

LexisNexis

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Contents

Executive Summary	3
Objectives	3
Participants	3
Findings	4
Section 1	5
1.1 The transactional nature of client-lawyer relationships	5
1.2 The historic transition from the relationship-based to the transactional model	5
1.3 The client-lawyer relationship of the future	5
1.4 How can law firms instigate this change?	5
Section 2	6
2.1 Impact on leverage	6
Section 3	6
3.1 The billable hour	6
Section 4	7
4.1 Technology and the drive for value	7
4.2 The race to the bottom and the \$25 precedent	7
4.3 Law without barriers	7
Section 5	8
5.1 Recruitment, retention and succession	8
5.2 Diversity in practice	8
5.3 Minding the succession gap	8
Conclusion	9
Appendix 1 – Attendee quotes for media	10

Executive Summary

The legal industry has often been accused of being slow to evolve. Be it billing processes, the adoption of time-saving technology or the perceived lack of flexible working practices – there is a view that the industry lags behind.

However, the global financial crisis (GFC) is forcing law firms to re-evaluate their working practices and for the legal sector, is a catalyst for change. While trade has slowed across the board, an opportunity exists to assess the current state of the industry and innovate for the better. If partners focus on reinvigorating the way they approach the business and practice of law, the law firms that emerge from the other side of the downturn will look and behave differently.

LexisNexis, a leading provider of legal, business, news and information sources and workflow solutions, hosted a roundtable event to engage with leading practitioners and managers and investigate how radically we can expect the legal industry to transform during (and following) the GFC.

Objectives of the roundtable:

The roundtable sought to identify and explore:

- How law firms of all sizes are being impacted by the GFC
- What a typical law firm will look like when the economy recovers
- How the downturn is affecting law firms in a number of areas including:
 - Client relationships;
 - Financial drivers including billing and leverage;
 - Staffing; and
 - Use of technology.
- What firms can do now to strongly position themselves for the economic recovery and the changing nature of legal operations moving forwards

Roundtable participants:

- Michael Rose, Chief Executive Partner, Allens Arthur Robinson
- Howard Harrison, Managing Partner, Carroll & O’Dea
- Peter Ellender, Chief Executive Officer, Carter Newell
- Christopher Freeland, Partner / Chief Operating Officer, Gilbert + Tobin
- Steve Sampson, National General Manager, Hunt and Hunt
- Mike Russell, General Manager – Legal Markets, LexisNexis
- Nick Nichola, Managing Partner, Middletons
- Stuart Westgarth, Junior Vice President, Law Society of NSW
- Fred Swaab, Managing Partner, Swaab Attorneys
- Graeme McFadyen, Chief Executive Officer, Trilby Misso Lawyers

Findings:

- The economic downturn provides an opportunity to redefine the client-lawyer relationship;
- Many customers currently take a cost-centric approach to legal matters, with insufficient value placed on personal relationships and the corporate knowledge their lawyers possess;
- Over the next five years we will see an evolution in the client-lawyer relationship. Clients will start to see the value in establishing a closer relationship with their legal teams. Lawyers will become ‘trusted advisors’ whose services can add value to their client’s business;
- This renewed focus on relationships will mean that we see less leverage, with senior lawyers required to invest more time networking with clients;
- There is a strong argument for moving from the billable hour model to pricing based on the how much value the client derives (outcomes) from the legal services in question;
- The lay person now has a wide variety of legal information available via the Internet. Lawyers must provide quality advice, driven through independent thought and analysis, in addition to the basic legal information provided;
- Globalisation means that law firms need to develop a truly international presence in order to maximise the work they can receive from the rest of the world;
- Legal intake is heavily weighted in favour of women. Management of work-life balance and the provision of flexible working practices will increase in importance as women move through a law firm; and
- There is an intensifying demand for lawyers from a breadth of ethnic backgrounds. Issues of race, ethnicity and social background have to be taken into account to ensure Australian law firms become representative of the country as a whole.

