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Solo, Small Firm and
General Practice Division

Thomson Reuters Institute

2023 State of U.S. Small Law Firms

A Year of Change



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“The world belongs to those who can change fast”

– *Maxime Lagacé*

Executive summary

Small law firms may be on the cusp of significant changes that could affect how they practice law, as well as their potential for better growth and financial performance.

Technology is definitely part of it, although not necessarily in the way that may come to mind immediately for many.

Small firms occupy a unique spot within the legal industry, making up the vast majority of law firms. Small firm lawyers are both simultaneously legal practitioners and small business owner-operators. Whether a solo-preneur or part of a firm with several dozen lawyers, small firm attorneys must manage and balance both the legal practice and business sides of their firms.

Potentially significant changes are currently underway – both in how small firms operate, and the emergence of new technologies such as generative artificial intelligence (Gen AI) and public-facing tools like ChatGPT – that could help firms more effectively manage of both the practice of law and their business.

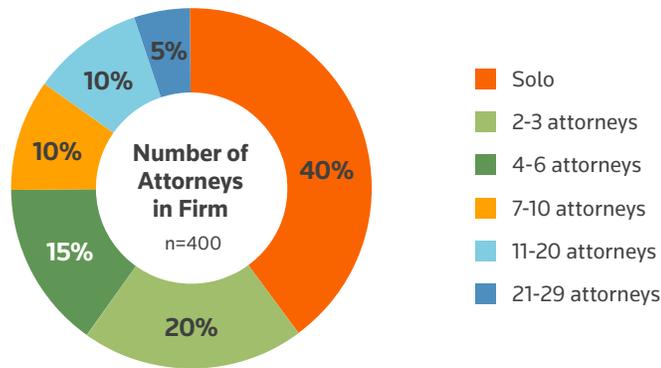
Key findings

- For the first time in several years, small firms are reporting progress against their biggest challenge – they’ve increased the amount of time they spend practicing law while spending less time on administrative tasks.
- Increasing efficiency and better cost control are rising as additional key challenges. Firms are taking steps including investments in technology to improve efficiency and reduce costs.
- Generative AI is currently a hot topic, but it’s too early to assess with any certainty how it will impact small firms. While generative AI tools for legal workflow are just beginning to emerge, other forms of AI-driven technology may have more immediate possibilities for assisting with back-office functions such as marketing.
- Focusing on fundamentals such as improving efficiency, reducing costs, and marketing & business development may hold the most immediate potential for further gains in firm performance.

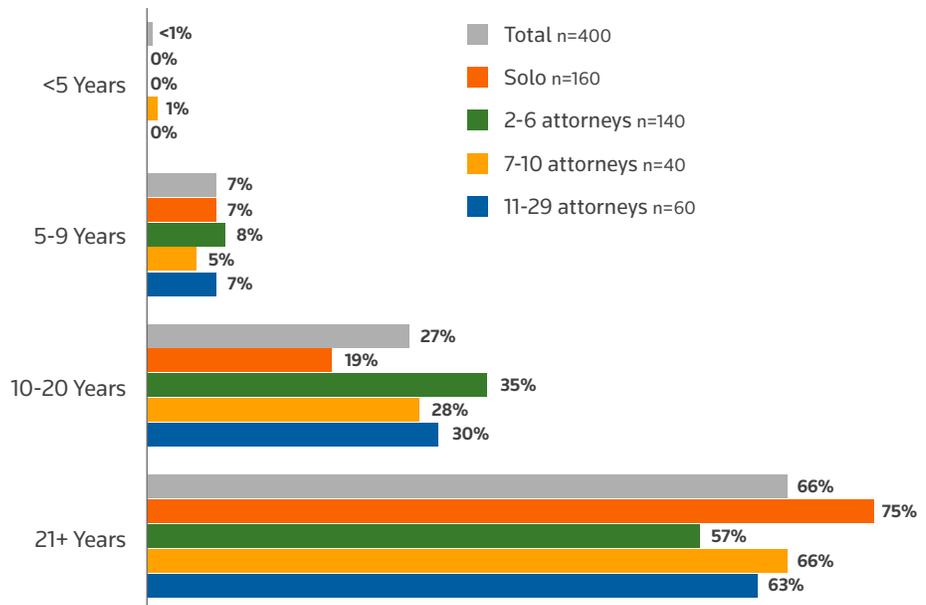
Methodology

The findings in this report are derived from a survey of lawyers within small law firms, defined as law practices with 29 or fewer attorneys. The survey was conducted in July and August 2023.

FIGURE 1:
Respondent demographics



Years of Practice Experience



Source: Thomson Reuters 2023

Time Shift: More practicing of law, less managing of administrative tasks

This marks the eighth annual edition of the *State of US Small Law Firms* report. Previous editions have frequently been a case of “the more things change, the more things stay the same.” Despite consistently identifying several key priorities and goals, small firms were often equally consistent in not making moves to address those priorities. That trend, however, may be changing.

The most significant finding from this year’s report is not related to any of the hot-topic technology discussions. Instead, small firm lawyers may have finally broken out of the recurring, frustrating pattern we’ve seen in previous years in which they have struggled to devote more time to practicing law and less time to dealing with administrative tasks. This is understandably of critical importance because it is literally how small firms and their lawyers make their money. The primary service that every law firm sells is each lawyer’s billable time – and the limitations are the number of hours in a day, and how many of those hours each lawyer can devote to billable activities. At the end of the day, being able to record more billable time is an essential way for small firm lawyers to bring in more revenue.

This year, the percentage of time spent practicing law went up from 56% to 61%.

Each year we’ve conducted this survey, spending too much time on administrative tasks and not enough time practicing law has been at or near the top challenges that lawyers report facing. Despite it consistently being among their top challenges, we had noted a disturbing pattern that the percentage of time spent practicing law had been declining — until this year.

After holding steady in 2021 and 2022, the percentage of time spent practicing law went up to 61% this year, compared to 56% last year. At the same time, time spent on administrative tasks declined slightly to 9% from 11% during the same time period.

FIGURE 2:
Time allotment

Percent of time doing activities



2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

A five percentage point gain in time doing legal work may not, on the surface, seem like a huge gain. However, applied over an entire year with typical workloads, it could equate to roughly 150 additional potentially billable hours or more – the equivalent of several weeks’ worth of time.

As law firms continue to work on every possible angle to increase revenue or decrease costs, few things can beat the ability to simply log more billable hours each month.

What brought about the change this year may be difficult to specifically pin down. As we’ll explore in this report, small firms are increasingly focused on improving efficiency. In addition, the continued normalizing of practice operations and expanded use of technology could be involved.

