

IS **AXIOM**
THE BELLWETHER FOR DISRUPTION
IN THE LEGAL INDUSTRY?

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I THINK THE ANSWER IS YES. For the last several years, I have been an avid watcher of Axiom's growth, but this article in Friday's *Houston Business Journal* finally convinced me that the top-end of the legal industry is changing and that Axiom is setting the standard for disruption.

On a surface level, many of the facts in the *HBJ* article are unremarkable. Axiom opened its Houston office back in May 2012. Since then, it has grown to 30 lawyers and expects to add another 15 over the next 12 months. Yet, during this same period, the boom in the energy sector has caused several national and international law firms to also open offices in Houston, including Reed Smith, Dentons, Katten Muchin, and K&L Gates,

Axiom and large law firms are definitely targeting and servicing the same clientele -- Fortune 100 legal departments. The substance of their work is also very similar -- sophisticated, complex legal work related to disputes, transactions, and compliance. But in many cases, the solutions offered by Axiom are radically different.

Okay, now a reasonable expectation of any reader is likely to be, "Now explain that difference." Back in 2010, Axiom's CEO Mark Harris told *Law Practice* magazine that Axiom was "trying to invent a whole new category of law firm. When you're doing that there is no vocabulary [to describe your business model]."

In my experience, the opaqueness of Axiom's business model actually works to its advantage. Specifically, it encourages its primary competitors (large law firms) to categorize Axiom based on an outdated

caricature, which gives Axiom more running room to develop that "whole new model." Let me start with the caricature; then I will do my best to explain what the company actually does.

THE INACCURATE AXIOM CARICATURE

In its early years, Axiom was described by many as a high-end "temp" service for legal departments. See, e.g., Peter Lattman, *Axiom: A Different Kind of Legal Practice?* WSJ Law Blog, Nov. 27, 2007 ("Axiom Legal has establish a niche as a provider of high-end temp services to blue-chip corporate clients.").

The simplified version runs like this. Lawyers working in large law firms trade in their partner status, or shot at partnership, for more autonomy and a better work-life balance. By brokering relationships between legal departments and skilled but disaffected lawyers, Axiom ditches the "class A" overhead and reduces the allocation of legal fees that would otherwise support record law firm profits.

Under this caricatured model, all parties are made better off -- the client (who gets the same quality work, but cheaper), the lawyers (who get off the billable hour trend mill and are able take vacations again), and Axiom (which collects a fee). The caricatured model also enables large law firms to dismiss the Axiom model on the belief that only a small tranche of legal work is at risk of being siphoned



Axiom Founder, Mark Harris

photo: axiomlaw.com

away. And that work is lower margin and price sensitive -- so-called “commodity” legal work. Finally, the lawyers leaving for Axiom are not the heavy-hitter equity partners who control client relationships. Hence, the analysis is complete: Axiom represents zero threat to the BigLaw model.

Yet, if brokering lawyer services was originally the core of Axiom’s business, they have subsequently expanded their offerings. Back in 2007, Axiom was #73 on Inc magazine’s list of fastest growing companies, with revenues of \$17 million per year and 1000%-plus growth over three years. Since then, its revenues have grown another ten-fold. Earlier this year, Axiom took \$28 million in outside investment, which it plans to invest in technology. See Mark Harris of Axiom Answers Hard Questions, Legal Whiteboard, Sept. 25, 2013.

With this kind of growth, and the backing of very serious venture capital funds, perhaps its time to check the assumptions surrounding the Axiom caricature.

THE “MANAGED SERVICES” BUSINESS MODEL

Based on my own discussions with Axiom management and several articles on the topic, see, e.g., Adam Smith, ABA Journal, Strategic Legal Technology Blog, the fastest growing part of Axiom’s business is its “Managed Services” practice.

Part of the managed services practice is

analyzing and redesigning workflows so that in-house lawyers have the cost and quality information needed to make better sourcing decisions. Because Axiom is helping to redesign the workflows, including the specifications for sourcing decisions, it is well-positioned to do much of the resulting work -- indeed, unless it can manage both the design and execution of the work flow, Axiom can’t warranty the results.

