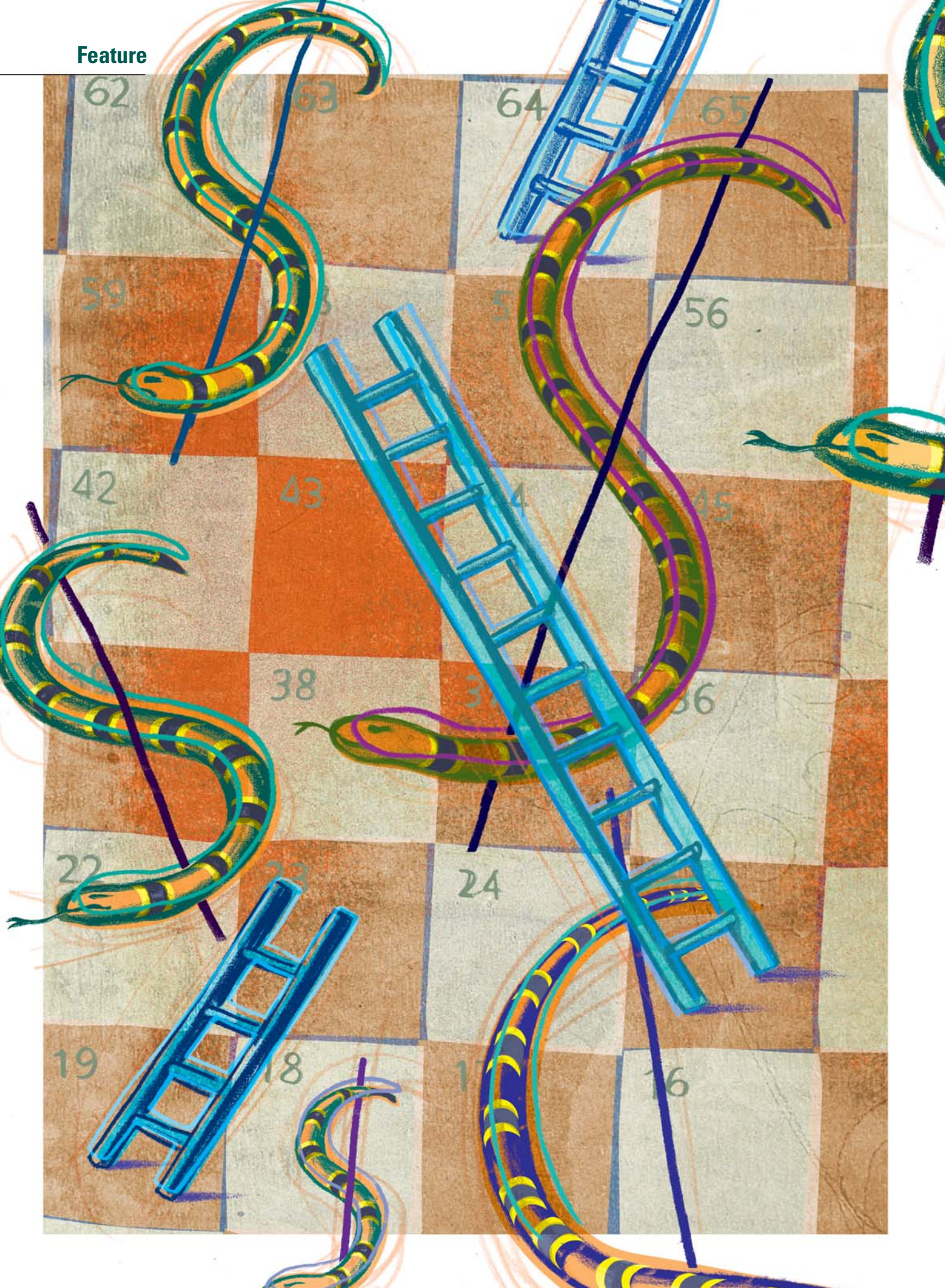
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Gaming a Broken System?