60 hours per week
x 52 weeks

3,120 hours

5%
x 3,120

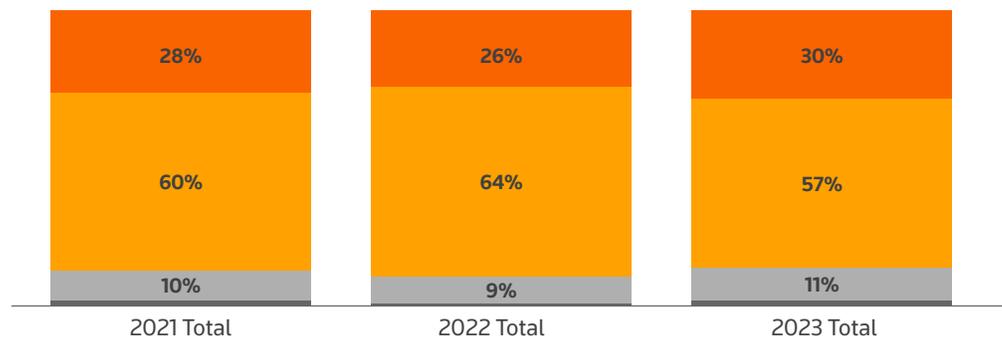
156 potential billable hours

How successful are small law firms?

After dipping slightly last year, the percentage of lawyers that consider their small firm to be very successful rose to a multi-year high of 30%. This was largely accounted for by gains among solo firms and firms with between 11 and 29 attorneys. Outside of those groups, responses were somewhat mixed. The good news is that an overwhelming 87% of lawyers across all small firm sizes consider their firm to be either successful or very successful.

FIGURE 3:
Success characterized

Very successful Successful Neither successful nor unsuccessful Not successful



2021 n=408, 2022 n=400, 2023 n=400.

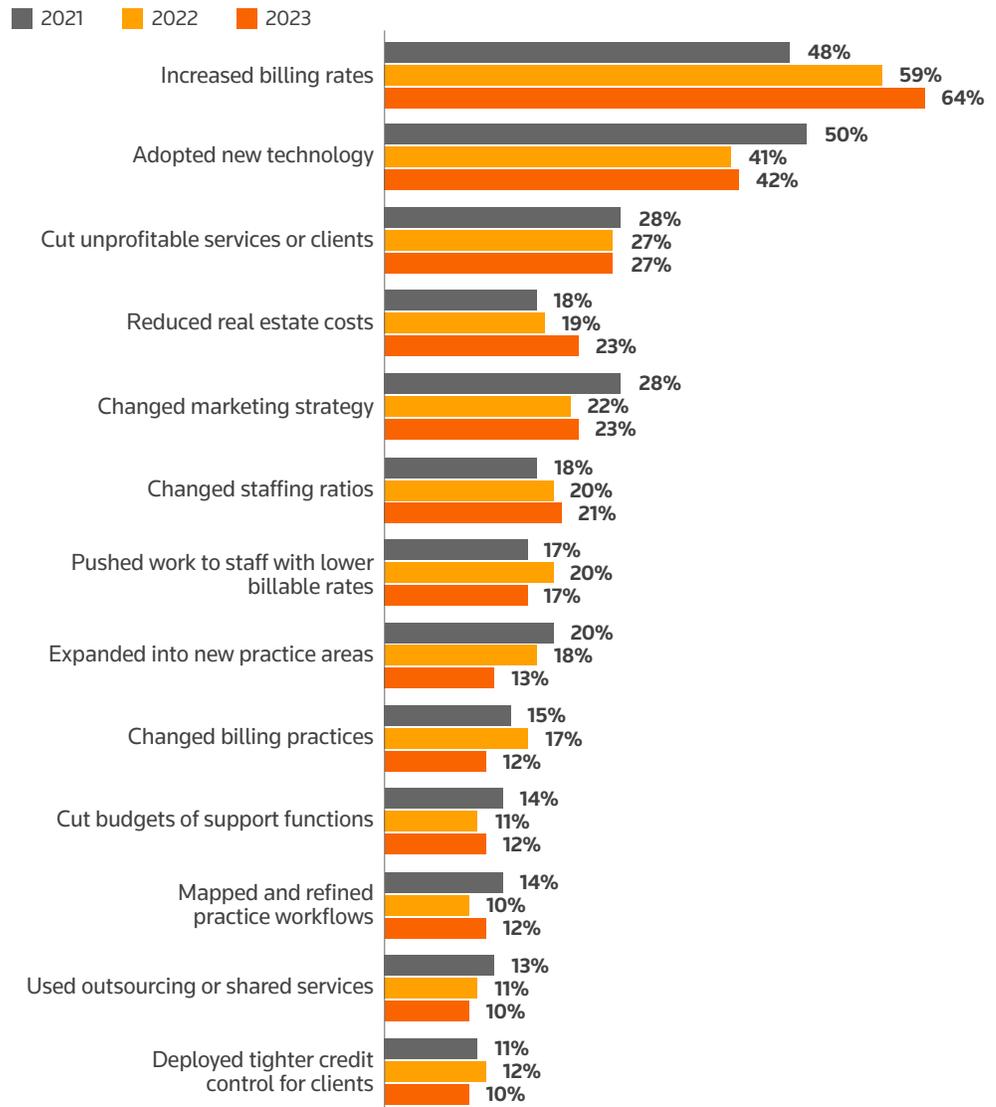
Source: Thomson Reuters 2023

It's noteworthy that looking at the changes that small firms have made over the last three years, the major change has been increases in billing rates. In 2021, less than half of small firms increased billing rates. In 2022, the figure jumped to 59%. It rose again this year to 64%, meaning that nearly two-thirds of small firms increased their rates. Rising inflation was a likely contributing factor prompting this year's rate hikes.

It will be interesting to see whether continuing to push higher rates in order to support revenues will be sustainable going forward. Evidence from larger firms shows that even law firms whose rates are typically higher than those charged by small law firms have been successful in pushing for higher rate growth in 2023.¹ However, if client pushback limits the ability to raise rates much further, firms will need to find other ways to bring in more business to maintain revenues, or conversely, find ways to reduce costs in order to maintain profitability.

¹ See, e.g., *Law Firm Rates in 2023*, available at <https://www.thomsonreuters.com/en-us/posts/legal/law-firm-rates-report-2023/>.

