

EDGE International Review

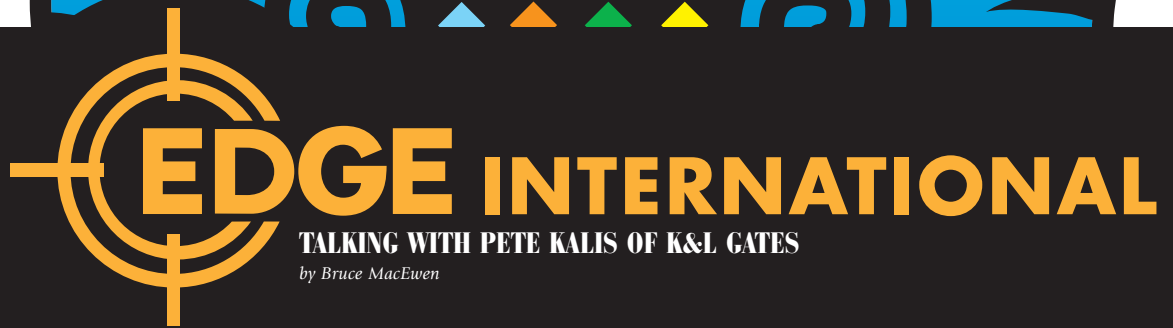
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**SUCCESSFUL
TRANSITIONS:
THE NEW MANAGING
PARTNER'S FIRST DAYS**
by Patrick J. McKenna



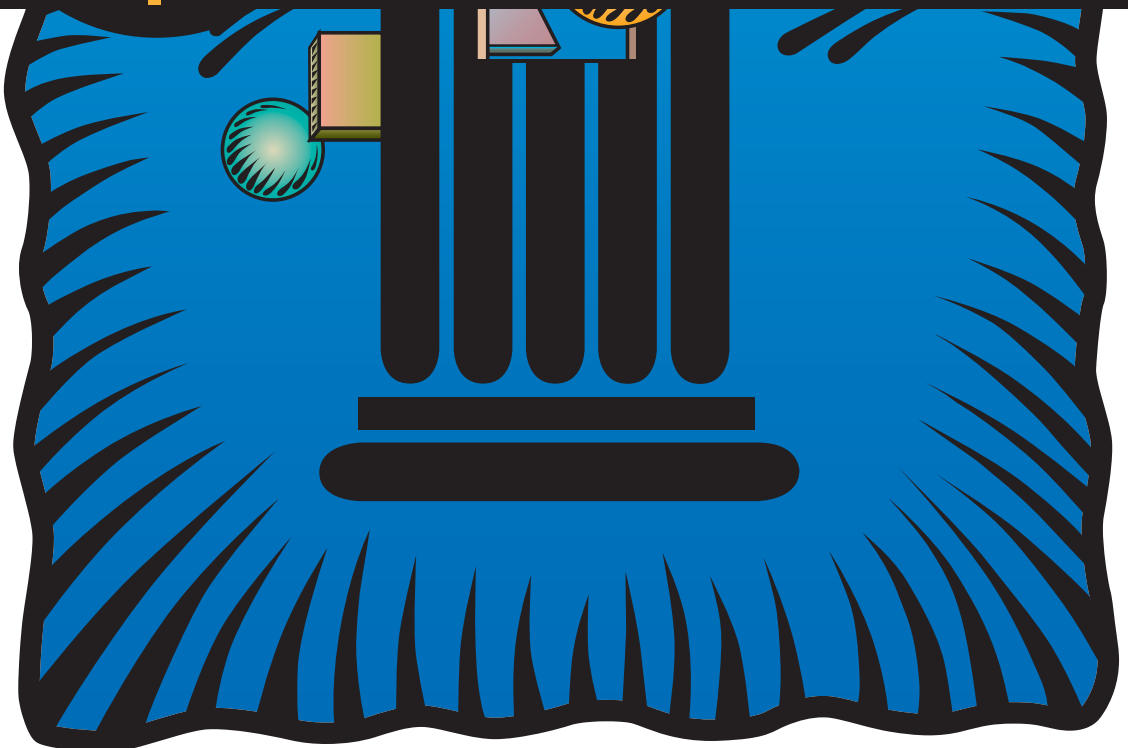
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TALKING WITH PETE KALIS OF K&L GATES
by Bruce MacEwen

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**PLANNING YOUR LAW
FIRM RETREAT**
by Edge International



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Talking With PETE KALIS

At age 56, Pete believes he stands at the dividing line between the maturation of the profession into an industry: He describes himself and his peers as the “ultimate, or more probably, the penultimate generation of unintended managers,” people who are selected largely by process of elimination.

