

Realizing the benefits of legal managed services

EY research shows that progressive law departments are using managed services more and reaping significant benefits that go beyond cost savings.



Building a better working world



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Pioneering law departments will keep innovating and working with managed service providers to come up with new ways to transform the delivery of legal services.

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EY Global Legal Managed Services Leader

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Introduction

The pressures facing the modern in-house law department are significant and well documented. General counsel must ensure that their companies remain compliant with an ever-changing regulatory and transparency landscape, while managing the day-to-day operations of their departments. This includes short-term goals, such as implementing cost reductions and responding to changing market conditions, and longer-term challenges, such as attracting and retaining talent, utilizing digital transformation and creating efficiencies in the operating model.

For many law departments, turning to external legal managed services (LMS) providers offers a solution to some of these challenges. Over the past decade, the legal industry has been filled with anecdotal stories of law departments

using non-law-firm providers, often utilizing technology-enabled LMS models, to increase efficiency and lower cost. Up to now, however, there has been limited data available to analyze this trend. Due to this, the extent to which these services are being used and the benefits that law departments have realized as a result of adoption have not been widely investigated.

In this EY report, we examine data from more than 1,000 law departments to understand why some are actively using LMS, while others remain reticent. The report also reveals the benefits of using managed services providers over the short and longer terms.

The primary findings from the report are

1 **There are three clearly defined groups of law departments, based on their sourcing strategies.**

The report shows that there are significant differences in the way law departments use managed services. It also reveals that a group of innovative law departments have embraced the managed services model and are actively looking for ways to continuously expand its use.

2 **Law departments use LMS for complex and varied reasons.**

Examining the data across the three groups, it is evident that the forces driving law departments to use LMS vary significantly and extend far beyond cost reduction. EY research shows that the key drivers leading law departments to pursue LMS include:

- ▶ Cost-savings targets
- ▶ The desire to optimize internal processes due to rising volumes of work
- ▶ Access to better quality information on comparable costs and the productivity of internal and external resources
- ▶ The arrival of new LMS products and services allowing for new technology-enabled delivery models

3 **The benefits of LMS are often dramatic and multilayered.**

Not only are there significant near-term benefits to be had from using LMS that extend beyond cost savings, but also there are ongoing positive impacts around technology, human resources and the ability to continue innovating in the future.

This research shows that law departments that use LMS most widely enjoy a broad range of benefits in that they are:

- ▶ More cost effective in service delivery today
- ▶ More confident about improving efficiency in the future
- ▶ More confident in their ability to respond to geopolitical and regulatory changes
- ▶ More confident they have built the right set of capabilities within their departments
- ▶ Better able to attract and retain talent

These areas are examined in more detail in the following pages.

Methodology

This report is based on a survey of 1,058 senior legal practitioners from businesses in 25 countries, which was conducted by Euromoney Thought Leadership Consulting on behalf of EY Law teams. Respondents were clustered into three groups using latent class regression based on their adoption of legal managed services in their law departments. Reported differences are determined to be statistically significant using Pearson's Chi-squared test with multiple comparison correction (FDR = 0.05).

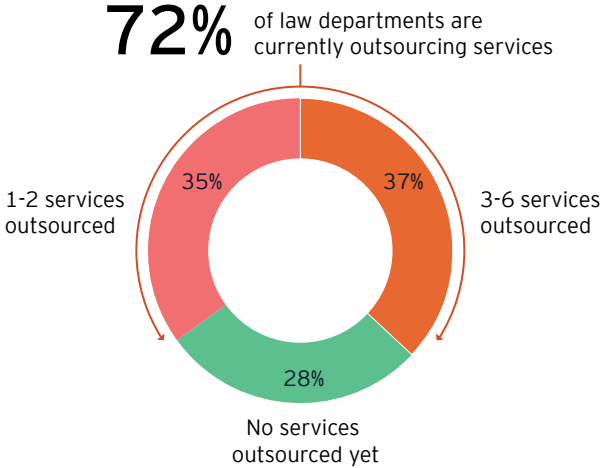
EY Advanced Insights brings together EY business leaders, thought leaders and data scientists to develop a data-driven understanding of the forces shaping the working world. They leverage advanced analytics and big data approaches to unlock deeper insights from data and create proprietary products and services to engage the market and EY clients.

Use of external managed services providers: three distinct types of law departments



To gain a sense of how widely law departments are using external LMS, we asked respondents which services they were currently “outsourcing” and which services they would consider outsourcing in the near future, as indicated in Figure 1.

Figure 1:
Law departments’ use of outsourcing



Status of outsourcing by service

Service	Currently outsourcing	Considering outsourcing	Total
Contract management	42%	34%	76%
Legal entity management and compliance	29%	46%	75%
Employment law	35%	39%	74%
Due diligence	29%	45%	74%
Document retention	30%	42%	72%
Records management	33%	38%	71%

Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)

Drilling deeper into the data, we were able to identify which law departments are using external managed services providers more than others. Using advanced statistics, we clustered respondents into groups based on their reported adoption of LMS across six law services (see Figure 2 for list of services). EY analysis shows that law departments clearly split into three distinct groups, which we labeled as follows (also see Figure 2):

Pioneers (37% of law departments)

This group is primarily made up of law departments at large- and medium-sized organizations.¹ These departments have been on a journey to transform their legal function. Many have already undertaken cost-reduction exercises, explored efficiencies, utilized legal technology and insourced certain types of legal work.

As part of their journey, this group has realized the benefits that new service delivery models provide and are looking for increasingly sophisticated solutions to improve the efficiency and effectiveness of their departments. They have already migrated many law services to non-law-firm providers and are actively looking to expand their use of LMS.

