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General Counsel with Power?

Mari Sako with Afterword by Richard Susskind

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Executive Summary of Key Findings

Size and shape of legal departments

- **In-house legal departments reflect the structure of businesses.** Some in-house legal functions are centralized at the corporate headquarter, whilst others are decentralized to a varying degree to business and geographic units.
- **In-house legal departments' reliance on external legal resources varies enormously.** This study identified a range from 12% to 93% in the proportion of external to total legal spending.
- **There are four types of general counsel with respect to their make-or-buy decisions,** namely Externalizer Type I, Externalizer Type II, Mid-ranger, and Internalizer. Externalizer Type II (proactively managing legal networks) and Internalizer (in-sourcing actively) are the ones with an appetite for change in legal services.

Convergence, panels, and legal networks

- **Panels mean different things to different general counsel** due to differential emphasis placed on competition and collaboration in managing a panel.
- **On convergence, GCs who believed in competitive selection for a panel followed by close collaboration reduced the number of law firms more rigorously than those who wished to retain competition within a panel.**
- **Online bidding for legal work was used selectively both within the panel and to identify new providers.**
- **The most collaborative form of a panel took the shape of 'legal networks',** in which the general counsel facilitated lateral collaboration amongst the law firms to deliver services as an extension of the in-house legal function.

A Production-line approach to legal work

- **A production-line approach to delivering legal work consists of three steps:** disaggregation and standardization, process flow management, and project management.
- **Many general counsel found a variety of reasons to reject or delay the wholesale adoption of this production-line approach.**
- **In practice, the general counsel adopted either a craft approach, an automation approach, or a process flow approach.** Internalizers tended to lead in implementing a combination of automation and process flow approaches.

What do lawyers do in a multi-sourcing world?

- **Multi-sourcing – the use of multiple sources of legal service delivery – is likely to change the contour of global value chains in legal services.**
- **Value migration away from the traditional corporate client – law firm transactions is more likely due to three factors:** (a) the more the motive for offshoring and near-shoring goes beyond mere labour cost arbitrage to the implementation of a production-line approach, (b) the more lead is taken by the in-house legal function in project management, and (c) the higher up the priority list the general counsel places the issue of efficient legal service delivery.



Chapter 1: Introduction

Globalization, digital technology, and multi-disciplinary professional knowledge -- these pervasive forces present opportunities and challenges for all major law firms, potentially transforming legal practice via two agents of change. One is the in-house legal function in corporations and financial institutions. In a buyer's market, the general counsel is exerting greater power in relation to the external lawyer. The other agent of change comes in the form of new entrants into the global legal services market. These non-traditional suppliers, including so-called legal process outsourcing (LPO) providers, deliver legal support services from low cost locations, onshore and offshore. How are lawyers responding to these gentle winds of creative destruction?

This report presents key findings from a study of legal services outsourcing and its impact on the legal profession. In order to analyze the ecosystem of key actors in the sector, we have focused first on the ultimate demander of corporate legal services, namely in-house lawyers. The aim of this report is to go beyond anecdotes about novel practices, to present a systematic analysis of what is happening in the in-house legal departments of major corporations and financial institutions.

This study is based on interviews with 52 general counsel in the UK and the United States during May 2010 – January 2011. Interviews explored four key areas: (a) the changing size and shape of the in-house legal department, (b) the changing nature of relationships with law firms, (c) the extent to which legal work has become disaggregated or decomposed in specific areas of work, and (d) how multi-sourcing (including outsourcing and offshoring) decisions are made. We targeted general counsel in major private and public organizations (see Appendix for details).

The report is structured as follows. Chapter 2 analyzes the size and shape of legal departments in the past five years. Chapter 3 examines the changing nature of relationship between in-house and external lawyers. Chapter 4 discusses the perspectives of general counsel on the disaggregation of legal work as a pre-requisite for implementing outsourcing and offshoring. Chapter 5 addresses what lawyers do in a multi-sourcing world. We conclude by discussing key issues for further consideration.



Chapter 2: Size and Shape of the Legal Department

In-house lawyers in major businesses are demanding cost effectiveness in the delivery of legal services. The 2008 financial crisis intensified the general drive to reduce costs including legal costs. In what ways have in-house lawyers reacted to these pressures to do ‘more for less’? This chapter answers this question by analyzing competing logics in three related areas, namely (a) the way the legal function reflects corporate structures, (b) the nature of legal budget control, and (c) the optimization of legal resources internally and externally.

Size of Legal Departments

In our sample, the absolute size of the legal department varies enormously, ranging from a small department with only a couple of lawyers to a globally distributed legal function with over 1000 lawyers at some banks (see Table 1). In the last five years, the majority of organizations have increased the number of in-house lawyers, generally reflecting business growth, either organically or through acquisitions. Sectoral differences are evident in the numbers. In financial services, the legal department grew enormously, reaching a peak in 2007 before the financial crisis led to a contraction in lawyer headcount. There was no such clear-cut impact of the financial crisis on lawyer headcount in other sectors.

Table 1: Size and shape of in-house legal departments in 2010

Sector	Number in sample	Number of in-house lawyers (range)	External to total legal spending (range)
Construction	4	25 - 61	20% - 83%
Manufacturing	2	150 - 314	30%
Energy	7	10 - 650	12% - 57%
Financial services	11	80 - 1068	50% - 77%
ICT	9	2 - 400	27% - 93%
Professional services	2	11 - 12	60%
Public sector	3	n.a.	n.a.
Retailing and wholesale distribution	5	8 - 35	60% - 90%
Utilities	2	n.a.	20%
Other sectors	7	7 - 72	40% - 60%
TOTAL	52	2 - 1068	12% - 93%

Source: Author’s interviews; n.a. = not available.

In a small number of cases, the general counsel managed to reduce the size of the legal department despite significant business growth. At an energy company, the number of lawyers was reduced from



750 to 650 in the past two years, as part of a corporate-wide drive to reduce all costs. Another energy company implemented its policy to create a lean legal function, reducing in-house lawyers from 30 to 12. Similarly, at a construction company, the total legal department headcount went down from 25 to 7 in five years with the creation of a global headquarter legal function.

Shape of Legal Departments

The internal legal department mirrors the corporate structure in some form. At its simplest, a single product firm operating in one country has a functional structure. The structure inevitably becomes more complex with multiple business lines and/or cross-national geographic coverage. With complexity comes a certain degree of freedom in choosing among alternative structures for the in-house legal function.

There is clearly a trade-off in this choice. The advantage of a centralized legal function is that the general counsel is in full control of overseeing all in-house lawyers. However, in-house lawyers may not give the best advice if they are remote from the business context. By contrast, by embedding themselves in business units or country operations, in-house lawyers acquire an intimate knowledge of the corporation for which they work. However, this devolved reporting structure hinders the sharing of best practice and the optimal allocation of legal resources across business units. Some general counsel have devised structural and process mechanisms that minimize this trade-off.

At one end of the spectrum, companies with a focused product or service have a centralized legal department structure, with all in-house lawyers reporting to the general counsel. If a corporation is focused in its product/service line but has an international presence, then it may have a legal department in each country-based or regional operation. In such a structure, only the headquarter-based lawyers have a solid reporting line to the group general counsel, whilst country-based lawyers have a solid reporting line to the country general manager and only a dotted line to the group general counsel. At the other end of the spectrum, large energy companies and financial institutions are typically both global and diversified in product/service lines. Then, the legal department structure tends to mirror the three-dimensional matrix applied to the firm, with geography, product, and function as dimensions.

The matrix is a complex structure that rarely works well with a sole reliance on formal reporting lines. It is therefore not just a matter of whether in-house lawyers have solid or dotted line reporting to the general counsel or business unit head. Typically, the matrix also requires much informal coordination and communication. With such processes in place, a global headquarter legal function can be a 'centre of excellence' providing specialist support (e.g. in litigation, corporate transactions, etc.) to legal departments in diversified business units. However, when a headquarter practice group (e.g. in litigation) lacks connectivity with business unit lawyers, this may lead to uncoordinated actions, or a situation of 'too many hammers in the same machinery', as one general counsel put it.



