

Global Strategies in the Legal Services Marketplace: Institutional Impacts on Value Chain Dynamics¹

Mari Sako

Professor of Management Studies

Novak Druce Centre for Professional Services Firms

Saïd Business School

Oxford University

Mari.sako@sbs.ox.ac.uk

July 2009 (LAST REVISED)

Abstract

What alternative strategies are being pursued by firms to capture profit in global value chains? In what ways are the sources of competitive advantage changing as they move up the value chain from low end to high end work, potentially changing the structure and boundary of the existing industry? This paper examines these questions by focusing on the outsourcing and offshoring of legal services, known as Legal Process Outsourcing (LPO). Legal services were chosen for study in order to highlight the relevance of both technological and institutional factors that influence value chain dynamics. In particular, the study examines how the nature of professions impact on make-or-buy decisions and industry structure. The legal services value chain is conceptualized as consisting of three blocks, namely knowledge and information management (KIM), consultative advice and representation (CAR), and client relationship management (CRM). The study shows that legal services are being unbundled, with the KIM component being separated by ownership and geography from CAR and CRM components. To assess the actual extent of disintegration, the study identifies the conditions under which demand and supply for LPO services is generated. Those conditions on the demand side include the corporatization of law firms and pressures on global corporations to cut legal costs. From the supply perspective, the study identified three distinctive strategies for LPO providers to capture profit, depending on their mode of entry influencing their initial capability mix, and whether or not the value chain is driven by a corporation or a law firm.

¹ This study was funded by the IBM Faculty Award, awarded to the author in 2006. The author wishes to thank all those who were interviewed for this study, and Gaurav Singh and Sunyoung Lee for providing highly professional research assistance.

1. Introduction

In the last decade or two, a revolution in information and communication technology (ICT) and international trade liberalization have facilitated the unbundling of global value chains in services as well as in manufacturing (Baldwin 2006). The disintegration of value chains gives rise to new supply markets with new opportunities for capturing profit. Profit capture on a sustained basis is based on uniqueness associated with brand, innovative technology, intellectual property, platform, or size (Berger 2005, Gawer and Cusumano 2008, Teece 1986). Manufacturing sectors such as shoes, clothing, electronic assembly and semiconductor have seen the rise of design-only firms profiting from brands, coexisting with contract manufacturers profiting from functional efficiency and scale (Gereffi et al 2004; Sturgeon 2002). This co-existence of buyer strategy and supplier strategy depends on certain credible commitments about the division of labour and expertise. In particular, as suppliers upgrade by moving upstream into product design or downstream into distribution, buyer firms need reassurance that their final markets are not cannibalized by suppliers.

In services, India's entrepreneurial IT services firms pioneered the global delivery model in the 1990s, starting with simple tasks in software applications development and call centers. More recently, they are climbing up the value chain to deliver increasingly complex and knowledge-intensive services, in accounting, business and market research, financial data analytics, engineering design, radiology, and R&D. In so doing, what alternative strategies are being pursued by providers to profit from the global value chain? In what ways are the sources of competitive advantage changing as they move from low end to high end work, potentially changing the existing industry structure along the way?

This paper examines these questions by focusing on the offshoring and outsourcing of one notable type of professionalized knowledge work, namely legal services. Legal services were chosen for study for two reasons. First, legal services are knowledge-intensive. This enables us to question to what extent the same criteria apply to the decision to offshore knowledge-intensive services as to that for simpler services. Second, legal services are delivered by one of the oldest and tightly organized professions. This enables us to study the impact of institutional factors on value chain dynamics. The intent is to study the full impact of the legal profession's role in articulating a set of cultural-cognitive, normative and regulatory frameworks (Scott 2008) on make-or-buy decisions and industry structure.

The offshore outsourcing of legal services is known as legal process outsourcing (LPO). To understand this phenomenon, it is important to analyze it as a piece in a large jigsaw puzzle undergoing transformation. The analysis will be both at the industry level to identify forces that are driving the disintegration of legal service delivery, and at the firm level to identify corporate strategies for profiting from the value chain. LPO services are demanded by global corporations facing rising legal fees (Leblebici 2007), and by law firms facing pressures to become more corporate and international (Empson 2007). The geographically dispersed supply of LPO services is facilitated by the use of ICT to transform legal service delivery (Susskind 1996, 2000). It is also caused by a hunt for talent in low-cost locations in a sector suffering from work-life imbalance and low diversity (Eversheds 2008; Wilkins 2007). This study aims to

analyze the legal services value chain, identify the factors causing disintegration, and evaluate the relative merits of alternative positioning to profit from the value chain. This exercise also entails fundamentally questioning what it is that modern lawyers do, and hence what constitutes practising law.

The paper is structured as follows. The next section (Section 2) discusses the drivers of integration and disintegration, and identifies profit opportunities created by different positioning in global value chains. The key contribution of this theoretical analysis lies in explicitly taking account of the impact of professionals as institutional agents on industry structure. Section 3 then identifies demand-side factors that have led to the outsourcing and offshoring of legal services. Section 4, a core empirical section, presents the main findings with respect to alternative strategies pursued by LPO providers in India. This section is based on interviews with 20 LPO providers and law firms in India (see Table 1 for the list of interviewed firms). The paper concludes by drawing implications of the findings for theories of global value chain dynamics, and the future of the legal profession.

2. Profiting from Global Value Chains: An Analytical Framework

This section attempts to synthesize distinctive theoretical literatures on global value chain disintegration, the evolution of industry structures, and the ecology of professions. The aim is to develop an analytical framework that helps us to understand and predict the evolving global value chain dynamics in legal services.

Global value chain disintegration

The value chain describes the process steps taken by producers to transform inputs into outputs, and to market and distribute them to end users. Value chain analysis involves the identification of process steps, and of which steps are carried out in-house and which out-of-house. Porter (1985) made a useful distinction between primary activities of the value chain, and support activities carried out by corporate functions of the firm. For corporations, legal affairs is one such support function, and may be carried out by in-house counsel or by external attorneys. From the perspective of the law firm, legal services are the primary activities in the value chain, and some of these activities may be outsourced or offshored (See Figure 1).

In order to prevent this from becoming a mere mapping exercise, value chain analysis must be underpinned by theories concerning why value chain disintegration occurs, and how value is created and captured in the chain. On the first topic, value chain disintegration occurs when firms decide to 'buy' rather than 'make', due to a reduction in transaction and coordination costs in market than in hierarchy. Lower transaction costs may result from less transaction-specific assets (Williamson 1985), whilst lower coordination costs (or mundane transaction costs) result from the codification of knowledge, standardization of information, and the modularization of tasks (Langlois 2006). The recent revolution in ICT enables codification and standardization, and facilitates geographically dispersed transactions (Mansell et al 2007). However, it should be noted that outsourcing (i.e. 'buy' rather than 'make') does not lead to

the ‘vanishing hand’ of managerial coordination (Langlois 2003). Instead, it requires an investment in the ‘visible hand’ to manage suppliers and logistics (Dosi et al 2008; Fields 2004; Helper and Sako 2009 forthcoming).