Acknowledgements

We acknowledge the input of the participants involved in this roundtable event. This whitepaper incorporates the views expressed during the roundtable panel discussion and LexisNexis credits them for the opinions put forward in this document.

A list of attributed attendee quotes is included in Appendix 1.

Section 1

1.1 The transactional nature of client-lawyer relationships

Over the past ten years, the nature of this relationship has evolved. While legal practitioners were once regarded as trusted advisors to clients, the dynamics have definitively shifted. Clients have largely developed a cost-centric approach to legal matters. Many no longer value long-standing relationships with their legal team, but rather issue briefs on a transactional basis dependant on who can offer the best price for a particular piece of work. In some transactions; clients will assign pieces of the same case to different law firms on the basis of cost.

However, the current economic climate is providing an opportunity for lawyers to reassert themselves in the minds of clients, re-establishing their role as a 'trusted advisor' and holder of a depth of knowledge required to understand and support their client's business.

1.2 The historic transition from the relationship-based to the transactional model

In times past, the strength of traditional client-lawyer relationships lay in the relationship itself. The in-depth understanding of a client's business acquired through a long-standing professional relationship allowed lawyers to better service that client. However, over the past 20 years, Australian businesses have become larger and more complex. As these businesses have evolved, so too has their workforce. New employees join, departments grow and priorities shift. In this climate, it is easy for the client-lawyer relationship to be overlooked, with the new wave of hires on the client side failing to recognise its inherent value. It is now less about relationships with a legal team and more about managing costs. Legal costs have come to be managed just like any other expense, with little value placed on personal relationships and the emphasis on identifying and retaining the most cost-effective supplier.

It is worth noting that law firms themselves have contributed to this state of affairs. The billable hour model, while profitable in the boom years, has meant that the primary focus was productivity and billing. It has been more valuable to be in the office and bringing in revenue, than out of the office and building and maintaining client relationships.

There is also little doubt that the billable hour model has cost law firms the trust of many clients. The apparent focus on profit and partner earnings by firms has undermined the 'trust' in the 'trusted advisor' role of the legal profession.

1.3 The client-lawyer relationship of the future

As the profession evolves and a harsh economy forces a change of approach, lawyers could expect to see the re-establishment of their 'trusted advisor' role within long-term client relationships. In this advisory role, they will deliver high quality, independent, dispassionate advice based on a long term view of what is best for the client's business.

Some businesses are already starting to realise the value of having a stronger connection with their legal team. The downturn has led them to question what they could have done better in the good times to protect their business. They are beginning to look for legal teams with a sound understanding of their business and its objectives, to help them plan for the future and ensure its sustainability. This presents an opportunity for firms to reposition themselves and become true partners to their clients. However, this will require a shift in thinking.

1.4 How can law firms instigate this change?

To re-establish the trusted advisor role lawyers need to think beyond the deal in front of them. They must take a more strategic approach, while remaining commercially-minded, to demonstrate the value-add their services provide. For example, an hour's work by a partner could save a client millions of dollars. The value here is in the outcome achieved, as opposed to the minimal investment of time by the lawyer.

To really add value to a client's business, lawyers must take a more holistic approach, by investigating the issues that impact the organisation as a whole and understand how their firm can assist in providing solutions. Lawyers will spend more time with their clients to gain a thorough understanding of their long term objectives. The firms that succeed will be those who are prepared to utilise staff with strong inter-personal skills to rejuvenate client relationships.

Lawyers also need to become more vocal about the value their services add to their client's businesses. There is a case for training lawyers to develop tangible ways to demonstrate the impact of their work. This can be illustrated through relatively simple mechanisms such as reports detailing achievements or cost savings. Reminding clients that legal work is adding value to their business is imperative when trying to prove credentials as a trusted advisor.