What is the goal of the workflow redesigns? To reduce legal risk and legal cost at the same time, primarily through process, measurement, and feedback loops. Virtually the entire law firm and law school universe is stuck in a mental frame that believes that better, faster, and cheaper are in permanent tension with each other. This is because our frame of reference is constrained to artisan-trained lawyers working in an traditional office environment with a state-of-the-art that consists of Word, email, and a searchable bank of forms and briefs.

Yet, when systems engineers, information technologists, and project managers become equal members of the team, “better, faster, cheaper” becomes a straightforward problem that can be solved through a four-part continuous process: design, execute, measure, repeat.

Much of the key design and execution work at Axiom is done by nonlawyers who formerly worked for global consulting businesses. See, e.g., this opening in Axiom (Chicago) for Project Management Director of Managed Contracts.



Axiom's Brian Bayne
photo: axiowlaw.com

Indeed, the head of Axiom's Houston office is Brian Bayne, a business development professional with an MBA from the University of Dallas. Before joining Axiom, Bayne worked for IBM. Here is how Bayne described Axiom to the HBJ:

"The heart of what motivates us as a company is to be seen as an agent of change We want to be a leading voice for transition in the industry. It really is a new way of doing business and offers a completely different value proposition that most law firms are not in a position to do."

IS AXIOM A LAW FIRM?

Over at the E-Lawyering Blog back in April, Richard Granat did a very careful job trying to answer this question, and concluded that the answer was "no." In fact, Axiom is a Delaware C-Corp with

nonlawyer investors as equity shareholders.

So, how is Axiom getting around the Rule 5.4 ban on fee-splitting with non-lawyers? The answer to this question has a lot to do with the nature of outsourcing and managed services within legal departments. A general counsel for a corporation controls the legal functions of the company. Because he or she can't do all the work themselves, they hire in-house legal staff and outside counsel. In recent years, legal departments have also contracted directly with LPOs, particularly on matters related to e-discovery and M&A due diligence. When it comes to non-law firm options, such as LPOs, the general counsel and his or her staff are "supervising" the work within the meaning of the legal ethics rules.

When a general counsel of a corporation uses a managed service provider, such as Axiom, they are diverting a tranche of work they control. The value of the managed service provider is process expertise plus economies of scale and scope. Axiom, through a contract with the legal department, manages some of that legal workflow that supports in-house lawyers in their counseling and compliance roles. Yet, the buyer of the managed services is himself a lawyer, and that lawyer is ultimately responsible for advising the corporation on legal risk.

On one level, Axiom is a niche business. As Granat notes, "If you don't have an in-house counsel, then you can't use Axiom's services. Not being a law firm, Axiom

cannot provide services to the public (individuals or organizations) directly.” Yet, this niche accounts for a huge proportion of the entire legal services market. In this *American Lawyer* article, one of Axiom’s venture capital investors, opined “With a worldwide legal market that is a trillion dollars each year, there is plenty of running room to build a successful business.”

Ultimately, the value proposition very simple. As an in-house lawyer, you can educate yourself on the Axiom managed services approach and be comfortable that, through process and measurement, you have a solid handle on this tranche of the company’s legal work, likely within budget. Or you can have the CYA coverage of a brand name law firm and continue to do battle with your CFO over rising legal fees. If you were an investor, which approach you would bet on?

So Axiom can’t help you with your divorce, will, or personal injury case. Don’t worry, Jacoby & Meyers, Legal Zoom, Legal Rocket, and others are trying to tap into that market. See *Legal Futures*, Nov 8, 2013. In the meantime, Axiom may be gunning to be a service provider to your large corporate employer.

