THOMSON REUTERS INSTITUTE

2024 Australia State of the Legal Market

Firms stand at the threshold

Foreword

I am delighted to introduce the 2024 edition of *Australia: The State of the Legal Market*.

This report paints a picture of a strong legal sector with an upswing in demand over the last year across many practice areas. The number of lawyers has increased, notably at the more senior levels, as has productivity. Questions are raised as to whether we are on the brink of a new era of legal practice defined by 'innovation and adaptability.'

In accordance with the trend towards innovation, Australian law firms have also increased their spending on technology in the last year. This is not surprising – the advent of generative AI has disrupted, and has the continuing potential to disrupt, ways of work in legal practice. Law schools are also grappling with the challenge of GenAI. Not only are there questions as to how such technology may be used by students in their studies, but also how GenAI should be integrated into the overall curriculum, given that this will be an important skill for future lawyers.

I make two other brief reflections on this report.

First, the report highlights that there has been a change in the nature of partnerships, with a growth in non-equity partners in many law firms. While this change has advantages for individuals, the report notes that it could potentially result in a lack of diversity in the critical decision-making processes of law firms which may limit innovative thinking in the future. More broadly, as legal educators, we must ensure that law students are equipped, not only with the necessary technical skills, but are also able to be creative in responding to changes in legal practice.

Second, as Professor Harding highlighted in 2023, while technology will continue to drive legal innovation, we must remember that good lawyering is comprised of a range of very human qualities. It is important that, while we continue to integrate technological innovation into the curriculum, we also teach skills that emphasise the role of empathy, critical reflection, and teamwork.

The report suggests that we may be at a pivotal moment in legal practice. I commend it to you for close reading.

Alison Duxbury

Professor Alison Duxbury
Interim Dean,
Melbourne Law School

© Thomson Reuters 2024

Executive summary

The Australian legal market is currently experiencing a period of unprecedented dynamism. The 2024 financial year (FY 2024), which ended 30 June, has seen demand for legal services across the practice spectrum rising at a stunning 7.5% average pace even as rates continue to grow at an historically high speed. At the same time, law firms are surging in size and technological investment, a direct response to the insatiable market demand for legal services. The ultimate result of this surge in demand and battle for scale is an explosion of profitability, with the average firm increasing its total profit by 19.0%.

Yet, beneath this surface of growth and prosperity, the path to long-term career stability for individual lawyers appears to be shifting. The door to full equity partnership for many lawyers is calcifying shut, even as the number of qualifying lawyers competing for the full ring grows. On a more fundamental level, the advent of generative artificial intelligence (GenAI) looms large, heralding a wave of disruption with its vast potential to redefine the roles and functions within law firms.

Are we experiencing the last great period of traditional legal practice, or are we on the brink of a new era that will redefine the industry through innovation and adaptability?

This pivotal moment raises a critical question: are we experiencing the last great period of traditional legal practice, or are we on the brink of a new era that will redefine the industry through innovation and adaptability?

This is by no means the first time that people have found themselves at a metaphorical crossroads, looking at both the past and towards the future. Indeed, the Romans even had a god for such moments of transition and change: Janus, the god of beginnings, doorways, thresholds, and endings. Distinct among Janus's many features were his two faces: one looking backward into the past and another forward into the future.

In this light, the challenges faced by today's law firms in Australia are not just hurdles but are also opportunities — doorways to redefine roles and to sculpt the future of the legal practice. And embracing these opportunities and addressing these challenges requires a Janus-like vision, a capability to maintain a foothold in the established strengths of the past while stepping forward beyond the threshold into the uncharted territories of the future.

How the legal industry responds to these aspects of opportunity and challenge will define its trajectory for years to come. Law firms that can balance the thriving demand of today with strategic adaptations for rapidly approaching technological shifts will be best positioned to thrive. Those that fail, either by remaining too entrenched in a past or by recklessly embracing a future they do not understand, may go the way of the Romans themselves.

© Thomson Reuters 2024

Methodology

Over the course of FY 2024, the financial metrics in this report were collected from Thomson Reuters Financial Insights data, which is based on the accounting systems from 20 participating law firms operating in Australia. These include some of the largest firms by qualified-fee-earner-count in the region. Global metrics are based on 240-plus law firms, primarily located in the United States and the United Kingdom, which also participate in the Financial Insights program. Some numbers may have changed since the issuance of the FY 2023 report due to revision or changes in methodology.

Client insights included in the report were based on interviews with 84 Australian legal service buyers over the course of FY 2024, conducted by Thomson Reuters Market Insights.

© Thomson Reuters 2024

A surging market

"For now, the times are better than they have been. And they hold the potential for so much more."

-2023 Australia: State of the Legal Market Report

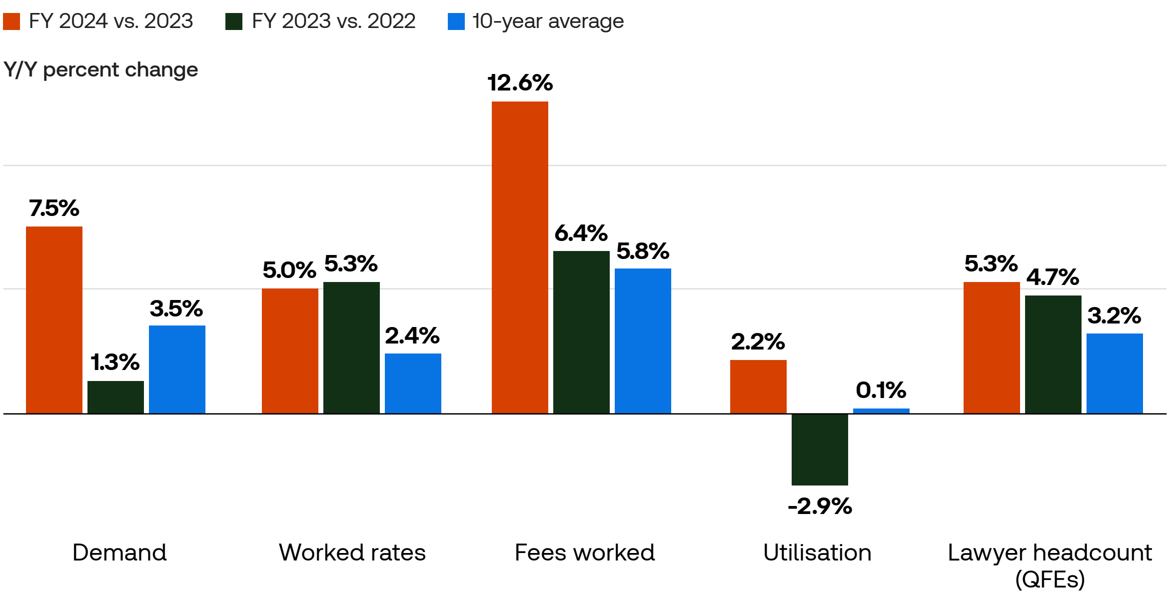
Fulfilling the promise of 2023

Before the large law firm industry's remarkable performance in FY 2024, it had faced a challenging recovery in FY 2023. The first half of FY 2023 was marked by low legal demand and high expenses, creating a difficult situation that took the subsequent six months for firms to largely overcome. Even then, firms ended FY 2023 with high expense growth and notably lower profits per equity partner (PPEP) than they did in FY 2022, snapping a long-running growth streak. Yet, the stage had effectively been set for 2024's titanic performance, as the average law firm ended FY 2023 with 6% growth in demand in the second half of the financial year, a significant spurt of momentum.

Compared to the up-and-down performance of the previous year, FY 2024 has been defined by a surge in demand which has not ebbed, even against volatile baselines. Law firms set a record for yearly demand growth with 7.5% average growth in FY 2024 compared to the previous year, far outpacing the previous 10-year (FY '14 - FY '23) average growth rate of 3.5%. On the back of another year of strong worked-rate growth, this pulled fees-worked[1] growth up to 12.6%. For perspective, if firms were somehow able to maintain this pace, they would *double* the total hours they work by 2030.

