Adapt Or Die: Law Firms In Tomorrow's Economy

Law360, New York (October 28, 2016, 10:50 AM EDT) --

This is part 1 of a multipart series exploring the metamorphosis that needs to take place in the world of corporate law firms in order for them to survive and thrive in the future.

The History of Finance's War on the Legal Function

Jill Dessalines

Any lawyer who's practiced for a few years, whether in a law firm or in-house at a corporation, and who has witnessed the increasingly adversarial relationship between corporate clients and their outside law firms, may very well have wondered: How did it come to this?

How did it happen that the very advisers you trust to guide your corporate employer through the legal morass could be so clueless about your corporate economic reality? How did it happen that the in-house counsel you rely on to help you navigate the corporate sand traps so often miss the ball?

At its heart, this adversarial relationship is based on the corporate perception that, as far as legal services are concerned, costs are disproportionate to value; and from the law firm perspective, that corporations are never satisfied unless firms are providing services at below cost. As is usually the case, one side of any argument ought to be convincing; and there are at least two sides to every story.

A walk through history helps tell the tale. For many years, large law firms had carte blanche to charge whatever they wanted for their services to corporate clients. Task-based bills were an oddity; rather, the now infamous "For Services Rendered" invoice was the standard. These invoices cloaked the details of the services and their costs from the client and created a legacy of distrust and feelings of exploitation, particularly as legal spend escalated.

Starting in the mid-1980s, first-year associate annual salaries at the largest law firms skyrocketed from a national average of $25K to $60K in the space of a year. This meteoric rise was predicated on BigLaw having more work than lawyers to handle it; along with the realization that some corporate clients could and would pay whatever they were billed.

The undercurrent of resentment from this perceived exploitation was most acutely experienced within the finance function of corporate clients due to the inherent inability of most law firms to provide a guaranteed product for an agreed upon price as is standard in the business world. Starting in the mid-1970s, the business world experienced the rise of the MBA as the gold standard for entry into the business elite.

When the first MBA classes of that era ascended to upper management in the late eighties and early nineties, this historic frustration gave birth to action. Corporations began looking for ways to reduce outside counsel spend, increase visibility into outside counsel billing practices and exert more control on outside counsel actions.

For example, the now legendary DuPont campaign of the early nineties to limit the number of outside counsel approved for business and to provide billing rules was probably a result of this new cost consciousness fueled by MBAs in senior management. Requests for proposals, approved counsel rosters, and billing rules and regulations were virtually unheard of at that time.

Another way corporations sought to reduce outside counsel spend was to bring more work in-house. Even the largest corporations before the insourcing trend started often had skeletal teams of in-house lawyers who farmed virtually all substantive work to outside counsel. It was during this period that large in-house law departments became common, and the ranks of in-house counsel continue to grow.

Coinciding with these corporate trends was the explosion of the mega-law firm and the pervasiveness of law as a business, with all of its repercussions. Some of the repercussions of the increased focus on law as a business were law firms' focus on profit over client service, reliance on the billable hour regardless of the value of services rendered, creation of profit centers from what had been cost centers;

portable books of business and the never-ending quest to snag the most profitable partners and associates; and the conflict of interest merry-go-rounds these frequent job hops caused.

Finally, the explosion of mass litigation, securities and consumer class actions and product liability cases, along with the general litigiousness of the American public, the rise of the corporate takeover and the heightened regulatory scrutiny of certain industries, all added to the mix that created the tug of war between Corporate America and BigLaw.

The collision of these forces resulted in years of pent up frustration by corporate clients that saw legal expenses go from a small percentage of profits to a major line item with reportable events in their public filings, all with a questionable value proposition.

Fast forward to 2008 when the market crashed and the economy contracted. Despite the fact that the market fell, it did rebound and large publicly traded corporations experienced record-breaking profits within a year. The rest of the economy — not so much. Jobs were lost, wages stagnated, outsourcing soared and more homes were foreclosed on than were bought or built. Corporate America experienced an upsurge in power that had not been seen since the days of the robber barons.

The relative economic power between the corporate client with work to give, and BigLaw with rent to pay and mouths to feed was decidedly unbalanced. And finance saw its chance to finally require some degree of predictability of spend and some degree of confidence in outcome from their outside counsel.

Enter the now ubiquitous billing guidelines, the refusal to pay for overhead items, the limitations on rate increases, the cyclical RFPs for getting on pre-approved panels. From the in-house perspective, enter the multi-quarter projections of legal spend, compensation tied to budget adherence, the deluge of administrative details required to create, track and manage budgets and enforce billing rules, all while taking more and more substantive legal work in-house.

