



The Last Mile

The 'Last Mile' Problem and
The 'Last Mile' Solution

LEGAL
EVOLUTION

The Legal Profession's 'Last Mile Problem'

Since the early 1990s, the telecom industry has struggled to solve the "last mile problem." In its initial stages, the problem centered around an information superhighway (later known as the internet) that connected together government, universities and large corporations in urban areas. The benefit of adding more users was obvious.

Unfortunately, the infrastructure of copper phone lines couldn't handle all the data, at least with existing technology. Thus, the "last mile" of connectivity—from the bundle of wires in a box on the street to the individual end user—was the most difficult and expensive to complete. Eventually, technical feats improved quality, which connected more users and spurred more infrastructure investment. If you have affordable, high-quality broadband in your home, please toast the engineers who solved the last mile problem in your locale.

The legal profession has its own last mile problem. Clients are clamoring for legal solutions that are better, faster and less expensive. And in many corners of the profession, we already have the personnel, technology and know-how to make this happen. Missing, however, are business models that will reliably reward lawyers and their organizations for quantum leaps in legal productivity.

I have sat in rooms with buyers and suppliers of legal services and witnessed the last mile problem firsthand, and it is very painful to watch. The following hypothetical illustrates the nature of the problem and why it is so difficult to solve.

A Legal Productivity Breakthrough

Smith & Jones is a large corporate law firm with 350 lawyers. It is in the broad middle of the Am Law 200 and NLJ 350 rankings. A small cadre of S&J lawyers have developed a working prototype of a "20-in-10 Box." Through an ingenious combination of data, process and technology, the 20-in-10 Box is able to double lawyers' productivity within their practice group. What used to be done in 20 hours can now be done in 10. The lawyers want Smith & Jones to build a larger version to market and sell to the firm's clients. This is good news, right?

Let's assume that the 20-in-10 Box will cost \$5 million to build and take 12 months to scale the innovation so it can be used throughout the firm. On one level, this is a no-brainer. It's exactly what clients are clamoring for. Yet, when the partners vote to approve the investment, presumably they are

expecting to increase firm profits. That outcome, however, depends upon an effective pricing model that clients will accept. Here are three possible options.

Option 1. Clients continue to pay by the hour at the same hourly rate. Clients get the full benefit of the productivity gain while Smith & Jones's revenues are cut in half. Clearly this won't work.

Option 2. Smith & Jones explains the innovation to clients and doubles its hourly rates. Although total cost and quality remain unchanged, clients feel insulted and refuse to go along.

Option 3. Smith & Jones shares the productivity gain with the clients 50/50, increasing rates by only 50 percent; alternatively, hourly rates are kept the same but the clients give Smith & Jones a much larger volume of work.

Clearly the solution lies somewhere in Option 3. Yet, what law partnership would approve the construction of the 20-in-10 Box without locking down the specifics? After all, it's investing \$5 million, and the result may idle a significant portion of the firm.

Likewise, what client would guarantee a financial benefit to an outside service provider without overwhelming evidence that the benefit to the client is real and sustainable? The most likely answer will be, "Build it first and let us try it. Then we'll decide."

Welcome to the world of complex technical sales, which is destined to be a big part of the legal industry's future.

The hypothetical continues.

