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An independent mind

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THE FUTURE OF BUYING LEGAL SERVICES¹

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Introduction

I'm delighted to be starting off this very welcome day devoted to the procurement of legal services. In 15 minutes, I'm not going to try to cover the waterfront, but rather offer a few reflections on the turn of events that prompts us to be considering so seriously the process that leads to the delivery of legal advice and representation to clients.

Part of the challenge here, it seems to me, lies in the nature of the four principal 'moving parts' that form the backdrop to procurement. These are: cost; price; value; and relationship. There are different types of legal services – ranging from highly bespoke and 'bet-the-company' issues to routine, standardised and commoditised offerings. And there are different types of procurement – ranging from personal engagement, through professional procurement and tender processes, to buying online with no human interaction at all.

What is clear is that not all types of procurement are appropriate to all types of services. The real issue, as I see it, lies in the potential disconnects among cost, price, value and relationship. There is an inevitable tension between short-term procurement wins and longer-term legal or relationship consequences. There are times or circumstances when cost-cutting just isn't worth it. Consider by analogy last week's furore over the prescription of the cheaper anti-malarial drug mefloquine to members of the UK armed forces serving overseas. At a time when they need to be in first-rate health, we appear to be penny-pinching and using drugs that since 2008 have led to a thousand of them being treated in psychiatric hospitals and mental health clinics.

¹ This paper was given as the opening session of the Buying Legal Council's Conference in London on 28 September 2015. It is not a transcript.

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Let me try to unpick these four factors and their disconnects a little.

Cost

The **cost** of legal services has generally been allowed to rise to unsustainable levels. This has been driven by a tendency to use qualified lawyers for just about everything, when other people or technology could have done just as good a job (or alternatively a good enough job). This has discouraged effective resourcing and project management, as well dampening the need or opportunity for innovation. When this is combined with an ownership model and media culture that gives a distorting emphasis to profits per partner, the total cost-base of the law firm can be significantly inflated beyond sensible levels of cost-efficiency and market sustainability.

Pricing

A longstanding approach to **pricing** based on 'cost-plus' compounds the challenge. If the cost-base is inflated, cost-plus pricing is bound to meet market resistance. Where inflated unit costs are then allied to pricing based on time spent, the price can quickly run beyond the bounds of sensible – especially where the time spent is not managed for efficiency or utility to the client. This is when there becomes a disconnect between cost and price: what the provider wants the market to pay is out of line because the cost-base of the provider is too high.

Equally, of course, a disconnect can arise because the price the market is willing to pay is below the level that even an efficiently structured business with a competitive cost-base can afford. A procurement process focused only on achieving the lowest price can create this asymmetry.

Value

While cost and price usually bear some relationship to each other – if only because the difference between them is profit – unfortunately, **value** often bears no relationship to either. Like beauty, value lies in the eye of the beholder – in our case, the client. Prices driven by inflated costs are bound to create a perception that services do not represent value for money. This exacerbates the pressure on providers to ensure that their costs and then pricing are aligned with the market's perceptions of value.

But the challenge here is not only about providers being misaligned with the market. From a commercial point of view, it might happen that the value of legal services lies simply in providing the necessary paperwork to support a relatively low-value transaction. So, when, for example, the value to the client of relatively straightforward documentation to effect the acquisition or disposal of real estate is low, but the cost to the provider is determined by mandatory registration processes and other regulatory burdens, it is not surprising that there is a disconnect between value and cost, and then between value and price. Pressure on prices from the market at that point is likely to drive even cost-efficient providers out of business.

Matters of value to my mind inevitably incorporate questions of quality and utility. If the technical quality of legal services, or the perceived quality of the delivery of those services, is low, then no client is likely to consider that they have received good value. Similarly, if the advice is technically correct and well delivered, but has no utility to the client because, say, it ignores the commercial realities of the circumstances, deal or dispute in which they are engaged, again it is unlikely that the client will feel that value has been achieved.

