



Using Technology to Source Legal Services

The Most Effective Method of Cost Reduction for Corporate Legal Departments

White Paper prepared
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RFXLEGAL
OPTIMIZING THE VALUE OF LEGAL SERVICES

Across most of their business units, progressive corporations rely on sourcing technology to help them save money and make better purchasing decisions. These tools automate the process of buying products with electronic applications to request quotes or proposals (RFXs) and negotiate with potential suppliers, resulting in savings. When it comes to the legal department, however, most have resisted deploying these tools because they are designed to source products like office supplies – not legal services.

Now, it is possible for legal departments to adopt and benefit from sourcing technology customized *specifically* for legal services. Such technology reduces the costs of legal services by 20 to 40 percent and substantially streamlines the legal services engagement process.

In a Tough Economy, Corporations Cut Costs

When hard economic times lead to reduced revenues, cost-cutting initiatives play a central role in corporate strategy.

Cutting costs directly affects a corporation's bottom line. One common rule-of-thumb states that cutting costs by \$100 has the same effect as increasing revenue by \$300.

Short-term benefits are often achieved by layoffs and reduced product quality. Long-term benefits, however, are best achieved by strategically managing corporate spending. Spend management is the way in which companies **control and optimize the money they spend**. An important component of business strategy, spend management is a process centered around how to spend money most effectively in order to build products and services, and involves cutting operating and costs associated with doing business. The term encompasses procurement, sourcing, and other ways to manage the supply chain. The goal: acquiring needed goods and services at the best possible total cost while meeting the defined needs of the purchaser. **Encouraging competition among suppliers and service providers** is a fundamental premise of spend management strategies.

As the norm for how organizations purchase direct materials (raw goods and materials used in the manufacture of products) as well as indirect materials (office supplies and other expenses that do not go into a finished product), companies are now looking for ways to reduce the “indirect” money spent on services, which can easily represent 70 percent of a corporation's total costs. Often, the cost of legal services dominates the services expense pie chart.

Legal Departments Are Under Pressure, Too

At a time when other business units have drastically reduced costs, **legal spending** has been growing twice as fast as other **areas of purchasing**. Current market conditions present an additional compelling reason to address the amount spent on legal services.

At a typical corporation, total legal spend (for both internal and external legal costs) accounts for approximately 0.5 percent of gross revenues. Based on 2009 Fortune 500 cumulative gross revenues of \$10.8 trillion (\$21 billion per company), these organizations spend \$32.4 billion on outside counsel. With approximately 60 percent of total legal spend attributed to outside counsel costs, that's an average of \$64 million per Fortune 500 company.

Today's corporate legal department is expected to operate like any other business unit. General counsel are under **increasing pressure to rein in their budgets**, and their compensation and career success are often tied to these efforts. As a result, achievement of certainty and predictability in the cost of outside counsel is imperative.

“Every other department in a corporation is relentless on costs -- and we're feeling that pressure as well,” said Michael Fricklas, general counsel at Viacom. “Yet I'm not seeing law firms thinking about process in a very sophisticated way.”¹

“The reality is that we are in the early stages of a seismic shift in the traditional cost and delivery model for legal services,” said Mike Dillon, general counsel at Sun Microsystems. “I see it every day in my interactions with the law firms that support us and in my discussions with peers at other companies.”²

“Our legal department is as metrics-driven as manufacturing, human resources or sales,” said Mark Chandler of Cisco Systems. “The bottom line is that I'm driven by the same need for productivity improvement as the rest of the company.”³

Legal Departments Purchase Complex Services

As one senior manager stated, “The process of procuring services is very collaborative and requires interaction with suppliers at every point of the engagement. Our products-oriented system is designed to support one-way interactions. With services, there is a high need for collaboration or negotiation throughout the engagement process. Also, every firm has a different answer, making it very difficult to compare.”

