Winning Legal Business from Medium-Sized Companies

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Chapter 1: Introduction

IN MANY ways, the perspectives of a lawyer and his business client could not be more different. A lawyer's focus is on compliance with law and regulation, about avoiding, or at least limiting, risk for his client (as well as for himself). Whether by nature or by training, lawyers are not only risk-averse but also tend to be perfectionists. They prefer the tried and tested. By contrast, businesses – in particular entrepreneurial medium-sized companies – tend to innovate, their goal being to obtain first mover (or at least early follower) advantage in their market sector. They choose or need to take business risk on a daily basis.

So how can these different perspectives be reconciled? How can these two character types best work together? As the bestselling book *Men are from Mars, Women are from Venus*[1] suggests, it is essential that two polar opposites communicate and make real efforts to understand each other, as difficult and insurmountable as it may seem. Just like men and women wishing to have great relationships, lawyers and their clients need to make the effort and communicate their needs, wishes and expectations. Paying lip service and hoping to get what they want will not work in the long-run (at least not with the same woman).

But wait… there's a fundamental difference: while in a romantic relationship Venus and Mars (one would hope) equally 'want' and 'need' each other, lawyers need the clients more than the clients need the lawyers. The legal industry is clearly a buyers' market, and will stay that way for any foreseeable future. The lawyer as the service provider has to ensure that he or she understands how clients make buying decisions in relation to legal services. It is the clients' needs alone which are at the centre of the relationship. Lawyers have to make sure that they please their clients. They need to understand the criteria on which clients base their buying decisions; how clients decide what legal service(s) they need; which law firms or lawyers they choose; and what makes them decide to change law firms.

The times are a'changing

Law firms operate in a drastically changed environment compared to less than a generation ago. The legal sector underwent greater transformations during the last two decades of the 20th century than in the last two centuries. In the 21st century, the changes have only continued to take place. Deregulation and liberalisation, particularly in England and Wales due to the Legal Services Act 2007, increasing consumer expectations, new information technology, generational differences and globalisation have resulted in a significantly changed, increasingly competitive marketplace. In the current economic climate most markets are still stagnant or at best growing more slowly than before and are significantly more price-sensitive.

Increasing numbers of lawyers, international competition and new entrants to the legal industry such as legal process

outsourcing (LPO) firms, are challenging the traditional law firm business model. Many services that were once considered to be highly specialised are being treated more and more like commodities today. Clients no longer necessarily consult only with traditional law firms. The internet provides some legal and business information at no cost. Professional associations offer online resources such as model documents, guidance notes and checklists. Supermarket chains such as Tesco and other retail stores sell do-it-yourself legal kits. Unless a legal issue is important to the company's core business activity and the client recognises that there is exposure to risk, the client may not buy legal services from a law firm, but instead seek alternative – less expensive – solutions. As Professor Stephen Mayson comments, "The AA [Automobile Association] and HBOS [Halifax Bank of Scotland] are doing [legal] work on a massive scale. There aren't that many law firms around that can compete. Are we going to roll over, or think about consolidation? … The one thing that makes an industry vulnerable is the incumbents not changing. Thinking like lawyers could spell the end."[2]

Many corporate clients have become sophisticated buyers and consumers of legal services since the 1980s, often having received the same training as external legal services providers. In some companies, the purchasing department now buys legal services, rather than the CEO, chief financial officer (CFO) or the in-house legal department. Clients today increasingly question and challenge the views of outside providers. They expect to benefit from a firm's accumulated experience, methodologies and efficiencies (and therefore cost advantages) that come from dealing with similar problems before. And they want to be involved in the process, understand what is going on and why, be kept informed of their options and be kept updated on the progress. This is particularly true for top decision-makers in medium-sized companies.