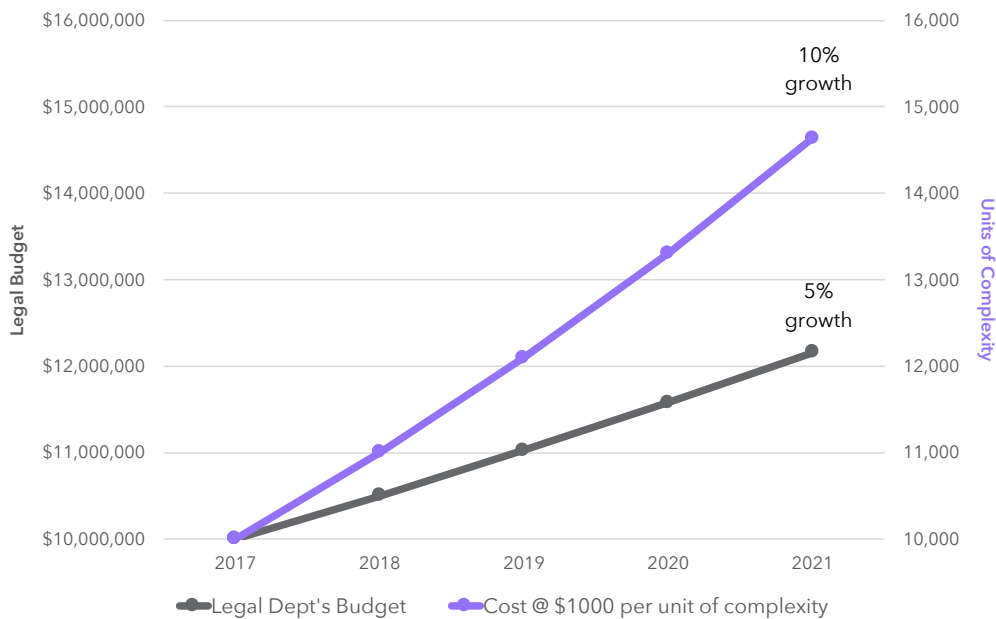
Acme's Productivity Imperative

One of Smith & Jones's longtime clients is Acme, an established global widget maker with \$2 billion in revenue and 5 percent annual growth. Acme spends \$10 million per year on legal costs. Acme's CEO and CFO won't tolerate increases in legal costs that exceed the overall growth rate of the company—5 percent.

Unfortunately, due to a myriad factors related to globalization, regulation and technology, the complexity of Acme's legal work is increasing at a rate of 10 percent per year. (Think this is an unrealistic assumption? Check out the growth rates of **federal regulations**, **the Tax Code**, **electronically stored information** or the growing importance of **U.S. corporate sales abroad**.)

Acme currently manages 10,000 units of legal complexity at \$1,000 per unit ($10,000 \times \$1,000/\text{unit} = \10 million). However, unless Acme's general counsel can figure out a way to increase legal productivity, she will soon be faced with difficult decisions related to cost and risk. The chart below illustrates the conundrum.

Forecast of Acme's
Legal Budget and Legal Complexity
2017 to 2021



Over the next five years, Acme's legal budget is anticipated to grow to roughly \$12.2 million (the gray line). Yet, because legal complexity is increasing at a 10 percent clip, the general counsel believes she needs a budget of \$14.6 million to effectively manage risk. This is to handle the steady increase in complexity up to 14,600 units (the purple line). The general counsel may frame this issue as a cost problem. But, in fact, the real issue is productivity.

Below is a chart showing the trend line of legal productivity that Acme needs to achieve if it wants to stay within the 5 percent constraint on its budget.

Cost per Unit of Complexity
needed to Stay within Budget



The cost of managing a unit of complexity has to drop from \$1,000 to \$830. One very helpful solution to this problem would be the 20-in-10 Box that Smith & Jones decided not to build. Instead, what is likely to happen is that Acme will press Smith & Jones and other outside service providers for a 17 percent discount over the next five years. Both sides are made worse off.

Thus, the last mile problem.

The constraints aren't technical. Rather, they are rooted in the failure of lawyers on the buy side and sell side to properly understand and allocate business risk—that, plus a heavy dose of poor communication.

Real Life 20-in 10-Boxes

I wish I could say that the Smith & Jones /Acme example is just a law school hypothetical. But that would be false.

In my travels as a researcher, I visited an innovative insurance defense firm that was specifically created to implement processes, technologies and staffing systems to drive down both legal costs and speed up cycle time (closing files in an average of 300 days rather than 500). The firm has been able to show that as the time and cost to litigate go down, the amount paid to plaintiffs in settlements and judgments is not going up. This is a big net saving for the insurance companies. Unfortunately, because these matters remain on the hourly billing model—because that is what large insurance companies are used to—the increased efficiency is actually reducing the total revenue on the founding partner's long-standing book of business.

The founding partner's insurance clients think his model shows promise—just not enough to guarantee him significantly more volume today, although he is seeing some early adopters. Ironically, he needs that volume to successfully solve his clients' long-term productivity problem, particularly since he is honoring their preference to stick with price-sensitive hourly billing.

I would like to believe that this innovative founding partner is a visionary rather than a fool. But until buyers and sellers of legal services accurately understand and coordinate their long-term business interests and realize that the lack of innovation has real costs to them both, we'll have yet another last mile problem.

Another example of the problem involves expert systems, which can deliver fast, high-quality answers for a large volume of legal questions through an online kiosk portal. The quality of the legal advice is backed up by partners at Am Law 200 firms that are building them, often with an initial investment of 1,000+ hours of nonbillable expert time.