In addition, **the selection of legal service providers is rarely price-driven**. For “bet the company” matters, (which typically account for a relatively small percentage of outside legal costs), cost is not a factor. The factors that influence legal services buying decisions include – in addition to cost -- important criteria such as quality, experience, unique capabilities, trust, reputation, responsiveness, location, and availability.

¹ Hildebrandt Insights, October 23, 2009 Issue.

² *The Legal Thing: Notes From a General Counsel*, June 18, 2009, <http://blogs.sun.com/dillon/entry/change>.

³ Chandler, Mark, “The State of Technology in the Law,” *Northwestern School of Law's 34th Annual Securities Regulation Institute*, January 2007, http://blogs.cisco.com/news/comments/cisco_general_counsel_on_state_of_technology_in_the_law.

Traditionally, legal spending has been highly fragmented, with relatively few negotiated contracts in place — resulting in high levels of “maverick spend,”⁴ or off-contract, non-structured engagements. Since most in-house lawyers have a list of favorite “go-to” lawyers for certain types of matters – these relationships become entrenched, creating a barrier to change.

Because of the perceived value of the relationship, regular rate increases of outside counsel have been scrutinized far less frequently than cost increases of raw materials or other products. Even when formal bidding processes, also referred to as “beauty contests,” are held every few years, other outside law firms (who could perform the work at a lower cost) often view these engagement contests as heavily biased in favor incumbent firms, and some even decline to participate.

In the past, these factors have **frustrated efforts to control of costs** by legal departments. Currently, however, economic pressures and evolving technology have combined to force legal departments to take a fresh look at spend management. Moreover, certain legal matters share so many common elements that they are essentially commodities. For these services, there may be many outside law firms capable of meeting client needs. Price then becomes an impactful differentiator.

“Where ‘very good is good enough,’ winners among law firms will be those who are able to standardize services to meet clients’ needs for cost-management and predictability,” said Cisco’s Chandler. “Firms that have found ways to produce ‘good enough’ services for less have become more attractive to corporate counsel, creating pressure on other outside counsel to find ways to reduce the cost of services as well.”⁵

Because businesses must constantly seek to reduce costs, legal departments are **highly motivated to find ways to standardize the delivery and cost of legal services**. Now in a buyer’s market, these clients are bringing about a sea-change in the sourcing of outside legal services.

The Cost-Control Toolbox

Outside legal services will continue to be a significant component of “total spend” for many corporations. Although the billable hour is still common, general counsel and chief financial officers (encouraged by the ACC Value Challenge and other initiatives) are now **demanding that law firms offer creative fee alternatives**.

The billable hour model creates a fundamental misalignment between client and service provider. Under a time-based billing model, additional hours are bad for the client (who must operate within a business budget) and good for the lawyer (who is rewarded for collections, resulting from more time billed). Consequently, the risks of inefficiency and cost overruns are borne entirely by the client.

⁴Mahler, Daniel, “Taming the Corporate Legal Spend,” *Supply Chain Management Review*, April 2007.

⁵Chandler, Mark, “The State of Technology in the Law,” *Northwestern School of Law’s 34th Annual Securities Regulation Institute*, January 2007 .

Alternative fee arrangements - including flat fees, discounts, blended rates, conditional and contingency fees – offer one approach to controlling costs. Of the 218 firms recently surveyed by Altman Weil⁶, nearly all have updated their models to offer alternative fee arrangements to their clients.

In a plan leaked to *Above the Law*, O'Melveny & Myers last year stated that it would become a "fixed-fee leader for high-end legal services" by fiscal 2012. According to this account, the plan outlines the firm's intention to offer volume discounts and "appropriate alternative fee arrangements."⁷

Nineteen percent of all respondents anticipate that alternative fee arrangements will account for more than one-quarter of their overall outside counsel spend in 2010, according to a recent article in *Inside Counsel* magazine.⁸

Corporations are also asking outside law firms to **look closely at the way they are staffing** cases and matters. General counsel do not want to pay pricey partner rates for work that can be done by associates, nor do they want to pay associate rates for work that can be done by less-expensive paralegals, legal assistants or contract attorneys. Many are simply refusing to pay for new lawyers to train on the client's tab.