Value chain disintegration is also caused by the existence of different capabilities which are not evenly distributed, creating gains from trade and new markets for vertically specialized actors (Jacobides and Hitt 2005; Jacobides and Winter 2005). Other existing explanations of disintegration combine transaction costs and capabilities (e.g. Gereffi et al 2005). Moreover, there are regulatory and institutional episodes that may trigger or facilitate disintegration (Jacobides 2005). For example, deregulation in financial markets and access to non-union labour were key drivers of disintegration in the United States in the 1990s (Lazonick 2008).

Profiting from the value chain

Next, moving to the second topic of how value is created and profit captured in the value chain, this study goes beyond the distinction between buyer-driven and producer-driven commodity chains (Gereffi), and beyond a typology of different modes of value chain governance (Gereffi et al 2005), by combining recent insights from the strategy, innovation and dynamic capabilities literatures.

In management and economics, value appropriation occurs by erecting barriers to entry, by making imitation difficult. For example, Porter identified a comprehensive list of drivers of differentiation, including policy choices (what activities to perform), linkages (with buyers and suppliers), timing (of activities), location, sharing of activities among business units, integration, and scale (Porter 1985: 124-7). Teece (1986) focused on investment into complementary assets in order to profit from innovation. In his analysis, intellectual property protection is necessary but not sufficient for first movers to profit from innovation; what is required to make it sufficient is a simultaneous investment in complementary assets. Gawer and Cusumano (2008) make a related point that a successful platform leader captures sufficient profit for itself, whilst giving incentives for suppliers of complementary products, services, or technologies to invest and develop co-specialized assets (Gawer, 2009 forthcoming). This co-existence of a leader and others in the platform eco-system thus solves an essential technological and business problem within an industry.

Ecology of professions²

What is the impact of professional expertise and orientation on organization design and industry structure? This is an important question when firm-level decisions about make-or-buy and positioning in the value chain are taken, not just by corporate managers but also by professionals such as lawyers. Whilst there is a vast sociology literature on the professions, this study focuses on answering the above question.

An expert possesses a stock of esoteric knowledge that is not widely shared. An expert becomes a professional when he/she becomes organized into a profession, possessing the following four properties

² Andrew Abbott said that in order to avoid the self-equilibrating notion of a system, he should have called his 1988 book the ‘ecology of professions’ rather than the ‘system of professions’ (private communication in Oxford, 2008).

besides expertise: an ethical code, cohesion, collegial enforcement of standards, and autonomy (Shriesheim et al 1977; Adler and Kwon 2006). Professional experts tend to be conservative, resistant to new ideas for a good set of reasons. First, clients and other experts may interpret experts' need to learn as evidence of deficient knowledge. Second, many experts get paid by the hour, and explicit learning reduces the time available for billable services. Third, expertise implies specialization, which reduces versatility and limits flexibility. Fourth, experts' niches are partial monopolies, and like other monopolists, experts hold favourable positions that confer high incomes and social status, which come under threat with social or technological changes. Fifth, expertise entails perceptual filters that keep experts from noticing these changes especially outside their domains (Starbuck 1992).

Professionals, nevertheless, have made incremental changes in their own professions over time, in response to large social forces, both endogenous and exogenous to the professions. In particular, with the tremendous growth in the knowledge base required of a profession, there has been an inevitable drive towards greater differentiation and specialization (Scott 2008b). Scott illustrates this with the growth of specialist physicians with hyphenated titles, and the parallel growth of contiguous occupations (e.g. chiropractors, pharmacists, etc.). Here lies an endogenous reason for greater division of labour in professional work, facilitating the disintegration of the value chain.

The pressures for fragmenting and consolidating professional work arise also in what Abbott called the 'system of professions' (Abbott 1988). In this framework, the jurisdictional boundary of what a profession does arises not only through regulation by the state, training, and self-regulation, but also in relation to other contiguous professions. The struggles between contending occupational groups for jurisdictional control may arise in the face of new kinds of knowledge or new technologies, i.e. when opportunities arise to expand and deepen control. Thus, what lawyers do is determined, not only in relation to its subordinate functions such as paralegals and legal secretaries, but also in relation to other business advisory professionals such as accountants, consultants, and investment bankers. In this framework, new technologies, such as ICT, impact on the professions in two distinct ways: it affects how the existing professional work is carried out, and it also affects the boundary of the work to be carried out by a specific profession.

Last but not least, the rise of large-scale corporations as clients has changed the internal structure and the logic of the professional organization itself. Historically, the organization of the professions has been associated with the use of partnership forms, public or non-profit auspices, and a rejection of market-based institutional logic. However, this professional partnership model, emphasizing 'collegiality, peer evaluation, autonomy, informality, and flexibility of structure' has increasingly given way to a managed professional business form (Hinings et al 1999). In the latter, the logic of individual autonomy and collegial controls is being replaced by a greater reliance on hierarchical control by managers who give priority to strategic planning and marketing (Scott 2008). In this transformation, claimants to professional status have given up using the 'social trusteeship model' (in which they make civic-minded moral appeals to clients) in favour of emphasizing the value of technical expertise. Even with these shifts in the institutional logic underlying lawyers and law firms, actual make-or-buy decisions and criteria used depend

on who has the authority to make those decisions, be they in-house counsels or CEO/CFO in corporations, and individual partners, managing partners, or non-lawyer managers in law firms.

Double-Helix, but with institutional as well as technological and market forces

Our starting point in synthesizing theoretical insights from the three literatures reviewed above is an industry-level model of vertical disintegration and integration, in the shape of a double helix (Fine 1998 Chapter 4) (see Figure 2). Fine argues that in any industry, there is a dynamic cycle, in which the structure becomes vertically integrated with an integral product architecture, followed by a phase in which it becomes horizontally disintegrated with a modular product architecture, and back again to a vertical/integral structure.

In the computer industry, IBM had considerable market power, designing and making virtually everything that went into its mainframe computers with closed, integral product architecture. In the late 1970s, however, IBM faced competition particularly from upstart Apple Computer, and decided to create its own personal computer with modular product architecture, outsourcing the microprocessor to Intel and the operating system to Microsoft. This invited new entry from producers, such as Compaq, making IBM-compatible computers, and from suppliers of subsystems and components. The industry therefore became horizontal, creating fierce competition within each horizontal segment. Over time, however, only players that incorporated technical advances could survive, leading to a shakeout and industry concentration. In particular, Microsoft dominated the PC operating system, able to exploit market power by bundling it with network services, Web browsers, server operating systems, etc., looking more like the old IBM.

