Unbundling a market

The appetite for new legal services models

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Foreword

Whether you are a buyer or a provider of legal services, this is an exciting time to be involved in the legal market. The industry faces unprecedented change. In response, companies are seeking out innovations in the way they procure, use and interact with providers of legal services.

To deepen our understanding of the critical issues, Allen & Overy commissioned independent research into how the delivery of legal services is changing around the world. The result is this report, based on the views of almost 200 senior buyers of legal services at companies with a collective annual legal budget of nearly GBP3.5 billion.

We want to share these perspectives to help you benchmark your organisation’s use of legal providers and illuminate some of the innovative, hybrid and collaborative approaches that are being adopted across the world as legal services are increasingly unbundled.

Although the landscape is shifting in many different ways, one thing is clear: the organisations we interviewed are determined to turn these changes to their advantage. Failure to meet this challenge head-on will be a missed opportunity for clients and providers of legal services alike.

David Morley
Senior Partner, Allen & Overy

Methodology and approach: This report is based on research with 198 general counsel and other business contacts at corporates and financial institutions in 27 different countries. The views of 185 individuals were captured through 20-minute structured telephone conversations. A further 13 individuals participated in a longer in-depth interview. Collectively, these organisations spend nearly GBP3.5bn on external legal services. Almost half (48%) of the interviewees are responsible for making legal decisions across their entire company or group globally. Research and analysis was conducted by Meridian West, an independent consultancy.

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An evolving legal services market: factors driving change

A host of internal and external pressures is causing general counsel to turn their attention to the way legal work is undertaken. “We are in an environment where flexibility is essential, and so we are very interested in creative approaches to delivering new services”, says the general counsel at one investment bank.

In 2012, Allen & Overy commissioned a research report “Innovation in-house: a five year retrospective” which detailed the journey GCs had embarked on to break down their siloed structure and create a commercial function that drives economic value. Since then, the pace of change has accelerated. 86% of the respondents to our latest survey say they are under pressure to deliver more value to their business for less cost. Many legal teams now face increased workloads with headcount and budgets that are cut or frozen.

This pressure is forcing legal teams to explore more fundamental change. “We are now more careful about using external legal providers: we think about it twice and tend to do more ourselves”, says the GC of a large European publishing company. This view isn’t unique. 51% of those interviewed say they have increased the amount of legal work completed in-house. Only 26% say the volume has decreased.

The consensus among in-house teams is that these market trends are structural, not merely a blip brought on by cost-cutting following the financial crisis. “The changes heralded for 20 years are finally coming to pass”, observes the CFO of a large investment bank.

CONSOLIDATION
Organisations are reducing the overall number of external law firms they partner with. 58% say they intend to consolidate further over the next three years. This is driven by a desire to have deeper relationships with fewer firms.

LEGAL TRENDS ARE GLOBALISING
53% of interviewees from the Middle East and Africa and 50% from Asia Pacific, agree that trends in other markets (namely the U.S., the UK and Continental Europe) appear in their market sometime later. That means it won’t be long before the shifts in client expectations witnessed in Western legal markets are felt as acutely in other parts of the world.

PROFESSIONALISATION OF PROCUREMENT
A third (33%) say their procurement function is playing a greater role in selecting which external legal providers they work with. This trend is even stronger with large financial institutions, where the proportion rises to 41%.

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Responding to change: appetite for new service delivery models on the up

Although organisations spend the majority (58%) of their legal budget on commissioning external legal services, our research reveals that the way this share of resource is divided up is evolving.

General counsel are reflecting on their precise needs to ensure they engage the right type of provider for the right type of work, trading off between price and quality. “Although there is pressure on us to reduce costs, it is very important for us to maintain quality”, says the head of Asian markets for a large retail bank.

In practice, this means looking afresh at the way tasks are approached, disaggregating larger pieces of work – for example, an M&A deal, a complex dispute or a regulatory investigation – into their constituent parts. It is then possible to divide work between multiple providers without compromising on overall quality.

Interviewees acknowledge that traditional law firms will always have a place in delivering complex, international legal assignments. “The need for high-value legal services in specialised areas will not go away”, says the head of legal affairs of a leading Nordic media company, a view shared by almost all participants in our research.

However, choice is increasing. Alongside the traditional firm sits a range of other types of provider (see definitions on page 5). Appetite for these new types of service is already high. Figure 1 shows that almost two-thirds (63%) of organisations have used contract lawyers in the last two years, and over a third (34%) have used document review services. Usage of these two services is highest among organisations based in the U.S. and the UK. On average, across all the services, usage tends to be highest among large financial institutions, and only organisations in the Middle East and Africa have been materially slower to adopt these.