Yet, how should these expert systems be priced? Can the client accurately gauge the volume of the legal work it no longer has to buy by the hour? And what about the value of getting answers that the client doesn't get today because it never calls the lawyers in order to save money—what's that worth? That's a complex risk-management question with potentially large

consequences for the client.

In the Smith & Jones hypothetical, the firm considered a 20-in-10 Box but decided to pass on the investment. But here's another permutation of the last mile problem. Recently, an Am Law 200 partner who has built an expert system in a very hot area of the law said to me, "We have the 20-in-10 Box in our inventory now. It's ready to ship. We just need a pricing model that ensures we can recoup our investment."

And that, it turns out, may be more complex and time-consuming than building the expert system. Complex technical sales are hard, especially when the buyers are skeptical lawyers who are unaware of the last mile problem. In the immortal words of Jerry Maguire, **"Help me help you."**

How Do We Solve the Last Mile Problem?

Step one is conceptualize the last mile problem as a problem of productivity rather than cost. Without that common understanding, buyers and sellers cannot have an intelligent dialogue on their long-term mutual interests.

Step two is to set aside ample time to engage in the intelligent dialogue. Resist the urge to bloviate at industry events and in the legal press about how the other side just doesn't get it. Instead, do the difficult intellectual and emotional work of listening, empathizing and letting go of old ideas. Start with clients or service providers you like and trust and express a desire for a long-term relationship.

Step three is to openly share successes and failures with peers in the industry. We need these examples to more rapidly converge on new business models. This iterative approach is true thought leadership. It is also consistent with the values of professionalism.

There are other solutions to the legal profession's last mile problem, but none will work as fast or as well as an honest dialogue between buyer and seller.



Bill Henderson

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The Legal Profession's 'Last Mile' Solution

Buyers and sellers of legal service must have prolonged and sustained discussions with each other on how to align their long-term business interests.

To create better, faster and less expensive legal solutions, the legal profession has everything it needs, save one thing: business models that reliably reward legal productivity. This gap is the legal profession's "Last Mile problem," which I wrote about in my last column.

The problem exists because lawyers on both the buy and sell sides view their business challenges in terms of cost rather than productivity. If we limit ourselves to cost-based solutions, we're in a zero-sum game that stifles innovation. If we become open to productivity-based solutions, both buyer and seller can be made better off.

For lawyers, the difference between cost- and productivity-based solutions can be subtle. Thus, let's walk through some examples.

Example 1: The In-Sourcing Solution

In the original Last Mile hypothetical, global widget-maker Acme was operating in an environment where the complexity of the legal and regulatory environment was increasing faster than company sales. As a result, demands on Acme's legal department were rising faster than the department's overall budget.

At the most practical level, Acme's legal department has a checkbook problem—there is not enough money in the account to pay for everything it needs. A common solution that requires no business training would be to find a way to obtain the identical goods and services but at a lower price.

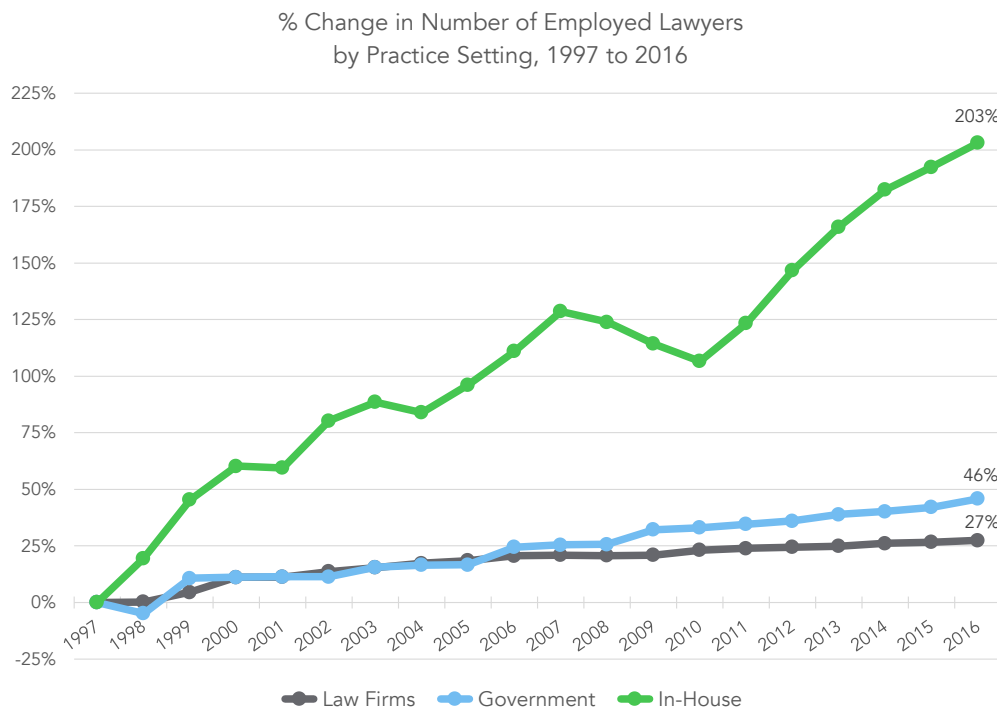
For example, Acme could offer full-time jobs to several talented law firm associates currently doing the company's work as outside counsel. There appears to be no shortage of lawyers willing to take a pay cut to be freed of billable hour and business development pressures.

