

Show Me The Math:

The importance of cost estimates
when engaging a law firm



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Executive Summary

Gone are the days when a law firm would provide their corporate client with a cost estimate for a matter that was based solely on subjective “gut” feelings and nothing more. Over my 20 years of legal operations experience, I have heard many partners at many firms say a variation of such things as “business people are not lawyers, so they don’t understand the nuances of the law and how we price our work”, that clients “don’t have our (legal) intuitive experience” or that “the legal work is bespoke, complicated and has too many variables to put into a cost estimate”. Over the past decade, an increasing intolerance has been building amongst the corporate community against such dismissive and diminutive comments.

I have worked with numerous general counsels, senior executives, and business clients at various companies on many different cost savings, control and effectiveness initiatives – all aimed at interpreting and leveraging cost and billing data to create savings. The corporate constituency will continue to use their buying power and control demand for legal services in the new legal marketplace that emerges post-pandemic 2020. Once the world returns to a new economic (near) normal, corporate clients will be increasingly looking to firms for objective and analytical cost estimates that are well thought out and supported by a clear understanding of what the client wants.

I expect that in the post-pandemic marketplace, the economic pressures facing clients today to control or reduce legal spend, generate cost savings and/or create operational efficiencies will only intensify. Consequently, clients will be forced to increase the scrutiny of their legal service providers, especially how they deliver their services.

Since the recession of 2008, law firms have increasingly begun to look inwards at their cost structures, business processes, and operations with a view to cut costs, invest in technology, and reduce margins to protect profits. Economic rationalization and efficiency practices will only intensify in the post-pandemic legal marketplace as firms will increasingly be challenged to manage and maintain market share and profitability in

the face of hyper competitiveness and a marketplace that may inevitably contract because of an impending global recession.

Therefore, because many firms today are already increasingly having to work smarter and more efficiently, clients expect that all of the efficiency and cost saving projects that firms undertake should translate into more affordable legal services for clients and that those savings should show up in the cost estimates that firms put forward.

Excellent legal advice and service delivery have always been and continue to be present in the requirements that many clients impose on the firms they engage. But just as important is the need for transparency when it comes to how a firm prices its legal services. Therefore, what better title for a book that discusses the importance of cost estimates than “Show me the math” – as I have asked this many times working with law firms around the world. I have also heard the same request coming from many other clients, so much so, that I think it has become the mantra of the corporate community that continues to search for constant assurance that they are paying a fair price and receiving value for the work that firms deliver. In my experience the value that is derived from the transparency that a client gains from a firm’s cost estimate is invaluable. If done right, clients get to understand not only how a law firm calculates the price of a matter, but also whether the firm understands the scope of the engagement, the utilization of its resources (staffing), the quantity of time each professional is expected to work on the matter, the cost for specific tasks or key deliverables, and how variances and assumptions will be dealt with if they should materialize. All of these individual components sum up to provide the client with the price in a cost estimate, but also help to provide an assurance of how the legal services and value of a matter will be delivered. I believe clients today want to see what is behind the “magic curtain” so to speak. “Show me the math” is another way of asking for greater transparency, an assurance that what the client receives from its law firm is backed up by real historical data, expertise, and experience and not just subjective or gut feelings. Clients see this level of transparency (i.e. backed up by real data) as synonymous with honesty and trust.

Show me the math walks the reader through a comprehensive analysis of all of the components of a successful cost estimate strategy. My intention in writing this book was not to create an instruction manual but instead to share my thoughts, experiences and what I have seen as best practices when it comes to cost estimate strategies and their importance in today’s legal marketplace for both the client and the legal service provider. This book can help corporate clients, lawyers, legal operations

experts, law firm CFOs, CMOs and finance experts to develop cost estimate strategies, increase efficiency, lower costs, and improve client/law firm relationships by understanding how value can be measured and monitored through the utilization of cost estimate tools and strategies. I have also spoken to numerous young lawyers, fresh out of law school, who have struggled with working with cost estimates. I hope this book can help those who may still be studying in law school with a better understanding of what corporate clients are looking for in terms of cost estimate proposals.

Whenever possible I have tried to address cost estimate strategies from both the client's perspective as well as the firm's, and highlight the pros and cons to the topic that is being presented.

I have divided the book into five principal chapters, starting with Chapter One: The benefits of a cost estimate, where I provide a detailed narrative around the benefits of cost estimate strategies and the attraction and increased popularity of cost estimates amongst corporate clients. The marketplace today and in all probability post-2020 will continue to be driven by clients looking for any and every opportunity to control legal costs. Understanding the benefits for clients, as well as firms, helps set the table for those parties looking to implement a cost-saving strategy or reinforce existing strategies that may be faltering due to user acceptance.

In chapter two, I review a variety of topics around cost estimate strategies but begin with the importance of different pricing models that clients are attracted to when engaging law firms on cost estimates. Although there has been a huge market push to move away from the hourly rate model, it continues to be the basis for many clients and law firms in calculating their cost estimates proposals. I look at the different AFA options that clients utilize and question the value of law firms continuing to utilize commercial (street) rates and ambiguous dollar ranges in the cost proposals that they propose to their clients.