FIGURE 1:

Key performance indicators



All fee earners; billable time type; AU Offices.

Source: Thomson Reuters 2024

1 Fees worked is a proxy for revenue growth before contingent matters, subsidiary revenue streams, and realisation are taken into account.

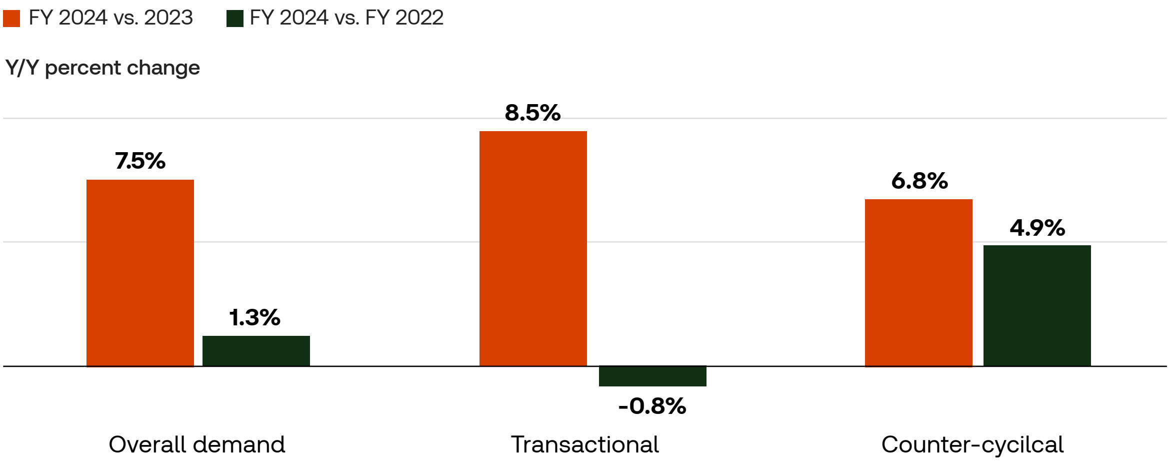
© Thomson Reuters 2024

Demand growth from all sectors

Recent history for law firms globally has been that demand operates in cyclical patterns, where surges in demand tend to be centered around particular macro-practice groups such as the transactional group.[2] Australian law firms experienced this in FY 2023, when counter-cyclical[3] law practices carried the day as transactional practices struggled. This was not the case for FY 2024 where the demand surge that law firms experienced was broad based, coming from both the transactional and counter-cyclical practice groups.

FIGURE 2:

Demand growth – macropractices



Practice proportion FY 2024:	50%	30%

All fee earners; billable time type; AU Offices.

Source: Thomson Reuters 2024

Transactional demand led the way with 8.5% yearly growth, while counter-cyclical demand followed closely at 6.8%. However, this comparison is somewhat skewed, as counter-cyclical growth was measured against the intense growth of FY 2023, whereas transactional growth had a baseline of a slight contraction. In this context, counter-cyclical's growth has been the primary contributor over the last couple years to firms' overall success, yet transactional demand's pickup is still greatly beneficial. Not surprisingly, there are multiple standout areas. Every major practice is experiencing growth, with those such as banking and finance, corporate general[4], construction, workplace relations, and dispute resolution at the forefront.

2 For the purposes of this report, the transactional practice group is composed of corporate general, mergers & acquisitions, banking & finance, real estate, and tax.

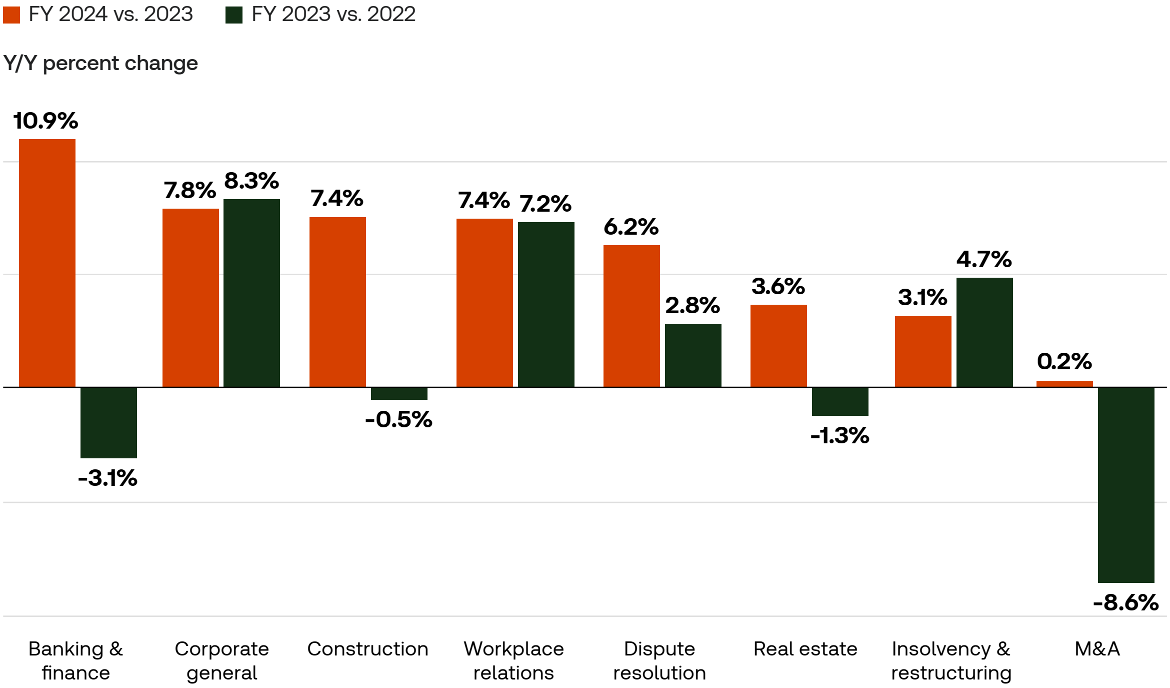
3 For the purposes of this report, the counter-cyclical practice group is composed of disputes & litigation, insurance coverage, insurance defense, workplace relations, and insolvency & restructuring.

4 Corporate general work is corporate work not explicitly related banking & financing or merger & acquisitions matters.

© Thomson Reuters 2024

FIGURE 3:

Practice demand growth



FY 2024 proportion:

Banking & finance	Corporate general	Construction	Workplace relations	Dispute resolution	Real estate	Insolvency & restructuring	M&A
9%	13%	9%	6%	20%	8%	2%	8%

All fee earners; billable time type; AU Offices.