Thus, the forces of disintegration are the challenge of keeping ahead of competition across many areas of technology in the face of niche competitors, and the organizational rigidities that often beset large bureaucratic companies. When an industry has a horizontal structure, the forces of integration are the technical advances in one subsystem making it a driver of market power in the value chain. The subsystem supplier has an incentive to enhance its market power further by bundling with other subsystems, and by seeking proprietary and integral solutions to product design.

The double helix framework, as devised by Fine, is therefore useful in analyzing the dynamics of the evolution of industry structure. It is also useful in identifying alternative strategies to profit from the value chain in different industry structures. However, the framework should be modified in two ways to suit the purpose of my study. First, the industry structure cycle in the shape of a double helix depends on specific assumptions made about institutions in capital and labour markets. In particular, new entry by subsystem suppliers requires mobile technical labour and availability of funding (e.g. venture capital) for new start-ups. Without these, no horizontal structures would emerge, even with modular product architecture, as was the case with computers and cars in Japan.

Second, as one goes around the loop in the double helix, the boundary of the industry for which the helix is drawn changes. The mainframe computer industry dominated by IBM because a PC industry when horizontal, and the dominant firm that integrates back is Microsoft whose industry is software. Similarly, Apple Computer was not so successful as an integrated PC firm, but emerged successful as Apple Inc. with

its iPod and iPhone, when it bundled entertainment and mobile telephony. So, dominant firms in an industry have the power to shape and reshape the boundary of the industry to which the double helix is applied.

As applied to professional services, the double helix is therefore useful in anticipating new entry by subsystem providers, and pressures for re-integration through technical advances in the future. Moreover, the first modification above points to the importance of professions as institutional agents (Scott 2008) in whether or not to translate modular architecture of professional services into more disintegrated organization design. The second modification alerts us to the fact that the exact way in which the boundary of legal services industry changes over time – e.g. with legal services offered as part of a bundle of professional business services -- depends on which subsystem provider captures the power and profit in the value chain.

3. Demand Perspectives in the Legal Services Value Chain

This section analyzes the demand side of the LPO industry. A necessary condition for the rise of LPO is the dis-integration of the legal services value chain. In particular, information and communication technology (ICT) has enabled such dis-integration, by (a) introducing a higher degree of standardization and codification of legal knowledge, (b) facilitating organizational modularity between the back office and the front office; and (c) making geographically distanced delivery possible.³ Whilst ICT potentially impacts different types of users and producers of legal services equally, we need to describe the history and context of why LPO came about. In particular, it is generally understood that business corporations, rather than law firms, drove the LPO phenomenon.⁴ The reason for this may be found in a number of factors that distinguish the business corporation from the law firm, including their ownership structure and its influence on strategic objectives. In particular, law firms' relative reluctance to offshore legal work may be due to (a) lawyers' conception of their work, (b) the notion of partners' autonomy to make make-or-buy decisions.

Business corporations' make-or-buy decisions

From the perspective of a business corporation, legal service is one of the support function activities. Corporations have typically managed this support function through employing a mix of in-house counsels and external attorneys, though the balance between 'make' and 'buy' has shifted over time. There has been a trend towards creating shared services in specific support functions such as finance and human resource management, and outsourcing and/or offshoring such shared services. Corporate functions had

³ See Sako and Chondrakis (2009) for greater details on the impact of ICT on the co-evolution of organizational and vertical architectures.

⁴ According to a 2008 survey of law firms by Prince OMC, an advisory firm, 27% of respondents thought that the key driver of offshoring was 'pressure from clients to lower costs', whilst a further 25% considered the key driver to lie in 'market leaders proving model' (Prince OMC 2008).

been treated as unavoidable overheads, but are unbundled from divisions and centralized in order to improve efficiency via standardization and consolidation (Gospel and Sako 2009).

Similarly, corporate legal departments came to be scrutinized for more efficient and cost-effective delivery. Interestingly, however, global corporations initially combated law firms' uncontrollable fee increases by bringing legal work back in-house in the late 1980s and early 1990s. This decision in favour of more 'make' rather than 'buy' appears to be different from the experience in other business services. Companies such as Dupont and GE rigorously applied Six Sigma to standardize and process engineer legal work in-house. Other measures to control legal cost included convergence (i.e. the use of a smaller number of law firms or a sole law firm in extreme cases), fixed fee contracts to replace billable hours, and the use of contract lawyers. Offshoring to India, initially via captive operations, as GE Plastics did in 2001, and later to independent LPO providers, is part and parcel of these cost reduction measures pursued by corporate legal departments. The key motivation for offshoring is wage arbitrage, i.e. access to skilled labour at a fraction of the cost in the US or Europe; the hourly rate for associates in the US is \$250-\$300 on average, compared to \$60 for US paralegals and \$30 for Indian legal professionals.

Global corporations are looking at LPO as a better more cost effective alternative to doing the work in-house within the national border. This, in itself, however, does not give much insight into which legal processes are kept in-house and which are outsourced. We need more systematic evidence on the make-or-buy decisions in legal services, and who make these decisions. In particular, a CEO/CFO would be more likely to make a radical outsourcing decision than if left to the general counsel of the corporation.

Make-or-buy decisions by law firms

From the perspective of a law firm, the value chain consists of three separable steps: (a) knowledge and information management (KIM) (b) consultative advice and representation (CAR); and (c) client relationship management (CRM). For example, in intellectual property work, prior art search and IP portfolio analysis are part of KIM, whilst commercialization studies of unused patents fall into giving consultative advice. Similarly, in litigation work, document discovery (including e-discovery) is part of KIM, which becomes a basis for advising and representing clients in court. Traditionally, a client placed trust on a particular lawyer to carry out all three steps, with some assistance from junior associates and paralegals.

Over time, however, the use of ICT has reduced coordination costs, enabling the separation of the knowledge and information management (KIM) block from the rest of the law firm's value chain. ICT has, in effect, enabled the separation of information service from advisory work, by employing what Susskind calls legal knowledge engineers, 'whose job it is to standardize, systematize, and package the law. They analyze, reorganize, and restructure legal knowledge in a form that can be embodied in smart systems' (Susskind 2000). The standardization and the modularization of legal tasks have facilitated disintegration.

