hitherto in demand, such as corporate, finance and real estate.

In a reversal of the position seen up to 2008, there was a strong supply and a low demand for good quality lawyers which resulted in:

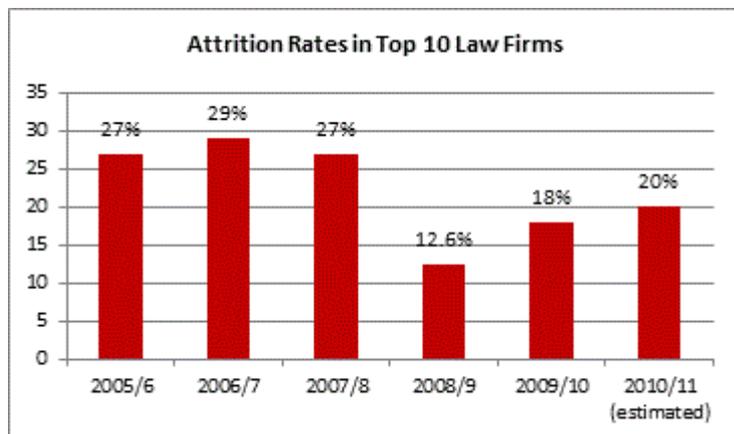
- Reductions in compensation – across the board base salary freezes for individuals and some actual reductions in pay bands in 2009 (at this time pay bands were generally frozen and lawyers were not matriculated up the lockstep resulting in a notional fall of c. 8% in associate base salaries);
- A lack of flexibility and willingness to compromise on the level, experience and quality of candidates. In addition, in virtually all areas new hires were required to have relevant UK experience which led to the complete collapse in the importation of overseas lawyers;
- Very low attrition rates – from a high of 29% in 2007, by 2009 the average attrition rate in the top 10 UK firms had fallen to 12.6%. Taking redundancy out of the equation, this probably meant a real “voluntary” attrition rate as low as 3%.

The Current Market

It is fair to say that the market has improved somewhat over the last 12 to 18 months. 2010/11 law firm financials generally show modest rises in revenue and in fact even by the end of 2009/10, chargeable hours were up 7% in the top 100 firms (source: PwC 2010 law firm report).

We have seen a significant demand for candidates from law firms and looking at the number of “live” assistant lawyer level vacancies in the 1st quarter of 2011, it was up by more than 1000% from the same period in 2009. Nevertheless the recovery in demand is still relatively weak and we estimate it to be about 65% of what it was in its 2007 and 2008 peak.

On the back of this steadily increasing demand by law firms, as well as by in-house organisations, attrition rates are starting to rise again and were averaging 18% in top 10 UK law firms in 2010 (compared to 12.6% in the previous year). We estimate that 2010/11 will see attrition rates of about 20%.



Source PwC 2010 law firm report

The Associate Recruitment Conundrum

So why then are some firms finding it difficult to find the right candidates? Despite law firms having the roles and recruiters having objectively “good” candidates, there is still a supply and demand imbalance when it comes to associate lawyer hiring. This is what we have called “The Associate Recruitment Conundrum.”

One of the main issues arises out of what we like to call “The Inflexibility Factor”. Over the last two or three years (particularly after redundancy consultations have concentrated minds) decision makers have somewhat changed their mind set. There seems to have developed a need (and expectation) that any incoming lawyers should be better, or at the very least on a par with, the current team. After all, if overall demand has fallen and supply is theoretically good, it makes perfect economic sense to expect this. The result is that objectively “good”, but not necessarily “stellar” candidates who, in the years between 2005 and 2008 would have been “walking placements”, have not been immediately placeable. As was the case during the “market fall” phase, firms have remained unwilling (or possibly unable) to compromise on level, experience and quality of candidate.

It’s worth noting that because the recovery is fragile and, although the latest financial results show that profits per equity partner (PEP) have generally increased, much of this is largely down to cost cutting measures so firms are reluctant to staff-up with anything other than “perfect fits”.

This “Inflexibility Factor” alters the supply and demand dynamic and has resulted in increased competition for the few candidates that 100% fit the bill.