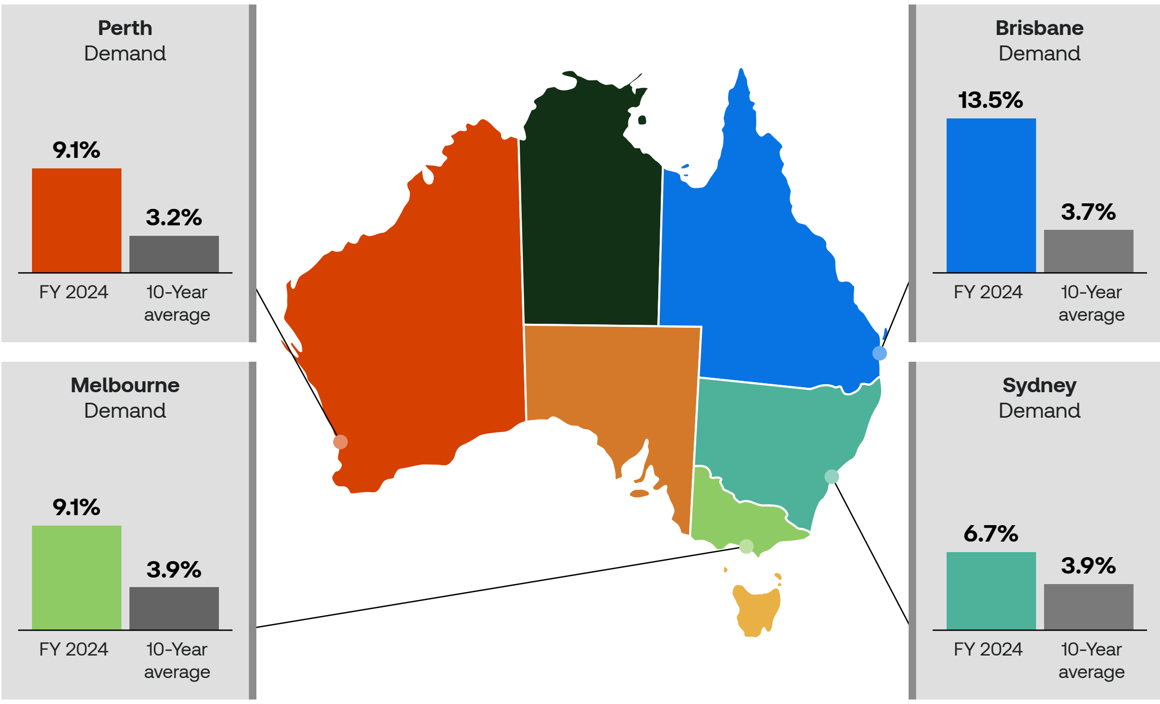
Source: Thomson Reuters 2024

From a geographic perspective, no region is being left out of this growth surge. Sydney, the largest market by total volume of revenue, is growing demand the slowest at a still-impressive 6.7% in FY 2024, notably outpacing its 10-year average growth pace. Other regions such as Melbourne and Perth are growing at more than 9% year-over-year, with Brisbane experiencing a searing 13.7% increase.

While the pace of the current upswing in demand is unprecedented in recent history, the overall upwards trajectory of Australian law firms is not. Firms have been on a long-term growth surge since the Hayne Royal Commission in FY 2018, which broke a stagnant period that had effectively lasted since the global financial crisis a decade earlier. Since then, Australian law firms, on average, have grown demand for the average firm by 38%, far outpacing the 6% average growth achieved by firms in the US during the same time span. It should be noted that it isn't just the biggest of the big Australian firms that are growing at this exceptional pace. Indeed, those large firms just outside of the largest echelon in Australia are also growing at a substantial (if not superior) rate.

© Thomson Reuters 2024

FIGURE 4:
Regional demand growth



All timekeepers, billable time type; non-contingent matters.

Source: Thomson Reuters 2024

Mining, politics, and beyond

As for why this growth in legal demand may be occurring, it may be because the economic fundamentals of Australia remain relatively strong compared to the global economy, with multiple boosting factors pushing demand to new heights.

A major source of this growth is the mining industry, which itself is undergoing an intense period of reorganisation. The greater push in Europe and the United States for supply chains to be centered in politically aligned nations (often referred to as *friendshoring*) is putting intense demand on many countries — Australia especially — to develop and expand existing capacity. Traditionally, *mining* in Australia has been synonymous with coal and iron but increasingly the industry is pivoting towards electric-battery-related minerals and rare earth elements, a transition that requires sizeable investments and thus, additional legal work. Unlike banking and finance work, for example, the legal work for mining tends to span multiple practices, from environmental law to corporate general and labour and employment, providing a broad upswell.

Brisbane's hosting of the Summer Olympics in 2032 may likewise be a contributing factor, with demand in that market growing by the most of any major region, with 13.5% growth compared to its 10-year average of 3.7%.

The potential for this demand to continue is apparent from data on buyer sentiment, which shows a Net Spend Anticipation (NSA) of 14,[5] reflecting that more respondents anticipate increased spending than are expecting a decrease. This strong NSA is particularly visible in regulatory as well as labour and employment, although M&A work is likewise appearing strong. While the

5 Net Spend Anticipation is calculated as the percentage of GCs that said they expect legal spend to increase minus the percentage of GCs that said they expect legal spend to decrease. Number of responses: Overall (2340); Australia (99).

© Thomson Reuters 2024

high demand for these practices is not unique to Australia, it's notable that Australia has been something of a leading indicator, standing alone with strong NSA scores until other regions recently saw improvements.

FIGURE 5:
Legal spend anticipation

> +20% 0% to +19% < 0%

Net spend anticipation by country/region: Jul23-Jun24 (percent of buyers increasing spend minus those decreasing spend in each work type)	Global overall	Australia	US	Mainland Europe	Japan	China
Regulatory	+28	+23	+30	+29	+44	+10
Labor & employment	+15	+23	+17	+10	+26	0
Corporate	+13	+8	+13	+9	+7	+6
Disputes	+10	+6	+12	+3	+22	+3
Intellectual property	+5	+1	+4	+3	+25	+5
Insurance	+3	+1	+5	-2	+4	+1
M&A	+2	+12	-1	+3	+30	+2
Banking & finance	0	-4	0	-5	0	+1

Number of responses: Global overall (2320); Australia (84); US (951); Mainland Europe (285); Japan (81); China (107).

Source: Thomson Reuters 2024

Prices rise at intense pace for third straight year

It is notable that the intense demand for legal services is perhaps manifesting beyond the sheer quantity of hours firms are now working. Worked rates, or the rates clients have agreed to pay at the onset of a matter, are also growing at a record pace, up 5.0% over FY 2023's historically high performance. FY 2024 maintains a continuing streak of growth that started in 2022 and has averaged 5.7% yearly increases. Prior to 2022, worked-rate growth averaged just 1.1% year-over-year, a period partially explained by the price-capped work of the Hayne Royal Commission but yet predated that event. As seen, these price increases have not blunted demand growth and while realisation has decreased over the last couple years, those decreases have been nowhere near the levels which would counterbalance this degree of rate growth.

As a result of all these factors, fees worked has been pushed to its highest yearly growth since at least 2014, with the average law firm seeing a 12.6% increase in fees worked over FY 2023, more than twice the 10-year average pace.[6]

6 See figure 1 on Page 5.

© Thomson Reuters 2024

Struggling to keep up, firms expand both their people and their tech

With legal demand growing by 7.5% year over year, it may not be surprising that law firms have had to considerably increase their capacity in order to keep up. The average Australian law firm increased its lawyer headcount or qualified fee earners (QFEs)[7] by 5.3% over FY 2023, an aggressive albeit not record-setting pace. When taking into account the growth since FY 2022 however, the true scale of firms' upscaling becomes more apparent.

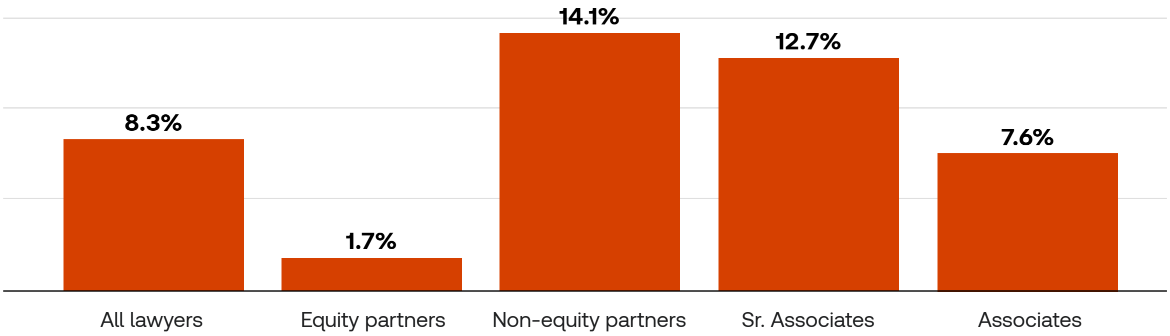
Most of the average firms' headcount growth since FY 2022 has been focused on experienced, veteran lawyers. Growth of 12.7% in senior associates has outpaced the rate of growth for junior associates, which has increased by 7.6%. Yet it is non-equity partners who have been brought on at the most aggressive rate of 14.1% growth.

Law firms thus seem to be prioritising experienced talent at a time when the future of the partnership and law firm talent in general is increasingly shifting.

FIGURE 6:

Lawyer QFE growth

Percent change since FY 2022



Lawyers (contractors excluded).