FIGURE 4:
Firm changes



2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

Defining and measuring success

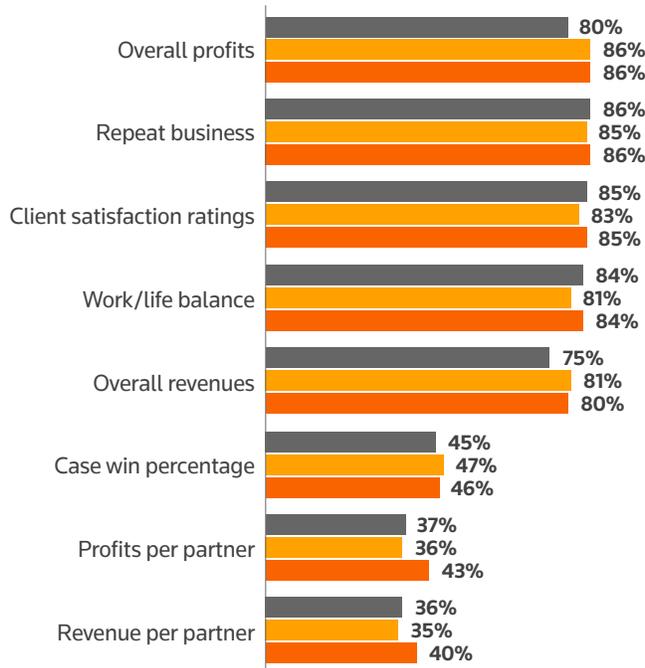
The primary ways that small firm lawyers measure their success have not changed. Overall profits, repeat business, client satisfaction ratings, work-life balance, and overall revenues remain the measures that the vast majority use to determine the success of their firms.

However, there has been a shift in some of the secondary measures of success. The percentage of small firm lawyers who say they use profits per partner and/or revenues per partner has noticeably increased. Although overall profits remains the primary measure of success, lawyers are taking a more detailed look at how those profits and corresponding revenues break out among the equity holders in the practice.

FIGURE 5:
Measures of success

Define success

■ 2021 ■ 2022 ■ 2023



Primary measure of success



2021 n=408, 2022 n=400, 2023 n=400.

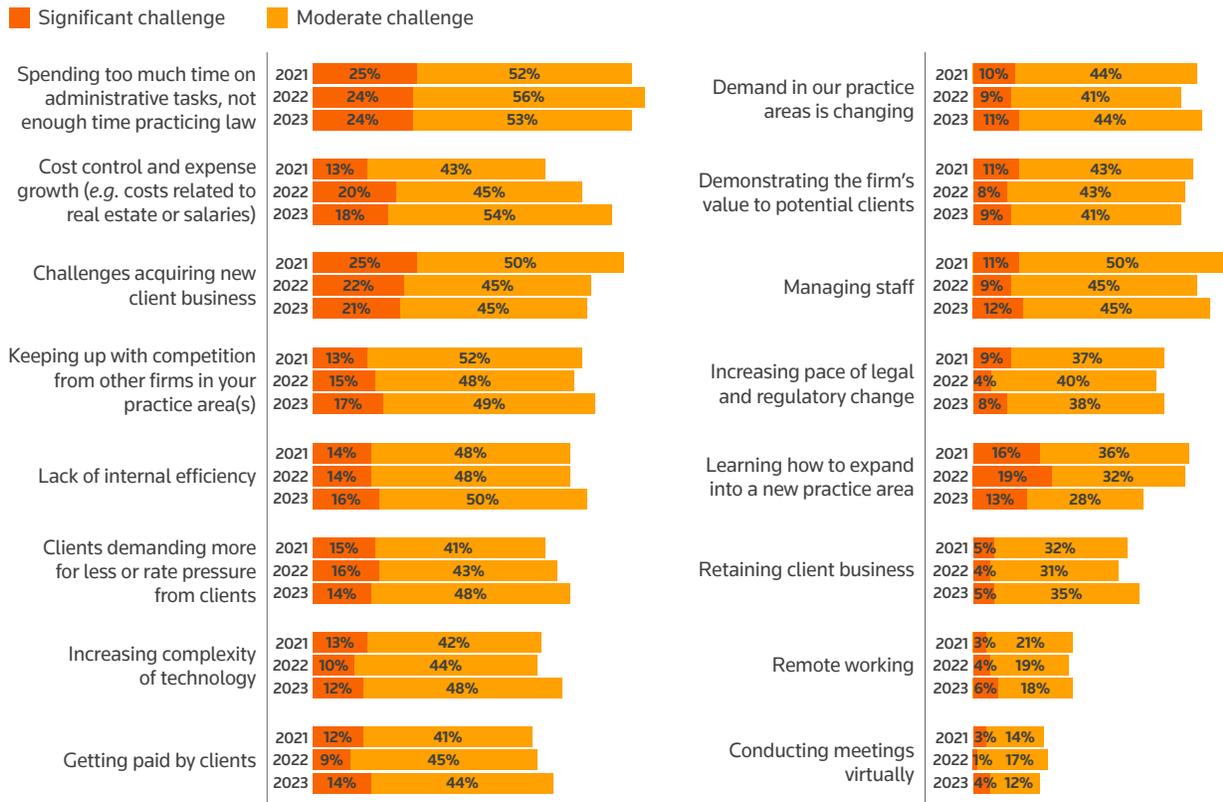
Source: Thomson Reuters 2023

Cost controls are a rising challenge

Meanwhile, controlling costs and expenses has been steadily rising as a major challenge for firms. Two years ago, cost control was only the sixth-highest concern, rated a significant or moderate challenge by 56% of firms. This year, fully 72% of firms say cost control is a significant or moderate challenge. This vaults it all the way up to the second-highest concern, behind only the perennial top challenge of spending too much time on administrative tasks and not enough time practicing law.

Other challenges, such as acquiring new client business, keeping up with competition from other firms in the same practice area, and rate pressure from clients are largely unchanged from last year.

FIGURE 6:
Small law firm challenges



2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

Goals: The quest for greater efficiency

Improving internal efficiency is the top priority for small firms, surpassing even growing the firm. The goal of achieving greater efficiency is also rated as one of the top drivers for firms making changes. This is both laudable and logical, as increasing efficiency, in turn, can make it easier for firms to achieve other goals, such as spending more time practicing law, devoting less time to administrative tasks, reducing costs, and achieving better work/life balance. If firms can achieve more efficiency, it opens the door for re-allocating time and resources into other areas of improvement that lawyers also seek to address.

In addition to efficiency, firms are increasingly focused on client service. In previous years, barely a quarter of firms stated that this was a priority, ranking it alongside other goals such as enhancing the firm’s reputation, differentiating the firm from competition, and succession planning. Now, almost one-third of firms (32%) rank improving client service as a priority, jumping it into a clear third place among firm goals.

