LEGAL SPEND REDUCTION ANY CFO CAN EMBRACE

Convincing the C-suite of the value of law department management technologies

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Introduction

"Why does the law department think it needs new technology to manage its work when the rest of the company is cutting back?" Recent press articles[1] have chronicled how corporate CFOs are becoming more concerned with controlling legal costs, which each year take an ever-greater bite out of company budgets. However, law departments that want to improve their systems often find it challenging to justify the expense in response to questions from their CFOs. The purpose of this white paper is to help in-house counsel bridge this gap by translating legal process improvement into a value proposition that will resonate with the CFO.

Corporate Financial Control

In the post-Enron era of Sarbanes-Oxley and other new regulations, the CFO has become a lightning rod for concerns related to the company's internal financial controls. With increased enforcement leading to possible criminal conviction, as well as substantial financial penalties, compliance with financial reporting regulations has become a central concern in the C-suite. Ironically, because lawyers generally are more attuned to practicing law than to managing the business aspects of law, the law department is often one of the last company departments to put systematic financial controls in place.

> ***"Because of our responsibility for managing company expenditures, we led the effort to have our law department put better financial controls in place. . . policing compliance automatically with a new legal electronic billing system."***
> *Adam Liu, former controller at VF Corporation*

Many law departments manage significant volumes of legal spending and legal exposure with a cobbled-together array of spreadsheets, files, and basic reports that require manual updates (from legal bills, correspondence, emails, court filings, etc.). The majority of these data sources are outside the company, primarily at law firms that handle the company's legal work. Sporadic updates and the constant torrent of data lead to law department financial reports lacking completeness, accuracy, and auditability, which are standard across company departments.

For the law department to measure up, CFOs need to become knowledgeable about the effective financial control provided by today's matter management systems, including electronic billing and auditing. Law departments can provide detailed financial reporting, meeting the same standards that apply to the rest of the company. The road from disorganized legal information processes to legal data integrity includes:

Efficient Collection of All Financial Data

Most law departments find it challenging to have a comprehensive view of all legal work taking place on behalf of the company. Legal work may be undertaken directly at the business-unit level, by outside counsel, or by senior management without the direct involvement of the General Counsel's office. The latest software as a service (SaaS) solutions track all of the company's legal work in a single online site, connected to everyone who is involved in such projects, both inside and outside the company.

When the law department has all of the company's legal work in a single system, it becomes possible to effectively manage all of that work and to generate complete legal spending and expose financial reports—often for the first time. With the ability to enforce a policy of no payment for legal work that is not processed through the law department system, in-house counsel have visibility for the first time into the company's entire legal landscape.

Keep Financial Information Current

Culling data manually from legal bills, budgets, accruals, status reports, etc., wastes valuable effort and involves significant lag time that makes it a challenge to generate accurate reports. Today's legal matter management systems pull such data directly from the work being done in the law department and at its law firms. For example, all of the data in a typical legal bill (hours, staffing, activities, rates, expenses, etc.) flow directly from the law firm's billing system directly into the company's reporting database without any manual intervention, enabled by a billing standard adopted by the legal profession ("LEDES").

Accruals of unbilled time building up on the books of law firms are also efficiently collected using the same system, ensuring that all material legal spending (both billed and unbilled) is accrued in company financial statements. Some systems go even further to ensure the validity of financial reporting data by automatically tying bill processing to the meeting of all other client requirements for current information, such as periodic legal exposure estimates and status updates from outside counsel.

> ***"By having our law department implement basic spending and budgeting controls with our new e-billing system, we achieved a hard savings ROI of over 600% in the first year."***

Generating reports in real time on current spend, budget performance, settlement payments, project status, exposure, and accruals becomes a standard best practice. Reports are always as current as the latest activity in each project. Systematic data collection alleviates CFO concerns about the accuracy of financial reporting generated by the law department.

Maintain Audit Trails for Integrity

A significant limitation of spreadsheets and internal databases used by most law departments is the lack of an audit trail – there is no systematic control that tracks the date and author of revisions, or that catches input errors in data collected from bills, emails, etc. As a result, the integrity of the financial reporting from such processes is suspect. State-of-the-art law department management systems automatically maintain a clear audit trail of all changes made to financial data (e.g., any revision to a legal exposure estimate for a case is automatically logged, including the author/date). As a result, there is an audit trail for all material reporting data, creating both accountability and financial data integrity.

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This accountability is also useful in getting legal bills paid on a timely basis to earn early pay discounts that many law firms offer. Unlike paper bills that get caught on desks and in inboxes, e-billing processing permits administrators to see where each bill is in the approval process, and to track approvals to timely completion. All bill revisions are captured electronically with an audit trail that ensures the integrity of the process.

Generate Financial Projections

Financial projections, particularly those that feed reports to shareholders and the financial markets, must be founded in accurate historical and trending data. However, because of a dearth of hard financial data in many law departments, budgets and financial projections of spending and exposure are more an art than a science. Sophisticated matter management systems that collect data directly from legal work at every stage provide a solid foundation for uncovering significant financial trends. From reliable trending data, it is possible to generate more realistic, more defensible predictions of the company's legal spend, exposure, and results, driving more accurate financial planning.

"When issues arose in the legal department, exceeding budgets or unexpected invoices, the buck basically stopped with finance. Now we have a cooperative tool to bridge the gaps, to achieve greater success in their joint efforts to conform to budgets and curb overall company spend."

Improve Law Department Financial Performance

CFOs quickly grasp that once better financial controls are in place, in-house counsel can become more effective stewards of the company's legal spend. The efficient collection, processing, and reporting of financial information by the law department will lead to significant savings, which go right to the company's bottom line.