Source: Thomson Reuters 2024

Productivity perspectives

Despite this intense headcount growth, productivity for the average Australian lawyer significantly increased over the previous year, with the average law firm logging a 2.2% increase in hours worked per lawyer QFE. While there have been some productivity difficulties in recent years, Australian firms remain in line with historic values.

Indeed, a major factor that sets these firms apart from their counterparts in the United States is that Australian firms have held a long-term advantage in maintaining productivity. US firms, on the other hand, have seen a double-digit percentage-point drop in utilisation since 2013, with the average US lawyer working 87% of the hours they may have been working in 2013. Australian firms, even after the productivity contractions over the last three years, are slightly up at 109% on the same measurement. In other words, Australian firms could afford some minor productivity loss and still hold their advantage.

7 Firm-employed lawyer, full-time-equivalent, or qualified fee earners.

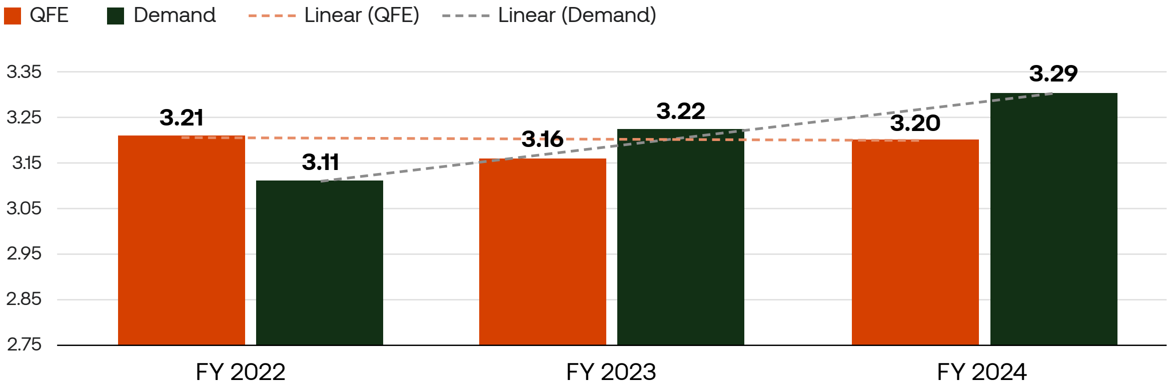
© Thomson Reuters 2024

Importantly, many Australian law firms have also managed to translate this utilisation increase into much stronger demand leverage.[8] Non-partner to partner QFE leverage[9] has remained relatively stable over the last three years as firms balanced increases in headcount on both sides of the equation. The important development for firms lately has been the increase in demand leverage, which in FY 2022 stood a few points below QFE leverage but has since surpassed it by a significant degree. In essence, this shows that firms are now effectively utilising their non-partner lawyers, pushing work to the lower echelons of the firm which in turn allows junior lawyers to develop professionally while providing a notable profit advantage for the firm.

FIGURE 7:

Leverage

Non partners QFEs to partner leverage



Qualified fee earners; billable time type; AU Offices.

Source: Thomson Reuters 2024

Firms rapidly investing in technology

There is far more to firms' efforts to scale than merely bringing on more lawyers. Firms' overhead[10] expenses have continued to balloon since FY 2023, with the average firm's overhead expenses increasing by 8.8% in FY 2024. So, what are firms spending their money on?

It would be malpractice at this point not to mention the 1,000-ton supercomputer in the room. Much in the way GenAI dominated the conversation in 2023, the current year continues to see this developing technology disrupt the large law firm market as firms scramble to keep up with a rapidly evolving space. While the industry may not yet be at the point in which GenAI is actively involved in legal work at a significant scale, it is having a substantial impact on firms' expenses. Knowledge Management, the expense category technologies such as GenAI fall into, grew 6.4% per QFE in FY 2024, making it the third fastest growing major category of expenses. If one groups the spending on knowledge management, other tech spending, as well as the compensation for related staff, the category as a whole is growing at 6.7%.

This is a significant degree of investment, but it is also one of the few areas in which Australian law firms are actually falling behind their counterparts in the United States. While Australian firms are investing in their real technology group[11] by 2.9% more than inflation[12] the average US law firm is growing its real tech group spending by 4.7% above inflation.

8 Demand leverage is a measure of how work is distributed to partners compared to all other lawyers at the firm in the form of a ratio; *i.e.*, 3.1 hours per non-partner QFE to every hour of partner QFE.

9 QFE leverage is a measure of how headcount is distributed to partners compared to all other lawyers at the firm in the form of a ratio, *i.e.* 3.1 non-partner QFEs per partner QFE.

10 Overhead expenses are those expenses not directly attributed to lawyer QFEs, such as support staff compensation, technology, rent, and office expenses.

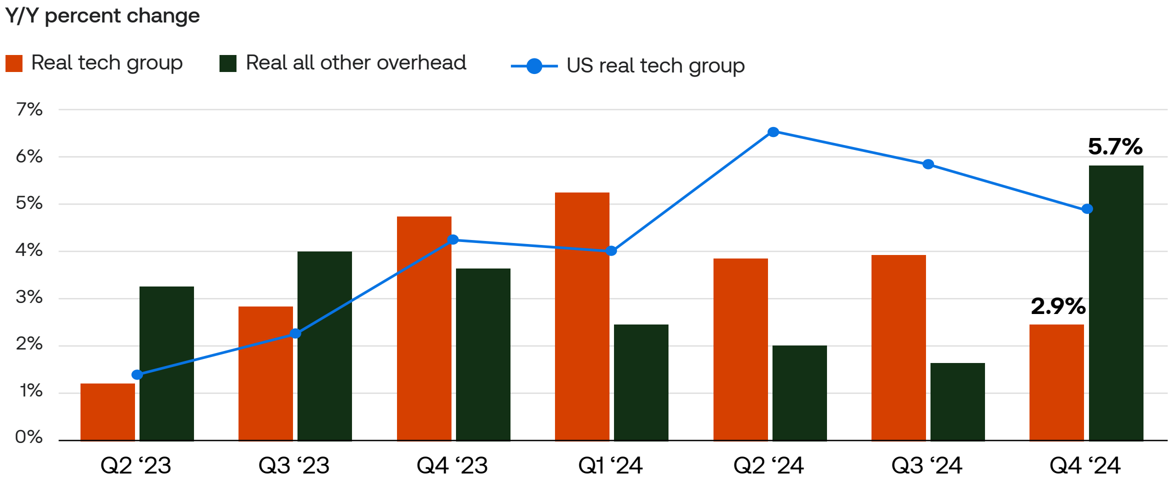
11 Real technology group spending is an average measure of firms' total spending on technology, knowledge management, and relevant staff compensation, minus inflation.

12 Measured as the year-over-year increase in Australia's Consumer Price Index (minus food and energy). Also referred to as CPI Core inflation.

© Thomson Reuters 2024

FIGURE 8:

Real tech group spending vs. real all other overhead



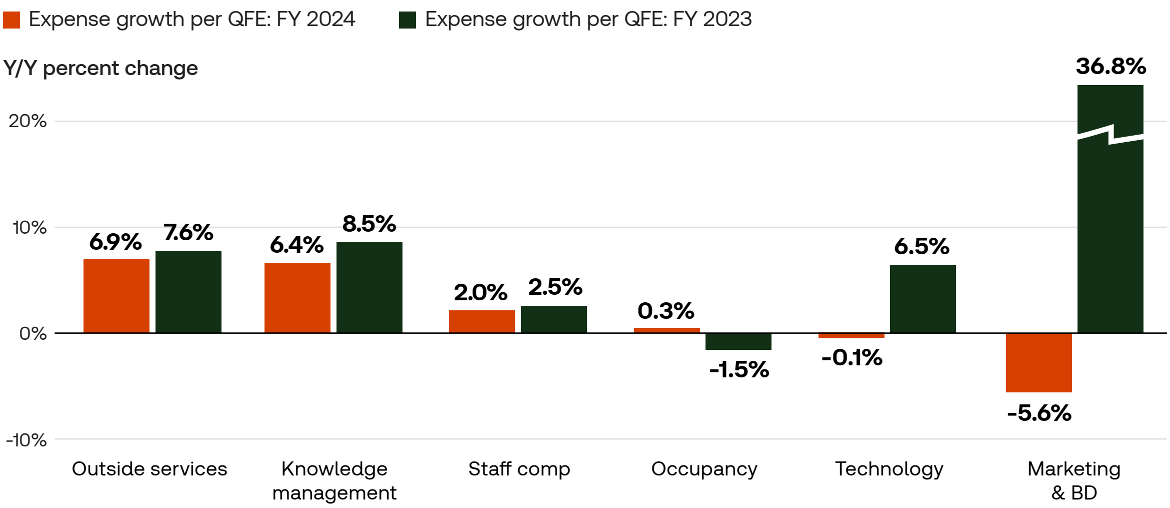
All expenses are calculated on a rolling 12-month average.