Just as price and value can be disproportionate in a bad way for providers, they can also be disproportionate in a good way. It can sometimes happen that the value to a client in achieving an excellent outcome in the negotiations for a deal or the resolution of a dispute can result in financial or reputational benefits that are significantly greater for the client than the cost or usual price of securing those benefits for the law firm. Pricing based on cost rather than value at that point creates possibly unfair asymmetry: the client receives a valuable benefit for which they are arguably underpaying; the law firm is securing an outcome for which they are not being adequately recognised and rewarded.

Relationship

Pricing for value brings different dimensions of cost and price into play. Not the least of these are dimensions that arise from the fourth factor of **relationship**. If value to the client is to be truly understood, then it requires some degree of personal or institutional relationship that can fully inform the business or commercial context within which legal advice and services are given.

This is the basis on which a ‘swings and roundabouts’ approach to lower pricing for some services can be balanced by higher prices for others. In this sense, low value for the client with unavoidable high costs for the lawyer can be compensated within a broader relationship when value to the client is in other circumstances disproportionately higher than the cost of production for the law firm.

Without a meaningful relationship, such compensating trade-offs can rarely be realised. The connection between value and relationship will be broken. But those relationships cannot be created by lawyers who focus only on billable hours and don’t invest in relationship-building because that is not chargeable time. There is a connection between cost and relationship, but it is not one that inevitably results in a direct and immediate uplift in price.

Nor is relationship and value-pricing possible if procurement processes intervene to prevent lawyers who are bidding for work talking directly to the end-client: this denies the lawyers the opportunity to understand the client’s corporate structures and dynamics, and commercial context, in which their services and advice will be used.

Purely transactional arrangements, and processes in which procurement obstructs any necessary relationship between lawyer and end-client, will undermine the creation of value. But let me temper this conclusion with a caveat: value does not need to be created in all circumstances. And to understand this, we also need to understand the differences between value creation, value added, and value for money.

Back to value

Value creation arises when the client's position improves substantively from the legal services themselves. So, for example, if a lawyer is able to reduce the cost of an acquisition, increase the proceeds of a disposal, negotiate a better financial outcome to a dispute, or advise in such a way that there is an improvement in the client's reputation or relationship with its customers, employees or suppliers, value is created.

On the other hand, value is added when the lawyer or law firm does something that is beneficial for the client, not in terms of the substance of the legal services themselves but in the context of the broader relationship with the client. This usually includes such things as legal updates, client seminars, secondments, and entertainment. To my mind, these operate in the periphery of the lawyer-client relationship rather than at the heart of the legal services delivered. They are still valuable, but are not value creation.

Both value creation and value added, it seems to me, can only be achieved within a meaningful relationship with a client. So, go back to the idea of commoditised services: these are not concerned with relationship and are not about value creation. They also provide little scope for value added. None of this undermines the business proposition of commoditised services. But 'bet-the-company' services do create value if they save the company; and value added elements will be necessary in any sustainable long-term relationship.

Value for money, on the hand, transcends all legal services: it must be perceived by all clients, for all services, if the firm is to remain in business.

Final thoughts

It seems to me that without a sustained attempt to reconnect cost, price, value and relationship, any wish for effective procurement of legal services will be unfulfilled.

However legal services are priced, and however their value is assessed, law firms must constantly work and innovate to keep their costs as low as possible, consistent with their intended client-base and position in the market. I don't go so far as to say that this is *all* about efficiency. But it certainly all *starts* with efficiency: without it, a firm will not have kept its cost-base within reasonable bounds, or then its pricing within market expectations; and without cost-efficiency, there is little scope for client perceptions of value for money, or a sound basis for a continuing relationship.

So my messages are for both sides – lawyers and client procurement. Cost-efficiency is vital and law firms must now constantly work to innovate and improve it. But value creation and value-add can only be achieved in the context of a meaningful relationship, and procurement must not avoidably disrupt this where relationship is necessary to the legal outcomes desired.