Figure 1: Which of the following types of legal service providers have you used in the last 24 months?
When asked about their future preferences, many organisations intend to increase their use of non-traditional providers of legal services (see Figure 2). For example, over the next five years, the number of organisations using contract lawyers is anticipated to increase from two-thirds (63%) to three-quarters (74%). Penetration of document review services will increase from a third (34%) to just under half (48%). Even services where take-up is modest at the moment will increase: a quarter (24%) of organisations say they will be using managed legal services by 2019.

**Figure 2: Expected change in usage levels of legal service providers over the next five years**

<table>
<thead>
<tr>
<th>Service Type</th>
<th>Current Market Penetration</th>
<th>Anticipated Market Penetration in Five Years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contract lawyers</td>
<td>63%</td>
<td>74%</td>
</tr>
<tr>
<td>Document review services</td>
<td>34%</td>
<td>48%</td>
</tr>
<tr>
<td>Online legal services</td>
<td>28%</td>
<td>37%</td>
</tr>
<tr>
<td>Legal consultancy</td>
<td>24%</td>
<td>30%</td>
</tr>
<tr>
<td>Hybrid legal solutions</td>
<td>24%</td>
<td>31%</td>
</tr>
<tr>
<td>Managed legal services</td>
<td>18%</td>
<td>24%</td>
</tr>
</tbody>
</table>

**Models of legal services: some definitions**

- **Law firms**: Traditional partner-led law firms.
- **Contract lawyers**: Self-employed, independent lawyers engaged for short periods or a fixed term to provide flexible project support or fill an absentee position.
- **Document review services**: Outsourced organisations that review high volumes of legal documents at a lower cost, sometimes by non-legally trained individuals; often used in litigation or due diligence.
- **Managed legal services**: Contracting out all or part of the function of the in-house legal team to an independent legal provider.
- **Online legal services**: Standardised legal advice available only online; often accessed through a subscription service.
- **Legal consultancy**: Independent consultants who advise on the management and operation of a legal department or the structuring of a large piece of work.
- **Hybrid legal solutions**: A collaboration between two or more of the above providers, often combined with process and technology innovations.
The largest increases are anticipated among organisations in the Middle East and Africa and Asia Pacific regions, which will quickly catch up with peers around the rest of the world. “I can see that we would use these types of services more as they become more readily available in our market”, says the general counsel of a bank based in the UAE.

Increases in usage of new types of legal services will have an impact on how organisations apportion their legal budgets. Among the 185 individuals with whom we conducted structured interviews, the vast majority (87%) of their total spend on external legal services is taken up by traditional law firms. Just 5% of total spend, for example, is on document review services and just 3% is on contract lawyers.

However, the organisations that are early adopters of ‘non-traditional’ legal delivery models are spending a higher proportion – close to a third – of their external legal budget with these types of providers. For example, organisations that are already using document review services spend, on average, GBP4 million in this area. This compares with an average spend of GBP20.8m that early adopters spend on traditional law firms (see Figure 3).

Our analysis also shows that organisations that are actively planning to decrease spending with traditional law firms are choosing to increase spending on other providers at a much higher rate.

These trends represent a significant shift in spending patterns. As more organisations move towards a similarly diverse spending mix, this will have a fundamental impact on how legal work is delivered.

Figure 3: Average annual spend per organisation among those using the following legal service models (GBP millions)
The emergence of alternative legal service delivery models has made hybrid approaches, where legal solutions are delivered through two or more types of legal provider working in collaboration, much more achievable. 24% of interviewees say they have adopted hybrid approaches to address legal challenges in the last two years. A further 14% say they intend to do so in future.

The success of hybrid approaches depends in part on superior project management. More than half (53%) of our interviewees agree that it is challenging to coordinate different types of legal service provider efficiently. This, perhaps, explains why more than a third (39%) of interviewees say they would prefer to use a one-stop shop for legal services, which would enable them to access different types of legal services from a single firm.

“A one-stop shop, if offered efficiently and cost-effectively, would make our lives easier”, says the general counsel of a U.S. manufacturing company. “I believe this will be the future of legal services if law firms can provide this cost competitively.” Our interviewees recognise that traditional law firms are well placed to take a coordinating role, but doing so means boosting project management capabilities.