Legal Budget Control

The shape of the legal function gives some, but not full, insight into how the general counsel controls the legal budget. There is much variation, first in how much budgetary information the headquarter legal function holds, second with respect to the system of accounting for legal fees, and third in what levers are used to keep legal expenses under control.

First, in terms of information, some multi-divisional firms hold information about legal spending of all divisions centrally, whilst others admit to not having a fully functioning central record keeping to date of the total corporate legal spending, including spending by autonomous business units. Many respondents mentioned that they have recently implemented, or are in the process of implementing, an e-billing system which, amongst other things, would enhance the transparency and accuracy of legal spending.

Second, in terms of accounting for legal fees, one approach at one extreme is a tightly controlled central legal budget, with a specific lawyer as a clear budget holder for each line of legal activity. At the other extreme, another approach is to have no central legal budget at all, by embedding all legal fees in business project costs. Many firms fall in-between, with a central legal budget which lawyers control directly (e.g. for major litigation or corporate transaction), and project-based budgets in civil engineering, for example, in which legal fees for contract drafting and negotiation are included.

Third, many respondents have an explicit policy to use in-house resources first before going out-of-house, as it is generally considered cheaper to do so. However, only a small number of general counsel interviewed rely on explicit mechanisms for cost control. In one case, the general counsel of a divisionalized company stated that 'our legal department is a planned economy', pointing to a performance 'dashboard' that the legal department at each operating business unit was required to submit on a monthly basis. At another company, the general counsel introduced a central approval system for legal fees above a certain sum. This led in-house lawyers to think twice about the necessity of putting work out to external lawyers.

Externalizers and Internalizers

Despite entertaining a common aim to contain legal costs, the interviews reveal an enormous variation in how corporate legal departments are attempting to fulfil this objective. One comparative indicator is the percentage of total legal spending on external lawyers, which ranged from 12% to 93% in our sample (see Table 1). Sectoral patterns are evident, with some retailers and high-tech firms relying heavily on external lawyers and financial services firms positioned in mid-range, but variations within sectors point to company-specific legacy and policy on this matter. Four generic types exist in the sample: Externalizers Type 1 and Type 2, Mid-rangers, and Internalizers.

Externalizers (Type 1 and Type 2)

The externalizers – companies that depend on external lawyers for 90%+ of their legal resource needs – fall into two types, and their logic is somewhat different. Externalizers Type 1 do not have an active in-house legal department, relying on external lawyers to act as though they were in-house general counsel. For example, one US retailer did not have an in-house lawyer at all until recently. Another



retailer in the UK has had a small in-house legal department which was often bypassed by the CEO and business managers who went direct to external lawyers for advice. According to the general counsel, 'our legal function was a little bit like an outside law firm dropped in here, and we sort of sat and waited for people round the business to come and talk to us, and then we'd give them some advice and then they'd go away. That was one part of the model. The other part was, we had outside lawyers that were more like in-house counsel.'

Externalizers Type 2 also rely heavily on external legal resources, but the in-house legal department has a proactive stance with respect to managing law firms. Typically, the general counsel hosts an annual conference of major law firms, and encourages lateral communication amongst these law firms in what they call a 'legal community', a 'legal network', or a virtual law firm. These general counsel are adept at balancing collaboration and competition, in order to induce law firms to work effectively and efficiently for the corporate client (see Chapter 3 for details).

Mid-rangers

Financial services firms, including investment banks and commercial banks, are the biggest spenders on big law firms in absolute terms. However, proportionately their reliance on external lawyers relative to internal lawyers is balanced. This might conflate clear patterns in different lines of work, for example, heavier reliance on external lawyers in corporate finance than in sales and trading due to large amounts of complex documentation and the use of syndicates in the former. At the same time, some interviewees indicated that apart from 'big ticket' items such as large litigation cases, internal and external legal work was somewhat fungible. As a general counsel at an investment bank asked rhetorically: 'What has to be done in-house? Nothing! A few years ago, I said to my bosses when we were having a debate about the structure of the legal department. I said we can hire another 200 lawyers and bring more of the work in-house, or we can fire all in-house lawyers and you two can manage all the outside counsel. Those are the two ends of the spectrum. The question to me is where do you want to be in the middle.' However, apart from some consideration for managing the existing capacity and internal lawyers' careers, the general counsel admitted to not being able to 'articulate where on the spectrum we should be'.

Internalizers

The internalizers – with 20% or less reliance on external resources – use a different logic. They have developed a strong in-house legal function that conducts most of the legal work for the corporation. The key advantage lies in in-house lawyers' intimate knowledge of the business. Amongst the internalizers interviewed, a general counsel at an energy company considered heavy reliance on external legal resources as not cost-effective overall. Transacting with many outside counsel, 'constantly keeping them up to speed on what the business was doing', was very expensive. The general counsel devised and implemented a law department strategy that placed importance on 'fit-for-purpose' lawyering, which involved staying very close to internal clients in business operations, and keeping tight control over external legal resources. Pursuing this strategy resulted in only 12% of total legal spending going to external lawyers by 2010, down from 19% in 2005 and 23% in 2000.



Whilst some firms reduced reliance on external lawyers by *increasing* the size of the internal legal department, a small but significant number of firms have done so by cutting back on the size of the internal legal department. On first reading, this is counter-intuitive. Surely, a reduction in internal legal resources would result in shifting more work out to external lawyers. However, in a small number of cases, the general counsel in charge achieved heavier reliance on in-house legal resources at the same time as reducing in-house lawyer headcount (see Table 2 for some extreme examples).

Table 2: Relationship between in-house lawyers and % of legal work done in-house in the last 5 years

	Number of in-house lawyers	% legal work done in-house
Case I	30 → 15	21% → 80%
Case II	750 → 650	48% → 55%
Case III	30 → 15	77% → 88%

Source: Author’s interviews.

This evidence is consistent with the claim that ‘supply creates demand’ for external legal work. In-house lawyers may go outside to get confirmation from external lawyers of what they are doing. A general counsel at a financial institution noted: ‘a result of having more in-house lawyers is that you are creating more external spend. So, the more activity you’re creating through that operating model, the more there is a sort of on-cost of doing external business’. Conversely, a reduction in in-house lawyers can trigger a reduction in the outside legal cost. Through rigorous in-house processes for avoiding or resolving disputes before they became litigation, an energy company reduced its external spending on litigation. Similarly, the same firm reduced its legal cost on patenting by being more disciplined about what went into its intellectual property portfolio. These are instances, not of in-sourcing, but of the elimination of the need for outside counsel.

Summary

With a diverse range of sectors and corporate structures in our sample, apples-to-apples comparisons are not easy and come with many caveats. Moreover, the diversity of practices captured by this study challenges existing studies and surveys that claim to have identified dominant definitive trends or fashions in the legal sector. This study has identified clear patterns in completing principles driving general counsel’s attempts to change the size and shape of legal departments. First, there are four generic types of general counsel: Externalizer Type 1, Externalizer Type 2, Mid-ranger, and Internalizer. Second, of these four, Externalizer Type 2 (proactively managing legal networks) and Internalizer (proactively in-sourcing legal resources) are the ones with the biggest appetite for change. As noted above, Internalizers have taken seriously the following dictum by the management guru Peter Drucker: ‘there is nothing more wasteful than doing more efficiently that which need not be done.’ First and foremost, internalizers have eliminated wasteful supply-induced demand for legal services.

We turn, in the next chapter, to how the nature of relationships between the corporate legal department and external law firms has been changing.



