Impediments To Legal Industry's 'Inevitable' Future: Part 1

By **Craig Levinson** (June 7, 2018, 12:09 PM EDT)

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Legal pundits continue to make predictions about the newer entrants into the industry — those featuring lower cost and higher efficiency solutions often driven by technology. The general consensus is that these companies will progressively seize greater amounts of market share from traditional law firms. In the book "Remaking Law Firms: Why & How" George Beaton and Imme Kaschner build a legal landscape scenario for 2025. It's a world where "the billable hour as the predominant way of pricing legal services is a distant memory," "NewLaw startups are the dot-coms of the roaring twenty-twenties," and "lawyers joke about BigLaw firms having gone the way of the Hollywood studios of old."[1]

Analysts point to internal corporate factions placing mounting pressure on general counsels to shift work away from law firms and toward alternative providers. They paint the Big Four accounting firms as "formidable competitor(s)"[2] due to their global footprint, size and existing relationships with corporate clients. And despite U.S. legal and accounting prohibitions, the scope of what alternative legal providers can handle remains a massive cross-section of existing law firm business. One might surmise that the Am Law 100 and 200 firms are making wholesale changes to counter this seemingly clear and present threat. In the U.S., however, the BigLaw response has been underwhelming at best. While there are firms making novel changes in a variety of areas, the law firm business model remains essentially intact.

A glimpse at the market forces affecting BigLaw puts its lack of urgency into perspective. BigLaw signifies the traditional law firm model being used by incumbent firms. Beaton wrote that "BigLaw is not about big law firms,"[3] but he also noted that it's typified by the Am Law 100 and 200.

NewLaw

Legal market analyst Jordan Furlong initially described NewLaw as "any model, process, or tool that represents a significantly different approach to the creation or provision of legal services than what the legal profession traditionally has employed."[5] Today, the term is often used in conjunction with three categories of industry disruptors: NewLaw firms, the Big Four and alternative legal service providers, or ALSPs.

NewLaw firms are actually not that new. The most recent varieties — "virtual" law firms — eschew the overhead and trappings of traditional large firms to pass on the savings to their clients. While the Big Four are among the largest law firms in the world, they will almost certainly represent a significantly different approach to the delivery of legal services in the U.S.[6] Although offering only international, and not U.S., legal advice, there was considerable forecasting about the Big Four's endgame when PricewaterhouseCoopers LLP launched ILC Legal last year in Washington, D.C.[7] The Big Four are deliberately sidestepping direct competition with U.S. law firms, yet many see them as an existential threat,[8] particularly with their nonaudit clients. The service most in peril appears to be driving the bus on mergers and acquisitions, where the Big Four firms, in their advisory capacity, could identify merger candidates, hire the law firms for the due diligence, then "transact" or oversee the deal along with the financial services companies.

ALSPs are companies providing solutions such as outsourcing, legal support, project and

process management, data mining and analytics, and technology solutions that make practicing law more efficient. The faces of the ALSPs are the giant "law companies" like Axiom and UnitedLex, which provide a smorgasbord of legal services. UnitedLex, for example, claims to have over 2,000 attorneys, engineers and consultants, and their offerings comprise litigation services, digital contracting solutions, law department consulting, IP, cyberrisk solutions and financial advisory.

Law companies' clients are both law departments and law firms. They're also asked, by in-house counsel, to collaborate with law firms on assignments. "It is not uncommon for a client to have its corporate law firm handle the intricate legal aspects of a billion-dollar acquisition while retaining us to analyze the thousands of contracts being purchased," said Bryan Caplin, Axiom's senior vice president of sales and operations. According to Caplin, clients are beginning to realize that Axiom's proprietary technology platform and contract review processes make contract review faster, far less expensive, and more accurate than that of law firms using human reviewers. "Ten associates might look at the same contract, and have 10 different interpretations, which leads to contracts having to be re-read multiple times. Our use of AI and review technology allows us to quickly identify all subjective and problematic clauses, across the portfolio of contracts — allowing us to almost immediately have our lawyers analyze those targeted clauses once, as a team, and reach a consensus about their effect on the acquiring company."