We'll call this the in-sourcing strategy. There is substantial evidence that the in-sourcing strategy has been growing in popularity for many years.

According to the Economic Census conducted every five years by the U.S. Census Bureau, over **three-quarters** of legal services in the United States are sold to organizations (as in, companies) rather than individual clients.

Although this allocation of labor may sound high, it is actually a dramatic understatement of how much lawyer effort is directed toward organizations, because in-house lawyers are not included in Census Bureau calculations.

As shown in the chart below, the proportion of lawyers working in-house has grown dramatically over the past 20 years—in fact, 7.5 times faster than that of law firms. More lawyers are now working in-house in the United States than in the domestic offices of Am Law 200 firms.



The in-sourcing solution has likely been very effective in helping legal departments like Acme cope with rising internal client demand and a relatively flat overall legal budget.

Is in-sourcing a cost-based or productivity-based solution? In the short to medium term, this seems like an academic question. Yet, the graph above suggests we are rapidly approaching the long term. In fact, in-sourcing is a cost-based solution because the financial saving flows from lawyers doing the same work for less money rather than savings that result from improved processes or deployment of labor-saving technology.

In-sourcing is likely approaching its natural limit as a cost-saving strategy. Bigger legal departments significantly increase communication overhead and necessitate a new layer of in-house middle management. Lawyers also get older and expect pay raises and longer vacations, even in the absence of additional skill development. Finally, a substantial range of legal problems remains that require specialized skills that cannot be brought in-house due to issues of quality and risk management.

Example 2: Aggressive Outside Counsel Management

Another potential solution to Acme's checkbook problem is to drive a harder bargain with outside service providers, particularly law firms.

Within the legal industry, this is a relatively new dynamic. Dating back to the **rise of the administrative state** in the early 20th century, there was a persistent shortage of lawyers who could handle sophisticated legal work for large corporate clients. That imbalance led to the creation of corporate law firms and, later, the rise of what we now call Big Law. Between 1978 and 2008, the average law firm listed in The National Law Journal's NLJ 250 increased from 45 partners and 102 attorneys to 213 partners (+473 percent) and 535 attorneys (+525 percent). Likewise, the average number of offices increased from 2.5 to 10.2. Essentially the nation's leading firms moved into each other's backyards, upsetting decades-old regional fiefdoms and creating a national marketplace for high-end corporate legal services.

For law firms, this growth felt wonderful until the clients realized that the world had change. With the economic shock of the 2008-09 financial crisis, general counsel awoke to their enormous bargaining leverage. How have they used that power? Primarily to negotiate **hourly fee discounts**.

The challenge of venturing too far into alternative billing arrangements (AFA) is that it requires in-house counsel to ascend a learning curve on how to calculate cost-savings. The most common method is "shadow billing." It is common because it is extremely simple to see which party has been made better off: At the close of a matter, the AFA price is compared to what the matter would have cost, had the firm billed by hour.

The virtue of both fee discounts and shadow billing is that they are simple and easy to use. The problem with these approaches is that they don't challenge existing and familiar work methods—it just needs to cost less. If legal complexity is truly growing faster than legal budgets (as in the Acme hypothetical), cost-based solutions are not a long-term solution.

How can buyer and seller get closer to productivity-based solutions?