Real change to legal services requires a new focus.

The chorus of change sings on. At national and international legal conferences, I hear a babel of opinions about "the system being broken," about the adversarial relationship between client and counsel fueled by the economic crisis.

Many voices, mine among them, highlight what to us seem inevitable trends: that provision of legal services is undergoing major and permanent change; that corporate counsel will take a stronger role in driving the relationship with their outside counsel as they themselves face extreme cost reduction pressures from their management; that the quality and value of legal services will be measured in new ways; that alternative fee arrangements will steadily supplant the billable hour as the basic unit of exchange.

So, are all these "paradigm shifts" really happening? Are they fundamental trends with lasting significance? Or, as some law firm managing partners insist, are they passing fads that strut their moment upon the stage before the legal profession returns to the same old same old? They say the "system" isn't really changing and doesn't really need to change. All the players are just responding to extraordinary and temporary external events, and pretty soon "everything will return to normal."

Are these the voices of calm reason — or the muffled head-in-the-sand cries of conservatives or vested interests intent on preserving the status quo? Over the last several years, I've watched the "negotiation wars" carefully from ground level, comparing what people seem to be *doing* with what they are *saying*. My observations channel Mark Twain's observation that a lot of people are talking about the weather, but nobody is doing anything about it, resulting in some thunderheads but little real change in climate so far. Some prime examples:

- While there are certainly innovators and first-adopters among CLOs, notably Jeff Carr at FMC Technologies, Mark Chandler at Cisco Systems, and Rio Tinto as they announce $100 million in offshoring legal work, there

By Pamela Woldow
Illustration: Kevin Ghiglioni, 121 Art Inc.

appears to be little change in the majority of corporate counsels' approaches to engaging, managing and pricing legal services.

- In Altman Weil's 2009 Chief Legal Officer Survey, a stunning 75 per cent of CLOs pointed the no-change finger at their law firms, charging that they show little interest in changing their delivery model. Some see this as a dramatic vote of no-confidence in the competency of law firms as innovative change agents, as well as evidence that inertia continues to rule the client-counsel relationship.

- Many CLOs, while bemoaning the intense pressure to reduce costs, tell me that their most frequently used approaches — asking for discounted billable rates and instituting draconian systems to audit legal bills — are proving ineffective in achieving real savings.

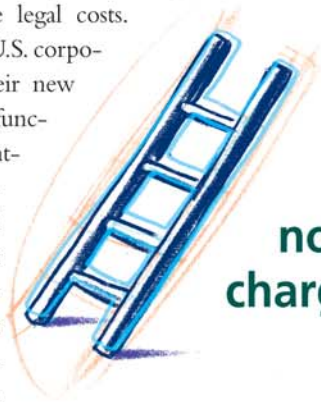
These examples suggest that it's fair to ask, "So, who *isn't* driving change — and why aren't they driving it?" Some attribute it to the reluctance of in-house lawyers to value the worth of law firm services by any other standard than the amount of time spent working on them. While they understand the need to link value to cost, they are as inexperienced as law firms in developing alternative approaches, holding fast to approaches they know well and have used for decades. Both in-house and outside counsel note how hard it seems to be for GCs to break long-standing habits, how readily they relapse into conventional wisdom. Many succumb to "magical thinking" cost-control tactics rooted to the billable hour.

Here's another theory for GCs' and law firms' reluctance to embrace change: both gain something by gaming the existing system. Both corporate counsel and law firm managers tell me that it's not hard to negotiate across-the-board reductions of, say, 15 per cent in hourly rates. When I recently asked the managing partner of one of the 10 largest U.S. "Big Law" firms whether discounted billable hour rates led to reduced revenues for his firm, he roared with delight: "We LOVE discounted billable rates, because the more clients increase the amount of work they send us in response to 'lower' rates, the more apparent savings that they can show off to their management. We trade off a little margin, but we get it back in volume. Net-net, our revenues increase and the overall legal spend actually goes up. But the CLO can wave around a spreadsheet showing these 'actual' savings."