THE LAST DAYS OF A BLOODLESS REVOLUTION

I am sure that a state bar regulator, taking a very formalistic approach, can take issue with Axiom’s construction of Rule 5.4, which prohibits profit-sharing

between lawyers and nonlawyers from income generated from the practice of law. But the purpose behind Rule 5.4 is to preserve lawyer independence so that the quality of the underlying legal advice won’t be compromised by the nonlawyer’s pursuit of profit.

In the case of Axiom, however, the person making the buying decision is a highly sophisticated lawyer who is struggling to manage his or her organization’s legal needs within a budget. Stated bluntly, the GC of a multinational corporation does not want the kind of consumer protection that a formalistic construction of Rule 5.4 would provide.

A betting person, such as a nonlawyer Axiom investor, would likely conclude that the bar regulators are not going to pick a fight with the largest corporations headquartered in their jurisdiction. Why would they? The subtext of economic protectionism would set them up for ridicule in the legal and mainstream press—who, exactly, is being harmed besides the law firms who are losing market share? And is there a principled basis to distinguish LPOs from managed services?

Expect to read more about state regulators in the “risk factors” section of Axiom’s S-1 registration statement if and when Axiom decides go public. I think these risks will likely remain hypothetical, but as my friend Ed Reeser is known to say, “That is just my opinion. I could be wrong.”

Truth be told, the nonlawyer revolution in U.S. legal services is occurring right

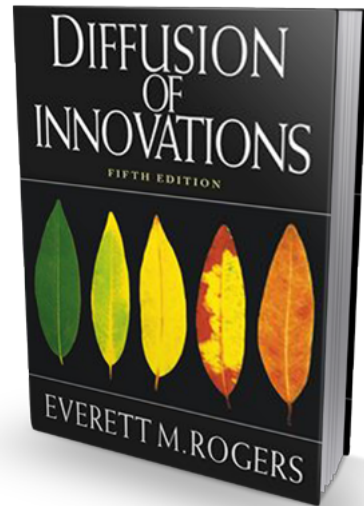
now. And there is a good possibility that the whole revolution will take place without a single shot ever being fired.

BACK TO HOUSTON

The *HBJ* reporter asked a local Houston legal recruiter about the future prospects for Axiom. The recruiter commented that he was “[n]ot sure how well they will do in Texas, given the conservative nature of the legal business here.”

In my own experience, general counsel in Texas are among the most innovative and entrepreneurial in the country. The General Counsel Forum was originally founded in Texas as a state-level organization, and it is now rivalling the Association of Corporate Counsel (ACC) in terms of educational programming for in-house lawyers and sharing best practices and benchmarking.

Lawyers as a group may be conservative, but within that distribution there is a small cadre of innovators and early adopters. Although most people don't change their behavior in response to abstract ideas, innovators and early adopters are at least drawn to the possibility. Not every idea will be successful -- indeed, the trial and error of the innovators is often a basis for dismissing them as fringe players. Yet, when an innovation produces a significant leap forward, the resulting success eventually sets off a widespread diffusion among the broader population.



There is a rich sociological literature on this topic, which was pioneered by Everett Rogers in his 1962 book, *Diffusion of Innovation*. It turns out that self-interest is often inadequate to overcome inertia and prejudice, at least in the short- to medium-term. The classic example is hybrid seeds, which have a host of advantages for producing more bountiful, disease-free crops. Yet, that innovation took decades to take hold among farmers.

Looking for another example? In the early 1980s, Bill James was publicizing the benefits of his stats-driven approach to baseball. The advertised benefits were clear -- “you can win more baseball games.” Isn't that what every baseball team wants? But what's the cost? “Well, you'll have to change the way your eval-

uate talent.” For nearly twenty years, the implicit answer of the baseball establishment was “no, that price is too high.” Within the last decade, however, the stats-driven approach has become commonplace in baseball and in other sports as well. The innovation has become diffuse.