With so much change occurring, where does this leave the relationship between clients and traditional law firms? The general counsel of one multinational conglomerate spells out the challenge for traditional law firms in no uncertain terms. “The firms that sit around and think they are going to be able to just continue doing what they have done for the last 100 years are going to become redundant”, he says. “The model of the provision of legal services is being challenged now more than ever. Law firms have to constantly think about how they are going to innovate and evolve.”

Not all law firms will be able to rise to this challenge, but it is clear that failure to do so carries the risk of not keeping pace with changing client expectations.
How do these trends play out in different parts of the world?

North America
- Leading the way for using new models of legal services: only 14% agree that legal trends appear in other markets first.
- In the U.S., the litigious environment has driven a high adoption of contract lawyers and document review services.
- 48% are using document review services, the highest penetration of any region.
- This is anticipated to rise to 59% by 2019.

UK
- Pressure to deliver value is felt most acutely in the UK.
- UK companies have adopted new legal service models earlier.
- Over four in ten are planning to decrease spending with traditional law firms.
- 70% are using contract lawyers, and 37% document review services.
- The pace of uptake is significant: usage is expected to rise to 79% and 49%, respectively, over five years.

Continental Europe
- Attitudes more conservative than among other Western organisations.
- More likely to have increased work completed in-house than use new types of external legal service provider.
- Procurement plays the greatest role here: 39% say its influence will increase.
- Take-up rates of new legal service providers anticipated to be low over the coming five years compared to other jurisdictions.

Middle East and Africa
- Most likely to look abroad to adopt trends from other markets.
- Usage of new types of legal services the lowest of any region: usage of document review is just 18%.
- 59% have increased work undertaken in-house.
- 64% will look to consolidate the number of external providers they work with.
- Usage of new services to increase significantly over the next five years, but will remain behind global average.
- Strong appetite for a one-stop shop: 53% say that is their preferred model.

Asia Pacific
- Catching up fast with approaches in other parts of the world.
- Leading the way for use of managed legal services: usage is the highest of any region at 28%.
- 50% anticipate using hybrid approaches over the next five years.
- 66% find it difficult to coordinate multiple providers effectively.
- 44% have a preference for a one-stop shop model.
How do these trends play out in different types of company?

Large financial institutions

- 99% are under pressure to deliver more value to the business for less cost.
- Procurement teams more active: 41% say their procurement function is playing a greater role.
- Spending most with law firms, but also significant amounts on document review services (£5.1m on average annually).
- Among the earliest adopters of new service delivery models: 76% using contract lawyers, 46% document review services and 24% managed legal services.

Other companies

- Catching up quickly with large financial institutions in using new legal service delivery models.
- Increases of 10%, 8% and 8% anticipated for contract lawyers, document review services and online legal services, respectively.
- 35% planning to reduce spending with traditional law firms.
- 57% agree it is difficult to manage multiple legal service providers effectively.
The adoption curve: from cost-cutting to hybrid legal delivery

Based on the experiences of the 198 senior legal and business executives interviewed in this research, we have devised a model to illustrate the route many in-house legal teams take to transform how their department manages legal work.

In the first instance, organisations strengthen their internal capabilities by completing more work in-house. They then set up panels of preferred external legal advisors to obtain more consistent provision, and they seek alternative fee arrangements or discounts. Many organisations have already made significant changes in these areas.

At the other end of the curve is a vanguard of the most innovative in-house legal teams. They are using hybrid approaches involving multiple types of legal provider to streamline projects, find efficiencies and devote more attention to areas that add real value. This group is more likely to use managed legal services, and, in some instances, to explore opportunities for generating revenue by developing their own commercial legal proposition, such as through an alternative business structure (ABS) licence for organisations in the UK.

As organisations move further along the adoption curve, the importance of effective project management comes to the fore. To address this challenge, in-house teams are developing part-legal/part-commercial roles, and external law firms are being asked to play a greater role in managing a supply chain of multiple legal providers.

- Bring more work in-house.
- Create a panel of law firms to benefit from increasing buying/bargaining power.
- Agree alternative fee arrangements/discounts.
- Supplement in-house capabilities with law firm secondees.
- Greater role of procurement to drive down price.
- Explore outsourcing of volume work, usually coordinated by external law firm.
- Further consolidation of legal panel.
- Hire non-grammatically qualified project managers into internal legal function.
- More active use of alternative legal providers, coordinated by internal project managers rather than third parties.
- Use of contract lawyers to fill gaps in resource or expertise in in-house team.
- Greater engagement with document review for high-volume work, and online legal solutions and technology to facilitate more efficient ways of working.
- Complete disaggregation of tasks, allocating all legal work to the most efficient cost-effective provider.
- Greater use of hybrid legal solutions using process and technology innovations to streamline projects and find further efficiencies and cost savings.
- Explore managed legal solutions to outsource whole functions or types of work. Some operate their own managed legal solutions for other buyers of legal services.
Case study: the changing legal function at Deutsche Bank

“Although it is difficult to change something as traditional as the legal profession,” concedes Jason Williams, UK & EMEA COO for Legal Services at Deutsche Bank, “a cultural revolution is coming, albeit slowly.”

