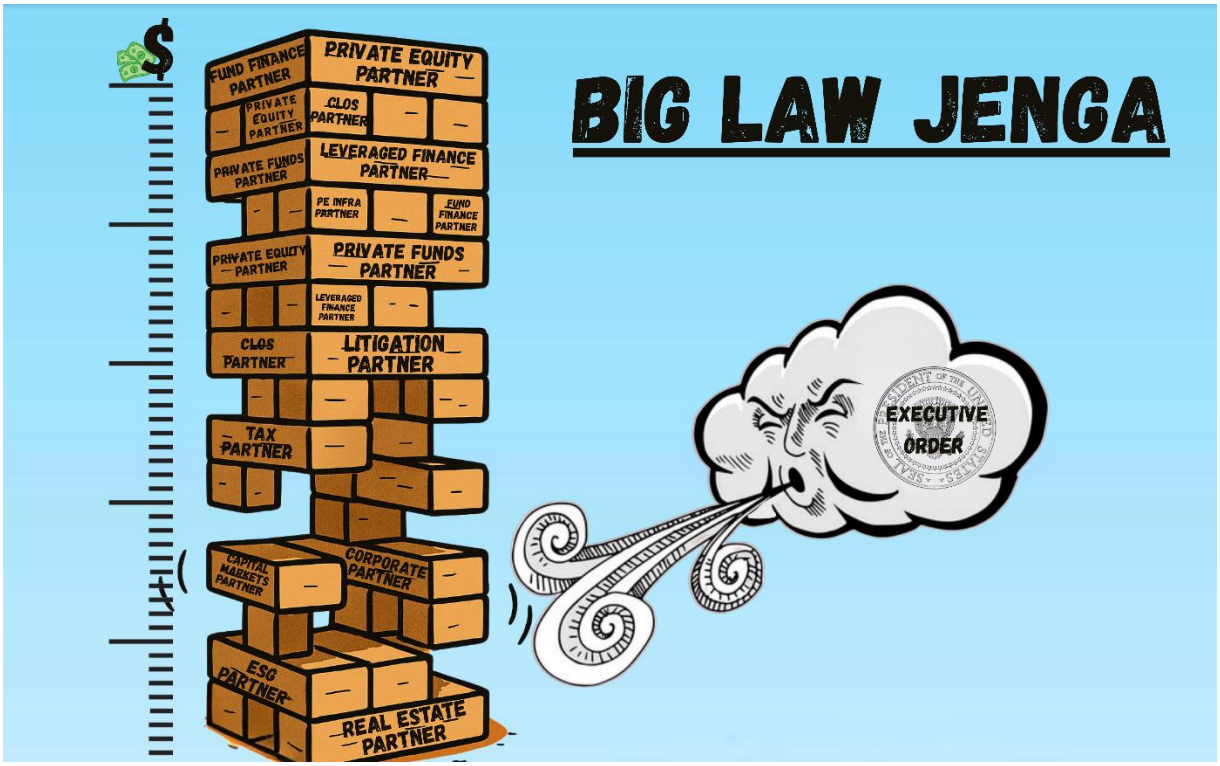
Big Law Jenga; Why Private Capital Stars are a Tragedy for the Rule of Law



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Executive orders, a functional death sentence

So far, the Trump Administration has issued executive orders against five Big Law firms (one now rescinded). Among many other restrictions, the orders bar lawyers at those firms from entering courtrooms and, importantly, they target, not just the law firms, but also their clients. As such, they have been termed "a functional death sentence". Unsurprisingly, challenges to the orders have led to temporary stays pending further court hearings.

Most senior lawyers admit privately to being appalled by these attacks. Moreover, as Edwards Gibson has previously argued, the financial success of Big Law is predicated entirely on the rule of law. So why has Big Law, that immensely powerful and well-connected collective, been so spectacularly ineffective in standing up for its own interests? And why, when a quartet of law firms –- **Perkins Coie, Jenner & Block, Susman Godfrey** and **Wilmer Hale** [The Quartet] - decided to fight the administration, did the much more powerful super elite New York firm **Paul Weiss** take a different tack and, together with a host of peer and near peer rivals, settle with the White House?

