

from Adam Smith, Esq. ...an inquiry into the economics of law firms

<http://www.adamsmithesq.com/archives/2009/06/an-international-perspective-and-a-guest-column.html>

Monday 15 June, 2009

An International Perspective (And a Guest Column)

Today we have an extremely unusual--for Adam Smith, Esq.--guest column. Indeed, if memory serves, this is only the third column in the history of this site (5 years, nearly 1,000 columns) not written by me.

[Leigh Dance](#) is today's author, and I will extend to her the courtesy every writer most devoutly wishes to receive from their editor and publisher, which is, without further ado, to get out of the way.

From my patio in Rome's centro storico, I read Bruce MacEwen's excellent [GM-RIP](#) piece and reflected that Rome didn't fall in a day either. A particular part of that post that resonated for me was Don Sull's comment that "Organisations often succumb to *active inertia* - they respond to disruptive changes in the environment by accelerating activities that worked in the past."

But the Rome analogy stopped there. Instead I pictured scores of squirrels furiously grabbing all the walnuts they could find--gorging themselves and squirreling hundreds more away for the hard winter. It's a vivid image, and immediately brings to mind the behavior of Big Law over the last six months.

Active inertia abounds, with talk squarely focused on the navel: projecting when deal flow may change, coping with fee income reductions and practice shifts, fewer associates, lower partner leverage, cutting travel and marketing costs, questioning international investments. Even talk of alternative fees is focused inwards: how can we make it work within the firm's billing system?

Forgive me for sounding harsh, but I have grown impatient with this ultra short-term thinking. When I ask corporate clients if their lawyers are visiting them, the tales are more bitter than sweet. A global General Counsel told me about a recent lunch with the lead partner of his biggest law firm provider. No interest in what was going down at the company. "I think I'll be able to build my deal base back up, don't you think?" the partner

asked his client, and went on to talk about his book of business. The GC described the encounter, shaking his head. "Hello?!? Could he have asked me 1 question about what I'm dealing with in *my* shop?" I guess that partner just wanted more walnuts to squirrel away. He didn't leave lunch with any, that's for sure. Stories like this are far too common.

Deep Freeze in Big Law

Summer begins any day, yet fear and loathing still has Big Law in a deep freeze. At GM it was a "cumulative and collective denial of reality" to change the organization and culture. We know why lawyers today feel paralyzed: there's still lots of pressure to produce; lawyers are accustomed to success; they built solid practices around businesses expected to grow forever; they adopted expensive lifestyles requiring ever greater income; they've lost valued colleagues; they don't know what's coming next.

Consultants make sweeping predictions that traditional law firm business models are dead. Wall Street rainmakers and their spouses reconsider the St. Bart's vacation as their environment changes. Revered investment banker and private equity friends are sliding down the food chain, and the New York/London social pecking order is in disarray.

At the coalface, private practice lawyers seem to be passing through a form of Elizabeth Kubler-Ross' stages of grief: 1) shock and denial, 2) anger and hostility, 3) bargaining and reorganizing, 4) depression, reflection and feelings of loneliness; and (we're not there yet) 5) acceptance.

Lawyers' identities are wounded-- many have or will face the possibility of losing their jobs. I'm no psychologist (as a law firm consultant it might be helpful), but I have surfed the web and learned that resentment and jealousy causes volatile and helpless feelings, plus serious distraction. According to grief experts, one of the effects is like a stun gun-- the person withdraws, anesthetized.

Sounds like Big Law to me. Adam Smith, Esq. has been raising the challenges up to leadership. I was happy to see Dan DiPietro, in his May *American Lawyer* article, voice frustration with lack of action among AmLaw 100 firms. Minutes after a conversation I had in Toronto where the Deputy GC of Bank of Nova Scotia marvelled to the Citigroup Canada GC that his bank was now larger in market cap than Citigroup worldwide, I received an email from Altman Weil summarizing their latest survey of major law firms. The big news: no news. *No dramatic changes.*

I'm impatient because the stagnancy among law firms is a whale of a lost opportunity. The biggest danger is the amount of legal work that seems to be migrating away from

law firms. While it's happening, many talented law firm professionals are not responding, much less preparing for the future.

In-house Counsel are Changing Like Gangbusters

While all is quiet on the law firm front, chief legal officers and their top teams within corporate law departments are changing like gangbusters. It's the opposite of *active inertia*. In-house counsel around the globe are fired up from long days working in crisis mode, big budget cuts and an impending avalanche of new regulation.

Corporate legal budgets for internal and/or external spending have been cut from 15 to 40% on both sides of the Atlantic (slightly less in Asia). Though many in-house functions have escaped staffing cuts, they must find cheaper ways to support their companies' global growth. General Counsels recognize that the world is full of legal landmines. They know they must increase productivity, reduce demand, and in every way possible lower the cost to buy and make legal services.

In-house counsel matter: they are the providers of work to many law firms, now more than ever. Rather than 'accelerate activities that worked in the past,' I believe they are in the process of changing the game.

Buon giorno, this is your wake up call.

My discussions with dozens of senior international corporate counsel (US, Europe, Middle East and Asia) over the last six months reveal a remarkable, disturbing and nearly unanimous view:

- they don't think law firms really understand or 'feel their pain';
- they say that their outside lawyers are not taking action to help, or even discuss their situation;
- corporate counsel are addressing these challenges on their own, having decided that their provider firms generally can't help because lawyers are pressured by the firms' conflicting objectives;

In most cases they say they haven't even *talked* to their law firm providers about their specific budget cuts and constraints.

In-house counsel in the US, the UK and with global corporations everywhere aren't whining about fees anymore. As I write, they are implementing various forms of outsourcing, shifting work to non-legal providers, automating certain functions. In a business climate where much is beyond their control, they relish their options in a buyer's legal market. The danger is that much of the work that is leaving big law firms may never come back.

