THE INTERNATIONAL DIVERSIFICATION OF PROFESSIONAL SERVICE FIRMS:

THE CASE OF U.S. LAW FIRMS

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This is dedicated to my wife and my parents.
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FIRMS: THE CASE OF U.S. LAW FIRMS

PATRICK H. GAUGHAN

ABSTRACT
The globalization of markets has necessitated increased demands on law firms to serve
the international needs of their clients. However, it is unclear how law firms have met
these needs. Although the internationalization process of U.S. law firms has been the
subject of some limited academic discussion, the overwhelming focus has been on only
the largest law firms. There is a noticeable absence of empirical analysis that defines, let
alone includes, the broader population of U.S. law firms who maintain international
operations. Moreover, the existing literature has not proposed any parsimonious
international diversification models that are easily applied to the entire population of U.S.
law firms. This includes consideration of Reputational Capital as a firm resource
impacting law firm internationalization. This dissertation helps fill the gap. The
descriptive statistics are based upon a census of internationally diversified U.S. law firms
at four points in time. Additionally, the quantitative research is based upon a panel study
consisting of virtually all U.S. law firms that maintained at least one attorney outside the
U.S. across all of the years 1998, 2003, 2008 and 2013. This ultimately resulted in a
panel study consisting of four observations on each of fifty-five (55) U.S. law firms (for a
total of 220 observations). The results revealed that, as related to International
Diversification, the interaction of Human Capital and Reputational Capital was negative
and statistically significant. This suggests that U.S. law firm internationalization may be
different than has been assumed in the previous literature.
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CHAPTER I

INTRODUCTION

Markets around the world are increasingly interconnected. In recent decades, barriers to trade have been drastically reduced. Communication technologies have improved. Global transportation has become less expensive and more efficient. Today, customers and suppliers are commonly distributed across national boundaries. Businesses routinely face cross-border opportunities and threats. All along the way, law firms have played an increasingly important role.

Increased international labor mobility has impacted immigration law. Increased global shipping has impacted maritime law. The Internet has raised numerous international legal and business issues related to privacy, fraud, and decency. Global supply chains have introduced an international dimension to consumer safety, labor standards, environmental protection, and tort liability. All the while, the international recognition and enforcement of intellectual property rights has continued to provide both opportunities and fertile ground for international legal conflict. Today, international business is as much defined, as informed, by the advice of legal counsel. However, what is not known is the extent to which the globalization of markets has translated into the globalization of legal services.
Undoubtedly, there has been an increase in the use of treaties and other types of international law between countries to facilitate international trade (such as through creation of the World Trade Organization). However, the vast majority of international business transactions - the type driving the international expansion of U.S. law firms - is focused on the private practice of law across national boundaries. The foundations of law in international business remain local.

As might be expected, the international practice of law of any type adds complexity and challenges to more than just the immediate commercial interests and law firms. Host governments and their citizens encounter challenges as well. Each country has its own expectations regarding the duties and obligations of all lawyers practicing locally. Each country has its own unique history, traditions, culture, government, and institutions.

As such, although business transactions are quickly converging toward regional and/or global standards, the international expansion of legal services faces a much more complex environment. Law firms face a “rip tide” of increasing domestic and international pressures while still firmly mired in diverse local restrictions and customs. Within this context, the challenge is to gain a better understanding of the deployment of U.S. law firm resources and their growth in international operations. It is submitted that the following research furthers this goal. In particular, the research focuses on the interaction of U.S. law firm Human Capital, Reputational Capital, Leverage, and Service Diversification in the determination of International Diversification.
Statement of the Problem (The Research Gap)

As shown on the chart below, there is a clear correlation between the growth in global trade and the increase in the export of U.S. legal services. One might reasonably expect that there would be a similar relationship between the growth of global trade and the international expansion of law firm operations – international diversification. After all, inherent in the growth of international business is the predictable increased need for international lawyers. International diversification should follow. But does it?

What we do know is that law firms are for-profit businesses. As with any other for-profit entity, law firms would be expected to pursue strategies to maximize firm

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1 The relationship appears to be approximately a $1 million dollar increase in the export of U.S. legal services for each $2 billion dollar increase in world merchandise exports.

profits. This would occur within the context of servicing the international needs of their firm clients. However, the international provision of client services can be accomplished in various ways – many of which do not require the permanent location of attorneys abroad. This raises some questions regarding the specific strategies being utilized by U.S. law firms to serve the international needs of their clients.

For instance, should the U.S. law firm refer their clients to external market providers (foreign law firms), or should the firm use its internal resources to fulfill client needs? (Coase, 1937). If the firm is going to utilize external providers, should the firm invest in developing a formal network? (Vahlne & Johanson, 2013). If the firm is going to use any of its own internal resources, how far should the firm commitment go? At the same time, what configuration of internal firm resources will enable the firm to serve international needs while also improving firm performance? (Penrose, 1959). What if international diversification is not consistent with maximizing firm performance? What types of internal organizational politics might be encountered in making these types of firm resource allocations? (Simon, 1959). What about the risk of losing the client to another law firm?

Conceivably, firm strategies could be limited to simply requiring all foreign clients to visit the law firm at their U.S. office(s). Or, the firm could simply use email and teleconferencing to service clients while they remain in a foreign country. Alternatively, the firm could send their attorneys abroad on a temporary, as-needed, basis. Lastly, the firm could take the step of setting up an office abroad – international diversification - that is permanently staffed by firm attorneys. See generally, General Agreement on Trade in Services, Apr. 15, 1994 [“GATS”].
Of those firms that decide to permanently staff firm attorneys abroad, what factors will weigh most heavily on how the firm decides who, and how many, attorneys to deploy abroad? Will the attorneys that are stationed abroad be expatriates from the firm’s home country or will they be locally hired into the foreign office? Will the foreign office offer legal services related to host country (foreign law) or be limited to the firm’s domestic (U.S.) legal services? Beyond the needs of the foreign office, what about the potential adverse impact on the firm’s domestic offices? How will the home office continue to operate if some of its key human resources are no longer readily available? These last considerations underpin the focus of the current research.

As the quintessential professional service firm, the most valuable resource of any law firm is its store of Human Capital. The Human Capital of the entire firm is one variable of interest in examining the International Diversification of U.S. law firms. Even if the firm hires foreign attorneys to staff the foreign office, the firm still has to integrate, manage and coordinate the foreign and domestic operations. Inevitably, the referral of clients to foreign offices will still require significant monitoring and input from the firm’s domestic attorneys. Often, it will require remote monitoring and management. In the least, someone will occasionally get on a plane. In all cases, the existence and deployment of Human Capital will underlie the provision of services and allocation of firm resources to foreign offices.

Given the difficulty in evaluating the actual quality of legal services, another consideration for the firm is its Reputational Capital. Clearly, if there is international brand recognition regarding the firms’ quality of legal services, it would be expected that the law firm would be able to more easily expand. An international reputation alone
should increase the competitive appeal of the firm to some clients. At the same time, the
greater the firm’s Reputational Capital, the greater the downside risk. Any shift in
reputation toward an international presence may be perceived negatively by the firm’s
domestic clients – especially if the domestic practice does not primarily involve
international issues.

Another firm consideration closely related to Human Capital is the extent to
which the U.S. law firm relies upon Leverage. Leverage is the relationship between the
number of firm lawyers who are owners or partners versus the number of firm lawyers
who are non-owners/non-partners. The concept of Leverage used to be represented by
the “partner-to-associate” ratio. The concept remains the same. However, in recent years,
the explosion of new titles has made the specific names less obvious. “Partners” can now
include titles like “members”, “shareholders”, “equity partners”, “senior partners”, or just
“partners. “Associates” can now include titles like “associates”, “staff attorneys”, “senior
associates”, “attorney”, etc. What is important is that Leverage has an impact on both the
profitability of the firm (to the owners) as well as the quality of the services provided to
the client. The two goals of profitability and quality in the use of Leverage do not always
align. This is made even more challenging when international operations are introduced
and there are interactions with other core firm resources – like Human Capital.

Lastly, another closely related variable to both Human Capital and Leverage is the
diversity of service offerings by the firm. Service Diversification can be extremely
narrow – as in a boutique firm practicing only patent law – or extremely broad – in full-
service firms. The extent of Service Diversification has an impact on the amount and
type of Human Capital necessary to provide the intended level of service quality.
Broader service diversification requires a broader array of legal skills – and presents even more internationalization challenges.

Of course, in the end, there are lots of additional variables that could have been tested. However, problems with data availability dictate use of a parsimonious model. Data quickly becomes a problem when – as here - the scope of the sample approaches the entire population of relevant firms. As such, the current research is limited to a model that focuses on the interaction of Human Capital, Reputational Capital, Leverage, and Service Diversification as they relate to the International Diversification of U.S. law firms.

Although there have been some longitudinal studies on the international diversification of the largest U.S. firms, the time periods have been relatively short – usually covering less than five years. Additionally, most have only examined data from before the year 2000. In fact, the only identified study that even attempted to examine the entire population of U.S. law firms with international operations was done over forty years ago and was based upon data from 1967. (Gaedeke, 1973). In the meantime, quite a bit has changed.

As such, the broader context of law firm International Diversification is largely unknown. There simply is no empirical research on the International Diversification of the complete population of U.S. law firms. What exists is either anecdotal or limited to the fifty or one hundred largest U.S. law firms. Practically speaking, these firms may be the most important - or maybe not. Without knowing the broader context, we simply do not know.
Of course, exhaustively delineating absolutely all aspects of the international diversification of U.S. law firms is beyond the scope of the current endeavor. The current effort focuses on the interaction of those firm-level characteristics that should have the greatest impact on the international diversification behavior of U.S. law firms. These characteristics are the interactions between the firm’s Human Capital, Reputational Capital, Leverage, and Service Diversification.

Purpose Statement

Focusing only upon U.S. law firms that maintained international operations across the years 1998, 2003, 2008 and 2013, the primary purpose of this study was to analyze the relationship between existing law firm resources and the extent of U.S. law firm international diversification. Another purpose of this study was to describe the entire population – and changes in the population – of U.S. law firms that maintained international operations in 1998, 2003, 2008 and 2013.

Research Questions / Hypotheses

1. What is a description of the population of U.S. law firms that maintained international operations in the years 1998, 2003, 2008 and 2013?
2. What characteristics of the population of U.S. law firm changed over the years?
3. What differences, if any, exist between the international diversification behavior of traditionally examined U.S. law firms (AmLaw 100) and all other U.S. law firms?
4. What relationship exists between the interaction of Human Capital and Reputation, to the International Diversification of U.S. law firms?
5. What relationship exists between the interaction of Human Capital and Leverage, to the International Diversification of U.S. law firms?
6. What relationship exists between the interaction of Human Capital and Service Diversification, to the International Diversification of U.S. law firms?
7. What relationship exists between Leverage and Service Diversification, to the International Diversification of U.S. law firms?

Significance of the Study

This study makes significant contributions to both the scholarly literature and practical understanding of the international diversification of U.S. law firms.

The study contributes to the scholarly literature by extending existing knowledge to the entire population of U.S. law firms that have maintained international operations. The study also highlights possible resource deployment strategies used by U.S. law firms that contradict some of the assumptions in existing literature. The study also introduces Reputational Capital within the U.S. law firm international diversification literature. Lastly, the study provides a parsimonious model for understanding the behavior and resource allocation of U.S. firms with international operations. Methodologically, the study introduces a novel rubric for systematically classifying whether two firm offices are sufficiently similar to be considered “related.”

The study contributes to broader practical knowledge by describing the characteristics of U.S. firms that have maintained sustained international operations. The study also shows how the composition of U.S. firms has changed over time. As such, this study informs both scholars and practitioners of potential future developments in the international diversification behavior of law firms.
Delimitations

- **Time period analyzed**: 1998 – 2013
- **Number of periods analyzed**: 4
- **Selection of Law Firms**: Must have had a listing in the Martindale Hubbell Law Directory and must have had at least one attorney listed in at least one office inside and outside the U.S, in each of the four periods
- **Determination of Related International Law Firms**: Pursuant to a Selection Rubric, See Appendix A.

Definition of Key Terms

Before expounding upon the overall organization of this paper, it is necessary to first clarify the meaning of certain terms that often have inconsistent or ambiguous meanings:

**Global Law Firm** – For some scholars, a “global law firm” is any law firm that simultaneously maintains a substantial physical presence in Asia, Europe and the U.S. (Beaverstock, Taylor, & Smith, 1999). See also (Faulconbridge, Beaverstock, Muzio, & Taylor, 2007). However, some scholars have taken it further by inquiring into the extent of efforts “to coordinate intra-firm activities… [to] enable a globalizing law firm to develop a consistent approach to cross-border service delivery, such that both clients and professionals experience a seamless process in all countries and offices.” (Segal-Horn & Dean, 2011), p. 196. In this regard, the “global law firm” actually represents an exceptionally small portion of all law firms.

According to the American Lawyer Magazine, of the 100 largest, global, firms by revenue, “77 are American, 13 are British,… five are Australian… and one each from Canada, China, France, Spain and the Netherlands. “ (“The Global 100,” 2013).
Curiously, there is absolutely no effort by the American Lawyer to evaluate the means by which even the Global 100 law firms operate around the world. As such, the “global” firms include firms that primarily export legal services from home offices, those that pursue a multi-domestic strategy, those that pursue a regional strategy and those that are actually seeking to provide a single global standard for their legal services. As used herein, “Global Law Firm” is synonymous with “International Law Firm.”

**Host Country Law** – The foreign, local, municipal, state, regional, and/or federal law governing the country into which a law firm enters, aka, the foreign law. See, e.g., “foreign law” in (Garner, 2009)(“Generally, the law of another country.”).

**Home Country Law** – The domestic, local, municipal, state, regional, and/or federal law governing the country from which a law firm develops or otherwise maintains its home office, aka, the domestic law. See, e.g., “domestic” in (Garner, 2009) (“Of or relating to one’s own country… [or] own jurisdiction”).

**International Diversification** – A firm-level strategy whereby a firm allocates firm resources across national boundaries. International diversification concerns foreign direct investment activity “across country borders into geographic locations (e.g. markets) that are new to the firm.” (Capar & Kotabe, 2003; M. A. Hitt, Hoskisson, & Ireland, 1994).

**International Law** – “The legal system governing the relationships between nations; more modernly, the law of international relations, embracing not only nations but also such participants as international organizations and individuals (such as those to invoke their human rights or commit war crimes). … “ (Garner, 2009). In this regard, “international law” is generally referring to public law between two or more nations. To
avoid confusion, in this document, “international law” will not refer to law governing private legal relations between individual citizens or corporations across national boundaries.

**International Law Firm** – As used throughout this document, “international law firm” is any law firm that maintains at least one domestic and related foreign office staffed with at least one attorney. The determination of whether or not a particular foreign office is “related” is determined by applying a rubric explained in Appendix A. Moreover, the same rubric was applied to law firms utilizing Swiss Verein structures. For more information on Swiss Vereins, see the separate definitional listing below. As used herein, “international law firm” does not include firms whose only involvement with the provision of legal services across national boundaries is limited to: serving foreign nationals who enter the firm’s domestic offices for services; firms who temporarily send attorneys abroad to serve clients located abroad; or firms who only use telecommunication services, such as video conferencing or email, to serve clients located abroad.

**Local Law** – As used herein, “local law” means “[t]he law of a particular jurisdiction, as opposed to the law of a foreign state. – Also termed internal law.” (Garner, 2009). Usually, “local law” will refer to “host country law.” However, in some contexts it could refer to “home country law.”

**National Law** – See local law. See also (G. Morgan & Quack, 2005);(John Flood, 2013).
Practice of Law – Those activities by which a particular jurisdiction requires licensure as a lawyer. According to Black’s Law Dictionary, the “practice of law” is “[t]he professional work of a duly licensed lawyer, encompassing a broad range of services such as conducting cases in court, preparing papers necessary to bring about various transactions from conveying land to effecting corporate mergers, preparing legal opinions on various points of law, drafting wills and other estate-planning documents, and advising clients on legal questions.” (Garner, 2009). See also, 6 Ohio Jurisprudence 3rd (2014), 519-520, Attorneys at Law. The Practice of Law is sometimes defined differently by different jurisdictions.

Swiss Verein – “An association of [independent] member organizations recognized under Swiss law.” (Kalis, 2011). Under this structure, separate law firms decide to operate under a common brand name. Swiss Vereins share an internal referral network and maintain fee sharing agreements between members. However, Swiss Vereins do not constitute a common partnership. There is no liability between members of the verein. See also (Vetula, 2009). Examples of U.S. law firms using the Swiss Verein structure are Baker & McKenzie and Hogan Lovells.

U.S. law - The domestic, local law, for state and/or federal laws within the United States of America.

U.S. law firm – Any firm who self-identified its home office as being located within the U.S. on either the domestic or foreign firm listings within the Martindale Hubbell Law Directory, or, who otherwise evidenced a significant historical connection to the U.S. market. The vast majority of firms self-identified a U.S. home office
(indicated by an “*” next to the location of firm offices located in the Martindale Hubbell Law Directory). However, a handful of other firms - formed by mergers of established U.S. law firms with non-U.S. firms (such as DLA Piper), did not indicate any home offices but were selectively included. Where the firm was formed by such a merger but the surviving firm did NOT indicate any central role for any particular U.S. office, the firm was excluded. (Bierman, 2006; E. S. Cohen, 2002; Warf, 2001).

**Organization of the Paper**

The remaining portion of this paper begins in Chapter II with a comprehensive literature review. Chapter II consists of five sections. First, Chapter II starts with a brief historical overview of the internationalization of U.S. law firms. Second, Chapter II covers the key theories of firm internationalization. Third, Chapter II addresses the distinctive characteristics of services and professional services. Fourth, Chapter II discusses the distinguishing characteristics between different types of professional services. Lastly, the paper examines literature related to the key resources used in the conceptual model. In this last section, the paper specifically examines the literature on International Diversification as well as Human Capital, Reputational Capital, Leverage and Service Diversification.

In Chapter III, this paper presents a conceptual model regarding the internationalization of U.S. law firms. This includes explanation of the proposed constructs, support for use of such constructs, and hypothesis development.
In Chapter IV, the paper discusses the research design, data collection, and variables. This includes a comprehensive explanation of the methods used for data acquisition and extraction and statistical techniques.

In Chapter V, there is a discussion of the census descriptive statistics of U.S. law firms that maintained international operations in 1998, 2003, 2008 and 2013. This is where the previously unknown population characteristics are examined - at four different points in time. Next, there is a discussion of the descriptive statistics of the fifty-five (55) U.S. law firms contained in the panel study.

In Chapter VI, the quantitative results and findings are discussed. This includes reference to possible explanations in light of the descriptive statistics from Chapter V.

Lastly, Chapter VII includes the summary, conclusions, implications and recommendations for further research.
CHAPTER II
LITERATURE REVIEW
The purpose of the literature review is to summarize and discuss research relevant to the current dissertation. (R. R. G. Javalgi, n.d.). It consists of discussing applicable theories and providing a theoretical framework for the study. (R. R. G. Javalgi, n.d.). In the present instance, the literature review consists of five sections:

1. An Historical Perspective on Law Firm International Diversification
2. The Internationalization Theories of the Firm
3. The Distinctive Characteristics of Services (as Opposed to Goods)
4. Distinguishing Between Different Types of Professional Services
5. Key Firm Resources and International Diversification

Each of these will be discussed in order.

International Diversification of Law Firms – An Historical Perspective
The first of the five sections in the literature review examines the international diversification of law firms within the historical context.

As might be expected, the economic growth and emerging globalization ushered in by the end of World War II also prompted a fundamental change in the structure of the
By 1960, the fifty largest U.S. law firms ranged from 50 to 100 attorneys. (Galanter & Palay, 1991), p. 22, See also (Sander & Williams, 1992), p. 391. By the early 1990’s, several U.S. firms “topped the 1,000-lawyer mark, and over 50 firms [had] more than 300 lawyers.” (Sander & Williams, 1992), p. 392. However, generally speaking, there was very little geographic expansion. Most firms still practiced in a single city. (Spar, 1997), p.10. International expansion was rare. (Spar, 1997).

For example, in 1967 the U.S. Census of Business identified 21,139 different U.S. law firms with more than one attorney. (U.S. Department of Commerce Bureau of The Census, 1970), Table 5-1. Of these, only 43 firms maintained international offices. (Gaedeke, 1973), p. 61. That is equivalent to slightly more than 0.2% of all U.S. law firms. Stated otherwise, 99.8% of U.S. law firms did NOT maintain any foreign office.

At about this same time, the former managing director of McKinsey & Company provided an intriguing summary of different internationalization strategies used by different types of U.S. service providers:

Often the [internationalization] strategy is rather obvious. Many advertising agencies, for example, have set up overseas branches to provide service for home client companies that were expanding their overseas operations. This is a simple defensive strategy. Servicing overseas clients is also one of the reasons for the major overseas movement of the accounting profession and the more limited overseas expansion of legal and management consulting firms.
But certainly the strategies of many firms that have moved overseas have not been solely defensive. They internationalized also because they saw an opportunity for profitable expansion. Or they had a dual strategy: to accompany their present clients overseas and to attract new clients. Moreover, the objective can be even the vague desire “to maintain leadership” by becoming international because it is “the thing to do”, the “in” thing. (Bower, 1968), p. 50.

In explaining the origins of the defensive client-following strategy, Bower quoted an unidentified commentator on ad agency internationalization as follows:

Madison Avenue has never forgotten that the D’Arcy agency, which once had the giant Coca-Cola account, lost it to McCann-Erickson in the U.S. after McCann first got its foot in the door abroad. (Bower, 1968), p. 50

To a very real extent, U.S. law firms apparently learned the same lesson.

Even though the basic law firm strategy was defensive, by 1968 a handful of U.S. law firms were nonetheless forced to expand internationally to serve the business needs of their largely U.S.-based clients:

Despite statutory restrictions, [in 1968] large U.S. law firms have some forty overseas offices. These are located principally in Paris, where there are twenty-two offices of New York- and Chicago-based firms. Brussels has seven offices (to service an expanding U.S. clientele and to handle matters at Common Market headquarters); Tokyo has five; London and Mexico City have three each. These overseas offices range in size from the single representative who serves in a liaison capacity to a few sizeable branches that offer full-scale services for U.S. and foreign clients interested in doing business in the United States.

These overseas law branches, no matter where they are located, have the competence to help U.S. business corporations to enter other countries as well. One important contribution they make to their client companies is an over-all conceptual approach to business / legal problems, as contrasted with European lawyers who work as individuals rather than as firms; typically each individual works in a narrow specialized role. To supplement their own competences, U.S. branches call on European specialists in taxation and certain fields of foreign law. This type of service enables U.S. corporations to get a coordinated and sophisticated approach to the legal problems of doing business in foreign countries, and usually some general advice along with the legal advice. **The overseas branches of U.S. law firms do not advise local foreign clients on problems in their own countries.** (Bower, 1968), p. 51 (emphasis added).
As of 1968, U.S. law firm internationalization was certainly limited to providing U.S.
legal services to U.S. clients abroad.

Five years later, the behavior of U.S. law firms had not changed. In 1973,
Gaedeke was the first to formally survey U.S. law firms regarding their
internationalization behavior. This effort was embedded within an analysis of a broad
selection of U.S. advertising firms, consulting firms, and law firms. Consistent with
Bower, Gaedeke found a significant difference between the internationalization
motivations of U.S. law firms and other U.S. service providers:

<table>
<thead>
<tr>
<th>Incentives for Overseas Expansion</th>
<th>Number and Percent of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total Firms</td>
</tr>
<tr>
<td>Profit Opportunities</td>
<td>13 (32.5%)</td>
</tr>
<tr>
<td>Following U.S. Clients Abroad</td>
<td>11 (27.5%)</td>
</tr>
<tr>
<td>Seeking Expanding Overseas Markets</td>
<td>10 (25.0%)</td>
</tr>
<tr>
<td>Assisting European Clients Doing Business in the U.S.</td>
<td>3 (7.5%)</td>
</tr>
<tr>
<td>Diversification</td>
<td>3 (7.5%)</td>
</tr>
<tr>
<td></td>
<td>40 (100%)</td>
</tr>
</tbody>
</table>


Unlike advertising or consulting firms, the primary reason for the internationalization of
U.S. law firms was “[f]ollowing U.S. Clients Abroad” (61.5%) while an additional 23.1%
were expanding in order to assist “European Clients Doing Business in the U.S.”