Conversations with executives from other leading law companies indicate that the most sensitive topic has been ALSPs competing directly with law firms. No one wants their clients and collaborators to perceive them as competition. Law companies say that they're keeping legal departments lean by doing work previously handled by superfluous in-house talent and that they're not targeting the high-value law firm work. While those arguments have validity, it's difficult to make a case that law companies aren't also siphoning off lower value work that has long served as law firms' profit engine. According to Furlong, "The foundation of the traditional law firm is exactly all the routine, repeatable, hours-burning work that ALSPs are taking away. Law firms aren't set up to perform only high-value, highly sophisticated work. Law firms are dependent on leveraging lower-cost labor … to carry out lower-value work. That's the whole point of leverage. That's where the partners' profit is, and always has been."[9]

Legal Ops

Within large companies, two groups endeavor to transform the purchasing of legal services. The first group, legal department operations, or "legal ops," resides within the legal department. Their charge is to focus on the business of law so that in-house lawyers can concentrate more on the practice of law. Optimally, that directive would include evaluating fee arrangements, driving department efficiency and innovation, and, in particular, assessing and implementing new technologies. The adoption of the role has been exponential. According to Connie Brenton, the president of the Corporate Legal Operations Consortium, or CLOC, her organization in two years "went from an informal group of 40 to nearly 1,300 legal operations professionals."[10]

As quickly as law firms embraced the marketing function in the late '90s, their clients are adopting legal ops at an even faster rate. Reese Arrowsmith, head of legal operations for Campbell Soup Co., said, "Companies are going to need more ops professionals evaluating the need for these technologies, implementing technologies, training systems, training legal staff on how best to use the systems, monitoring results and tweaking input to get better output."[11]

Procurement

The group outside the legal department is procurement, which has become more relevant as GCs have been asked to do more with less. A solid procurement function can partner with the legal team to evaluate data, facilitate e-billing, negotiate discounts, establish panels and oversee requests for proposals — thus providing a clear summary of the available options.

"In the coming years," said Silvia Hodges Silverstein, executive director of the Buying Legal Council, "the impact of legal procurement in the legal industry will continue to grow. Eventually, nearly all major companies will have established a legal procurement function. This function will work hand in hand with the general counsel and legal ops to reduce the number of legal services provider per company, establish alternative fee arrangements, and specify discounts and incentives for better outcomes."

Despite the threat of NewLaw undermining the law firm leverage pyramid, and the effects of the practical processes and technologies recommended by legal ops and procurement, BigLaw largely remains married to the way things have always been done. Perhaps we shouldn't be surprised. Law wouldn't be the first industry in which leaders intellectually agree with sensible strategic advice, but then allow emotional decision-making (or rather, non-decision-making) to delay action, thus resulting in inertia.

Cost of Doing Nothing

My former business partner, Mike O'Horo, and I used to train lawyers to stop selling and to start collaborating with prospects. The approach: Help them clarify the financial, operational and personal impacts of not taking action on issues they had placed in their "should handle someday" buckets. The goal was for prospects to conclude that the cost of doing nothing was too high and that the issue *had* to be moved to their "must handle today" buckets. As O'Horo wrote, "People only make the decisions they *must* make."[12]

A Georgetown Law study[13] indicted BigLaw for 1) disregarding signs that their approaches to process and project management, leverage, alternative fee arrangements, technology, etc. are failing, and 2) choosing to "double down on their current strategies rather than risking the change … required to respond effectively to evolving market conditions." This "consensual neglect" is evidence that the financial, operational and personal impacts on law firm leaders remain *too low* to spur action. Upon reading Ron Friedmann's examination of Altman Weil's survey showing NewLaw stagnating around 5 to 6 percent[14], one must presume that BigLaw considers NewLaw another "should handle someday" issue. BigLaw's greatest advantage and NewLaw's foremost obstacle almost certainly derive from the same place: in-house counsel's own resistance to change. This corporate counsel mindset can be ascribed to, or reinforced by, many factors, but three are conspicuous.

In-House Counsel Are People Too

In general, we're all averse to change, particularly when the cost of doing nothing is not high enough to impel action. Every Sunday, for seven years, my father has told me he's getting fleeced by the cable company and is going to change providers. When that occurs, I'll alert the media. Once again: "People only make the decisions they *must* make." When the lawyer personality is superimposed onto people with a prevailing aversion to change, who are then dropped into institutions that don't incentivize change, you get "buy-side inertia."[15] Most companies inhibit innovation[16] within the legal department by punishing good behavior.

"Generally, the sole 'reward' for coming in under budget is a lower budget going forward," says Casey Flaherty, a former outside and inside counsel, a legal operations consultant, and the founder of Procertas LLC. "Indeed, why would an inside counsel voluntarily reduce their budget in the first place? Inside counsel's budget is, like a partner's book of business, their source of power. The bigger their budget, the more sway they have."