IS

of K&L Gates

We had an opportunity to sit down with Pete Kalis, Chairman and Global Managing Partner of K&L Gates, which is the product of the January merger of Kirkpatrick & Lockhart with Preston Gates & Ellis, creating a firm of 1400 lawyers in 22 offices on three continents. Although that milestone was a spark for the meeting, we had long wanted to get his views on the current state and future trajectory of our industry, and our supposition that his thoughts would be nuanced, astute, and every so often contrarian, were borne out in spades. Pete has thought long, deeply, and hard, about the evolution of our profession—and our industry, a distinct, but equally apt, perspective—all the while with his hands under the hood, as it were, of an increasingly prominent firm. His thoughts demand attention, reflection, and ultimately, action.

A Generational Shift

Firms have a peculiar, unscientific and very time-and-place specific approach to choosing leaders. They must be:

Not too

young, not too old; must have the respect of the partners; equity not income partners, etc.; and at the end of the process there may be very few viable candidates left standing.

Contrast this with corporate America: When they need a new leader, Pete says only half-facetiously, they get on I-95 and head up to Fairfield, Connecticut where they swipe someone from GE. Why? GE's senior executives are known to be globally oriented, bottom-line focused, with an intense strategic perspective on their business and the mandate to be in a leading position. Imagine if

law firms exercised similar rigor in their choice of leaders. He predicts that the next generation or two of law firm leaders will "almost certainly" be chosen through a more sophisticated process.

Parenthetically, here's a thought experiment for you - Question: How will we know when law firms have truly evolved to the corporate model? Answer: When they look outside their own four walls for a firm chair.

Pete said he didn't mean to be self-deprecating, but his career objective had never been to be leader of a global law firm: His selection to that position in 1997 was by consensus, but still didn't amount to the equivalent of a rational search by an elite recruiting firm. [We should interject here, in case you didn't know it, that Pete has nothing whatsoever to be self-deprecating about: His credentials include being Editor-in-Chief of the Yale Law Journal, a Rhodes Scholar, and law clerk to Skelly Wright, chief judge of the DC

Circuit, and then Byron White on the Supreme Court.]

Composition of the Elite Firms Today

We ask if he thinks leadership matters, and he virtually erupts: "*Absolutely*, and the bigger and more sophisticated the firm, the more so." He proceeds to share his view of how the structure of the legal industry came to be as it is today, and divides the high end into two types of firms:

- Those who appear to have been born with a brand: The New York "bulge bracket" firms, the Magic Circle in the UK, firms that appear to have sprung entire onto the scene at birth with impeccable pedigrees and

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nearly-insurmountable market positions. Of course that's an illusion, and we all know most of these firms began as two guys sharing a partners' desk on the second story of some passable building in a marginal neighborhood, but that's scarcely how it appears today.

- The second type of firms are the "strivers" who have come up from regional cities like Atlanta, Boston, Chicago, Los Angeles, Pittsburgh, San Francisco, and so forth, who have followed a well-trodden path to "end up on the right side of history."

So what **does** it take to be one of the leading firms today? Whatever other commendable features they must have, the winners all have had:

- A dominant position in their home market (they need not be #1, but they must be top of mind in that market)
- A great Washington, DC office (Washington is important not so much in terms of the size of your office as that it

must comprise a strategically sound fit with the regulatory and governmental needs of your client base: And economically, if Washington is not precisely countercyclical it is surely “evergreen” in the sense that the government’s schedule of initiatives bears no relationship to peaks and troughs in the economy)

- A great office in a financial capital (domestically, this means New York)
- Critical mass in California
- And strategic combinations offshore.

Going forward, firms must add in these ingredients:

- London, and eventually key markets on the Continent of Europe;
- And China (which has historically meant Hong Kong and will now mean Shanghai and Beijing as well)

If you’re not in a silver spoon firm, or a successful striver firm, is there still time to join the ranks of the emerging elite?

“If there’s any time left, there’s not much.” The critical obstacle is cracking the New York market, which is “by far the hardest in the world.” Some formerly-from-California firms (we mention Latham and Orrick, and he nods vigorously) have pulled it off, but for those that haven’t yet cracked Manhattan; they’ll be paying “predatory” prices to attract substantial talent. Elaborating on this, Pete says establishing an office with critical mass in Manhattan today, from a standing start, involves “house to house combat.” Not that it’s impossible, but it’s far far more vexing and expensive than it was even a decade ago.

We’re by no means fully evolved as an industry. We have little looking over the horizon capability. We only saw private equity coming when deal flow from traditional M&A clients dried up, and we asked, Where did the deal flow go?

Why, then, do firms keep trying? Simply stated, to align your firm with your clients, how can you **not** be formidable in New York?