Given the cultural differences and uniquely local aspect of the practice of law, the
focus of U.S. law firms in the period of 1965 to 1985 was rarely to compete with local
law firms regarding the provision of host country law. (Spar, 1997), p. 13. During this time, most U.S. law firms handled foreign-originated work through their home office. (Warf, 2001), p. 400. The U.S. firms were only internationalizing in order to assure client access to U.S. legal services while abroad:

“We became aware that a substantial number of our corporate clients were engaging or becoming engaged in the acquisitions of and investments in European industry. … The clients had need for American legal services which could not conveniently be provided from the United States.” (Gaedeke, 1973), p. 62 (emphasis added).

Driving the internationalization of legal practices was both the increasing demand of clients with global interests plus improved access to new communication technologies. (Beaverstock, Smith, & Taylor, 2000), p. 97.

Although U.S. firms initially expanded abroad simply to serve the existing demands of clients, by the 1980’s and 1990’s larger numbers of U.S. and U.K. law firms began to aggressively expand internationally. (Beaverstock et al., 1999), p. 1859. The establishment of international networks by law firms was necessary to support the increased international trade, international investment, and “the increasing globalization of finance.” (Warf, 2001), p. 399. See also (Beaverstock et al., 1999).

By 1997, 100 of the 250 largest U.S. law firms (by total number of attorneys) maintained offices outside the U.S. (Beaverstock et al., 2000), p. 96. These firms sought to predict the needs for their core clients while protecting them from competitors and prospectively seeking to attract new clients from around the world. (Spar, 1997). According to some observers, what emerged was a new, global law firm. See, e.g. (Beaverstock et al., 2000), p. 96.
Regardless of whether or not the resulting firms were truly “global,” the rapid expansion of international operations by U.S. law firms started the equivalent of an international “gold rush.” However, just as with California Gold Rush, it is unclear just how typical the notable successes actually were. Nonetheless, international expansion by large U.S. law firms “became integral to staying competitive.” (Spar, 1997), p. 13.

Making the competition and market restructuring of U.S. law firms even more acute was the emergence of global accounting firms providing similar international legal services.

Since many foreign countries have long-permitted ownership of law firms by non-lawyers (unlike in the U.S.), by the 1990’s there was an additional surge of accounting and auditing firms seeking to provide legal services abroad:

Apart from the major Wall Street [law] firms who… seem to have a virtual monopoly as far as big business is concerned, there are plenty of new firms that are attacking the less prestigious but far larger market for legal and financial services to small and medium-sized enterprises. Old established firms of accountants now purvey themselves as audit specialists or financial engineers. Supported by the structures which have been developed through the formidable market penetration of the major accounting firms, these newcomers make no secret of their desire to take business from European law firms, who thus find themselves caught in a crossfire. (Dezalay, 1990), p. 285.

The change in the motivations for U.S. firms to internationalize, combined with the influx of new competitors, precipitated a breakdown of the status quo. Rather than relying on established referral networks between U.S. and non-U.S. law firms, the U.S. law firms wanted it all.

Further stoking the flames of international expansion of legal services was the implementation of the General Agreement on Trade in Services (adopted in 1994 as “Annex 1b” as part of the Uruguay round of negotiations related to the World Trade
Organization). Several years passed as various countries signed on. By 2001, there were 141 signatory countries. (Terry, 2001), p. 999. Although the intricacies of GATS are beyond the scope of this inquiry, suffice it to state that GATS began a process of increasingly open access to the provision of cross-border legal services in many countries. (Terry, 2001), p. 1000. See also (Warf, 2001), p 400. Nonetheless, the international diversification of legal services remained “a complicated quilt of varying national legal systems, qualifications to practice, and barriers to entry for foreigners. (Warf, 2001), p. 399.

By 2008, the focus of most U.S. law firms had shifted. The global recession had a major negative impact on global commerce. Corporate clients took the opportunity to benefit from a “buyer’s market” for international legal services. Indeed, many U.S. law firms were far more concerned with survival than establishing global domination. At the same time, the Internet, communication technology, transportation, and market deregulation all continued to improve in quality and access. Lost in all the confusion was an understanding of how, exactly, U.S. law firms were approaching International Diversification.

**Firm-level Internationalization Theories**

In the second of five sections in the literature review, we examine a handful of the key internationalization theories. These theories provide the general backdrop for understanding the International Diversification behavior of law firms. For the sake of simplicity, the current discussion will distinguish between three groups of firm-level, internationalization, theories: 1) structural market imperfection theories; 2) market efficiency theories; and 3) incremental stage theories.
Prior to 1960, there were no firm-level theories seeking to explain why firms decide to expand operations across national boundaries. At the time, the closest thing to such a theory was the “neoclassical financial theory of portfolio flows.” (JH Dunning & Rugman, 1985), p. 228. Under that theory, the flow of international investment capital was the result of arbitrage with cash flowing to the locations with the highest interest rates. (Teece, 1985). However, there was a problem with this approach. It simply did not align with the observed patterns of actual international investment.

**Structural Market Imperfections Theories**

The first of the three internationalization theories is based upon the assertion that firms internationalize in an effort to create or capitalize upon structural market imperfections. See, generally, (Bain, 1956). International expansion is inherently predatory. The poster-child for this perspective is Stephen Hymer.

Hymer.

In 1960, Stephen Hymer submitted his doctoral dissertation at MIT on “The International Operations of National Firms, A Study of Direct Foreign Investment.” (Hymer, 1960). This represented the first time that anyone had attempted to explain why U.S. firms chose to expand operations internationally through foreign direct investment (“FDI”). According to Hymer, the internationalization process is typified by the effort of firms to create barriers to market entry by competitors. This way, the internationalizing firm is able to obtain superior rents based upon the resulting monopolistic market power. (Hennart, 2010), p. 258, (Teece, 1985).
Hymer noted that the MNE must have (or acquire) some “countervailing advantage” sufficient to overcome the liability of foreignness inherent in competing in the foreign market. (Calvet, 1981), p. 44. The local competitors naturally know more about their local market than a potential foreign competitor. As such, absent the MNE buying an existing local competitor, the MNE must possess its own advantage sufficient to overcome the liability of foreignness. Otherwise, international expansion would not be profitable.

Additionally, the market for the countervailing advantage must be imperfect. See, e.g. (Hymer, 1960), p. 46. See also (P. Buckley & Casson, 1976), p. 67. Assuming the MNE has an advantage that overcomes the liability of foreignness, the advantage must continue to exist. Otherwise, there would not be any way to sustain the profitability of the venture or recoup the investment. The competitors would quickly adjust and the above-market profits would evaporate. Consistent with neoclassical economics, there would be no means for FDI to occur if the markets were perfectly efficient. All international involvement would be by way of international trade. (Calvet, 1981), p. 43.

For Hymer, proof that the structural imperfections continue to exist was shown by the movement of capital by U.S. firms engaged in foreign direct investment. This movement “is motivated by the desire to control and not by differences in interest-rates.” (Hymer, 1960), p. 4. If interest-rates were the only criteria for an investor, then portfolio investment – without control – would serve that criterion just fine. (Hymer, 1960), p. 23. Therefore, the deeper issue for Hymer was why firms seek control through direct investments in international operations.
Hymer identified three main reasons why firms would want control over through FDI: as an attempt to reduce risk (Type 1); as an effort to remove competition through buying out competitors (what could be called “Type 2a”); or in order to extend “special advantages” abroad to extend access to superior rents (what could be called “Type 2b”). (Teece, 1985), p. 234.

As to removing competition (“Type 2a”), Hymer essentially viewed the removal of competition as a collusive direct means for establishing monopolistic power in the foreign market. Rather than competing with each other, the combined MNE could appropriate superior rents – at the expense of consumers and the host market. This is basically the traditional anti-trust concern.

As for extending “special advantages” (“Type 2b”), Hymer still viewed the behavior as an effort to benefit the firm through utilizing market imperfections. Hymer recognized that these could be achieved through “superior production techniques, imperfections in input markets that allow lower buying prices for established firms, and similar first-mover advantages.” (Teece, 1985), p. 234. This also included “scale economies, knowledge advantages, distribution networks, product diversification, and credit advantages.” (JH Dunning & Rugman, 1985), p. 229. As to both Type 2 direct investments, Hymer posited that international expansion occurs where the firm has the ability to “close markets” through the development of monopoly powers that exceed the initial disincentives created by the liability of foreignness.

In fact, the biggest criticism of Hymer has been that he exclusively relied upon structural market imperfections to explain the existence of international operations. (JH
Dunning & Rugman, 1985). For a different take on Hymer’s contribution, see (Horaguchi & Toyne, 1990). Notably, Hymer did not reference Coase (1937) or TCE anywhere. (Williamson, 1998). See also (JH Dunning & Rugman, 1985), p. 229. As such, Hymer did not attempt to explain or integrate any of the efficiency concepts of internalization and/or transaction cost economics. (Teece, 1985). Hymer also did not attempt to address any of the geographic/locational dimensions subsequently developed by Dunning. (JH Dunning & Rugman, 1985), p. 230. Another criticism was that the theory was too static. (Teece, 1985).


Hymer also introduced the fundamental concept of the “liability of foreignness” as a consideration across many other internationalization theories. To some extent, the “liability of foreignness” may be viewed as an analogue to the assumption of non-zero transaction costs in Coase (1937). However, while the existence of transaction costs
exists in both domestic and international markets, the liability of foreignness is uniquely international.

In applying Hymer to the internationalization of law firms, one fundamental option that all U.S. law firms face is whether to acquire a locally existing law firm or whether to expand directly and engage the “liability of foreignness” issue. In this regard, how a law firm expands abroad is inherently linked to the type and nationality of the law practiced in the foreign law office – not just the nationality of the law firm. This, in turn, will directly impact the extent to which there will be a “liability of foreignness.”

For instance, if a New York law firm practicing U.S. securities law were to open a London office, there are still three different potential practice configurations: 1) the firm could be planning to only practice U.S. securities law (and not U.K law) in London; 2) at the other extreme, the firm could be planning to only practice U.K. law in the London office (and not U.S. law); and 3) the firm could be planning to be practicing a mix of U.S. and U.K law.

In the first instance, the establishment of the London office would likely require a significant redeployment of New York attorneys to the London office. However, depending upon the number of London firms also practicing U.S. law, the liability of foreignness might be minimal. In fact, many indigenous London law firms would likely work cooperatively with the U.S. firm since they would not be competitors. In this instance, the motivation for the establishment of the London office could be simply a matter of reducing risk (Type 1 behavior). The primary motivation for the U.S. law firm expansion might not be to pursue either of the Type 2 goals. However, the firm could
conceivably achieve better economies of scale and improved capacity utilization if the work that originated in London were used to fill unused capacity in the New York office.

In the second instance, the fact that the London office would be exclusively practicing U.K. law would mean that the firm would be viewed as a direct competitor by all of the indigenous London law firms. If the U.S firm decided to “import” and adapt the U.S. lawyers, there would certainly be a maximum amount of the liability of foreignness (and unnecessary expense in re-training attorneys). This would be a Type 2b strategy. A much more reasonable option for the U.S. firm would be to acquire or merge with an existing London firm (or at least recruiting the vast majority of U.K. lawyers locally). This would be a Type 2a strategy. Depending upon how the U.S. firm went about establishing its London operations, there could be significant variation in the actual liability of foreignness – as well as the benefits realized by the home office.

In the third instance, the firm could pursue the “perfectly awful compromise.” Since the firm would be competing locally, there would be a liability of foreignness in the provision of U.K. legal services. At the same time, the deal flow for services based upon U.S. law would be minimized since there would be fewer referrals from the local firms. The result would be increased cost, increased competition, and decreased coordination. In this situation, the only way there would be Hymer Type 1 benefits would be if the law firm already had a captive, international client that required both U.S. and host country law to be practiced. Alternatively, a law firm aggressively pursuing Type 2a strategy (with significant risk), could also engage in the same behavior.
When consideration is given to the jurisdiction of the law practiced abroad, it becomes clear that the assumption of the liability of foreignness for international law firms is much more complex than presented by Hymer. Beyond the law practiced, the type of law firm clients could also have a huge impact on the liability of foreignness. For instance, there probably are a handful of U.S.-based clients needing and willing to pay for a single law firm to handle ALL of their legal work around the world. A U.S., publically-traded, corporation might insist on such representation. In this limited situation, since the U.S. law firm would essentially be following a pre-existing client, the liability of foreignness would be minimal. However, one would expect such a situation to be the exception rather than the rule.

More often than not, it would be expected that most international clients of U.S. law firms would simply rely upon its primary outside counsel to help identify and evaluate legal counsel in other countries to fulfill specific legal tasks. Alternatively, the corporate client could manage the global provision of legal services in-house. The reliance upon outside, global, legal counsel would be expected to diminish as the size and experience of the in-house legal department grew.

Beyond the liability of foreignness issue, the concept of “market closing,” monopolistic intentions, does not appear to have much application to the international expansion of U.S. law firms. Much more commonly, the monopolistic behavior of law in international markets generally takes the form of domestic protection of local host country lawyers – not exploitation. Competition is inherently anchored locally by virtue of local government regulations that favor local attorneys. As such, the international expansion of U.S. law firms is unlikely to be part of any international firm strategy to
close markets – even if there is significant variation in the liability of foreignness depending upon specific firm internationalization strategy.

**Market Efficiency Theories**

As noted above, the fundamental assumption of the market imperfection theories is that the internationalization of MNEs (through FDI) is inherently an effort to reduce competition and to exercise market power. These theories, based largely upon Hymer (1960), view market imperfections as a “zero sum game” where monopolists gain at the expense of consumers. (Hennart, 2010), p 258. The moral of these theories is that host countries should monitor and control MNEs closely. However, as might be expected, there were other internationalization theories that viewed internationalization as “market opening.” These market efficiency theories represent the second of the three internationalization theories.

These theories, based upon Coase (1937), view the expansion of firms across national boundaries as enabling transactions that otherwise would be unfeasible in the open market. See generally, (J Dunning, 1988), p. 2. For these theories, internationalization occurs because internalization (within the firm – by opening new offices) is more efficient than attempting to achieve a cost-effective solution through market-based solutions. For these theories, internationalization is a positive sum gain. Trade occurs where it would not have otherwise occurred at all. (Hennart, 2010).

**Buckley and Casson.**

Based largely upon the work of Coase (1937), in 1976 Buckley and Casson sought to explain the operations of multinational enterprises specifically regarding the
international production of intermediate products. (P. Buckley & Casson, 1976), p. 34.

“Because intermediate-product markets are difficult to organize due to various [market] imperfections, there is an incentive to bypass them and to bring the activities of producing and marketing within the organization’s ownership and control, that is, to ‘internalize’ them.” (Boddewyn, Halbrich, & Perry, 1986), p. 49.

Like Coase, Buckley and Casson assumed that firms rationally evaluate economizing alternatives through selective internalization decisions. However, Buckley and Casson expressly added an international dimension by seeking to explain why manufacturing firms extend their production of intermediate products across national boundaries.

Their work subsequently became known as the first installment of the “Reading School” of international thought (consisting of Buckley and Casson, Dunning, Rugman and Hennart). (Fina & Rugman, 1996), p. 200. See also (P. Buckley & Casson, 1976).

Buckley and Casson began by defining the MNE as “an enterprise which owns and controls activities in different countries.” (P. Buckley & Casson, 1976), p. 1. Their theory of an MNE was based upon three assumptions:

- Firms maximize profit in a world of imperfect markets.
- When markets in intermediate products are imperfect, there is an incentive to bypass them by creating internal markets. These involve bringing under common ownership and control the activities which are linked by the market.

As to the process of deciding whether or not to internalize, Buckley and Casson identified four relevant factors:
• **Industry-specific factors** relating to the nature of the product and the structure of the industry,

• **Region-specific factors** relating to the geographical and social characteristics of the regions linked by the market,

• **Nation-specific factors** relating to the political and fiscal relations between the nations concerned, and

• **Firm-specific factors** which reflect the ability of management to organize an internal market. (P. Buckley & Casson, 1976), p. 33-34.

As applied to the internationalization of law firms, Buckley and Casson is informative to the extent that the legal services can be framed as a singular finished client “product” representing intermediate “legal” components sourced across different national jurisdictions. Undoubtedly, there are some situations – such as where there is an international commercial transaction needing to comply with unique legal standards in different countries – where Buckley and Casson can be directly applied. Buckley and Casson would also raise the possibility of understanding how the industry, region and nation factors might play a role – in addition to firm factors – in the International Diversification behavior of law firms. However, the geographical/locational implications are beyond the scope of the current study.

**Dunning**

To a very large extent, Dunning extended the concepts of “location” and “internalization” from Buckley and Casson and added “ownership advantages” to create his O-L-I model. (P. Buckley & Casson, 1976), p. xiv. Although not strictly a “theory,” no discussion of firm-level internationalization theories would be complete without mentioning Dunning’s “Eclectic Paradigm” (“O-L-I” model). The Eclectic Paradigm has been “widely recognized as the preeminent theoretical [FDI] paradigm within IB.” (John Cantwell, Dunning, & Lundan, 2009), p. 568. See also (Vahlne & Johanson, 2013), p.
Dunning made his first presentation of his O-L-I model.

Dunning’s O-L-I model actually went through numerous extensions. (J Dunning, 1988). However, the differences between the versions is not particularly relevant for the current discussions. (Narula, 2010), p. 6. See also (Eden, 2003). For our purposes, we will generally focus on the original O-L-I version. As with Hymer (1960), Dunning noted that the first condition for firms to expand internationally is their ability to overcome the internationalization barrier presented by the liability of foreignness. However, Dunning made a significant distinction between competitive advantages caused by Hymer/Bain structural defects and those caused by Williamson-like, TCE market defects. (JH Dunning & Rugman, 1985). See also (J Dunning, 1988), p. 2. Dunning then identified three advantages, which in combination, could potentially overcome the liability of foreignness: ownership advantages, internalization advantages, and location advantages.

As to “ownership advantages,” Dunning sought to identify those circumstances in which a firm might initially own anything that could potentially provide the basis for a competitive advantage if the firm were to directly enter a foreign market. Dunning broke down the category into three sub-types: 1) advantages arising from the exclusive use of a particular asset; 2) advantages arising from achieving greater economies of scale and scope; and 3) advantages arising from superior geographic access. (J Dunning, 1988), p. 2.

The first ownership advantage might exist if, for instance, the firm possessed proprietary knowledge as to a new manufacturing technique either through patenting or
maintaining a trade secret. It is unclear how this might be relevant to the internationalization of law firms.

The second advantage might exist if, for instance, extending production internationally would enable fuller capacity utilization across the entire firm’s manufacturing facilities. This advantage might exist if the presence of international operations were to encourage a law firm to increase the capacity utilization of both its domestic and foreign practice areas.

The third advantage might exist if, for instance, the extension of international production would enable the firm to reap the benefits of a transaction while avoiding uncertainty or costs of an arms-length transaction. An example of this would be building a factory in a region with a culture of corruption in market exchanges. As related to law firms, an example of this would be the ability of the law firm to avoid the risk of losing a client to a competitor (similar to the advertising agencies mentioned by Bower (1968)).

Beyond the existence of ownership advantages, the O-L-I model additionally required that there be sufficient reason for the firm to decide to internalize the firm’s ownership advantages across national boundaries. Dunning’s concept of internalization advantages clearly had its origins in Coase (1937) and Buckley and Casson (1976).

The distinction between “ownership” and “internalization” advantages was subject to criticism as essentially being the same thing. If a firm decided to internalize, then they had to have an ownership advantage. However, Dunning pointed out that the opposite was not necessarily true – if a firm had an ownership advantage, the firm might nonetheless decide to pursue other domestic opportunities rather than expand.
internationally. In these instances, the firm might choose to engage in contractual agreements with foreign firms or simply export from the home country. (J Dunning, 1988), p. 3.

To a very large extent, this distinction between ownership and internalization is at the crux of the problem facing U.S. law firms. Clearly, U.S. firms benefit from an ownership advantage if the client is controlled by the firm. However, the countervailing costs of internalizing the benefit – through the establishment of international operations – may actually exceed the ownership benefits. Under these circumstances, it would logically make sense that some U.S. law firms might avoid internalization by referring clients to foreign law firms.

Under the O-L-I model, ownership advantages are necessary but not sufficient to support FDI. Pursuant to the Eclectic paradigm, the determination of ownership and internalization advantages is directly intertwined with the existence of corresponding location advantages as well:

Enterprises will engage in foreign production whenever they perceive it is in their best interests to combine spatially transferable intermediate products produced in the home country, with at least some immobile factor endowments or other intermediate products in another country … the decision on where to site a mine, factory or office is not independent of the ownership of these assets nor of the route by which they or their rights are transacted. (J Dunning, 1988), p. 4.

Once again, the O-L-I model recognized that the existence of location advantages inevitably result from some underlying market failure. However, Dunning reiterated that the market failure could be caused by structural and/or transactional market defects. Dunning additionally clarified (contrary to Hymer) that the existence of structural defects may have been caused by host government trade barriers rather than the monopolistic
intentions of MNEs. To a very large extent, this distinction has direct application to the internationalization of law firms.

Although the local regulation of the practice of law is not necessarily intended to be a trade barrier, the fact remains that the regulations and differing cultural and institutional histories of different countries constitute a significant challenge. In this situation, the monopolistic barriers tend to benefit the domestic law firms. As such, many U.S. law firms might rationally decide to minimize international diversification as long as trustworthy network partners can be identified. However, imbedded within the U.S. law firm calculus will be the type of law and legal questions that the client needs to have handled. If the questions largely relate to U.S. law, then it is reasonable to assume that no external firm would be considered sufficiently trustworthy. In that instance, the OLI model would predict a client-following behavior by U.S. law firms.

The criticisms of the Eclectic Paradigm are that it is “too much of a ‘paradigm’ … and too little of a ‘model’ to provide detailed advance on research design and hypothesis testing.” (P. J. Buckley & Casson, 1998), p. 540. Its continual extension introduced unnecessary complexity and risked being tautological. (Narula, 2010). Even Dunning admitted that “precisely because of its generality, the eclectic paradigm has only limited power to explain or predict particular kinds of international production; and even less, the behavior of international enterprises.” (J Dunning, 1988), p. 1. Other criticisms of the O-L-I model are that the “O” – ownership advantages – is not necessary to explain the internationalization behavior and that model does not sufficiently incorporate the role of differences between firm-specific, resource-based, advantages. (J Dunning, 1988), p. 2, 6.
Nonetheless, the O-L-I model provides a useful basis to survey the general International Diversification behavior of U.S. law firms. Most notably, the relationship between the firm ownership advantages and potentially related locational advantages may help to explain some relationships between firm home office and subsequent internationalization decision making. As such, the O-L-I model would predict some - and ignore other - types of relationships between firm practice areas and the locations in which U.S. firms place their offices.

In addition to the O-L-I model, there are certainly other internationalization theories that rely upon Coase (1937) and are based upon internalization and/or TCE. See, e.g. (R. E. Caves, 1982; Hennart, 1982). However, for our purposes, these other theories are unnecessary to provide the firm-level internationalization perspectives resulting from Coase (1937), or the TCE discussion from Williamson (1979).

**Incremental Stage Theories**

The last of the three groups of internationalization theories focuses upon the behavioral processes connected to a firm’s foreign commitment decision. To a large extent, most of the incremental stage theories are an extension of the behavioral theory of the firm as applied to international markets. (R. E. Morgan & Katsikeas, 1997), p. 72. These theories also usually include aspects consistent with the resource based view of the firm. (Penrose, 1959).

The incremental stage theories focus on how firms learn and how they ultimately share knowledge and deploy assets. The focus of these theories is not so much on “market opening” or “market closing.” The focus is on the organizational processes by
which firms internationalize and engage in international business. For our purposes, the
two primary theories propounded by Johanson and Vahlne are sufficient to summarize
the stage theories.

Uppsala I.

