

**STRATEGIC STRENGTHS:
THE BASIS OF AN EFFICIENT DESIGN
FOR A CORPORATE LEGAL FUNCTION**

by

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STRATEGIC STRENGTHS: THE BASIS OF AN EFFICIENT DESIGN FOR A CORPORATE LEGAL FUNCTION*

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Corporate law departments are expected to manage the legal affairs of the companies in a cost-efficient manner more today than ever. Many departments have undertaken recently quality programs; they applied considerable resources to seeking the opinions of their internal clients. One message that they heard was very clear: the cost of legal service is too high, not only in absolute terms, but it is often too high in respect of the value that the clients perceive it provides to their business operations. Moreover, clients often expressed frustration at the near-total absence of data about the cost structure of those services.

As a result, in-house counsel are searching for ways of reining in those costs. Their efforts to date have been only moderately successful. They have depended largely on things such as negotiating lower hourly rates, refusing to pay for certain services (such as overtime word processing) and imposing ceilings on certain expenses.

Many departments have reconfigured their own staffs in an attempt to effect the ideal structure. Some companies have completely outsourced their law departments. Other companies have reduced their internal staffs considerably, with the legal work devolving on one or more outside law firms. Still others have implemented a very different solution — they have increased the size of internal staff and brought work in-house.

The variety of answers that different companies have identified when addressing the same questions suggests that there is no “right” one. What works for one company does not necessarily work for another. The degree to which a solution can be effective varies from one organization to the next. In other words, the solution is very specific to the situation.

I. Analyzing the Legal Function

Though there is no “universal truth” as to how to organize a company’s legal function, there are some basic approaches that are useful in crafting the appropriate structure. These approaches reflect a consistent theory of legal service function. By following this theory, a company can identify the right formula for its own success. It can design a legal function that serves its needs.

This conceptual tool can be applied by in-house counsel to address the questions that surround their companies’ use of legal talent (inside and outside). Adhering to a consistent theoretical construct can provide continuity to the development of the companies’ legal function over time. The application of this strategy will, of course, vary from situation to situation, but the framework has broad application.

Once the legal function is so designed, the implementation of that plan can be undertaken with more confidence that the various parts will complement each other better than they might have had the function grown without a consistent theory. That plan can also guide further development of the legal function, as a company’s needs change along with its business and with the environment in which it operates.

What is that theory? What does it offer that can help in this analysis?

You must analyze a company’s legal function systematically. You must proceed from the premise that all the company’s attorneys — inside and outside the company — together comprise the legal function. The analysis is of the entire legal function.

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Then, you need to understand the full breadth of the law department's role. What does the company want from its legal-service providers? Do the company's executives want very proactive lawyers, who are expected to search out legal problems, or to identify unexploited opportunities for the company in changing laws and regulations? Are the attorneys expected to provide legal service only in the context of new transactions, and only in response to litigation filed against the firm? Do the law department's responsibilities include those related to compliance?

Once you understand that background well, you need to identify the need for legal services with some specificity. What sorts of legal work will be needed? Is it exclusively transactional in nature or does it involve litigation and other disputes? How does the scope of that need vary geographically? How much does that need vary over time?

When you have a general idea of the types and degree of variety of the legal work needed by the business (as to volume, substantive areas of law, etc.), you can begin to determine how that work should be provided and by whom. Should in-house staff be the primary or sole source of that service? Should you forgo in-house expertise and place sole reliance on outside counsel? Should you utilize both in-house and outside expertise? If so, in what mixture? How can you assure the maximum effort with the minimum duplication of effort?

The answers to these questions will vary tremendously from one company's situation to that of another. While at first blush that may be somewhat frustrating, it also provides a hint as to how to approach those questions.

The first step is to delineate the responsibilities of the legal function. To do this, you must explore the expectations of the senior management of the company as to how the company's lawyers (whether inside or outside the corporate structure) should serve their needs. In-depth interviews of senior executives are the best means to secure this perspective. Their views not only represent the "official" line, but they also shape the attitudes and expectations of lower-level staff, where most of the work is actually conducted and with whom the attorneys have greater daily interaction, as a group.

Don't ignore the views of middle- and lower-level

managers and staff, however. In daily exchanges between staff and attorneys in the course of business, the expectations of the staff as to the role of the attorneys will have a very significant impact on what the attorneys actually do, and what it will cost. You must fully understand the constraints that can affect how the legal service is delivered. A survey of some staff and possibly some representative interviews might be worthwhile.