The legal function is not the exclusive target of finance's quest to reduce cost and extract ever-increasing profit margins. Most every corporate function has gone and

continues to go under the microscope. The difference is that, unlike sales, marketing, product development or human resources, expansion or contraction of the legal function does not always demonstrate a direct correlation to higher or lower profits.

This inexorable race to ever-decreasing spend will undoubtedly have consequences to the corporate legal function, whatever they may be. One consequence is that the antagonism between corporate client and BigLaw continues.

Yesterday's MBA is Tomorrow's CTO

There was a time, not so long ago, when an MBA was an express ticket into the elite of Corporate America. In fact, getting an MBA from a top business school at one time pretty much guaranteed a vice president title for your first post-graduate job. True, you may be one out of hundreds of vice presidents, but the title still had a nice ring and it beat the heck out of chief lackey or head bottle-washer.

These MBAs rose through the ranks of Corporate America and left their marks on every part of the corporate environment. The corporate legal function went from being a fairly small group of lawyers, who counseled their internal corporate clients with the assistance of largely outsourced expertise in specific areas, to large law departments with insourced expertise in a myriad of specialties. Outside counsel went from routinely sending “For Services Rendered” invoices to today’s world of budgets, budgeting and death by budget. Controlling legal spend and driving predictability has nearly become the exclusive focus of the attorney-corporate client relationship.

Today, there is a movement within the power dynamic in some corporations.

Chief Technology Officers or other similarly named functions have been in the C-suite of technology companies for years. Non-technology companies have often had Chief Information Officers who oversaw the enterprise-wide information technology infrastructure but did not usually have technology functions that were consolidated across business lines.

That trend appears to be changing, with more non-technology companies now pooling technology resources and expertise within one centralized function, often the

Chief Technology Office, with the fruits of that expertise distributed across several business lines in order to drive technological consistency, cohesiveness and interconnectivity.

As this model becomes more common, just as the MBAs of the last several decades remade the corporate world in their image, so too will the CTOs. What does this mean for the legal function? It will mean many things; but primarily it will reflect a fundamental shift in mindset as it relates to the consistency, predictability and cost of delivery of legal services.

Many law firms already share matter management information seamlessly with their corporate clients by utilizing common software products, including document sharing, electronic billing software and budget tracking. Most law firms with multiple offices have adopted the team approach across disciplines, irrespective of location, to enable the delivery of substantive work product not hobbled by time zones or geography. But these uses of technology merely repackage old school methodology.

Tomorrow's CTOs will likely ask for a much broader use of technology in order to transform the delivery of legal services. Much of the work performed by law firms is repetitive. In fact, the frequency of repetition of a task is what creates experience and thus expertise. Yet, most law firms fail to harness that experience to drive the predictability that such repetition should foster.

Why should budgets be created from whole cloth? Why don't law firms routinely access historical costs from years of existing data and model budgets based on case-specific factors? Why are documents initially reviewed by legal staff (aside from the profit motive) rather than engaging some level of machine review first? Why aren't trends and statistics on everything ranging from judicial rulings to opposing counsel profiles to regulatory investigation outcomes instantly available from existing data repositories? Why aren't case protocols standardized by matter type based on historical data and best practices so that deviations in standards of care are minimized if not eliminated? For that matter, why can't law firms use this same historical data to not only model potential outcomes, but to predict time horizons, decision trees and contingencies within a matter's life cycle?

Organization of existing information and the application of technology to produce

answers to these fairly basic questions will be fundamental requirements in the world of CTO-lead corporate clients. And even aside from whether CTOs will take the helm of many corporate clients, technological savvy is a given in the era of millennials and beyond.

Tomorrow's leaders will have been weaned on "at your fingertips" access to any and all information desired — we have all been "Google-ized" for better or worse — and that demand for instant access will permeate every aspect of the corporate environment, function by function, faster than it will overtake the legal industry. These demands will gain traction as mandatory requirements for outside counsel because they also have the benefit of reducing the cost of legal services.

In short, the same drive that has been fueling the push for "faster, leaner, more efficient" work in all major corporations will reshape the way that law firms do business. As each trend reshapes the corporate environment, with the market power exerted by corporate clients, each trend will push beyond corporate boundaries into the industries that service them. Fiscal accountability and technological innovation to reduce costs are two of those transformative trends. An analysis of other corporate trends that have emerged will surely reveal others.

Tune in Tuesday for part 2 of this series: "Overhead-Based Billing and Corporate Demand for Value."

Jill Dessalines, founder of Strategic Advice for Successful Lawyers, has been practicing law for over 30 years and is a former senior vice president and assistant general counsel of McKesson Corp. She was recently named one of California's Top 10 In-House Counsel by the Daily Journal.