In 1977, Johanson and Vahlne presented their original “Uppsala Model” (aka
Stages Model) of firm internationalization. Their primary assumption was that “lack of
knowledge about foreign markets is a major obstacle to international operations, but such
knowledge can be acquired.” (Forsgren, 2002), p 259. Another major assumption is that
knowledge about internationalization grows incrementally. (Forsgren, 2002), p. 259.

Primarily relying upon Cyert and March (1963) (though also citing, among others,
Penrose (1959)), Johanson and Vahlne asserted that the internationalization of firms was
largely based upon the “gradual acquisition, integration, and use of knowledge about
foreign markets and operations, and on its successively increasing commitment to foreign
markets.” (Johanson & Vahlne, 1977), p. 23. Starting with foreign markets that were
similar to the home market (and therefore only a small “psychic distance” from the home
market), firm internationalization was presented as a gradual learning process
incorporating a series of decisions leading to increased foreign market commitment at
each step. (Erramilli & Rao, 1990), p. 137.

The concept of “psychic distance” was defined as the factors “that make it
difficult to understand foreign environments” and originated from the concept of
“liability of foreignness” by Hymer. (Johanson & Vahlne, 2009), p. 1412. However, the
problem of large psychic distance was overcome by the firm through increasing firm knowledge and “market commitment.”

In this regard, the “market commitment” decision is composed of the amount of resources required, perceived risks, and the opportunity costs of applying those resources for international expansion. If the difficulty in using the resources for alternative, non-internationalization purposes is high, then international market commitment should be quite easy. In contrast, if there are multiple alternate uses for resources that are less risky or more profitable, then international expansion becomes much more speculative and difficult. (Johanson & Vahlne, 1977), p. 27.

According to Uppsala I, at the beginning of the firm’s internationalization process, the firm is not committed to any internationalization and the firm’s knowledge of the foreign market is virtually zero. As such, the firm’s market commitment is minimal. The firm only chooses to engage in passive exporting. The cycle is complete when the firm, which initially had no knowledge of the foreign market, now learns a little bit from its exporting experience.

Next, since the firm has learned that there may be demand for their product in a specific foreign country or region, the firm seriously considers having a foreign agent – either through a licensee, franchisee, or directly hired sales representative. Consequently, the firm pursues a strategy to more actively cover the foreign market. This increased market commitment sets the stage for the next stage.
At the third stage, the firm has learned enough about the foreign market opportunity to decide to set up a foreign sales subsidiary. This commitment leads to even more activity in the foreign market and provides the basis for even more knowledge.

In the fourth stage, the firm has so much market knowledge that the firm makes an even larger commitment through the establishment (either through acquisition or green field operations) of production facilities in the foreign country. These activities, in turn, help build the firm’s commitment to pursue other international opportunities. (Johanson & Vahlne, 1977), p. 26.

Although parallels can be seen between Uppsala I and the internationalization of U.S. law firms, the match is not perfect. Within the context of law firms, the first stage of Uppsala I occurs when the law firm becomes aware that a new client, or one of its existing clients, requires international support. If the client is perceived as important, the law firm will be more motivated to consider the options for improving international support. However, as recognized by Uppsala I, the motivation for international diversification will depend upon the risks and opportunity costs for the law firm – including the potential for greater profit by focusing on domestic expansion.

Having become more aware of existing client demand in a given international location (and assuming the risks and opportunity costs are not too high), the firm would then have an incentive to determine the extent of additional potential demand and feasibility of maintaining either a temporary or permanent foreign presence in the appropriate jurisdiction. Unlike other industries, professional service firms are largely unable to use licensees or franchisees. Consequently, the firm would face decisions
regarding temporarily or permanently establishing a presence abroad – or otherwise using communication technologies for providing legal services internationally. Maximizing firm profit would remain the underlying goal.

Applying Uppsala I to the international expansion of U.S. law firms provides some interesting insights. For instance, Uppsala I assumes that the initial products being exported are either similar or identical to the products being sold domestically. This would suggest that the expansion of U.S. law firms would be based upon the export of U.S. legal services – rather than host country legal services. Unlike the manufacturing context underlying Uppsala I, the transition from home country legal services to host country legal services would usually present significant challenges due to the different cultural, historical and theoretical foundations of different country legal systems. As such, the psychic-distance in most instances would be significantly large. This would seem to correspond nicely with the historical international expansion behavior of U.S. law firms. Most were providing services related to U.S. law.

However, Uppsala I still presumes that the impetus for international growth is the recognition of a foreign, indigenous, demand for the home country product. While this undoubtedly happens in some instances, most U.S. law firms expanded internationally based upon existing domestic clients. In this regard, the dynamics of U.S. international expansion includes a sizable dose of “follow the client leader” in addition to any demand by the foreign market. Presumably, this is made all the more acute due to the risks and opportunity costs of ignoring domestic expansion.
Although Uppsala I is easy to understand and apply, there are still criticisms of its approach. One criticism is that the model fails to include the impact of relationship behavior, such as trust and commitment, by trading partners. (Johanson & Vahlne, 2009), p. 1414. In fact, Uppsala I is not instructive as to individual firms, markets or situations. (Johanson & Vahlne, 2009), p. 1417. Uppsala I also assumes that gradual learning is inherent in internationalization. (Johanson & Vahlne, 2009), p. 1417. This assumption is clearly violated by virtue of the existence of “born global” firms.

Nonetheless, Uppsala I is still informative in that the International Diversification of many law firms has likely progressed as the firm has increased their comfort, knowledge and commitment about foreign markets. Just as with Penrose, Uppsala I recognizes that firms evaluate the benefits likely to accrue from committing resources (U.S. lawyers) to additional international expansion. This theme is central to the evaluation of international strategies of all law firms.

Uppsala II.

Although the Uppsala model has gone through a number of iterations over the years, in 2009 Johanson and Vahlne made some particularly significant revisions (“Uppsala II”). Most notably, Uppsala II substitutes the network-based view and the “liability of outsidership” for the concept of psychic distance and the liability of foreignness in Uppsala I. (Johanson & Vahlne, 2009).

Importantly, the network-based view (“NBV”) adopted in Uppsala II is based upon the same “idiosyncratic resource bundles” discussed by Penrose and Barney under
RBV. However, the NBV under Uppsala II adds an additional assumption that “exchange within a network allows a firm to acquire knowledge about its relationship partners, including their resources, needs, capabilities, strategies, and other relationships.” (Johanson & Vahlne, 2009), p. 1414. This is the same question that U.S. law firms face when deciding whether to diversify internationally or trust a client matter to a foreign law firm.

Uppsala II embraces the view that the markets in which firms operate consist of connected network relationships linked in “various, complex and, to a considerable extent, invisible patterns.” (Johanson & Vahlne, 2009), p. 1411. By “connected” the authors specifically mean that “exchange in one relationship is linked to exchange in another.” (Johanson & Vahlne, 2009), p. 1414. Rather than uncertainty linked to the “liability of foreignness” caused by psychic distance (as in Uppsala I), the authors in Uppsala II view the challenge faced by internationalizing firms as caused by the “liability of outsidership” from the relevant networks in the particular international market. (Johanson & Vahlne, 2009).

For Uppsala II, the core concept in the internationalization of a firm is its membership in relevant business networks that result in appropriate embedded knowledge creation and trust building.

As for knowledge creation, Johanson and Vahlne (2009) noted that Uppsala I implicitly included the role of operational and experiential learning. Under Uppsala I, operational learning is critical to the day-to-day operations of the firm – including the technical ability to expand. However, experiential learning about the dynamics of the
foreign markets is what enables the firm to develop the capabilities to increase foreign market commitment.

In Uppsala II, Vahlne and Johanson (2009) frame knowledge differently. They couch their original concept of experiential knowledge within a concept they refer to as “institutional market knowledge.” Next, they distinguish “institutional market knowledge” and “business market knowledge” as follows:

A lack of institutional market knowledge – that is, lack of knowledge about language, laws, and rules – has to do with factors relating to psychic distance, and the liability of foreignness. Lack of business market knowledge is related to a firm’s business environment that, according to the business network view, consists of the firms with which it is doing business, or trying to do business, and the relationships between firms in this environment. The lack of such market-specific business knowledge constitutes the liability of outsidership. (Johanson & Vahlne, 2009), p. 1416.

Unlike the original model, Uppsala II focuses on the trust and relationship-specific knowledge gained through the business network.

This relationship-specific knowledge enables the firm to better understand the firm’s – as well as the partner’s – “heterogeneous resources and capabilities” within the foreign market context. Moreover, the interaction of knowledge possessed by the two partners may even result in the synergistic creation of new knowledge. The acquisition of partner knowledge also serves to enhance the ability of the firm to recognize foreign market opportunities. (Johanson & Vahlne, 2009), p. 1419. Beyond this, the ability of a firm to develop relationship-specific knowledge may enable the firm to improve its ability to develop general-relationship knowledge too. (Johanson & Vahlne, 2009), p. 1416.
As for trust, the building of business network relationships begins with the development of integrity and reliability between partners. (Johanson & Vahlne, 2009), p. 1417. Once trust has been established, the network partners may – but need not necessarily - decide to develop a commitment to a long-term, mutually beneficial, relationship. The development of mutual commitment introduces greater dependency and flexibility between partners in dealing with short-term uncertainty. (Johanson & Vahlne, 2009), p. 1418.

Notably, the concept of “commitment” in Uppsala II runs directly contrary to the concept of opportunism inherent in transaction cost economics. (Williamson, 1979) Rather than assume a dichotomy of internalization or market reliance, Uppsala II adopts a continuum that includes inter-firm cooperation based in part upon mutual commitment rather than an exchange transaction. Furthermore, Uppsala II incorporates a multi-party network “web” approach rather than the largely bi-directional exchange relationship.

In its most recent 2013 version, the authors continue to extend Uppsala II to better account for persistent complexity, uncertainty, and dynamics within a networked global business environment. (Vahlne & Johanson, 2013). In the process, Vahlne and Johanson intentionally shift the focus of the model from the determinants of foreign direct investment toward an improved model of “how individual MNE evolves over time.” (Vahlne & Johanson, 2013), p. 191.

Applying Uppsala II to the internationalization of U.S. law firms raises some intriguing issues. Most notably, Uppsala II would suggest that there is a significant role played by network relationships between law firms in international markets. Given the
complexity of issues encountered in deciding whether to enter a particular market and what type of legal services to provide, Uppsala II would suggest that the cost effective service to global clients would be more a function of inter-firm alliances and relationships than actual international expansion of U.S. lawyers abroad. After all, the role of risks and opportunity costs remains a firm consideration. Furthermore, given the differences between the laws (and lawyers) of different countries, it would be a truly rare event where it would be more economical to permanently position U.S. attorneys abroad than it would be simply to maintain a trusted network-relationship abroad.

Based upon the inefficiencies of distributing U.S. firm resources internationally and the challenges of integrating legal operations of firms practicing law under different national traditions, there are at least two situations that would be supported by Uppsala II. One prediction would be that many U.S. law firms would primarily rely upon network relationships for the servicing of firm clients in foreign jurisdictions – as to foreign law issues. Another related prediction would be that many U.S. firms would seek to impose at least some sort of enhanced control over the network relationships in order to assure a stronger alignment of interests among network members. To a very real extent, this second prediction would appear to suggest informal enforcement mechanisms and/or account for the increasing use of Swiss Verein structures by several U.S. law firms.

Recall that a Swiss Verein is essentially an association of independent law firms operating under a common brand name. The members of the verein refer matters between each other with fees distributed based on origination, servicing, and verein overhead costs. In fact, there are some commentators who have asserted that vereins
should NOT be considered a single firm. (Kalis, 2011). The argument has been that the proper measure of vereins – as associated members of a network - should be to break down the individual members into separate entities. While it is unnecessary to resolve this question right now, it should be noted that several of the largest international law firms are in fact vereins. For instance, the first major U.S. law firm to adopt a Swiss Verein structure was Baker & McKenzie. What is notable is that the actual verein structure represents a more formal and secure method of pursuing the NBV proffered by Uppsala II.

In sum then, the internationalization theories constitute a particularly relevant extension of the underlying firm theories. In each instance, greater insight is provided as to the approach and issues facing U.S. law firms regarding International Diversification. Per Hymer, the U.S. law firms could be internationalizing to close and control markets. Per the market efficiency theories, the U.S. law firms could be internationalizing to facilitate the internalization of legal services more effectively than relying upon foreign market mechanisms. Per Johanson and Valhne, the firms could be simply learning how to increase foreign market commitment – or growing their international network of trusted relationships. Indeed, all of these perspectives could be partially correct.

**Distinctive Characteristics of Services**

The third of the five sections in the literature review discusses the distinctive characteristics of services. Up to this point, we have discussed firm theories relating to how and why firms exist, grow, behave, and internationalize. However, all of these

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3 In fact, this author agrees that vereins should not be considered single firms. However, given the traditional listing of vereins as firms in the AmLaw 100, adjustment to data on vereins was accomplished through the rubric (contained in Appendix A) used for determining related international firms in the Data Extraction Methodology section.
theories were developed within the context of manufacturing or the sale of goods. In this section, we examine and distinguish the unique characteristics of services. We also explain how the general category of “services” can be broken down further.

It is now generally agreed that the management and marketing of services is sufficiently unique that services should be examined to account for their different characteristics. See, e.g. (Edgett & Parkinson, 1993), p. 19. This is not to imply that services are so completely unique that traditional manufacturing/goods theories are irrelevant. Quite often, the considerations related to services and goods are essentially the same. (Boddewyn et al., 1986), p. 42. “Insights gained through research within the manufacturing sector may provide for a greater understanding of the internationalization of service firms.” (R. G. Javalgi & White, 2002), p. 575. Nonetheless, services can present unique problems determining and/or allocating the location of service activity, providing for comparisons across different types of services, and determining the minimum amount of service activity necessary to constitute an “international” behavior for MNE status. (Boddewyn et al., 1986), p. 43-44.

It has been stated that a “good may be defined as a physical object which is appropriable and, therefore, transferable between economic units.” (Hill, 1977), p. 317. In stark contrast, a “service” consists of a “deed, act or performance.” (CH Lovelock, 1983), p. 10. Another commentator has described services as “activities, benefits or satisfactions which are offered for sale, or are provided in connection with the sale of goods.” (Regan, 1963), p. 57 (emphasis added). The later part of the definition (starting with “or”) simply reminds us that the “goods/services” distinction is not an all or nothing proposition. Indeed, it has been observed that “most goods embody some non-factor
intermediate services, and most services embody some intermediate goods.” (Sanchez-Peinado & Pla-Barber, 2006), p. 217. A single firm can provide value that is both “partly tangible and partly intangible, without diminishing the importance of either characteristic.” (Shostack, 1977), p. 74.

The fundamental difference between goods and services is that services are inherently intangible, heterogeneous, inseparable, and perishable. (Zeithaml, Parasuraman, & Berry, 1985), p. 33 (Edgett & Parkinson, 1993), p.22. “Because services are performances, rather than objects, they cannot be seen, felt, tasted, or touched in the same manner in which goods can be sensed.” (Zeithaml et al., 1985). See also (Edgett & Parkinson, 1993), p.22. Professional services possess additional characteristics known as “credence qualities”.(Christopher Lovelock & Gummesson, 2004) Knowledge-based services inherently involve a high degree of customization, high degree of uncertainty and a high degree of risk. (Czinkota, Grossman, Javalgi, & Nugent, 2009), p. 274. As such “it is wrong to imply that services are just like products ‘except’ for intangibility.” (Shostack, 1977), p. 73. The other characteristics of services, and professional services, also need to be considered.

As to heterogeneity, services present unique challenges regarding consistency. (Edgett & Parkinson, 1993), p. 26. Services must be “created” (or “recreated” to some extent) with each step and exposure to the customer. As such, the “quality and essence of a service… can vary from producer to producer, from customer to customer, and from day to day.” (Zeithaml et al., 1985), p. 34. Even the service performance by the same individual will likely vary on a day-to-day basis. (Zeithaml et al., 1985). For each consumer, the services experience is heterogeneous.
Heterogeneity is present in virtually all legal services. Even within a single legal matter, there are multiple client exposures to firm attorneys and other personnel. Each exposure is largely independent from all other exposures. The actual delivery of legal services on one day is distinct from the delivery on any other day. Therefore, one of the major challenges in the delivery of legal services is achieving consistency across people and time. At the same time, the law firm has to address the differing cultural expectations that exist where the clients are from different nationalities. What may be expected and routinely accepted in one country may be quite unexpected and unacceptable to clients in another country.

As to inseparability, services cannot be separated from production and consumption. (Edgett & Parkinson, 1993)p. 24-25. “Whereas goods are first produced, then sold and then consumed, services are first sold, then produced and consumed simultaneously.” (Zeithaml et al., 1985), p. 33-34. See also (Regan, 1963). As a result, the marketing of services is inherently indirect – promoting something that will only be produced after the consumer has already made their purchasing decision. (Edgett & Parkinson, 1993), p. 25. In this regard, it should not be surprising to find Reputational Capital as being a key law firm resource since it provides some basis for reasonable expectations regarding future services.

As to perishability, services cannot be saved for use at a future time. (Edgett & Parkinson, 1993), p. 27. If the opportunity for producing a particular service is lost, it cannot be saved or stored for some future sale. (Zeithaml et al., 1985). It is impossible to save a service.
Lastly, specifically focusing attention on professional services, the credence characteristics are even more defining. The professional services are known as credence goods because their purchases inherently involve a level of trust by the purchaser. (Sheehan & Stabell, 2010), p. 201. See also (Goldring, 2013). The professional services, as premier knowledge-based offerings, inherently include high customization, uncertainty and risk. (Czinkota et al., 2009). As such, the “benefits of these complex services are both difficult to define prior to sale and may be difficult to evaluate even after the service has been provided.” (Goldring, 2013), p. 73. Consequently, “intangible, subjective factors are likely to greatly influence selection” and evaluation of performance. (Day & Barksdale, 2003), p. 566. A high degree of buyer trust is necessary.

Of course, all of these characteristics apply to the provision of legal services. When a client retains an attorney, there is little way for the client to define in advance the exact measure of legal performance or value received. This requires a degree of trust by the purchaser that the quality of services received is appropriate. A large reason for this problem is that the provision of legal services is inherently subject to high customization, uncertainty and risk. There are multiple means by which the attorney can zealously represent the interests of the client. However, in many instances, the outcome of the legal matter will have no objective measure linked to the quality of services provided.

For instance, a criminal defendant who is convicted of capital murder and sentenced to life in prison may have had outstanding legal representation – and otherwise may have been a sure candidate for the death penalty! On the other hand, if the criminal defendant was clearly innocent, the same outcome could actually indicate horrid legal
representation. In this way, the nature of legal services is often difficult to evaluate even after the outcome is known. (Christopher Lovelock & Gummesson, 2004).

Unfortunately, there is no single universally accepted system for distinguishing between the various types of services. Instead, there are dozens of different proposed approaches. Many overlap. Each provides its own unique approach to distinguishing different types of services. See, e.g. (Vandermerwe & Chadwick, 1989). For our purposes, we will consider three particularly significant approaches.

The first of the three approaches categorizes services based upon whether the service is primarily capital-based or knowledge-based. (Contractor, Kundu, & Hsu, 2003), p. 10. The distinction between the two categories is determined by the extent to which the category is primarily dependent upon capital assets, or “more driven by intangible assets and have a much lower fixed capital cost burden.” (Contractor et al., 2003), p. 11.

For Contractor, et al, capital intensive services include “air transportation, construction, hotel, restaurant and fast food chains, wholesale trade, retail trade, and shipping and trucking.” (Contractor et al., 2003), p.11. In contrast, knowledge-based service sectors include “advertising, marketing research, publishing, securities, and diversified financial services, accounting and legal services.” (Contractor et al., 2003), p.10 & 11 (emphasis added). Clearly, the provision of legal services is part of the knowledge intensive group of firms.

The second of the three approaches categorizes services based upon the extent to which the production of the service offering can be spatially separated from the
consumption of the service. This occurs where the service is in some way linked to use or consumption of a related product. As you might expect, the extent to which a service can be separated from a related product could have a significant impact on the related firm’s internationalization process.

For instance, a car rental service could have a significant spatial separation between the reservation and delivery/use of the vehicle. Companies like Zipcar.com are completely virtual without any direct personal interaction between the rental company and the clients. The car rental company could therefore easily embrace International Diversification.

At the other extreme could be dental services. All dental services are usually provided in person on the premises. For these types of services, there is no spatial separation. It would be extremely difficult to extend these types of services internationally. See generally Bottewyn, et al. (1986) and Erramilli & Rao (1990).

As applied to legal services, this second approach is a little problematic. Although law firm clients would likely expect highly-customized personal service, they usually would not expect that all attorney work be done in their personal presence. To the contrary, a single lawyer contact could quite easily manage diverse projects actually fulfilled at great distances. The spatial distances could be quite significant. As such, the spatial characteristics of legal services would not be a major impediment to international expansion.

In the last of the three approaches, the categorization of services is based upon the extent of client contact and the extent of customization inherent in the particular service.
(Maister & Lovelock, 1982). See also, (Schmenner, 1986). Using this approach, there are four fundamental categories of services. Services with both low customer contact and low customization are considered “Factory services.” Services with low customer contact but a high amount of customization are considered “job shop” services. In contrast, if there is a high degree of customer contact but a low amount of customization, then the service is considered a “mass service.” Lastly, if the service has both a high degree of customer contact and a high degree of customization, then the service is a “professional service.” (Silvestro & Fitzgerald, 1992), p. 65.

In looking specifically at professional service firms, the traditional structure has been the use of professional partnerships. (Greenwood, Hinings, & Brown, 1990). The distinctive characteristic of this structure is that “ownership, management and operations are fused. A partner is an owner of a firm, and is a key production worker.” (Greenwood et al., 1990), p. 730. A second distinctive characteristic of this structure is that “employment at a national or international office is frequently a temporary contractual arrangement… [with such leading partners usually] returning to the ranks of local offices after … a period of perhaps five or six years.” (Greenwood et al., 1990). P. 730. Of course, typical of all corporate structures, the professional partnership has been forced to adapt in recent years. (Greenwood & Empson, 2003).

In the present evaluation, law firms undoubtedly use the same governance structure as other professional services. They traditionally have used professional partnerships. The law firms provide knowledge-intensive services that have a location bound component. Law firms are generally “soft firms” to the extent that it is impossible to completely decouple production and consumption of legal services. Moreover, the
provision of legal services involves a high degree of customer interaction as well as a high degree of customization. Clearly, legal services constitute some form of “professional service.”

We also know that “professional services” constitute “extreme examples of knowledge intensity.” (Von Nordenflycht, 2010), p. 155. Consistent with all knowledge-intensive firms, professional service firms therefore must have “the capacity to solve complex problems through creative and innovative solutions”. (Alvesson, 1993), p. 1000. However, this raises the rather obvious question of what exactly are “professional services and how can they be distinguished”? These questions are addressed in the next section.

**Distinguishing Among the Different Types of Professional Services.**

In the fourth of five sections in the literature review, we examine how to distinguish between the different types of professional services. Importantly, it is necessary to realize that many scholars have used the term “professional service” or “professional service firm” without any definition. (Von Nordenflycht, 2010). Others have simply referenced varying lists of exemplary “professional services” ranging from accounting, law, and consulting to such things as executive recruiting, talent agencies, fashion design, hospitals, and social work agencies. (Von Nordenflycht, 2010), p. 156. Across these different services, there is a startling amount of heterogeneity. (Malhotra & Morris, 2009).

As a starting point, one definition of “professional services” that is particularly useful is as follows:
Professional services: organizations with relatively few transactions, highly customized, process-oriented, with relatively long [customer] contact time, with most value added in the front office, where considerable judgment is applied in meeting customer needs. (Silvestro & Fitzgerald, 1992), p. 73.

The advantage of this definition is that it expressly distinguishes the value-adding feature of front office contact from potential back office services. However, additional distinctions are informative.

In distinguishing between different professional services, it has been proposed that professional service firms can be distinguished based upon the varying degrees of: knowledge intensity, capital intensity and the extent of a professionalized workforce. (Von Nordenflycht, 2010), p. 157. Importantly, these proposed dimensions are not intended to determine if a service is “professional” or “not professional.” But rather, the proposed dimensions can be used to determine the relative differences between “degrees of professional service intensity, based on the presence of more or fewer of the three characteristics.” (Von Nordenflycht, 2010), p. 157.