Source: Thomson Reuters 2024

Indeed, Australian firms' spending on technology has also fallen behind their own spending in other categories, the result of an investment spree firms undertook in the final quarter of the year. Accounting for inflation, Australian firms are growing all other overhead spending by 5.7% more than inflation.

FIGURE 9:

Indirect expense growth per QFE detail



FY 2024 proportion:

Outside services	Knowledge management	Staff comp	Occupancy	Technology	Marketing & BD
9%	4%	32%	21%	11%	5%

Expense growth is on a rolling 12-month basis.

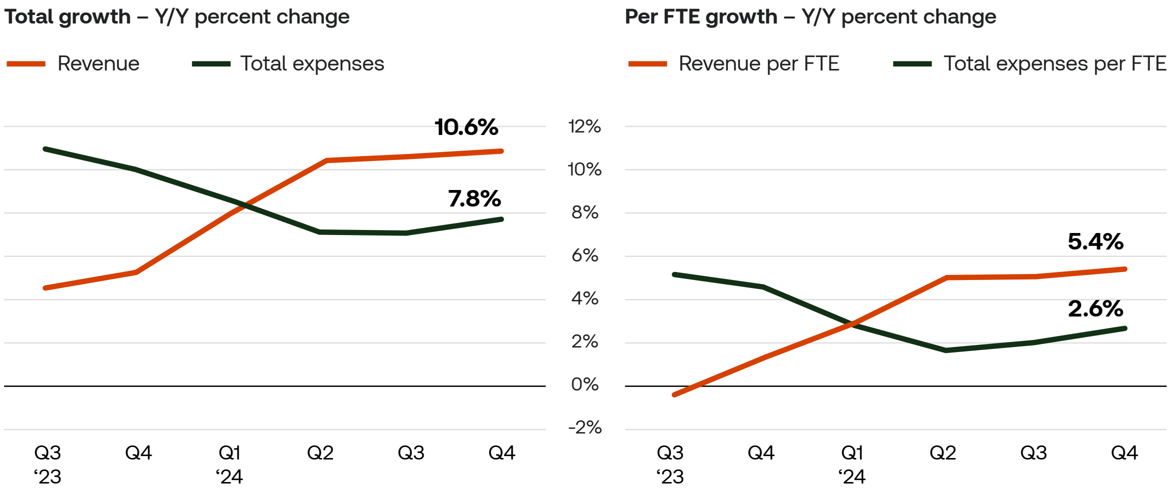
Source: Thomson Reuters 2024

© Thomson Reuters 2024

Recent history for large law firms shows how easily historic profit growth can be erased if expenses are allowed to grow out of control. In Australia, late-FY 2021 and early-FY 2022 saw a surge in transactional demand and rates that brought revenue growth to previously unforeseen levels. Yet an incredibly expensive war for talent combined with a subsequent hiring spree greatly depleted any of the revenue that these firms were amassing. Once transactional demand fell off in late-FY 2022, firms were left in a lurch that resulted in FY 2023's profit contraction.

FIGURE 10:

Total expense vs. revenue



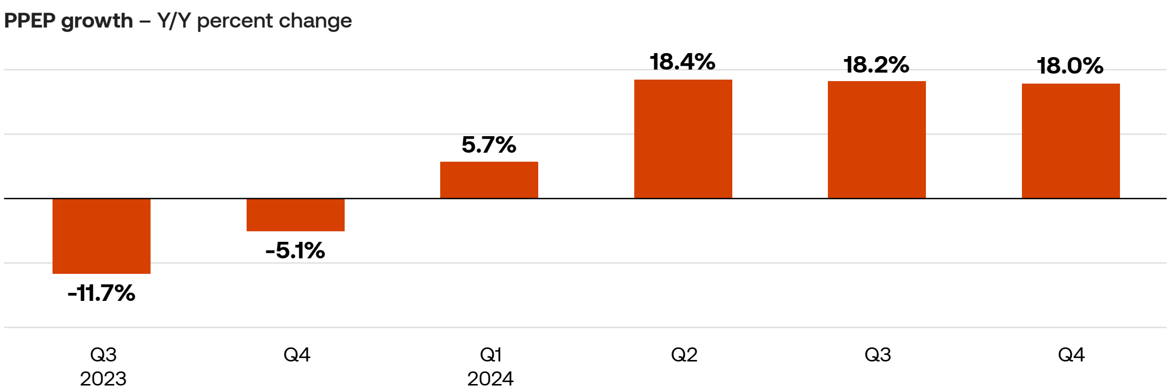
All metrics are calculated on a rolling 12-month average.

Source: Thomson Reuters 2024

Even with their end of the year spending spree though, firms have managed to keep their expense growth under much tighter control. Expenses still grew at relatively high rates, with direct[13] expenses up 6.5% and overhead rising by 8.8%, but much of this was due to firms' upscaling headcount. Expense growth per lawyer QFE was relatively reasonable, with total expenses per QFE rising by 2.6%. Revenue per QFE meanwhile, was up 5.4%. In combination with the aforementioned scaling, this has set firm profits to grow at a pace one could mildly describe as *considerable*.

FIGURE 11:

Profit per equity partner



PPEP growth is on a rolling 12-month basis.

Source: Thomson Reuters 2024

13 Direct expenses are those expenses directly related to QFE compensation.

© Thomson Reuters 2024

Profit and the partnership

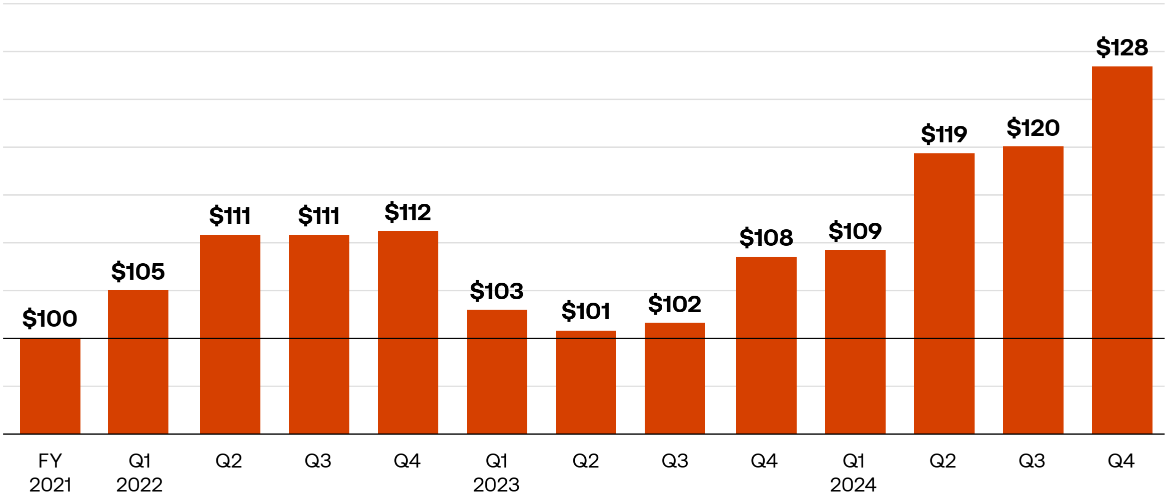
The average profit per lawyer QFE rose by 14.1% in FY 2024 compared to FY 2023, a number which was mitigated by the aggressive headcount growth firms have undertaken. When taking in the headcount expansion and what it means for equity partners, the true scale of the increase in profitability becomes apparent. The average firm's equity partner saw an a 18.0% increase in profits compared to last year. This sounds good, but it is somewhat difficult to conceptualize given the contraction in profits per equity partner (PPEP) that the industry experienced in FY 2023. To measure the grand outcome, it may be best to return to a graphic presented in last year's *Australia: State of the Legal Market Report*.

