

Adapt or perish

Technology, globalization, liberalization – how to survive the second wave

By Dr. Bruno Mascello

All sectors are faced with the challenge of digitalization; and the legal market is no exception, as borne out by the fast-growing number of conferences on “LegalTech”. This article does not want to analyze the impact of technology on the law, but look instead at the business of law, i.e., the operations required by law firms and legal departments to provide legal services. There are many challenges to consider when planning a strategy and drafting a business model to position oneself better in the legal services market. This becomes even more challenging against the backdrop of lawyers having been educated to handle threats and risks rather than look for business opportunities.

Current trends in a nutshell

Even though LegalTech currently seems to be at the forefront, it is certainly not the only trend to consider. The legal market is driven not only by technology but also by globalization and liberalization trends. The economy and customers are growing into new markets and the lawyers’ former

monopoly is steadily shrinking. Further, with regard to the still important market of (human) lawyers, one must consider that soon the baby boomer generation will retire, the new generation is already knocking on the partners’ doors, and the war for talent will be even fiercer. Then, customers and their legal departments will be faced with a continuously growing number of legal risks and regulations in all industries; in addition, the more-for-less challenge and the pressure to run legal operations more efficiently (including managing outside counsel) is accelerating. Finally, law firms will experience new challenges, such as difficulties with the traditional business model (often based on an hourly billing model paired with a leverage effect), decreasing profitability (per partner), and a growing number of traditional and alternative competitors.

Customers – the biggest competitor, so far

Until a few decades ago, outside counsel was the only option for legal services. As long as customers’ demand for legal ser-



The vast, deep sea of digitalization: The legal sector is facing a big challenge here.

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vices was growing faster than the steadily increasing number of lawyers and law firms, there was no real risk to outside counsel. However, this view overlooks the fact that one particular legal service provider has been growing continuously over recent decades: customers’ legal departments. Since the 1970s, companies

have started to increase their internal legal resources. Today, a customer spends some 40% of the overall legal budget on internal legal resources; and, depending on the country, industry or size of the customer, it can be much more. Moreover, when considering the workload that legal departments absorb, they deliver →

some 75% of a customer's overall legal work. Consequently, law firms have lost substantial ground as exclusive first-hand legal service providers, and customers have shown that they are willing to take the lead. It must be emphasized that while this trend is ongoing, so is the tendency to insource previously outsourced work.

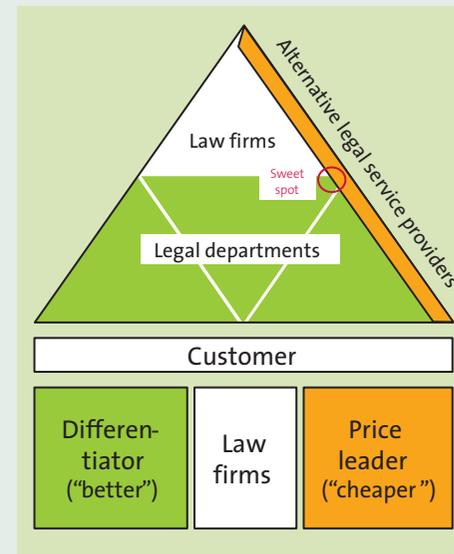
Alternative legal service providers – the second wave

The first wave, led by the legal departments, is now followed by a second one, which is becoming increasingly relevant. This second wave was triggered by the “alternative” services providers, so called to distinguish them from law firms and legal departments. They consist of all other providers of legal services to individuals and corporates, such as financial-services companies, legal-protection insurers, the Big Four, and, last but not least, the mushrooming “NewLaw” and LegalTech providers. All these alternatives to law firms are of interest to customers for various reasons: They are either better, faster, cheaper or simply more convenient to buy from. They focus only on a small part of the value chain and provide this service extremely well. Furthermore, they are powered by process knowledge and technology – two skills that are not natu-

rally attributed to traditional law firms. It is expected that alternative legal service providers will move up the food chain to claim the more attractive customers and mandates.

A series of missed opportunities

When we look at the success of legal departments, it is worth looking at just some of the unsatisfied needs of customers. For example, customers started to establish law-firm panels mainly to reduce the time it takes to instruct outside counsel and to increase control over legal fees. Calls for alternative fee arrangements are the result of the fact that customers are dissatisfied with the hourly billing system, which shifts the business risk to the customer. This dissatisfaction has meanwhile also spilled over to general counsel, who need to cooperate with procurement. Also, law firms did not like to grant secondments to customers only based on a cost-plus basis, which enabled new temporary employment companies to step in and grow. Now they have, and can indeed exploit, valuable direct contact with customers. Other customer requests – those related to compliance, risk management and project management – are being used as a gateway to legal services, particularly by the Big Four. These few examples show that many



Legal departments as first wave and ALSP as second wave

opportunities were not used by law firms, which left the way clear for others.

LegalTech as the next (missed) opportunity?

LegalTech is not about replacing lawyers, but changing their roles and mandates. Law firms do not seem to be optimally positioned: They are neither better nor cheaper than legal departments, nor are they more efficient nor cheaper than alternative legal service providers. Therefore, law firms need to question how to position themselves in terms of the digi-

tal challenge. Technology, alternative legal service providers and, most importantly, also customers and legal departments as well will continue to develop and react to what the market is offering. They will not wait for law firms to come to a decision, and law firms do not have a “right of first refusal.” Considering the attitude shown by law firms in the past, I fear that they – deliberately or otherwise – will again miss these opportunities and either pass them back to the customer or, even worse, offer them to their competitors for free. Keeping in mind how legal departments cornered the legal market in a first wave, the growth of alternative legal service providers has the potential to become a second wave that will shift the market substantially yet again.