“Knowledge intensity” as used by Von Nordenflycht indicates the extent to which the “production of a firm’s output relies on a substantial body of complex knowledge.” (Von Nordenflycht, 2010). This knowledge is embodied within an “intellectually skilled workforce” that extends to its frontline workers. (Von Nordenflycht, 2010), p. 159. This is NOT referring to organizational knowledge. It relies upon the cumulative effect of individual knowledge.

According to Von Nordenflycht, two key challenges result from high knowledge intensity. One involves the challenge of retaining and directing an exceptionally skilled workforce. This is referred to as the “cat herding” problem. (Von Nordenflycht, 2010), p.
The other challenge is the difficulty that non-experts have in evaluating the quality of the services that are provided. This is referred to as the “opaque quality” problem resulting from knowledge asymmetry. (Von Nordenflycht, 2010), p.161.

Clearly, legal services require a significant amount of knowledge intensity. This partially explains the old adage that “a lawyer’s time and advice is his stock in trade.” Given this knowledge intensity, it should not be any surprise that the direction and coordination of lawyers presents a significant challenge for all law firms. It also should not be any surprise that the evaluation of legal service quality is almost always a challenge to non-lawyers.

Aside from knowledge intensity, the second dimension of PSF characteristics is the extent to which the service involves “low capital intensity:”

Low capital intensity does not involve significant amounts of nonhuman assets, such as inventory, factories and equipment… Note that low capital intensity is not a necessary implication of knowledge intensity: one can image firms whose production requires both an intellectually skilled workforce and significant nonhuman assets (e.g., hospitals…). (Von Nordenflycht, 2010), p. 162.

There are several important consequences of low in capital intensity.

First, employee bargaining power may increase because the employee skills are more central to the creation of value. This means that firm employees are more mobile and able to defect to competitors or start their own operations if they choose. Firms with this combination of high knowledge intensity and low capital costs must watch all of their valuable human capital “go down the elevator each night… and the firm can’t control whether they come back.” (Von Nordenflycht, 2010), p. 162. Of course, market forces could work the other way. The firm may be able to easily replace existing employees by
Notably, large multinational corporations can do the exact same thing. Many large multinational corporations have hired leading attorneys away from external law firms to access the knowledge at a lower price.

As applied to law firms, the challenges of retaining quality attorneys would seem to align nicely with the combined characteristics of knowledge intensity and low capital intensity. As competition increases, it explains the increasingly common practice of experienced attorneys being recruited by other competitor law firms.

Lastly, services can be distinguished by the extent of there being a “professionalized workforce.” Von Nordenflycht notes that the traditional features of any “profession” are a particular knowledge base, regulation and control, and a unique ideology. (Von Nordenflycht, 2010), p. 163. Since the knowledge aspect is already captured under “knowledge intensity,” this essentially leaves the “professionalized workforce” with two sub-dimensions: professional ideology and occupational self-regulation. (Von Nordenflycht, 2010), p. 163.

The concept of professional ideology relates to the extent that the profession asserts and requires values such as fiduciary obligations, conflicts of interest, “altruistic service”, or trusteeship. (Von Nordenflycht, 2010), p. 163. This distinction is particularly important in examining the difference between those occupations – like lawyers – from similar knowledge intensive and low capital intensity occupations – like management consultants. Lawyers are strictly subject to the professional ideology while consulting
may vary wildly. Again, while the presence of professional ideology make lawyers more professional, this does not mean that management consultants are not professional.

In similar fashion, occupational self-regulation is the remaining characteristic of a professionalized workforce:

Professionalized occupations have strong control over the practice of the occupation. A central association certifies membership into the profession, based on demonstrated expertise and adherence to the ethical code. And in the archetypal profession this certification is backed by the state such that no one can legally practice the profession without certification by the association. (Von Nordenflycht, 2010), p. 164-64.

As is hopefully evident from the quote above, the “archetypal profession” is actually the legal profession. Other scholars have even described law firms as the “canonical” examples. (Zardkoohi et al., 2011).

An alternative means of distinguishing among the different types of professional service firms was also presented by Malhotra & Morris (2009). These authors utilized a sociology of professions perspective to distinguish the professions based upon three different dimensions than Von Nordenflycht: “knowledge, jurisdictional control and client relationships.” (Malhotra & Morris, 2009). The sociology of professions perspective is based upon the view that professions are “occupationally distinctive because of their control and use of what is socially constructed expert knowledge.” (Malhotra & Morris, 2009), p. 897 (emphasis added).

The first dimension, “the nature of knowledge,” is based upon the extent to which the knowledge possessed by the particular profession is normative, technical or a mixture of both. (Malhotra & Morris, 2009), p. 902. This, in turn, has an impact on the manner
and extent to which the knowledge can be readily evaluated. This also has an impact upon both the tasks conducted by the respective professions and the organizational structures commonly adopted. (Malhotra & Morris, 2009)

Normative knowledge, which is typical of the legal profession, is focused upon the judgement to determine the “correct” application of statutes, regulations and common law to the specific matter. (Malhotra & Morris, 2009). Professional traditions and expectations guide the largely individual interpretation and application of “encoded legal knowledge.” (Malhotra & Morris, 2009; Robertson, Scarbrough, Swan, & Scarbrough, 2003). However, the evaluation of quality and performance is often difficult and obscure. “Law’s normative knowledge base is compatible with low levels of hierarchy, high levels of task autonomy, high decentralization of authority, and high consensus in decision making, resulting in a predominantly professional form of organization.” (Malhotra & Morris, 2009), p. 904.

At the other extreme is technical knowledge, which is typical of the engineering professions. Technical knowledge is focused upon the application of well-established “formulas and processes.” (Malhotra & Morris, 2009). This also includes systematic project management with relatively transparent performance measures. This enables greater bureaucratic monitoring and control. Engineering firms are “likely to be supported by the highest levels of hierarchy, relatively less task autonomy, and a balance between centralization (firm level) and decentralization (project level), resulting in a more bureaucratic form.” (Malhotra & Morris, 2009), p. 905.
Of course, other occupations – like auditors – can possess a combination of the two types of knowledge. The extent and mixture of normative and technical knowledge has implications for the management, organizational structure and evaluation of performance of the respective profession.

Beyond differences in knowledge, the second dimension that distinguishes the different types of professional services is jurisdictional control. In this regard, “jurisdiction” relates both to the geographic boundaries for a specific profession as well as the tendency of the profession to clearly define and defend an area of work from incursions by other professions. This second aspect of jurisdiction is known as the extent of “social closure.” (Malhotra & Morris, 2009), p. 907.

The professions with high social closure are those that occupy occupational areas that are clearly defined, materially attractive, successfully defended from other occupations providing similar services. (Malhotra & Morris, 2009). In this regard, the practice of law is considered to possess a high degree of social closure. The practice of law is commonly regulated by organizations sanctioned by one or more governmental entities. In fact, the unauthorized practice of law can sometimes even be punished by criminal sanctions.

Professions with low social closure are those that are not as clearly defined or successfully defended from non-members of the profession from practicing the same or similar services. In this regard, the practice of engineering is considered to possess a low degree of social closure. This arose because engineering emerged from several different
traditions. This made it difficult for engineering to “establish a unified professional control of a well-defined jurisdiction.” (Malhotra & Morris, 2009), p. 910.

Similar to social closure, geographic boundary control also creates barriers between different types of professions. However, this type of jurisdictional control is more spatially defined. (Malhotra & Morris, 2009). As noted above, the legal profession has routinely been regulated by organizations sanctioned by one or more governmental entities. Inherent in the connection with governmental entities is the geographic limitation of the given government. In this regard, the culture, history and traditions of the governmental affiliation often tend to further reinforce the geographical limitations of the profession. Consequently, “a majority of law firms operating globally maintain their autonomy in their national jurisdictions but become a part of a network of relationships with firms in other jurisdictions.” (Malhotra & Morris, 2009), p. 911. See also (Johanson & Vahlne, 2009; G. Morgan & Quack, 2006).

In contrast, other professions, such as auditing, “possess forms of knowledge that are more or less universal, usually based on scientific laws.” (Malhotra & Morris, 2009), p. 910. These professions tend to utilize broader geographic jurisdictional organizational structures. (Malhotra & Morris, 2009). This provides for a more uniform international structure.

The last dimension used by Malhotra & Morris to distinguish between types of professional service firms is based upon the frequency of face-to-face interactions between clients and service providers. (Malhotra & Morris, 2009), p. 912. “The extent to which the client interacts face-to-face with the service provider has a direct impact on
the geographic dispersion of assets indicated by the number and spatial distribution of offices of the professional firm.” (Malhotra & Morris, 2009), p. 914. In the instance of law firms, the provision of legal services is not so much dictated by the need for face-to-face interactions with clients as understanding the client’s legal needs within a particular legal context. (Malhotra & Morris, 2009). It is the legal context that is geographically linked to jurisdiction more than need for face-to-face interaction. (Malhotra & Morris, 2009).

In applying the categorizations and dimensions suggested by both Von Nordenflycht and Malhotra & Morris, it is clear that law firms are a unique subset of professional service firms. Consistent with Von Nordenflycht, the practice of law is conducted only by attorneys with the extensive education, training and licensure. The capital necessary to practice is exceptionally low with barely any need for inventory, factories or equipment. This has become even less of an issue as technology has revolutionized both transportation and communication. Similarly, the legal workforce is highly professionalized with the ability to practice of law regulated by bar associations that are sanctioned by the state.

Consistent with Malhotra & Morris, the knowledge used by law firms is largely normative and often closely linked to the jurisdictional considerations of the law that the firm practices. In this regard, the licensing of the practice of law is inherently local in nature. Moreover, the legal profession has a high degree of social closure that reinforces the geographic limitations of law firm practices. This is not changed much by virtue of any insurmountable needs for face-to-face communication with clients.
Taken as a whole, it should also be relatively clear why the International Diversification of U.S. law firms would involve the interaction between such core firm resources as Human Capital, the deployment strategies of Human Capital (through both Leverage and Service Diversification) and the international Reputational Capital of the firm. The knowledge intensity of law firms inherently places Human Capital at the center of the organization. In turn, the management of this Human Capital is inherently people-centered and closely linked to firm organizational strategies like firm Leverage and Service Diversification. Moreover, due to the opaque nature of legal services and high degree of uniqueness, the Reputational Capital of the firm also would be expected to play a major role in the ability of law firms to expand internationally. Consequently, in the next section we discuss how each of these firm resources conceptually relate to the international diversification of U.S. law firms.

**Key Firm Resources And International Diversification**

In this last of the five sections of the literature review section, we discuss how key firm resources relate to the international diversification of law firms. Having looked at some of the broader theories, it is now time to more specifically examine the theoretical underpinnings of the current research. This will entail examining the literature on International Diversification, Human Capital, Reputational Capital, Leverage, and Service Diversification. Each will be examined more closely in the following sections.

**International Diversification**

As best as can be determined, the use of the term “international diversification” within the international business context originated with Alan Rugman as part of his 1974 Ph.D. dissertation in economics. (Rugman, 1975), p. 571, footnote 10. Just before this,
there were several articles in the American Economic Review discussing the
“international diversification” of investment portfolios – but not business operations.
(Grubel, 1968; Levy & Sarnat, 1970). However, both Grubel and Levy & Sarnat were
specifically cited by Rugman in his 1976, JIBS Decade Award winning article entitled
“Risk Reduction by International Diversification.” (Rugman, 1976). In fact, Rugman
expressly thanked Grubel for “helpful advice” with Rugman’s 1975 article “Motives for
Foreign Investment: The Market Imperfections and Risk Diversification Hypotheses.”

The basic gist of Rugman’s use of “international diversification” was that,
completely separate from the market imperfections theories, internationalization also
could provide a risk-diversification opportunity. (Rugman, 1975, 1979). To some extent,
Rugman’s risk-reduction theory could be seen as an extension of one of Hymer’s
secondary arguments in his 1960 dissertation. Recall that, pursuant to Hymer, one type
of FDI (Type 1) is similar to portfolio investments and are simply based upon reducing
this further. However, his extension is beyond the scope of the current research.

Nonetheless, although Rugman may have technically been the first to link the
exact words “international diversification” to foreign direct investment, it is clear that
Rugman did not create the concept. Setting aside Hymer, in 1968 Fouraker & Stopford
beautifully stated that “international business activity is a form of diversification.”
(Fouraker & Stopford, 1968), p. 48. See also (M. Hitt, Tihanyi, Miller, & Connelly,
2006a). Clearly, international diversification and product diversification share common
foundations.
Indeed, at about the same time as Fouraker & Stopford, Vernon was proposing the international product life-cycle theory that clearly included diversification components and Chandler was looking at corporate diversification behavior. (Chandler, 1966; Vernon, 1966). All of the articles clearly involved the consideration of expanded business operations across national boundaries – international diversification.

So what is “International Diversification”? For the purposes of the current study, International Diversification is a strategy whereby a firm chooses to expand operations by allocating firm resources across national boundaries. International Diversification concerns foreign direct investment activity “across country borders into geographic locations (e.g. markets) that are new to the firm.” (Capar & Kotabe, 2003; M. A. Hitt et al., 1994). As such, it should not be any surprise that “international diversification has been studied from a broad range of theoretical perspectives, resulting in debates regarding its fundamental characteristics and appropriate measurement.” (M. Hitt et al., 2006a), p. 833. See, e.g. (John Cantwell et al., 2009; J Dunning, 1988; JH Dunning & Rugman, 1985).

Conceptually, “internationalization” is sometimes subject to overlapping, but distinct, meanings. (Coviello & McAuley, 1999). See also (Dörrenbächer, 2000), p. 119. For instance, internationalization has been studied from FDI theories, international stage models, and the network perspective. (Coviello & McAuley, 1999; Johanson & Vahlne, 1990). These differing perspectives have sometimes introduced subtly different meanings and led to inconsistent and confusing results between studies. (Sullivan, 1994).
In the current study, International Diversification is intended to be used as a structural indicator relating to foreign activities. (Dörrenbächer, 2000; Ramaswamy, Kroeck, & Renforth, 1996). It directly relates to the broader theories discussed previously. For instance, pursuant to Coase’s Theory of the Firm, it is to be expected that international diversification represents an economizing decision. (Coase, 1937). See also (P. Buckley & Casson, 1976; J Dunning, 1988). The firm expects to be better off by virtue of internationalizing than if the firm were to simply refer clients to foreign service providers. Otherwise, the firm would rely upon arms-length market transactions to support the provision of international legal services.

Moreover, International Diversification balances concerns about the potentially opportunistic behavior by foreign law firms against the cost of investment into foreign markets. (Williamson, 1981). This decision may also be driven in response to uncertainty and bounded rationality as to the choice. (March, 1978).

Pursuant to Penrose, it is expected that the decision to expand beyond national borders will represent the decision by the firm to efficiently allocate slack resources. The decision to locate human capital in a geographically remote location would be expected to represent a significant challenge. Especially for professional service firms, the potential loss of human capital – either to existing domestic operations or to the whole firm - would pose a serious issue. (Spender & Grant, 1996). The mere distant proximity – and loss of ready access to a knowledge worker – would present a challenge in all instances.
Of course, one of the primary reasons for the scholarly interest in International Diversification has been due to the expected theoretical relationship with firm performance. See e.g. (Ghoshal, 1987; M. Hitt, Hoskisson, & Kim, 1997; W. C. Kim, Hwang, & Burgers, 1989; W. Kim, Hwang, & Burgers, 1993). The underlying premise is that International Diversification is based upon the profit seeking activities of a firm through the “exploitation of foreign market opportunities.” (J Dunning, 1988; Rugman, 1979). For some, International Diversification is considered to be a growth strategy with a close relationship to firm profitability. (Capar & Kotabe, 2003; Chandler, 1962). As such, International Diversification is considered to be a strategic option rather than a necessity. (Lu & Beamish, 2001).

One would expect that there would be some form of consensus regarding the basic relationship between international diversification and firm performance. However, “one” would be wrong. Some studies have shown a negative relationship. See, generally, (Capar & Kotabe, 2003; Contractor et al., 2003). Even where a positive relationship has been shown, the specific form of relationship remains unclear. (D. M. Brock, Yaffe, & Dembovsky, 2006; D. M. Brock & Yaffe, 2008; M. Hitt et al., 1997; Michael A Hitt, Bierman, Uhlenbruck, & Shimizu, 2006a). It also is unclear whether or not omitted mediating variables – like implementation - may be adding unnecessary complications. See generally, (D. M. Brock & Yaffe, 2008).

Under these various circumstances, it should not be all that surprising to find inconsistent research results relating International Diversification to firm performance. (Capar & Kotabe, 2003; Gomes & Ramaswamy, 1999). In fact, at least one observer has stated that “despite a wealth of empirical research, whether and how international
diversification impacts firm performance remains one of the major unresolved research questions in the fields of strategy and international business.” (Wiersema & Bowen, 2011), p. 152. See also (Cardinal, Miller, & Palich, 2011; Contractor, 2012). Underlying it all, there can be – and often are - different motivations for firms to expand abroad. As such, there is more than one way where engaging in International Diversification can lead to increased profitability for the firm. Listed below are just some of the different potential motivations.

Firms can realize economies of scale by accessing an international market. (R. Caves, 1971). Firms may be benefiting from getting access to resources and markets that could not be achieved in arms-length market transactions. (Hennart, 1982). Firms also could benefit by closing market access. (Bain, 1956; Hymer, 1960). Other firms could simply be deploying slack resources in accessing foreign markets. (Teece, 1982). Yet other firms could be spreading their market risks across various countries. (Rugman, 1975, 1979). Or, as suggested by Gaedeke (1973), the firms may simply be pursuing a defensive, client-following, strategy.

**Human Capital**

Having discussed International Diversification, it is now necessary to discuss the literature regarding the independent variables. In this regard, there is no question that the most central resource for all law firms is Human Capital.

As observed by Kiker in 1966:

“the concept of human capital… is by no means new *** Economists who considered human beings or their skills as capital include such well-known names in the history of economic thought as Petty, Smith, Say, Senior, List, Von...

However, within modern thought, the renewed conceptualization of Human Capital can be directly attributed to Theodore Schwartz. (Schultz, 1971), p 1.

At the 1960 meeting of the American Economic Association, Schultz took issue with the failure of economists to view education as an investment – rather than simply as an expenditure related to consumption of discretionary capital. (Schultz, 1971), p 1:

What economists have not stressed is the simple truth that people invest in themselves and that these investments are very large *** The failure to treat human resources explicitly as a form of capital, as a produced means of production, as the product of investment, has fostered the retention of the classical notion of labor as a capacity [only] to do manual work requiring little knowledge and skill, a capacity with which, according to this notion, laborers are endowed about equally. This notion of labor was wrong in the classical period and it is patently wrong now. (Schultz, 1971), p. 3.

In this way, Schultz intrinsically linked the modern concept of Human Capital to the possession and deployment of knowledge and experience.

Not long after Schultz, Becker began his own in-depth analysis of the relationship between education and income:

Some activities primarily affect future well-being; the main impact of others is in the present. Some affect money income and others psychic incomes, that is, consumption. Sailing primarily affects consumption, on-the-job training primarily affects money income, and a college education could affect both…. These activities are called investments in human capital. (G. S. Becker, 1993), Introduction To The First Edition (1964).

Unlike other forms of firm capital, like physical or financial capital, Human Capital cannot be separated from the individual possessor. (G. S. Becker, 1993; G. Becker, 1962). The individual is central.
It is specifically for this reason that Human Capital is so central to professional service firms. For professional services – like those offered by law firms – Human Capital is “the fundamental resource endowment of [the firm].” (R. Javalgi & Grossman, 2014). See also (Kor & Leblebici, 2005). “Human capital resources include the training, experience, skills, relationships, and insight of individual managers and employees in a firm.” (R. R. G. Javalgi & Grossman, 2014), p. 289. In fact, strategic choice and firm performance are largely dependent upon the firm’s available Human Capital. (Finkelstein & Hambrick, 1996). See also (Michael A Hitt, Bierman, Shimizu, & Kochhar, 2001).

As to professional service firms, there is agreement that Human Capital constitutes the core firm resource that enables the firm’s professionals to actually produce professional services. (Swart, 2006), p. 140. See also (Pennings, 1998). As such, Human Capital is “a critical intangible resource that enables professional service firms to achieve sustainable competitive advantages.” Hitt, et al (2001), p. 14. See also (Kor & Leblebici, 2005). Regardless of which strategy a professional services firm chooses to pursue, there will be a need to consider the usage of, and impact upon, firm Human Capital.

Human Capital is directly related to the resources available for deployment by the firm in pursuing International Diversification. (R. G. Javalgi & Todd, 2011), p. 1005. See also (Michael A Hitt et al., 2006a). This is especially true of law firms, given the central role played by the knowledge and judgment of the firm’s attorneys. Consequently, one of the core considerations impacting the International Diversification behavior of U.S. law firms is the Human Capital possessed or readily available to the firm. Perhaps more importantly, the International Diversification behavior of U.S. law firms will inherently link the allocation of the firm’s Human Capital to interactions with other firm resources.
**Reputation**

While Human Capital is a firm resource that is predominantly under the internal control of the firm, Reputational Capital is at the other extreme. Reputation is “a perceptual representation of a company’s past actions and future prospects that describe the firm’s overall appeal to all its key constituents when compared to other leading rivals.” (C. J. Fombrun, 1996), p. 72. See also (R. Javalgi & Grossman, 2014). Consequently, Reputation is part of the relation of the external market or society outside the firm, to the internal life of the firm. (Stinchcombe, 1965), p. 142. See also (Brown, 2014).

Regardless of whether a firm is trying to overcome the “liability of newness” or “liability of foreignness,” one of the initial key challenges for the firm is “selling the idea of one’s reputational score in the marketplace.” (Brown, 2014). This is because consumers within new markets quite often rely on firm reputations when selecting firms or products. (C. Fombrun & Shanley, 1990).

The core reason for the importance of Reputation for firms in foreign markets is information asymmetry. The potential consumers have little means to directly evaluate the quality of the new offering. This is especially true of professional services due to their opaque nature. (Rosenbaum & Madsen, 2012; Von Nordenflycht, 2010). Reputational Capital is especially important to professional service firms since the quality of legal services is generally beyond the competence of the firm client. (Greenwood, Li, Prakash, & Deephouse, 2005), p. 663. As such, many law firms compete on indirect indicia of quality through emphasis on branding and reputation. (D. M. Brock et al., 2006).
In this regard, “reputation mitigates inefficiencies associated with information asymmetries by providing an informative signal of quality.” (McDonald & Slawson, 2002), p. 633. See also (Weigelt, 1988), p. 447. A “positive reputation is a resource leading to competitive advantage.” (Deephouse, 2000). Indeed, the mere maintenance of international operations may enhance a firm’s reputation. (D. M. Brock & Yaffe, 2008). A firm’s reputation may also increase the recognized ability of the firm to engage in international transactions. (JA Flood, 2007), p. 38.

As noted by Napapiet & Ghoshal, reputation is a form of social capital that provides a unique benefit to the firm. (Nahapiet & Ghoshal, 1998), p. 243. Reputational Capital is a “key intangible resource that [enables leveraging] competitive advantage.” (Petrick, Scheier, Brodzinski, Quinn, & Ainina, 1999), p. 58. Reputation is the perception “about an organization’s ability to create value relative to competitors.” (Deephouse, 2000; Rindova, Williamson, & Petkova, 2005).

**Leverage**

Beyond the basic amount and quality of Human Resources, and the externally-centered role of Reputational Capital, there are two remaining concepts that relate to the international diversification strategies adopted by firm management. The first of these topics is Leverage.