A series of fundamental changes has occurred within Deutsche Bank’s legal function in recent years. First, the volume of transactions has decreased and the focus of legal work has shifted to regulatory implementation and investigation. Second, internal legal support has become more generalised. “In a changing environment, it’s not feasible to have a specific person providing specific support on every single product the bank has,” he says.

Third, the role of the in-house legal function has evolved to provide front office colleagues with commercial, as well as legal, advice on the appropriateness of business activities. “Rather than just advising the business on how to pull a deal together, we now also say whether we think the deal should or shouldn’t move forward at all.”

What impact has this had on Deutsche Bank’s relationship with external law firms? “We will always want the very best lawyers for the job working on our behalf. However, the bank is now more conscious about how it gets its legal services, what kind of service and when.”

In 2008 Deutsche Bank began a process of interrogating its legal spend to determine how best to get the right advice for the right transaction at the right price. This resulted in the implementation of a tendering process, delivered through a technology platform called Click4Legal. This system, widely acknowledged as a market-leading approach, invites specifically selected law firms to pitch for a legal work by submitting online bids.

The impact has been significant. Deutsche Bank’s external law firms have had to re-examine how they deliver work to reduce price but maintain margin. For example, some firms have taken the opportunity to undertake higher volumes of similar work more efficiently by using expertise gained from previous matters.

Another innovation implemented by Deutsche Bank is the near-shoring of up to 20% of legal work to lower cost centres. “We have a risk threshold chart to assess the volume, risk exposure and complexity of any piece of legal work. We use this to decide whether work goes offshore and to which centre,” says Jason. This approach is supplemented by workflow management tools and online documentation management to give Deutsche Bank full oversight, control and governance of outsourced work.

According to Jason, these new approaches are gaining traction: “The US is more familiar with these types of ideas, continental Europe less so, so we have learnt to adapt.”

So where next? Deutsche Bank plans to use the data and insight obtained from Click4Legal in increasingly sophisticated ways in order to spot further opportunities for innovation and efficiency. At the same time, Jason expects law firms to respond with their own innovations.

“I think it’s incredibly important for law firms to look at their own value chains to review and reassess how they deliver different types of legal work. I’m optimistic that we’re on the right track, with no U-turn in sight.”
Embracing change: key takeaways for your organisation

Our research has confirmed that change is underway in all parts of the legal market. Although the pace and depth of change is unique to each individual organisation, the broad trajectory of change is constant. We summarise the learnings from our research into five questions that the most innovative in-house teams are grappling with right now:

1. **Balance**
   - What is the most effective balance between completing work in-house and with external legal service providers?

2. **Process**
   - How can you approach legal processes differently? Where are the opportunities to disaggregate tasks between different legal service providers?

3. **Technology**
   - What role will technology and intelligent systems play in driving innovation within your legal function?

4. **Hybrid**
   - Where can you introduce more hybrid approaches to legal work – combining different services, process and technology into new solutions?

5. **Coordination**
   - How can you coordinate multiple legal service providers more effectively to ensure efficiencies aren’t lost through poor project management?
Case study: A&O’s Legal Services Centre

The scale and complexity of litigation disclosure exercises has driven streamlined and cost-effective alternatives to traditional legal resourcing. In response, A&O has harnessed these new ways of working, brought them in-house and is also applying them to transactions.

Typical disclosure exercises can involve many hundreds of thousands of documents, email chains, chat-room messages and audio files. The pressure to manage costs is enormous.

In 2012, A&O created a Belfast-based Legal Services Centre (LSC) that specialises in first and second stage document reviews of large cases, supporting A&O offices around the world. Belfast benefits from a highly educated workforce and competitive costs – one-third lower than those for London-based lawyers, for example.

When a document set is particularly large, A&O may outsource the first stage review to a legal process outsource provider (LPO), with the LSC quality-checking a percentage of the LPO-reviewed documents to manage risk and ensure quality. The result is a ‘hybrid’ resourcing model which delivers the same A&O quality but utilises the most cost-effective solution for each stage.

