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THE BURSTING OF THE PEDIGREE BUBBLE

BY WILLIAM D. HENDERSON

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One of the advantages of going to an elite law school is the presumption that you are a very smart and able lawyer. If you made law review, graduated Order of the Coif, or clerked for a federal judge, the presumption grows stronger.

Most large law firms are very sensitive to pedigree, though you would be hard pressed to find any hard empirical evidence why the kid who went to Harvard is a better bet than someone who went to, say, Boston College, Illinois, or the University of Houston. Although the performance benefits of

elite pedigree are little more than a hunch, the entire market for corporate legal services has bought into the notion that better résumés equal a better firm. As the demand for corporate legal services continued to grow over the last several years, this herd-like branding strategy produced the \$160,000+ associate pay structure and the now famous “bi-modal” salary distribution.¹

Yet, as the economy has slipped into recession, the pedigree bubble has finally burst. It is now painfully obvious to everyone that it does not matter where you went to school, or who you clerked for – a lawyer in his or her first or second year of practice is just not worth \$275 per hour.² A few star lawyers, or a handful of marquee firms, may be able to levy these rates for junior lawyers as part of a bundled package of

>>> PAGE 12

PAGE 4

“LAW IS AWESOME!” — A REPORT ON A DIVERSITY PIPELINE PROGRAM'S FIRST YEAR



services. But the vast majority of large law firm partners are experiencing overwhelming downward pressure of fees. Because of high overhead added during the boom years, many firms are in the unprecedented position of slashing associate salaries to generate a large enough profit pie to keep key rainmakers in the firm. As a result, elite credentials are now in the process of getting repriced.

To get a better handle on how this repricing process is likely to play out, it is worth examining the economic and historical factors that made elite law school credentials such a potent market signal.

Here, the story can be traced to the phenomenal success of the “Cravath system,” which was an ingenious lawyer recruitment and development model devised by Paul Cravath in the early 20th century. The primary breakthrough of the Cravath system was the creation of an incentive structure that could develop and deploy a large group of well-trained lawyers for the benefit of large and rapidly growing corporate enterprises (e.g., banks, railroads, steel companies). During the 1930s, a journalist for *Harper’s Magazine* visited the Cravath firm and famously dubbed it a “law factory.” Yet, the combination of quality, technical experience, efficiency, and scale of the Cravath firm was truly remarkable.

One of the fundamental misconceptions of the Cravath system is that the firm hired the best lawyers. In reality, the Cravath system created them. Junior lawyers spent years in apprenticeship rotations that immersed them in the details of every aspect of corporate law practice. According to Cravath, the purpose of this lengthy, expensive, labor-intensive process was to create “a better lawyer faster.” Moreover, advancement to the highest levels of the firm required not only superior legal work but also the ability to manage, supervise, and delegate legal work to junior lawyers, attributes “requiring the nicety of balance which many men with fine minds and excellent judgment are unable to attain.”

For reasons of morale and quality control, the Cravath system required very low attrition and virtually no lateral recruitment of lawyers. What bound the lawyers to the firm were the substantial profits of partnership (for the lucky few who made it) and the outstanding training and work experience that created numerous employment opportunities for everyone else. In essence, the impeccable quality and value generated by the Cravath system created a brand. And brands, of course, are very powerful because they reduce uncertainty and search costs upon which clients and prospective lawyers come to rely. Hence, the brand commands a premium in the form of higher rates (for clients) and longer hours (for associates). Not surprisingly, the Cravath system was widely emulated by firms in New York and other large industrial cities.

One of the hallmarks of the Cravath system was the recruitment of law school graduates from a handful of Ivy League schools. And herein lies the source of a lot of misconceptions. As of 1948, when Robert Swaine published the firm’s three-volume history, the Cravath firm had hired 67.7% of all its lawyers from Harvard, Yale, and Columbia. (As noted in the firm history, Cravath gradually expanded its hiring to include other so-called national law schools, such as Michigan, Virginia, and the University of Chicago.) Yet, this selection criterion had a clear business purpose. During the first half of the 20th century, very few law schools required an undergraduate education, and Cravath observed that a sound liberal arts education was an essential ingredient for developing a disciplined legal mind.