A traditional law firm in England or the United States, offering integrated legal services under one roof, is a limited liability partnership (LLP). Equity partners typically use profit per partner as a measure of

performance of the firm. Profit per partner may be improved by either reducing costs or increasing revenue, through the following mechanisms. They may reduce costs by:-

- Consolidating and restructuring business support functions through shared services
- Using IT and process engineering to improve the efficiency of knowledge and information management
- Relocating to cheaper locations

They may consider increasing revenue by:-

- Raising average fee per hour (e.g. by moving into higher end work)
- Increasing the number of hours billed per fee earner
- Increasing ‘leverage’ (i.e. no. of fee earners per equity partner) (achievable by employing more associates and paralegals, and contracting with LPO legal professionals)

Thus, outsourcing and offshoring is only one of several ways in which profit per partner may be increased. Lawyers may appear reluctant to use the outsourcing and offshoring option because the billable hour does not give an incentive to necessary lower costs rather than raise revenue. Moreover, the partnership model with distributed authority implies that decisions to outsource or offshore are typically taken at the decentralized level, practice by practice, or even partner by partner.⁵ This makes it unlikely that law firms adopt a centralized firm-wide decision to outsource, in the way P&G had done (Gospel and Sako 2009), for their paralegal work. Resistance to change in the way work is done, that is inherent in a tightly defined profession, also contributes to the reluctance to offshore.

Nevertheless, the corporatization of law firms, i.e. the move away from a partnership model to a corporate model, may change this situation. For example, law firms are employing more professional managers who have capabilities other than legal expertise to manage law firms using indicators other than profit per partner. Following the Australian example to deregulate the ownership structure of law firms,⁶ Britain enacted the Legal Services Act, facilitating entry by new types of legal services providers with alternative business structures (www.legalservicesboard.org.uk). New ownership structures, with investment by private equity and hedge funds, would change the criteria for make-or-buy, whilst entry by firms that can offer other professional services alongside legal services would alter the boundary of the industry.

Notwithstanding these possible future changes, corporations rather than law firms are the more proactive demander of outsourcing and offshoring.

⁵ It would be interesting to investigate whether or not the mix of different legal practice areas in law firms influence their propensity to outsource and offshore legal services. Armour and Skeel (2008) identified a negative correlation between the number of lawyers outside home jurisdiction and the proportion of litigation partners in law firms, suggesting that litigation-oriented law firms need not be global, whilst corporate transaction-oriented law firms are more international. Does this difference translates into greater willingness to use LPO by international corporate transaction-oriented law firms than domestic litigation-oriented firms?

⁶ The worlds’ first initial public offering (IPO) of a law firm, Slater & Gordon in Australia, may be the precursor to what’s to come with regulatory changes, e.g. the Legal Services Act in the UK.

4. Profiting from the Value Chain: Evidence in India

This section presents a preliminary typology for analyzing legal process outsourcing (LPO) in India, based on interviews with LPO providers and law firms. The section is in three parts. We will first survey the industry landscape, identifying different points of entry into this relatively new sector. Next, we describe two types of legal services value chain, one led by a law firm and other led by a corporation, in order to identify upgrading opportunities for LPO providers. Lastly, we analyse the dynamics of three distinct strategies pursued by LPO providers to create value and profit from the chain.

LPO as part of India's BPO/KPO sector: points of entry with different capabilities

Back in the 1980s, global corporations began to outsource and offshore software applications development and maintenance to India. Captive establishments belonging to firms such as GE and Citibank were followed by third-party service providers, led by large players such as TCS, Cognizant, Infosys, HCL, Patni, and Wipro. In the 1990s, India began to establish its reputation as an offshoring destination, and these providers went beyond IT services to transaction processing in administrative and support functions and in voice-based contact centres. Everything that was offshored came to be called business process outsourcing (BPO). In the 2000s, with India's reputation rising, global corporations and financial institutions began to consider offshoring more complex and knowledge-intensive professional services, in business and market research, financial data analytics, engineering design, radiology, and R&D. This phenomenon came to be known as knowledge process outsourcing (KPO). Legal process outsourcing (LPO) is regarded as part of KPO, and is projected to employ 40,000 (compared to 1200 in 2008) and be worth \$4-6 billion by 2010 (ValueNotes 2008).

GE Plastics is credited with pioneering the phenomenon of offshoring the legal support function by establishing a captive offshore base in India to draft contracts in 2001.⁷ Since then, legal departments of other global corporations, such as Microsoft, have followed suit in their attempt to curtail mounting legal fees in the US or Europe. More recently, foreign law firms are exploring possibilities either by establishing captive operations, as Clifford Chance had done, or by outsourcing to independent service providers. At the same time, IT-BPO providers, such as Infosys and Wipro, started offering LPO as part of their higher value adding service offering, in order to 'climb up the value chain' to improve their profitability. Evalueserve, the firm that is credited with coining the term KPO, started in 2000 with intellectual property work, as part of a more diversified set of business lines including business and financial research. There are also more focused new entrants into LPO, namely 'pure play' LPO providers (such as Mindcrest and Pangea3), and Indian law firms creating LPO subsidiaries (such as AZB's Bhodi Global and FoxMandalLittle's Legal Circle).

There are, therefore, at least five different types of entrants into the LPO sector, with different distinctive capabilities that they bring. For example, foreign and Indian law firms have deep knowledge and expertise in practising law, but may lack in-house capability in using IT to improve processes and to

⁷ *Corporate Counsel*, March 2003, p.78.

enable distanced delivery. By contrast, IT-BPO providers have the latter set of capabilities in IT, process improvement, and project management, but must buy in legal knowledge and expertise to create an LPO operation.

These LPO providers are located in Indian cities like New Delhi/Gurgaon, Mumbai/Powai, Pune, and Hyderabad to provide legal support in patent filing, contract reviews, legal research, litigation, and compliance. Instead of having paralegals and contract lawyers down the hall, corporate legal departments and law firms are using professionals to carry out equivalent work thousands of miles away.

Actual and anticipated changes in international and national regulations have influenced the speed with which the LPO sector has grown, modes of entry into the sector, and the nature of work that LPO providers are permitted to carry out. In particular, notwithstanding on-going – largely bilateral -- negotiations for liberalizing international trade in legal services, foreign lawyers are forbidden from practising law in India (and Indian lawyers are forbidden from practising law in the United States, England, etc. This restriction forecloses certain options for foreign law firms; for example, Clifford Chance cannot open a law practice in India, and the work of its knowledge centre in India is limited to employing Indian law graduates to provide paralegal support to Clifford Chance's partners and associates worldwide. Within India, law firms remained relatively small, but the shift from unlimited liability partnership to limited liability partnership in early 2009, as well as the growing corporate law work, may provide opportunities for some Indian law firms to grow in size and become more international. In the United States, there had been concerns that LPO infringe client-attorney privilege as it involved passing on information pertaining to specific cases to a third party. However, the American Bar Association opinion published on 2 September 2008 has given sufficient confidence to give legitimacy to the business of LPO.⁸ A clear regulatory impediment remains, however, for LPO providers as they upgrade to high end work, as they are not permitted to practise law.

More work needs to be done to understand the extent to which actual and anticipated regulatory changes concerning legal services are influencing the strategies of LPO providers and law firms.