Once you have a grasp of the general function of lawyers for the company, at least in terms of the expectations of the company's managers and other employees, you need to analyze the legal needs of the company from a substantive perspective. What fields of law are relevant to the company? This requires some understanding of the company's business. Assuming that you are examining the legal affairs of a well-established business, you should first review the company's historic use of lawyers. The first source of information is the past payments for service from law firms. A review of invoices can yield much helpful data, not in terms of the fine detail of the time entries and expense payments, but in terms of aggregate costs of various types of legal service and the variability of that service. Does real estate law predominate in the company's legal needs? Is the firm often involved in prosecuting patent applications or protecting intellectual property rights?

Where is that legal talent applied or purchased? Is it concentrated in a very small geographic area? Is it spread evenly across the country? Does it vary with the type of legal service in question? The answers to these questions can impact the final design of the legal function. If a particular substantive area of law arises across the country in the context of litigation, you might need more outside firms with established expertise in that field. A single in-house attorney with that substantive expertise can serve as coordinator. If the same substantive area occurs in transactional contexts only, one or a small number of firms may be needed, with a larger number of in-house lawyers with that expertise.

You can't ignore the past staffing levels inside the law department. How many attorneys have been on staff? What sorts of service have they provided? Was it all counseling, or a combination of counseling and transactional work? How much and what type of involvement did they have in the company's litigation? Are there any relevant staff constraints?

Through interviews, you need to get some sense of whether past staffing levels were adequate for the work. Here, the perception may be as important as the reality. If, through interviews, you learn that staffing was historically thin, you might discount time records that suggest the opposite. Speak with the in-house attorneys as well as the company's senior executives. Ask the line professionals whether the legal staffing was adequate for their day-to-day needs.

It might be useful to observe some typical days for the in-house staff. Reality may be different from what records indicate, as many people cannot or do not keep track of every emergency phone call or of each short-lived interruption. The aggregate of all those unanticipated interruptions can be a substantial portion of the day and they can say more about the workload than timesheets and invoices. The latter provide useful perspective, though.

How is the work accomplished? Does the legal staff closely supervise outside counsel or has it adopted a more hands-off approach? How detailed is the direction that it provides the company's outside law firms? Has the company prepared and disseminated guidelines for its outside firms? If so, how well were they followed?

Once you clearly understand the types, amounts, and locations of the legal service the company has needed previously, you have to measure the company's anticipated needs. As businesses grow and develop, their needs change. Business plans will have tremendous implications for future legal needs. Even if you know what the company's business plans are, however, your estimates as to future legal needs are merely educated guesses. Those needs are notoriously difficult to predict with any degree of certainty. Nonetheless, you need to include some analysis of those projected needs based on the company's intended plans in order to fully explore how the legal service should be structured.

Again, interviews with the management of the company are important to understand that issue. Further, by clarifying to those executives why you are exploring that question, you simultaneously accomplish two things: you gain an understanding of the company's future needs for legal service; and you educate the executives on how those business plans can impact the

company's need for legal assistance (*i.e.*, you practice demand management). The same two goals should animate all the interviews that you conduct with the company's nonlegal staff.

Has the company previously forecast its needs for legal service? If so, how accurately did it do so? How reliable are those data? Can they be used again?

II. Determining Inside/Outside Staffing Needs

After completing that investigation and analysis, you should have a good understanding of the legal needs, present and (to some degree) future. Those needs should reflect the types of legal service needed (*e.g.*, substantive areas of law, litigation versus transactional versus counseling needs, geographic variation, etc.).

The next step is to convert that understanding into an estimate of how much of each of the various types of legal service will be needed and where. In many cases, only a very rough estimate can be made after the initial analysis, but as time goes on you can refine that estimate to make it more accurate. To some degree, you are trying to translate that estimate into "attorney equivalents." In other words, how many attorneys will be needed to provide the services that will be called for? The more widespread those needs are in geographic terms, the more you might find that the needs increase in terms of head count (even for the same amount of work), because it is more difficult to achieve economies of scale over wide distances.

The translation into "attorney equivalents" is a very unscientific process. Seek opinions from disparate sources. Speak with the company's outside lawyers, among others. Compare the "attorney equivalents" that you calculate with comparable calculations of past legal usage. This can serve as a "reality check" for your computations.

