



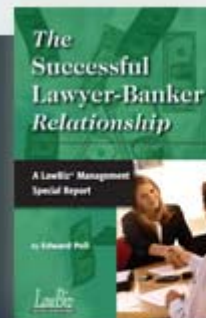
Week of **February 10, 2009**

If You're Not Liquid, You May Have to Liquidate

In times like these the old cliché about the economy hits home: "If other people lose their jobs, it's a recession; if I lose my job, it's a depression." All law firms today are in some way dealing with recession. But what if the situation is more serious - business has slowed to the point where the firm's survival is at stake. No firm can ignore such a drastic possibility, or be ignorant of the three unpleasant alternatives it will face.

(1) Downsize. We've warned previously about the danger of cutting muscle as well as fat when reducing expenses. But sometimes surgeons have to cut to save a life, and law firms can face the same hard option. Some of the cuts can be financial. Begin with planned capital expenditures, progress to current expenses for maintenance and facilities, and as a last resort reduce compensation (in order, bonuses, staff/associate pay, and partner income). Beyond this, cuts unavoidably involve people. Two rounds of staff layoffs could be attempted before eliminating associates, with de-equitization or forced retirement of counsel and partners as a final step.

(2) Demerger. Law firms that have grown by merger or acquisition may be required to reverse the process if the firm can no longer support its expanded size. A merged practice can be split up into premerger units, especially if the internal cultures of the groups are still largely intact. Other demerger alternatives are cutting lose an area of the practice that is not profitable, or dramatically scaling back those areas of nonessential practice hardest hit by the economic decline - which today might include structured finance, or some aspects of M&A practice. Segments of the firm, or even individual lawyers, may be encouraged to leave and form boutique practices to which the parent firm can still have access (without adding people) if it survives the business



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decline.

(3) Liquidation. When the law firm's survival is doubtful, and it's not possible to find a buyer at any reasonable price, it may be time to consider liquidation. While the firm will cease to exist, individual lawyers will go on. They can join another firm or start a new one. The trickiest aspects of liquidation require the division of both partner financial assets and firm clients. In the latter, partners who take clients with them to a new firm should get formal, written client authorization to remove files from the sinking firm.

All law firms must provide value to their clients. And they must be profitable in order to open their doors the following day. The point when cash stops coming in the door is much too late to start wondering if there is a problem. The seeds of the problem were undoubtedly sown weeks, months, or even years earlier. At this point, recognizing harsh reality is the only real option.

Personal Commentary

Has your firm asked you to pony up money? Have you faced a capital call recently? Are your partner distributions being reduced?

A recent (January 29th) *Wall Street Journal* article discusses the new phenomenon. Several top law firms are asking their partners to increase their capital accounts and/or are reducing the partner distributions, all in an effort to raise more cash for the law firm. Why? Because the new focus is on reducing law firm debt and increasing liquidity in an era where banks are restricting their loan portfolios, even for "favored customers." With revenues and profits constricting, law firms are wise to review their debt structure.

When the law firm cannot open the bank's loan window, or doesn't want to abide by the many restrictions and covenants that are attached to any bank loan, the firm will look to partners. And, for those partners who are themselves financially thin, they may have to be the one asking the bank for help in order to satisfy the capital call. To get the personal loan needed to fulfill the capital call, the lawyer may have to mortgage his/her home, pledge other assets as additional collateral or even get guarantors.

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"The practical steps that Ed Poll provides in this little volume cover everything from how to choose a bank that's right for you, to how to improve your credit score and how to negotiate the best commercial loan to meet your needs."

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-Howard Putnam, Former CEO of
Southwest Airlines and Braniff Airlines

Solo and small firm lawyers experience the peaks and valleys of compensation as a normal course of business. To survive tough times such as we currently are experiencing, reduced debt and a reservoir of savings is essential to survival.

Perhaps it is not unreasonable to ask yourself the question, "Do I really want to be a law firm partner?" Do the benefits outweigh the risks?

Best wishes,

Ed Poll

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