As seen below, PPEP is shown measured from the baseline of FY 2021. This chart shows the overall positive change in PPEP for every $100 of equity partner profits as indexed to the end of FY 2021. For example, the average Australian partner collected an indexed PPEP of $100 in June 2021; then 12 months later, they would have collected $112 at the end of FY 2022.

FIGURE 12:

Profit per equity partner since FY 2021

Indexed Change Since FY 2021 – Rolling 12-month change



Source: Thomson Reuters 2024

FY 2023 was a challenging year to be sure, but one from which most law firms were able to fight back. The latest fiscal year, by contrast, was an almost unceasing success. PPEP soared past the previous high set in FY 2022 of $112 indexed growth and set a new high-water mark at more than double that level of profit growth. PPEP for the average law firm has grown on average, 28% since just FY 2021.

This observation, however, cannot be attributed solely to robust business growth. While FY 2024 was undeniably a strong year, the difference in profits per lawyer QFE and PPEP growth was also due in part to firms increasingly restricting the path to equity partnership.

© Thomson Reuters 2024

New lawyers face an uncertain future

New lawyers joining today's law firms are matched up against a dual-threat which, when combined, makes their futures uncertain in a way that many lawyers have not previously faced. The first threat is a closing equity partnership, in which the doors to entry are becoming increasingly calcified even as the competition for the remaining seats intensifies.

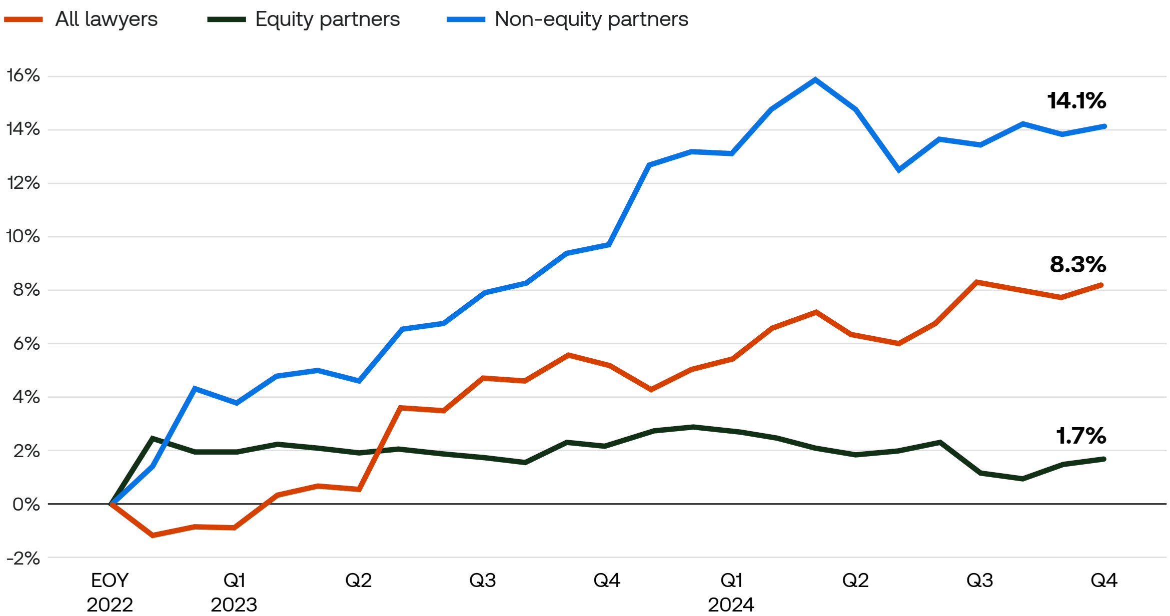
The average law firm has grown its headcount by 8.3% since FY 2022, meaning that more people are theoretically competing for the brass ring than ever before. However, despite this increased competition, the average Australian law firm has hardly increased their average equity partnership in that same time. In other words, new members of the firm face greater competition to reach the top of the partnership. If one looks back even further, one sees that a decade ago equity partners constituted on average 18% of the lawyers in the typical Australian large law firm. As of the end of FY 2024, they constitute only 13%.

This is not to say that the partnership has become entirely unattainable. Indeed, a certain class of partners has been notably on the upswing: the non-equity partner. Defined as partners whose compensation package is less than 50% based in equity, this class has been growing its prominence over the last few years at a pace far faster than other titles. Since 2022, non-equity partnership has grown by nearly double the rate of overall headcount growth, up 14.1% in two years.

FIGURE 13:

Lawyer QFE growth since FY 2022

Indexed Change Since FY 2021 – Rolling 12-month change



Source: Thomson Reuters 2024

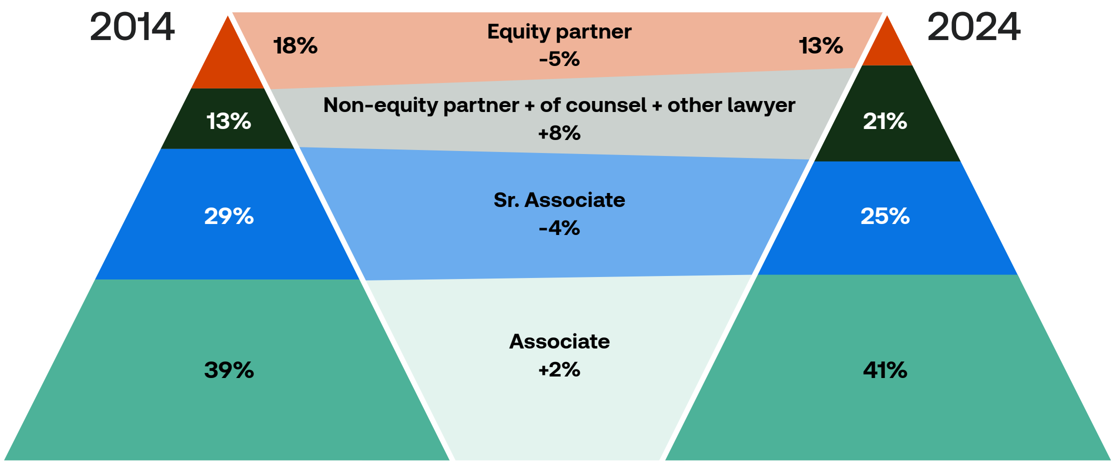
© Thomson Reuters 2024

The bifurcated partnership

It is becoming clear that the upper echelons of many law firms are bifurcating, creating an upper and lower echelon of partnership. This is not to assign a value judgement to the existence or worth of the non-equity partnership, as there are extremely strong cases to make for both its existence and expansion. Simply put, the full brass ring itself and the lifestyle that often accompanies it may not be perceived as strongly as it once was by junior and mid-career lawyers. By establishing a higher position in the firm that offers a better work-life balance distinctly different from that of the full partnership, the non-equity partnership thus opens up new options for those seeking to rise above the senior associate levels and cement their position in the firm. This is not itself a bad thing; however, it does have consequences.

FIGURE 14:

Change in title proportions



Source: Thomson Reuters 2024

As the full equity partnership becomes smaller as a portion of total headcount, the control and profits of the firm will become increasingly concentrated among fewer individuals. By dramatically shrinking the portion of equity partners relative to non-equity partners, firms risk creating a hierarchical structure in which decision-making power and financial rewards are disproportionately held by a select few. This concentration can potentially lead to several implications for the average law firm's dynamics.