Chapter 3: Convergence, Panels, and Legal Networks

The practice of law is in part based on building and maintaining relationships. Personal rapport remains highly significant particularly for high-end bespoke work in litigation or corporate transactions. Some in-house lawyers therefore stated that instructing a specific lawyer was more important than, or just as important as, retaining specific law firms. Nevertheless, most general counsel in this study said that these relationships are largely institutional, and that working with a smaller number of law firms would be of mutual benefit. Such generic belief, however, disguises subtle differences amongst in-house lawyers in how they think they can balance the use of competitive forces and collaborative commitment to engage law firms.

Panels

To the question 'does your firm have a panel?' some said yes, others said they had informal ones, and yet others said no, revealing a strong dislike for the notion of panels. Why is there such disagreement amongst the general counsel?

Disagreement stems from the fact that the notion of a panel incorporates several characteristics, and the general counsel interviewed have in mind a different mix of these characteristics. Panels may involve some or all of the following:-

- (a) A rigorous process of selection onto the panel with specific criteria such as expertise, market reputation, values and branding
- (b) A periodic review of panel members, leading to some turnover in the membership
- (c) A stable group of preferred suppliers who commit to a long-term relationship
- (d) An element of competition among panel law firms
- (e) Lateral communication amongst suppliers, with the use of knowledge management tools to facilitate this.

Some general counsel put great importance on building long-term relationships (i.e. an emphasis on (c) above). Without such relationship building, law firms are unlikely to develop good knowledge of the client firm. According to one general counsel: 'I've always believed in a panel pledge, on the basis that if you spread your job too thinly, one, people don't have much knowledge of your business, and two, you might save a bob on one deal but I bet you it will come back and haunt you.'

Some other general counsel focused on having a very small number of law firms without calling them panel firms. For example, one general counsel retained five 'chosen partner' law firms, each with a 20 – 30 year-long relationship. He said: 'I don't believe in a panel because our work does not generate the

sort of panel mentality, although occasionally, we might put a few of them in competition’ (revealing a distaste for (d) in the panel characteristics above). Thus, the five ‘chosen partners’ are typically not asked to tender, but are allocated legal work in non-compete areas.

One respondent defined a panel succinctly as ‘a group of interchangeable suppliers with whom you have preferential supply terms.’ Evident in this definition is the inherent tension between competition and collaboration. There are three mechanisms in use – convergence, online bidding, and legal networks – to navigate this tension. A different mix of these mechanisms gives rise to differential incentives for law firms, as elaborated below.

Convergence

An overwhelming majority of general counsel in this study noted a recent trend towards reducing the number of law firms the company instructs. In the last five to ten years, drastic ‘culling’ occurred at some firms (see Table 3). (At the other extreme, one global manufacturing company continued to have as many as 170 law firms on its practice-based panels put together).

Table 3: Number of Law Firms on the Panel

	Five years ago	Now (2010)
Case I	55	14
Case II	60	6
Case III	38	26
Case IV	49	9
Case V	70	20

Source: Author’s interviews.

The general counsel saw obvious advantages in giving larger chunks of legal work to a smaller number of law firms. For example, a financial institution has 15 law firms on a global panel, which includes three magic circle firms. Its general counsel echoed many others interviewed in noting three key benefits of having a panel, namely (a) deeper relationship with panel firms arising from focus, (b) discounted fees for volume work, and (c) ‘freebies’ such as secondees, free advice, seminars and training, and the allocation of good partners and associates for the bank’s legal work. Hence, the panel is a good mechanism for enhancing corporations’ bargaining power vis-à-vis law firms.

Despite these obvious benefits, a minority of general counsel are not convergence fans. There are three problems, in their views. First, there is the problem of diminished local autonomy: convergence requires centralized legal department control, and some GCs felt it politically impossible to take power away from in-house lawyers in divisions and regions. Second, there is the problem of inefficiency: ‘firms that have converged have focused that work on a number of large law firms, and we have found the larger law firms to be what we consider the more inefficient of the bunch’, according to a US energy firm GC. Mid-tier law firms are less costly and often have better connections with local counsel. Third, there



is the problem of false aggregation: ‘when firms focus on a very small number of firms, those firms, in turn go out and hire local counsel anyway. So it looks like it is aggregated, but it truly always is not.’

Online Bidding

Law firms, once they are selected onto a panel, are asked to bid for specific pieces of legal work. Panel structures vary from firm to firm and put restriction on who can bid for what kind of work. Some firms distinguish between a global panel and regional/country panels, whilst others have specialist practice panels. Yet others have a tiered panel, with high-risk high-value work going to a Tier 1 panel of global or national firms and lower-risk lower-value work going to a Tier 2 panel of regional law firms.

In the last several years, some firms (notably financial institutions) have intensified competition among law firms by using online auction for commoditized types of work or discrete pieces of work. At one bank, legal work in small claims and conveyancing is subjected to ‘slice and price’, i.e. disaggregating work into well-defined tasks before each task is put out for bidding. Only firms on the panel are able to participate in the auction. A time window such as a couple of hours is given for an auction.

One valuable outcome of online bidding is significantly lower prices. Whilst this creates short-term gains in price reduction via margin compression, it has not necessarily given incentives for law firms to invest in cost reduction. A general counsel at a financial institution reflected on the pros and cons of online bidding: ‘that’s great today, but I don’t think it particularly gives you an incentive to be creative in the way that you do the work, and the reason for that is it’s a one-off transaction. So I think what the firms do today, particularly in an environment where they are in, they will get to the right price mostly through margin compression. Now, I’m not against margin compression, but there is a limit to margin compression because the law firm says, you know what, I’ll do this at a loss, but they won’t at some point when they get too busy, and the prices will go up.’ Thus, in-house lawyers have not made sufficient progress in devising incentives for law firms to change the way they do their work in the long run.

A US manufacturing company also made some use of reverse auctions¹ for legal matters, but restricted the use to occasions when the firm did not have an incumbent law firm or was dissatisfied with the incumbent firm for whatever reason. Even with this different use of bidding to reach out beyond panel firms, the general counsel noted a disadvantage: ‘we don’t believe in doing them (auctions) for every matter because we think they’re value-destructive, or they are relationship-destructive, and we do value our relationships.’

Because of the downside to online bidding, a few companies with a panel minimize elements of competition among panel firms. One civil engineering firm has only three firms on the panel. According to the general counsel, ‘I don’t let our panel law firms compete against each other. What I mean by that

¹ In an ordinary auction, buyers compete to obtain goods or services, and prices typically increase during the auction. In a reverse auction, sellers compete to obtain business, and prices decrease over time.



is, if I have a piece of work, I don't say to all three of them, "Give me a price." We tend to spread the work around, and we work with each of them individually. We've got good relationships with each of them, and it's a non-confrontational approach.' This general counsel, therefore, relies on competition during a comprehensive panel selection process, but avoids the 'them and us' mentality by treating panel firms as an extension to the in-house legal department.

Legal Networks

At a handful of companies in this study, the general counsel went further to promote collaboration, not just bilaterally with each law firm, but also among the chosen law firms. Lateral collaboration amongst preferred law firms is tricky to craft because they are in potential or real competition to bid each other out. Nevertheless, it is encouraged at a civil engineering company at which 13 law firms, chosen via a rigorous selection process, are brought together as a Legal Network (Page *et al.*, 2007).

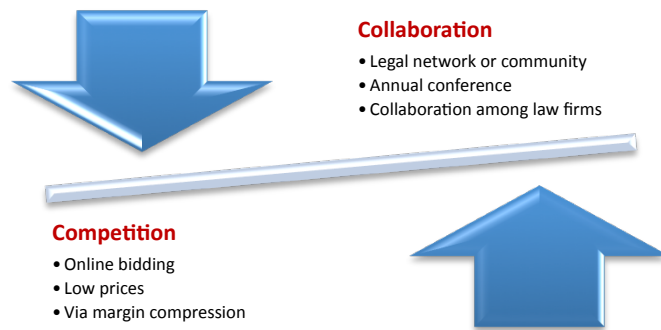
According to its general counsel, 'we do require them to work together, so we disaggregate some work and put certain parts to certain law firms. For instance, we have three or four firms who do Private Finance for us, and we will require them to sit together and work out what is a market position on particular documents. So rather than having one network firm act for this client company and another for the bank, each having a different view on what is a standard parent company guarantee, or what is an appropriate finance model, we have caused them to sit in a room and say, "Here is a document which is acceptable from both perspectives." So when we go into a transaction, we don't have to go through all of the preliminary maneuvering around all those things. We can simply say, okay, all of that is done, and that saves time and saves effort and saves money.'