The answer lies in three interconnected developments in Big Law: (i) the inherent fragility of the law firm partnership model which, post financial crisis, has become even less cohesive; (ii) the increasing reliance by Big Law on private capital clients to drive its stratospheric profitability; and (iii) (thanks to (i) and (ii)) the increased ease in which individual rainmaker partners can switch law firms, taking all of their lucrative private capital clients with them.

- **Law Firms are a confidence trick**

For all their many advantages, law firm partnerships are inherently unstable entities. This is because, unlike normal businesses, the value of a law firm derives, not from its manufactured product or its IP, but entirely from its people. Its working capital is quite literally provided by its equity partners who, together with their clients, can swiftly decamp *en masse* to rivals should they wish. Big Law firms such as **Brobeck, Phleger & Harrison**, **Dewey & LeBoeuf**, **Heller Ehrman**, **Howrey**, **Stroock & Stroock & Lavan, Thelen** and **KWM** (SJ Berwin in old money), all collapsed – often within months – after partner departures. For the same reason, scores of other law firms would have gone the same way had they not been rescued in fire sales often on terms which were highly disadvantageous for their remaining members.

- **Big Law's reliance on private capital clients to drive stratospheric profitability has created a "star culture", making partnership structures more fragile than ever before**

Post financial crisis the dramatic growth in size and profitability of the most successful law firms has been on the back of their private capital clients which, due to their strong personal relationships with individual lawyers, has increasingly fostered a "star culture" within Big Law. In areas like leveraged finance and private equity, individual law firm rainmakers now have portable client relationships running into the scores of $millions.

Unsurprisingly, these rainmaker lawyers are in great demand and so are very highly paid – even in London, laterals at US law firms have reportedly moved for $20 million p/a.

To accommodate the financial expectations of these rainmakers, over the past decade, virtually every single elite law firm has abandoned their once sacrosanct lockstep pay structures (where partner compensation increased with seniority) in favour of models which more directly reward rainmaker partners for the massive levels of work they personally bring in.

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Whilst this has been highly successful as a recruitment strategy for some and has (at least partially) inoculated others from raids by head-hunters, it has come at a price of weakened partnership cohesion. Until comparatively recently, lawyers who qualified and made partner at truly elite law firms tended to remain at those firms until they retired. Even where the pay arbitrage at peer and near-peer rivals was sufficiently tempting for them to move, the cultural mores of the firm they grew up in were just so imbedded that it prevented them from ever seriously considering a lateral move. However, a combination of: (i) altered partnership compensation structures, where existing partners perceive the (once immutable) "rules" to have dramatically changed; (ii) an infusion of highly paid partners from other firms joining, whose very arrival subtly (and sometimes not so subtly) changes the DNA of the firm; and (iii) the eye watering levels of compensation on offer, have upended this. Today even law firm "lifers" regularly move and expensive laterals, particularly those in private capital, are statistically more likely to move than anyone.

On both sides of the Atlantic, over the past two years, a private capital fuelled internecine talent war between US law firms has caused a boom in partner compensation and according to the *84th edition of Edwards Gibson's Law Firm Partner Moves in London*, has been responsible for record levels of partner hiring in the world's second largest legal market.

- **Elevated potential for super elite law firms to rapidly collapse**

More so than any time in history, today's Big Law culture demands that elite law firms remain profitable relative to their peers – failure to do so means that its rainmaker partners will quickly decamp to rivals taking scores of $millions in client fees with them. Where teams, or multiple teams, depart this could result in the loss of $hundreds of millions further drastically decreasing profitability and inevitably causing a "run on the partnership" – a self-fulfilling prophecy where partner after partner loses confidence and jumps ship in order to escape the financial consequences of reduced profitability and, after a point, the inevitable rapid collapse, or fire sale, of the business.

When this process starts, the push factors for remaining partners can be overwhelming; equity partners who fail to get out whilst the going is good risk being left holding the baby in an insolvent collapse.[1] If this is not enough of an incentive for partners to jump ship early, those who leave it too late often find that the suction effect of the law firm's gravitational collapse exposes them to the very same liabilities as the remainers.