Section 2

2.1 Impact on leverage

In boom times, law firms increased profitability by boosting the amount that is billed in respect to each equity partner. This is done by increasing the ratio of lawyers to equity partners. Known as high leverage, this practice has been prevalent in the Australian legal industry in recent years.

High leverage can be demonstrated by examining the partner profits at mid tier firms. Over the past five years we have seen an increase in these partner profits, jumping from around \$300,000 to in excess of \$500,000. This has happened largely through leverage and the transition of work from more expensive 'top-tier' firms. While the market for legal services remains fairly static, mid-tier firms have increased partner profits by increasing leverage, tightly controlling equity and increasing volume.

However, as we see a shift in the relationship between lawyers and clients, this highly-leveraged model will be impacted. The growing emphasis on relationships will go hand in hand with less leverage. If law firms want to establish trust based client relationships they will need to ensure that senior staff are available to invest time in these relationships.

With leverage used to boost profits, a reduction in leverage will be a concern for law firms. Lower leverage will mean lower income, especially at the top end. However, this is an issue that law firms can address through their approach to billing.

Section 3

3.1 The billable hour

The death of the billable hour has been mooted for years, but with lawyers aiming to move back to the 'trusted advisor' role, we may finally see a real impact on billing methods.

The billable hour leaves clients wondering how much they will be charged every time they speak to their legal advisor. Add to this the fact that in-house lawyers have largely come from a large law firm background – and consequently have a solid understanding and potentially a mistrust of billable hours. The billable hour has led to widespread suspicion of law firms and there is a considerable amount of work needed to restore trust. If lawyers want to evolve client relationships and be regarded as trusted advisors, they may be forced to rethink this model.

If client service will be focused on the value-add that a lawyer can bring, this could also be utilised as a new focus for billing. Take again the example of an hour's work by a partner that saves a client millions of dollars. Rather than charging for an hour's work, the partner could charge in proportion to the value of that work to the businesses. This kind of work can be priced based on the value derived by the client, as opposed to the billable hours invested by the firm. This value-based model is already used effectively by corporate advisors and there is no reason it would not translate to the legal industry.

At the other side of the spectrum, we are seeing a huge move towards fixed-price work. In small firms this is common practice, with clients demanding certainty when it comes to popular transactions such as conveyancing and probate. When it comes to medium and large sized firms, there is an acceptance that fixed price billing could easily be implemented for transactional work.

With the rise of online availability of legal documents, there is an understanding in society that basic legal transactions do not need to be costly, and can even be carried out by consumers themselves. When it comes to this standard transactional work, a transparent, fixed-price model is likely to come into play within firms, in a bid to provide cost certainty and restore trust.

Moving forward, we are likely to see these two models working in tandem, allowing clients certainty when it comes to transactional work, with a different regime for high level work.

Section 4

4.1 Technology and the drive for value

The past 10 years has seen technology transform the way we do business. The ubiquity of technology and its subsequent commoditisation of information through the Internet have inalterably lowered the barriers of entry to the legal world. Being a credible advisor no longer means having access to a legal library, but a telephone line and a simple Internet connection. Easy access to the law is no longer the sole preserve of the law firm.

The corporate legal team's ability to access information and legal documentation has eradicated lawyers' cash flow through arbitraging information. The current focus on cost and return on investment could lead to more instances of in-house counsel utilising online legal information instead of engaging their retained firm. New generations of lawyers are growing up with an inherent reliance on technology and the ability to access information, anywhere and at any time. However, they must remember that reliance on online information can be dangerous. Free online sources can easily become outdated and can never replace the meticulous research and in-depth experience that are the hallmark of a legal professional equipped with the best available information and tools. Law firms have an opportunity to prove their worth, by demonstrating what they can offer above and beyond this so-called 'Wikipedia law'. Value must be driven through the independent thought and analysis imparted, in addition to the basic legal information provided. Near enough is simply not good enough.