Similarly, a retailer developed a 'Legal Community' of ten law firms, in order to implement cross-firm communication and collaboration in the interest of the corporate client. These preferred law firms are invited to an annual conference at which the retailer explains the nature of its business and its future strategic direction. The external lawyers at the conference, according to the general counsel, are the virtual law firm he needed. 'If it were one firm, one virtual law firm, what would they be doing? One thing they would be doing is to help each other do better work for us.' This requires overcoming inter-firm rivalry, and it is not a natural instinct for law firms to collaborate in this way. The general counsel said they have to work hard to make firms work together. This idea of a lateral legal network or community, therefore, is a step change from the more traditional bilateral relationship model.

Our last example comes from a US company which has effected lateral collaboration by inviting six panel law firms (which survived a rigorous selection process) to form a case-by-case 'joint venture'. When a new litigation case comes up, one of them is assigned a coordinator role, and it is that firm's job to work closely with the in-house lawyer in charge to involve other law firms in the matter. The general counsel is clear in his aim: 'the critical element in doing it this way is that all of the vendors have to share your philosophy. If they don't share your philosophy and if they're not focused on efficiency, it won't work.'



Figure 1: Balancing Competition and Collaboration among Law Firms



Summary

Regardless of the existence of a formal panel, the general counsel in our study already have, or are shifting towards working with, a small number of law firms. But this trend is shadowed by the need to balance competition and collaboration with law firms (see Figure 1). Some GCs rely predominantly on intensifying competition, even after a panel is selected by using online bidding, whilst others take a two step approach, relying on competitive forces to establish a panel, but then enhancing collaboration by developing ‘legal networks’. None relies on both online bidding *and* legal networks for the same category of legal work, as this mix would create contradictory signals and incentives for law firms. Law firm incentives matter for the long-term sustainability of specific practices. But in-house lawyers have found it challenging to provide carrots and sticks for law firms to find new ways of doing their work differently and more cost effectively. This study did not go into details of various alternatives to hourly billing as incentive mechanisms for law firms.

The next chapter addresses how corporate legal departments are considering ways of making legal work more efficient and effective, involving disaggregation and standardization.



Chapter 4: A Production-line Approach to Legal Work

‘Commoditization’ is a dirty word in legal practice. All lawyers recognize that some parts of what they do are repetitive, routine, and boring. Nevertheless, lawyers consider those legal tasks to be a necessary part of legal work particularly for trainees and junior lawyers, resulting in deeper knowledge and experience for making better professional judgement. However, when corporate clients ask for better value for money, most lawyers begin to see that some of the work could be simplified, standardized, and shifted to less qualified workers in low-cost locations. A nagging worry persists, nevertheless: how can one maintain the quality of work done, the overall custody, and client confidentiality? But not so fast.

This chapter summarizes the findings of this study in an area that is in a state of flux. There is little agreement on terminology – disaggregation, decomposition, unbundling, etc. all uttered interchangeably. Several techniques originating from manufacturing – process mapping, Lean Six Sigma, Just-in-Time, etc. -- fall off the tongue of some enthusiasts intent on transforming the way legal services are delivered, but without a system-wide perspective on what is holding back key actors from jumping on the bandwagon. Despite the existence of a well-articulated five-stage model from bespoke to commoditized legal service delivery (Susskind, 2008), the clock speed for adopting this model appears slow. This study attempts to describe and analyze the state of play – what the interviewed general counsel said and observed – without a teleological vision of the future. In this sense, this study does not judge whether legal services should become more like manufacturing; nor does the study take an optimistic or pessimistic stance on the possibility of change. It attempts, however, to accurately reflect and understand who is implementing what types of change for what reason.

A ‘Production-line Approach’

Ted Levitt was one of the earliest advocates of the ‘production-line approach’ to service in the early 1970s. He argued that services would benefit from drastic improvements in quality and efficiency at the same time if they adopted a manufacturing approach to its activities that substituted technology and systems for people and serendipity (Levitt, 1972). What he had in mind was the key principles of scientific management that Fredrick Taylor articulated in the 1910s, namely the separation of planning from execution, the standardization of products and processes, and the training of workers to carry out tasks. History tells us that mass production based on these principles supplanted craft production due to discontinuous efficiency gains.

The work of lawyers today may be on the cusp of a similar transformation due to digital technology, globalization, and new entrants. Whilst bespoke work continues to exist, legal work may be subjected to treatment similar in nature to that which has been applied to automobile assembly for over a century.



For example, the standardization and templating of legal documents is the legal equivalent of interchangeable and standard components in manufacturing. And why not a just-in-time approach to legal service delivery? In legal services, as in other sectors, the production-line approach requires the following three steps.

1. Disaggregation and standardization: to break down legal work into constituent tasks which are then standardized or modularized
2. Process management: to ensure the smooth flow of process steps and to eliminate waste
3. Project management: to separate planning from execution, to define who does what, and to ensure that milestones and deadlines are met on time

Objections to the Production-line Approach

The general counsel interviewed for this study tended to fall into three groups. First, a small group of enthusiasts demonstrated an enormous appetite to embrace this approach. Second, some sceptics stated that there was nothing new in this approach (that for quite some time, lawyers have been parcelling out work to junior associates and paralegals). Third, the wait-and-see group were happy for others to take a lead, particularly as this approach did not apply to their own area of work.

The adverse consequences of standardized mass production are well known. One does not need to evoke the image of Charlie Chaplin spinning around repetitively tightening nuts and bolts in *Modern Times* to feel how disheartening routine tasks could be. However, unlike in manufacturing which encountered vocal Luddite opposition in its history, the opposing segments of the legal profession are gentle sceptics and passive resisters.

In the legal world, some objections to the production-line approach are common to manufacturing, whilst others are peculiar to legal work. Below is a list of objections gleaned from the interviews.

- (a) Our volume is too low, so we cannot exploit economies of scale (mentioned most frequently)
- (b) Quality would go down with disaggregation
- (c) Legal work has to be holistic to meet clients' need
- (d) Collaboration, iteration, and interaction are inherent in doing legal work
- (e) Over-disaggregating carries the risk of de-motivating lawyers who do not see the whole picture
- (f) Standardization gives lawyers a 'license not to think'
- (g) Lawyers are not trained to think in this way
- (h) Routine tasks, if outsourced or offshored, will undermine training opportunities for junior lawyers
- (i) Upfront costs in technology investment and/or visiting unfamiliar locations (e.g. India) are too high
- (j) Lawyer culture does not fit with disaggregated task delivery
- (k) Law of privilege gets in the way of disaggregation
- (l) Disaggregation, resulting in the use of unqualified non-lawyers, is bad because they do not have the same ethical standard as lawyers



So, what types of legal work are most easily subjected to disaggregation? Who decides how much disaggregation is too much or too little? Is there one best way to break up a piece of legal work into constituent tasks? In order to answer these questions, this study asked general counsel to choose a specific practice area to discuss their achievements and aspirations.

Litigation Tasks

Litigation is often the largest component of external legal expenditure, a component that also fluctuates widely from year to year. For this reason, the general counsel are keen to consider ways of reducing and controlling litigation costs. However, those interviewed varied in their philosophy on how best to tackle this. During the interview, a general counsel was shown a list of litigation tasks (see Figure 2) (see Susskind 2008) which became a basis of discussion.

