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— GUEST EDITORIAL — IMPLICATIONS FOR PROFITABLE LEGAL DEPARTMENTS

by *JEFFREY FORBES*

Hats off to Tom Sager, the visionary GC of DuPont, and others like him, for acting more like a stakeholder in their company. After all, it's not easy changing the mindset of in-house lawyers and others in a company to become more vigilant and pro-active to recover or prevent future financial losses. This is no doubt quite a shift in thinking for in-house lawyers, and external lawyers too, come to think of it. But now that the genie is out of the bottle, it got me thinking about wider implications for this evolution.

Here are four:

Was somebody not doing their job here?

I do not mean to criticize at all. I merely wish to point out that the ability to recover so much revenue for a company, as in the case of DuPont, only indicates that such losses have been considered as a cost of doing business for many years. Again, I am not suggesting anyone be chastised here or lose their job, but clearly it must have been a big mental shift internally, for DuPont to get unit managers and in-house lawyers to act more like owners of the business. So I wonder how many other

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THE PROFITABLE LEGAL DEPARTMENT: The 'Revolution' takes hold

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Since our ground-breaking article in Issue 6 of European GC on the hugely-profitable legal department of the global pharmaceuticals-to-chemicals company, DuPont, the concept of in-house lawyers making money for their organisations – as opposed to being a cost centre – is gathering a head of steam.

So revolutionary is such a modus operandi in companies small and large, general counsel are beginning to re-align their thoughts, and more importantly, some are now willing to go on the record to speak of similar achievements in the past year or two. The only difference between them and DuPont appears to be that the legal departments are not, per se, described as profit centres.

The most remarkable to be reported is the case of the giant British-based insurer and asset manager Standard Life plc which last year, due to the ingenuity of its chief counsel and company secretary Malcolm Wood and his team, was able to preserve £101 million of cash in the company – and this, at a time, when companies and banks all over the world were strapped for cash in the most serious downturn in generations.

The remarkable nine-figure 'bonus' at Standard Life was done by switching the method by which shareholders who wanted to do so, could forego a cash dividend and increase their shareholding.

Mr. Wood explained: "Most listed companies have schemes which allow their shareholders to take more shares instead of taking a cash dividend. If you are a shareholder the company pays a dividend twice a year, but the shareholder can instead just buy more shares. So the shareholding accumulates.

"There are basically two ways of doing that. When we became a quoted company

in 2006 we set up what is known as a DRIP scheme (Dividend Re-Investment Plan) This works thus: if shareholders sign up for it, the company takes the aggregate amount of money it would pay out in dividends and goes off into the market and buys shares from shareholders who want to sell. It then allocates them to those choosing shares as opposed to cash.

"The disadvantages are that if you have a big take up the company has substantial amounts of cash going into the market twice a year to buy shares. The market sees the company coming, the stock price tends to go up, and the number of shares that the shareholders receive reduces.

"It's not much of a problem for companies where they don't have much of a take up. Typically companies will have 6-7% of shareholders who subscribe to this. We've had anything up to 30% of our shareholders signing up to the DRIP scheme. It's a great expression of confidence in the company but it did mean we had a large amount of money going to the market and we were concerned that it was not producing the best results for the shareholders – who also had to pay stamp duty of 0.5% on their purchases.

"It's neutral for the company because the company still pays out the cash to sellers in the market.

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About the editor: **Patrick Wilkins**

Patrick Wilkins is the founder, editor and publisher of the award-winning the European Lawyer magazine from its launch in 2000 until 2009 when the publication

passed into new hands. A former British national newspaper journalist, he began to specialise in the reporting of law and legal issues in 1994, becoming in 1999 executive editor of Commercial Lawyer. The European Lawyer won the prestigious Queen's Award for Export in Great Britain in 2006.

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country, instead of engaging an expensive outside law firm, can go to this person internally. It's being efficient with costs because there are no costs involved in that process. So we spend a lot of time internally making sure that everyone knows who knows what within the legal team. This is a way that you can look at saving costs. Most people want to be consulted by their colleagues and usually they get straight to the answer, be it competition matter, a privacy matter, whatever. They enjoy being a centre of excellence and it encourages them to keep on increasing their knowledge in the area. That, I think, is a smart mix of internal/external management of legal costs.

What is the future of fee structures, post-downturn?