Address Areas of Largest Financial Impact

Once the law department has access to organized data on all of the company's legal work, it can more effectively manage that work by consolidating specific types of projects with certain service providers for better service, rates, and discounts. This strategy of convergence has been successfully applied by many law departments, which also benefit from significant time savings from having fewer firms to manage. Whether or not a convergence strategy is adopted, improved reporting on costs, budget performance, and results provides opportunities for in-house counsel to re-assign work to those firms that regularly furnish demonstrable value—the best combination of low cost, fast resolution, and optimal results.

Law departments also use improved reporting in areas of growing legal spend and exposure to identify opportunities to practice preventive law, reducing the volume of legal issues that need to be addressed by the company. For example, an uptick reported in employment claims from newly acquired business units can be a wake-up call that the law department should conduct additional training for those handling the transition of employees during acquisitions.

Accountability and Savings from Process Improvements

Comprehensive and accurate, SaaS systems allow law departments to immediately increase efficiency at handling routine tasks with automation that reduces cycle time and improves performance. For example, in place of manual legal bill review, the latest legal electronic bill processing software automatically analyzes bills for appropriate law firm staffing, changes in personnel and rates, compliance with expense guidelines, and budget performance. In addition to being faster than manual review of paper bills, such automation leads to much greater savings by keeping rate changes, personnel changes, and expenses in check.

Automatic collection of accruals of unbilled time from law firms ensures complete financial accrual data from the law department, whether the CFO needs it monthly, quarterly, or at fiscal year-end, ensuring that there are no adverse last-minute spending surprises. The new reporting data helps law departments apply their limited resources to those areas where they can add the most value. For example, when the law department can run a report that compares budget to estimated exposure for all litigation cases, it quickly becomes apparent that those cases where the budget is a relatively high percentage of exposure should be a priority for early settlement.

Create New Opportunities for Savings

When a law department has a management system that facilitates the use of better business processes, lawyers can—for the first time—find practical ways to apply basic financial management practices to the oversight of legal projects, strategies that are familiar to the CFO. For example, having a mechanism to require budgets in major projects by holding any bills until the budget is approved generally results in a significant decrease in the spend of outside counsel, who realize that they must operate under a budget rather than with a blank check. Having the system automatically compare bills, individually and collectively, against the budget during the course of the project saves even more by highlighting any spending issues so they can be addressed immediately, rather than at the end of the project when it is too late for meaningful changes.

"For the first time, our law department could generate complete and up-to-date financial reporting for our legal operations with just a few mouse clicks – work that took us weeks in the old system of paper and spreadsheets."

Newly available financial analyses of what certain types of legal projects cost, how long they take, and the results obtained can also facilitate the use of alternative fees that incent beating the averages, rather than getting paid to spend more hours (a specific priority of CFOs described in the *Washington Post* article cited above).[2] CFOs quickly understand that when the management system can tell the law department what projects should cost and what results should be expected, the company can begin to move away from the reverse incentive of billable hours, to align compensation with the ability of outside counsel to meet the company's goals.

Demonstrable ROI

The bottom line is that CFOs expect a detailed ROI evaluation to justify the purchase of any new system. This analysis includes the initial installation costs (both time and expense), as well as the ongoing costs for the initial term and renewal periods. Such costs have to be clearly outweighed by the other side of the ledger: the projected savings in both time and spending that are expected from the system.

To allay CFO skepticism over vendor claims of savings, the law department should conduct its own due diligence by requesting that vendors provide: (1) ROI analyses performed by independent third parties who analyze the actual savings experienced by similar law departments using that system; and (2) the identity of comparable law departments from whom the law department can obtain its own direct verification of reasonable savings. From this savings information, the law department can compare what it is currently doing as a baseline, to calculate a range of reasonable savings predicted from use of the new system—both short-term and longer-term. The ROI is calculated by dividing the savings estimated for specific time periods by the system costs for comparable periods. By applying such independent benchmarking data to what is currently being done by the law department, the ROI will assuage CFO concerns about whether the new system will provide significant economic value to the company.

"By working with our law department to put an e-billing system in place with outside counsel, we saved our company significant money, increased the law department's productivity, and significantly improved our internal financial controls and legal financial reporting."

Conclusion

Law departments that want to improve their financial controls with new technology must justify the new system in financial terms that are familiar to their CFOs. By analyzing the financial value of the new system, and undertaking a detailed ROI analysis that is backed up by independent due diligence, the law department can anticipate primary areas of concern and earn the CFO's support for a system that will improve the company's management of its legal work.

[1] Corporate Counsel, *"As In-House Roles Change, More Teamwork between GC and CFO Needed,"* 12/6/11

[2] The Washington Post, *"To Rein in Legal Costs, Think Outside the Billable Hour," 3/21/12*

About the author: Rob Thomas is co-founder of Serengeti Law and currently serves as vice president, Strategic Development, for Thomson Reuters. He was an architect of Serengeti's Internet-based e-billing/matter management system, which is the most widely used and highest-rated system for managing legal work in the world, with thousands of users in 189 countries.

Rob created the ACC/Serengeti Managing Outside Counsel Survey, and is a widely published author and frequent speaker on the use of technology by in-house counsel to efficiently manage their work with outside counsel. His articles have appeared in the ABA's *Law Practice Management*, ACC's *Docket*, LawNet's *Peer-to-Peer* and *Risk Management*.

Prior to joining Serengeti, Rob had more than 20 years of diverse experiences as a practicing attorney.