An initial discussion was whether or not the list made sense, and what might be an optimal degree of disaggregation. It is evident that some general counsel had never considered the way they deal with each litigation matter in this laundry list sort of way. However, once they recognized that the list made generic sense, some started making comments on the possibility of finer disaggregation. Legal research is a good case in point. Generally, many general counsel made a distinction between information gathering (e.g. a fifty state survey in the US) which can be disaggregated easily and may be carried out by junior lawyers or paralegals, and researching legal precedents which require a high level of judgement in context by experienced lawyers. Another example is document review, which may be disaggregated into first-level reviews and further reviews that require professional judgement on what is relevant or privileged.

Figure 2: Litigation tasks



A further point of discussion was who was best placed to do each task. The starting point for this discussion revealed which one of the three approaches a general counsel adopted. First, in what may be called a **craft approach**, the in-house counsel homed in on the importance of Strategy and Tactics, which should be led by the in-house lawyer with close counsel from the lead law firm. Beyond this, however,



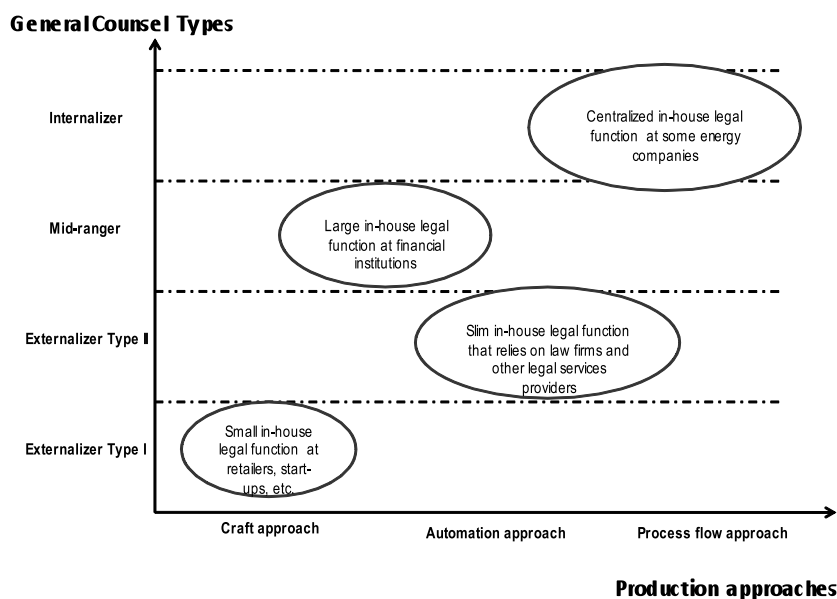
the in-house lawyer delegated the whole matter to the law firm, and expected many of the tasks – be they negotiation or legal research – to be carried out iteratively and collaboratively. Negotiation, for example, was a matter of collaboration between in-house and external lawyers, with a tactical aspect of matching the other side.

Second, in an **automation approach**, the general counsel regarded automating one chunk in the task list – namely litigation support and e-discovery (or e-disclosure) – as the primary focus of efficiency improvement. Starting with computerizing the collection and hosting of data, the general counsel focused his attention on replacing humans with machines to undertake rule-based data processing (e.g. de-duplicating, coding, etc.), moving eventually onto pattern recognition in first-level document review.

Third, in a **process flow approach**, the general counsel had established processes and procedures, in some cases using process mapping, to ensure the smooth flow of legal tasks from the start to the end of a case. This approach forces in-house lawyers to clearly scope out each task, and to define who is going to do what at the planning stage. An automation approach may be combined with a process flow approach, but some corporations adopted an automation approach without a process flow approach.

One of the intriguing issues in this study is how these approaches relate to the general counsel’s internalization vs externalization tendencies (see Chapter 2). Internalizers amongst the interviewed tended to be most systematic about adopting the process flow approach, eliminating waste in the whole matter by taking a lead in disaggregating and in-sourcing litigation support and/or document review (see Figure 3). Externalizers Type 2 exercised their voice to induce law firms to take a lead; one general counsel told law firms “you’d better unbundle, or else we’ll unbundle for you.”

Figure 3: Schematic association between general counsel type and production approach

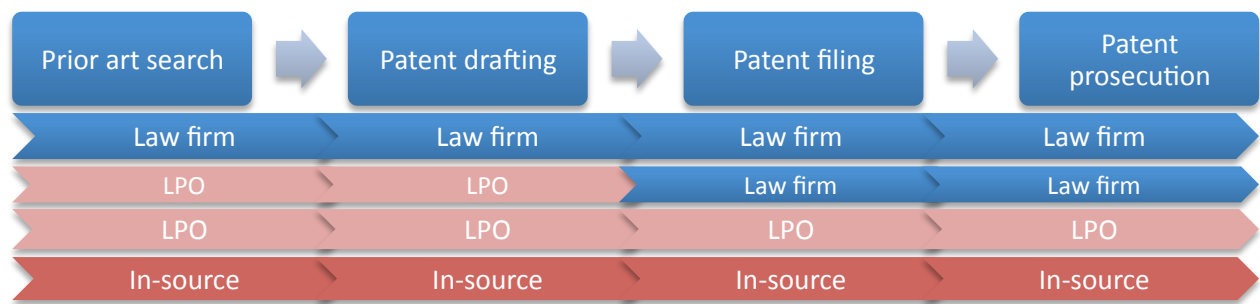


Intellectual Property Tasks: a Case Study

Patent filing and prosecution was another area mentioned frequently by interviewees. All three approaches were detected as in the case of litigation. In a craft approach, the general counsel continues to use law firms to manage the whole matter, starting from prior art search to patent prosecution (see Figure 4). Corporations in the ICT sector were at the forefront in adopting an automation approach, investing in patenting software so as to enable self-service by inventors to use electronic filing.

As before, Internalizers have gone furthest in implementing a process flow approach. This has led not only to the disaggregation of patenting tasks, but also to the use of multi-sourcing, that is, the use of multiple types of suppliers via in-sourcing, offshoring, de-lawyering, etc. (Susskind 2008, p.47). As shown in Figure 3 (last line), the Internalizers tended to in-source most or all stages of patenting by hiring more patent agents who carry out tasks that used to be done by patent attorneys in law firms. Alternatively, Externalizers Type 2 disaggregated some tasks – prior art search, patent drafting – which they sourced from legal process outsourcing (LPO) providers directly or indirectly via law firms.

Figure 4: Patenting tasks



Summary

The corporate cost pressure to do ‘more for less’ has led many general counsel in this study to consider (and in some cases implement) a production-line approach to legal service delivery. In totality, this approach requires three steps: not just disaggregation and standardization, but also process management and project management. The approach therefore requires a system-wide end-to-end perspective. However, the majority of general counsel found a variety of reasons – lack of scale, lawyers’ mentality, lack of time, expensive upfront cost, etc. – to reject or delay wholesale adoption. Nevertheless, some general counsel found tactical advantage in making significant efficiency gains by relying primarily on the automation and digitization of specific tasks. Moreover, a handful of general counsel, led by Internalizers, have appointed Directors of Legal Operations to take a lead in implementing the production-line approach.

