



## **DELIVERING STRATEGIC SOLUTIONS ACCA'S 2000 ANNUAL MEETING**

### **VALUING THE IN-HOUSE LEGAL DEPARTMENT**

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#### **I. VALUE PROPOSITIONS IN BUSINESS AND LAW**

- A. A business must continually decide what value it wants its customers to perceive of its products and services.
- B. To carry out the strategy requires organization and discipline. In executing the strategy, management must ask: what do we need to do to demonstrate to our customers (or clients) that we have added value?
- C. A similar approach is useful for the in-house legal department. How does the department want to be perceived by its clients? Are the department's services what clients believe they need, and with the appropriate priorities? How does the department assure that clients recognize the value added?
- D. The sub-elements for demonstrating value for the law department can include price, timeliness, clarity of communications, accuracy of advice, quality of results, etc.
- E. What follows are two possible approaches for the corporate law department to demonstrate value: (a) a matrix budget; and (b) a highly integrated organizational approach.
- F. As with most things in life, there is no single correct answer.

#### **II. USE OF A MATRIX BUDGET**

- A. Was an important part of the Stanford partnership/outsourcing project, but can be used by almost any corporate law department, for both internal and law firm budgeting.
- B. As part of the process, in-house lawyers estimate where they are likely to spend their time in the forthcoming year. (Note: a similar process can be used for a specific matter or project.)

1. Estimates might be based on last year's actual time spent, or a projection of matters that are anticipated in the forthcoming year, or some combination.
  2. Estimates can be based on hours or on a percentage of FTE by day, week, month or year.
  3. Estimates are then converted to a dollar equivalent, using an hourly rate or a percentage allocation of an attorney's total cost (salary, benefits, secretarial support, information support, etc.).
  4. Estimates should cover both substantive areas as well as internal clients to be served. In other words, an attorney might estimate that 20% of her time is likely to be spent on labor matters, and that this 20% is likely to be divided equally among three specified internal clients.
- C. Similar estimates are requested of the outside law firms.
1. In the case of outside law firms, at Stanford, we agreed upon at a fixed price retainer for the year, but other arrangements are possible.
  2. As with the in-house attorneys, the retainer should be allocated to substantive areas as well as internal clients. For example, a firm might estimate that 10% of its retainer will likely be used to provide basic legal services on labor matters, and that 70% of this amount will be for one business unit and the remaining 30% will be split evenly among three other business units.
- D. These estimates, of both the in-house and law firm attorneys, can then be distributed on a chart, with clients listed across the top, and substantive areas along the left side. The net result at Stanford was a set of nearly 70 boxes, each one showing how much legal resources were likely to be available from both the in-house and outside attorneys.
- E. Throughout the year (or the specific project), the budgeted projections can be compared with actual figures (either monthly or quarterly). This requires some form of reporting from both the in-house attorneys and the law firms, but there is considerable flexibility in how this tracking function can be accomplished.
- F. Likewise, monthly or quarterly reports can be circulated to the internal business clients, so that they can see the budget versus actual usage of legal resources and, in turn, become wiser users of those resources.
- G. At times, you are likely to see significant variations from the budget. That is to be expected. This serves as an early warning system. It allows you to ask, is something going on in a particular area that appropriately needs more legal services than anticipated? If so, you should regroup and decide (i) how best to meet this unexpected need and (ii) whether you can reallocate legal resources from other areas that might not require what was budgeted. Sometimes, you might intentionally decide to cut back on some of the legal resources previously budgeted for other areas, but in doing so, you need to decide how to keep risk to a minimum, and what you will need to do in the future in light of the current reallocations.
- H. In many ways, this is what an in-house legal department does continually. That is, there are only so many in-house attorneys, and so many hours in the day. So, all things being equal, the department is continually reallocating its resources. The matrix budget provides a structure in which this process can be managed, including a method for pressing outside law firms to learn to operate within a world of finite resources.

- I. The net result at Stanford was, at year end, the vast majority of "boxes" came within \$100 to \$1000 of budget (on a base of anywhere from \$2,000 to \$200,000 per box).
- J. In one client area, with a combined projected budget of \$2.1 million, we regularly came within \$1,000 of target.
- K. The reason for this success is not that anyone was clairvoyant. Rather, when you show people (clients, in-house counsel and outside counsel) what their targets are, they are usually quite good at managing themselves to that target.

### III. INTEGRATED METHOD OF PRODUCTION

- A. This approach is quite different from a matrix budget. It looks at the total cost of producing a product or service and fully integrates the legal function as part of the production process.
- B. The process requires a monthly report of what it costs to produce a million dollars of some aspect of a company's business (for example, each million dollars of loans at a bank, each million dollars of product for a manufacturer, etc.).
- C. To be most effective, this approach fully integrates the lawyers with specific business units. The salary and overhead costs of the attorneys thus are automatically included within the budgets of the business units, and thus in the total costs of production.
- D. Because the lawyers are fully integrated into each business unit, they automatically are part of the daily decision making of their units. And each business unit is highly focused on what it takes to produce a million dollars of product, including not only the overhead of inside and outside lawyers, but the legal costs if something goes wrong.
- E. The net result is that the business and legal personnel are continually making appropriate decisions (i) to be in strict compliance with all applicable statutes and regulations, and (ii) how otherwise to allocate resources to handle transactions, or respond to litigation, and the like.
- F. This approach requires a willingness on the general counsel's part to exercise less direct control, but to be apprised continually of any major developments and to have the authority to intervene whenever she or he deems it appropriate.
- G. Among the major benefits of this approach are that it is:
  - 1. Self-promoting. That is, there is far less need to "justify" the legal function, or to arrange "coordinating" meetings, etc. The lawyers are fully a part of the business units they serve.
  - 2. Self-regulating. The integrated approach creates a built-in incentive for the lawyers and business personnel together to make wise decisions, since any "gamesmanship" will quickly be reflected in the monthly "cost per million" reports.
  - 3. Highly focused. There is no need to debate what counts and doesn't count in the mix of legal concepts with business concepts. To the extent there are any tensions between the legal and business personnel, they are dynamic and useful tensions, but with a single focus: what will assure efficient operations in both the short-term and long-term, including the best use of legal resources?

### IV. AND THE ANSWER IS...

- A. As already stated, there generally is no single correct answer.
- B. For your company, consider the corporate culture, the history of the legal department, what is working well, and what can use improvement.
- C. Then develop a strategy, and if it doesn't work well, be ready to make further changes.

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