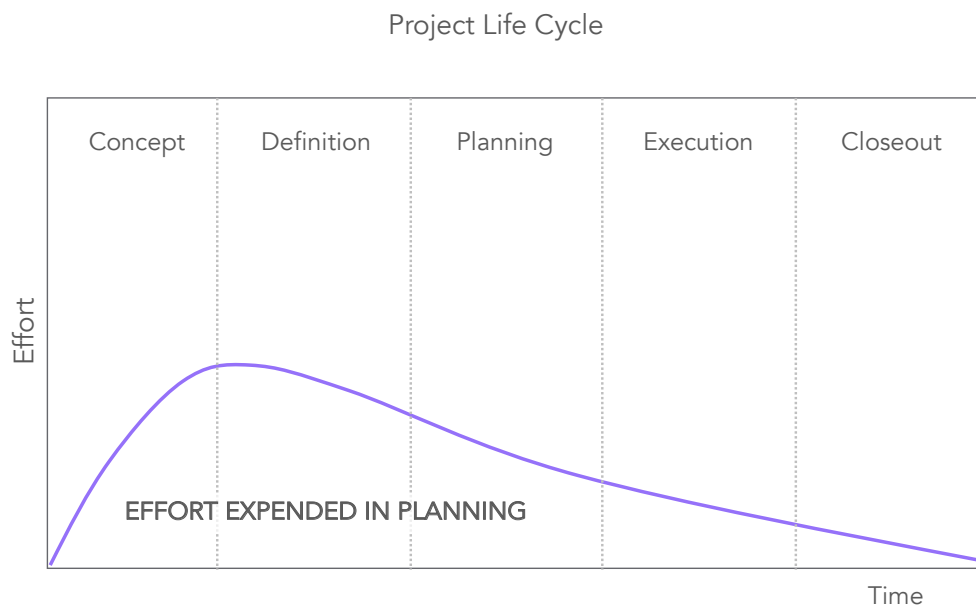
Example 3: A Conversation About Business Problems

The Last Mile problem is a problem of: first, misaligned incentives between buyers and suppliers; and second, the complexity of coordinating a realignment that is stable for all parties. Stated another way, it is a difficult, time-intensive problem to solve. And time is something that lawyers are very reluctant to invest, either because they perceive themselves to be too busy or because their organizations will be unforgiving of time allocations that don't produce material short-term benefits. The villains here may not be the law firm managing partners or executive committee; it could just as easily be the short-sighted corporate CEOs or CFOs.

Several years ago, I witnessed this dynamic firsthand. During the middle of winter, I had the opportunity to travel to a fancy resort to give a talk to the leadership of an Am Law 50 law firm and a small coterie of its biggest and most important clients. After walking them through several slides of data that showed how the market was changing, I offered some thoughts on the future.

At Indiana University Maurer School of Law, I had recently created a course called "Team-Based Project Management for Lawyers." In the presentation at the resort, I inserted several slides that covered the basics of project management, including the answer to the question "What is a project?" According to the **Project Management Body of Knowledge**, which is the compendium of guidelines and standards used to certify project managers, a project is "a temporary endeavor undertaken to produce a unique product, service, or result." Everyone agreed that lawyers work on projects.

The next two slides, however, turned out to be showstoppers.



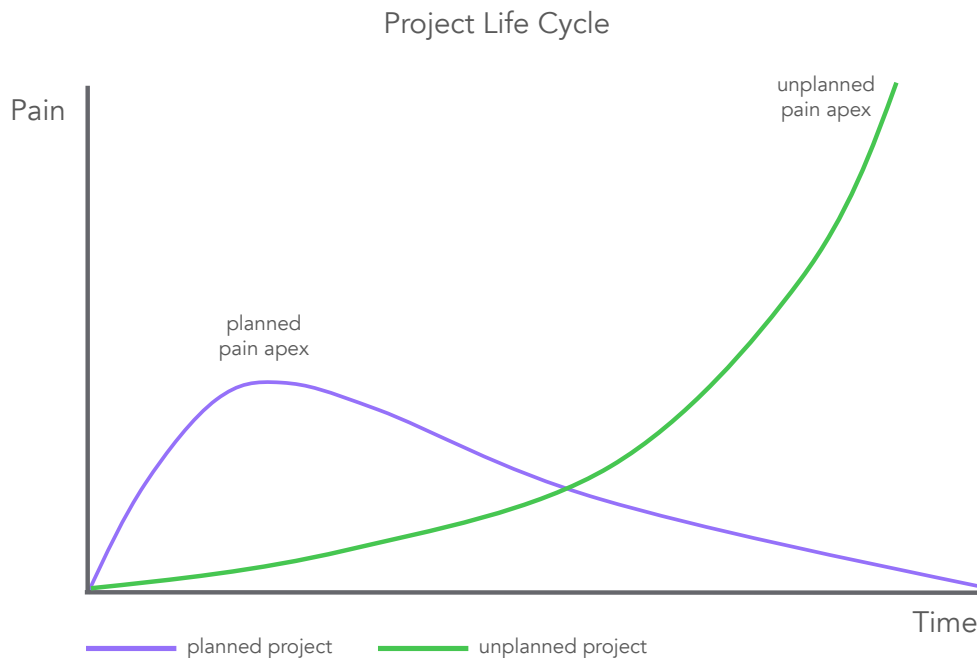
Adapted from James P. Lewis, *Fundamentals of Project Management* (3rd ed. 2007)