Effective management of resources is fundamental to the performance of any firm. (J. Barney, 1991; Penrose, 1959). It is not just the amount and quality of the firm
resources but how firm acquires, develops, disposes and deploys its resources to
determine the firm’s capabilities. (Kor & Leblebici, 2005; Mahoney & Pandian, 1992).
In this regard, the “proper deployment of human resources involves delegating less
complex work by expert resources (e.g., partners) to less experienced employees (e.g.,
associates).” (Kor & Leblebici, 2005), p. 969. This is generally referred to as Leverage.
(Maister, 1993). Leverage “represents the structure of the primary human capital” in law

For professional service firms, it is not just the location and numbers of
individuals that matters. The firm must also consider the existing and prospective unique
knowledge and experience of the individuals in determining how and where they should
be deployed. (Michael A Hitt et al., 2001) This has ramifications as to firm geographic
diversification (both domestic and international); service diversification (as discussed in
the next section); and the relationship between the number of individuals with extensive
expertise and those with less expertise. In dividing the attorneys based upon degrees of
expertise, the distinction has traditionally been to distinguish between Partners and
Associates.

Partners are licensed attorneys and the source of extensive legal and firm
knowledge. Partners hold some claim to the profits and retained earnings of the firm. (P.
Sherer, 1995), p. 671. In contrast, Associates are also licensed attorneys but are usually
employees with less knowledge and experience. (P. Sherer, 1995). The fundamental
question for the law firm is therefore what “mix” of partners and associates to maintain.
At one extreme, the firm could recruit only experienced partners. Each partner could specialize in a unique area of the law. However, there would be no matching of lawyer qualifications with the skills required by the client matters. Assuming more advanced matters existed, the partner would still need to spend time resolving the easier matters. This would be economically suboptimal. Although the easy matters would be handled expertly, proper delegation to less experienced attorneys would likely provide more economically efficient services. Furthermore, a partner-only structure would result in little generation of firm-specific knowledge. Firm matters requiring multiple attorneys would be difficult to serve unless there just happened to be multiple partners with matching skillsets. Even then, the cost of the services provided would be relatively expensive.

As such, if the firm only has partners, then the firm profitability – and individual partner income – would likely be diminished relative to other leveraged law firms. (P. Sherer, 1995). Given the additional value created in more leveraged competitors, the partner-only structure would encourage loss of the most qualified partners to lateral hiring by competitors. Alternatively, the firm would likely decompose into a pooling arrangement between sole practitioners. (Gilson & Mnookin, 1985).

At the other extreme, the firm could have only one experienced partner, and all other attorneys in the firm could be associates. Just as at the other extreme, this solution would also suffer from the failure to match attorney qualifications with the skills required by the client matters. In this second extreme, due to the lack of a broad array of experienced specialist partners, the firm would be forced to offer a narrow service offering or only handle “easy” matters. The firm would be limited to the ability of the
single partner to deploy his or her limited knowledge base. Firm capacity would be limited by the capacity of the single partner. This would adversely impact the ability of the firm to deliver unique value to its clients. See, generally, (Chang & Birkett, 2004). It would also limit the ability of the firm to provide services that increase client dependence upon the specific firm’s services. (Greenwood et al., 2005).

Beyond the limited capacity for advanced legal matters, the “super-leveraged” strategy would provide little incentive for associates to remain with the firm. Although some advanced work might “spillover” from the single overworked partner, the prospect of never achieving partnership status would encourage the associates to continually search for other opportunities. As such, the experience offered to its associates generally would be less valuable than jobs at less leveraged firms. See generally, (Pennings, 1998).

Of course implicit in both extremes along the leverage continuum is the recognition that “law firms with different human capital structures also have different organizational capabilities.” (P. Sherer, 1995), p. 672. The challenge for the law firm therefore is to combine the proper number and quality of partners with the proper number and quality of associates to achieve the optimal organizational capabilities. Making matters even more challenging, firm International Diversification presents yet an additional level of complexity. The potential loss of valuable knowledge workers – of either the partner or associate rank – from the domestic offices would need to be balanced against the needs of a geographically remote foreign office.
Service Diversification

Service Diversification refers to the variety of legal practice areas offered by the firm. It is important to recognize that service diversification, leverage and international diversification are all closely related. “Both international and product diversification play key roles in the strategic behavior of large firms.” (M. Hitt et al., 1997), p. 767. See also (Fouraker & Stopford, 1968), p. 48. From the firm’s perspective, diversification can be achieved internationally (across countries), across services, or both. (Kor & Leblebici, 2005), p. 970.

Pursuing a broad Service Diversification strategy can enable a firm to achieve economies of scope as well as benefit from the problems inherent in information asymmetries and service opacity. (Nayyar, 1993). Rather than a client needing to qualify separate firms for different legal service needs, the client could simply select one. As such, service diversification may improve the “total package” of service offerings to potential clients. (Michael A Hitt et al., 2001), p. 17. At the other extreme, a narrow focus in service offerings may enable a firm to communicate unique competence. This results in at least two distinct strategies regarding service diversification:

Two commonly identified strategies within the professional services literature are the narrowly focused firm, commonly referred to as the specialized ‘boutique,’ and the more diversified practice. (Greenwood et al., 2005), p. 664. See also (P. Sherer, 1995).

Boutique firms specialize in a narrow field of law – such as intellectual property law only. This enables the firm to refine expertise within a clearly defined subject matter. As such, the boutique practice permits for greater internal focus with clearer delineation of attorney activities and easier delegation and training of attorneys. (P.
Sherer, 1995), p. 676. It also presents less of a management challenge for the firm’s partners. Presumably, this increases the ability of the firm to leverage its associates without any adverse effect on the firm’s quality of services.

In contrast, “full-service” firms provide a broad array of service offerings. In this way, the full-service firms provide their clients with the convenience of a single service provider; potential recognition of economies of scope; and cross-selling opportunities. The success of a full-service strategy requires more than diversity of practice offerings. A full-service strategy needs to link “related” services that support a consistent reputation. (Nayyar, 1993), p. 569. See also (Greenwood et al., 2005), 664. Moreover, for full-service firms, the distribution of resources across practice areas needs to be balanced. Otherwise, the full-service firm will appear to lack the ability to successfully serve all areas. (Greenwood et al., 2005).

Additionally, the full-service firms increase the demands upon the firm’s partners. Diversification into additional service areas increases the managerial demands of partners in order to be able to coordinate the increasingly complex service offerings. (Kor & Leblebici, 2005), p. 971. This likely reduces the ability of the firm to leverage its associates.

Of course, the selection of firm Service Diversification strategy is more complex than simply selecting “narrow” or “broad”. The ability of a firm to pursue Service Diversification may depend upon the specific services being offered, the firm’s leverage, and the human capital possessed by the law firm partners. (Kor & Leblebici, 2005), p. 971. Perhaps more importantly, if the Leveraging and Service Diversification of the firm
are done incorrectly, the quality of the firm’s service offerings may be adversely effected. (Kor & Leblebici, 2005). This would negatively impact the firm’s performance and undermine the intended firm goals for pursuing International Diversification.

**Literature Review Summary**

At this point, we have completed the review of the relevant literature. We began with the historical perspective of when, how and why U.S. law firms approached International Diversification. We then proceeded to briefly look at a handful of the central theories explaining how and why firms internationalize. We then briefly looked at the potential differences between service firms and non-service firms. We also looked at the differences between professional services. Lastly, we looked at the specific aspects of a theoretical model involving International Diversification, Human Capital, Reputational Capital, Leverage and Service Diversification.

In the next chapter we apply the specific aspects of a theories discussed so far to a specific conceptual model with related hypotheses.
CHAPTER III

CONCEPTUAL MODEL AND HYPOTHESIS DEVELOPMENT

At its most fundamental level, the management of professional service firms involves the management of firm resources. (J. B. Barney, 2001; J. Barney, 1991; Penrose, 1959). This includes an effort by the firm to economize in light of the external market conditions. (Coase, 1937). It also involves tailoring the bundle of firm resources and capabilities to complement the firm’s chosen strategy. (J. Barney, 1991; Michael A Hitt et al., 2001). It is within this context that firm’s pursue – or decide not to pursue – international diversification. See, generally, (Wiersema & Bowen, 2011). However, the process of pursuing international diversification and tailoring firm resources to match is inherently based upon the interaction between core firm resources.

For these reasons, the core focus of the present conceptual model on U.S. law firm International Diversification is on the interactions between Human Capital, Reputational Capital, Leverage and Service Diversification. None of these resources are managed in a vacuum – without regard to the interactions with other resources. Therefore, one of the core challenges for U.S. law firms pursuing International Diversification is to manage these interactions. This leads to the conceptual model on the following page:
As would be expected, the main effects are Human Capital, Reputational Capital, Leverage and Service Diversification. However, the greater challenge is understanding the relationships between these main effects.

**Relationship Between Human Capital and Reputation**

As stated previously, Human Capital is “the fundamental resource endowment of [the firm].” (R. Javalgi & Grossman, 2014). See also (Kor & Leblebici, 2005). This is because the “primary asset providing a base for professional service delivery is knowledge.” (Michael A Hitt et al., 2006a). Human Capital is the “coin of the realm” for
professional services. Without Human Capital, no law firm would exist – regardless of
the strategy pursued.

In considering interaction effects with Human Capital, we would readily expect
that “[s]ome [firm] capabilities are based on firm-specific knowledge and others are
valuable when integrated with additional individual capabilities and specific firm
resources…” (Michael A Hitt et al., 2001), p. 14. Stated otherwise, it should be expected
that there will be some sort of interaction between most – if not all - of a firm’s critical
resources. At the center will likely be the level of Human Capital possessed by the firm’s
partners.

An additional core intangible resource is the firm’s capability for establishing
relationships with potential clients. The relationships are “one of the most important
assets held by professional service firms.” (Michael A Hitt et al., 2006a), p. 1140. One
way to consider this capability is to examine how a firm maintains and expands the
broader awareness of a firm within the potential marketplace. This is Reputational

Reputation is “the external stakeholders’ consensual ranking of a firm’s track
record.” (Sheehan & Stabell, 2010). See also (C. J. Fombrun, 1996; Spar, 1997).
Reputation is “a well-recognized intangible resource for any organization.” (R. Javalgi &
Grossman, 2014), p. 289. It is routinely a basis upon which corporations make decisions

Reputational Capital is all the more important to professional service firms by
virtue of the inherent invisibility and intangibility of professional services. (D. Brock &
Alon, 2009), p. 53. See also (R. Javalgi & Grossman, 2014). Reputation is especially important to professional service firms due to “the intangibility of the service and the importance of the professional.” (Greenwood et al., 2005), p. 663. See also (JA Flood, 2007).

In this way, Reputational Capital is “a perceptual representation of a company’s past actions and future prospects that describe the firm’s overall appeal to all its key constituents when compared to other leading rivals.” (C. J. Fombrun, 1996), p. 72. See also (R. Javalgi & Grossman, 2014). As such, although Reputational Capital is necessary for a firm to benefit from International Diversification, it is not sufficient. Without sufficient Human Capital, the Reputational Capital will only signal an illusion of firm opportunity. Absent Human Capital, the firm will not have the capacity to actually deliver the services needed by the firm clients.

Of course, implicit in the relationship between Human Capital, Reputational Capital and International Diversification is the assumption that firm performance is positively related to the extent of International Diversification. Based on this, we propose the following hypotheses:

H1: The interaction between Human Capital and Reputational Capital is positively related to the degree of international diversification of U.S. law firms. Specifically: H1(a), At higher levels of Human Capital, the level of Reputational Capital will positively facilitate a higher level of International Diversification; and H1(b), At lower levels of Human Capital, Reputational Capital will have little impact on International Diversification.

**Relationship Between Human Capital and Leverage**

Since Human Capital is core to all professional service firms, and since these resources are necessary to access benefits from International Diversification, it is
expected that there will be a core requirement for high Human Capital in order for there to be the ability to benefit from Leverage. Recall that Leverage involves the “proper deployment of human resources [by] … delegating less complex work by expert resources (e.g., partners) to less experienced employees (e.g., associates).” (Kor & Leblebici, 2005), p. 969. If the firm is initially lacking in Human Capital by its partners, then there will be less ability of the firm to either delegate to less experienced attorneys or pursue International Diversification.

At the same time, it would be expected that the greater the quality of firm Human Capital, the greater the ability of the firm to use Leverage, and therefore the greater the ability of the firm to deploy resources abroad. See, generally (Michael A Hitt et al., 2001). Once again, implicit in the relationship between Human Capital and Leverage is the assumption that firm performance is positively related to the extent of International Diversification. Based on this, we propose the following hypotheses:

H2: The interaction between Human Capital and Leverage is positively related to the degree of international diversification of U.S. law firms. Specifically: H2(a), At higher levels of Human Capital, the level of Leverage will positively facilitate a higher level of International Diversification; and H2(b), At lower levels of Human Capital, Leverage will less positively impact International Diversification.

Relationship Between Human Capital and Service Diversification

As noted by Hitt et al., 2001, “often service firms achieve growth through diversification into [both] new services and into new geographic areas.” (Michael A Hitt et al., 2001), p. 16. See also (M. Hitt et al., 1997). Quite often, the pressures for service and geographic diversification originate with clients expecting the provision of full services at the national and international level. (Howard, 1991). At the same time, the effort to diversify may result from the firm attempting to spread costs over a larger base
and to achieve economies of scale (to the extent possible). (Howard, 1991). See also, (Michael A Hitt et al., 2001; Nayyar, 1993).

Nonetheless, the expansion of firm – either geographically through International Diversification or through the expansion of services - is inherently linked to the availability of adequate Human Capital. (Kor & Leblebici, 2005), p. 971-72. See also (Penrose, 1959). When firms leverage beyond their available human capital their profitability will be hurt. (Kor & Leblebici, 2005). “Managing substantial diversity requires significant management acumen (often gained through substantial experience)… the gestalt of which suggests a complex positive interaction of human capital and firm diversification.”(Hitt, et al. 2001). See also (MA Hitt, Bierman, & Collins, 2007).

Once again, implicit in the relationship between Human Capital and Service Diversification is the assumption that the resulting firm performance is positively related to the extent of International Diversification. Based on this, we propose the following hypotheses:

H3: The interaction between Human Capital and Service Diversification is positively related to the degree of international diversification of U.S. law firms. Specifically: H3(a), At higher levels of both Human Capital and Service Diversification, international diversification will be higher; and H3(b), At lower levels of both Human Capital and Service Diversification, international diversification will be lower.

**Relationship Between Leverage and Service Diversification**

The last interaction in the conceptual model involves the hypothesized interaction between firm Leverage and the level of Service Diversification. Both of these areas are intimately linked – and limited – by the Human Capital of the firm. For instance, increasing the Service Diversification of the firm inherently increases the demands upon
firm partners in acquiring new areas of professional expertise. (Kor & Leblebici, 2005), p. 971. Moreover, the process of communicating with firm clients becomes more complicated as partners attempt to communicate across a broader array of client needs. (Kor & Leblebici, 2005). The requirement for expertise in multiple legal areas also has a consequence of requiring “closer monitoring and coaching of associates by partners.” (Kor & Leblebici, 2005). Consequently, generally speaking, the greater the service diversification of the firm, the lower the amount of Leveraging. (Kor & Leblebici, 2005; P. Sherer, 1995).

This aligns nicely with the firm’s profit seeking goals. “Owing to the large positive main effect of leverage on firm performance, firms achieve highest levels of profitability when they combine high levels of leverage with low levels of service diversification.” (Kor & Leblebici, 2005), p. 976. Based on this, we propose the following hypotheses:

**H4**: The interaction between leverage and service diversification will have a negative effect on the degree of international diversification of U.S. law firms. Specifically: **H4(a)**, At higher levels of both leverage and Service Diversification, international diversification will be lower; and **H4(b)**, At lower levels of both leverage and Service Diversification, international diversification will be higher.
CHAPTER IV

RESEARCH DESIGN AND METHODOLOGY

The purpose of this chapter is to discuss the research design and methodology used to test the proposed conceptual model. This section discusses the data sources, the methodology used in collecting the secondary data, measurement, and statistical techniques.

Data Sources

The data for the current research technically constitutes secondary data. The use of the term “technically” is meant to clarify that the extracted data is almost certainly of a higher quality than if primary data had been independently acquired. Rather than responding to a survey instrument for this project, the firm data was obtained by using responses to a recognized, widely responded to, legal directory. With minimal exceptions, all of the data for the proposed study was extracted using the Martindale Hubbell Law Directory.

Within the practice of U.S. law firms, the preeminence of the Martindale-Hubbell Law Directory is widely recognized and relied upon:

This annual multivolume directory, published by Martindale-Hubbell, Inc. [Now, Lexis Nexis] is by far the most extensive and widely used source of information.
on American attorneys, with more selective coverage of Canadian and other foreign lawyers. (M. L. Cohen, Berring, & Olson, 1989), p. 421.

In fact, at least one article in the American Bar Association Journal went so far as to state that “the names of almost all of the nation’s lawyers appear in the Martindale-Hubbell Legal …” (Harnsberger, 1963), p. 35 (emphasis added).

In explaining why the Martindale Hubbell Law Directory is so valuable as a data source, one recent scholar has commended as follows:

The Martindale directory has been published (in print form) for over one hundred years and is widely known as the legal service’s more comprehensive professional directory. While there is no requirement that firms list, listing in Martindale has become standard practice for virtually all law firms in America. Martindale offers free basic listings for firms and lawyers, offers premium listings for a fee, and charges subscribers for its directories. While sole practitioners and very small firms may not all list, we are confident that the Martindale directory represents a near census of the legal services industry for lawyers in firms of more than a few people. (Baker & Parkin, 2005), p. 1638-1639 (emphasis added).

Within this context, there is little wonder why numerous academic scholars have relied upon the Martindale-Hubbell Law Directory for both authority and data. See, e.g. (Baker & Parkin, 2005; Gaedeke, 1973; Phillips, 2001; Quack, 2012; Quesenberry & Garland, 2003; Silver, 2007; Terry, 2008); (Galanter & Palay, 1991).

Of course, merely because the Martindale Hubbell Law Directory is the best source of law firm data does not necessarily mean that it is without potential limitations. For instance, as noted by Baker & Parking, above, the Martindale Hubbell Law Directory may have a bias against firms with only a few attorneys. (Baker & Parkin, 2005).

Additionally, according to Kotabe, the risks of using external secondary data in international research generally falls into one of five categories: data accuracy, data age,
data reliability over time, comparability of data and lumping of data. (Kotabe, 2001), p. 163. Each of these concerns is addressed in order below.

The first concern, data accuracy, can be broken down further into three subcategories: data problems caused by different definitions or indicators in different countries; differences in resources and sophistication in different countries; and “lack of parity between the purpose for which the secondary data were originally collected and the objective of the research for which the secondary data are being sought.” (Kotabe, 2001), p. 163. However, these concerns are not present in the current data.

In the present research, the research is limited only to the international diversification of U.S. law firms. By limiting the analysis in this way, there should not be any internal data equivalency issues. The present research utilizes a single set of definitions and indicators based upon those firms with a single established origin in the U.S.

Moreover, using the Martindale Hubbell does not present any risk of “lack of parity” between the original data purpose and the objectives of the research. To the contrary, the proposed research purposefully extracted specific firm-level and individual attorney-level data. The individual data was used to calculate additional firm-level data. In this regard, it could be asserted that the comprehensive nature of the Martindale Hubbell Law Directory actually provides a significantly improved accuracy of data than if this information were sought through any primary survey or alternate data acquisition effort. Data accuracy should not be a major concern.
The second problem identified by Kotabe in using secondary data in international business research is the age and frequency of different country data collection cycles. However, since the Martindale Hubbell Law Directory is published annually and since only U.S. based firms are included in the research, this simply is not an issue.

The third problem identified by Kotabe relates to questions of data reliability over time. Since the current study covered a period of fifteen years, there probably were some slight changes in some of the conventions over time. However, the data extracted was overwhelmingly objective in nature with little room for significant variation in reporting over time. For instance, the distinction between equity and non-equity partners has clearly taken on greater meaning over time. However, to the extent that the changes have been noted, every effort has been taken to minimize these concerns in the selection of constructs (discussed later).

Fourthly, Kotabe identified concerns about the comparability of data presented by using secondary data in international business research. However, as noted previously, the decision to limit the research to U.S. based firms only and to use a single directory source minimized this type of risk. The research did not combine data from different sources in different countries. To the contrary, there was a single source of data that includes information regarding both domestic and foreign operations.

Lastly, Kotabe also identified data concerns in those circumstances where the data set was compiled by agencies that “lump” categories of information together. This is often done as a means of summarizing or reducing the complexity of the dataset. However, this simply does not apply to the data extracted from the Martindale Hubbell
Law Directory. None of the data from the Martindale Hubbell Law Directory constitute summaries. To the contrary, all of the data was extracted from the raw directory data and then compiled.

In sum then, it can be stated that the Martindale Hubbell Law Directory represents the best available information on a purposefully tailored research project. Although the directory is a secondary data source, its comprehensive nature presented an accurate and consistent means of capturing the relevant variables.

Methodology Used For Data Collection

The sample frame for identification of U.S. firms maintaining international offices was obtained by using the CD/DVD versions of the Martindale Hubbell Law Directory for the years 1998, 2003, 2008 and 2013. Unfortunately, the CD/DVD datasets could not be directly queried because they were locked with restricted dataset access by Martindale-Hubbell. Moreover, the Martindale-Hubbell data was not structured for direct search within a single firm-level profile. Instead, separate profiles were provided for each office location. As such, the identification of U.S. law firms maintaining foreign offices had to be done indirectly and over a total of six (6) steps.

Step 1: For each year, the extraction of U.S. law firms that maintained international offices was achieved by utilizing a boot-strap sampling technique. The seed search began with a few major international law firms and the locations where they maintained foreign offices. The output resulted in the identification of all additional law firms with offices in the same foreign locations – as well as additional locations where listed law firms maintained foreign offices. This output was then used as the basis for the
next iteration of searching. The process was repeated until no additional firms or locations were identified.

**Step 2:** The list of all firm offices identified in Step 1 was then checked to confirm that each had at least one domestic and one international listing and that each location listed at least one attorney as being resident. Firms that listed offices without any attorneys were removed.

**Step 3:** Having identified the total population of law offices with both domestic and international operations, the next challenge was to systematically determine whether there were sufficient organizational relationships between the offices to consider them to be part of the same firm. Unlike multinational corporations, the vast majority of law firms operate as professional partnerships. Even firms with very similar names can be completely unrelated. At the other extreme, a firm can have a formal relationship with a partnership with a completely separate name that nonetheless effectively operates as a wholly-owned subsidiary. Since there is no single charter number or filing requirement that expressly sets forth the technical relationship between partnership entities, the linkage of firm office listings is especially problematic. Therefore, the challenge was to systematically determine where each pair of offices were sufficiently related to each other to be deemed the equivalent of either a majority owned subsidiary or division of the same firm. Relationships that were relatively minor, such as a mere “affiliation” were discarded. To accomplish this end, a Rubric (see Appendix A) was used to systematically determine whether or not two or more firm offices could be deemed to be part of the same firm. Once distilled, all firms were removed that did not have at least one pair of
related U.S. and foreign offices. For more information on the Rubric and related issues, see Appendix A.

**Step 4:** For each law firm remaining on the list, its home office and nationality was determined. Most indicated the home office by an “*” in one or more of the firm office listings. Several of the remaining firms contained home office and historical information within their firm profile listings. The remaining firms maintained web pages that disclosed their firm histories and/or their home office locations. From this information, a determination was made as to the nationality of the firm. Law firms formed by the merger of at least one U.S. law firm were deemed to remain U.S. law firms as long as some portion of the original U.S. firm’s name remained in the successor firm’s name. For example, Hogan Lovell’s was considered to be a U.S.-based successor to Hogan & Hartson (a U.S. firm) even though Lovell’s was a U.K. firm.

**Step 5:** Once the determination was made as to the nationality of the identified international law firms, each firm was assigned a unique identifier.