FIGURE 7:
Goals and priorities



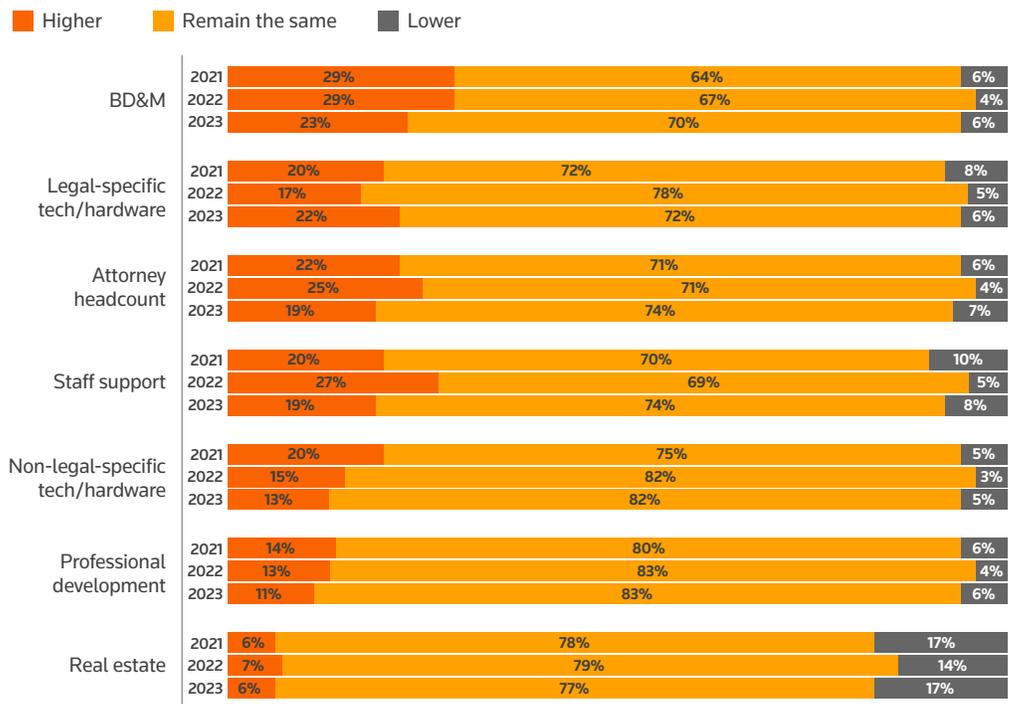
2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

Technology

Not surprisingly, greater investment in technology is one of the top priorities for firms in their push to improve efficiency and reduce costs. And firms are showing a willingness to follow-through in making investments in technology. More than 4 in 10 firms (42%) report they have adopted new technology in the last two years – the most frequently mentioned change aside from increasing billing rates.²

FIGURE 8:
Next 12-month investment areas



2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

And firms appear willing to continue making those investments. Legal-specific technologies and software are the second most-common investment priority, only slightly behind business development and marketing. Some of the biggest projected technology needs include software for case management, legal research and e-billing/invoicing. For non-legal-specific technology, more than twice as many firms are planning to invest in hardware such as computers compared with last year.

² See Figure 6.

FIGURE 9:
Technology/infrastructure investments

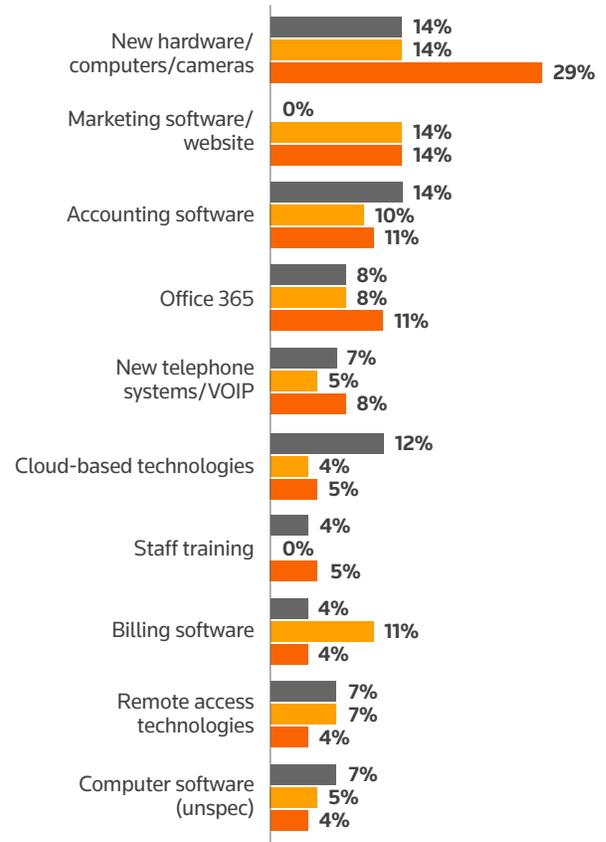
■ 2021 ■ 2022 ■ 2023

Legal-specific tech/infrastructure investments



Investments with at least 4% mentions listed. 2021 n=408, 2022 n=400, 2023 n=400.

Non-legal-specific tech/infrastructure investments



2021 n=83, 2022 n=59, 2023 n=42.

Source: Thomson Reuters 2023

Generative AI & ChatGPT: Big deal or no deal (yet)

When it comes to technology, the most frequent discussions are around artificial intelligence (AI) generally, and generative AI in particular. Since it seemingly burst on to the scene in late 2022 with the release of ChatGPT 3.5, the considerable discussion (some may consider it *hype*) about generative AI has dominated headlines, conversations, and conferences.

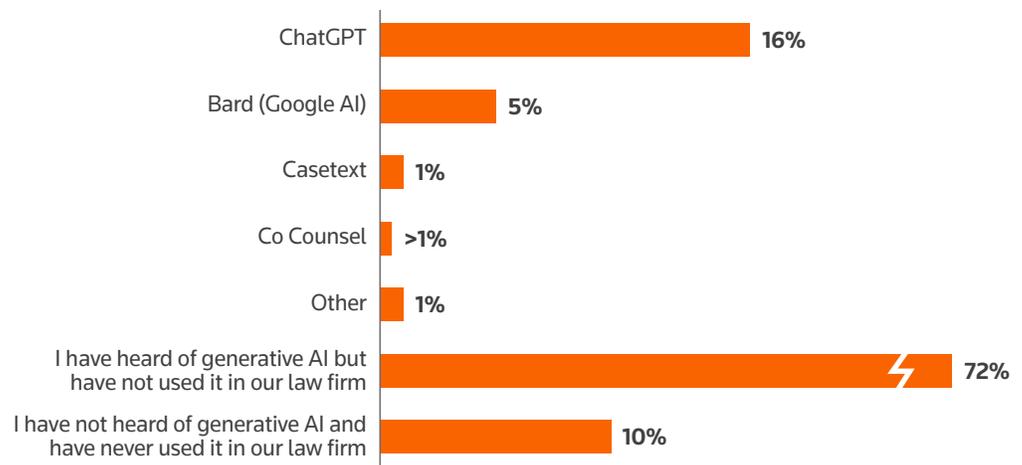
However, it's important to maintain perspective as we're still in the very early stages of generative AI. Like any other technology, it is a tool. And in this specific case, it's a tool whose potential impact is still very much unclear, as very few law firms are currently using it.