Stephen Poor, chair emeritus of Seyfarth Shaw LLP, has been the driving force behind the firm's adoption of Lean Six Sigma, an award-winning management approach emphasizing process improvement and efficiency in legal work. While he anticipated the extraordinary change management process that would be required inside his firm, he did not account for an unexpected constituency.[17] "What we did not anticipate was the resistance from other stakeholders — especially clients," Poor said. "What we overlooked at the outset is that, by and large, our clients are lawyers, too, and products of the culture of their own business." According to the firm, Seyfarth offered a process that saved clients up to 50 percent on legal fees[18], along with peer testimonials and case studies, yet still encountered pushback. A law firm approaches its clients, offering to do the same work, more efficiently, at a significant discount, and still some of them resist. Could any anecdote be more revealing about in-house lawyers' reluctance to embrace change?

Lawyers Are Lawyers

Outside counsel don't undergo some grand transformation when they move in-house. They remain among the most skeptical people in any profession.[19] Their Myers-Briggs types[20] don't change overnight. In fact, they remain as resistant to change as do their outside lawyers. "There are few discernible differences between the modal in-house lawyer and the modal law-firm lawyer. They are the same people," Casey Flaherty said[21].

According to Dr. Larry Richard's studies[22], there are some vital personality attributes where lawyers deviate considerably from the general public. These psychological traits seem to cultivate in-house-lawyers' overriding impulse to maintain the status quo and resist assistance from others.

Flaherty postulates the ways in which these traits manifest themselves:

- Autonomy: "Lawyers prefer to do things themselves and react poorly to being told what to do. Telling them that they should focus on something other than what they prefer/choose to focus on is a violation of their autonomy. So, too, is bringing in someone else to do it for them."

- Sociability: "It's not just that lawyers do not like relying on or taking direction from others; they dislike interacting with them, period. Lawyers score their lowest (12 out of 100) on the sociability measure."

- Urgency: "Lawyer time is valuable. Deadlines are imminent. Failure is not an option. Lawyers have an ineffable urge to get everything done now. Combine this urge with high autonomy and low sociability, and it all needs to be *done now by them*."

The Small Percentage of Revenue That Is the Legal Spend

Many in the legal industry tend to over-inflate the magnitude of the legal department. The reality is that U.S. companies spend 0.4 percent of revenue on legal services.[23] Contrast that with marketing departments. According to a Gartner survey[24], larger companies (>$5 billion revenue) spend 13 percent of revenue on marketing, while smaller companies ($250-$500 million) spend 10 percent of revenue on it. That means Fortune 500 companies spend roughly $32.50 on marketing for every dollar spent on legal services. While cost-savings in legal for the Fortune 500 can be in the millions, what's recouped often lies somewhere between "slightly significant" and "a rounding error." If procurement wants to implement a new, cost-saving legal process, and the GC vigorously objects, the CEO is generally going to side with the seasoned GC who has consistently kept the company out of trouble. With the relatively meager savings at stake, there's little motivation for a CEO or management team to upset the GC's apple cart.

Good Intentions

In-house lawyers are saying all the right things. They acknowledge that the threats are real and that many of legal ops' and procurement's recommendations are prudent. This is merely a case of human nature interceding between intention and execution. Beaton and Kaschner modeled a scenario principally based on what legal departments *said* they planned to do, not what they *had done*. In the legal industry, the difference between those two data points can be decades. While they appear to have predicted a foreseeable future for the legal services industry, they may have overestimated the pace of the ramp-up.

Is this an indication that BigLaw can relax and that NewLaw companies should revisit their collective approach to the market? Absolutely not. There are far too many unknowns in this equation. If, for example, we faced another Great Recession, the effect on the legal industry would likely be much different than it was a decade ago. Law companies didn't have nearly the credibility in 2008 that they enjoy today. Both law departments and law firms could integrate law companies so deeply into their delivery models that there would be no turning back. The Big Four, meanwhile, according to Nicholas Bruch, a senior analyst at ALM Intelligence, "can (provide legal advice) under Sarbanes-Oxley regulations — just not to its audit clients."[25] PwC's opening of a U.S. law firm appeared to be a shot across the bow. The message: "We can get into this game any time we want."

For those reasons and more, part two of this article series will present a defensive blueprint BigLaw should consider adopting for this uncertain future. Firms fail to do so at their peril, as the tactics from this same playbook can also serve as NewLaw's offensive strategy for capturing more legal services market share — in both present and future scenarios.

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