The first slide, reproduced above, showed the five sequential phases of a project. A substantial component of project management is planning. Indeed, for many projects, planning can account for over 50 percent of the time allocation, with a peak occurring during the concept and definition phases. This deliberate approach makes it possible to obtain large quality and cost gains, particularly as teams accumulate learnings from similar projects and the organization adopts the related discipline of process improvement.

As James Lewis, the author of the graphic, points out, obtaining clarity and consensus within a work group is time-consuming and arduous. It also

requires outstanding people skills, as many professionals would rather work by themselves than sit through meetings trying to conceptualize and define the problem they have been asked to solve. (To the skeptical lawyer, the clarity and consensus process goes a lot faster with practice, particularly when procedures are standardized across an organization.)

The second slide, reproduced below, was a variant of the first. Yet, instead of showing effort on the Y-axis, it substituted pain.



As Lewis points out in this book, if professionals were permitted to give in to their natural urge to get to work rather than plan, the near-term discomfort they are avoiding (the purple line) eventually resurfaces in the form of mistakes, rework, missed deadlines and blown budgets (the green line). Further, if the context is a legal project such as a litigation matter or a complex corporate deal, it is the client experiencing ever higher levels of pain. Aside from some uncomfortable conversations with in-house counsel, the green line has historically reflected higher profits for the outside service provider, as virtually all the work is done on an hourly cost-plus basis.

Thus, I put the question to the general counsel: “How would you react to an invoice from a law firm that billed 200 to 300 hours of time to conceptualize and define the project?”

For the next 45 minutes, I said nothing, toggling between the two figures above as directed by the audience. Much to my chagrin, the corporate clients and law firm leadership were engaging in dialogue that was unprecedented in its depth and honesty, with each side confiding that they had never taken the time to ask about, much less listen to, the challenges the other side was facing.

In our personal lives, we all understand that rewarding relationships

require time investment and honest dialogue. Not just one personal epiphany and the emotional statement to our friend or partner that we are ready to change our ways, but a regular, ongoing dialogue that fosters understanding and trust. This is the type of relationship that is capable of finding a third and better way. Why would we think that the rules of success would be drastically different in the commercial realm?

The Real Last Mile Solution

In the original Last Mile problem hypothetical, some innovative lawyers at Smith & Jones invented a 20-in-10 box, which enabled work to be completed twice as fast (20 hours of work done in 10) with no drop-off in quality. Scaling 20-in-10 firmwide would cost \$5 million and take 12 months to complete.

The firm's clients, including Acme, had a difficult time envisioning how the innovation would work and how a change in the pricing model would benefit them. With no clear path to recover their investment, and the risk of spending \$5 million to idle half the firm's lawyers, S&J passed on the 20-in-10 box. Ironically (and unfortunately), the 20-in-10 box would have solved the long-term and growing budgetary constraints within Acme's legal department.

In this digital age, I worry that lawyers are becoming resistant to any solution that is not as easy to operate as a smartphone. Ironically, even that sentiment is rooted in misunderstanding, as the design principles that made the first smartphone so easy to use were paid for in advance through enormous financial and human investment. (Brian Merchant's 2017 book, *"The One Device: The Secret History of the iPhone"* discusses the hardships endured by Apple engineers as part of the creation of the iPhone.) Because of the constraints on nonlawyer investment in businesses that engage in the practice of law, private industry cannot solve this problem for us.

In the year 2017, it is impossible to solve the Last Mile problem unless the true thought leaders in the legal ecosystem, both buyers and sellers, carve out the time to have prolonged and sustained dialogues with each other on how to align their long-term business interests. We have hit the natural limits of what can be accomplished through simple cost-based solutions such as in-sourcing and fee discounts. Yet, we are all on this learning curve together. Improved legal productivity is the next frontier.



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