

Sourcing and Scoping Legal Services

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This is the twenty seventh in a series of articles about how corporate and government law departments can improve their performance and add measurable value to their organizations.

1. SECURING SPONSORSHIP FROM LEGAL

Multi-nationals such as banks, insurance companies, pharma, the full spectrum of technology companies, as well as manufacturers with global supply chains and distribution networks have complex legal requirements. The stakeholders affected by strategic sourcing for legal services can be many and varied

within the company. A successful sourcing program goes beyond managing a process efficiently to save on legal costs. To secure stakeholder sponsorship, it must actively engage primary and secondary stakeholders at key intervals.

Who Are the Stakeholders?

The primary stakeholder for a strategic sourcing initiative should be the Chief Legal



or General Counsel. As a company executive, the Chief Legal Officer can mobilize the support of key Board members, the Chief Executive Officer, the Chief Financial Officer as well as other corporate executives. There are too many instances of very elegant, and potentially effective arrangements with law firms that are eviscerated by carve-outs and exceptions. This outcome can be avoided with strong stewardship of the program by Procurement and Legal. The Chief Legal Officer's role is to identify the range of legal stakeholders across the company, secure their support, and communicate the developments and results of the sourcing process.

Two Steps

Procurement faces one of two possible dynamics in its efforts to secure sponsorship. The first is a reluctant law department that is less than enthusiastic because the company's executive leadership has mandated more systematic and cost-effective sourcing of all goods and services across the company.

The second is one where Legal is more engaged and has learned that many other companies have successfully completed legal sourcing programs – some of them over many years. Because this is a leading management practice, the CLO wants to “stay ahead of the curve” rather than react to a sourcing program that is imposed. In both scenarios, Procurement should take two steps to “secure sponsorship” from Legal.

It is no longer sufficient for Procurement to say that it can manage an efficient sourcing process and that it will negotiate better discounts on hourly rates through a competitive process with a limited number of legal service providers. That may have worked 15 years ago. It will not work in the 2020's for the relationship-based business that is legal services. This is especially true for companies that have completed their fourth or fifth wave of sourcing legal services in the last two decades.

The second step to effectively secure sponsorship is a meeting where Procurement presents its formal program to Legal. There are four parts to the program,

- a description of the *Qualitative and Financial Objectives* to be achieved during the reference period – possibly over several years,
- the *Mandate* setting out Procurement's precise role in point form,
- a detailed *Work Plan* setting out the necessary research, documentation, demand forecast / scope of legal services, the invitations for strategic partnering / RFPs, the analysis of law firm proposals, the schedule of meetings and negotiations, how best to measure the results, and
- the *Logistics and Schedule*

Procurement would be well-advised to liaise with one member of Legal when preparing the program and its presentation to legal leadership.

Roles and Responsibilities

Many companies and their law departments

are decentralized. Often, many individuals in business units and members of Legal have their preferences for specific external legal counsel and how best to instruct them. Procurement should serve as the Project Manager for the legal sourcing program. Legal should be responsible to:

- supply data and other reports on legal spend and on the historical use of external counsel by legal specialty, by business unit and by jurisdiction,
- provide insight on arrangements and agreements which may currently be in place with legal service providers,
- ensure that the other members of Legal and other business units are consulted about the forecast / demand for legal services and about their preferences for certain firms to be invited to participate in the sourcing process,
- identify a limited number of members from Legal who will be required to read law firm proposals as well as the analysis and recommendations prepared by Procurement, and
- identify those members from Legal who will attend meetings with the law firms – a maximum of four representatives from Legal and two from Procurement should be sufficient.

Apart from coordinating all communications with law firms and with other legal service providers during the sourcing process, Procurement should manage all logistics for the meetings with law firms. Experience demonstrates that success and effectiveness in sourcing and negotiating legal services depends on an intimate knowledge of law firm culture, law

firm economics, and the variety of relationships that a company has with its law firms. These relationships can range from routine to specialized to highly strategic. Procurement must exhibit greater proficiency with non-hourly fee arrangements than Legal if it is to be entrusted with negotiating arrangements with a company's legal business partners in the 2020s.