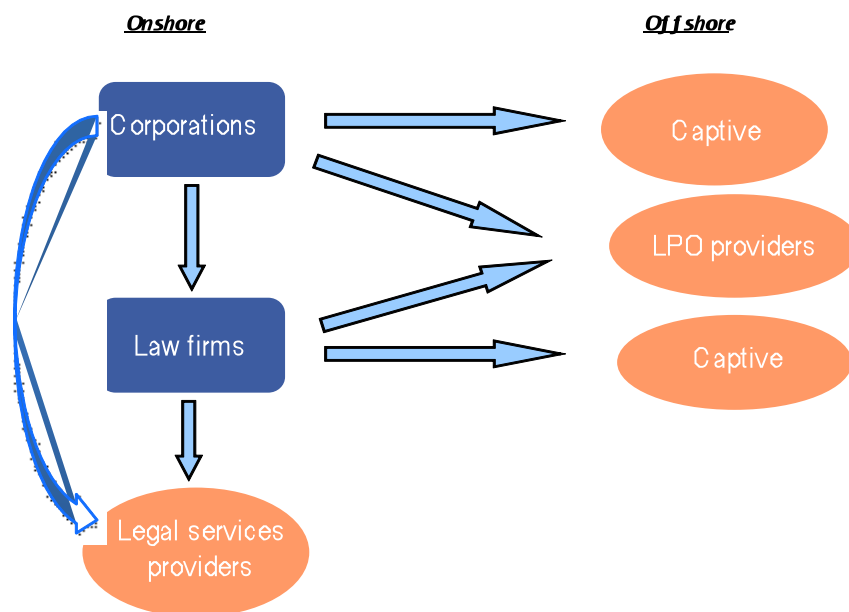
The next chapter turns to the issue of multi-sourcing, the criteria used to make a decision on who does what tasks once legal work is disaggregated, and the resulting patterns in what lawyers do in relation to non-lawyers.



Chapter 5: What Lawyers Do in a World of Multi-sourcing

Once legal work is disaggregated into constituent tasks, the in-house legal department must consider the most efficient and effective way of sourcing each task. In the last several years, the portfolio of possible sources of legal service has expanded – hence the notion of multi-sourcing – as new providers and new locations have become available. Up until recently, the only thick pipeline of legal advisory work that mattered was the one connecting the corporation to the law firm. Whilst this will continue to be important, the corporation now has a diverse set of sourcing options, ranging from (i) offshoring a captive in-house legal department (as GE had done); (ii) relying on law firms to set up a captive low-cost centre (as Clifford Chance or Baker & McKenzie have done); (iii) sourcing from contract lawyers on a project-by-project basis; to (iv) going direct to new legal services providers that have a global presence (as Rio Tinto did with CPA Global) (see Figure 5). Despite these emergent models for sourcing legal services, the offshore legal process outsourcing (LPO) sector remains a mere drop in the ocean, around \$500 million in revenue, or 0.1% of the worldwide legal market worth around \$500 billion in 2010 (Datamonitor, 2010).

Figure 5: Global value chain in legal services



1



How significant will the phenomenon of multi-sourcing be in the future? In particular, how much value might migrate from transactions between corporate clients and law firms to other parts of the global value chain? The answer depends on who is making multi-sourcing decisions using what criteria. This chapter discusses (a) labour arbitrage vs process efficiency as sourcing criteria; (b) de-lawyering; and (c) who does project management. The chapter concludes by drawing implications for what lawyers do in a multi-sourcing world.

Sourcing Criteria: Labour Arbitrage vs Process Efficiency

In our study, only a small minority of general counsel actively set out to source from remote offshore locations, most notably India. The key reasons mirrored the list of objections to the production-line approach noted in the previous chapter. By contrast, those who enthusiastically endorsed new low-cost locations, be they nearshore (e.g. Belfast for London-based financial institutions and law firms) or offshore (e.g. India, South Africa, the Philippines, etc.), divided into two camps. The first camp is primarily after labour cost arbitrage and nothing much else. The general counsel may look to contract lawyers on demand or foreign lawyers familiar with English or US law to conduct legal work in a manner that is no different from if it were carried out by lawyers onshore.

The other camp expects to obtain much more than merely lower labour rates. In these cases, the general counsel is intent on attacking both the denominator (i.e. productivity) and the numerator (wage rate) in the unit labour cost equation. At Greenfield sites, some financial institutions sought greater efficiency in processing derivatives documentation, for example, not only by templating and standardizing documents, but also by investing in software technology, improving the process flow of work, and exploiting economies of scale. The choice between captive and outsourced offshoring, then, depends in part on the general counsel's views on who has the best package of capabilities in process management and project management. Thus, a 'new location' is often a code for accelerating the implementation of new modes of working, not a mere attempt at seeking temporary labour cost arbitrage.

De-lawyering in Legal Product Lifecycle

A key aspect of taking cost out of legal work – combining process improvements and billable hour reduction – derives from 'de-lawyering' i.e. the use of non-lawyers to do work that had been done by fully qualified lawyers. As noted in Chapter 4, in-house lawyers disaggregated patenting tasks in order to use patent agents to do work previously done by patent attorneys; similarly, and paralegals were employed to do simple legal research previously done by junior lawyers. Perhaps the most significant use of non-lawyers has occurred in contract documentation in a variety of sectors.

In civil engineering, for example, in-house lawyers push routine contract documentation work to engineers who lead projects. According to one general counsel, 'we look at the contract if it's non-standard and comment on that. But most of the issues are not legal issues; they are around fees and scope. Those are the issues engineers can deal with. So what we want to do is to give engineers



confidence, and train them up to look for issues that matter.’ Thus, engineers are encouraged to negotiate contracts and deal with clients directly without a lawyer involvement.

In financial services, also, documentation work is pushed down to non-lawyers working in the relevant business departments. According to one general counsel, ‘I’d like to get into the business of templating things and give them to the business function. ... Let’s be honest. Lawyers are not good at providing either systems or process or handling volume.’ Derivatives documentation is a good case in point, as the sheer volume of work often creates bottlenecks in workflow. It is now common practice for non-lawyers – called document analysts or documentation specialists – to handle derivatives documentation, often at captive (i.e. in-house) offshore or nearshore centres. Investment banks are in the business of creating new financial products that are initially complex, low volume and high margin. But they commoditize them and turn them into high volume, lower margin work. Law firms may be involved in early stages, but when the work becomes a repeat exercise, banks have an incentive to internalize them eventually. De-lawyering, therefore, appears to be a cyclical trend, most evident during the mature stage of legal product lifecycles.

Who Manages the Reassembly?

Multi-sourcing – including outsourcing and offshoring – requires someone to take a lead in supervising and managing a variety of providers. Just as making an aeroplane requires systems integration by the aircraft manufacturer to manage the final assembly of engines, wings, and fuselage made by different suppliers, we would expect an ‘architect’ to manage the integration – final assembly – of disaggregated legal tasks so the final ‘product’ works and is delivered seamlessly to the client. But which entity should assume this architecting role? Should it be the law firm or the in-house legal department? The answer to that question is almost the Holy Grail to gauging the future shape of legal services markets. The picture that emerges from this study is far from clear cut.

When asked if their law firms use outsourcing or offshoring, some general counsel responded that they did not know, and that it was up to the law firms to decide. A general counsel at a bank stated: ‘our preference is to deal directly with law firms and for them to outsource to the alternative providers if they choose in order to drive their costs down to us. We want those firms to be responsible for managing that. I am not keen to deal with people in other jurisdictions who may not have the same requirement as us in confidentiality and security of information. We’d like to place the onus on the major law firms we deal with to ascertain that for us.’

An alternative approach, adopted by a small number of general counsel, was to instruct law firms to disaggregate and to use a specific LPO provider for work chunked out, such as data room management, e-discovery (e-disclosure) work, and contract review. The in-house department would have a direct contractual relationship with such a provider. Delegating decisions on what to outsource/offshore to law firms would not work because ‘you effectively run the risk of delegating the control of what needs to be done, which inevitably ends up being more expensive’, according to a general counsel.



Several general counsel expressed the view that had law firms been willing and able to take an initiative in managing legal projects, they would rather not have to step in. However, even with such a competency gap in project management skills amongst law firms, these in-house lawyers felt ambivalent about investing in in-house capability. At least two future scenarios are possible here. In one scenario, law firms will retain a thick pipeline of legal work if they are able to take a lead in filling the competency gap in project management. In an alternative scenario, law firms might be bypassed – disintermediated – as the general counsel invests in project management capability and engages aggressively in multi-sourcing, including trading directly with new types of legal services providers. These new entrants bring new financial capital and professional talent into the sector. Thus, the future shape of legal services value chain depends heavily on the role the general counsel wishes to play in project management.