**Step 6:** For each law firm, individual attorney biographical data was summarized to generate firm-level data regarding International Diversification, Human Capital, Leverage, Service Diversification and Firm Size. Separate data was accessed to compile the Reputation construct. Where there were multiple entries for any particular attorney, a full-time equivalent (FTE) number was generated to weight the individual attorney’s data across the various offices in which the attorney was listed. Once this information was obtained, firm-level data was compiled for each firm, in each year, for each construct in the model.
In summary, the data collection process was completed in six steps:

1. A boot-strap sampling technique, ultimately converging on a finite number, was used to identify the bulk list of firm offices and cities for each year;
2. Each putative firm was confirmed to have at least one attorney listed as working within the U.S. and at least one attorney listed as working abroad;
3. The Rubric was used to distill the firms down that only had a significant intra-firm relationship between the U.S. and non-U.S. offices.
4. The home office and nationality of the firms was determined;
5. Each firm was then assigned a unique firm identifier; and lastly,
6. The relevant, individual, biographical data was then summarized and average values were calculated at the firm level.

**Measurement**

Having finished examining the data sources and data extraction methodologies, we next discuss how each of the constructs within the Conceptual Model will be measured. First, we begin by discussing the dependent variable, International Diversification. Next, we discuss each of the main effects – Human Capital, Reputational Capital, Leverage, and Service Diversification. Lastly, we briefly discuss the literature supporting the interactions and some miscellaneous measures.

**International Diversification**

As suggested in the conceptual discussion regarding “international diversification,” if there is any agreement as to the proper measurement of internationalization, it is that there is no agreement. As noted by Daniel Sullivan in 1994, “despite its theoretical and practical centrality, estimating the degree of internationalization (DOI) of a firm remains arbitrary.” (Sullivan, 1994), p. 325. See also (Capar & Kotabe, 2003; Coviello & McAuley, 1999).
In response, Ramaswamy, et al. published a comment that largely agreed regarding the continuing measurement problems with “internationalization.” (Ramaswamy et al., 1996), p. 168. However, Ramaswamy, et al. also raised conceptual concerns about the assumed unidimensionality of Sullivan’s proposed solution. (Ramaswamy et al., 1996). In particular, the index measure proposed by Sullivan actually included three different “attributes of internationalization: a structural attribute, a performance attribute, and an attitudinal attribute.” (Ramaswamy et al., 1996). See also (Dörrenbächer, 2000; Johanson & Vahlne, 1990; Sullivan, 1996).

Several years after Ramaswamy, there still was no “general indicator encompassing the whole phenomenon of corporate internationalization…”. (Dörrenbächer, 2000), p. 125. In fact, by 2000, literature had used the following different measurement for structural attributes:

- Number of countries a company is active in
- Number or proportion of foreign affiliates
- Number or proportion of cases of non-capital involvement
- Amount or proportion of foreign assets
- Amount or proportion of value added abroad
- Amount or proportion of sourcing abroad
- Number or proportion of foreign employees

(Dörrenbächer, 2000), p. 120, Table 1. See also (M. Hitt et al., 2006a).

Following the literature, there were several measurements that could have been used as the dependent variable. The one selected was the percentage of attorneys stationed abroad. “A crude measure of the aggregate diversification is the number of manufacturing employees outside the primary industrial activity in which the firm has
been classified.” (Fouraker & Stopford, 1968). “Since the late 1980’s, researchers have studied the phenomenon of international diversification by analyzing the share of operations – sales, assets, subsidiaries, or profits – within the MNE.” (M. Hitt et al., 2006a), p. 833.

Alternatively, the number of countries in which the firm operated was included as part of Models 7 and 8 to see what impact it had in relation to percent of foreign attorneys. However, as a practical matter, there were no other options regarding the use of more “elegant” measures of International Diversification. These limitations were inherent in the data possessed.

**Human Capital**

As noted previously, “[t]he human capital embodied in the partners is a professional service firm’s most important resource. Their experience, particularly as partners, builds valuable industry specific and firm-specific knowledge, which is often tacit. Such knowledge is the least imitable form of knowledge.” (Michael A Hitt et al., 2001), p. 15. See also Napapiet & Ghoshal, 1998. Just as the measurement of International Diversification was limited by the available data, so too was the measure of Human Capital.

In the present model, the measure for Human Capital has only one dimension: the average total experience, in years, of the firm partners. This was calculated by subtracting the year the individual partner graduated from law school from the year of the individual profile (1998, 2003, 2008 or 2013).
For each firm, the value of the years of legal experience for all firm partners was then averaged. Similar to Hitt, et al. (2001), the human capital variable is intended to serve as a “proxy for tacit knowledge.”

**Reputational Capital**

“The first step in constructing a corporate reputation is corporate visibility, that is, the level of public prominence that a company reaches. Many researchers … identify recognition as a key factor in constructing corporate reputation.” (Capriotti, 2009), p 228. Media visibility therefore “affects perceptions of organizations both by the provision of information on specific issues and by introducing availability biases.” (Brammer & Millington, 2005; C. Fombrun & Shanley, 1990). The importance of media visibility is based on two aspects: it facilitates the distribution of and accessibility to the information about the firm, and it reduces the level of uncertainty about the company. Baker, Powell and Weaver (1998), p. 20. See also (Brammer & Millington, 2005), p. 34.

Accordingly, the measure of Reputational Capital was based upon the firms media visibility in global publications for each year. This was done by searching the names of each law firm in the Major World Publications dataset of Lexis/Nexis Academic. Each search was restricted to the specific year in question. Each of the referenced articles was then manually checked to confirm that the article referred to the law firm in question. The total number of references was then totaled. Next, all firms that did not have any observed articles for the year were coded with a value of “1” and the natural logarithm for all firms was calculated. By coding the data without observations as “1”, this gave a natural logarithm value as “0.”
Leverage
The third independent variable is “leverage” and is intended to represent “the structure of the primary human capital” in the firm. (Michael A Hitt et al., 2001), p. 19. See also (Samuelson & Jaffe, 1990). Traditionally, leverage has been defined as the ratio of associate attorneys to partners. (Samuelson & Jaffe, 1990), p. 193. However, there are other variations. See also, (Michael A Hitt et al., 2001), p. 19; (P. Sherer, 1995), p. 679, (P. D. Sherer & Lee, 2002).

In recent decades, there has been an explosion of new titles for attorneys working within many law firms. Consequently, it is no longer always easy to identify the partners or distinguish between associates and other non-partners. (D. M. Brock, 2012). The organization of professional services firms has been constantly changing. (D. M. Brock, 2006). Now, partners often can be (though not always) distinguished as being an “equity partner” or “non-equity” partner. (Raasch, 2007). Associates often (though not always) can be distinguished as “senior” or “junior” or “partnership-track” or “staff”. (Raasch, 2007).

Making matters more confusing, the meaning of other non-partner positions has expanded to include “counsel”, “of counsel” and “special counsel.” All the different titles “vary from firm to firm, and from lawyer to lawyer.” (Raasch, 2007). Over time, the challenge has become even more complicated as firms created additional non-partner positions to retain associate attorneys who, for one reason or another, would never become partner. (P. Sherer, 1995), p. 675. At the same time, many U.S. firms also increased the usage of contract, non-employee, attorneys hired as “of counsel”:
Of counsel grew to include retired partners who took cases on a contract basis, law professors who worked on special cases, lawyers who operated as internal contractors renting space and taking referrals, and part-time and fixed-term lawyers who worked for a fee. (P. Sherer, 1995).

Consequently, the distinction between what constitutes “partner” and what constitutes “associate” has become increasingly blurred over the years and even more so with the emergence of multi-tiered partner models. (Galanter & Henderson, 2008).

Accordingly, rather than using the traditional measure of Leverage as being the ratio of “associates” to “equity partners”, the measure was updated. This leverage measure was the ratio of all non-partner attorneys in a firm to all partners. This slight adjustment in the definition avoided the categorization challenge of ever increasing numbers of firm attorneys to be excluded because they were identified as neither being an “associate” or “equity partner”.

**Service Diversification**

The last independent variable, service diversification, was used to capture the focus/diffusion of practice areas as a proxy for the distribution of business activity. (Michael A Hitt et al., 2001), p. 19. Based upon the work of Kor & Leblebici, the services offered by law firms were categorized as falling into eight categories: Corporate and Banking; Tax & Trust; Property; Employment; Litigation; Government; International; and Other. (Kor & Leblebici, 2005), p. 975. This was used as the basis for calculating the service diversification in the proposed research.

Unfortunately, the selection of “practice areas” in the Martindale Hubbell is not restricted to just eight categories. The Martindale Hubbell web site lists several hundred officially recognized practice areas. Even worse, the Martindale Hubbell accepts entry of
practice areas as an unrestricted text space. As such, typographical errors, abbreviations, and “made up” practice areas are all entered into firm-level profiles without any restriction.

In order to address this data challenge, a frequency distribution was constructed for the occurrence of ALL practice areas listed across ALL individual profiles in ALL the firms in the dataset. Based upon the total number of different practice areas, any area constituting less than 2% by number of the total frequencies was discarded. Next, all of the remaining practice areas were then allocated to one of the eight practice areas as identified by Kor & Leblebici.

Next, for each individual profile, each occurrence of the matching practice areas was counted as a “1” within each of the eight main categories. Based upon the total number of “1’s” for each individual, each entry was then calculated as a percentage assigned for each of the eight practice areas. For instance, if an individual lawyer listed five practice areas but they all related to banking, then the distribution assigned 1.00 (5/5) to Banking and left all other categories with a value of 0. The values were then each multiplied by the Full Time Equivalent (FTE) value for the individual profile to adjust for over counting individuals with multiple entries in a particular year.

This had the advantage of providing individual distributions that could then be interpreted as percentage of individual attorney time allocated to each of the eight categories. Consequently for each firm, in each year, the total number of category values approximately equaled the number of firm attorneys who have provided practice area information. As such, the firm-level distribution of practice areas was simply the result
of adding the total values for each of the eight categories for the entire firm on a year-by-year basis.

Based upon the firm-level distributions across the eight categories, a Herfindahl Index was calculated for each firm. (P. Sherer, 1995). See also, (Michael A Hitt et al., 2001, 2006a). To ease in the interpretation, consistent with Hitt, et al. ( 2001), each firm’s Herfindahl Index value was then subtracted from one. As such, lower values reflect lower diversification and higher values reflect higher diversification. (Michael A Hitt et al., 2001), p. 19.

### TABLE 2.

**SUMMARY OF MEASURES**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Definition</th>
<th>Measurement</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Diversification</td>
<td>&quot;Percentage of lawyers abroad.&quot; Scaled 0.001 to 99.99 with 99.99 being the highest international diversification. Calculated by the number of full-time equivalent attorneys stationed abroad divided by the total number of attorneys in the firm.</td>
<td>Brock, Yaffee, and Dembovsky, 2006. Similar to Capar and Kotabe, 2003.</td>
<td></td>
</tr>
<tr>
<td>Human Capital</td>
<td>Average years of practice since first licensure as an attorney for all firm partners.</td>
<td>Scored 1 to 64 years with 64 being the largest value for firm Human Capital.</td>
<td>Modification based upon Hitt, et al. 2001.</td>
</tr>
<tr>
<td>Reputational Capital</td>
<td>Amount of Media Exposures for the specific law firm.</td>
<td>The Natural Logarithm of the number of references for the firm in each year in the Major World Publications database of Lexis/Nexis.</td>
<td>Wartick, 1992</td>
</tr>
<tr>
<td>Leverage</td>
<td>Total number of non-partner attorneys divided by the total number of partner-equivalent attorneys.</td>
<td>Scaled 0.000 to 3.33 with 3.33 being the highest firm leverage.</td>
<td>Sherer, 1995; Hitt et al. 2001; Kor and Leblebici 2005</td>
</tr>
<tr>
<td>Service Diversification</td>
<td>Herfindahl index based upon the number of attorneys, measured at full time equivalents, in the eight largest legal practice areas within the firm.</td>
<td>One(1) minus a Herfindahl Index value, ranging from 0.00 indicating low service diversification up to evenly distributed firms having a maximum value of 0.875.</td>
<td>Hitt, et al, 2001; Kor and Leblebici 2005.</td>
</tr>
</tbody>
</table>

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**Statistical Techniques**

Based upon diagnostic tests done on the data and appropriate prior literature (explained more fully in Chapter VI, Model Results and Findings), the basic statistical method applied was Least Squared Dummy (LSDV) Regression on panel data including both fixed effects and time fixed effects. (Lee & Yu, 2010). The basic fixed effects regression, including time effects is:

\[
y_{it} = \beta_0 + \beta_1 x_{it} + \beta_2 z_i + \beta_3 s_t + u_{it},
\]

\(i = 1, \ldots, N\) (individuals), \(t = 1, \ldots, T\) (time)

Where:

- \(y_{it}\) = Percentage of Firm Attorneys Abroad
- \(x_{it}\) = the "ith" observation of explanatory variable \(X\) at time "t"
- \(\beta\) = parameter coefficient
- \(z_i\) = the unobserved individual-specific time-invariant effects
- \(s_t\) = the unobserved time-specific individual-invariant effects
- \(u_{it}\) = residual disturbance term

(Stock & Watson, 2003)

As explained below, the use of both fixed effects and time fixed effects in regression is appropriate under a very specific set of circumstances:

If some omitted variables are constant over time but vary across states ..., while others are constant across states but vary over time ..., then it is appropriate to include both state and time effects. This is done by including both \(n-1\) state binary variables and \(T-1\) time binary variables in the regression, along with the intercept. (Stock & Watson, 2003), p. 284.
The advantage of the fixed effects method is that it is able to statistically control for variables that have not or cannot be measured and that nonetheless vary across entities but not across time. (Allison, 2005), p. 1. (Stock & Watson, 2003), p. 278. The fixed effects model helps to reduce the biased impact of potential heteroscedasticity and autocorrelation. (Kor & Leblebici, 2005), p. 976. Similarly, time fixed effects statistically controls for variables that have not or cannot be measured and that nonetheless vary across time but not across individuals within a given time. (Stock & Watson, 2003), p. 283.

Unlike random effects models where “unobserved variables are assumed to be uncorrelated with all the observed variables” the fixed effects model accounts for correlations between observed variables – such as would be expected in time series data. (Allison, 2005), p. 2. See also (Bai, 2009; Park, 2005). The fixed effects model is appropriate where there is a focus on a specific set of firms and “our inference is restricted to the behavior of these sets of firms.” (D. H. Baltagi, 2008), p. 14. In order to use the fixed effects models, it is necessary that there be variation across (in our case) both individuals and time. (Allison, 2005), p. 2. Another concern is that fixed effects may have “substantially larger” standard errors, higher p-values, and wider confidence intervals. (Allison, 2005), p. 2.
CHAPTER V

DESCRIPTIVE STATISTICS

As stated previously, the only previous effort to define the entire population of internationally diversified U.S. law firms was based upon data from 1967. (Gaedeke, 1973). As such, the contribution of the current research consists as much in its general descriptive statistics across the years 1998 to 2013 as in its multivariate analysis. For this reason, we briefly discuss the descriptive statistics for each census in 1998, 2003, 2008 and 2013. Next, descriptive statistics are provided on the fifty-five (55) U.S. law firms that constituted the panel used for the quantitative analysis. The discussion of the results and findings from the quantitative model are contained in Chapter VI.


Looking at the descriptive statistics for the entire population of law firms that maintained offices both in the U.S. and abroad, there is an obvious, linear, decrease in the total number of law firms – both U.S. and Non-U.S. – across the years 1998 to 2013:
Figure 3. Total Number of both U.S. and foreign law firms with offices both inside the U.S. and outside the U.S. in 1998, 2003, 2008 and 2013.

Importantly, this is not firm survival data. The chart above indicates the total number of law firms for each year - including new market entrants and non-U.S. law firms with U.S. offices.

The total population of law firms maintaining U.S. and non-U.S. operations decreased linearly from 237 to 143 over the period of 1998 to 2013. The number of U.S. law firms (only) that maintained international operations decreased from 178 to 111 over the period of 1998 to 2013. Contrary to what might have been expected, there was not a precipitous drop in the number of firms around the 2008 global recession. In fact, the decrease was consistent with the prior periods.

Moreover, the firm-level data shows that AmLaw100 firms are not the most prevalent U.S. firms (by number) with international operations. For all of the years, about 60% of all internationally diversified, U.S.-based, firms were not members of the
AmLaw100 (1998 – 61% [109/178]; 2003 – 58% 94/162]; 2008- 57% [82/144]; 2013-60% [67/111]).

Figure 4. Total Number of U.S. law firms (both Amlaw 100 and non-AmLaw 100) and foreign law firms with offices both inside the U.S. and outside the U.S. in 1998, 2003, 2008 and 2013.

Of course, one question might be whether the decrease in the number of U.S. law firms with international operations can be attributable to firm-level consolidation rather than to any decrease in the international deployment of attorneys by U.S. firms. To answer this question, it is necessary to look at employment numbers based upon geographic areas.

Below is a table showing the continents where firms with U.S. offices (including both U.S. and non-U.S. firms), located their attorneys abroad for each of the years. The combined total employment numbers suggest some minor consolidation of firms in the period of 1998 to 2003 since the total employment increased in the period from 1998 to 2003 even though the number of law firms decreased. However, there does not appear to be any significant consolidation after 2003:
Table 3.

*Continent Distribution of Attorneys- All Firms (n=774)*

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Africa</td>
<td>17</td>
<td>28</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>Asia</td>
<td>1337</td>
<td>2017</td>
<td>1547</td>
<td>1260</td>
</tr>
<tr>
<td>Australia/Oceania</td>
<td>315</td>
<td>301</td>
<td>20</td>
<td>30</td>
</tr>
<tr>
<td>Europe</td>
<td>7882</td>
<td>8278</td>
<td>6902</td>
<td>2820</td>
</tr>
<tr>
<td>North America</td>
<td>1321</td>
<td>3164</td>
<td>3464</td>
<td>2216</td>
</tr>
<tr>
<td>South America</td>
<td>277</td>
<td>827</td>
<td>273</td>
<td>144</td>
</tr>
<tr>
<td>Grand Total</td>
<td>11148</td>
<td>14615</td>
<td>12211</td>
<td>6474</td>
</tr>
</tbody>
</table>

*Note: North America numbers are net of U.S.*

Of course, it is conceivable that the consolidation could have occurred in the foreign offices of the non-U.S. firms. If so, the inclusion of deployment data for non-U.S. firms would have provided a distorted representation of the extent of international diversification. As such, it is necessary to also look at the international deployment of attorneys for the U.S.-based law firms only:

Table 4.

*Continent Distribution of Attorneys – U.S Firms Only (n=595)*

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Africa</td>
<td>16</td>
<td>25</td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td>Asia</td>
<td>1094</td>
<td>1486</td>
<td>1341</td>
<td>1026</td>
</tr>
<tr>
<td>Australia</td>
<td>133</td>
<td>300</td>
<td>19</td>
<td>30</td>
</tr>
<tr>
<td>Europe</td>
<td>2196</td>
<td>5221</td>
<td>4048</td>
<td>2341</td>
</tr>
<tr>
<td>North America</td>
<td>256</td>
<td>433</td>
<td>373</td>
<td>406</td>
</tr>
<tr>
<td>South America</td>
<td>158</td>
<td>219</td>
<td>55</td>
<td>106</td>
</tr>
<tr>
<td>Grand Total</td>
<td>3853</td>
<td>7684</td>
<td>5840</td>
<td>3911</td>
</tr>
</tbody>
</table>

*Note: North America numbers are net of U.S. employment.*
When looking at the U.S. firms only, it appears that there was, in fact, a very significant increase between 1998 and 2003 in the international deployment of attorneys. This occurred at the same time as there was a decrease in the number of U.S. law firms with international operations. Nonetheless, there was a sustained deterioration in the international deployment of attorneys after 2003.

Looking at these numbers as a percentage of total employment is even more telling. Looking at the U.S. firms only, the number of attorneys working inside the U.S. (for U.S. based firms, only) for these same law firms was: 38,054 (1998), 50,875 (2003), 52,907 (2008), and 35,285 (2013). Therefore, for each of the respective years, the percentage of attorneys deployed abroad, as compared to the total number attorneys in all the firms (U.S. only) was only 9.19%, 13.12%, 9.94% and 9.98%, respectively. Contrary to some of the literature, it is clear that there has not been any globalization “explosion.” Even at its peak in 2003, there were less than 15,000 total attorneys working outside the U.S. for firms with U.S. operations (both U.S. and non-U.S. firms). In fact, the international deployment by U.S. firms peaked in 2003 at only about 7,684 attorneys!

Of course, looking at the deployment of attorneys at the continent level may also hide changes within the continent at the country level. For this reason, the next page ranks the fifteen (15) highest average international deployments per year over the period of 1998-2013 (for U.S. firms only). Not surprisingly, the country-level deployment table shows that the largest deployment of attorneys was into countries with significant trading relationships with the U.S. What is surprising is that the concentration increased over the years. In 1998, 50% of all attorneys were deployed in the top five (5) countries (England,
China, France, Germany and Belgium). In 2003, 50% of all attorneys were deployed into the top four (4) countries. In 2008 and 2013, 50% of all attorneys were deployed into the top three (3) countries.

In sharp contrast, over the fifteen year period of 1998-2013, U.S.-based law firms stationed at least part of one attorney (on a full-time equivalent basis, “FTE”), for at least one year, in a total of seventy-eight (78) different countries. If international diversification of attorneys was increasing, it would logically follow that increasing numbers of attorneys would be deployed in increasing numbers of foreign markets. This is not what the data shows.

Table 5.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>England</td>
<td>760</td>
<td>1748</td>
<td>1892</td>
<td>1149</td>
</tr>
<tr>
<td>2</td>
<td>China</td>
<td>493</td>
<td>585</td>
<td>706</td>
<td>561</td>
</tr>
<tr>
<td>3</td>
<td>France</td>
<td>341</td>
<td>731</td>
<td>535</td>
<td>398</td>
</tr>
<tr>
<td>4</td>
<td>Germany</td>
<td>109</td>
<td>842</td>
<td>624</td>
<td>369</td>
</tr>
<tr>
<td>5</td>
<td>Belgium</td>
<td>247</td>
<td>424</td>
<td>260</td>
<td>160</td>
</tr>
<tr>
<td>6</td>
<td>Japan</td>
<td>109</td>
<td>278</td>
<td>320</td>
<td>232</td>
</tr>
<tr>
<td>7</td>
<td>Mexico</td>
<td>126</td>
<td>275</td>
<td>236</td>
<td>233</td>
</tr>
<tr>
<td>8</td>
<td>Italy</td>
<td>149</td>
<td>430</td>
<td>134</td>
<td>49</td>
</tr>
<tr>
<td>9</td>
<td>Russia</td>
<td>171</td>
<td>283</td>
<td>187</td>
<td>36</td>
</tr>
<tr>
<td>10</td>
<td>Canada</td>
<td>109</td>
<td>123</td>
<td>109</td>
<td>152</td>
</tr>
<tr>
<td>11</td>
<td>Australia</td>
<td>133</td>
<td>300</td>
<td>19</td>
<td>30</td>
</tr>
<tr>
<td>12</td>
<td>Singapore</td>
<td>148</td>
<td>166</td>
<td>78</td>
<td>57</td>
</tr>
<tr>
<td>13</td>
<td>Thailand</td>
<td>111</td>
<td>196</td>
<td>75</td>
<td>32</td>
</tr>
<tr>
<td>14</td>
<td>Poland</td>
<td>118</td>
<td>136</td>
<td>95</td>
<td>57</td>
</tr>
<tr>
<td>15</td>
<td>Spain</td>
<td>53</td>
<td>175</td>
<td>48</td>
<td>29</td>
</tr>
<tr>
<td>Total Top 15</td>
<td>3178</td>
<td>6591</td>
<td>5316</td>
<td>3544</td>
<td></td>
</tr>
<tr>
<td>Countries 16-78</td>
<td>675</td>
<td>1101</td>
<td>525</td>
<td>368</td>
<td></td>
</tr>
<tr>
<td>Grand Total</td>
<td>3854</td>
<td>7692</td>
<td>5841</td>
<td>3911</td>
<td></td>
</tr>
</tbody>
</table>
Of course, another way to examine the international diversification of U.S. law firms is to look at the number of firms (rather than number of attorneys) that chose to staff offices in the particular country. Although we might expect to see a high correlation between the number of attorneys and the number of firms, this is not necessarily correct. Some countries may be staffed by a large number of firms with small offices while other countries may be staffed by a small number of firms with large offices. These relationships may also vary across time.