Methodologies developed for disclosure exercises are now being utilised on transactional due diligence. For example, the LSC employs workflow technology and sample-based extrapolation techniques to assist with large document review exercises and due diligence on purchases and sales of loan portfolios for major financial institutions.

Effective project management supported by technology is vital. A&O has developed its own systems to manage the workflow of lawyers submitting information from different geographies and to provide an audit trail and real time status reports.

A&O’s legal expertise has been applied to developing techniques that collect and store legal information as data, rather than lengthy legal opinions, to enable fast, efficient and accurate analyses of highly complex data sets.

By employing its own people in Belfast to conduct review tasks, A&O can rely on judgement calls made to minimise costs and enable those leading the case to concentrate on the overall strategy.
A&O’s strategy for an evolving industry

Allen & Overy has been investing in new services to evolve its business model and help clients meet the ‘more for less’ challenge. This global survey underlines the benefit to our clients of thinking radically.

Of the six new legal services that this survey examined, A&O has invested in five (see next page). Some are mature offerings, others are at early stages, but the findings of this survey confirm that we are pursuing the right strategy and should do so with vigour.

Figure 4: To what extent do you agree or disagree with the following statements about Allen & Overy?
Proportion saying ‘agree’ or ‘agree strongly’:

<table>
<thead>
<tr>
<th>Statement</th>
<th>Proportion</th>
</tr>
</thead>
<tbody>
<tr>
<td>A firm like Allen &amp; Overy offering multiple models of legal services would be an appealing proposition</td>
<td>81%</td>
</tr>
<tr>
<td>This approach sounds credible for Allen &amp; Overy</td>
<td>75%</td>
</tr>
<tr>
<td>This approach sounds distinctive</td>
<td>57%</td>
</tr>
</tbody>
</table>

We also asked about the brand impact of a high-end law firm providing these types of services. Two-thirds of the respondents (66%) believe it will have either a positive or neutral effect on our brand. 15% say it would greatly strengthen the A&O brand. Many comment that it plays to our strength in innovation and would position A&O as a market leader.

A clear consensus emerges: A&O signifies premium-quality legal services. People are open to using the firm for non-traditional services and are attracted to a one-stop shop solution, but only if that same stamp of quality is guaranteed.

“Innovation will not come from A&O simply expanding these new services and running them all as separate high-quality businesses under the A&O brand. The value to our clients will be in combining these services alongside high-end law firm work. A matter, for example, may require consulting, contract lawyers and document review, together with technology and business processes to create a totally different, joined-up legal solution.”

Jonathan Brayne, head of A&O’s Innovation Panel
A&O’s ‘non-traditional’ legal services

**Document review**

Our Legal Services Centre (LSC) in Belfast is led by an experienced partner and comprises junior legal professionals handling transaction-related work including document reviews, drafting and research tasks. They are supervised by qualified associate solicitors, each with at least six years’ post-qualification experience. The legal professionals are top-quality law graduates who have completed an intensive Business Law programme, designed and delivered by the College of Law and A&O.

**Online legal services**

Derivative Services, established over a decade ago and serving over 185 institutions, provides online subscription products to help clients reduce legal, regulatory and operational risk. The products codify A&O’s unique legal expertise and cover all aspects of derivatives trading and key compliance issues, such as shareholding disclosure, marketing restrictions and cross-border data transfers.

**Contract lawyers**

Peerpoint, A&O’s flexible resourcing business, was launched in late 2013 in London. Peerpoint provides a panel of experienced, high-calibre lawyers available to work flexibly on contract for Allen & Overy. Within a year, once Peerpoint reaches a critical mass, it will also offer clients direct access to A&O quality lawyers for temporary placements or for specific projects.

**Legal consulting/hybrid solutions**

A group of ten A&O partners is developing a consulting-style approach to solving our clients’ legal challenges. We are deploying technology, business process and project management to combine traditional law firm services and new legal services into hybrid legal solutions.
GLOBAL PRESENCE

Allen & Overy is an international legal practice with approximately 5,000 people, including some 526 partners, working in 44 offices worldwide. Allen & Overy LLP or an affiliated undertaking has an office in each of:

- Abu Dhabi
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- Antwerp
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- Bangkok
- Barcelona
- Beijing
- Belfast
- Bratislava
- Brussels
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- Budapest
- Casablanca
- Doha
- Dubai
- Düsseldorf
- Frankfurt
- Hamburg
- Hanoi
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- Luxembourg
- Madrid
- Mannheim
- Milan
- Moscow
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