First, non-equity partners are effectively a fixed cost, much in the same way that associates are. By increasing the non-equity partnership, firms are incurring a cost that will weigh greater when times are sparse, compared to equity partners whose compensation primarily comes from profit. If firms are assuming only good times are ahead, they may be mostly safe from this consequence; however for an industry which only a year ago saw a contraction in profit, this may be an overly optimistic viewpoint.

Second, the shift towards a larger non-equity partner cohort may impact firm culture and cohesion. Non-equity partners, while contributing to the firm's revenue and operations, may not have the same level of commitment or sense of ownership as equity partners. This distinction could lead to a disconnect within the firm, in which larger cohorts of the partnership are less engaged than their peers and may be more prone to short-term decision-making.

© Thomson Reuters 2024

The implications on talent retention cannot be overlooked. Equity partners typically enjoy higher compensation and a direct share of the firm's profits. By expanding the non-equity partner ranks, firms may be redistributing profits in a way that reduces the overall financial rewards available to each partner and concentrates it in the hands of a smaller group of equity partners. This is, after all, part of the point of non-equity partnerships, to reduce the total compensation available to these partners in exchange for either a superior work-life balance or easier access to the partnership.

Yet with this arrangement growing in proportion, it could affect partner satisfaction and retention, especially among high-performing individuals who may seek greater financial incentives elsewhere. If firms are unable to provide access to the full equity partnership to their most competitive lawyers and instead shepherd them into the non-equity position due to the firm-favouring inherent financial incentives of doing so, those firms may be under increasing risk of proven talent deserting them for other firms which may not have taken the same path.

However, the most significant threat that this shift in firm structure brings is not based on compensation or engagement. With fewer equity partners, the decision-making process may become more centralized and less diverse in perspective. A decrease in the numbers in the highest echelon could limit the range of viewpoints considered in critical decisions, potentially hindering innovation and adaptation to market changes.

Modern law firms risk centralizing decision-making power and limiting innovative thinking if they overly concentrate the equity partnership, especially during a period in which the very nature of law is changing. A generational transition is currently underway in law firms, and the very practice of law is greatly shifting for young lawyers compared to the experiences of the partners who are expected to lead them.

Such a disconnect between the experience of partners and the growing technological nature of the practice of law on the ground could result in misinterpretation or downright misalignment of strategic priorities.

Such a disconnect between the experience of partners and the growing technological nature of the practice of law on the ground could result in misinterpretation or downright misalignment of strategic priorities. Firm leaders might find themselves reacting to the ghosts of past lessons rather than the new reality which their firm now inhabits. The good news for law firms is that this technological transition appears to be only in its early stages. The bad news is that the growing consensus is that it is increasingly inevitable, and its true practical implications are so far quite unknowable.

© Thomson Reuters 2024

GenAI – Where it is in Australia and where it's going

Now nearly two years since OpenAI introduced ChatGPT to the general public, GenAI technologies have promised to change the way lawyers perform a variety of tasks, including legal research, contract and document drafting, internal and external communication, and more. The thought is that ultimately, GenAI systems will become the newest type of legal assistant as increased automation frees lawyers to perform more complex work. This, however, may undersell the true potential of the technology in its capacity to act less as a more advanced, specialized secretary but also its capacity to analyse situations as well as to mentor and enhance its users. As of this current point in time, the true potential of GenAI remains unknown. Thus, the first question is not what will be the ultimate potential of GenAI in the legal industry but rather, where do things stand now?

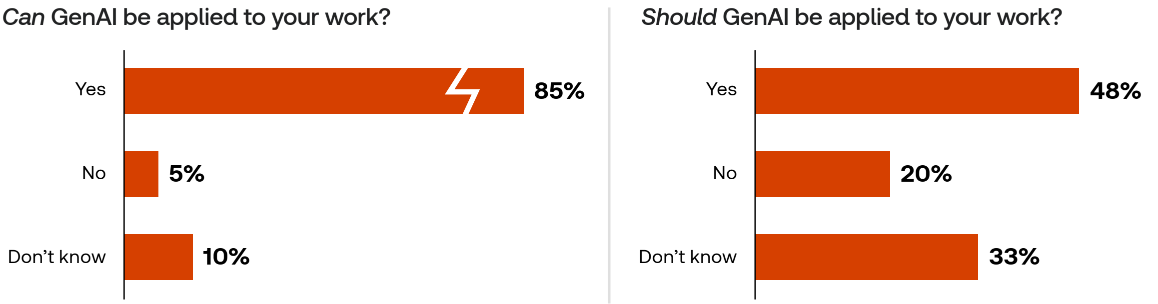
As it stands, the approach to GenAI adoption in Australia is less reverence and more cautious consideration.

Acceptance with reservations

Overall, lawyers said they believe that GenAI will be a part of their daily work lives, perhaps sooner rather than later. According to the *Generative AI in Professional Services Report*[14] from the Thomson Reuters Institute, published earlier this year, Australian legal professionals across law firms, corporate legal departments, government agencies, and the judiciary largely agree that GenAI can and should be a part of legal work. In fact, just 5% believe there is no use case for GenAI in today's legal work, while only 20% believe GenAI should not be applied.

FIGURE 15:

Can and *should* GenAI be applied to legal work?



Source: Thomson Reuters 2024

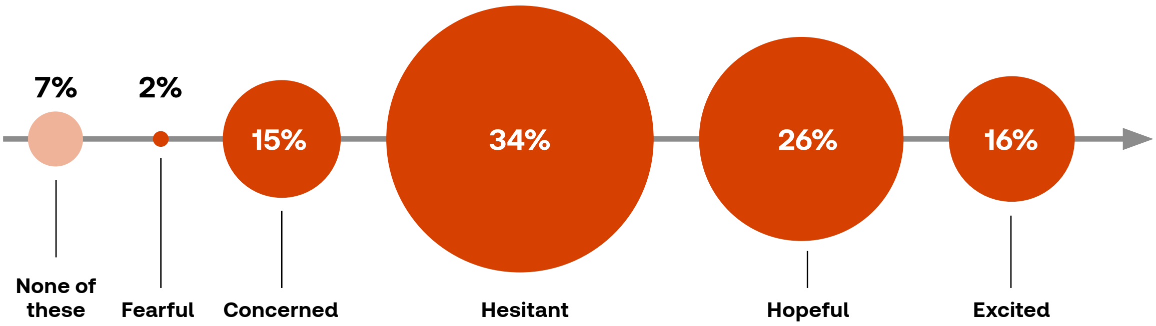
Notably, this also includes how corporate legal departments feel about GenAI use among their outside counsel. When asked whether their outside law firms *should* be using GenAI, 50% of corporate legal respondents said yes, 15% said no, and the remainder said they did not know. Government legal respondents, meanwhile, were more evenly split as to whether their outside firms should use GenAI, with 33% saying yes, and 29% saying no.

14 https://www.thomsonreuters.com/en/reports/2024-generative-ai-in-professional-services.html

© Thomson Reuters 2024

Sharp-eyed readers may spot one of the main issues surrounding GenAI at this time, however: There are a sizeable number of people who haven't made up their minds about GenAI's ultimate role within the legal industry. When asked about their sentiments towards GenAI in the legal industry, Australian lawyers largely offered more positive sentiments (being hopeful or excited) than negative sentiments (being concerned or fearful). However, their primary emotion was one of hesitance – preferring to wait and see how the technology will develop.

FIGURE 16:
Sentiment on the future of GenAI



Percentages may not total 100% due to rounding.

Source: Thomson Reuters 2024

When asked to elaborate, some respondents said their hesitance was due to the unknown nature of how the technology will translate to a human-led profession. "As a prosecutor, AI could be useful to make written submissions," noted one government lawyer from Australia. "However, I am hesitant because so much of my work is to translate the emotion of an incident into a submission to get the correct penalty, so that the defendant is adequately punished and the victims get the closure they deserve, and I am hesitant because I don't know how well that will translate for an AI system."

Still others said they believe that, at this early stage of the technology, it is too early to make a determination without more demonstrable use cases. "As with many 'new things,' there is hype around generative AI. I have learned over the years [age 62] to be hesitant about hype," explained one general counsel. "Rarely, if ever, does the hype match the reality. For instance, hype is often 'general' where reality is specific to the many and varied circumstances which we face."