Once you have identified the total need, how can you determine whether those services should be provided with in-house staff or outside lawyers? The most efficient and effective team is one that takes advantage of the strengths of its members. Accordingly, you need to understand the respective strategic strengths of inside

and outside counsel. Match those against the particularized needs of the company.

What are strategic strengths? They are inherent attributes that distinguish one party from others and that contribute value to that party's performance or role. Those attributes might result from the organizational "place" of the specific person (inside counsel as opposed to outside counsel, for example). Some of them derive from personal characteristics of the individual (some people are more capable than others of the type of analysis that is necessary in litigation).

If you identify the strategic strengths of the members of the legal team, you then can harness each member's strengths so as to achieve more than would otherwise be possible. There also may very well be some identifiable weaknesses for which you need to compensate in your planning. On a properly staffed team, the members' skills complement each other.

What are examples of the strategic strengths and comparative weaknesses of inside counsel? Inside counsel generally works closely with a company's business executives and managers on a day-to-day basis. In the course of that daily toil, a staff attorney develops a strong appreciation of the business's needs. That understanding enables that attorney to anticipate how the company's legal position (in litigation or otherwise) might later impact the company's operations. He or she will have a sense of which cases might be problematic for the corporation because they might have a very adverse precedential impact on those operations. An outside attorney might not be as able to make that determination.

Inside counsel generally enjoys greater proximity to the operational personnel of a company. That can be a strong advantage in order to fulfill certain responsibilities. One important responsibility of inside counsel is to counsel the business executives and managers on risk. This counseling is best administered over time, in large and small doses as the opportunities present themselves, often unexpectedly; as a rule, it is not as effectively accomplished merely by infrequent, formal presentations. Gardens respond to continuing, low-volume watering better than they do to infrequent gully washers. A due appreciation for legal concerns should be similarly nurtured.

Generally speaking, the attorneys who are on the staff of a company acquire over time experience representing the company in a variety of contexts and in connection with a variety of initiatives of the company. Whereas outside counsel are typically retained for discrete assignments (*e.g.*, to handle the sale of a property, to represent a company in connection with a corporate acquisition, to represent the company in a particular case, etc.), the role of inside counsel spans all the situations that might confront the firm. This creates two distinct strengths of inside counsel: the development of "institutional memory" over time that provides some context and foundation for subsequent situations; and the opportunity to measure the company's responses in those varying contexts, providing a more "textured" understanding of the company's needs and preferences. All this animates the inside attorney's representation of the firm. It allows that attorney to view each problem and situation in relation to other situations in which the company has found itself in the past, in which it finds itself at present and in which it might find itself in the future.

Another strength of inside counsel, which is related to several already mentioned, is that he or she typically has or acquires a greater commonality of perspective with the business client than does outside counsel. This often manifests itself in a greater appreciation for cost effectiveness or as a sharing of the business goals, by virtue of which the attitude of inside counsel is usually different than that of outside lawyers (this is not a criticism of the latter, merely an observation).

On the other hand, in-house counsel are generally subject to staffing constraints. They are often geographically removed from the courts and agencies with which they deal. They may lack the bar admissions necessary to fully perform certain assignments, since corporate lawyers generally do not secure admission in all states in which their employers conduct business or in which they might have to avail themselves of the courts. In those situations, companies must retain outside firms that have the requisite admissions.

What are some of the strategic strengths and relative weaknesses of outside counsel? First and perhaps foremost, a law firm exists because of the attorneys who comprise it. As self-evident as this may seem, it is significant in this analysis. The attorneys of a firm direct

its activities, and its structure is designed to support its mission of providing legal service. In the case of litigation, for example, a law firm is configured to participate in the litigation process; a law department, on the other hand, is only part of a company, and the company's *raison d'être* is not defined so singularly. The demands for the services called for in the practice of law are not outweighed in a law firm the way that they may be in a corporate environment. An inside attorney might have to grapple with corporate procedures and other concerns in order to secure appropriate contract assistance for litigation, for example. Such concerns are less significant in a law firm and the end might be more easily achieved.

The single focus of a firm creates other strategic strengths. Outside counsel is likely to be viewed as functioning solely as a lawyer in respect of corporate clients. Some courts view an inside attorney, on the other hand, as serving the company as a businessperson as well as a lawyer. This has implications for the availability of the attorney-client privilege and the attorney work-product doctrine (even though the analysis as to the availability of the protection is the same), since the commingling of functions can undercut the protection that some courts will accord communications and materials otherwise protectable.