Law firm driven vs. corporation driven value chains

Given the institutional context described above, profit-capturing opportunities for LPO providers vary according to whether their clients are law firms or business corporations. In a law-firm driven value chain, the major part of LPO providers' work lies in knowledge and information management. Climbing up the value chain implies taking all steps in KIM. But even as the LPO provider accumulates internal legal process capabilities, it is unlikely to be able to take on advisory work, unless the law firm as client wishes to dis-intermediate itself. LPO providers' growth is therefore likely to come more from new client markets, by developing low-cost efficient solutions (in effect a new product) for new segments in the legal marketplace which had previously not been able to afford the service, for example small and medium-sized

⁸ The conditions sought by the ABA opinion are the adequate supervision of offshored work by a lawyer, reference check on confidentiality and data protection, the charging of reasonable rates, the proper education of employees, and the retention of client-attorney privilege.

firms and low-income households. This is what Susskind calls a latent market, which may also grow if self-service replaces some of the one-to-one advisory work done by lawyers (Susskind 2000).

By contrast, in a business corporation driven value chain, an LPO provider deals directly with a client corporation, specifically with its in-house counsel or with R&D managers (for IP work). Upgrading opportunities, taking on advisory work, appear larger in this value chain, with external attorneys hired directly by the corporation joining only at times to deliver premium advice. Then the major part of the profit pool may be shared between the LPO provider and its corporate client. In corporate transactional work, LPO providers may have the opportunity to undertake multi-disciplinary business advisory work, by combining legal and non-legal work in mergers and acquisitions, for example.

Differences between legal services areas

Profit earning opportunities also differ between LPO areas in part due to differences in the nature of legal work involved. For instance, comparing litigation support and intellectual property (IP) work sheds light on the ease (or difficulty) with which LPO providers may move up the value chain.

First, litigation support is a volume business, particularly with the recent law to subject all electronic files to e-discovery work. Margins for LPO providers appear to be lower in much of paralegal work, compared to IP work that requires a combination of science and technology knowledge at the doctoral level and jurisdiction-specific patent law knowledge. Moreover, law firms tend to be more conservative than business corporations in outsourcing and offshoring, rendering the growth in the LPO market for higher end litigation support work uncertain.

Second, intellectual property work carried out by LPO providers range from patent search, patent drafting, IP asset management, patent valuation, and commercialization studies. Given the need for doctoral level knowledge in a specific branch of science, medicine, and engineering, much of the IP is higher value adding than coding work in litigation support. With effective customer relationship management with corporations, it may be easier to extend IP services from information management (e.g. patentability assessment, freedom-to-operate studies) to advisory work (e.g. IP asset management including commercialization studies).

Alternative strategies for capturing profit in the chain

Much of the LPO activities lie within the knowledge and information management (KIM) component of the value chain. LPO providers are distinct from law firms in that the former provide support services for professional lawyers. Legally trained employees of LPO providers, therefore, do not practise law. This distinction is important to LPO providers as they solicit work, so as not to be seen to be cannibalizing or dis-intermediating law firms.

Strategies pursued by LPO providers may vary according to (a) the mode of market entry with a different mix of capabilities (legal knowledge, process improvement capability, IT knowledge), (b) whether the predominant value chain is driven by the corporation or the law firm, as this affects opportunities for upgrading, and (c) the extent of specialization or diversification in legal service practice areas, such as

litigation support or intellectual property work. These three dimensions were described above, and it is now time to put them together. The study has identified three generic strategies for LPO providers. The three are not necessarily mutually exclusive, but there are some trade-offs in pursuing two or three at the same time.

1. Competing on scale and process efficiency

The first strategy is to compete on volume, exploiting economies of scale and applying management tools such as process mapping and Six Sigma to improve productivity and quality. Among the firms interviewed for this study, Infosys BPO, Integreon, CPA Global, and UnitedLex are pursuing this strategy.

Infosys BPO Ltd. is a subsidiary of Infosys Technologies, providing 'functional solutions' in finance & accounting, human resources, customer services, order management, sourcing & procurement, and knowledge services. LPO is part of knowledge services, which Infosys entered in 2008 as a result of demand by its existing corporate clients. An early example was LexisNexis, for whom Infosys Technologies managed the IT infrastructure. Infosys BPO then began to manage some behind-the-scene content, with a view to moving into more advanced content work, such as head-noting and case summarization. In mid-2008, this project employed around 300 employees at Infosys in Pune, of whom 40% were said to be trained as lawyers. Legal services work at Infosys BPO is said to be infused with the DNA of Infosys Technologies, with its process driven approach and robust project management in which a solutions design team provides advice to a corporate client, devises a solution, and puts forward an execution plan before implementing. This upfront work leads to less variability in processes once the project reaches steady state. There are three phases to a project: transition, parallel runs, and steady state. The LexisNexis legal publishing project involved 12 weeks of training in transition, and 16 to 18 weeks of parallel runs before moving into steady state. Infosys BPO intends to apply the same methodology to three key areas of LPO, namely contract review, IP, and e-discovery.

Integreon is another relatively large provider of business services with a strong emphasis on efficiency and quality. It provided the management expertise for Clifford Chance to start this magic circle law firm's captive shared services centre in Gurgaon (*Financial Times* 25 February 2008). In its business services work, Integreon collects and monitors data on work productivity, capacity utilization, on-time delivery, quality levels etc. Integreon started offering legal services by reviewing contracts in 2006. The head of Integreon's legal services department said: 'our aim is to make contracting activities more repeatable and scaleable, to make them predictable and totally consistent.' Much of the scalability and repeatability is enabled by the use of technology, by putting all contracts onto a database. The same can be said about document discovery in litigation support. Not surprisingly, therefore, Integreon's two leading LPO areas were litigation support and contract reviews, the legal processes that benefit from scale. Integreon employed 400 legally trained employees in 2008.

CPA Global had specialized in patent renewals and IP management since its inception in 1969 until it decided to diversify into other legal services in 2007. In India, CPA in 2008 employed 400 workers, of

whom 60 are law graduates who worked on IP work, legal support work, and paralegal work. CPA hired process management experts in order to apply process mapping and quality control to processes such as docketing, patent proofreading, and contract review. CPA Global monitors performance by collecting internal data on utilization (how many workers are used relative to capacity?), productivity, turnaround time (from the day work comes in to completion), and quality (measured in terms of defect per million opportunities; a patent document may contain 10 opportunities including the date of application, inventor name, etc.). Productivity is a measure of individual efficiency, the ratio of the time set by a time and motion study for a task to the actual time it takes an employee to carry out the task. For example, in reviewing contracts, the metric of 10 minutes per document was established through a time and motion study to review only 8 specific clauses per contract. If the actual time taken was 8 minutes, then productivity is $10/8 = 125\%$. Repeatability is a pre-requisite for learning-by-doing and productivity improvement over time.