Table 6.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>England</td>
<td>84</td>
<td>92</td>
<td>79</td>
<td>51</td>
</tr>
<tr>
<td>2</td>
<td>China</td>
<td>47</td>
<td>42</td>
<td>48</td>
<td>33</td>
</tr>
<tr>
<td>3</td>
<td>Belgium</td>
<td>31</td>
<td>36</td>
<td>29</td>
<td>18</td>
</tr>
<tr>
<td>4</td>
<td>France</td>
<td>27</td>
<td>33</td>
<td>27</td>
<td>20</td>
</tr>
<tr>
<td>5</td>
<td>Germany</td>
<td>20</td>
<td>30</td>
<td>31</td>
<td>14</td>
</tr>
<tr>
<td>6</td>
<td>Japan</td>
<td>24</td>
<td>26</td>
<td>23</td>
<td>15</td>
</tr>
<tr>
<td>7</td>
<td>Canada</td>
<td>17</td>
<td>16</td>
<td>21</td>
<td>25</td>
</tr>
<tr>
<td>8</td>
<td>Russia</td>
<td>25</td>
<td>17</td>
<td>15</td>
<td>5</td>
</tr>
<tr>
<td>9</td>
<td>Singapore</td>
<td>15</td>
<td>17</td>
<td>11</td>
<td>7</td>
</tr>
<tr>
<td>10</td>
<td>Mexico</td>
<td>10</td>
<td>13</td>
<td>11</td>
<td>12</td>
</tr>
<tr>
<td>11</td>
<td>Italy</td>
<td>4</td>
<td>13</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>12</td>
<td>Switzerland</td>
<td>8</td>
<td>7</td>
<td>6</td>
<td>4</td>
</tr>
<tr>
<td>13</td>
<td>Poland</td>
<td>9</td>
<td>8</td>
<td>5</td>
<td>2</td>
</tr>
<tr>
<td>14</td>
<td>Taiwan</td>
<td>9</td>
<td>5</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>15</td>
<td>U.A.E.</td>
<td>3</td>
<td>2</td>
<td>9</td>
<td>8</td>
</tr>
<tr>
<td></td>
<td>Total Top 15</td>
<td>333</td>
<td>357</td>
<td>330</td>
<td>224</td>
</tr>
<tr>
<td></td>
<td>Countries 16-78</td>
<td>93</td>
<td>105</td>
<td>59</td>
<td>42</td>
</tr>
<tr>
<td></td>
<td>Grand Total</td>
<td>426</td>
<td>462</td>
<td>389</td>
<td>266</td>
</tr>
</tbody>
</table>

The ranking above, based upon the number of firms in each country, shows only some minor differences as compared to the rankings based upon number of attorneys. Apparently, Belgium has a larger number of smaller firms – they are ranked higher based
on firms rather than attorneys. In contrast, Mexico appears to have fewer firms but tend to have larger deployments. This appears to be evident from Mexico having a firm rank of 10 but an attorney rank of 7.

One last set of informative descriptive statistics regards the percentage of attorneys deployed abroad who are admitted in the U.S. and/or who are admitted the Host Country. Unfortunately, without a direct survey of the firms, it is impossible to determine for certain what law they are practicing while stationed abroad. However, for the purpose of percentages estimation, the individual attorney biographies were examined to determine whether the attorneys were admitted in the U.S. and/or in the Host Country where they were located. Only those biographies that specifically listed as having been admitted into a U.S. state were counted as being admitted in the U.S. Similarly, only those biographies that listed admission in the Host Country were counted as being admitted in the Host Country. In calculating the percentages, the denominator for all calculations was the total number of individuals expressly admitted either in a U.S. or Host Country jurisdiction.

The results of these calculations are as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>All U.S. Firms</th>
<th>Only U.S. Firms Surviving All 4 Time Periods</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>41.68%</td>
<td>30.16%</td>
</tr>
<tr>
<td>2003</td>
<td>27.50%</td>
<td>21.41%</td>
</tr>
<tr>
<td>2008</td>
<td>27.89%</td>
<td>28.51%</td>
</tr>
<tr>
<td>2013</td>
<td>28.19%</td>
<td>25.71%</td>
</tr>
</tbody>
</table>
What is particularly notable about these percentages is the relatively low number of attorneys working abroad that are actually admitted in the U.S. It appears that about only 1 in 4 attorneys have been admitted in the U.S. The percentages remain relatively stable across all U.S. law firms and only those U.S. law firms that survived across all four time periods.

Perhaps not surprisingly, the percentage of attorneys admitted in the host country (but working for U.S. law firms) is appropriately high.

Percentage of Attorneys Abroad Admitted in Host Country (working for US firms Only)

<table>
<thead>
<tr>
<th>Year</th>
<th>All U.S. Firms</th>
<th>Only U.S. Firms Surviving All 4 Time Periods</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>69.05%</td>
<td>78.82%</td>
</tr>
<tr>
<td>2003</td>
<td>81.92%</td>
<td>86.53%</td>
</tr>
<tr>
<td>2008</td>
<td>82.27%</td>
<td>83.55%</td>
</tr>
<tr>
<td>2013</td>
<td>85.19%</td>
<td>86.54%</td>
</tr>
</tbody>
</table>

Once again, the percentages remain surprisingly stable across all U.S. firms and only those firms that survived across all four time periods.

In construing the percentages above, it might be inferred that the attorneys deployed abroad are actually practicing Host Country Law rather than U.S. law. However, this is not necessarily the case. It may be that, in order to increase the potential for referrals from other attorneys within the Host Country, that the U.S. firms retain a disproportionate number of foreign born (and licensed) attorneys. The high percentage of attorneys admitted in the Host Country would then indicate a characteristic of the U.S.
law firm’s client origination marketing strategy more than the type of legal services actually provided in the Host Country. Consequently, this issue will need to be subject to future factual research.

Obviously, the examination of the population characteristics of U.S. law firms with international operations could fill a book of its own. However, what is clear from the descriptive data is that the international diversification of U.S. law firms is far more complex than would be suggested by the traditional examination within the literature.

Generally speaking, there has been a sustained deterioration in the deployment of attorneys abroad. This deterioration appears to parallel the decreases in the number of U.S. law firms maintaining foreign operations. From this, it may be generally implied that the international diversification behavior of U.S. law firms have decreased the number of countries in which the law firms maintain offices and by significantly decreasing the number of attorneys deployed in existing foreign offices. The percentage of attorneys working abroad for U.S. law firms that are admitted in the U.S. and the Host Country raise even more questions. Collectively, this raises the very real possibility that U.S. firms are serving international demands differently than has been assumed in prior literature. Exactly how this is being accomplished will need to remain for future research.
CHAPTER VI

PANEL DESCRIPTION AND MODEL RESULTS

While the population of U.S. law firms with international operations varied over the years, the preferable multivariate technique required a balanced panel for analysis. This meant that each firm included in the analysis had to have international operations in each of the years 1998, 2003, 2008 and 2013. Moreover, each of the firm observations needed to have valid data for each of the variables contained in the model.

Of the 44 AmLaw100 firms that existed in 2013, 40 of them were also international across all prior relevant years. In stark contrast, of the 67 U.S. based, Non-AmLaw100 firms that existed in 2013, only 20 of them were also international in 1998, 2003, and 2008. As such, the starting sample size for the research was sixty (60) U.S. law firms. However, five (5) of the sixty (60) surviving U.S. firms did not have complete data for each of the variables contained in the model. This reduced the panel to fifty-five (55) firms. A summary of the survival of firms from 1998 to 2013 is contained on the next page.
As can be seen from the chart above, the survival of firms from 1998 declined the greatest during the period from 1998 to 2003. Afterward, the decline was stable and less dramatic from 2003 to 2013.

Listed below are the descriptive statistics and correlations for the fifty-five (55) firms that were contained in the panel data set:

Table 9.

| Variables          | Mean   | s.d.   | Min.    | Max.    | 1   | 2   | 3   | 4   | 5   | 6   | 7   | 8   |
|--------------------|--------|--------|---------|---------|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| 1. Int'l Diversification | 12.51% | 20.91% | 0.11%   | 97.64%  | .449** | - .158 | .013 | - .136 | .370 | - .131 | .004 |
| 3. Reputation       | 2.7448 | 2.0016 | 0.0000  | 6.5088  | - .158 | - .251** | 1   | .419** | .342** | .474** | .741** | .742** |
| 4. Leverage         | 1.2230 | 0.7011 | 0.0000  | 3.3364  | - .136 | - .253** | .419** | 1   | - .035 | .351** | .390** | .354** |
| 5. Svc. Diversification | 0.7072 | 0.1182 | 0.1107  | 0.8285  | - .136 | - .166** | .342** | - .035 | 1   | .094 | .259** | .243** |
| 6. NoCntries a      | 3.96   | 3.504  | 2       | 31      | - .370** | - .194** | .474** | .351** | .094 | 1   | .355** | .749** |
| 7. AmLaw01 b        | .47    | .500   | 0       | 1       | - .131 | - .218** | .741** | .390** | .259** | .355** | 1   | .634** |
| 8. TotAtys          | 403    | 396    | 2       | 2486    | - .274** | .742** | .354** | .243** | .749** | .634** | 1   |     |

\[**. Correlation is significant at the 0.01 level (2-tailed).

\[*. Correlation is significant at the 0.05 level (2-tailed).

a. This represents the total number of countries - including the U.S.

b. Dummy variable.
Looking at the correlation matrices, the panel data has quite a few variables that have statistically significant correlations at the .01 or .05 level. What is a little curious is that there are negative correlations for Reputational Capital as related to both International Diversification and Human Capital. This suggests that some other mechanism, beside International Diversification (as measured in the model) is being used by U.S. law firms to serve the international needs of their clients.

Beyond this surprise, the Total Number of Attorneys of the panel firms (indicated by total number of firm attorneys) was surprisingly variant. The mean number of total attorneys was 403 with the median of 294. However, the bottom 20th percentile of the panel data had less than 100 attorneys. The minimum number of firm attorneys, that had international operations across all fifteen years was only two (2) attorneys. In sharp contrast, the top 25 percent (by size) had in excess of 560 attorneys. This is a very significant distribution, by size, of firms engaged in law across country borders.

Similarly, there was a surprising lack of international expansion as measured by the number of countries in which the U.S. firms operated. In order for the firms to be included in the data set, they had to operate both in the U.S. and in one foreign country. Therefore the minimum number of countries had a value of 2. Over 40 percent of all U.S. countries operated in only one foreign country (meaning NoCntries=2). The mean number of total countries was 3.96 (so 2.96 foreign countries) with a median of 3.00 (so 2.00 foreign countries). Only the top 30 percent of law firms that had operations in total countries of 4 (so 3.00 foreign countries) or more.
The mean percentage attorneys stationed abroad or U.S.-based law firms was 12.5 percent and the median percentage was only 4 percent. Seventy-five (75) percent of all U.S. law firms had less than 10 percent of their attorneys stationed abroad. Clearly, most U.S. firms continued to maintain a distinctly U.S.-centric locational structure. Comparing the percentage of foreign attorneys across the years, it is clear that the general distributions remained largely stable. Across all periods, most firms had less than ten percent of their attorneys abroad.

It is also clear that all U.S. firms with international operations have extremely experienced partners. The average partner experience covering all the years has a mean experience at 24.7 years and a median of 23.65 years. Even more telling, the bottom ten percentile of law firms still had average partner experience exceeding 20 years. Comparing the average firm partner experience across the years, it appears that slightly less experienced partners were engaged in the 1998 period but there was a clear shift upward to the 20 years of minimum experience thereafter. It is also interesting to note that the upper end tail of the distribution also was shifted higher in 2008 and 2013.

Another surprise was the relatively low firm-level nonpartner-to-partner leverage for the U.S. firms with international operations. The mean leverage value for all firms across all years was only 1.223 and the median was 1.088. Approximately 50% of the U.S. law firms with international operations had less than 1 non-partner lawyer for each partner in the firm. It is not until the top ten percentile that the leverage exceeds more than two non-partners for each partner.
The measurement of law firm Reputational Capital, as measured by the natural log of the number of references to the firm in major world publications during the given year, exhibited a significant dispersion of references across the firms. The mean value was 2.745 and the median was 2.890. However, 25% of all law firms had a value of less than 1. However, the top 25% had values greater than 4.533.

Looking at the Service Diversification, the mean value for the panel was 0.707 and the median was 0.743. The distribution appears generally symmetrical within the middle 80th percentile range only varying from 0.56 to 0.80. This indicates that most firms provide a very wide service offering. Recall that a value of 0 indicates that the firm is a pure boutique firm with all attorneys practicing in a single practice area. In contrast, a value of 0.8750 represents a firm that is perfectly balanced across all eight practice areas.

In sum then, the descriptive statistics of variables within the panel appear to provide a nice foundation upon which to conduct the multivariate analysis.

**Multivariate Analysis**

Although the basic conceptual model and hypotheses were set in advance, the specific form of the panel regression could only be determined after the preliminary analysis of the panel data. This was done as described immediately below.

The first item that needed to be determined regarding the quantitative analysis of the Conceptual Model was whether Fixed Effects should be used (as used in the prior literature), or, whether the dataset was more properly analyzed using Random Effects. The quantitative evaluation of for this purpose was accomplished by running the
Hausman test. (Hausman, 1978). Notably, the Hausman Test was previously used for this exact purpose in the context of international diversification models. (Qian, Li, Li, & Qian, 2008). The results of the Hausman Test on the current data indicated a ChiSq of 59.97 with p>0.0000. As such, we rejected the H₀ that the difference in the coefficients was not systematic. (B. H. Baltagi, Bresson, & Pirotte, 2003), p. 362. Pursuant to Hausman, this indicated that it was appropriate to run Fixed Effects.

It should also be noted that the preliminary diagnostics were run on data that had not been re-centered to create a mean of zero of each variable. Use of the raw, non-centered, data was used because some of the variables in the model had meaningful zero values. For instance, Human Capital was based upon years of experience. Re-centering the data would have resulted in negative values for experience that would not have been meaningful. As such, pursuant to Cohen, et al., the decision was made to use the non-centered data. (J. Cohen, Cohen, West, & Aiken, 2003).

Next, the Conceptual Model (Model 5 in the overall output) was run using both Fixed Effects and Time Effects. The purpose was to determine whether or not there were any statistically significant Time Effects. Relative to the base year of 1998, the model indicated that the year 2003 was statistically significant at α=0.025. Likewise, 2008 and 2013 were statistically significant at α ≤ 0.000. The coefficient values were 0.032, 0.065, and .127 for all three years. As such, it was clear that the model needed to include time effects. This too was consistent with the literature. See generally, (Michael A Hitt et al., 2006a), p. 1144.
Next, the Frees test for cross-sectional dependence was run on the data. Unlike the Breusch and Pagan Test, the Frees Test is appropriate where there the number of observations, \( n \), is large relative to the number of time periods, \( T \). In this case, \( n=220 \) while \( t=4 \). The Frees’ test value on the current data had a value of 3.933 at \( \alpha<0.01 \). (Frees, 1995). This indicated that there was a lack of cross-sectional independence in the data. (DeHoyos & Sarafidis, 2006).

Given concerns about both a lack of cross-sectional independence and time effects, the Conceptual Model (Model 5) was run consistent with clustering along two dimensions – firm and time. (Petersen, 2008). See also (Cameron, Gelbach, & Miller, 2011; Miller, Cameron, & Gelbach, 2006; Thompson, 2011). As explained previously, consistent with Cohen, et al. (2003), the regression was run on the “noncentered” data because some of the independent variables had meaningful zero values. (J. Cohen et al., 2003), p. 271. See also (Aiken & West, 1991). The correlation matrix and descriptive statistics for the panel data was provided at the beginning of this Chapter.

The fixed effects regression results across eight related models are shown immediately below. All models were tested using the Percent of Foreign Attorneys as the dependent variable. The results of each model are discussed in order. However, the key conceptual model for the purposes of the current research is Model 5.
Table 10.

<table>
<thead>
<tr>
<th>Models with DV = Percent of Foreign Attorneys</th>
</tr>
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<tbody>
<tr>
<td>Independent Variables</td>
</tr>
<tr>
<td>---------------------------------------------</td>
</tr>
<tr>
<td>H. Capital (Partner Exp.)</td>
</tr>
<tr>
<td>Rep. Capital (Major W. Pols)</td>
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<tr>
<td>Leverage (NonP/P)</td>
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<tr>
<td>Service Div. (Minus Herf.)</td>
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<tr>
<td>Interaction (Hum C. x Rep. C.)</td>
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<tr>
<td>Interaction (Hum C. x Lev)</td>
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<tr>
<td>Interaction (H. Cap. x Serv. Div.)</td>
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<tr>
<td>Interaction (Lev x Serv. Div.)</td>
</tr>
<tr>
<td>Control (No. of Countries)</td>
</tr>
<tr>
<td>Control (Elite firms - AmLaw100)</td>
</tr>
<tr>
<td>Constant</td>
</tr>
<tr>
<td>R-Squared</td>
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<tr>
<td>F Value</td>
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</table>

p<.01= ***
p<.05= **
p<.10= *

Results Hypothesis 1 (H1)

In Hypothesis 1, we argued that the interaction between Human Capital and Reputational Capital would be positively related to the degree of International Diversification of U.S. law firms:

Specifically: H1(a), At higher levels of Human Capital, the level of Reputational Capital will positively facilitate a higher level of International Diversification. H1(b), At lower levels of Human Capital, Reputational Capital will have little impact on International Diversification. To the extent that there is any effect, it will be positive.

Looking specifically at the results for the interaction of Human Capital and Reputational Capital, the interaction coefficient turned out to be negative (-0.0119) and significant at α< .01. The sign was opposite of what was originally hypothesized. However, the original hypothesis was based upon several assumptions that were inconsistent with the actual behavior disclosed by the descriptive statistics across the years. Rather than the globalization of markets increasing the international diversification of U.S. law firms, the exact opposite has occurred. See generally, Chapter V, Descriptive Statistics.
Recall also that both Bower (1968) and Gadaeke (1973) found the primary reason for U.S. law firm internationalization to be “client following.” Given the absence of any recent comprehensive empirical data, it was assumed that U.S. law firms had subsequently adopted more proactive, entrepreneurial, market-seeking internationalization strategies. As such, the original hypothesis was based on an assumed positive relationship between the extent of international diversification and firm financial performance. This assumption was then applied to the general premise that firms “expand internationally with an intention to improve their long-run financial performance.” (D. Brock & Alon, 2009), p. 55.

However, based upon several discussions with various international law firms, firm financial performance maximization is not necessarily achieved by deploying more attorneys abroad. To the contrary, financial performance appears to be maximized by minimizing the foreign deployment of U.S. attorneys and increasing the utilization of existing U.S. resources. The question that therefore arises is how law firms respond to this financial reality as it is reflected in the extent of their international diversification (and related to the interaction of Human Capital and Reputational Capital).

One partial potential explanation is that U.S. law firms have simply continued to limit international diversification to client-following. However, this does not fully explain the statistical significance of the interactions. Alternatively, U.S. law firms may be pursing aggressive market-seeking activities in ways other than simply through international diversification. For instance, the U.S. firms could be using video teleconferencing, email, and temporary trips to service their client needs. U.S. law firms also could be utilizing
external network referrals and/or other means that do not require the permanent deployment of attorneys abroad. Any of these strategies, or combination of them, could explain the negative interaction of Reputational Capital and Human Capital as regards firm International Diversification.

In order to examine the interaction between Reputational Capital and Human Capital more closely, a chart of the simple slopes of the interaction was constructed. Pursuant to Aiken & West (1991), the simple slope of the interactions can be examined by “recasting the regression equation as the regression of the criterion on one predictor.” (Aiken & West, 1991), p. 12. See also, (J. Cohen et al., 2003). In the present instance (for the first hypothesis), this involves “recasting” the basic regression equation from:

\[ \hat{Y} = b_0 + b_1 \text{HumanCap} + b_2 \text{Rep.Cap} + b_3 \text{Lev} + b_4 \text{SvcDiv} + b_5 (\text{HumanCap} \times \text{Rep.Cap}) + b_6 (\text{HumanCap} \times \text{Lev}) + b_7 (\text{HumanCap} \times \text{SvcDiv}) + b_8 (\text{Lev} \times \text{SvcDiv}). \]

To:

\[ \hat{Y} = [b_1 + b_5 \times \text{Rep.Cap} + b_6 \times \text{Lev} + b_7 \times \text{SvcDiv}] \times \text{HumanCap} + [b_0 + b_2 \times \text{Rep.Cap} + b_3 \times \text{Lev} + b_4 \times \text{SvcDiv} + b_8 (\text{Lev} \times \text{SvcDiv})]. \]

Next, we substitute the coefficient values from the main regression (Model 5). This gives use the following:

\[ \hat{Y} = [.0041 + -.0119 \times \text{Rep.Cap} + .0105 \times \text{Lev} + .0193 \times \text{SvcDiv}] \times \text{HumanCap} + [.2457 + .2801 \times \text{Rep.Cap} + -.4144 \times \text{Lev} + -.8177 \times \text{SvcDiv} + .2591 (\text{Lev} \times \text{SvcDiv})]. \]
Since we are only interested in the relationship between Human Capital and Reputational Capital, we substitute the mean values of Leverage (1.223) and Service Diversification (.7071). This gives us:

\[ \hat{Y} = [.0041 + -.0119*RepCap + .0105*1.223 + .0193*.7071]*HumanCap + [.2457 + .2801*Rep.Cap + -.4144*1.223 + -.8177*.7071 + .2591*(1.223*.7071)]. \]

This reduces to the following:

\[ \hat{Y} = [.0305 -.0119*RepCap]*HumanCap + [-.6152 + .2801*Rep.Cap]. \]

Next, pursuant to Aiken & West, the equations for Reputational Capital\textsubscript{High} and Reputational Capital\textsubscript{Low} were derived by substituting the one standard deviation plus (high= 4.746) and minus (low= 0.743) for the Reputational Capital variable. This resulted in the following two equations\footnote{Note, exact coefficient values vary slightly due to rounding errors.}:

At RepCap\textsubscript{High} = 4.746: \[ \hat{Y} = [-0.025]*HumanCap + [0.7146]. \]

At RepCap\textsubscript{Low} = 0.743: \[ \hat{Y} = [0.021]*HumanCap - [0.4071]. \]

Thus the interaction of Reputational Capital and Human Capital can be charted as the simple slopes as follows:
The simple slopes of the interaction shows that the unexpected decrease in International Diversification is largely accounted for due to firms with high Reputational Capital. For firms with high Reputational Capital, International Diversification decreases as Human Capital increases. In this regard, it may be that firms with high Reputational Capital and high Human Capital are most able to maximize their firm financial performance by successfully reducing the number of attorneys deployed abroad.

Looking at the interaction relationships for low Reputational Capital, it was originally hypothesized that the increase in Human Capital would have little effect on the extent of International Diversification. However, in fact, an increase in Human Capital resulted in a notable increase in the International Diversification of the law firm. Again, one possible explanation is that, although the financial performance of all law firms was
maximized by minimizing the number of attorneys stationed abroad, the firms that lacked Reputational Capital needed to position more attorneys abroad to provide tangible proof of the quality of their services to their clients. Possibly, the lack of an established reputation forced these firms to deploy more bodies abroad in order to better support client perceptions and satisfaction.

Digging deeper, the sign and statistical significance of the coefficient for the interaction of Human Capital and Reputational Capital was consistent – and negative - across all nested models. Nonetheless, additional research is necessary to better understand the underlying causes of this relationship.

**Results Hypothesis 2 (H2)**

In Hypothesis 2, we argued that the interaction between Human Capital and Leverage is positively related to the degree of International Diversification of U.S. law firms:

Specifically: H2(a), At higher levels of Human Capital, the level of Leverage will positively facilitate a higher level of International Diversification. H2(b), At lower levels of Human Capital, Leverage will less positively impact International Diversification.