On the other side of the ledger, the cost of in-house counsel is typically lower than that of outside attorneys. A law firm is a profit-seeking organization. Its client charges are intended to provide its owners and members with a return above their subsistence needs. On a purely comparable basis, then, a company should be able to save money by having the same services performed in-house.

There are several issues relevant to that determination that flow from the differing statuses of inside and outside attorneys, however. The final determination of whether hiring staff is the cheaper alternative to retaining comparable outside attorneys is a more complex analysis than simply comparing the relative hourly rates. For example, even though more and more companies are explicitly disavowing any guaranty of employment (often expressing an assurance of employability but not employment), an in-house staff of attorneys represents an ongoing financial commitment. By retaining a law

firm instead, a company can preserve greater flexibility for fulfilling its legal needs. The commitment to pay fees is limited, generally, to the services already performed, rather than for employment expectations reaching into the future. The financial obligation to outside counsel may be more easily ended.

Outside counsel often have geographic proximity to entities outside the company that are relevant to the company's legal affairs. A prime example is the court systems with which we must deal. In-house lawyers are often located with or near the business operations, regardless of whether that is convenient for dealing with courts, government agencies or any other constituencies that are external to the corporation. Law firms, on the other hand, often locate near the entities with which they must deal frequently, whether those are courts, agencies, or other outside attorneys. Familiarity with court procedures and the vagaries of administrative interpretations of statutes and regulations is often greater in law firms than it is in law departments, as a result.

Inside counsel have reporting mechanisms that are more closely geared to the company's needs. Whether as to budgeting or as to litigation reserves, management expects timelier reports from inside counsel than they generally do from outside counsel. They often expect the latter to report on a schedule that is less frequent.

Outside lawyers represent multiple clients. Each client benefits from that diversity because lessons learned in one client's context can be applied in another's. That diversity can have negative effects for each client as well, however. Despite the best of intentions and the most professional approach, a firm's multiple representations can restrict its pursuit of a particular client's interests, even unintentionally and perhaps only marginally.

There may be other, less obvious issues that can impact the analysis. For some companies, the costs of inside and outside counsel might have disparate ramifications. For example, companies that manage funds on behalf of third-party investors might be able to charge the time of outside attorneys who handle legal issues for those investments directly to the investment accounts. The internal cost of in-house counsel might not be

reimbursable. Each company might have different preferences as to the size and makeup of its staff. Such complexities aren't subject to generalization in a treatment such as this.

III. Putting It All Together — Designing and Implementing a Seamless Team

How can a law department take advantage of the respective strategic strengths of inside and outside counsel? The objective should be a "seamless" team of attorneys, some inside the corporate structure and others outside, who provide their common business clients with the needed legal service, whether that is advice and counseling, litigation representation, or transactional work.

The critical step is for the attorneys to communicate with each other as to their respective roles. They must have a common understanding of what each of them will do so that together they provide the complete service. Their roles should reflect their distinct strengths, so as to maximize the effectiveness of the legal representation while avoiding duplicative work as much as possible.

Let's examine some of the tasks necessary in the litigation context, for example. Inside counsel's familiarity with business personnel, office locations and the structure of files can be very useful in planning the company's litigation posture, and in responding to discovery demands from the adversary. Outside counsel is more familiar with the rules of discovery and with the preferences of local courts and, sometimes, the adversary's counsel. That familiarity should enable outside counsel effectively to advise inside counsel on the scope of discovery demands, and the company's obligations in response to those demands. The initial screening of files and the location of witnesses, information and other material can be completed by inside counsel, and outside counsel can then review that material for production. By dividing between them the discovery-related tasks in such a way as to maximize their respective strengths, inside and outside counsel will be able to most effectively complete that operation.

The different perspectives of inside and outside counsel can be useful in litigation in other ways as well. Outside litigation counsel is a "hired gun," whose

reputation should be one associated with an adversarial posture. Settlement overtures might be perceived by an opponent as undercutting that posture. If such overtures are made by inside counsel, however, a company can preserve the outside attorney's "bulldog" reputation, and the inside counsel can appear as the more reasonable representative of the company. This dichotomy can be a useful tool if effectively wielded.