To summarize, this strategy of scale and efficiency enables LPO providers to capture profit not just through labour cost arbitrage, but through their proprietary capability to manage projects and workflows. As a manager at Integreon put it: 'In the long run, it is not about costs. The question is: can you do the work better than the client? If the answer is yes, then there is less worry about costs.' The LPO providers pursuing this strategy tend to have corporate clients, rather than law firm clients, for ease of achieving scale. They also tend to believe that much of the LPO work can be done by employees without legal training, particularly if the work can be disaggregated.

2. Competing by climbing up the legal services value chain

A second strategy for LPO providers is to compete on adding higher value by climbing up a specific legal services value chain. Bodhi Global Services, Legasis, Mindcrest, and QuisLex have this as their dominant strategy. These providers have in-house legal knowledge due to the fact that lawyers were founders. They employ primarily law graduates (and science and engineering graduates for IP work), and tend to work with law firms as clients, with small boutique law firms rather than large top-tier law firms as early pioneers.

Bodhi Global is a joint venture between a prestigious Indian law firm, AZB, and an Indian IT services provider, Patni. Based in Pune, the litigation support department is headed by a litigation lawyer who used to be at Weil Gotshal & Manges. He reflected that when he was a junior lawyer, he was part of a team that had to go through 5000 documents in boxes. With the volume of electronic documents multiplying, US law firms started using contract lawyers to do document discovery, but there has been no knowledge retention as contract lawyers turn over. In India, by contrast, his intent was to bank on developing a dedicated team that develops a close understanding of a specific client. He travels between New York and Pune frequently to facilitate this, in Pune to train law graduate employees and to familiarize a team with facts of a specific case. Bodhi Global also employs a director of operations who had been a practising lawyer, to apply process control and Six Sigma to legal work. Thus, whilst taking process control seriously, Bodhi Global wishes to develop long-term relational contracting with law firm clients.

Over time, it is expected that Bodhi Global may be able to write deposition summaries and even summary judgement in collaboration with the trial team.

Mindcrest Inc. was founded by US-trained lawyers and an ex-Sun Microsystems technical professional in 2001. By 2008, its India operation in Pune employed 450 law graduates, to focus on litigation support and corporate work (including contract management, due diligence, compliance). Although the nature of work at Mindcrest may not look so different from that at Infosys, Integreon, or UnitedLex, the principles applied to conduct the work were different. First, Mindcrest said it provided only the type of LPO that required legal training, and therefore did not take on processes in transcription or coding. They consequently recruited law graduates only. Despite the firm's early mover advantage, the Managing Director was modest enough to say that 'we're learning still' in applying process control to legal work. 'We take something inherently subjective, give it objectivity in measuring output without taking away that subjectivity', he said. This practice can be institutionalized, he believed, as long as employees are reminded that 'lawyers are at the heart of the company. Tempting though it might be, we must not over-processize the company.'

Legasis Services is also based in Pune, and founded by an entrepreneurial Indian lawyer who recognized the power of combining IT and lawyering. For example, Legasis has a virtual data room in which clients can conduct due diligence on a self-service basis on-line; it also developed a contract management software for a bank, which might be licensed to other clients. Legasis's other niche area is legal research, again an area difficult to standardize because the content is not repeatable. Legasis therefore derives added value through complementary investments in IT and legal knowledge.

QuisLex, based in Hyderabad, is another LPO provider founded by an ex-Skadden lawyer from India. QuisLex, like Mindcrest, does not take on certain low-end work, such as objective coding. It sees itself as 'constantly moving up the value chain', which is seen as a natural progression as risk tolerance by clients has grown and clients are getting more comfortable with the idea of offshoring. For example, QuisLex might have started with document review only in litigation support, but it is assisting some clients with formulating a strategy on how to use the documents in cases, and writing deposition summaries. Like Bodhi Global, moving into higher end work within the litigation support value chain requires a relational contracting mindset.

QuisLex recognizes the need to have an onshore-offshore mix, but this is not because higher end work gets done onshore. Much of the onshore presence is due to regulatory constraints; for example, a regulation may prevent certain types of documents, e.g. in defence, to be reviewed outside the US border. Interestingly, QuisLex has a joint venture with a US temporary labour agency that provides contract lawyers onshore. It is used to create the initial comfort for new clients. The QuisLex CEO said that a one-off engagement requiring only a few days is done onshore, because it is not worth the investment of time to train employees, to get to know the client, and to plan and implement the processes. So, 'if anything, India has permanent employees and therefore better processes.' By contrast, the onshore operation is not based on robust processes, using temporary attorneys in transition, who come and go. For offshoring to be work, it has to be a partnership, and clients must be willing to make the investment in the relationship.

To summarize, the LPO providers pursuing the above strategy capture value and profit on the basis of deep in-house legal knowledge with complementary investment in process control or IT. These providers regard long-term relational contracting at a distance essential in achieving their objective to climb up the value chain within a specific legal process. There is less emphasis, as compared to in the first strategy, for growth in headcount. And the need for onshore presence may arise from marketing activity, but is largely seen as a regulatory constraint. Offshoring requires investment, and therefore predicated on long-term relationships, whilst onshoring suffers from exit-based relationships which are not suitable for complex tasks.

3. Competing by delivering multi-disciplinary professional services

A third strategy is to compete on offering legal support services as part of a broader set of professional services. On a simple level, many LPO providers offer legal support services in multiple areas, combining patent work and litigation work for example. In seeking volume, LPO providers with the first strategy may also cross-sell between LPO and other types of business services.

Evalueserve, a knowledge process outsourcing (KPO) firm based in Gurgaon and Noida, provides business research to consulting and industry analyst firms, financial and equity research to investment banks, and legal services to corporations and law firms.⁹ With this portfolio of knowledge-intensive professional services, opportunities to climb up the value chain have arisen in providing consulting-like advice to client firms, although some of them may feel threatened by the possibility of Evalueserve cannibalizing client business. Nevertheless, Evalueserve is seeking an ‘umbrella deal’ in which a client places order for multiple projects in different business lines, such as market research, intellectual property, and M&A due diligence. Although not part of an espoused strategy, Evalueserve sees ‘offering services related to law, company restructuring, and financial accounting under one roof’ as a source of competitive advantage.¹⁰

Ultimately, the pursuit of this strategy redefines the boundary of the industry for which the value chain and the double helix are being drawn. In this case, the market power in the value chain is driven by a subsystem supplier bundling services. Although some way to go still, LPO providers might be a precursor to a multi-disciplinary professional services firm.

5. Conclusions

This paper developed a value chain framework for analyzing the growth and viability of the LPO market in India. The legal services value chain consists of three blocks, namely knowledge and information management (KIM), consulting advice and representation (CAR), and client relationship

⁹ See a Said Business School teaching case ‘Evalueserve: Globalizing the Business of Giving Insight?’, 2009, for details.