I continue my analysis with a focus on how firms should leverage all of their internal resources, historical data and especially their legal operation folks when working on a client's cost estimate. Once upon a time, it used to be a couple of lawyers in a board room with a billing clerk working on a cost estimate that was based mostly on intuition and some data. However, today clients expect to see real data backed up by real historical experience. They want to see and understand a law firm's efficiency ratio, whether a firm staffs its matters partner- or associate-heavy (i.e. staffing ratio), or how a firm measures its work in progress (WIP ratio) relative to an agreed budget amount. I also focus

on the law firm efficiency and clients' expectations with regards to firms increasingly having to work smarter and more efficiently. All of these components are discussed in chapter two, as are the changes that are taking place with the traditional legal model.

Communication and proper scope definition are two areas where clients, as well as law firms, have struggled to get "it" right and that are perhaps areas that can have the biggest impact on both parties to a cost estimate agreement. In chapter two, I highlight this section and the importance of defining scope at the outset of a matter and how firms should not shy away from challenging clients if the scope is not defined properly. When things do go wrong, such as in an overage situation, both the client and the firm should avoid the blame game and focus on correcting the issue and working through the problem. Lastly, I end chapter two by discussing how law firms should communicate overages to their clients. It's not always easy, but both parties to the cost estimate should look to find a middle ground, especially if the work behind the overage was of value to the client.

Operationalizing a successful cost estimate strategy is just as important as the mechanical components that comprise it. In chapter three I share my thoughts around some of the thematic challenges that clients and law firms face when implementing cost estimates. I highlight my experience in a case study where I helped a US insurance company by implementing a cost estimate strategy and provide some guidance for clients looking to do the same. I explore the reasons behind internal corporate resistance that is commonly in some in-house legal departments and companies and how those challenges handicap a successful cost estimate strategy. In this chapter I further address such challenges as lack of executive leadership, in-house counsel apathy, training and support. One of the biggest challenges that I have encountered with regards to the successful implementation of cost estimate strategies has been the inability of lawyers to learn basic accounting skills and familiarize themselves with a process that is valuable to their organizations. Many lawyers still see anything outside of the law, such as administration, not worth their time or that takes away from their ability to bill time. Yet cost estimates are valuable tools by which clients make decisions as to which firm they will engage on any given matter. Resistance to implementing cost estimates does not just reside at firms, but more so in many in-house legal departments or the internal business clients that many in-house legal teams service. Clients are quick to point out that it's not always easy implementing processes that require a little work. All too often people will dismiss something as just another administrative

chore. Convincing them otherwise requires work, but it's well worth it once they understand the value and added trust that can be derived through a cost estimate process. I end this chapter with a discussion around trust and how transparency can help achieve that for the client as well as the law firm and a final look at what law firms, not clients, dislike most about cost estimates.

In chapter four, I examine the question of value, specifically how value factors into a cost estimate and how clients can benefit from measuring value using value indicators. Ultimately if a cost estimate has been done well and has outlined the framework for the engagement or the relationship, the client will be satisfied and the firm has delivered value. I provide some insight into how cost estimates provide clients with a strategic advantage and how clients can track the success of a cost estimate. Firms should understand the value of cost estimate data and they should learn to leverage that information for their benefit. Developing a well thought out pricing or cost estimate strategy helps differentiate a firm from its peers and may give it a competitive advantage. Lastly, I tackle the question of whether or not there is still any opportunity to consider subjective or instinctive approaches in today's highly data-driven legal marketplace.

In chapter five, I present my final thoughts around a variety of topics related to cost estimates that clients and firms should be aware of. Many clients are beginning to utilize the cost estimate process and templates and use them as simplified bid processes with multiple firms. I compare the cost estimate process to a more formalized request for proposal (RFP) process and reinforce the belief that firms should approach the cost estimate like an RFP and never assume that they are the only firm that was asked to submit a cost estimate proposal.

If done correctly, a well-defined cost estimate can provide clients with greater visibility and transparency into validating the analysis that is used by a law firm to price its legal services. In chapter five, I also review the importance of trust and how clients should be prepared to challenge a law firm's cost estimate as greater transparency leads to greater comfort for the client and an assurance that the firm is acting in its best interest and that the client understands the value proposition of the cost estimate as it relates to the success of the matter. Those firms that cannot demonstrate how they have objectively determined their cost estimate (and potential cost savings) for the client will be at a competitive disadvantage and increasingly challenged to find newer clients – as existing clients may have moved on to more competitively priced efficient firms.

Finally, I conclude the book with my thoughts on the outlook around the future of cost estimates. Firms that can deliver transparent value through transparent pricing will be able to sustain themselves, satisfy existing clients and be the most attractive to new clients.

About the author

Richard Brzakala is a recognized legal marketplace thought leader and expert in legal operations, sourcing, and cost efficiency strategies. He has been a trusted advisor to many senior executives and general counsels, having worked and consulted for numerous FIs, law firms, and government agencies. Richard is a frequent speaker, panelist, and writer, having published numerous articles on a variety of legal ops topics such as legal sourcing, winning RFPs, convergence practices, and creating corporate cost-saving strategies. Richard's most recent essay, "The Impact of COVID-19 On Future Legal Operations and the Legal Marketplace", appeared in *Horizon Scanning: Modernizing Legal service Delivery* (ARK Group). He is a contributing author for Thomson Reuters Legal Executive Institute, chairs a number of legal sourcing discussion groups, and also participates in an executive advisory capacity for a global IT legal service company. In 2017, a leading US publication recognized and awarded Richard with its annual Trailblazers award for his work in developing a comprehensive global methodology for evaluating law firm compliance with cyber security standards. Richard is currently working as the global director of external legal services at a large FI in Canada where his mandate includes the oversight of legal ops, compliance, finance, and risk management practices as they relate to the management of external counsel globally.