Similarly, Cravath’s emphasis on law school grades also had a specific business purpose. During the early 20th century, the primary barrier to admission to an Ivy League law school (besides race, religion, or gender) was money and the ability to stay out of the workforce for three years. Indeed, the Ivy League has always been exclusive, but the basis for the exclusivity has gradually changed. In 1948, when the LSAT was administered nationwide for the first time

(to over 25,000 law school applicants), between 20% and 50% of first-year classes at “elite” institutions, such as Harvard, Berkeley, the University of Michigan, and the University of Pennsylvania, scored below the 50th percentile. In other words, under the admission standards of today, a good portion of these students would have a hard time being admitted to any ABA-accredited law school. Thus, Cravath’s emphasis on grades was, in effect, a rough screen for legal aptitude. At a talk given at Harvard Law School, Cravath explicitly told students that a successful corporate lawyer must possess “the fundamental qualities of good health, ordinary honesty, a sound education and normal intelligence ... character, industry and intellectual thoroughness. ... Brilliant intellectual powers are not essential.”

For decades, corporate law firms throughout the nation adopted some variant of the Cravath system and successfully established their own “white shoe” brand. Indeed, many Midwestern men traveled to the Ivy League for their law degree only to return to Chicago, Detroit, Cleveland, or St. Louis to join the establishment corporate bar – assuming the candidates attained the requisite law review credentials and were white, male, and Protestant.

As the years passed, legal education underwent a dramatic transformation: requiring undergraduate degrees, screening candidates based on the LSAT, and offering subsidized, full-time education through dozens of public law schools. Although these changes undercut the original business purpose of Cravath’s selective hiring model, the rarified educational credentials of the typical large corporate law firm had nonetheless become an integral part of the firm’s brand (and, perhaps, a source of ego gratification for partners). By changing nothing, large law firm partners were virtually guaranteed comfortable profit margins and social prestige. Thus, for several decades ending with the recession of 2009, many of the nation’s largest and most prestigious firms operated on auto-pilot, at least in terms of lawyer recruitment and development.

IT TURNS OUT THAT AS A GROUP, ELITE LAW SCHOOL GRADUATES TEND TO BE MUCH LESS SATISFIED WORKING IN LARGE LAW FIRMS THAN THEIR REGIONAL LAW SCHOOL COUNTERPARTS.

To illustrate how this strategy affected the entry-level market, consider the hiring statistics from the 2005-2007 economic boom. During this time period, the nation's largest 250 firms increased their hiring from 5,600 to 7,200 new associates. Because the Top 20 schools as ranked in *U.S. News* produce only 6,500 lawyers per year, the laws of supply and demand were finally in severe tension. Remarkably, 54% of the *additional* 1,600 jobs went to graduates of Top 20 schools, many of whom had lackluster grades or little long-term interest in corporate law. But for \$160,000 per year, why not give it a go – at least until they law school loans are paid off!

On paper, anyway, most large firms maintained the pedigree of their workforce. But by hiring so many young lawyers with no long-term interest in corporate law, attrition rates increased substantially. In turn, this fueled clients' skepticism on the business rationale for paying such high rates for associates. Similarly, senior partners became disillusioned with the perceived lax work ethic of Gen Y lawyers.

The *After the JD* project (AJD), a major longitudinal study of over 4,000 law school graduates who passed the bar in 2000, provides valuable insight on the preferences of young lawyers. It turns out that as a group, elite law school graduates tend to be much less satisfied working in large law firms than their regional law school counterparts. Because law school eliteness (based on *U.S. News* rankings) is strongly correlated with the socio-economic background of student bodies – e.g., the median Harvard student comes from a better educated, more affluent family than the median Hofstra student – AJD researchers have suggested that these group differences may be

traceable to different perceptions of what it means to be upwardly mobile. For a first-generation professional, a job with a major New York law firm is quite a coup. But for a third generation professional, it is just a job with very long hours and little personal autonomy. Not surprisingly, as a group, elite law school graduates in the AJD sample have left large firm practice at higher rates than their regional counterparts, typically taking in-house jobs in government or business.