Legal departments have also implemented **electronic billing platforms** and require law firms to submit invoices online. E-Billing software tests for data integrity and guarantees compliance with the rates specified in the firm's engagement agreement. These applications not only eliminate pricing discrepancies and errors such as double-billing and over-billing, they also provides real-time visibility into both paid and pending legal services spend, and automate spend tracking for future analytics.

Finally, recognizing that competition can **reveal the true market value of legal services**, legal departments – deploying a cost-reduction strategy used by other business units -- have been conducting beauty contests as a means of building preferred provider lists and reducing the number of firms under engagement. Premised on competition, the beauty contest allows a company to leverage its purchasing power and negotiate discounted rates in exchange for a predictable pipeline of work or an opportunity (or continued opportunity) to provide legal services to the client. Typically, a legal department disseminates an RFX (request for information, proposal, or quote) to a number of prospective firms in order to collect information for purposes of evaluating whether to engage that particular firm.

Theoretically, the RFX process allows buyers to make comparisons and informed sourcing decisions. However, because RFX processes are conducted on a manual basis, using Outlook calendars, e-mail

⁶New Law Firm Survey: A Consensus on Change, Altman Weil, http://www.altmanweil.com/index.cfm/fa/r.resource_detail/oid/6ddd4b8a-88a3-44ef-85a1-5a9a7ce501ac/resource/New_Law_Firm_Survey_A_Consensus_on_Change.cfm.

⁷Weiss, Debra, "O'Melveny Aims to Become Fixed-Fee Leader, Leaked Plan Says," *ABA Journal*, September 17, 2009, http://www.abajournal.com/news/omelveny_aims_to_become_fixed-fee_leader_leaked_plan_says.

⁸Ecker, Keith, "Proper Proposals," *Inside Counsel Magazine*, June 2008, p.63.

and PDF documents, the process is cumbersome, inefficient, and time- and resource-consuming. In addition, because the nature of legal services, proposals often lack uniformity, making it **very difficult to compare “apples to apples”** when making a sourcing decision.

The New Frontier: e-Sourcing

As one Fortune 500 global procurement executive stated, “Electronic [sourcing] applications consume half the resources, are twice as fast, and deliver twice the savings.”

Since the late 1990s, large organizations began to automate their sourcing processes by using electronic tools to build and distribute RFXs, negotiate with suppliers (through sealed bids and reverse auctions), and to analyze and evaluate bids.

“E-Sourcing” applications **not only automate but also improve upon** the strategic sourcing and procurement processes, enabling buyers to achieve far greater savings than those available with traditional manual methods. These applications use mathematical algorithms to rapidly solve business problems by evaluating all possible outcomes and selecting those that yield the best solution (in terms of cost, quality and timeliness) and least risk in a particular situation.

Using technology to strategically source services maximizes savings through online negotiation with suppliers. It’s more than merely automating the sourcing process — online events provide suppliers with real-time visibility into the most competitive bids available. For that reason, bidders often respond with lower prices, resulting in a **true market price**.

Now, legal departments can achieve the same benefits from e-Sourcing technology.

Using e-Sourcing Technology to Purchase Legal Services

Many widely available e-Sourcing applications — either free-standing or part of enterprise resource planning systems — are designed for the sourcing of raw materials or products. Although useful across many categories, they are either too product-focused to work well for legal services, or because they are designed for broad application, fail to take into account the nuances unique to legal services.

General counsel and procurement leaders desiring to strategically manage legal spend should strongly consider products that are customized specifically for legal services. In general, lawyers prefer to deal with vendors who are also lawyers – and who speak the same language.