Managing 21st Century Firms

We’re by no means fully evolved as an industry, he observes. For example, we have little “looking over the horizon” capability. We ask about today’s practice specialty prom queen, private equity, and he admits that they only saw it coming in a back-handed way, when deal flow from their traditional M&A clients — strategic buyers looking to acquire firms for horizontal or vertical expansion rather than for financial re-engineering — dried up, and they had to ask, “Where did the deal flow go?”

In K&L/Gates’ defense, they were scarcely alone in failing to foresee the explosive growth of private equity in the first half of this decade, which we personally attribute to the catalytic mixture of the Sarbanes-Oxley “public company excise tax,” with unprecedented scrutiny of borderline GAAP interpretations, and the tsunami of global liquidity. As Pete joked, “if you think having a hair-trigger hedge fund manager looking over your shoulder is bad, would you rather it be the US Attorney?”

We note that K&L Gates has accomplished mergers with these firms (and others), and ask Pete what were the promise, and the most challenging aspect, of each:

- Nicholson Graham
London
- Preston Gates Seattle,
Asia, and other venues
- Hill Christopher
Washington
- Warner & Stackpole
Boston

Wryly, he notes that those have only been the publicly announced and successfully consummated mergers, and says that the firm is always willing to discuss a combination that might make strategic sense, but that “it’s very very hard to get to the finish line” in merging law firms. We ask if the cancellation of the Dewey-Orrick and Bryan Cave-Squire Sanders means that mergers are riskier than we assume, and he responds that “risky” probably isn’t exactly the right word, but that assuring firm buy-in by the partnerships beforehand is indispensable. Without stating it, his opinion clearly is that working out the ramifications of a proposed merger of two complex and storied firms populated by head-strong people is not an exercise prudently to be conducted in public.

What makes for a successful tenure as managing partner?

You have to realize that “there are such smart people in these firms,” people deeply versed in everything from history and literature to current affairs: This is a resource that one must tap. Look for insights from a wide array of people — “mining the wisdom of your partners” might be the slogan — and combine that with analysis of what’s going on in the world (e.g., the private equity boom), and meld them into a strategically coherent strategy.

Thus, being an integral participant — and instigator — of the interior dialogues going on in the firm is the bare minimum for a managing partner, the price of admission.

In the press release announcing formal approval of the Kirkpatrick & Lockhart/Preston-Gates merger, which went out under Pete's signature, one phrase struck us as out of place — out of place in the sense that one virtually never hears such things, so we ask him about it. The phrase is that a core value of the new firm is to advance "reasoned discourse and articulate communication."

Needing no more prompting, Pete erupts: "There is nothing that transforms a decision-making process more into vitriol than *ad hominem* arguments or, perhaps even worse, **silence**—which is passive-aggressive." By contrast, having candid, open conversations, and being prepared to actually change one's mind, is an act of strength, not an act of capitulation.

The War for Talent

Applying this to the topic of mergers means having an open dialog about what can be done to unlock the synergies that the combination presents, while simultaneously recognizing that no synergy will be achieved without true integration, which he calls "absolutely key."

Intriguingly, he notes that there's inherent tension between "consumption" and "investment" in running a firm. At K&L/Gates, they view professional development and excellence as a "destination for investment." This sounds like motherhood and apple pie, until you run into a coterie of people who are more accustomed to immediate consumption, which is antithetical to K&L/Gates' preference for investment in the brand positioning, and "the platform," which "work for you while you're sleeping." If communicating the

preference for investment to your partners is indispensable, it's a *fortiori* the case with potential merger partners and potential lateral recruits.

On the subject of lateral recruits, we note that there's a school of thought that laterals "capture" much or all of the present discounted value of their contribution to profits, leaving little if any left over for the firm — a phenomenon that has been widely studied in the context of professional athletes and celebrity entertainers — and ask Pete for his views on this. Essentially, he believes that some firms have a "comparative advantage" in lateral recruitment, particularly those that can offer laterals a superior "platform" for their practice, and cites as a somewhat generic example a partner with a \$1.5-million book of business who, by coming to a K&L/Gates, could grow that revenue to \$5-million within a few years by being able to offer his clients (again, hypothetically) additional venues, M&A expertise, project finance capability, a more sophisticated corporate governance/compliance structure, etc.

The one non-negotiable principle to keep in mind when dealing with talent is this: The institution should not impose any ceiling on partners' success: You cannot put limits on what the best people can achieve.

This prompts us to read Pete the following quote and ask for his reaction:

"The competitiveness of any place in the world, including a place called the United States, depends less and less on the profitability of companies headquartered in that location, and more and more on the capacity of the people that live there to add value to this increasingly integrated global economy."—*Robert Reich*, Dec. 2006

His reaction is immediate, and terse: "*Indisputable.*"

The US/UK Divide (and the Hegemony of Anglo-Saxon Common Law)

We observe that it's fair to say that US firms have fared better invading the UK than vice versa, and ask Pete why he thinks that is.