Objectives

Non-financial objectives are often as important as financial ones in the drive to source external legal counsel for formal multi-year agreements. These objectives include:

- reducing the number of law firms in order to reduce the amount of time the company's inside counsel and business units spend maintaining relationships and instructing law firms. The time saved can be re-allocated to other priorities within the company. Just changing the configuration of law firms and how they work together for greater geographic coverage. Some companies have chosen to retain a handful of firms that can coordinate local, regional and country counsel. In effect, these firms serve as general contractors of legal services,
- simplifying reporting requirements, including billing and payment protocols, in order to reduce the company's administrative load for analysis and processing payments. Under the right conditions, law firms will take on this work at no cost to the company,
- leveraging technology to achieve measurable improvements in service delivery and, possibly, in legal outcomes. Efficiency and

effectiveness are critical key performance indicators, but are often mis-aligned with non-hourly fee arrangements,

- changing the ratio of risk / reward between the company and its legal service providers primarily through the use of alternative fee arrangements,

Financial objectives in sourcing external counsel can be quite straightforward. A target should be set to reduce the projected legal spend for the ISP / RFP reference period. It is not inevitable that legal fees should increase every year simply because law firm standard rates increase. However, the pathway to achieving significant reductions in legal expenses rarely includes greater discounts or hourly-based fee arrangements. That approach offers marginal savings to companies that have had formal sourcing programs in place for more than 10 years.

Securing Sponsorship

“Securing sponsorship” means obtaining a formal sign-off from Legal for a detailed sourcing program. The program proposal must pass the **S.M.A.R.T.** test in that it must be **S**pecific, **M**easurable, **A**chievable with the available resources, **R**esults-oriented and **T**ime-bound. Procurement and Legal must regard each other as equal partners in legal sourcing. The way ahead must be clear. Accountability for specific steps must be unambiguous. Only in this way will “sponsorship” for a legal sourcing program be secured.

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2. SCOPING LEGAL SERVICES

Scoping is that portion of a Request for Proposals (RFP) or of an Invitation for Strategic Partnering (ISP) designed to inform law firms of the scope of work (SoW) in a way that can achieve a company's objectives. This is particularly important when covering portfolios of work or multiple jurisdictions over time.

Historical Data

The past is not a predictor of the future when it comes to expressing the demand for legal services. However, historical data is the first place to start. A matter management system is a superior source of data when compared to accounting data.

Still, companies that maintain a matter management system may find that some legal activity is not captured because it is a pass-through charged to customers, to insurers, to special projects or is cost-shared with other companies in the same industry.

Experience shows that asking each law firm that has been paid more than a certain threshold (e.g. \$10,000) in one of the last two years, to produce data in a uniform format will generate a more comprehensive picture of the company's historical demand for legal services. A basic spreadsheet supported by clear definitions of each legal category is sufficient to secure what is needed from firms. Ensure that the spreadsheet covers at least two complete calendar years plus as many months as possible in the current year. Data is required for each legal specialty and should be broken down according to jurisdiction or region, by legal specialty and matter complexity, and

with the total hours per year for each. In turn, the annual hours should be available by experience level for lawyers and technical staff to map practice patterns and staffing ratios for each law firm and legal specialty.

Analysis of Law Firm Data

Provided the data sourced internally and from law firms is comprehensive, then it is straightforward to determine the volume of activity (hours, number of matters), total fees and effective rate, as well as the staffing patterns for each legal specialty for each law firm by jurisdiction, and for the company and its subsidiaries for each year covered by the RFI. As part of a supporting document, law firms should describe discount and favorable fee arrangements that were applied to the spreadsheet data. For companies that retain dozens, not to mention hundreds, of primary and secondary firms across multiple jurisdictions, asking the firms to provide pricing information is more efficient than sourcing fee arrangements internally. Apart from rates, internal data may not be current or well-documented.

The analysis of the RFI data and discount arrangements should be prepared by Procurement and discussed with the law department. Experience shows that companies are seldom aware of the extent and detail of their company's external legal activity, including

- the precise number of primary and secondary firms used across the company each year
- fees, not including disbursements and taxes, paid to each firm by jurisdiction and legal specialty

- the number of matters and hours for each firm, again by specialty and jurisdiction
- variations in effective rates, discount arrangements, and alternative fee arrangements for similar work
- variations in practice patterns and staffing ratios by law firm for similar work

A comprehensive review and discussion with the law department should generate clearer objectives for the RFP / ISP including