4.2 The race to the bottom and the \$25 precedent

The free availability of legal documentation has also helped to fuel the rise of cheap, or even free, legal advice – the so-called \$25 precedent. The global financial crisis is driving extreme competition and law firms are responding by offering parts of their business for a nominal fee in the expectation that the relationship they build will accrue additional fees later. This approach has accelerated the declining perception of the value provided by legal professionals.

Competition and commoditisation are changing legal pricing models, a trend that is transforming the competitive pitch process. The black letter of the law is no longer valued. Process documentation, previously a valuable commodity, is now being used as an incentive for clients rather than as a billed task. In this scenario, it is the value that lawyers can add to the deal that will win them business rather than the documents they create.

The corollary to this devaluation is that lawyers operating at the smaller end of the market are under increasing price pressure. Sole practitioners in particular, whose cash flow is often supplemented by such work, are under threat from larger organisations able to use their economies of scale. But sole practitioners, who specialise in niche areas of law, such as Intellectual Property or Environmental Planning for example, are able to focus solely on being experts and have fewer overheads than the large law firms so they can be extremely competitive. It is the sole traders on the transactional high street end that will struggle to differentiate and find the margins necessary to survive.

4.3 Law without barriers

Another facet of the role of technology in today's legal sector is the ease of communication across borders. Globalisation is inevitably leading to legal work being outsourced. Legal discovery in particular has been off-shored to take advantage of the lower price points available.

This trend is both an opportunity and a threat to Australian firms. Opportunities for work are no longer confined to the domestic market, and Australian firms are seeing revenue inflow from regions such as the US and the UK. However, traditionally domestic work is also beginning to leave the country for cheaper shores.

In five years time, globalisation will mean that many large- and mid-sized law firms will have developed a true international presence or relationship in order to maximise and maintain a consistent flow of work. Meaningful relationships with both global clients and international lawyers will be necessary to compete with rivals and satisfy both their clients and the ambitions of their staff.

Section 5

5.1 Recruitment, retention and succession

The demographic make-up of legal practices has long been a bone of contention across the industry. The traditional legal stereotype of the aged middle-to-upper class white male is both pervasive and entrenched. But as social, racial and gender norms evolve, so too do the profiles of the legal intake.

These changes impact not only the recruitment policy of practices, but also the means by which morale and retention are managed and, ultimately, succession.

One ongoing trend is the gender disparity in legal intake, which is currently heavily weighted in favour of women. Two years ago, it was estimated that women were numbering 60 percent of entrants to the legal workforce; a figure that is only expected to have grown. In five years, entry level positions in practices across Australia are expected to be dominated by women, particularly in the government and corporate arenas.

The predominance of women starting out in law has implications for their management, for their retention, and even for maternity planning. Management of work-life balance and the provision of flexible working practices will continue to increase in importance as women move through an organisation. The acceptance that work-life balance and individuality go hand-in-hand must be implicit, as should the need for firms to begin to accommodate provision for these factors into their business model.

Retention in particular should be top of mind as family friendly values and parental leave are discussed. It's notable that mothers are substantially more likely to return to their firm following parental leave if the firm proves its commitment to the needs of the individual. While there are practice areas where such adaptability is more testing – litigation for example – the human capital resource involved means that all firms should be investigating economically viable initiatives to maintain the right balance.

5.2 Diversity in practice

The imbalance of gender within law firms should not be the sole focus of the industry's recruiters, however. Law firms are currently not proportionally representative of the Australian community, and it would be hard to argue that law schools differ significantly from that assessment.

Client wishes may emerge as the biggest driver in this area. It was noted that there is an intensifying demand for lawyers from a breadth of ethnic backgrounds and this is often demanded by a client. Expert advice from professionals with inherent background knowledge of a client's language or culture is becoming a prized commodity. As Asia in particular becomes more globalised, clients will demand that the lawyers they deal with better represent a wide breadth of ethnicity. Ethnic groups are starting to become heavily represented in the corporate world and law firms must keep up with this trend. Therefore, issues of race, ethnicity and social background have to be taken into account to ensure Australian legal firms become representative of the country as a whole.