Usage today

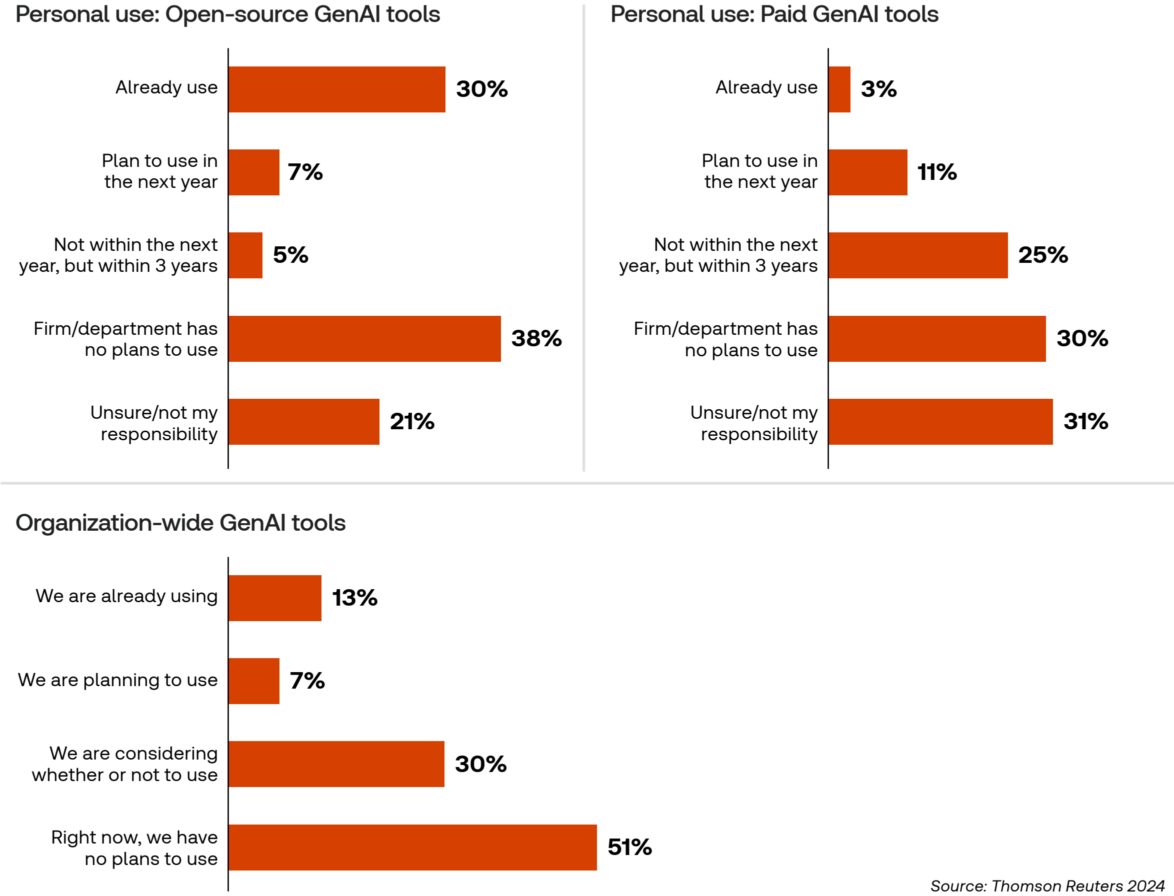
The problem is, there may be a wait-and-see aspect to how that hype will translate into practice. Many lawyers said their organisations are looking to be *fast followers* with GenAI, interested in its benefits, but not willing to be the first to test out its capabilities for fear of potential inaccuracy and data privacy and security concerns. The result is an Australian legal market that may be willing to experiment with GenAI tools but has not yet instituted them for widespread use.

Indeed, already many lawyers reported having used open-source GenAI technologies such as ChatGPT for some element of legal work – most often research, document drafting, or correspondence drafting. At the time of the report in April 2024, however, not many reported having used *legal-specific* GenAI technologies, particularly as such technologies are in the process of early arrival to the market. Perhaps as a direct result, few legal respondents said their employers have instituted GenAI technologies on an organisation-wide basis.

© Thomson Reuters 2024

FIGURE 17:

Current use of GenAI tools for legal work



Source: Thomson Reuters 2024

The implications of this slow roll-out may be that legal organisations remain unsure how exactly to consider GenAI when conducting long-term strategic planning. For instance, 29% of respondents said they believe that GenAI will have a major impact on billing practices and law firm revenue, while an additional 43% said they believe it will have somewhat of an impact. Due to the low adoption rate, however, few firms have actually had that conversation with their clients – less than 5% of law firms, for example, said their clients have provided any sort of direction around GenAI usage for outside counsel guidelines, RFPs, or elsewhere.

Similarly, there is a belief that GenAI may have a long-term impact on legal staffing, but at this early stage of adoption, those opinions have not yet had time to bear fruit. Not surprisingly then, 71% of Australian lawyers said GenAI would be either a major threat or somewhat of a threat to legal jobs. However, less than 20% said their organisations are currently considering GenAI at all when hiring, and just 2% called GenAI usage skills a must-have.

The result is a general uncertainty in which lawyers at all levels understand that a dramatic change is being undertaken yet have none of the answers as to how they may prepare individually.

© Thomson Reuters 2024

Conclusion

It is not the role of this report to provide individual lawyers career advice, but it is within its scope to better position the Australian legal industry for future success. Failing to address either the changing nature of the partnership or the evolving nature of legal work in the era of GenAI will impact firms in the decades to come. Some law firms will inevitably get it right; and others will get it wrong.

However, many law firms may have all they need in order to alleviate these challenges while still partaking in the benefits of each shift. Indeed, FY 2024's historic windfall of profits may have come at the best potential time for firms to not just enjoy the fruits of their labour, but to safeguard their future efforts.

By carefully managing firm culture and promotions, ensuring that the upper echelons of firms do not succumb to forces of inertia, firms can cut off the potential downsides of their partnership developments while still enjoying the benefits an expanded non-equity partnership class offer. In the same vein, properly researching the capabilities of GenAI, deploying an understood system of using it within a firm, and clearly communicating with lawyers how they can best adapt to this technology, will greatly shield law firms from potential pitfalls while opening up new doors they could scarcely have dreamt of a few years ago.

Doing these things will not be easy. Leadership cannot simply sleepwalk through these transitions. Rather, they must keep all eyes open, with a glance cast both towards the lessons of the past and the potential of the future.

If Australian law firms can strike this balance, the record profits of FY 2024 do not have to be a one-time occurrence. Instead, they can serve as a foundation for sustained growth and innovation, positioning firms to thrive in an evolving legal landscape.

If Australian law firms can strike this balance, the record profits of FY 2024 do not have to be a one-time occurrence. Instead, they can serve as a foundation for sustained growth and innovation, positioning firms to thrive in an evolving legal landscape. The future is ripe with possibility, and those firms with an attentive vision will be best equipped to cross the threshold into the future that lies ahead.

© Thomson Reuters 2024

Thomson Reuters

Thomson Reuters is a leading provider of business information services. Our products include highly specialized information-enabled software and tools for legal, tax, accounting and compliance professionals combined with the world's most global news service – Reuters.

For more information on Thomson Reuters, visit **tr.com** and for the latest world news, **reuters.com**.

Thomson Reuters Institute

The Thomson Reuters Institute brings together people from across the legal, corporate, tax & accounting and government communities to ignite conversation and debate, make sense of the latest events and trends and provide essential guidance on the opportunities and challenges facing their world today. As the dedicated thought leadership arm of Thomson Reuters, our content spans blog commentaries, industry-leading data sets, informed analyses, interviews with industry leaders, videos, podcasts and world-class events that deliver keen insight into a dynamic business landscape.

Visit **thomsonreuters.com/institute** for more details.

© Thomson Reuters 2024 TR4655990/8-24