Disadvantages for HR Teams

In contrast to the 10 years prior to the recession, law firm HR teams and hiring partners are facing a number of disadvantages when it comes to recruiting:

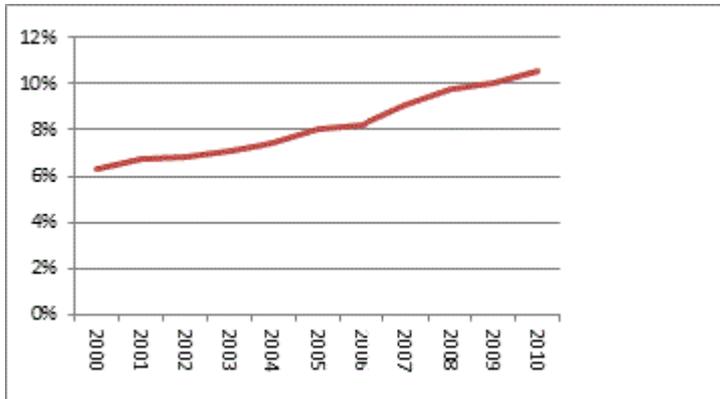
- No compensation incentives – throughout 2009, 2010 and 2011, salaries have remained flat, or at best increased by less than inflation. In addition, and perhaps surprisingly, there has been a significant increase in retention bonuses paid by law firms in order to keep their best people. The PwC 2010 law firm report states:

“Firms continued to pay bonuses in 2010 and at a higher percentage of salary than in 2009 (which in turn were higher than 2008), using bonuses as a method of rewarding staff without increasing base salaries and giving greater flexibility to the management on staff costs.”

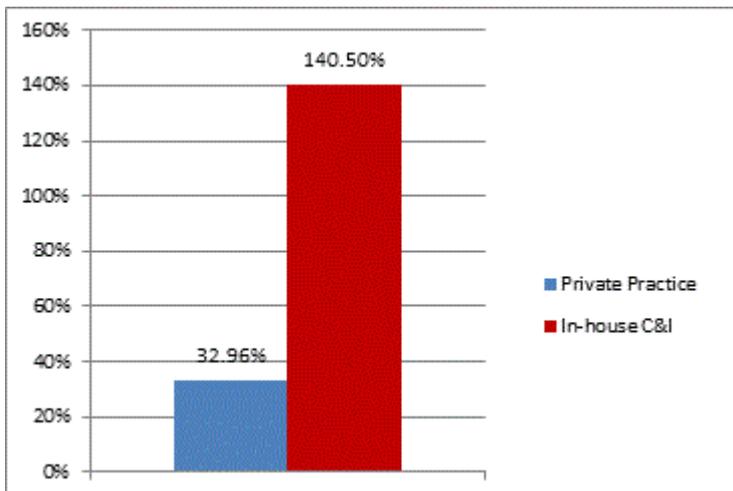
Hiring firms have not been able to counter these retention bonuses with sign-on bonuses.

- A “sealed recruitment market” – a lack of demand in recent years has led to fewer overseas qualified lawyers in the UK market, but importantly, despite an increase in demand, the confusion surrounding new Home Office guidelines on visas and sponsorship and a fear of falling foul of the seemingly forever changing restrictions has made some firms steer clear of “importing” overseas lawyers;
- Candidate fear – in what are still clearly economically uncertain times, the “last in first out” fear of lateral assistants has remained very real. The redundancy rounds of 2009/10 also suggest that this fear is entirely justified;
- Competition from in-house organisations – over the last decade, the number of solicitors with practising certificates working in commercial in-house organisations (as opposed to public sector or trade union positions) has risen by more than 140% (see graphs below). In 2010 alone the number of commercial in-

house solicitors with practising certificates increased by nearly 8% which, considering that less than 3% of solicitors train in-house, means this supply has been met with candidates from private practice law firms.