But that single tactic is unlikely to be enough to keep corporate management off the CLOs' backs. If a company's revenues plummet 35-40 per cent over the last quarter, you can bet the shareholders lean on the C-suite executives and line managers to do *everything* they can to reduce costs. By analogy, isn't it fair to ask CLOs to go beyond rate discounts and look at all possible approaches for curbing legal spend: convergence programs utilizing smaller or out-of-region firms with better rates, requests for

proposals, offshoring legal work, and various forms of alternative fee arrangements? As many GCs have said, reducing legal spend goes right to the company's bottom line.

But effecting real change just does not seem to be front and centre. I recently moderated a panel of corporate counsel discussing how they manage legal costs. Two panelists from major U.S. corporations proudly touted their new internal legal bill auditing functions, complete with dedicated auditing staff, sophisticated new software and fierce determination to cut the fat from each and every legal bill. Both said that their specialized lawyer-auditors were expected to cut total legal bills by about 10 per cent every month. Whenever they fail to meet this quota, an unpleasant "conversation" takes place. At one company, bonuses are predicated in part on consistent bill-whacking.



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Bill-whacking poses a number of problems, not the least of which is that it doesn't really solve the underlying cost problem. Audits take place post hoc and are a fundamentally antagonistic exercise that rely, month after month, in accusing outside counsel of padding bills. This approach not only requires an additional expenditure of corporate time, money and resources, it has a predictable chilling effect on the trust relationship between counsel and client. Imagine how warmly law firm leaders respond, month after month, to demands to remit or write off significant amounts.

Moreover, it is all too easy for *both* sides to game this system. If you know your client is required to cut bills every month (and that his/her personal bonus depends on lopping off that monthly 10 per cent), wouldn't you simply tack a "sacrificial surplus" on every month? Couldn't you then graciously agree to monthly bill reduction as a way to "keep everybody happy?"

More than a decade ago, the former general counsel of Elf Atochem, and a former Saul Ewing partner thought they saw a common sense solution to the absurdities of the post-hoc audit game. They created a consultancy to serve as "buyers' agents" to

On connaît la chanson

Une panoplie d´opinions circulent dans des conférences légales nationales et internationales sur le « système qui ne fonctionne plus » et sur la relation entre client et conseiller légal qui se trouve envenimée par la crise économique. Il est temps de trouver des solutions, écrit Pamela Woldow.

Plusieurs personnes, incluant moi, constatent un certain nombre de tendances inévitables : d'abord, que les conseillers juridiques en entreprise occuperont de plus en plus d'espace dans les relations avec les avocats externes, tandis que les pressions s'accentuent pour réduire les coûts de leurs prestations; ensuite, que la qualité et la valeur de services légaux sera mesurée de nouvelles manières; et enfin, que des arrangements alternatifs de rémunération remplaceront graduellement le système des heures facturables.

Or, selon mon expérience, il semblerait que, suivant les paroles de Mark Twain, beaucoup parlent de la température, mais la plupart laissent aux autres le soin d'y changer quoi que ce soit. Mais pourquoi dont? Selon certains, cela peut s'expliquer par une certaine difficulté à trouver un juste milieu pour la rémunération de services légaux.

Tandis que les conseillers internes comprennent l'importance de faire en sorte que les coûts reflètent la valeur des services, ils sont aussi inconfortables que les firmes qu'ils embauchent pour évaluer la valeur de ces services, autrement que par le nombre d'heures travaillées.