There's going to be a heavy reliance on the billable hour; it's difficult to get away from in instructions where there is uncertainty of scope. But flat rates, which we use in some cases, are a good way of doing business. There are other ways. Law firms have had to come up with new offerings because they have flat times at the moment. We've had very good proactive contact from our law firms during the downturn. I have no complaints on the fact that they have recognised that we need to look at different ways of pricing, giving value for money, and of course making sure that they survive.

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IMPLICATIONS FOR PROFITABLE LEGAL DEPARTMENTS

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boards or shareholders at other companies, will now look to their legal departments, to help them bring in cash and not just burn it? In these turbulent economic times, where savings and budget cuts are at the top of everyone's agenda, it would not surprise me to see more companies like DuPont turning to their in-house lawyers to ensure that they are not squandering valuable revenue. If I were in a GC's shoes right now, I would be thinking about how I can get on top of this issue before it is thrown on my desk - from above.

What is in it for profitable legal departments?

Or put it another way, if you bring in a lot of revenue and make your legal department into a profit centre, then it seems only reasonable that such a department should have no problem receiving funding for the latest technology, training and recruitment, so that it can continue to produce high quality work. In other words, are in-house lawyers being taken care of for what now seems like going above and beyond the call of duty? If not, I could imagine that over time, they might feel like they are being taken advantage of. I think many would agree that the "sales" function in any businesses is one of the most important, because no one gets paid until something gets sold. But whether money comes in to a business from a sale or a recovery, it is still treated like revenue that can be further invested in the business. It is common knowledge that the "untouchable" partners in law firms are those so-called rainmakers who are blessed with supernatural powers to generate revenue for the firm. Of course I am being facetious here, but only just. The fact is, someone who is seen as a "fee-earner" and not a "fee-burner" is considered more valuable, and is compensated accordingly. Will this kind of attitude also prevail in

the corporate legal department? Surely some kind of incentive system would be in order.

A new ranking for legal departments?

Has anyone thought about the fact, that if the DuPont global legal department were a law firm, it would be the 96th largest by revenue, according to the ALM Global 100? It would also be the second richest law firm when measured by revenue per lawyer. And just for the sake of argument, what would their profits per partner (PPP) be if you divide their profit by heads of legal departments globally? Nothing gets people's attention more than numbers, especially revenue and profits. After all, many law firm leaders have been driven or influenced by such rankings ever since they came out. So is it unrealistic to think that maybe now, or at least in the near future, that a similar financial ranking should benchmark in-house legal departments? For the record, let me just state that I am now coining the ranks for "AM IN-LAW 100" and "GLOBAL IN-LAW 100". In ten years time, these rankings will probably drive the recruitment process in the top in-house teams. This will make it easier for them to siphon off promising young talent who fear being burned out at a big law firm, not least because they no longer have to sell, they just have to intimidate. Now isn't that more the reason why people go to law school? Even if you think I am taking this a bit too far, which I admit I am, it does underscore that profitable legal departments have a vastly different cost structure that more law firms should probably try to emulate.

Time sheets for in-house lawyers?

Now that we have gone this far in extrapolating how an in-house legal department is becoming more like an

external law firm in the business sense, is it not time for in-house lawyers to be filling in time sheets too? That is apparently what some in-house counsel are thinking of introducing. But this is where I have to draw the line. It's OK as an occasional exercise or spot check just to show that your external law firm can do better. But do you really want to adopt this flawed model? If so, I ask you to read again, the excellent article by James Wilber: Back to the Future? EGC Volume 1, Issue 5. He shows how the ABA has been trying for more than two decades to eradicate the billable hour, and with it time sheets. Why? Because selling time has no value. It's not what clients buy. In the second book published by the ABA on this topic back in 1992, Win-Win Billing Strategies, Alternatives That Satisfy Your Clients and You, they include a list of 14 generic billing methods, stating their advantages, disadvantages, when to use, and, wait for it, recognition of value to the client. Now of these 14 methods only 4 come close to offering true value. They are: fixed or flat fees, contingent fees, percentage, and retrospective based on value - with the latter offering the most value. Regarding straight hourly billing, which requires you to fill in time sheets, this is what they have to say about recognition of value to the client: "Generally unrelated to value to the client. The lack of relationship between the amount of the fee and the value to the client may penalize either the lawyer or the client." So instead of encouraging your in-house lawyers to track their time, why not encourage them to find innovative ways to do things faster, better or cheaper? This requires inspiration, which is hard to capture on a time sheet.

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See page 7 for Jeffrey Forbes' full details.