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Law firm KWM to appoint administrators for European arm

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Group ran into problems following pioneering merger that created it three years ago

International law firm King & Wood Mallesons has announced its intention to appoint administrators for its European arm after running into problems following a pioneering merger that created it three years ago.

The firm, formed from a Chinese-Australian and a UK business in 2013, has suffered an accelerating exodus of partners from its European business' London headquarters, with rival law firms saying they have poached at least 16 in the past week.

KWM now has 10 working days to stave off creditor demands while it works to reach a restructuring deal that could see its Chinese arm buy its offices in Dubai, Germany, Spain and Italy, said two people involved in the process. "The London office is still an open question," one of the people said.

The Christmas holidays mean that the firm has essentially three weeks to broker a rescue deal, but if that fails its European business could wind up in pre-packaged administration, according to that person. The Chinese and Australian divisions are expected to continue operating as normal.

KWM said in a statement that the notice of intent to appoint administrators was "designed to protect the firm from its creditors and allows it to maintain client service as it continues to explore all available options".

"The firm's management team and financial advisers continue to work to ensure the best possible outcome for clients and staff, and this move supports these efforts at a key point for the business," it said.

The group was created when SJ Berwin, a well-known mid-tier UK law firm that was a specialist in the private equity and real estate sectors, combined with the Chinese- Australian King & Wood Mallesons.

The merger was plagued with problems from the start as the three firms struggled to bring together their different activities.

But the potential collapse is also a sign of broader problems among mid-tier firms as so-called "silver circle" players struggle to compete against the well-known brands of "magic circle" firms such as Clifford Chance and Allen & Overy in an increasingly crowded and stagnant market.

"It shows stress within the broad middle tier," said Tony Williams, head of Jomati, the UK legal management consultancy, and a former managing partner at Clifford Chance. "In a market where competition is increasing and the market isn't growing it is inevitable that is going to produce winners and losers."

A slowdown in dealmaking because of the uncertainty over Brexit has “increased the level of concern”, he added.

SJ Berwin had struggled to recover following the 2008 financial crisis, which hit its main real estate and private equity customers hard. Following the merger, the combined firm bet big on expanding its reach into M&A and other sectors that its Chinese and Australian partners had focused on.

“Like a number of law firms, it has overextended itself,” said one insider. “It has grown too quickly and hired too many partners who are paid too much.”

In addition, the expanding activities did not suit some of the partners used to the narrower private equity and real estate focus of SJ Berwin.

“The worst thing happened, they lost focus,” said one former partner. “They started hiring people in M&A and project finance. It started losing revenue and people started to leave.

“I didn’t think it would collapse. But I thought it was turning into a third-rate international law firm with low profitability.”

The firm had been undercapitalised before the merger and remained so afterwards, said two people close to the company.

The European arm had been funded by a credit facility from Barclays that increased to £35m this year from £25m, the people said. But the bank sought to reduce its exposure to the business this autumn as the extent of the problems became clearer. “The company was living off credit rather than living off its own means,” one of these people said. “The bank had been effectively bolstering the business for years.”

KWM’s partners were to agree a plan that would boost the firm’s capital at the same time as reducing the firm’s debt to Barclays, according to the two people. The Chinese arm had agreed to provide £10m, while the partners were to stump up £14m.

But the plan collapsed after only 20 per cent of the partners agreed to back it in a vote in November. The vote came after four of the firm’s most significant partners announced that they were going to resign.

Since then talks to sell the firm’s European arm, including its debt, to other firms, including Winston Strawn, Dentons, DLA Piper and Addleshaw Goddards, have collapsed.

One of the people involved in the process blamed the partners for the collapse. “It shouldn’t have got to administration. But the truth is the partners have mismanaged the business over time.”

The firm has told staff it cannot guarantee payment of wages after January, this person said. “The people most at risk are the juniors and the support staff,” he said.

AlixPartners, the global consultancy firm, is advising Barclays and KWM and is the proposed administrator, according to one person involved. It declined to comment. Barclays also declined to comment.
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