As it stands currently, at least as of the time this survey was conducted in August 2023, nearly three-quarters of small firm lawyers (72%) say they have heard of generative AI but have not used it. More than a quarter (26%) say they don't fully understand generative AI – not surprising given the newness of the technology. It is also important to note that awareness of and attitudes toward AI generally, and generative AI specifically, are rapidly evolving.

FIGURE 10:

Awareness and use of generative AI

Generative AI tools used



2023 n=400.

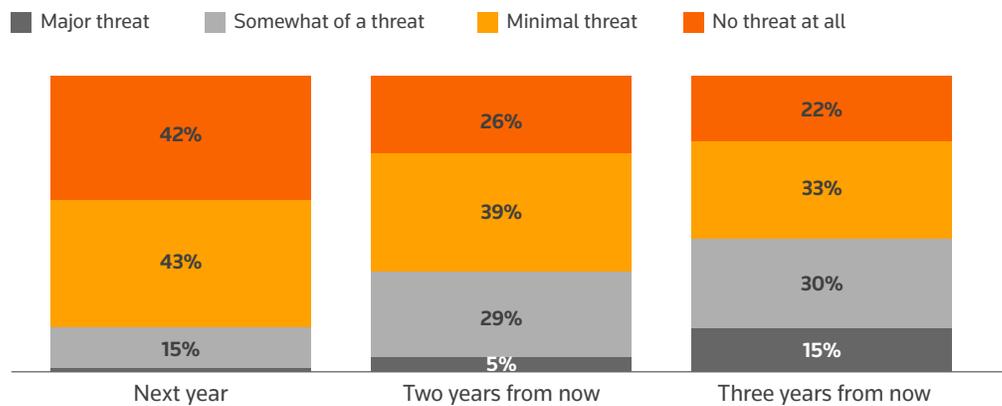
Source: Thomson Reuters 2023

For the legal industry, it remains to be seen whether generative AI will have a transformational impact, like the Internet, be a here-today-gone-tomorrow technology like Second Life, or fall somewhere in between.

As mentioned earlier, small law firms occupy a unique space in that each lawyer’s work involves both practicing law and also functioning as a small business owner-operator. Broadly speaking, AI certainly has the potential to change how small firm lawyers perform both of those roles, and to possibly allow them to do both more effectively and efficiently.

The current uncertainty isn’t stopping small firm lawyers – just like everyone else – from contemplating how much of an impact generative AI could have. As is the case in numerous other industries, much of the discussion involves speculating whether AI represents a threat or opportunity to the future of the profession. At the moment, small firm lawyers are not overly concerned. Fewer than 15% believe it represents a major threat even three years from now. Over the next year, an overwhelming 85% believe it poses a minimal threat or no threat at all.

FIGURE 11:
Potential impact of generative AI



n=400.

Source: Thomson Reuters 2023

The recent Thomson Reuters *Future of Professionals*³ report found that lawyers are generally optimistic about the potential impact of AI. While there are some concerns about job losses, lawyers also believe that AI will create new job opportunities, make their skills more valuable, and enable firms to create new services and revenue streams. One interesting area of speculation is whether AI could help small firm lawyers expand their areas of expertise, potentially enabling them to grow their service offerings and practices to compete with larger firms.

Small firm lawyers are anxiously waiting to see how new AI tools will impact their workflow. While a few tools for legal-specific tasks have begun to appear, a flood of new tools – or familiar tools with AI capabilities added to them – are likely to appear in coming months as vendors race to bring more AI to the legal market. Lawyers will no doubt see growing

³ Available at: <https://www.thomsonreuters.com/en/campaigns/future-of-professionals.html>

AI capabilities in areas such as legal research, contract management, data analytics, case outcomes, and more, although precisely when and how AI will be integrated into those workflows remains unclear.

Perhaps because of that uncertainty, small firm lawyers are also split on how much of an impact AI is likely to have on their legal workflows. Forty percent said they believe generative AI represents either a major or minor opportunity to automate processes. Thirty-five percent said they feel that it does not present such an opportunity.

FIGURE 12:

The opportunity created by generative AI

Opportunity for generative AI to automate processes



n=400.

Source: Thomson Reuters 2023

While much uncertainty remains, we are increasingly confident of one thing: whether one believes AI represents an opportunity or a threat, they are likely both right. Anyone viewing AI as an opportunity will be more likely to undertake a deeper exploration of its increasing capabilities and spot new avenues for adoption and even revenue generation. Those who view it as a threat are more likely to avoid it and risk falling behind the market.

Marketing & business development

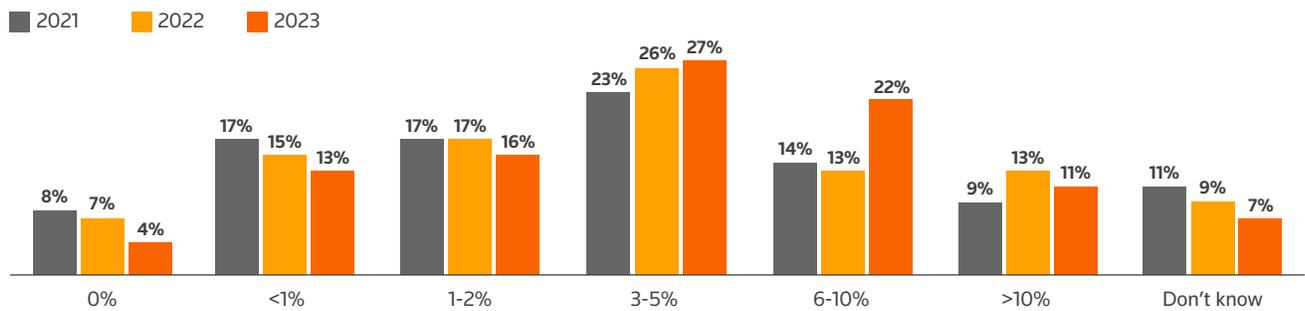
While discussion and speculation about AI continues, in the meantime, there are other areas that demand more immediate action.

Even as firms prioritize improved efficiency and cost controls, they still harbor a desire to grow. In fact, many firms are showing signs of giving the levers of growth increased attention, even amid their efforts to tackle other priorities at the same time.

Chief among the growth levers that they are using to expand their client base is *marketing*. Nearly all firms (93%) report that they are currently conducting marketing or advertising campaigns, up markedly from 84% in 2021. And those firms that were already doing marketing are stepping up their spend. Two years ago, barely more than half of firms were spending 3% or more of their total firm expenses on marketing. That figure this year jumped 8 percentage points to 60%.

And firms that until recently had minimal or no marketing spend are stepping things up as well. Two years ago, more than one-third of small law firms (35%) spent less than \$2,500 on marketing and advertising. That number shrank substantially over the last two years to only 27% of small law firms, meaning more and more small law firms are seeing the necessity of marketing to acquire new business.