¹⁰ Dr. N. Saluja, head of IP at Evalueserve, in ‘US meltdown prompts LPOs to step up hiring’, *Business Line (The Hindu)*, 29 September 2008.

management (CRM). The evidence from our interviews reveals that legal services are being unbundled, with the KIM component being separated by ownership and geography from CAR and CRM components. To assess the actual extent of disintegration, the study identified the conditions under which demand and supply for LPO services is generated. On the supply side, the study identified three alternative strategies for LPO providers from the value chain.

By making explicit the impact of the nature of professions on make-or-buy decisions and industry structure, the study shows that the impact of ICT in facilitating organizational modularity and distanced delivery may not translate into value chain dis-integration if there are professional autonomy and values that mitigate the perceived benefits of offshoring. Moreover, the use of the modified double-helix framework highlights LPO providers' opportunity to rebundle LPO with other professional services, thus redefining the boundary of the industry.

The impact of LPO on the legal profession is complex. There are two opposing pressures on what lawyers do, one towards contraction and the other towards expansion. On the one hand, the contraction of legal work is due to commodification brought about by the use of IT and process engineering, leading to the separation of KIM from what lawyers do. On the other hand, the expansion of legal work is primarily in consulting advice and representation (CAR), as 'lawyers become more commercial, going beyond the delivery of black letter law and adding value as business consultants as well as legal advisors' (Eversheds 2008). This phenomenon is most prevalent in relatively new practice areas such as in venture capital financing (Suchman and Cahill 1996), outsourcing (Sako 2008), and private equity. However, there is no guarantee that lawyers retain an upper hand over other professionals in offering premium, cutting edge advice.

References

Abbott, Andrew (1988) *The System of Professions*, Chicago: University of Chicago Press.

Adler, P. S. and S.-W. Kwon (2006) *The Evolving Organization of Professional Work*. mimeo, Marshall School of Business, USC.

Armour, John and Skeel, David A. (2008) *A Theory of Law Firm Globalization*, Oxford University mimeo.

Baldwin, R. (2006) *Globalisation : The Great Unbundling(s)*, paper for the Finnish Prime Minister's Office, Economic Council of Finland as part of EU Presidency.

Berger, Suzanne (2005) *How We Compete*, MIT Press.

Fine, Charles (1998) *Clockspeed*, Reading, Mass.: Perseus Books.

Empson, Laura (ed.) (2007) *Managing the Modern Law Firm*, Oxford: Oxford University Press.

Eversheds (2008) *Law Firm in the 21st Century: an Eversheds Report*, London: Eversheds LLP.

Gawer, A. and Cusumano, M. (2008) 'How Companies Become Platform Leaders' *MIT Sloan Management Review* Winter: 28-35.

Gawer, A. (2009 forthcoming) 'Platform Strategies, Firms' Capabilities, and Platform Industry Dynamics' in Gawer, A. (ed.) *Platforms, Markets, and Innovation*, Edward Elgar.

Gereffi, Gary et al (2005) 'The Governance of Global Value Chains' *Review of International Political Economy* 12: 78-104.

Gospel, Howard and Sako, Mari (2009 forthcoming) 'The Unbundling of Corporate Functions: The Evolution of Shared Services and Outsourcing in Human Resource Management', *Industrial and Corporate Change*.

Helper, Susan and Sako, Mari (2009 forthcoming) 'Management Innovation in Supply Chain: Appreciating Chandler in the Twenty-first Century' *Industrial and Corporate Change*.

Hinings, C. R., Greenwood, R. and Cooper, D. (1999) 'The Dynamics of Change in Large Accounting Firms' in Brock, David M. et al (eds.) *Restructuring the Professional Organization: Accounting, Health Care, and Law*, London: Routledge.

- Jacobides, Michael G. (2005) 'Industry Change through Vertical Disintegration: How and Why Markets Emerged in Mortgage Banking' *Academy of Management Journal* 48(3): 465-498.
- Jacobides, M. G. and Hitt, L. M. (2005) 'Losing Sight of the Forest for the Trees? Productive Capabilities and Gains from Trade as Drivers of Vertical Scope' *Strategic Management Journal*, 26: 1209-1227.
- Jacobides, M. G. and Winter, S. G. (21005) 'The Co-evolution of Capabilities and Transaction Costs: Explaining the Institutional Structure of Production' *Strategic Management Journal*, 26: 395-413.
- Langlois, Richard N. (2003) 'The Vanishing Hand: The Changing Dynamics of Industrial Capitalism', *Industrial and Corporate Change*, 12(2): 351-385.
- Langlois, Richard N. (2006) 'The Secret Life of Mundane Transaction Costs', *Organization Studies*, Vol.27 No.9, pp.1389-1410.
- Leblebici, Huseyin (2007) 'Your income: Determining the value of legal knowledge: billing and compensation practices of law firms' in Empson, L. (ed.) *Managing the Modern Law Firm*.
- Mansell, Robin et al (2007) *The Oxford Handbook of Information and Communication Technologies*, Oxford: Oxford University Press.
- Porter, Michael (1985) *Competitive Advantage: Creating and Sustaining Superior Performance*, New York: The Free Press.
- Prince OMC (2008) *Learning to Benefit from Outsourcing: Legal Industry Outsourcing Trends 2008*, London: PrinceOMC, in association with Legal Business.
- Sako, Mari (2008) *The Role of Lawyers in Relational Contracting*, Said Business School working paper.
- Scott, W. Richard (2008a) *Institutions and Organizations*, Third Edition, Thousand Oaks, CA: Sage.
- Scott, W. Richard (2008b) 'Lords of the Dance: Professionals as Institutional Agents' *Organization Studies*, 29 (2): 219-238.
- Sherer, Peter D. and Lee, Kyungmook (2002) 'Institutional Change in Large Law Firms: A Resource Dependency and Institutional Perspective' *Academy of Management Journal*, 45(1): 102-119.

Starbuck, William H. (1992) 'Learning by Knowledge-intensive Firms' *Journal of Management Studies*, 29 (6): 713-740.

Sturgeon, Tim (2002) 'Modular Production Networks: A New Model of Industrial Organization' *Industrial and Corporate Change* 11(3): 451-496.

Suchman, Mark C. and Cahill, Mia L. 'The Hired Gun as Facilitator: Lawyers and the Suppression of Business Disputes in Silicon Valley' *Law & Social Inquiry* 21(3): 679-712.

Susskind, Richard (1996) *The Future of Law: Facing the Challenges of Information Technology*, Oxford: Oxford University Press.

Susskind, Richard (2000) *Transforming the Law*, Oxford: Oxford University Press.

Susskind, Richard (2008) *The End of Lawyers? Rethinking the Nature of Legal Services*, Oxford: Oxford University Press.

Teece, David (1986) 'Profiting from technological innovation: Implications for integration, collaboration, licensing and public policy' *Research Policy* 15: 285-305.