What this means is that, if an elite law firm whose profits per equity partner are, say, $7million p/a suffers the sudden loss of major clients through a series of high-profile rainmaker defections, even where its remaining underlying business would have remained profitable and strong, it still runs a high risk of collapse or fire sale. This is because those partners, who might otherwise be perfectly happy to take the financial hit and remain at the firm, perhaps earning a more modest $4 million p/a, simply cannot afford to risk the consequences of staying.

- **Super elite firms - paper tigers, rational economic actors**

So it is that, despite being extremely powerful global businesses with the expertise to confront such challenges, the largest and most powerful Big Law firms are so impotent when faced with the Trump administration executive orders.

Indeed, the most profitable transactional law firms are now so disproportionally reliant on relatively few star rainmakers with large portable private capital client bases, that any major existential shock which significantly impacts their profitability relative to other firms – such as an executive order targeting their clients – has a very good chance of causing those rainmakers to leave, inadvertently trigging a law firm death spiral.

In relation to the Trump executive orders, this is not to say that all rainmakers are so self-serving and devoid of a wider responsibility to their partnership that they would all immediately jump ship just because their firm might be about to take a hit on profits. Especially in the face of such a seemingly noble cause. However, because the executive orders target not just the law firms but the law firm's clients, most rainmakers will simply have no choice. In those circumstances, private capital clients fearful of being on the wrong side of the administration are likely to want to switch law firms. Any rainmakers who refuse to go along will not only permanently lose these incredibly lucrative client relationships, but simultaneously become expensive, not to mention unwanted, dead weight at their law firms. This is especially the case if they are a lateral on an eight-figure guaranteed income.

[1] In those circumstances, whilst their personal financial exposure is theoretically limited by the LLP agreement to the extent of their capital contributions, as Yale Law School Professor John Morely writes in "*Why Law Firms Collapse*", the LLP "shield will be useless against a variety of indirect claims that flow from the partners' status as owners and come out of the laws of fraudulent transfers, preferential transfers, and unfinished business." Happily, for partners, due to the difficulties of recovery, Morely states that bankruptcy trustees and creditors nearly always settle these claims at a fraction of their value. However, as equity partners from a multitude of collapsed law firms will attest, even if they "only" lose their capital, vexatious recovery actions, and painful tax issues, will trail them for years to come.

Big Law's collective action problem; live by the lateral die by the lateral

It is against this backdrop that, when faced with a similar executive order, **Paul Weiss**, the super elite Wall Street Titan with impeccable liberal credentials, settled with the Trump Administration much to the chagrin of many, including a good number of its own associates within the legal community. In return for the Administration rescinding its order Paul Weiss agreed to: provide $40 million in *pro bono* over four years, which according to Trump will support his Administration's agenda; weaken its DEI policies; and arguably admit to unspecified "wrongdoing" on the part of one of its former partners, (whose only wrongdoing appears to have been involved in the successful prosecution of Donald Trump).

Whilst this settlement was certainly inglorious and has been contrasted unfavourably with that of the litigation flavoured Quartet for the reasons above, Paul Weiss probably had no choice. Unlike those firms, Paul Weiss is predominately a transactional (deals) firm with radically different workflow and economics, its profitability is ordinarily double, even triple, that of those others. Furthermore, over the past two years, Paul Weiss has become the apex predator of Big Law - the archetype of the aggressive New York recruiter ripping out rainmaker private capital partners from peer and near-peer rivals, including from the equally rapacious Chicago spawned outfit **Kirkland & Ellis**. For example, in London, it is no exaggeration to say that, over the past two years, the impact of this one firm's spate of lateral hiring, has been to upset the entire Big Law ecosystem.[2]

As such, it is hardly surprising that, when singled out by the Trump administration, Paul Weiss had few friends in its Big Law peer group, indeed amongst the fear for their own business, there was likely an element of *schadenfreude*. As Paul Weiss' Chairman Brad Karp pointed out in his message to the firm on 23rd March, "*we waited for firms to support us in the wake of the president's executive order targeting Paul Weiss. Disappointingly, far from support, we learned that certain other firms were seeking to exploit our vulnerabilities by aggressively soliciting our clients and recruiting our attorneys."*

[2] Edwards Gibson 2024, *Paul Weiss - The invasive species that upset the London Big Law ecosystem*

There is a jurisprudential maxim which every law student should know, "*he who comes to equity must come with clean hands*"**.** It was undeniably in Big Law's longer term financial interest to come together to fight the Trump administration on this existential threat using Paul Weiss – a true Wall Street colossus – as a figurehead to stiffen the resolve of all. However, in view of the firm's leading role in fuelling the lateral talent war that was never likely to happen. After all, tigers, even paper tigers, don't hunt in packs.

