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Corporate clients shift priorities for law firms

Tired of high hourly rates and a no-bid mentality, corporations are demanding changes in the way law firms bill their clients. And the law firms are responding.

By Jay Fitzgerald - March 02, 2014

As legal operations manager at Boston Scientific Corp., Elizabeth Murphy's job is to get the best deal from law firms for services from patent filings to product liability cases. For years, she has cajoled, pressed, and pleaded with them to discount fees, set fixed prices, and bid on projects, only to be rebuffed by top firms that insisted on sticking to rates as high as \$1,000 an hour.

But with more choices as lower-cost players enter the market, Murphy, who farms out tens of millions of dollars in legal work a year, is no longer pleading. Her message to those clinging to traditional hourly rate structures: "I'm not sure how much longer we'll continue to work with firms that won't change."

A seismic shift is underway in one of Boston's leading — and most prestigious — industries as more corporations like the Natick medical device maker have become determined to shop for legal services on price, rather than brand. Until the last decade, many top-tier, white-shoe law firms tended to act more like members of an elite guild, setting both the hourly rates they would charge and the number of hours they would work on cases — and expecting corporate clients to pay the bills with few or no questions asked.

Today, the balance of power has shifted from large, powerful law firms to corporate clients, who are using newfound bargaining power to demand lower fees and more flexibility in the ways law firms charge them, according to industry officials and observers.

As a result, many law firms are adopting new business models and doing what once seemed almost unthinkable in the industry: cutting hourly rates, bidding for corporate work against rival firms, capping prices, and keeping a sharp focus on the corporate client's bottom line. In turn, the firms are cutting their own costs in a drive to become more efficient, using fewer attorneys on cases, and moving back-office operations to lower cost states — and even nations.

"They're more and more attacking the old hourly fee structure," said Joel Carpenter, managing partner at the Boston firm Sullivan & Worcester LLP.

Sullivan & Worcester, which has 175 attorneys, is among the nimble, smaller firms that are benefiting from the changing environment by undercutting the prices of large firms.

The smaller players are agreeing to hourly fees that are sometimes 25 percent less than what top-tier firms might charge and, at the request of corporate clients, holding down costs by not assigning as many lower-level firm personnel to work on cases. They're also agreeing to what the industry calls

“alternative fee arrangements,” including fixed fees for certain duties, such as filing patents, or flat rates for individual cases, rather than charging by the hour.

The result is that the smaller firms are starting to nab more corporate business — growing in both in revenue and number of attorneys at their firms.

Nelson Mullins LLP opened a Boston office in 2006 with only two attorneys, but started with a competitive advantage: Its administrative, technology, and other back-office operations are located at its headquarters in South Carolina, where labor and other costs are lower. Today, its Boston office has about 60 lawyers, due to aggressive recruiting, a merger four years ago with a small local firm, and winning corporate business by offering quality legal work at lower prices, said Peter Haley, managing partner of the Boston office of Nelson Mullins.

“We’ve definitely benefited a lot from all the recent changes,” Haley said. “We’re trying to become more client centric, not lawyer centric.”

But not all large white-shoe firms — many with long relationships with corporate clients — are standing pat.

Robert Novick, a comanaging partner at WilmerHale, with 316 attorneys in Massachusetts and 1,178 attorneys worldwide, said his firm has heard loud and clear the calls for change. WilmerHale has not only begun bidding for work and agreeing to fixed prices for some legal services, but also taken other steps to cut costs.

Four years ago, for example, it opened a “business center” in Dayton, Ohio, where the cost of living is about a third less than in major Northeast cities. The firm now employs nearly 250 back-office workers there.

“No one can allow themselves the luxury of not being more competitive these days,” said Novick, whose firm has 15 offices around the world. “The client community is trying to be as fiscally responsible as they can, and we in the legal industry and at WilmerHale have reacted to that.”

Goodwin Procter LLP, with more than 400 attorneys in the city and 827 worldwide, has begun outsourcing document work and record management to a firm in Wheeling, W. Va., another low-cost state compared to Boston. “It’s largely being driven by our clients,” said Regina Pisa, chairman of Goodwin Procter.

Law firms also are facing the same forces that have driven other industries to become leaner and meaner, namely globalization and technology. Law firms today must compete across borders for business while technologies, such as Internet search engines and online law libraries, call into question the need for legal associates and researchers poring over hard-cover law books and documents.

The recent recession and slow recovery have added additional pressures, legal industry specialists said. They’ve driven profit-conscious corporations to find ways to cut legal bills, which can cost companies tens of millions of dollars per year, and have accelerated the shift among law firms towards more efficient, lower cost business models.

That partly explains why employment in legal services has not recovered from the recent Great Recession nearly five years after it ended, industry officials say. The US legal industry is down more than 40,000 jobs compared to its prerecession highs. Legal employment in Massachusetts is still down about 2,600 jobs from prerecession peak, according to the US Labor Department.

The effects of these changes extend beyond corporate clients and law firms. Since firms are not hiring as many entry-level associates, many recent law school graduates can’t find jobs; members of the class

of 2012 had a 13.9 percent unemployment rate nine months after they graduated, said James G. Leipold, executive director of the National Association of Law Placement, a nonprofit that provides career services for attorneys and recently graduated law students.

Such statistics, meanwhile, have led to plummeting applications to law schools, throwing those institutions into their own industry turmoil, legal officials say.

But even longtime attorneys acknowledge that changes were inevitable. At one time, they noted, it was not unusual for firms to boost legal fees 5 percent or more per year, well above inflation. That created unsustainably high legal costs for many clients.

“The business has had to change,” said Joseph Ryan, chief executive at Brown Rudnick LLP, with about 230 attorneys in Boston and 430 worldwide. “Because clients are more cost conscious, we’re spending more and more time [pitching to clients] and answering their requests for proposals.”

It’s about time, said Veta Richardson, chief executive of the Association of Corporate Counsel, a group that represents 34,000 in-house corporation attorneys. Many other professional services, such as accounting and consulting, she noted, have moved away from old-fashioned hourly fee pay structures.

“Law has been much slower to switch,” she said. “But it’s happening now, and it’s going to continue. I think we’re going to see even more innovations in the future.”