FIGURE 13:
Percentage of firm expenses spent on marketing and advertising



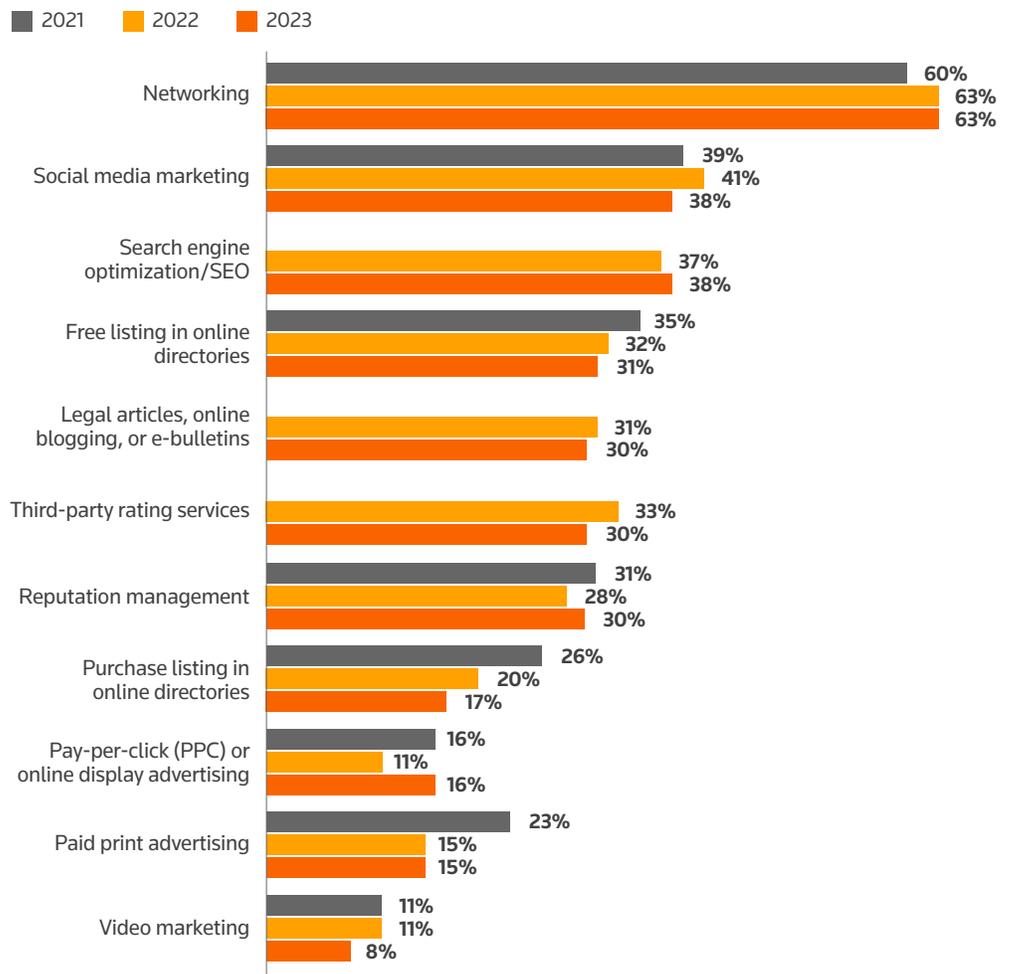
2021 (n=408), 2022 (n=400), 2023 (n=400).

Source: Thomson Reuters 2023

Networking is the most commonly used marketing technique, used by 63% of firms. But other marketing approaches are much less widely used. Online marketing tactics, such as social media, search engine optimization, online directories, blogs, pay-per-click advertising and online video, remain relatively uncommon – none of these tactics are used by more than 38% of firms. This is both puzzling and a tremendous missed opportunity. Firms looking to

ramp up their marketing have ample opportunity to leverage the plethora of online marketing tools and channels that are available to them. A focused online marketing approach could yield huge dividends for small firms. A well-trod marketing cliché holds that “you catch the fish in the ponds you fish in.” Anyone who fishes also knows that you’re more likely to catch fish in waters that aren’t overpressured. Today’s consumers search for nearly everything they purchase online. Why would shopping for a lawyer be any different? And given the relative rarity of online marketing efforts by small law firms, those that make even a modest push in this area may well be among the only boats in those particular waters.

FIGURE 14:
Marketing tactics



Risks with at least 10% mentions listed. 2021 n=408, 2022 n=400, 2023 n=400.

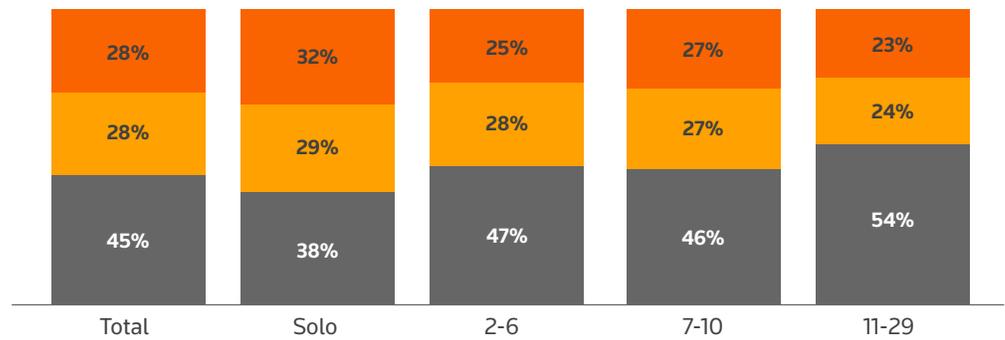
Source: Thomson Reuters 2023

What’s more, many small firm lawyers are quick to admit that they need help in this area. Currently, 45% say they are not confident that their marketing helps drive business for the firm. Barely a quarter (28%) say they are very confident in their marketing. In addition, more than half of firms (53%) say that less than half of their business each year comes from new clients, suggesting significant room to expand their practices.

FIGURE 15:
Confidence in marketing

Confidence market mix/tactics drive business

Very confident Somewhat confident Not confident



Total (n=400), Solo (n=160), 2-6 (n=140), 7-10 (n=40), 11-29 (n=60).

Source: Thomson Reuters 2023

Addressing other challenges

In addition, small law firms are showing increased willingness to tackle other pressing challenges as well.

Getting paid by clients is of increasing concern and seen as one of the top threats to profitability going forward. With it weighing prominently on their minds, the majority of small firms (51%) now report that they are actively addressing the issue.

Similarly, 37% say they are taking steps to deal with the increasing complexity of technology, compared with only 29% last year.

Two years ago, most small firms said they were addressing challenges brought on by pandemic-related disruptions such as remote working and conducting meetings virtually. As the need to address those issues has now greatly diminished, lawyers are able to turn their attention to deal with other challenges they face.