% of solicitors with practising certificates working in C&I. Source: Law Society's Annual Statistical Report



% increase in no. of solicitors in private practice and C&I 2000-10. Source: Law Society's Annual Statistical Report

Suggestions for HR personnel as to what can be done

Unfortunately, as with most things in life, there is no magic solution. But we have a few ideas of things you can do which may at least alleviate the stalemate a little.

Redeploying resources

Perhaps there is someone being under-utilised in another department or another office either in the UK or internationally. Make sure that other HR managers across the firm are aware that the vacancy exists in your office (some firms are better at communicating internally than others!).

Recognise the limitations of the brand

Of course a firm should play to its strengths and shout about their success from the rooftops, but it is as important to be realistic about non-core areas. For example, if you are known for litigation, the market will find it hard to see beyond this and a top 5 firm corporate lawyer is not necessarily going to see you as a natural

home for getting involved in headline grabbing transactions. You need to be targeting candidates at firms that will see you as a step-up.

Affording flexibility

Making small compromises can make a big difference to whether or not you will fill a role. Perhaps look at the next tier down of firms from your ideal, slightly expand the ppe range and consider candidates that may be lacking experience in a particular area but are bright and willing to learn. In fact, something you should remember is that if you want say a 2 year ppe equity capital markets lawyer with a decent chunk of experience, you'll find that there are very few of them around. The capital markets have been depressed for some time and very few candidates will actually possess this experience let alone want to leave their current firm.

It's important to think about what the consequences might be if you don't hire somebody and use this to instill a sort of "fear" if you like in the partners. How will they be able to bring in new work if they don't have the team to support them and how will the current (perhaps overworked) assistants feel? Will they see the lack of hiring as a lack of commitment and consider moving on themselves?

Using recruiters

Are you using recruitment consultants and if so are they the right ones? Generalist recruiters will be more inclined (consciously or sub-consciously) to focus on areas that are easier to fill. Niche legal recruiters don't have a choice: they just recruit lawyers. Make sure your recruiters know exactly what you are looking for by speaking to them in detail and ideally getting them in to meet partners where possible – this will always make them work harder on your roles. It's also important to think about the "value" recruiters can provide in terms of efficiency, speed and market knowledge rather than just "cost" when it comes to decide whether to use an agency or hire direct.

Persistence

Once a vacancy has gone live and you've let your recruiters know, don't just leave it there – keep plugging it by reminding them it is live and give feedback as to how many CVs you've received and how many candidates have been interviewed. Although CV Mail or similar systems may be an important part of your process, they can often remove the personal communication element from recruitment which will dissuade many recruiters for wanting to work on your roles. And just as important as letting recruiters know of vacancies, is letting them know when they've been closed – there's nothing worse than finding the perfect candidate only to discover that you've now filled, or withdrawn, the role.

Advertising and marketing

It is worth thinking about advertising, either direct or through an recruitment agency where you can benefit from substantial discounts, as not only are you making potential job seekers aware of your hiring needs, you're also letting the rest of the market know that your firm is doing well enough to put it in the position of needing to hire in the first place. Social media is becoming more and more popular throughout the legal community so it is worth exploring the likes of Twitter and LinkedIn as excellent ways of both networking and building brand awareness amongst the passive community.

Prognosis for the future

It all really depends on where the economy goes from here, but the current market is more likely to be within the bounds of "the new normal". Recent UK law firm revenue increases have, in the main, not been of any significance and in fact much of the increase has been generated by firms' international operations. In the absence of a UK economic renaissance (of which there is currently no evidence) we expect to see only small compensation rises over the next couple of years and a (general) continued unwillingness to compromise on

that “perfect” candidate. We also expect attrition rates to remain steady at around 20% with in-house recruitment continuing to take a steady toll on law firm talent.

If our predictions are correct, this "Inflexibility Factor" will continue to exist in relation to law firm lawyer recruitment and the associate recruitment conundrum will perpetuate. Taken to its logical extension and, in conjunction with a fading of lockstep ppe, we may see an increase in disparity of compensation between assistants as stellar (in demand) lawyers are necessarily looked after at the expense of just “good” lawyers. Indeed, the result may be a complete recalibration for recruitment consultants and law firms of exactly what a “good” candidate is.