Many have alternative fee arrangements and demand that law firms make costs more transparent and predictable. Some in-house teams systematically scope projects and then set fixed fees or caps for various predictable stages (in the UK referred to as "slice and price").

Unfortunately, the tendency for most in-house lawyers who've been told to 'cut costs or be shown the door' is to seek alternatives to outsourcing. When they need to go outside, they get competitive bids from known providers and take the biggest discount.

Few in-house legal functions have the management expertise, technology or time to implement metrics and processes for a higher functioning, leaner corporate legal function to better serve their global operations (and precious few law firms are helping; a major lost opportunity). So they opt for discounts, which scores quick points. Once discounting starts, it's hard for your firm to propose smarter approaches.

A moment for the discounting topic, which merits attention.

Corporate counsel are amazed by the deep discounts they are getting on competitive bids. It's now typical for European corporate counsel to bid out a transaction to a few global and domestic firms thought to have the requisite expertise. Usually inside counsel will determine what the combined costs may be for the firm to make a small profit. Proposals from many firms, including the Magic Circle, are coming in at discounts far greater than 50% of the cost of such transactions 18 months ago. Often corporate counsel choose the firm they prefer on the condition it meets the lowest cost bid.

Discounting is a short-term tactic. In-house, it can't reduce a legal function's outside legal spend by more than 15 or 20% over time, and the inevitable reduction in quality and service creates new and potentially costly risks. For law firms, much of the pricing resulting from pressure to discount is unsustainable.

Law firms must change the client dialog from discounts to helping clients build a better legal function for today's corporate demands. Partners should be trained and authorized to talk specifically about alternative staffing and fee approaches. It's particularly complex for multi-jurisdiction work, and surprisingly few firms do it well.

A relationship of trust with your client is among your greatest assets today. In-house lawyers want a reason to be loyal. They highly value expert advice and a trusted-advisor connection. They regret the inevitable loss of loyalty caused by cost pressures.

Lawyers must get out and reconnect with their clients, giving them big figurative bear hugs. Don't stay away for fear clients will tell you they're cutting back, and don't just go out and ask for more business. The only way you'll really reconnect is to dig in and

understand their issues. Then come back to them with viable approaches and structured options.

Law firms generally know how to use information technology far better than corporate legal departments (among the exceptions, Cisco soars). Take steps to share that expertise for the client's advantage. In the last few years law firms have become highly skilled at cost control and (for their own benefit) resource management. Your clients would really value having your firm's experience and skill to help improve the productivity and profitability of their in-house functions. Figure out how to make it work.

Play the Global Card

Now, for the holy grail of opportunities today: global reach. From my vantage point, the biggest opportunity you have to out-compete other law firms is to deliver your clients a combination of your legal skill, your IT expertise, your cost control sophistication and your global reach. Every day, I see global law firms miss a chance to win by playing the global card.

Most corporate legal functions don't come close to matching the international breadth and depth of most global firms, yet their companies are truly global. A year ago I was amazed to hear more than three quarters of a group of 100 large global in-house counsel say their corporate legal function is *not* sufficiently global. Far from it, they say. In-house lawyers are very nervous about meeting the demand. Many don't have the coverage or the international skill, and sourcing the right expertise is difficult and time consuming, not to mention expensive.

Global law firms can help in concrete ways. Connect the clients' situation from one jurisdiction to another and demonstrate your value by spotting key issues which help them avoid costly, distracting problems. Unfortunately, most global firms are not in the equation because they haven't connected their offering effectively to the client's global needs. When global law departments look for international legal services coverage, they seem to have a fundamental lack of confidence in the law firm's ability to help them build a better, more efficient global legal mousetrap.

Internationally-positioned law firms will come out far ahead if they can manage to effectively offer clear and compelling global legal service. They will win by showing clients what they can do *that matters to the client* in the short- and mid-term.

The environment has changed and the heat is on. No time for inertia. It's time to get out there. If you have it, play the global card.

Buon giorno, this is your wake up call. Would you like another call in ten minutes?



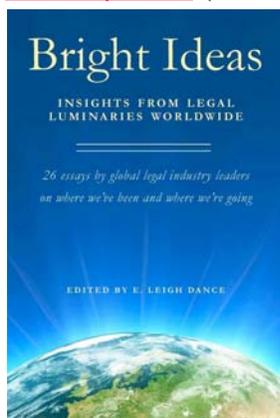
I am compelled to add that Leigh Dance is the editor of the very recently released book [Bright Ideas: Insights from Legal Luminaries Worldwide](#), which Ralph Baxter describes as follows:

"This collection of 26 impressive essays, skillfully edited by Leigh Dance, creates a superb textbook for leaders as they consider current and future strategies, whether as global law firms or corporate law departments. A unique compendium of global perspectives and ideas, it makes very useful reading for all who are working to chart a course in these unprecedented times."

Some of the 26 authors, drawn from law firms, major in-house departments, and the consulting world, are:

- Peter Beshar, EVP & GC, Marsh & McLennan
- Jeffrey Carr, GC, GMC Technologies
- Bruno Cova, Paul Hastings (Milan)
- Fadi Hammadeh, GC, Dubai Properties Group
- Alan Jenkins, Chairman, Eversheds
- Pete Kalis, Chairman and Global Managing Partner, K&L/Gates
- Despina Kartson, CMO, Latham
- [yours truly]
- Jolene Overbeck, CMO, DLA
- Thomas Sabatino, EVP & GC, Schering-Plough

Profits from sales of the book will be donated to [Advocates for International Development](#) (www.a4id.org). I recommend you take a look.



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