Changes to ways of working

While some of the effects of remote working and online meetings remain common among small law firms, there appears to be an emerging trend in favor of returning to doing business in person.

Remote working clearly declined this year. The number of small firms that reported their lawyers were working remotely peaked in 2022 and declined noticeably this year. While a majority of small firms still report at least some attorneys working remotely, (61%), that's down from 68% last year.

Small firm lawyers are now highly confident in their ability to manage work whether it's conducted virtually or in-person.

Meanwhile, remote client in-take meetings continue to dwindle. An overwhelming 91% of firms conducted some or all of their initial client meetings in-person this year, up from 85% last year.

Regardless of what the future holds, small firm lawyers are now highly confident in their ability to manage work whether it's conducted virtually or in-person. Fewer than one in ten small firm attorneys now say that remote working, conducting meetings virtually, or retaining client business in the current environment present challenges. In short, after weathering the pandemic disruptions, small firm attorneys feel they are ready for whatever the future of working and client interactions will look like.

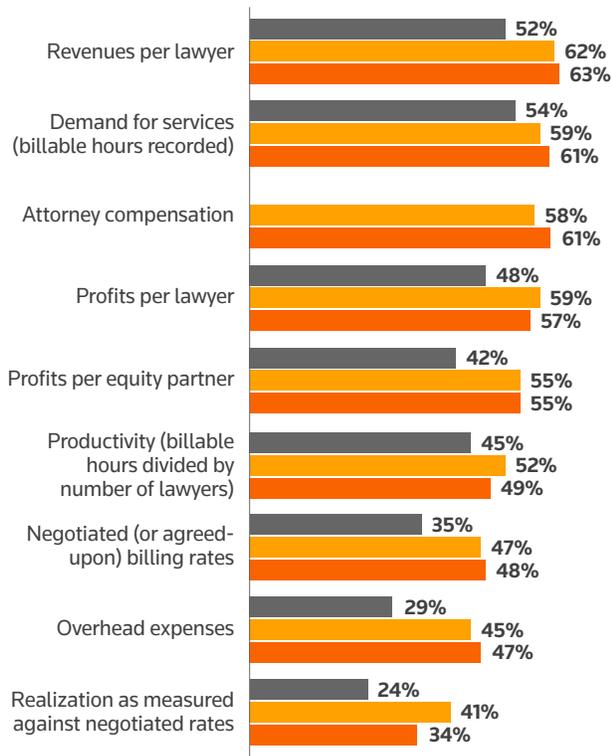
Optimism about the road ahead

Beyond feeling prepared for the future, most small firm lawyers actually appear optimistic about their future prospects. A majority expect moderate-to-high growth across most major financial performance measures over both the next year and the next three years, including demand for services, overall revenues, attorney compensation, profits per lawyer, and profits per equity partner. Bankruptcy, taxation, and intellectual property are the practice areas that are expected to see the most growth over the next year.

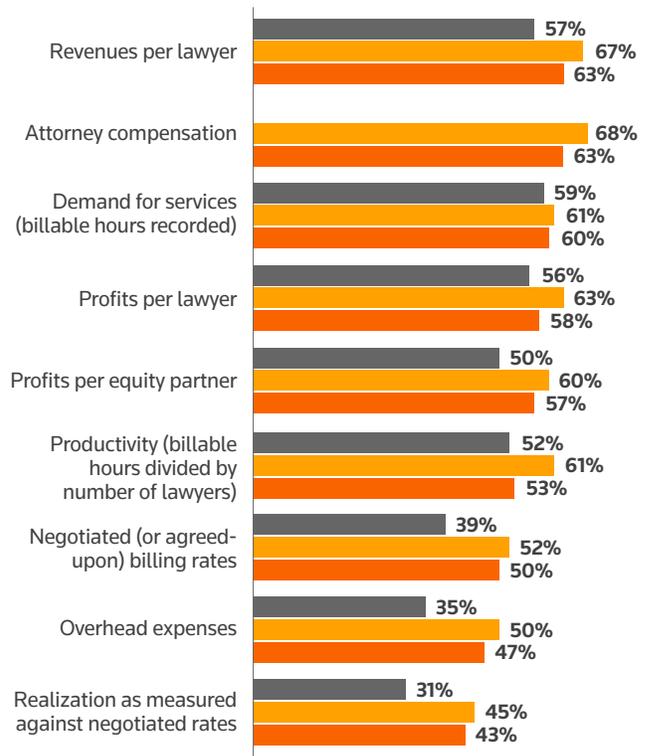
FIGURE 16:
Expected changes in financial performance indicators

■ 2021 ■ 2022 ■ 2023

Change in next year (High/moderate growth)



Change in next three years (High/moderate growth)



2021 n=408, 2022 n=400, 2023 n=400.

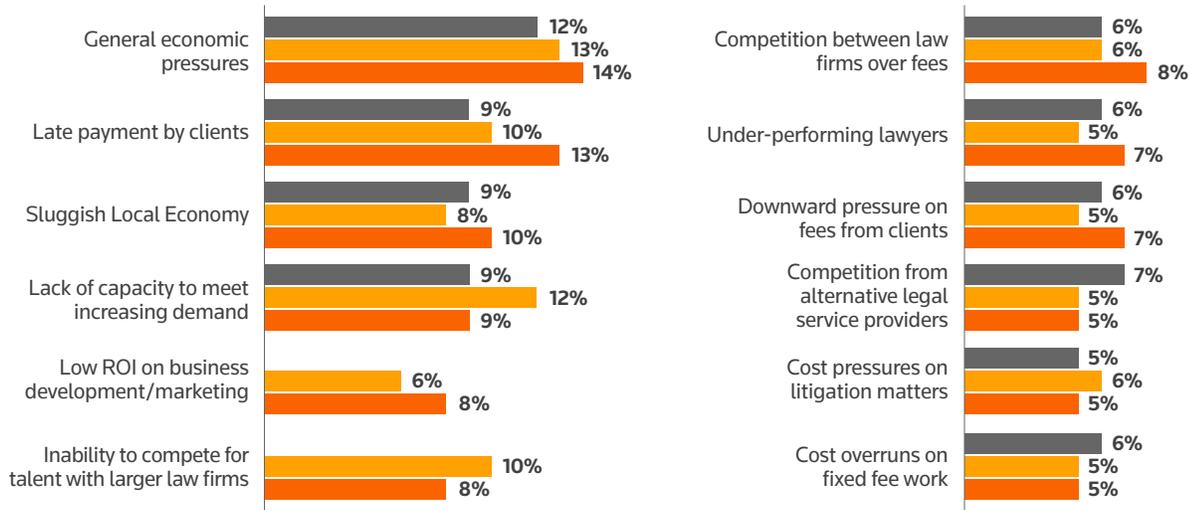
Source: Thomson Reuters 2023

Counter-balancing this optimism, however, is that small law firms have also identified causes for caution. Looking ahead to the next year, general economic pressures, late payments by clients and sluggish local economies are seen as the highest risks to profitability. While these and other risks are definitely present, they currently don't rise to the level to which they are dampening optimism for further growth.