Advantages of using an e-Sourcing tool designed for legal services include:

More market participants. With an average success rate of only 30 percent, and a perception that the process favors incumbents, law firms often decline to participate in the RFX process. In addition, because the manual process is so time- and resource-consuming⁹, firms decline to respond because the return on investment (ROI) is so low. With fewer participants, the value of conducting the event declines. Automating the process — by making it easier to respond — increases the ROI for firms, and builds transparency and fairness into the system.

Value = quality and price. The process facilitates comparison among lawyers and law firms based on price, but also based on qualitative and subjective metrics.

Flexibility. The process is flexible enough to accommodate single bids for complex “bet the company” work as well as ongoing bids for more routine work.

Analytics, reporting and negotiations. E-Sourcing tools offer robust reporting capabilities, and through “what if” scenarios, reveal the cost implications of decisions. With such information, legal departments can better negotiate with firms.

Streamlined engagement process / cycle. Research indicates that this technology-driven approach should reduce the time it takes to find and hire the right law firm by 30 percent — on top of reducing services costs by 15 to 40 percent. Additionally, savings result from setting up a robust system coupled with process excellence.

Important Features of an e-Sourcing Tool

Leveraging technology to reduce legal spend involves more than mere RFX automation. Deploying a comprehensive e-Sourcing solution maximizes savings opportunities in the following ways:

Legal spend analysis. Analyze legal spending patterns – especially undisciplined “maverick” spending patterns – and reveal opportunities to save.

Legal services network. A searchable, centralized database of quality legal service providers (new and existing) is a key component of an e-Sourcing platform. Although preferred incumbent firms are invited to complete a questionnaire to participate, a corporation also has access to a wide range of new firms interested in bidding on work. Firms can compete for work opportunities when they experience excess capacity, and opt out when their pipelines are full.

Automated RFX process. With an automated RFX, buyers can clearly define and weight their specifications — all online — so that all bids can be evaluated against the same criteria, and then ranked in accordance with how well each matches the buyer’s needs specification. With real time bid visibility, subsequent bidders have an incentive to enter at progressively lower — and more competitive — price points.

⁹ An Altman Weil survey reported in 2008 that the cost to a law firm of responding to a traditional RFP ranged from \$35,000 to \$65,000 – or between 100 to 200 partner hours.

http://www.altmanweil.com/index.cfm/fa/r.resource_detail/oid/170b61e2-0828-479e-8c89-3099007ed1b7/resource/Whats_the_Real_Cost_of_Responding_to_RFPs.cfm.

Optimization. Optimization tools allow buyers to run alternative award scenarios, yielding a dashboard of valuable data on which to base a decision or negotiate a service agreement. Customized scenarios show the cost implications of allocating different parts of the representation among different firms to yield the best overall price and quality combination to the legal department.

Corporations understand how e-Sourcing helps them control costs on purchased raw materials and products. Legal departments are now in a position to implement similar **cost control measures that go beyond traditional methods in terms of effectiveness.** E-Sourcing technology facilitates this process to help general counsel save money and make better “apples to apples” decisions on the purchase of costly legal services.

Concluding Thoughts

A growing number of economists are predicting an extended period of slow growth for the economy. To weather the storm, businesses must continue doing more with less, and controlling costs will continue to be a top priority. Legal spending will continue to be a focus of cost containment, and internal pressures to reduce the legal budget will continue to intensify.

With a solution that drives savings on outside legal services, e-Sourcing technology designed for legal services can help legal departments achieve these objectives.

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RFX Legal: Optimizes the Value of Legal Services™

RFX Legal delivers the first online sourcing application - tailored by lawyers for the legal industry – to reduce costs and to increase the predictability of legal spend. The RFX Legal solution helps organizations analyze legal spending, streamline operations, negotiate rates, and optimize sourcing decisions. Our mission is to create an efficient, disciplined and objective marketplace in which legal service providers compete for business based on quality, service, expertise and value.

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