What Do General Counsel Do?

The general counsel continues to navigate a fine line between being a lawyer first and foremost with its professional ethics on the one hand, and being a business person offering legal advice in context without selling one's soul to commercial enterprises on the other. Over time, the power base of in-house lawyers appears to have enhanced, due not only to the short-term impact of the financial crisis, but also to longer-term trends. Perhaps the most significant of these trends is the increasing importance placed by corporate executives in legally astute firms on the general counsel as joint risk managers (Bagley, 2008). Not only can the general counsel front-load legal inputs to pre-empt disputes, thus reducing litigation costs significantly. They can also alert CEOs to potential risks arising from likely government investigations in a tougher regulatory enforcement environment. The general counsel's intimate knowledge of the business is indispensable, and they consider this an advantage in offering better legal advice. In the words of one general counsel, 'I'm a business person who happens to be a lawyer, a business partner who brings legal background to business problems.' Nearly all the general counsel interviewed regularly rub shoulders with the CEO by dint of having a seat on the corporate executive committee.

In this context, how important is the efficient delivery and multi-sourcing of legal services in the general counsel's priority list? Opinions were split on this score. At one extreme, commoditization – disaggregation and standardization – is regarded as the stuff for legal operations directors with support from legal technologists. The general counsel's primary job is to contribute to corporate strategy and to manage legal risk. As such, the downside risk of messing up a litigation case by cutting corners is too huge compared to the marginal benefit arising from cost savings. Thus, however powerful the general counsel might be, he is highly risk averse, and cost becomes a secondary concern to obtaining appropriate advice and support. 'No body ever got fired for hiring IBM', quipped one respondent. In this view, unless there is a supply side revolution, rearranging the legal services market would remain 'a game of inches', a tactical game rather than a strategic game.

At the other extreme, the general counsel considers his own role to be the guardian of the legal process architecture in his organization. Such a GC spends little time being a lawyer, exercising legal judgements



only in extreme cases, whilst delegating much of the day-to-day legal advisory work to other in-house lawyers in his department. What is more 'strategic' is the formulation of a legal strategy, involving the management of performance in the legal department, the proactive and pre-emptive legal inputs into the business, and the management of outside relationships, etc. all with a view to enhancing the value added of the legal department to the business. In this view, the efficient multi-sourcing of legal services is part and parcel of an effective legal process architecture.

Summary

Multi-sourcing – the use of multiple sources of legal service delivery – is likely to change the contour of global value chains in legal services. However, how much value might migrate from transactions between corporate clients and law firms to other parts of the value chain depends on a number of factors. This chapter demonstrated that we are likely to see greater value migration away from the traditional corporate client – law firm transactions, (a) the more the motive for offshoring and near-shoring goes beyond mere labour cost arbitrage to the implementation of a production-line approach, (b) the more lead is taken by the in-house legal function in project management and in establishing direct contractual relationships with LPO providers, and (c) the higher up the priority list the general counsel places the issue of efficient legal service delivery.

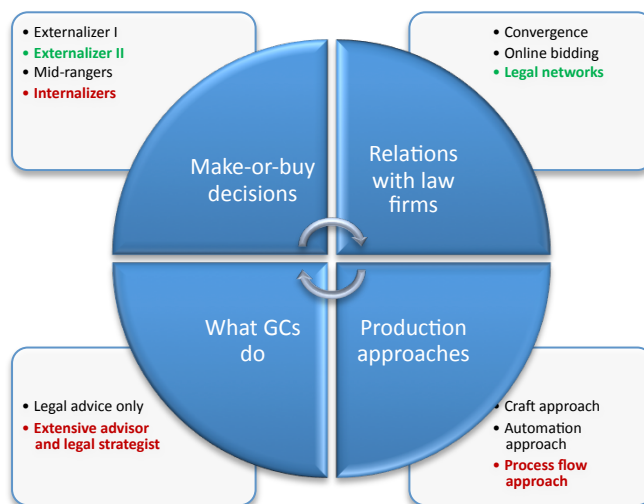
The general counsel is a business partner in corporate top management teams. This study found that beyond this rhetoric, some GCs believe that cost-cutting efficiency should not be a direct concern and should be delegated to managers of legal operations and legal technology. By contrast, a small number of GCs believe in the central importance of being a chief 'legal architect' whose task is to add value to the core business of the corporation or financial institution, by embedding process and project management in the implementation of a legal strategy.



Conclusions

This report discussed what general counsel do in relation to the corporation they work for (Chapter 5), in implementing efficiency drives (Chapter 4), balancing competition and collaboration with law firms (Chapter 3), and managing the make-or-buy decisions (Chapter 2). In Chapter 2, we identified four types of general counsel with respect to their make-or-buy decisions, namely Externalizer Type I, Externalizer Type II, Mid-ranger, and Internalizer. Chapter 3 considered three tools – convergence, online bidding, and legal networks – put to use by general counsel to improve relations with law firms. Chapter 4, in elaborating the production-line approach to legal services delivery, identified three approaches in practice – namely, craft, automation, and process flow approaches.

Figure 6: Clustering of practices



Whilst much of the practices gleaned from the interviews are in a state of flux and yet to be implemented, the study highlights some practices that tend to cluster more strongly than others. There are at least two clusters of practices that GCs are using to drive change, although these may not be the only clusters that work well.

The first cluster (see green legends in Figure 6) concerns Externalizers Type II, who have committed to rely heavily on law firms. Consequently, the main locus of action is to improve the multilateral links amongst the chosen law firms as much as the bilateral relationship with each law firm. Externalizers Type II also expect law firms to take a lead in implementing multi-sourcing and components of the production-line approach to legal service delivery including project management.



The second cluster (see red legends in Figure 6) concerns Internalizers. They rely heavily on internal legal resources, are most systematic in implementing the production-line approach, and view themselves as legal strategists in charge of managing legal projects and process flows.

This study attempted to provide a systematic analysis of current trends and possible future directions in legal services. We conclude by summarizing a set of key factors that will influence who drives power in legal service global value chains in the future.

It is often argued that corporate clients are becoming a force for change in legal services. However, the general counsel's power to drive change in a sustainable manner depends on the sources of power. The most temporary of GC power lies in the buyer's market during the post-financial crisis recession. Much of the bargaining power resulting from the economic climate is likely to erode when the economy picks up. By contrast, the general counsel will remain a more sustainable force for change if they proactively invest in new capabilities such as project management, as Internalizer GCs are doing. So, law firms, beware of Internalizers amongst the general counsel. However, GCs with a power base in corporate managerial hierarchy may not necessarily regard efficient legal service delivery on a strategic par with legal risk management. If such GCs dominate the in-house legal function, power does not equate to an appetite for change. It is, therefore, equally possible that we are heading for a supply side revolution with new entrants – legal services providers – driving discrete and disruptive changes in the way legal services are delivered.



Afterword: The Future for General Counsel

Richard Susskind

It was fascinating to be in regular dialogue with Professor Sako during the project discussed in this report. Rarely have I had the chance to hold in-depth discussions about the legal market with someone who is not a lawyer. And here is one of the main contributions that Professor Sako makes – she does not have the limited perspective of a practising or academic lawyer, she has no legal axe to grind, no legal business to sustain or disrupt, nor any legal overlord to appease. Rather, she brings the expertise and experience of an economist and management theorist, someone who understands economic forces, business strategy, industry upheaval, and organizational change. And she applies this knowledge to the law, as part of her growing interest in the professions more generally. The legal world should warmly welcome the objective insights of an expert outsider who is looking afresh at its marketplace.

Methodologically, this report is different from much that is held out as research into the legal industry. I had anticipated a document that was brimming with data, diagrams, tables, and percentages; and maybe even a formula or two. But I now see this would be pseudo-science. This research shows us that General Counsel are a grouping of lawyers that are too diverse in the nature of their work, in the size of their teams and broader organizations, in their industries and markets, and in their geographical presence, for it to be sound to claim that x% of GCs believe this or Y% prefer that. These statistical claims are the stuff of the transient PR-based research that surfaces every few weeks whose aim is to secure a headline in the trade press. I see more clearly now that these superficially plausible pie charts and bar graphs do not in fact improve our understanding.