These are significant changes and it will take time to produce visible results. Already there are fewer strong candidates entering the legal profession, irrespective of ethnicity. Additionally, the pool of law students does not represent the ethnic mix that we see in society as a whole. The profession will need to actively encourage students from these ethnic groups to join the profession to see change.

5.3 Minding the succession gap

With an ageing population, succession planning for the future is an even more pressing concern. Often the lawyers of the firm hold more corporate knowledge than some executives within client organisations. If a key contact retires or leaves, the revenue can leave with them. Who is going to run the practice when the founding partners retire?

It has been said that the legal profession is caught in the middle of a serious succession gap. Observers note a cluster of senior legal professionals over the age of 50, with another mass of lawyers around the mid-30s age range. However, between those two age ranges there is a much thinner spread of lawyers – and this is leading to a generation gap.

That lost generation poses a significant problem for the industry as a whole. As elder partners draw their careers to a close, some will take their accumulated knowledge and relationships with them rather than pass it down to their apparent successors.

The days where lawyers grow up alongside their clients, through marriages, divorces and children may be gone. However, there is no excuse to let these relationships and working practices leave the industry because of a succession gap. Legal firms not only have to ensure skills and knowledge are passed on to the next generation, but also the ability to act as a trusted advisor.

Conclusion

Change does not happen quickly in the legal profession. However, in five years' time, the legal landscape will have been inevitably altered. Evolution in the industry is absolutely necessary, whether that is prompted by the impact of the global financial crisis, by the impact of technology or by a conscious effort to leave the transactional model and return to the role of trusted advisor.

Australians are well known for their innovation. In tough times, innovative thinking is needed to ensure Australian lawyers not only survive, but prosper. The current downturn has allowed us the impetus to re-evaluate the client-lawyer relationship to discard a transactional approach and concentrate on a value-added, advisory role. Relationships, whether external, with clients, or internal, with a firm's own staff, are at the heart of the challenges that the industry must assess – and address.

LexisNexis Whitepaper – Media Quote Sheet

Section 1

1.1 The transactional nature of client-lawyer relationships

“I think that over the next five years we will see a return to a more traditional relationship between clients and lawyers. Clients will accept that the value is in the relationship itself.”

Michael Rose, Chief Executive Partner, Allens Arthur Robinson

1.2 The historic transition from the relationship-based to the transactional model

“Billable hours drove mistrust into what were otherwise strong, trusted advisor relationships. Clients saw that law firms were focusing mostly on productivity, profit and partner earnings.”

Steve Sampson, Partner, Hunt and Hunt

1.3 The client-lawyer relationship of the future

“CEOs are starting to question why their businesses were not protected when the economy took a turn for the worse. They are starting to realise that they need trusted legal advisors who they know well. At least some groups of clients are starting to reposition lawyers in this way.”

Michael Rose, Chief Executive Partner, Allens Arthur Robinson

1.4 How can law firms instigate this change?

“We have to spend more time actually demonstrating that we are adding value to a clients business. Many lawyers are not comfortable doing this, but we must train them to be able to talk this way.”

Peter Ellender, Chief Executive Officer, Carter Newell

Section 2

2.1 Leverage

“The outsourcing of legal tasks will mean that the pool of work available to local law firms is going to shrink. As this happens, clients will choose the firms who offer real quality work. This is why I think the pressure will be on less leverage and more real engagement with clients.”

Michael Rose, Chief Executive Partner, Allens Arthur Robinson

Section 3

3.1 The billable hour

“I think we will see two sectors. One will be the value-adding, high level work where you can charge what the client should pay in accordance with the value they derive from the transaction. At another end there is a huge move to fixed price certainty. I don't see any problem in accepting fixed price in relation to a lot of transactional legal work.”