Law firms as businesses

As painful as it may be to the traditionalist's view of the profession, from a microeconomic point of view, a law firm is essentially a service business like any other: it renders services to clients for payment. Like any other business, a law firm needs to adhere to the basic principles of economics: profitability and financial liquidity. In addition, it needs to carefully manage its market position, levels of productivity and innovation, as well as its ability to recruit and retain professionals. The growth in the size of the profession, the size of firms and the volume of the market, has led lawyers to have to treat the practice of law as a business. Any businessperson will tell you that customers are the lifeblood of any commercial organisation. Without customers – or clients – an organisation has no revenues, no profits and therefore no market value. Providing legal services today is a service business and the client determines satisfaction. Sir David Clementi, who was appointed by the UK government to undertake a wide-ranging independent review of the regulation of legal services in England and Wales, believed that access to justice requires not only that the legal advice given is sound, but also "the presence of the business skills necessary to provide a cost-effective service in a consumer-friendly way".[3]

There is no denying that the legal profession – once driven by the practice of law itself – today is driven by the clients. Lawyers no longer have the luxury of waiting for business to come to them. They have to go out and get the business. With clients becoming more

demanding and less loyal, firms increasingly have to compete not only with each other but also with new business models to attract and retain clients. For some time, technical legal competence alone has been insufficient or, at least, no guarantee of success in winning new business or retaining existing clients. If law firms do not update their business models and approaches, in terms of service delivery, they will be unable to survive the challenges of the changing industry landscape. As Lindsey Muir and Alex Douglas put it, "A once elite and learned profession is now operating in a competitive, cut-throat business environment much like any other profession."[4]

The solution: Marketing?

There is general recognition in academia and business that marketing provides the answers for organisations faced with competitive challenges and that the implementation of the marketing concept is necessary to ensure an organisation's long-term ability to survive. The marketing concept holds that the way to success lies in continually meeting customers' needs. This is particularly important for service firms due to the direct interaction with their customers. Marketing is linked to a number of benefits, including improved business performance, customer perception and loyalty. Marketing can potentially help focus attention on service delivery and offerings in chosen market segments and detect early warnings should a client be in danger of being lost.

Business strategy clearly demands a marketing perspective, whether or not lawyers are willing to recognise or acknowledge it. Lawyers need to keep in mind that clients are the reason for the existence of the legal profession and not *vice versa*. If one firm cannot or does not supply the services desired, its competition will. Since unsatisfactory relationships between professional service providers and clients present problems for both parties, understanding how organisations select and subsequently evaluate professional services is critical.

While marketing guru Philip Kotler described marketing as "the most reasonable and voluntary way for people to acquire goods in a civilized society"[5], lawyers' feelings towards marketing generally have historically been less enthusiastic. Traditionally, lawyers not only disliked marketing, but considered it unprofessional and inappropriate. The strong influence of tradition and history in the legal profession and its consequences in terms of the understanding of the value, the perception of and the attitude towards marketing were substantial barriers to the advance of marketing in this field. This may, in part, be due to marketing having often been equated with advertising among lawyers. As this is not an uncommon misconception, the Chartered Institute of Marketing stresses in its definition that:

"[m]arketing is sometimes wrongly defined within the narrow context of advertising or selling, but this is not the whole story. Marketing is a key management discipline that enables the producers of goods and services to interpret customer wants, needs and desires and match, or exceed them, in delivery to their target customers."[6]

While there are distinct challenges or barriers to the marketing of professional services, the hope is that lawyers internationally will eventually understand that marketing is not inherently unethical or manipulative, nor is it defined by the field of advertising. It is a tool for achieving competitive advantage. Lawyers need to keep in mind that anyone in the firm who is in touch with clients is the service,

personifies the organisation in the client's eyes, and is therefore the 'brand' and the firm's marketer. There should be little debate that marketing plays a central role in a law firms' operations. What is of concern is the effectiveness of any marketing undertaken.

What needs to be done?

The marketing concept implies more than merely delivering a service; it requires a thorough understanding of the clients' needs and wants and an in-depth knowledge of what factors impact and drive their decisions. Only when looking at the firm from the client's perspective and understanding the decision-making process of buying legal services, is it possible to predict a client's choice of law firm and develop a competitive edge essential for long-term success.