So imagine two potential candidates, one from a solid regional law school who actually wants to build a career at the firm and another with a degree from a national law school who evinces an attitude of either slight detachment or entitlement. Why did so many large firms favor – indeed, pay a premium for – the elite law school graduates? A managing partner once explained to me the logic of the elite school heuristic: “If I hired a lawyer from Harvard and he doesn't work out, it's his fault. But when a candidate from a regional school washes out, it's my fault.” This “pure smarts” theory may be a great way to keep from getting second-guessed by your partners, but it contains none of the elegant business logic of the original Cravath system.

Indeed, the proponents of the pure smarts theory would make a lot better hiring decisions if they consulted the literature on cognitive and industrial psychology. Although intelligence (or its component, verbal reasoning ability, which is measured by the LSAT) is correlated with job performance across the economy as a whole, predictive models have virtually no explanatory power when the sample is limited to workers who all have above-average cognitive ability (e.g., law students). As noted by Malcolm

Gladwell in his recent book, *Outliers*, “The relationship between success and IQ works only up to a point. Once someone has reached an IQ of somewhere around 120, having additional IQ points doesn't seem to translate into any measurable-real world advantage.” Even the “IQ fundamentalist,” Professor Arthur Jensen, acknowledges that toward the upper part of the scale, differences in IQ “are generally of lesser importance for success in the popular sense than are certain traits of personality and character.”

These findings are corroborated by a recent study by UC Berkeley professors Majorie Shultz and Sheldon Zedeck. Drawing upon the techniques of industrial psychology, Shultz and Zedeck identified 26 discrete competencies that form the basis for successful lawyering. In turn, using carefully devised questions, peers and supervisors were asked to evaluate the skills of approximately 2,000 law students and alumni of UC Berkeley and UC Hastings. Remarkably, LSAT scores, undergraduate GPA, and first-year law school grades were correlated at statistically significant levels with between zero and six of the 26 success factors, depending upon the subgroup. The strongest correlations (albeit still relatively weak) were to constructs associated with the traditional law school curriculum, such as writing, researching law, and analysis and reasoning. Conversely, within the student sample, seemingly better academic credentials were negatively associated with other success factors, such as networking, building relationships, practical judgment, ability to see the world through the eyes of others, and/or commitment to community service.

>>> PAGE 14

Although traditional academic measures of ability had limited predictive power, the Berkeley researchers found that a variety of other psychometric tests were positively correlated (at statistically significant levels) with one or more of the remaining 20 success factors. Yet, these tests focused on personality attributes, biographical information, situational judgment, and a candidate's values, preferences, and drive.³

To my mind, the market has paid a premium for elite academic credentials because elite large firm partners, corporate general counsel, and, frankly, law professors, who all typically possess these attributes, want to believe that they are valid measures of innate ability and potential. In other words, big lawyerly egos clouded good lawyerly judgment. Now, downward pressures on legal budgets and shrinking law firm profit margins have pressed a sharp pin into the credentials bubble. Clients need more than shiny résumés to allocate their legal spending – they need hard evidence that any price premium can be counted on to deliver actual value. As firms retool their business models, they should consider the original Cravath system, which invested in young lawyers to create an organization capable of exceptional client service. This type of value proposition is how you build and maintain a franchise. ■

ENDNOTES

1 See <http://www.nalp.org/anotherpicture> for an example of the bimodal curve for the Class of 2007.

2 According to data from the Law Firms Working Group, \$275 is roughly the prevailing rate for first and second year associates among large firms in major markets.

3 The full study, Marjorie M. Shultz & Sheldon Zedeck, "Identification, Development, and Validation of Predictors for Successful Lawyering" (Final Report to LSAC, Sept. 2008) is available online at www.law.berkeley.edu/files/LSACREPORTfinal-12.pdf.