Strategic positioning is key

Law firms need to pay attention to three key points: First, there is nothing wrong with focusing on traditional lawyer services and disregarding new opportunities and competitors, as long as this is a deliberate decision. Lawyers can focus on key strengths, such as personal interaction with customers, legal assessment and counseling, representation of customers, and negotiation of transactions. Such a strategy implies accepting that lawyers are reduced to such key →

tasks and risk losing clients to alternative providers. Second, a law firm must decide whether it wants to position itself as a cost leader by offering cheaper services, or as a differentiator by providing a better service than an alternative provider. Third, a law firm must decide how to react to LegalTech and the ascendancy of other legal service providers.

New business models required

Disregarding alternative legal service providers does not seem a reasonable option. A law firm may choose to create some digital services itself, but this does not seem reasonable considering the expected lack of skills in law firms and the big investments anticipated. What remains is the option of cooperation between law firms and alternative service providers. Law firms could bring existing trusted relationships with

customers to the negotiating table and the alternative service providers could contribute their technology and process-driven expertise. In this way, customers would be served by a one-stop shop, resulting in a win-win solution for all stakeholders.

Today, legal service providers have the chance to act as game changers with regard to this second wave in the legal market. It is now up to them to decide how they want to position themselves and whether and how to react to the potential opportunities and threats. There are interesting times ahead and it remains to be seen what the most promising strategy will be. ←

Editor's note:

A longer version of this article in German can be found in: Anwaltsrevue, 1/2018, pp. 18–24. (tw)

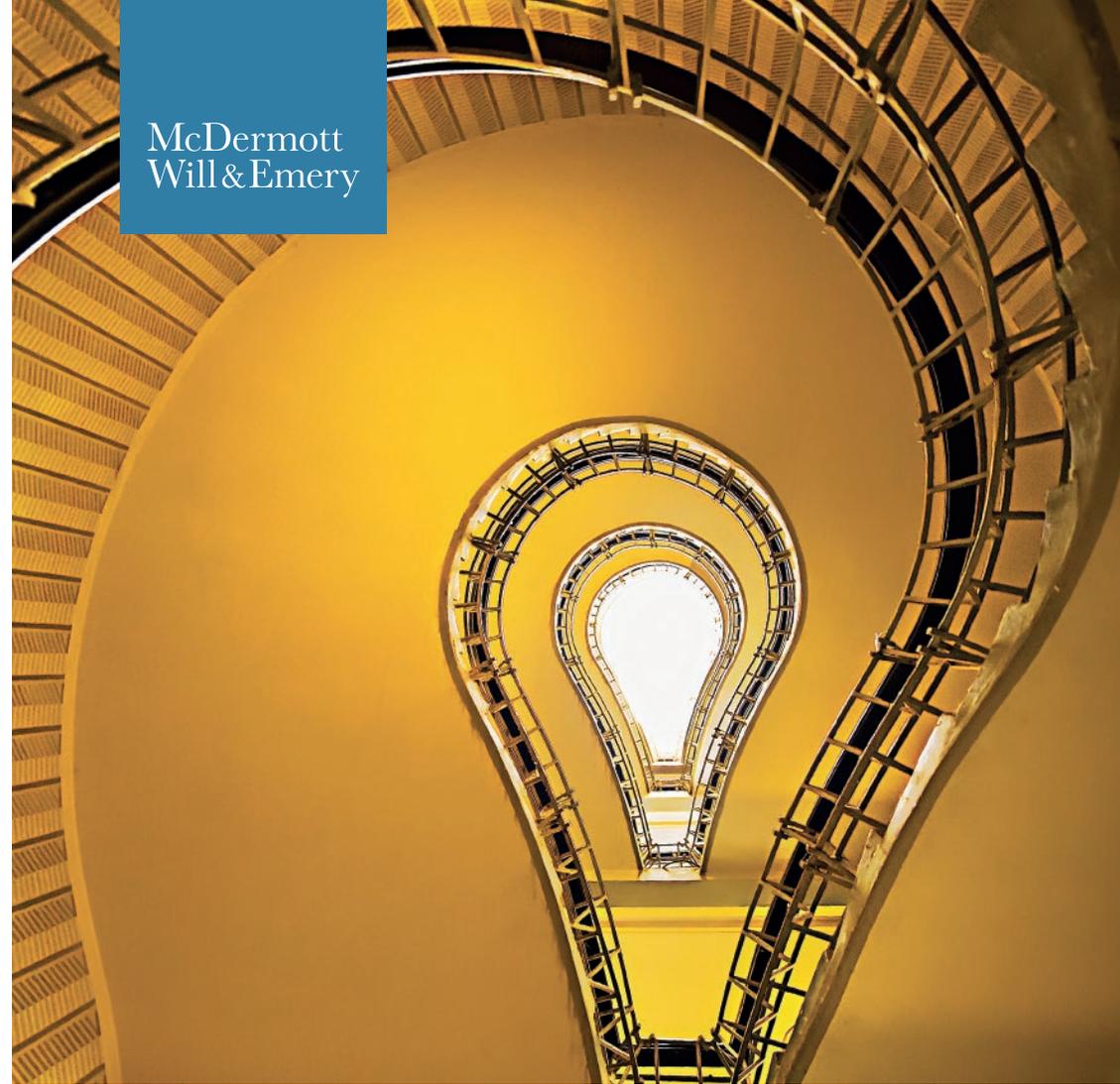


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