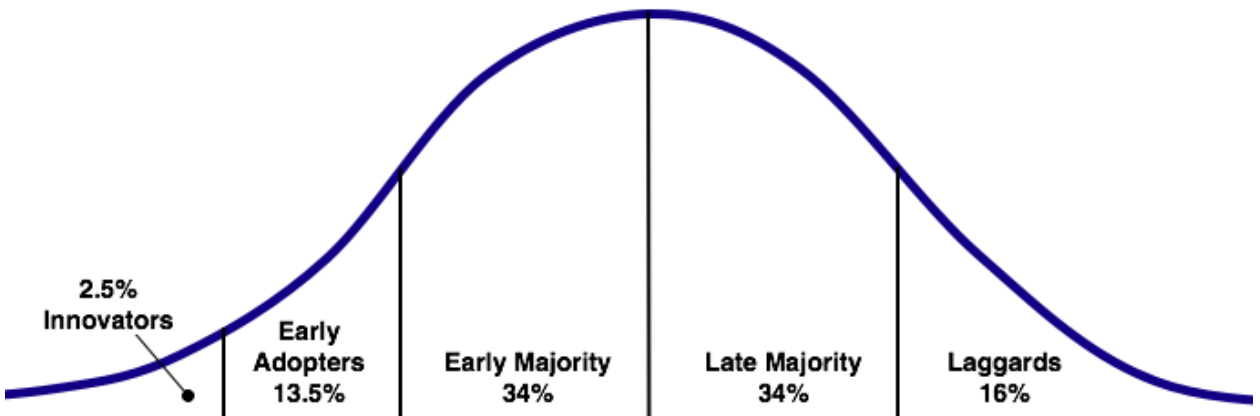
I suspect that Axiom’s senior management fully understands these dynamics. Looking at the distribution model from Everett Roger’s book, if you are trying to sell your unproven innovation, you are literally wasting your time trying to sell to your wares to 85% of the market. Indeed, if you are in the very early stages of innovation, 98% of the potential buyers are likely to be resistant to your pitch.

The problem here is not economics -- its human nature. This may be hard for many lawyers to believe, but lawyers, including general counsel, are human beings. And human beings are prone to a series of predictable reactions when presented with various stimuli, such as new ways to perform their work. Rather

than process the merits of the idea, many human beings, including lawyers, will instead gauge the reactions of the market leaders. If the market leaders react with approbation, the early and late majority become willing to actually engage with the idea.

What this means is that the merits of a good idea are not enough to ensure its success, at least immediately. This is a key practical insight that the reformer/innovator class seldom grasps. Without understanding Roger’s Diffusion of Innovation curve, an innovator’s success becomes a function of timing and luck -- that is the story of Bill James.

But if you understand the diffusion process, it is possible to construct a filter that locates the innovator/early adopter class. And if you study their beliefs and problems, you can more effectively tailor your pitch. This approach saves time and money and holds the team together in the belief that they will ultimately be successful.



Source: Everett Rogers (Diffusion of Innovations model)

SO, WHERE IS AXIOM ON THE ROGERS DIFFUSION CURVE?

My best guess is the “early adopters” stage, as Axiom has relationships with roughly half of the Fortune 100 and is working hard to widen those relationships with more ambitious projects. Their goal, as best as I can tell, is to generate a clear proof-of-concept that they have solutions to the risk/cost conundrum that plagues so many legal departments and causes them to blow their budgets. With sufficient market testimonials, and as in-house lawyers with exposure to Axiom migrate to other legal departments, the broader legal market will begin to tip.

I find the Axiom story refreshing, primarily because the legal market has fallen under the spell of the fast follower strategy. In my travels, I often encounter the attitude “Let someone else prove that it can be done differently and better and then we will follow.” When virtually the entire market adopts this worldview, incumbent institutions begin to relish the false starts of others and a general sense of complacency begins to set in. Frankly, I find this whole dynamic unprofessional in the classical sense of that word -- i.e., at variance with professional standards and conduct.

Axiom, in contrast, is on the brink of demonstrating the benefits of the first mover advantage in law. This is bound to have the beneficial, balancing effect on the rest of us.