Howard Harrison, Managing Partner, Carroll & O'Dea

Section 4

4.1 Technology and the drive for value

“We need to make sure that technology is not being used to replace the intellectual side of the legal profession. Lawyers need to make sure that they are adding value, applying intellectual rigour rather than just picking up information from the internet.”

Peter Ellender, Chief Executive Officer, Carter Newell

4.2 The race to the bottom and the \$25 precedent

“The black letter of the law is no longer valued. These days legal information is readily available, but processing this information and adding value is what lawyers get paid for. Lawyers need to stop and think about the precise situation that their client is in and the precise advice they are being asked for.”

Fred Swaab, Managing Partner, Swaab Attorneys

4.3 Law without barriers

“In five years time most law firms will, in some form, have an international presence or, at least, have thought about their networks with other law firms around the world.”

Christopher Freeland, Partner / Chief Operating Officer, Gilbert + Tobin

Section 5

5.1 Recruitment, retention and succession

“The current make-up of the legal profession in NSW is 55% male and 45% female. However, the growth rate of females coming into the profession is much more significant than men coming in. Projecting forward, the number of women will overtake the men in due course.”

Stuart Westgarth, Junior Vice President, NSW Law Society

5.2 Diversity in practice

“I think there are some interesting demographic changes for this profession. Clients will demand that they have Chinese lawyers, Indian lawyers or Malaysian lawyers to deal with. However, it can be difficult to recruit these groups as they are still under-represented in Australian Universities.”

Michael Rose, Chief Executive Partner, Allens Arthur Robinson

“We tend to be focused exclusively on the gender imbalance in law firms. However, ethnic diversity and flexibility are equally as important. Historically law firms have not been adept at dealing with either of these issues.”

Nick Nichola, Managing Partner, Middletons

5.3 Minding the succession gap

“Law firms tend to have a large number of partners aged 50 or more. However, there is only a scattering of lawyers in their 40s which means that these partners will have nobody to hand over the practice to. In these circumstances, succession planning is very important.”

Graeme McFadyen, Chief Executive Officer, Trilby Misso Lawyers

LexisNexis Quotes on Whitepaper Topics

Mike Russell, General Manager - Legal Markets for LexisNexis Australia, chaired the roundtable discussion. His views on the issues raised at the roundtable are included below:

On the roundtable

“This event was specifically designed to discuss the future of the legal industry, in particular how we expect a typical law firm to look like in five years time. The legal industry has been accused of being slow to change. Be it billing, adoption of technology or an alleged lack of flexible working practices – the perception is that we lag behind the times.”

On relationships

“Customer experience is critically important in price sensitive markets. Legal practitioners must improve their customer relationships to ensure the firm has a deeper understanding of customer preferences and business needs. Loyalty-based marketing initiatives and seconding junior staff to clients at reduced rates are alternative options, but it could be that nothing but reduced costs will entice customers.”

On the impact of the GFC

“With clients demanding efficiency and greater return on investment, we can expect to see a transformation in the way that the legal world operates. It is often said that when one door closes another one opens, and this is never more true than of a law firm in an economic downturn. M&A work is dropping off while areas such as climate change, insolvency litigation and commercial litigation are becoming more of a focus.”

On technology

“Lawyers are often accused of being slow to adopt time saving technologies. Tech savvy lawyers can take advantage of matter and knowledge management tools to enhance productivity and increase returns. However, with budgets tight, will law firms invest in these solutions? If they do, firms could come out of this downturn with more streamlined and efficient working practices.”

On billing

“A recent ACLA survey¹ stated that only 3% of 125 respondents thought hourly billing was the best option, with 38% concerned it is “not very appropriate” and “rewards inefficiency”. But billable hours are a legal institution and it would be a bold move to get rid of them entirely. At the moment, there is a distinct lack of a suitable alternative.”

1 ACLA/CLANZ Legal Department Benchmarking Report 2008, available via www.acla.com.au