Trends

What the Oxford research instead provides is a snapshot of the central trends in the buyer's side of the legal market. Its scope is limited, though, because the focus is on the in-house functions of very large organizations. As the list in the Appendix shows, most of the businesses involved in the study are major household names (it is unusual in itself, incidentally, in the world of research into the legal market to be able to see who has actually been consulted).



Within this sector of the market, some of the trends are quite clear: GCs want to secure 'more for less', more legal service at less cost; and most are wrestling, but doing so tentatively, with various new ways of sourcing legal services.

Two divides also emerge. First, there is a stark contrast between the conservatives who see the future as a mildly finessed version of the past; and the radicals, who anticipate and are implementing major change in the way that legal services are delivered. Second, there is the split between those GCs who argue that external law firms are best motivated by urging them to compete with one another and those who believe that law firms will be individually and collectively more productive and efficient if encouraged to collaborate.

Issues

My own interest has always been in change. I am not a dispassionate observer. I believe lawyers must modernize - to survive in law firms and to meet the needs of clients. One issue that currently interests me is who these agents of change might be. From the transcripts of Professor's Sako's interviews, it is clear that some GCs think they themselves should drive innovation; but a larger proportion think that law firms should be leading the way. Many law firms seem hesitant about this. Yet, in the history of industry and commerce, customers or clients have rarely redefined the services they receive or the markets of which they are part. That is the job of the provider.

Law firms, generally, have always been reluctant to change. As I like to point out, or did at least until 2007, it is hard to convince a room-full of millionaires that their business model is broken. And it is tougher still to compel managing partners to innovate radically when they have only two years or so left in post; their understandable inclination, rather, is to squeeze more out of the existing model and keep the figures looking rosy. In the long run, this thinking will be to the detriment of law firms.

But, of course, the providers in the legal market are no longer just the law firms. As this report shows, there are new players in the legal game, not least the legal process outsourcers. I believe we will also see the resurgence into the legal sector of the large accounting firms, as well alternative business structures fuelled by private equity. These new providers tend to have much greater appetite for rethinking legal services than conventional law firms. The competition is stiffening. In the end, then, the agents of change may not be lawyers.

Another issue that flows from this report concerns the discipline that I call 'legal process analysis'. This is the job of analyzing legal requirements (of an individual matter or of an entire business) and specifying the most efficient way of sourcing the legal work, consistent with the level of quality needed. Following the terminology of one of the interviewees, the question here is - who should the architects (the process analysts) be? I worry about those GCs who immediately see this as a role for law firms. Surely, shareholders and directors of business can reasonably expect that their own in-house lawyers are the people ideally placed to assess legal problems and identify the best way to sort them out.



The evolution of the legal market

From this report and my own research, I now see that the mainstream legal market is likely to evolve in three phases. The first, extending from 2007 to 2013 or so, is the period during which most law firms and GCs will seek to maintain the status quo. GCs will resist fundamental change of their own departments and try to meet the 'more for less' challenge by inviting law firms to charge much less. In turn, law firms will be similarly reluctant to change radically and so will propose alternative fee arrangements. But these deals will not give GCs the savings they need and so there will be a shift to a second phase, from about 2013 to 2016, when GCs will dramatically re-engineer their legal functions; and law firms will move from pricing differently to working differently. Both will embrace legal process outsourcing, off-shoring, de-lawyering, and agency lawyers. The endgame, though, will not be about labour arbitrage. I predict that the third phase, from 2016 onwards, will involve great uptake of information technology across the profession, such as automated production of documents and intelligent e-discovery systems – these are applications that will be staggeringly less costly than even the lowest paid lawyers.

Strategy for GCs

In practical terms, how should GCs prepare for this future? I am often asked this question by in-house lawyers in the following terms – what should our strategy be? I cannot answer that query in generic terms. But I can suggest that there are four broad types of strategy for GCs. They differ in their scope and ambition.

The first strategic approach is to concentrate largely on external law firms and drive their prices down. This will be the preferred method of Professor Sako's 'externalizers'. The second approach, better suited to the 'internalizers', is to focus instead on reshaping the in-house department. Third, is simultaneously to review internal and external capabilities and to seek to streamline both. The fourth approach is the most ambitious – it is to start with a blank sheet of paper, to forget about current resources (in-house and outside) and instead to undertake a comprehensive legal needs analysis for the business. Once these requirements have been identified, the task then is, dispassionately, to identify how best to resource the full set of needs; drawing not just on conventional lawyers but on the new legal providers too.

This final strategy, in my view, is the one that will deliver the most cost-effective and responsive legal services for large businesses in the future.



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About the Authors

Mari Sako is Professor of Management Studies at Said Business School and Professorial Fellow at New College, University of Oxford. After reading Philosophy, Politics, and Economics at Oxford, she completed an MSc in Economics at London School of Economics (LSE), an MA in Economics at the Johns Hopkins University, USA, and a PhD in Economics at London University. Before taking up her current position, she taught at LSE's Industrial Relations Department for ten years. She was also a visiting scholar at Kyoto University Department of Economics, Tokyo University Institute of Social Research, RIETI (Research Institute of the Ministry of Economics, Trade and Industry in Tokyo), Ecole Polytechnique, Paris, and MIT Sloan School of Management. Her research focuses on the connections between global strategy, comparative business systems, and labour markets. Publications include *How the Japanese Learn to Work* (with Ronald Dore) (1989), *Prices, Quality and Trust* (1992), *Japanese Labour and Management in Transition* (with Hiroki Sako) (1997), *Are Skills the Answer?* (with Colin Crouch and David Finegold) (1999), and *Shifting Boundaries of the Firm* (2006). She was a principal researcher for the MIT International Motor Vehicle Program (IMVP) during 1993-2006, working on modularisation, outsourcing, and supplier parks in the global automotive industry. She is also a Senior Fellow of the ESRC-EPSRC Advanced Institute of Management in Britain. More recently, as a member of the Novak Druce Centre for Professional Services at Said Business School, she has been researching about the globalization of law firms, the outsourcing and offshoring of professional services and their impact on the professions.

Richard Susskind OBE is Visiting Professor in Internet Studies at the Oxford Internet Institute at Oxford University and Emeritus Law Professor at Gresham College, London. He is IT Adviser to the Lord Chief Justice of England and Wales, President of the Society of Computers and Law, and the author of numerous books, including *The End of Lawyers?* (Oxford University Press, 2008).



Appendix: Research Methodology

Fifty-two GCs were interviewed, 36 in the UK and 16 in the US. Interviews typically lasted one hour. Where permission was sought and granted, interviews were recorded. In many cases, interviewees also provided further data by email, and internal policy documents (and an authored book on one occasion) at the interview.

Table A1: List of Interviewed Organizations

Alliance Boots	HP
AMEC	HSBC
Archon Group	Infineum
ARUP	ISS
BAE Systems	ITV
Barclays	M&S
Barclays Capital	Medtronic
BAT	Ministry of Justice, UK
Boston Consulting Group	Qwest
Bechtel	Royal Bank of Canada
BP	Royal Bank of Scotland
BT	Royal Dutch Shell
BUPA	Sainsburys
Carillion	Sigma Aldrich
Centerpoint Energy	Solicitor General Counsel, UK
Christies	Sony Ericsson
Cisco Systems	Southwest Airlines
CITI	State Street Bank
Conoco Phillips	Team AOL
Datacert	Tesco
Deutsche Bank	Thomas Miller
Dollar Tree	UK Experian
Financial Services Authority	United Utilities
FMC Technologies	Vodafone
Goldman Sachs	Williams Corporation
Hanson Ltd	Yahoo