Des pistes de solutions ont déjà été explorées. C'est le cas de la réduction du coût des services juridiques externes par un pourcentage préétabli. Certaines entreprises favorisent plutôt la vérification et l'audit des factures. Or, la réduction proportionnelle des coûts engendrent souvent un volume plus élevé d'impartition, et elle n'est pas nécessairement susceptible de faire économiser suffisamment d'argent à l'entreprise. L'audit des factures, d'un autre côté, pose un certain nombre de problèmes, dont celui d'engendrer un refroidissement des relations entre juriste-client, en plus de hausser les coûts d'opération de l'entreprise, sans pour

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negotiate transaction or engagement rates and fees on behalf of the client before work commenced. This prototypic approach to alternative fee negotiations was written up favorably in *The Wall Street Journal*, which added that it was probably a sad sign of the times that an additional tier of negotiators was needed to produce mutually agreeable engagements. The buyers' agent idea was greeted warmly by a few innovative corporate clients, but overall its expected beneficiaries shied away. "It was a sound idea before its time," one of its founders says today.

My point is not to suggest that some parties to the client-counsel relationship are more blameworthy, lazy or change-averse than others. Clearly, we are going through a period where, in law school parlance, "reasonable people can disagree," even as all players do what they've always done: operate in what they perceive as their rational self-interest. Though no one may have set out to create a system they can manipulate, today's economic pressures certainly create unprecedented incentives to game the system.

The babel of conflicting perspectives I hear mirror the conclusion of Seventh Circuit Appeals Judge Richard Posner in his recent book, *A Failure of Capitalism*. Posner believes that the current chaos in the business of law today is not the result of devious or irrational forces. He suggests, however, that even though all stakeholders — clients, partners, associates, consultants, headhunters, law students and law schools — may behave in a way consistent with rational self-interest, *the overall effect may turn out to be something none of them expected or wanted, something neither rational nor mutually beneficial.*

Unquestionably, it is hard to plan and control change in the face of constantly changing conditions. Still, top corporate counsel will not produce effective, collaborative change simply by putting the monkey on law firms' backs by demanding that *they* change, that *they* innovate, that *they* unilaterally initiate new and different fee arrangements.

In that regard, the babel I hear at conferences is noisy, but it may ultimately prove constructive. Rather than squaring off in a finger-pointing contest, the legal profession's shell-shocked stakeholders should spend their time and energy comparing notes, sharing horror stories and war stories, and, ultimately, creating a new set of best practices that becomes the new conventional wisdom. ■

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autant adresser le problème fondamental.

En fait, il est sans doute plus facile pour les intervenants des deux côtés de continuer à jouer le jeu selon les mêmes vieilles règles.

Je ne tente pas ici de dire que certains sont plus à blâmer que d'autres, plus réfractaires au changement ou simplement plus paresseux. Néanmoins, la panoplie de perspectives et d'opinions qui circulent actuellement reflètent la conclusion du juge Richard Posner du Seventh Circuit Appeals dans son dernier livre, *A Failure of Capitalism* (L'échec du capitalisme). Le magistrat soutien que le chaos actuel dans le commerce du droit n'est pas le résultat de forces irrationnelles. Il suggère plutôt que même si tous les intervenants — clients, associés, consultants et même étudiants en droit — agissent de manière cohérente avec leurs intérêts personnels et rationnels, le résultat pourrait en être un que personne ne souhaite ou n'a anticipé — un résultat ni rationnel et ni mutuellement bénéfique.

Il est évidemment difficile de planifier et contrôler le changement dans de telles conditions, en perpétuelle évolution. Néanmoins, les conseillers juridiques qui peuvent exercer une influence ne changeront rien s'ils se limitent à blâmer le comportement des firmes externes.

Dans cette perspective, le concert de rumeurs et d'opinions qui a cours dans les conférences légales pourrait s'avérer constructif. Plutôt que de s´affronter et de se pointer du doigt, les professionnels du droit pourraient décider de passer leur temps et leur énergie à comparer leurs notes et leurs expériences et, ultimement, créer un nouvel ensemble de pratiques, qui pourrait bien devenir la nouvelle norme. ■

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