While it may be tempting to forego such analysis, assuming knowledge of what clients expect or value is wrong. Assumptions do not make effective strategies. Studies have found significant differences regarding the importance of attributes of selection and evaluation between users and providers of professional services. According to Susan Hackett of the Association of Corporate Counsel:

"Many law firm lawyers are woefully ignorant of what corporate counsel do, what their clients demand from them, how they operate, and what drives their buying decisions. […] most law firm lawyers aren't even aware of this knowledge gap."[7]

Law firms need to understand the entire buying process by which their target clients identify, evaluate and ultimately select, as different segments of clients might have distinct preferences. In addition, clients' behaviour is dynamic, changing and evolving, and thus requires continuous monitoring. Only through careful analysis and better understanding the challenges, needs and expectations of prospective buyers can firms be confident that they are engaging with the clients on their terms.

What exactly is a medium-sized company?

There is no universally accepted definition of a 'medium-sized company', but there are a number of official definitions. Countries typically classify companies for economic analyses and political discussions, competition rules, funding and promotional programmes. Some definitions are based on quantitative criteria, while others are a combination of quantitative and qualitative criteria. Quantitative criteria include data such as employment, turnover and asset size. While they are relatively easy to obtain and measure, they vary significantly by industry and country. It is therefore necessary to apply different approaches depending on the industry to which an organisation belongs. The number of employees might be a better 'fit' for services, while for manufacturing the turnover may be a better indicator. The balance sheet total is not a good measure as it can be increased for reasons which are not connected to the size of the enterprise. Quantitative measures need to be seen in relation to the economic activities which the enterprise carries out, as, for example, some industries tend to be labour-intensive, while others are not. A firm of a given size could be small in relation to one sector where the market is large and there are many competitors, whereas a firm of similar proportions could be considered large in another sector with fewer players and/or generally smaller firms. An enterprise with more than 500 employees may have the character of a medium-sized company, while an enterprise with 200 employees might have the character of, and be managed like, a big enterprise.

Due to these limitations a number of definitions take into account qualitative measures such as ownership, management or autonomy, the control of the business or beliefs and behavioural aspects that differentiate medium-sized companies from large firms. In qualitative terms, three types of enterprises can be defined:

- In type 1 or 'family enterprises', the manager is also the owner or a member of the owner family and decides short and long-term issues in the interest of the enterprise.
- In type 2 enterprises, the manager makes the short-term strategic decisions and prepares the ground for long-term decisions. The owners then decide in their own interest, typically aiming to maximise their profit and thus the profit of the enterprise.
- Type 3 enterprises belong to enterprise groups where strategic issues are decided in the interest of the group and in the group headquarters. It is possible that profits are not maximised within that enterprise but elsewhere, for example by setting internal prices deviating from market prices.

The main differences between medium-sized companies and enterprises belonging to such enterprise groups are to be found in qualitative features and not primarily in their size, therefore the main purpose for a definition of medium-sized companies is to describe enterprises of type 1 and 2 up to a certain size and to distinguish them from the rest of the enterprise population because their character is completely different.

The EU definition for medium-sized companies is based on both quantitative and qualitative measures. According to EU Recommendation 2003/361/EC a medium-sized company has to satisfy the criteria for the number of employees and one of two financial criteria – see Table 1.

Enterprise category	Headcount	and	Annual turnover	or	Annual balance sheet total
Micro	< 10		< €2m		< €2m
Small	< 50		< €10m		< €10m
Medium-sized	< 250		< €50m		< €43m

Table 1: Staff headcount and financial ceilings determining enterprise categories[8]

In addition, it must be independent, which means less than 25 per cent owned by one enterprise or jointly by several enterprises falling outside the definition of a medium-sized company. While the definition applies to all EU member states, the UK Department of Business, Enterprise and Regulatory Reform describes that a medium-sized company meets the following criteria:

- Turnover of not more than £22.8m;
- Balance sheet total of not more than £11.4m; and
- Not more than 250 employees.

The research discussed in this report defines a medium-sized company as any independent legal entity engaged in an economic activity, irrespective of its legal form. This includes, in particular, self-employed persons, family businesses, and partnerships or associations engaged in an economic activity. The headcount of a medium-sized company must not surpass 250. In addition, the annual turnover must not exceed €50m and/or the annual balance sheet must stay not exceed €43m.