FIGURE 17:

Profitability risks**High risks to firm profitability**

■ 2021 ■ 2022 ■ 2023



Risks with at least 5% mentions listed. 2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

More evidence of this can be found in the fact that few firms have been trimming their attorney ranks. In 2021 and 2022, roughly a quarter of small firms said that the size of their firm decreased. That number fell to only 17% this year.

Part of the reason for firms' optimism may be the mobility of demand currently seen across all levels of the legal market.⁴ Although 40% of small firms rank competition from significantly larger firms as their biggest source of competition, corporate clients are increasingly demonstrating willingness to move work towards smaller firms so long as they can maintain the desired quality of legal work. This desire for strong value-to-price has primarily been seen in work moving from large law firms to midsize firms. However, the same effect is also taking place to some degree with work shifting from both large and midsize to small law firms, especially boutique and specialized small firms.

Another factor likely driving small firms' optimism is their recent success in raising rates – a time-honored method that firms of all sizes have often used to increase revenue. Given recent rate increases, it's not surprising that more than two-thirds of small firms (68%) expect to continue increasing billing rates over the next year. This makes increasing rates by far the most common strategy that small firm leaders said they plan to implement to further improve firm performance.

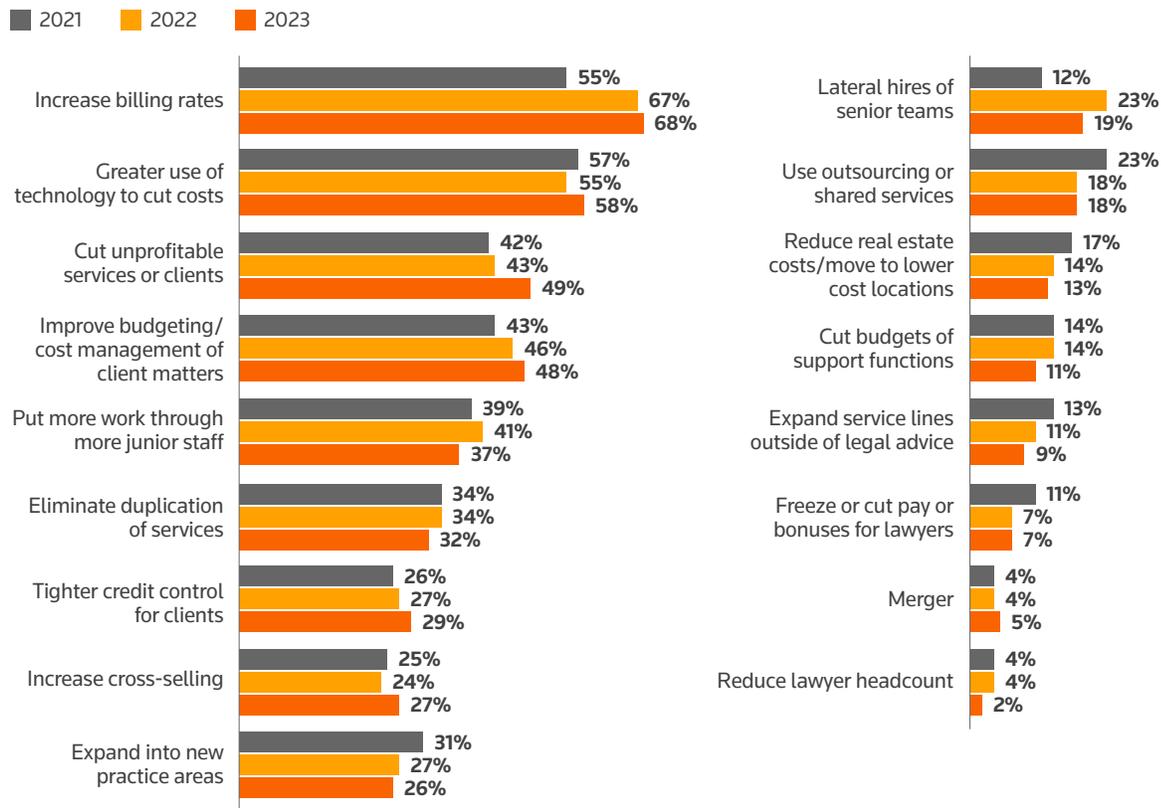
4 See, e.g., *Law firm rates in 2023* at 4. <https://www.thomsonreuters.com/en-us/posts/legal/law-firm-rates-report-2023/>.

While firms expect higher rates to continue boosting revenues, they are simultaneously looking to improve the other end of the profit equation by reducing expenses. Technology will be a key part of that, as more than half (58%) are planning greater use of technology to cut costs in the next year.

After that, expected strategies to improve firm performance are scattered. Less than half of firms expect to cut unprofitable services or clients, improve budgeting or cost management of client matters, shift work to more junior staff, or eliminate duplication of services.

FIGURE 18:
Improving Firm's Performance

Likely performance improvement steps



Steps with at least 10% mentions listed. 2021 n=408, 2022 n=400, 2023 n=400.

Source: Thomson Reuters 2023

Building on a foundation of success

Small law firms have shown this year that they have the ability to “move the needle” and, for the first in several years, have made meaningful progress against their long-standing top goal of spending more time practicing law and less time on administrative tasks. There are a plethora of tactics that firms could employ to further improve efficiency and bring in more business. Additionally, there are numerous avenues for making progress on other goals such as reducing costs.

That begs the question, however; will small firms continue to work those levers and improve their performance, or will they be content to accept current performance because they already view their firms as being successful? The latter could be a recipe for not only stagnation but regression. Client expectations for legal services continue to change, and competition continues to increase, not only from larger law firms but from other providers of legal services.

Small firms have shown they have the ability to make meaningful progress toward the goal of spending more time practicing law and less on administrative tasks.

And lastly, the rapid advancement of artificial intelligence, although still in its early stages, could potentially bring significant transformation to the small law firm space – both in terms of opportunities and threats.

It is of critical importance that small firms hold on to their hard-won gains this year in spending more time practicing law and less time dealing with administrative tasks. Avoiding backsliding into previous habits or losing focus because of distractions or shifting attention to other goals will be key.

Firms remain optimistic about their prospects, and most indications are that such optimism is largely justified. Challenges remain; and change – particularly in areas such as generative AI – could come quickly. But if small law firms can build on the tangible progress of this year and continue to demonstrate the initiative and focus that brought about their recent progress, they may be well poised to continue their upward trajectory.

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