- the preferred number of primary and secondary firms for the future
- preferred practice patterns and staffing ratios by legal specialty
- opportunities for non-hourly fee arrangements and for more favorable financial terms
- how best to formalize and improve internal protocols and operating practices governing how legal work is assigned and how it is managed with law firms
- how the law department and law firms can introduce and manage detailed matter budgets for all files over a minimum threshold (e.g. 50 hours)

Forecasting the Demand

Companies balk at divulging projected volumes / hours of work for each legal specialty and jurisdiction in their RFP / ISP. There will always be concerns that doing so can be interpreted as a company guarantee or commitment that the work (hours) will be there. For this reason, it is a common practice for the procurement process to be limited to creating a panel of qualified firms with the best possible hourly discount. Regrettably, this approach fails to leverage the data to stimulate

non-hourly pricing, innovation, and efficiency from the law firms selected. It also fails to support many of the non-financial objectives. In short, the company is not using its buying power to maximum advantage.

Determining the scope of work for purposes of the RFP / ISP should be a joint process between Procurement and the Law Department. Consider a SoW that covers at least three years. Express the demand for each specialty and jurisdiction as the total hours per year. Projections should be adjusted up or down from historical patterns, based on the law department's knowledge of work that is recurrent and work such as litigation, regulatory matters and transactions which can be irregular in its timing. Volumes can vary for each calendar year. The text of the RFP / ISP should explain the type and configuration of the legal work in the SoW.

Significant migration towards non-hourly pricing in favor of alternative fee arrangements (AFAs) which stimulate efficiency in law firms should diminish the number of hours required by the firm to do some of the work. The introduction of rigorous matter budgeting for files exceeding the defined threshold will also reduce the number of hours used. Companies have been successful in reducing the SoW (hours) by up to 15 % with the combined use of AFAs and legal matter budgets.

Four Considerations

There are important strategic and practical considerations when preparing the SoW for the RFP / ISP. The first is strategic because it addresses a non-financial objective of possibly

changing the number and configuration of primary firms. Creating a critical mass of work that is sustainable for firms over the RFP / ISP reference period means reducing the number of firms invited for proposals.

A smaller number of law firms should be kept in mind for maximum leverage. Consider that 10,000 hours per year represents a full workload for only 5.5 lawyers and paralegals.

A three-year projection in the SoW is always an estimate at best. There will be fluctuations in volume by jurisdiction and specialty from year to year. Favorable fee arrangements, even hourly arrangements, will be influenced by the amount of work the law firm hopes to receive. The RFP / ISP should state that the terms of engagement with each primary law firm will contain an annual review and adjustment mechanism which is both retrospective and prospective. Such reviews will consider variations from the anticipated scope of work and the potential for adjustments to fee arrangements.

Many law firms have at least 10 years and some have 20 years of experience with formal sourcing of legal counsel. Many legacy firms will be successful in remaining on panels and will not be at risk of losing legal work on active matters. Leading practices suggest that legacy work should be included in the SoW for the RFP / ISP, even if the same firms continue the work. Legal matter budgeting and optimal staffing ratios will usually be accepted by legacy firms as part of a concerted cost management program.

The composition of law firm panels can

change for many reasons. Lead partners leave the firm, or the law department changes its preferences, and because some legacy firms emerge from the sourcing process as comparatively too expensive. The SoW for the first year following a multi-year sourcing process should allow for a transitional period to the new panel configuration.

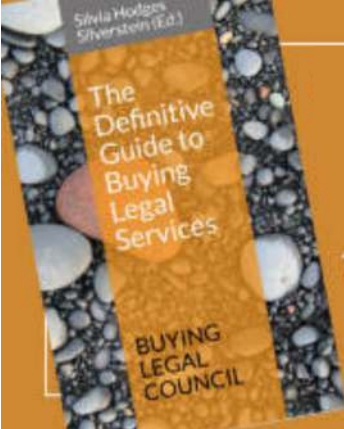
RFPs and ISPs should seek to reduce panel sizes, prescribe optimal staffing ratios by specialty, and target a reduction from current pricing. Once sourcing is complete, incorporate an annual review and adjustment mechanism. Allow for the work of legacy firms and provide for a transitional process when changing the configuration of firms or introducing new pricing arrangements.

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THE DEFINITIVE GUIDE TO BUYING LEGAL SERVICES

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