In the litigation context, the attorneys must have clearly defined communications channels between them. In litigation, one often has to respond quickly to unanticipated developments. In those situations, it can be critical to avoid delays in getting the information to the appropriate person, for consideration of a position to take or for some other purpose.

The analysis of the legal function should not ignore the role of the business client. Too often, the legal needs of the company are analyzed in isolation from the business staff. In reality, the actions of the operations staff have great significance for the legal service. Ultimately, almost all disputes arise in business relationships. Their resolution can be achieved effectively only by taking into account the business ramifications of the legal positions advocated. Moreover, lessons are more easily learned and applied in the business (so as to avoid repeating actions that led to disputes) by those who have been involved in dealing with the aftermath of those mistakes or actions.

The cost of legal service is similarly impacted by the actions and inaction of the business staff. Only if the business staff understand their role in securing the proper legal advice, and the impact that their actions can have on the scope and cost of that advice, and service can the law department be effective in addressing the issues discussed here.

In essence, this is a question of demand management. Educating the consumers of legal service as to its costs and as to their ability to impact that cost can create incentive for them to reduce their use of that service. Business personnel must also understand that the sooner legal advice is applied in business situations, the more effective it often can be. A well-designed legal function will find that fine balance between those two opposing forces.

In order to be accepted and to be effective, a company's legal function must take into account its impact on and the impact on it of business activities. This requires that both the lawyers and the business executives be educated, each by the other.

Once the basic legal function is understood, you need to analyze ways in which it is performed and ways in which that performance can be improved. Issues related to technology and teamwork come into play.

How much is technology already used in the legal function? Do the attorneys, inside and outside, rely extensively on electronic communication? Do they have other technology tools that can improve their performance? For example, can they apply groupware that enables them to collaborate more effectively? If they have such tools, do they use them effectively?

Surveys of available technology are useful in this inquiry. Interviews can be invaluable in determining how effectively the available tools are in fact applied in practice.

How much information do the lawyers share with each other? How often and well do they communicate? With what tools? Does the relationship between inside and outside attorneys reflect a true partnership, in which they are interdependent and trust one another fully? Do they share the goal of providing the most cost-efficient legal service feasible, perhaps even forsaking short-term goals in favor of long-term ones? In-depth discussions may be the only means of learning this because you need to get behind the facile answers often given to such questions in a survey.

With all this information about past usage and anticipated needs, as well as an appreciation of the scope of the legal function, you can move to the next critical steps — design and implementation. Much of the design should be clear from the data developed. The implementation, however, requires more than abstract analysis. It is a test of client-management skills and of the dynamics of interpersonal and organizational relationships.

The design should encompass the internal and external components of the legal function — the in-house staff and the outside firms. When you have clarity about

which tasks are better performed inside the legal department, and which outside, you are able to select the types of legal talent to best perform them. That could mean more legal assistants on staff than has been the norm. It might mean attorneys or staff with the appropriate experience to provide clients the on-site, day-to-day counseling they need and rely on, with much of the drafting and nuts-and-bolts legal work performed by law firms under their direction.

Determining how many attorneys, legal assistants, and support personnel are appropriate is an inexact exercise. In establishing internal staffing levels, it is generally appropriate to err on the side of fewer, rather than overstaffing. Try to estimate how much work will be performed and of what types. Convert that estimate into an approximate staff count, expressed as "full time equivalents" or similar "units." (Actually, the units will be for the various types of staff — attorneys, legal assistants, secretaries, clerks, etc.)

The amount of outside legal service, even if estimable, will be similarly imprecise. There is somewhat greater flexibility in securing the appropriate amount of service, however, since the company need not commit to or guaranty any particular volume of work. It should pay only for what it needs.

You can try to achieve efficiency by means of well-designed fee structures, however. The fee arrangements should be structured so as to align the law firm's interests with those of the client. Hourly rates do not reward efficiency. They lead to greater profit for attorneys who are inefficient and take more time for the same work. If the hourly rate declines as the number of hours increases, however, that particular effect can be reduced. Alternatively, a fee structure that totally eliminates the hourly rate as a determinant of the total cost can create incentives for the law firm to be efficient. You must be careful of creating disincentives to effective lawyering, however.

The design of a legal function must take into account many concerns. All elements of that function can be designed to achieve the desired goals, however, but only if done in a well-planned, coordinated fashion. If carefully done, however, the result should be an efficient, effective legal team and a well-served client. ■