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- **Transactional Big Law surrenders**

Big Law's failure to support **Paul Weiss** was a tragedy, it was the best chance for the collective to mount a truly effective counter to the Trump Administration's assault on the rule of law. It should be noted that any notion of collective action was somewhat undermined from the get-go by fellow super elite New York firm **Sullivan & Cromwell,** which advised the Trump Administration on the settlement with Paul Weiss and is now under congressional scrutiny for its actions in facilitating the administration's measures against other law firms.[3]

Of the fourteen law firms which the Trump Administration announced that it intended to probe on the 14th March 2025, all of the major transactional firms (**A&O Shearman**, **Cadwalader**, **Kirkland & Ellis**, **Latham & Watkins**, **Milbank**, **Paul Weiss**, **Simpson Thacher**, **Skadden**, **Willkie Farr**) have now agreed to settle.

In terms of *pro bono* payments, the going rate appears to be $100-$125 million, although Paul Weiss (the only one of these firms to actually have an administrative order issued against it), settled for $40million. Unsurprisingly, all the firms have put a positive gloss on their settlements. None have admitted to specific wrongdoing and the accommodations they have made have been portrayed as being entirely consistent with their values and longer-term goals.

Most commentators, not to mention lawyers, at these firms, regard the settlements as capitulation to the administration. Gregory Wallance in his article, *Law firms that settle with Trump have a Sword of Damocles over their heads,*[4] points out: *"Ordinarily, settlements spell out the obligations of each party, and include detailed definitions and sometimes elaborate dispute-resolution mechanisms if a disagreement arises over a party's compliance. I doubt that … any of the settling law firms would have recommended that one of their clients sign a settlement agreement that did not include such terms — yet that is what these firms have done."*

Certainly, Trump himself seems to consider that some of the nearly $billion in settlements could even be used to assist the United States in its trade negotiations with other countries over tariffs.

- **A forlorn hope**

The first substantive hearing against any of the orders is scheduled for **Perkins Coie** on the 25th April 2025. Although Perkins Coie does not fall into the super elite category, it is a major full service Big Law firm and, even though the order has been temporarily stayed, it has likely already suffered real damage to its business.

Over 500 law firms have put their names to an amicus brief in support of Perkins Coie. Whilst there are some notable names, including **Arnold & Porter** – a Washington DC firm which became famous in the 1950's for standing alone against the McCarthy Witch hunts, the only globally significant law firm

[3] United States, Congress, *April 6 2025 Congress of United Sates Letter*

[4] Gregory Wallance, *Law firms that settle with Trump have a Sword of Damocles over their heads*, The Hill, 23rd October 2023

to sign is **Freshfields**. Bearing in mind that Freshfields is UK headquartered and was not even in the administration's crosshairs, its decision is brave and even noble.

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Given the legal merits of its arguments, Perkins Coie, like the rest of the Quartet, will likely win at first instance. Longer term, like 1950's Arnold & Porter, those firms may even gain new work flows precisely because they have stood up for the rule of law. That being said, the administration has a very sympathetic Supreme Court which, on appeal, might find some quixotic way to re-interpret the Constitution. Moreover, this administration has shown itself to be quite shameless in its utilisation of state apparatus to impose its will on those who thwart it, so The Quartet should not discount some, as yet, unforeseen blow-back.

A pyrrhic victory

Regardless of whether Perkins Coie and the other holdouts succeed in overturning the executive orders against them, the rule of law has already been undermined in a way previously unimaginable. Going forwards, no law firm, including those who have fought the executive orders, will be able to take on any matters without considering their political sensitivity. Law firms will deny this, but the concept of legal representation "without fear of favour" has died in the United States. Amidst the Big Law legal community the "fear" is real and the consequences for justice are terrifying.