Medium-sized companies – An interesting target group

Medium-sized companies are an interesting clientele for law firms due to their economic significance. Often called the backbone of economies or engines of economic and social development, they generate employment, economic growth and international competitiveness. In numerous countries they are the driving force for growth and future economic prosperity. In the European Union, 20.7 million small and medium-sized companies represent 99.8 per cent of all enterprises; provide around 89.9 million jobs by employing about 67.4 per cent of the workforce; and generate more than half of its value added.[9] The UK Department for Business, Innovation and Skills released a report in 2010 that of the 4.8 million private sector enterprises in the UK, 99.9 per cent were small to medium-sized. In 2009, SMEs accounted for 59.7 per cent of UK private sector employment (medium-sized companies accounted for 11.5 per cent) and 49 per cent of the UK's estimated business turnover of £2,400bn (medium-sized companies accounted for 14.3 per cent).[10]

The large number of small and medium-sized companies is of interest not just because of the sheer volume of potential business, but also due to additional advantages specific to the legal sector. A widely dispersed client base reduces the source of potential conflicts of interest compared to a more concentrated client base and thus potentially reduces situations in which law firms would have to turn down business. Medium-sized companies typically do not have an internal legal department as they appear to prefer outsourcing activities that are not directly related to their core processes. Thus medium-sized companies typically lack legal expertise, which causes them to buy legal services disproportionately to their size, outsourcing a wide range of legal services instead of handling the work internally.

While medium-sized companies have not historically been associated with international business activity, according to a study from the Organisation for Economic Cooperation and Development (OECD), they account for about a quarter of the exports in most industrialised nations.[11] Technological advances have stimulated the trend towards globalisation of business and trade, in which they have begun to play a critical role. Progress in logistics and distribution enables nearly every business to buy, sell and cooperate on a global scale. As a result, even smaller and locally oriented businesses today work in a global context, collaborating with partners, suppliers or customers in other countries. This wider market area requires the management of more differentiated legal and cultural issues, thus introducing a higher level of complexity as well as facing competitive pressures which characterise international markets and potentially necessitate a greater need for legal services.

The size of a company is likely to have significant impact on its organisational buying behaviour. However, the majority of existing – mostly non-academic – studies in the legal sector focus on the high value, multi-jurisdictional buying activity involving Global/European 500, FTSE 100 or Fortune 500 companies. Although some of the findings might be pertinent to medium-sized companies, law firms have to remember that medium-sized companies are different and have unique characteristics. These are determined by the inherent characteristics and behaviours of the entrepreneur or owner/manager as well as the size and stage of development of the enterprise.

Organisational buying behaviour

Traditionally, buying activity was seen as largely clerical with purchasing agents being evaluated on their negotiation skills. Purchasing performance was typically measured by the levels of price discounts obtained from suppliers. This 'reward' system fostered an adversarial climate between buyers and sellers since their goals were in direct competition. The model was characterised by a short term orientation, buying based on lowest price and very little interaction with suppliers other than the initial negotiations and to express post-purchase dissatisfaction when performance was poor.

Newer models of organisational buying behaviour imply that buyers and sellers take a longer-term perspective of their business activities. The satisfaction of joint goals ('win-win') is the desired outcome. To achieve efficiencies, many organisations started to reduce the number of their suppliers in order to build vendor loyalty/supplier partnerships. Suppliers get a larger share of the business and in return must provide high quality products and services more cost effectively.

The nature of organisational buying typically requires extensive decision-making. Organisational buying models suggest that buying is a complex process rather than a single act, consisting of a multi-stage decision-making or problem solving process that involves both buyers and users.[12] The individual buying decision process includes the stages of:

- Identification of needs;
- Search for information;
- Evaluation of alternative;
- Purchase; and
- Post-purchase evaluation,

while the organisational buying process comprises:

- Problem recognition;
- General need description;
- Service specification;
- Supplier search;
- Proposal solicitation;
- Supplier selection;
- Order routine specification; and
- Performance review.

These models provide the framework for high-involvement decision-making, applicable to the purchase of services as well as products, and individual consumers as well as organisational customers.

Linear decision-making models look at buying and selling as two separate functions. In addition, they lack feedback loops. For these reasons, circular decision-making models that integrate buying and selling allow the service providers to gain better understanding of the client's needs. In other words, in order to approach marketing/selling legal services successfully, law firms and lawyers need to thoroughly understand the clients' decision-making process.

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