First, the US firms with articulated platforms in the US offer UK merger partners access to the largest legal market in the world. Second, such US firms have long and deep client lists composed of US-based global corporations that are investing in and through London, and these firms offer more inbound work to UK firms than vice versa. And third, and most intriguingly, he believes that UK firms with the reach to come over here "have ignored the last decade of history." By that he means that they have aspired to merge with the *crème de la crème* of US firms, ignoring that:

- US firms of that caliber (Cleary Gottlieb, Cravath, Davis Polk, et al.) have no reason whatsoever to dilute their brands, and every reason to preserve their supra-normal profitability; and
- Now that many "strivers" have succeeded in the past decade, it's likely that the US firm would end up being the "senior partner" in the merger; the UK firms might like to merge in principle, but they won't want to relinquish their sovereignty.

Spontaneously, the conversation turns to the global dominance of firms with roots in the former British Empire. Almost shockingly, of the "Global 100" firms (the top 100 by revenue, jointly compiled by the UK's "The Lawyer" and the US's "The American Lawyer," 98 of the 100 have British Empire roots: In the US (75), the UK (17), Australia (5), or Canada (1), leaving one in France (#77) and one in the Netherlands (#99).

Pete attributes this (as do we) to two powerful barriers to entry favoring Anglo-American firms:

- The *lingua franca* of business being English; and

- The infinite extensibility of the common law tradition. (Imagine trying to write the indenture for a collateralized debt obligation [CDO] under the Napoleonic code—it simply could not be done.)

On the Manageability of Law Firms

Professional service firms in general, and high-powered global law firms in particular, are notorious graveyards for well-intentioned management initiatives and managers in general. But clearly Pete has found K&L/Gates receptive and welcoming of his leadership. Has his experience been different than the conventional wisdom that high-achieving lawyers are autonomy-seeking missiles, dismissive of efforts to channel their efforts, antithetical to team playing, and generally allergic to top-down direction?

He responds energetically that in his experience it's utter myth that lawyers aren't team players. Warmly, he recounts that he has probably never experienced such an intense exercise in teamwork as getting the *Yale Law Journal* out (giving the lie to the notion that only MBA students, not JD students, collaborate and work in teams).

More subtly, he points up an analogy between a global law firm and a University, or even a complex socioeconomic organism such as New York City. How are they similar? In all three, human beings spontaneously self-organize into smaller and larger groups connected by common interests, goals, or simple propinquity. People, Pete insists, *like to work together*, and they will, left to their own devices, form communities: The structured finance group, the biology faculty, the garment district, Kappa Kappa Gamma.

Athenian Democracy, or Parris Island?

An essential theme in the early years of the 21st Century seems to me to be the tension in our industry between the Quaker

Meeting style of management which was the order of the day 20 and 30 years ago, and the increasing pressure to move towards a corporate, hierarchical, executive management style as law firms scale into serious multinational enterprises. So we ask: On a scale of 0—100, where 0 equals full-bore total-consensus Athenian democracy, and 100 equals Parris Island boot camp command-and-control, where should an aspiring, competitive global law firm fall? He responds immediately, "80," then seems to rethink it, and concludes that the real question is different: "What you really need is to make good decisions that translate positively in to the lives of your major stakeholders. This is more important than a nominalist exercise focusing on your form of governance."

But, we insist, is the "corporatization" of the law firm inevitable?

Yes, Pete agrees; he repeats that his generation may be the last not to be purposely groomed for leadership, possibly even selected and recruited for the position of chair.

Fairfield, Connecticut, anyone?

And Why This Matters

Spending time with Pete focuses and integrates one's thoughts on the changes with which globalization is assaulting our industry, and the changes we're spontaneously initiating to become ever more competitive, and to match our clients' geographic footprints and the complex demands of their increasingly sophisticated, "real time" businesses.

At the start of Pete's career, businesses were:

- Local or regional
- In one, readily understandable line of business
- With predictable relationships (typically of long-standing) with clients, suppliers, and labor

- Subject to regulations which changed glacially if at all.

Today, businesses are:

- Global, operating in real time 24/7
- Opportunistically acquiring and shedding, expanding and contracting, lines of business as marketplace demand shifts (often in unforeseeable and discontinuous jumps)
- Tightly integrated to their suppliers and labor, albeit with loyalty cycles re-measured quarterly
- Facing complex multi-jurisdictional regulations which can conflict and contradict each other (just for example—records retention requirements under electronic data discovery standards in the US vs. privacy requirements in the EU).

Law firms which don't evolve as rapidly as our clients will lose the "Global 100" race. Pete is determined that K&L/Gates will excel.

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