As hypothesized, the interaction between Human Capital and Leverage was found to be positive (+0.0105), statistically significant at α<.05, and generally consistent with the hypotheses. As with the results of the previous hypothesis, in order to chart the simple slope of the interaction between Human Capital and Leverage, we started with the same basic regression equation that we started with in the previous interaction:

\[ \hat{Y} = b_0 + b_1\text{HumanCap} + b_2\text{Rep.Cap} + b_3\text{Lev} + b_4\text{SvcDiv} + b_5(\text{HumanCap} \times \text{Rep.Cap}) + b_6(\text{HumanCap} \times \text{Lev}) + b_7(\text{HumanCap} \times \text{SvcDiv}) + b_8(\text{Lev} \times \text{SvcDiv}). \]

Similarly, we then inserted the same values for the coefficients:
\[ \hat{Y} = [0.0041 - 0.0119*RepCap + 0.0105*Lev + 0.0193*SvcDiv]*HumanCap + \\
[0.2457 + 0.2801*Rep.Cap + -0.4144*Lev + -0.8177*SvcDiv + 0.2591*(Lev*SvcDiv)]. \]

However, since this time we are interested in the interaction of Human Capital and Leverage, we substitute the mean values for Reputational Capital (2.744) and Service Diversification (0.7071). This resulted in the following equation:

\[ \hat{Y} = [0.0041 - 0.0119*2.744 + 0.0105*Lev + 0.0193*0.7071]*HumanCap + [0.2457 + \\
0.2801*2.744 - 0.4144*Lev - 0.8177*0.7071 + 0.2591*(Lev*0.7071)]. \]

\[ \hat{Y} = [-0.0150 + 0.0105*Lev]*HumanCap + [0.4361 - 0.2312*Lev]. \]

Next, pursuant to Aiken & West, the equation for Leverage_{HIGH} and Leverage_{LOW} were generated by substituting the one standard deviation plus (high= 1.924) and minus (low= 0.521). This resulted in the following two equations5:

At Leverage_{High} = 1.924: \( \hat{Y} = [0.005]*HumanCap - [0.008]. \)

At Leverage_{Low} = 0.521: \( \hat{Y} = -[0.009]*HumanCap + [0.315]. \)

This results in the simple slope charts immediately below.

---

5 Note, exact coefficient values vary due to rounding.
As hypothesized, the relationship to international diversification was positively sloped when high Human Capital interacted with high Leverage. In the presence of low Human Capital, the relationship was hypothesized to “change very little.” In fact, although the results were statistically significant, the amount of change across all values of the interaction was relatively slight. Notably, the test results actually showed that, in the presence of low Human Capital, the relationship was slightly negative.

Unlike the results for the first hypothesis, the results of the second hypothesis were largely as expected. The only notable aspect of the results which was a little surprising is that the simple slopes were not greater. However, part of this may be explained by the relatively narrow ranges in the data for both firm Human Capital and Leverage.
**Results Hypothesis 3 (H3)**

In Hypothesis 3 we argued that the interaction between Human Capital and Service Diversification is positively related to the degree of international diversification of U.S. law firms:

Specifically: H3(a), At higher levels of both Human Capital and Service Diversification, international diversification will be higher. H3(b), At lower levels of both Human Capital and Service Diversification, international diversification will be lower.

As tested, the interaction between Human Capital and Service Diversification was found to be positive (+.0193), statistically significant at $\alpha < .05$, and generally consistent with the hypotheses. Consistent with the previous hypotheses, we therefore charted the simple slope of the interaction between Human Capital and Service Diversification. Once again, we started with the same basic regression equation that we started with in the previous interactions:

$$
\hat{Y} = b_0 + b_1*\text{HumanCap} + b_2*\text{Rep.Cap} + b_3*\text{Lev} + b_4*\text{SvcDiv} + b_5*(\text{HumanCap} * \text{Rep.Cap}) + b_6*(\text{HumanCap} * \text{Lev}) + b_7*(\text{HumanCap} * \text{SvcDiv}) + b_8*(\text{Lev} * \text{SvcDiv}).
$$

Similarly, we then inserted the same values for the coefficients:

$$
\hat{Y} = [0.0041 + -.0119*\text{Rep.Cap} + .0105*\text{Lev} + .0193*\text{SvcDiv}] * \text{HumanCap} + [.2457 + .2801*\text{Rep.Cap} + -.4144*\text{Lev} + -.8177*\text{SvcDiv} + .2591*(\text{Lev} * \text{SvcDiv})].
$$

However, since this time we are interested in the interaction of Human Capital and Service Diversification, we substitute the mean values for Reputational Capital (2.744) and Leverage (1.223). This resulted in the following two equations$^6$:

$$
\text{At ServiceDiv}_{\text{High}} = 0.825: \hat{Y} = [0.0002] * \text{HumanCap} + [0.094].
$$

$^6$ Note, exact coefficient values vary due to rounding.
At ServiceDiv \(_{\text{Low}} = 0.589\): \( \hat{Y} = -[0.004] \times \text{HumanCap} + [0.212] \).

This resulted in the following simple slope chart:

![Human Capital and Service Diversification](image)

\( \beta = 0.193, \text{ Statistically Significant } \alpha \leq 0.01 \).

Figure 8. Simple slope results for Hypothesis 3.

As expected, there was a positive slope relating International Diversification in the presence of both high Human Capital and high service diversification. What was less expected was that there would be a more negative slope relating International Diversification in the presence of low Service Diversification and high Human Capital. This may simply reflect that more Human Capital may be necessary to adequately serve a highly diversified legal practice. In turn, this might adversely impact the ability of the law firm to internationally diversify. Nonetheless, this relationship should be subject to additional clarification in future research.
Results Hypothesis 4 (H4)

In Hypothesis 4, we argued that the interaction between leverage and service diversification would have a negative effect on the degree of international diversification of U.S. law firms:

Specifically: H4(a), At higher levels of both leverage and Service Diversification, international diversification will be lower. H4(b), At lower levels of both leverage and Service Diversification, international diversification will be higher.

Importantly, the test results on this interaction were not statistically significant.

Nonetheless, although the results for hypothesis 4 were not statistically significant, the simple slopes were calculated to determine if there were any intriguing possibilities. The equations for the simple slopes were as follows\(^7\):

At ServiceDiv\(_{\text{High}}\) = 0.825: \(\hat{Y} = [0.060]\times \text{Leverage} + [0.027]\).

At ServiceDiv\(_{\text{Low}}\) = 0.589: \(\hat{Y} = [-0.001]\times \text{Leverage} + [0.107]\).

\(^7\) Note, exact coefficient values vary due to rounding.
Looking at the single slope chart, it appears that low Service Diversification effectively had no interaction with Leverage as it related to International Diversification. In contrast, high Service Diversification had a positive tendency related to high Leverage. However, given that the interaction was not statistically significant, great care is necessary in implying anything from these results.

In sum, the results of Hypotheses 1, 2 & 3 were all statistically significant. The result for Hypothesis 4 was not significant. Although the sign of the interaction for Hypothesis 1 was opposite of what was expected, it was completely consistent with the behavior of U.S. law firms as reflected in the trends in the descriptive statistics. It is also consistent with several possible explanations.
Discussion of the Nested Models

Turning now to the various nested models, it is clear that there is a high degree of coefficient stability. In fact, the coefficients remained largely stable even when “extra” potentially confounding variables were included in models 6, 7 & 8. Each of the models is discussed in order, below.

Model 1 represented the base model that only included the main effects and a constant regressed (using fixed effects and time effects regression) against the percentage of the firm’s attorneys deployed abroad. None of the main effects were significant. The R-Squared was 0.2291.

Model 2 was identical to the main effects in Model 1 except that a single interaction term was added to represent the interaction between the firm’s Human Capital and Reputation. This resulted in an increase in the model’s R-Square to 0.3425. The main effects for Human Capital and Reputation, as well as the interaction between them were significant at an $\alpha \leq 0.01$. Notably, the coefficient for the interaction was negative.

Model 3 was identical to the variables in Model 2 except that an additional interaction term was added to represent the interaction between the firm’s Human Capital and Leverage. The results were consistent with the Model 2 results. Additionally, the main effect and interaction of Human Capital and Leverage were significant at an $\alpha \leq 0.05$. The R-Squared for the model was 0.3754. The interaction of Human Capital and Reputational Capital remained significant at $\alpha \leq 0.01$ and negative.

Model 4 was identical to the variables in Model 3 except that an additional interaction term was added to represent the interaction between the firm’s Human Capital
and Service Diversification. Neither the main effect for Human Capital nor the interaction of Human Capital and Service Diversification were statistically significant. Nonetheless, the signs and coefficient values for Model 4 remained consistent with the prior models. The R-Squared for Model 4 was 0.3758. The interaction of Human Capital and Reputational Capital remained significant at $\alpha \leq .01$ and negative.

Model 5 represents the full conceptual model as proposed consisting of four main effects and four interactions. Model 5 is identical to Model 4 except that a fourth interaction was added for Leverage and Service Diversification. All the main effects, except Human Capital, were statistically significant. All the interactions, except Leverage-to-Service Diversification were statistically significant. The R-Squared for Model 5 was 0.3800.

The last interaction under Model 5 was the interaction of Leverage and Service Diversification. This interaction was positive (+.2591) as hypothesized but was not statistically significant. The interaction of Human Capital and Reputational Capital remained significant at $\alpha \leq .01$ and negative.

The purposes of Models 6, 7 & 8 were to consider the impact, if any, of including separate dummy variables for the AmLaw100 firms and/or a control for the number of countries in which the firms had offices. Model 6 is the same as model 5 except that a dummy variable was added to determine if there was any difference between the elite AmLaw100 and non-AmLaw100 U.S. law firms regarding their international diversification behavior. All of the variables that were contained in Model 5 remained stable. The additional dummy variable for the elite AmLaw100 firms was not
statistically significant. All of the Model 5 variables remained essentially the same. Notably, the interaction of Human Capital and Reputational Capital remained significant at $\alpha \leq .01$ and negative.

Model 7 was also identical to Model 5 except that an additional independent variable was added for the Number of Countries in which the firms had operations. Recall that, per Brock, et al. (2008), percentage of foreign attorneys and number of foreign countries are considered to be alternative measures of international diversification. (D. M. Brock & Yaffe, 2008), p. 605. As such, Model 7 was intended to determine how Model 5 would respond if both percentage of foreign attorneys and number of foreign countries were both included.

Given the close common relationship between international diversification between both percentage of foreign attorneys and number of countries, the increase in the R-Squared to 0.5488 was expected. However, the only other notable changes were 1) interaction between Human Capital and Service Diversification ceased to be statistically significant and 2) Service Diversification ceased to be statistically significant. The signs and coefficient values remained surprisingly stable. The interaction of Human Capital and Reputational Capital remained significant at $\alpha \leq .01$ and negative.

Lastly, Model 8 is identical to Model 5 except that both the dummy variable for elite AmLaw100 firms was added along with the Number of Countries. Again, there did not appear to be any notable changes. The interaction of Human Capital and Reputational Capital remained significant at $\alpha \leq .01$ and negative.
CHAPTER VII

CONCLUSIONS, LIMITATIONS AND IMPLICATIONS

Clearly, the deployment of attorneys abroad presents unique challenges for law firms. There are cultural challenges within firms that contain attorneys from different countries. There also are cultural challenges between the international firm and the foreign jurisdictions in which the firm operates. In fact there are even cultural challenges between the firm and their foreign clients. There are jurisdictional differences. There are regulatory differences. Often, there also are logistical and operational challenges. To date, these complications have been compounded by the lack of previous quantitative research on exactly how U.S. law firms, as a whole, have approached international diversification. The current research is a first step in addressing these issues.

Based upon the descriptive statistics of the populations contained in Chapter V, we now have a glimpse of the characteristics of U.S law firms that maintained international operations in 1998, 2003, 2008 and 2013. We now know that the size of the U.S. firms maintaining international operations ranged from just two to thousands of attorneys. Therefore one implication of the present research is that smaller U.S. law firms can develop international practices of their own. Clearly, internationally diverse
practices are not the exclusive preserve of large firms. Many small U.S. law firms can – and do – maintain successful international operations.

The descriptive statistics also reveal that forty (40) percent of the U.S. law firms maintain international operations in just one foreign country. An implication of this is that U.S. law firms do not need to pursue an entire global strategy to successfully sustain international operations. In the very least, many firms are pursuing regional strategies. Moreover, a sizeable number of U.S. firms are actually pursuing an even more limited strategy that simply links from the U.S. to a single foreign country – such as the U.K.

The descriptive research also has identified that the number and geographic dispersion of U.S. law firms maintaining international operations has been decreasing for years. The deterioration began long before the great recession. The number of attorneys living abroad for these firms has also been decreasing for years. Indeed, in absolute terms, the number of attorneys working for U.S. firms living internationally is stunningly low with less than 4,000 lawyers working permanently abroad for U.S. firms in 2013. Clearly, the globalization of markets has not directly translated into the globalization – through international diversification – of U.S. law firms. Something else is at play and firms of various types are participating.

Looking at the results of the multivariate analysis, the results of the primary model (Model 5) suggests that U.S. law firms are using alternative strategies for serving the international needs of their clients (rather than simply deploying attorneys abroad). This is suggested by the consistent, negative coefficient for the interaction between Human Capital and Reputational Capital. This is also consistent with the descriptive
statistics discussed above. The implication of this is that U.S. law firms developing an international practice should not measure the success of their international ambitions by the number of attorneys actually stationed abroad. What appears to be more appropriate, apparently, is the need to manage capacity utilization of domestic resources as a lynchpin of their international strategy. The way to maximize firm financial performance is to optimize the production of revenue at home – with revenue originated or otherwise facilitated by limited foreign activity. However, more research is necessary to confirm these suspicions.

Optimizing firm performance of international law firms may be achieved in various ways including: usage of communication technologies so that domestic attorneys can remotely serve the needs of clients abroad; utilizing temporary project-based international travel (rather than permanent foreign assignment) for short-term international personal services; and/or cultivating an international referral network or association structure (like vereins) to enable international client service without an international presence. Only additional research will be able to better describe how firms are actually doing this.

Furthermore, the current research (especially Model 5) supports the expected interactions between Human Capital and Leverage. The implication is that International Diversification is positively impacted by increased Leverage in the presence of high Human Capital. The only caveat is to recall that the actual range of Leverage for law firms with successful International Diversification is relatively low compared to some exclusively domestic U.S. firms. Adding one standard deviation to the mean to the Leverage still only resulted in a value that was less than a 2:1 ratio (1.924:1).
Similarly, the current research generally supports the expected interactions between Human Capital and Service Diversification. The presence of higher amounts of Service Diversification and higher levels of Human Capital tend to support a greater amount of International Diversification. Though curiously, lower service diversification paired with low Human Capital also tends to support a greater amount of International Diversification. International Diversification appears to be diminished when there is a mismatch in the level of Human Capital and Service Diversification.

The implication for law firms is that they should adjust the amount of Service Diversification to match their level of Human Capital. Firms with less Human Capital (experience) generally pursue a more focused service offering. In contrast, law firms with more Human Capital can pursue a more full-serviced approach. Both approaches facilitate greater International Diversification.

Lastly, the interaction between Leverage and Service Diversification remains a bit blurry. The interaction was not statistically significant. This might suggest that there are multiple ways that firms balance the extent of Leverage and Service Diversification. Hopefully, future research that will better account for the different strategies of U.S. law firms serving international needs while clarifying these otherwise results.

Beyond the basic quantitative model (Model 5), some of the supplemental models also have practical implications. Based upon the results contained in Models 6 and 8, and the lack of statistical significance of the AmLaw100 dummy variable in each, there does not appear to be any major difference between the International Diversification behavior of the elite, AmLaw100 firms, and the remaining populations of U.S. firms with
international operations. This has important implications. It suggests that smaller firms can – and do – internationally diversify. However, more research in this regard is necessary.

The managerial implications from the current research are intriguing. Quite clearly, the firms that have exhibited exceptional longevity across fifteen years have done so by carefully allocating attorneys abroad while also increasing their media visibility in international publications. Based upon the absence of growth in the foreign deployment of attorneys, it appears that either a) U.S. law firms are utilizing alternate means of serving the international needs of their clients; b) U.S. law firms are actually referring much of the international service needs to foreign firms; or c) both. More research is necessary.

Of course, the current research has some limitations. The research does not include U.S. firms who only send attorneys into foreign jurisdictions on short, temporary, projects. The research does not include U.S. firms who exclusively have foreign clients who enter the U.S. for receipt of services. The research does not include U.S. firms who exclusively use teleconferencing/Skype and email to provide legal services to clients located abroad. The research does not include any network and/or correspondence relationships used by U.S. firms to enable the provision of the firm’s clients by unrelated foreign service providers.

More fundamentally, the current research does not include any analysis of international law firms that were not substantially founded within the U.S. – even though many such “foreign” law firms have offices within the U.S. The research also does not
compare the differences in resource configurations of U.S. firms with international operations to comparable firms without international operations. The research does not include any law firms that failed to have at least one attorney listed as being stationed abroad for each of the years 1998, 2003, 2008 and 2013.

Future research should address these limitations while continuing to clarify the behavior of U.S. law firms as they relate to International Diversification. Besides seeking to address the areas for future research previously mentioned, data from 2014 and 2015 should be examined to determine the extent to which there has been a recovery – if any - in the foreign deployment of U.S. attorneys. Future research should provide a firm survival model that better explains the characteristics as to those who successfully use international diversification and those who are unsuccessful. Future research should also begin to clarify (to the extent possible) whether or not the international diversification behavior of U.S. law firms is typical of all firms – regardless of nationality. Likewise, future research should seek to clarify the broader picture of how U.S. law firms are serving the international needs of their clients. This should involve clarifying how U.S. law firms are utilizing all internationalization modes under the General Agreement of Trade of Services.

In the end, more research is necessary to better understand the strategies used by law firms in serving the international needs of their clients. Hopefully, the current research is the first of many steps in that direction.


APPENDIX
APPENDIX A: Rubric Used For Determining Relation of Law Firm Offices

In regard to the Rubric, a literature search did not identify any articles where any methodology was discussed to systematically classify whether or not different law firm offices were “related” (meaning equivalent to a division or subsidiary). However, given that the Martindale-Hubbell Law Directory did not appear to enforce any strict limitation on listing of purported relationships, a custom rubric was deemed to be necessary.

As a starting point, it should be noted that the traditional organizational structure of U.S. law firms has been the partnership. A “partnership” is a voluntary unincorporated association of two or more persons in pursuit of profit. (*Black’s Law Dictionary*, 1999). Technically speaking, a partnership ends whenever a single partner dies or withdraws. Similarly, a new partnership is created whenever a new partner joins the firm. Unlike a corporation, a law firm usually has as many iterations as lawyers (or groups of lawyers) have joined and exited the partnership over history.

Making matters even more complex is the fact that individual attorneys may belong to more than one partnership at a time. Different partnerships may even have partial overlap roughly equivalent to wholly-owned subsidiaries, partially-owned subsidiaries, divisions, strategic partnerships, etc. The challenge, therefore, was to adopt a methodology for consistently distinguishing those offices that would be considered part of “the firm” for analytical purposes and those that would be excluded.
Looking at the Venn diagram below, the challenge was to systematically identify those offices which had sufficient integration to be considered within “the firm” and distinguish them from those that would be considered NOT within “the firm.”

The approach which was developed was to evaluate all Office-to-Office pairs based upon the rubric below.

The rubric required the scoring of three related questions:

**Question 1:** Do each of the potentially related offices share a common name or URL that suggests significant common or majority ownership?

**Rationale 1:** Independent organizations will rarely risk confusion of trade names with other independent organizations. Similar considerations relate to sharing of web site names. Confusion regarding entity identity undermines the value of brand equities for at least one of the parties – if not both. As such, the greater the similarity of names/url, the greater the likelihood that the different offices are, in fact, related.

**Question 2:** Do each of the potentially related offices indicate significant (but not necessarily identical) links to shared offices?
Rationale 2: If any individual office is, in fact, part of a larger organization, it would be expected that offices within the larger organization would cross-reference each other. In situations where there are only two offices (and therefore no additional offices to reference, the answer to this question must be inconclusive).

Question 3: If any home office is identified in each listing, do each of the potentially related offices – either through express identification or firm profile narrative – identify the same home office profile?

Rationale 3: If two potentially related offices each indicate that their “Home Office” is at a different location, it is much more likely that the two offices are not, in fact, within the same organization for purposes of determining the outer boundaries of “the firm.”

For each of the three questions above, the putative Office –to- Office pair was scored as follows:

“YES, probably” (value=1);
“Unsure” (value=2); and
“NO, probably not” (value=3).

Since there were three questions with three possible answers, the range of total scores for each Office-to-Office pair varied from values of 3 (all “Yes, probably”) to values of 9 (all “No, probably not”). Logically, a score of 6 or greater meant that there was no positive view that the two offices were probably related.

As such, the rule adopted for the Rubric was that an insufficient relationship existed where the rubric score was 6 points or higher. Fortunately, the vast majority of offices were either obviously related or obviously not related. However, when applied to problem situations, the rubric proved invaluable in providing a consistent criteria for inclusion.
Listed below are specific examples of how the methodology was applied.

**Example 1:** Steptoe & Johnson (WVa) to Steptoe & Johnson (Washington, DC). Both offices had a common history and a common name. However, the firm apparently had previously split into two unrelated firms. Foreign offices were only linked to the Washington, DC “home” office.

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<tbody>
<tr>
<td>Application:</td>
<td>Identical Names</td>
<td>None</td>
<td>No</td>
</tr>
<tr>
<td>Score:</td>
<td>1</td>
<td>3</td>
<td>3</td>
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<tr>
<td>Result:</td>
<td>A score of 7, Steptoe &amp; Johnson (WVa) was removed. This was consistent with firm profile comments that the groups were no longer related.</td>
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**Example 2:** Chase Kurshan Suhr Herzfeld & Rubin to Herzfeld & Rubin. The names of the two office groups were distinct but overlapping. The firms linked to each other but only Herzfeld & Rubin linked to foreign offices.

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<tbody>
<tr>
<td>Application:</td>
<td>Maybe. Unclear</td>
<td>Maybe. Unclear</td>
<td>Yes</td>
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<tr>
<td>Score:</td>
<td>2</td>
<td>2</td>
<td>1</td>
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<tr>
<td>Result:</td>
<td>A score of 5, Chase, Kurshan, was listed as part of Herzfeld &amp; Rubin.</td>
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**Example 3:** Deacons, Graham & James to Graham & James. The two office groups had very similar names indicating some relationship. However, each had extensive, separate, international links. However, only Graham & James had a U.S. office.

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<tr>
<td>Application:</td>
<td>Probably.</td>
<td>Not really</td>
<td>No.</td>
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<tr>
<td>Score:</td>
<td>1</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Result:</td>
<td>A score of 7, Deacons, Graham &amp; James was removed.</td>
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Example 4: Studio Legale Gallavotti Honorati & Pascotto to Pascotto & Gallavotti. The two offices each contained two attorneys who apparently had cross-listed their offices. One attorney operated one office and listed the other attorney as of counsel. The other attorney did the same thing. Neither office had any other links to any other U.S.-International offices. The two firm profiles only referenced (but did not link to) each other. Each office profile claimed that it was the “Home Office.”

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<tbody>
<tr>
<td>Application:</td>
<td>Unclear. Maybe</td>
<td>Unclear (only 1 bilateral link)</td>
<td>No.</td>
</tr>
<tr>
<td>Score:</td>
<td>2</td>
<td>2</td>
<td>3</td>
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<tr>
<td>Result:</td>
<td>Total score was 7. Since neither office had any other U.S.-International links, both were removed.</td>
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Example 5: Law Offices of His Royal Highness Prince Saad Al Faisal Bin Abdul Aziz in Association with Arent, Fox (Jeddah) to Arent, Fox, Kintner, Plotkin & Kahn (Washington, DC). Although the only similarity of names was “in association with”, this might have reflected a cultural bias of relating the authority of Saudi royalty to a non-Saudi business association. As such, the profile for Prince Saad could indicate a very significant relationship with Arent, Fox.

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<tr>
<td>Score:</td>
<td>2</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Result:</td>
<td>Total score was 5. Prince Saad was listed as part of Arent, Fox.</td>
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From the examples provided, above, it is clear that the determination of whether or not an office could be considered part of a firm was somewhat subjective. However, in light of these difficulties, the primary goal of the Rubric was to achieve consistent treatment in
determining which offices would be linked to, and included, in the analysis. This purpose was achieved.