Wilkins, David (2007) 'Valuing diversity: Some cautionary lessons from the American experience' in Empson, L. (ed.) *Managing the Modern Law Firm*.

Table 1: LPO Providers and Law Firms in India, interviewed for this Study

ALMT Legal

AZB*

Bodhi Global Services Pvt. Ltd.

Clairvortex Knowledge Processes Pvt. Ltd.

CPA (Computer Patent Annuities) Global

Evalueserve Pvt. Ltd.

FoxMandalLittle*

Infosys BPO

Integreon

Intrust Global Services

Lawscribe

Legasis

Lexadigm

Luthra & Luthra*

Mindcrest (India) Pvt. Ltd.

Pangea3

Quattro BPO Solutions Pvt. Ltd.

QuisLex

Suprawin Technologies Ltd.

Unitedlex

* law firms

Figure 1: The Disintegration of Legal Services

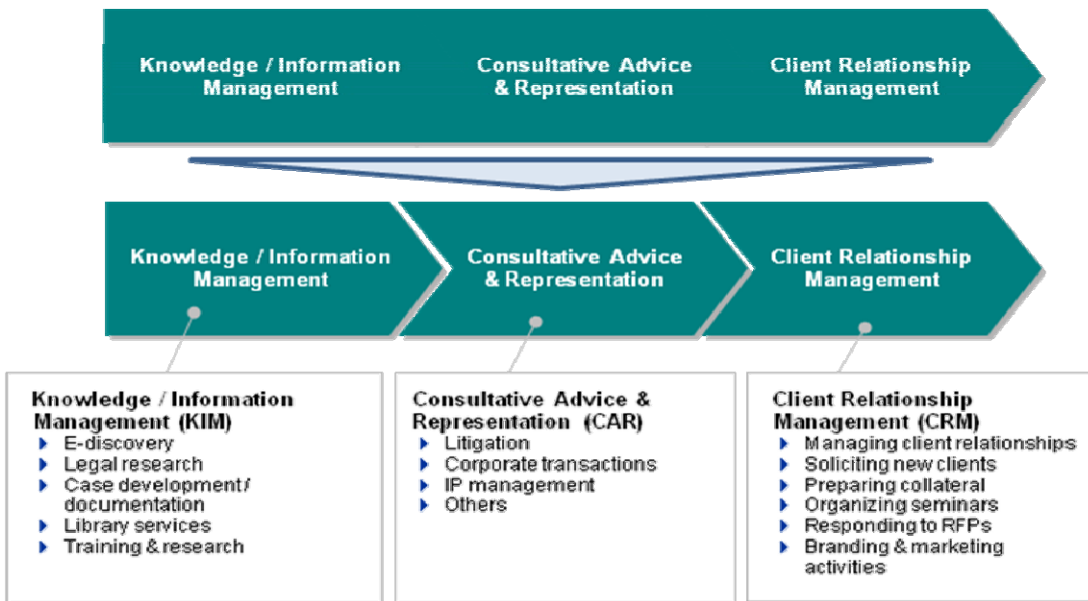
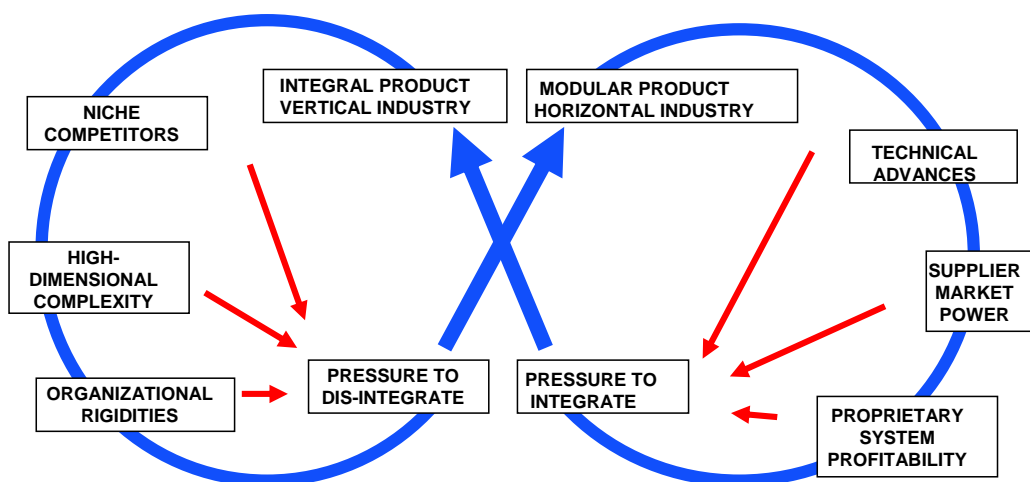
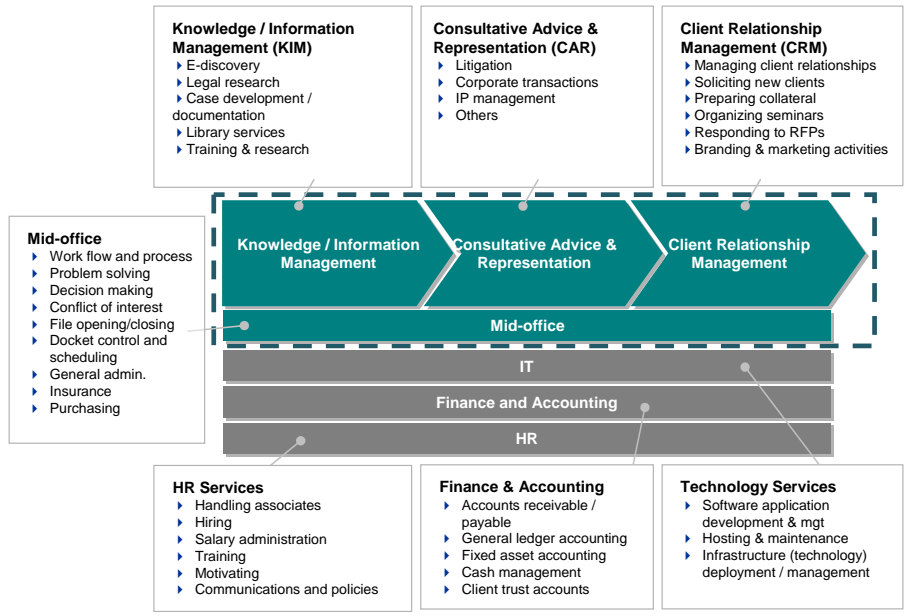



Figure 2: Double Helix Pattern of Industry Structure Evolution, from Vertical/Integral to Horizontal/Modular, and Back



Source: Charles Fine (1998) *Clockspeed*, p. 49

Figure 3: Value Chain of a Law Firm



 Primary services in a law-firm value-chain