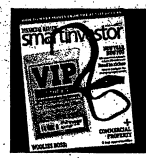

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Lawyers float a multibillion-dollar idea

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Legal editor

Partners at major law firms are sitting on billions of dollars of wealth that could be unlocked if they followed the lead of Slater & Gordon and floated their businesses.

According to an analysis by *The Australian Financial Review*, if valued similarly to Slater & Gordon, each of Australia's top law firms could be worth up to $2 billion.

This week, Blake Dawson Waldron, Freehills and Mallesons Stephen Jaques all indicated they were considering ditching their traditional partnership structure and incorporating – a prerequisite to listing.

While the major law firms have indicated they do not intend to float,

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the potential for a large windfall from listing on the ASX is likely to focus partners' minds on the prospect.

A number of firms have been approached by Sydney investment bank Beerworth + Partners about the possibility of a listing, but this approach was rejected.

A major motivation for incorporation is the ability to offer lawyers, particularly younger ones, equity in the firm apart from through traditional partnerships.

"The partnership model is very unsophisticated," Blake managing partner John Atkin told the *AFR* Legal Reform Summit this week.

"You have to pay the profits every year for tax reasons, which doesn't encourage long-term investment or thinking – but that could be possible with a different structure.

"Where else do you find organisations which run a business as large as ours which are unincorporated other than where there is a regulatory reason for doing so? The answer is none."

Freehills indicated it was preparing to incorporate as early as next year, while Mallesons said it was an option although there were tax hurdles at present that prevented it occurring.

Slater & Gordon will make Australian legal history on Monday by becoming the first law firm to list after a successful capital raising in which 20 million of the 35 million shares on offer were locked up by 40 institutional investors before the float even opened.

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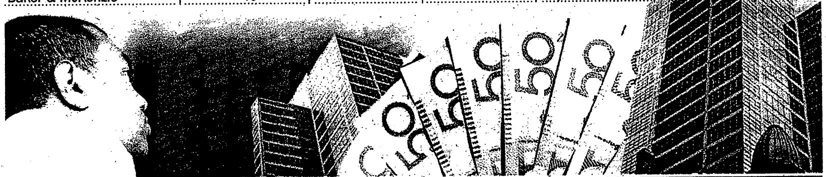
Estimated values of large Australian law firms if they floated

Firm	Number of equity partners	Estimated profit*	Estimated profit margin*	Estimated market value* ($bn)
Freehills	209	195.3	42%	2.65
Clayton Utz	207	176.0	45%	2.38
Mallesons Stephen Jaques	175	173.0	38%	2.35
Minter Ellison	217	151.7	37%	2.03
Allens Arthur Robinson	184	148.0	40%	1.99
Blake Dawson Waldron	156	109.8	36%	1.47
Corrs Chambers Westgarth	113	92.4	44%	1.24
Phillips Fox	107	68.0	32%	0.90
Deacons	90	65.0	33%	0.87
Baker & McKenzie	40	41.8	31%	0.56



*Assuming a P/E of 14, a base partner salary of $400,000 and no retained earnings

Source: *AFR Partner Profit Survey (2006)*

On the basis of the offer price for the shares, the firm's market capitalisation will be $107 million and it will trade on a price-earnings multiple of 9.8.

But the market value of big firms like Mallesons Stephen Jaques, Allens Arthur Robinson and Freehills could be much higher because, at the time of valuing Slater & Gordon, the firm's advisers had little on which to base their valuation because there are no other listed law firms.

Based on the number of partners at the 10 major law firms, the average value of equity per partner is $10 million, although senior partners would be likely to receive significantly more than junior partners.

The analysis is based on per-partner profits for the 2005-06 financial year. Per-partner profit is expected to be even higher this year, with a number of firms enjoying double-digit revenue growth in the merger and takeover mania.

Much would depend on what existing partners were paid as employed solicitors in a corporate structure and whether the law company retained earnings to fund future growth.

In the case of Slater & Gordon, the firm's seven principals are paid $225,000 to $375,000 a year. Yesterday, a managing partner of one of the 10 large law firms said existing partners would need to be paid a base salary around $500,000 in order to retain them.

One senior Sydney investment banker said the price-to-earnings multiple for the big corporate firms could well be 14 to 15 times, given their practices and size. "It is hard to determine a value – Slaters will set a benchmark," the banker said.

"But they have a very different revenue stream from a larger firm, which would be more like a merchant bank and I would think they would have a mid-teen P/E."

Bill Beerworth of Beerworth + Partners said that when he had approached a number of major law firms about the possibility of floating, there had been resistance to the idea because of the public reporting requirements of a publicly listed company. But he said he expected this resistance would change.

Part of the attraction to listing was that it would unlock partners' equity which is now encumbered by bank debt. "Once a major law firm in Australia lists, it is almost inevitable that a number of other major law firms will quickly follow," Mr Beerworth, a former Mallesons partner, said.

"Once law firm partners understand that floating will rediscover the hidden equity they have in firms, in my view it will happen because partners will become quite wealthy and they will have equity in shares, in options that they can cash at the end of their time as partner. Currently, they start with nothing and leave with nothing but their superannuation.

"The major law firms are also losing talent to major banks like Macquarie and UBS, which can offer them equity, but if they float, they can offer their young turks a huge bundle of shares."

Part of the problem in valuing Australian law firms is that they have very few tangible assets and there is little with which to compare the value of providing legal advice.