Explorers (35% of law departments)

This group is also mainly made up of law departments at large- and medium-sized organizations. These departments are aware of new models of service delivery that exist and the benefits that may come from using them.

The majority have tried outsourcing discrete tasks to external providers but have not done so on a widespread basis. These firms are actively considering expanding their use of LMS but may be unsure of how to proceed.

¹ Large- and medium-sized organizations are defined as those with over \$5b in annual revenue. These companies typically have law function headcounts greater than 50 and external and internal legal spend greater than \$50m.

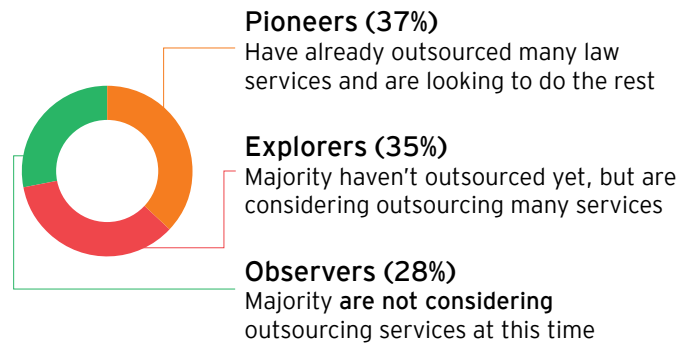
Observers (28% of law departments)

The majority of this group is largely made up of law departments at smaller organizations,² with businesses below \$500m in revenue making up the largest proportion.

Many of these departments are not considering using LMS currently even if they are aware of the benefits anecdotally.

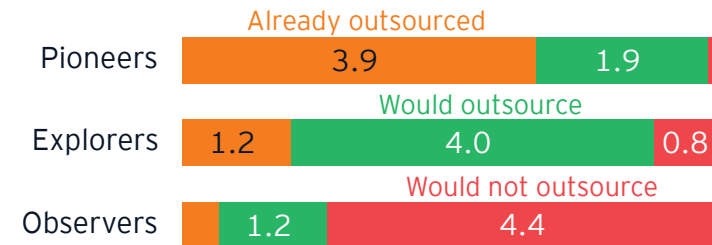
Figure 2:

Percentage of law departments by outsourcing strategy



Average number of law services outsourced

The six services assessed are contract management, legal management and compliance, employment law, due diligence, document retention and records management.



Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)

² Smaller organizations are defined as companies with less than \$5b in annual revenue. These companies typically have legal function headcounts below 50 and internal and external legal spend less than \$50m.



Smaller law departments may have difficulty innovating and leveraging new models — they need prepackaged solutions that are ready for use on day one.

Peter Krakaur

Managing Director, Ernst & Young LLP

EY Americas, Legal Operations Markets Leader

Why are there such differences in the sourcing strategies across law departments? Peter Krakaur, Managing Director, Ernst & Young LLP, EY Americas, Legal Operations Markets Leader, explains: “This data reveals something that many legal industry watchers already knew – that attitudes toward the use of managed services and the extent to which these services are used vary widely. It is also significant that smaller law departments fall more broadly into the Observer category.

“Larger law departments have the resources and bandwidth to innovate and leverage new models. They, along with their LMS providers, are innovating together and creating new services. Smaller law departments have difficulty doing that – they need prepackaged solutions that are ready for use on day one. Up until recently, these types of ‘ready-for-use’ solutions were not available, although that is changing.”

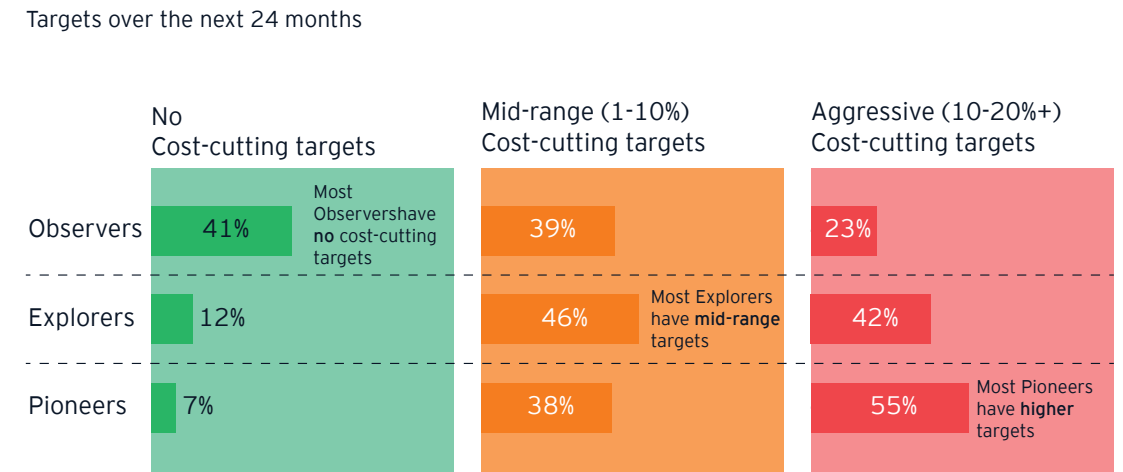
Drivers for greater use of legal managed services: a complex picture emerges



Leading law departments, many of them Pioneers, have been on a journey over the past decade. In many instances, the journey began during the global financial crisis with the need to reduce costs, including putting significant effort into optimizing external counsel costs with strategies such as rate freezes and price negotiations, along with the need to reduce the number of vendors.

It is interesting, then, that of the three groups, Pioneers continue to have consistently higher cost-cutting expectations – with 55% having targets in excess of a 10% reduction (see Figure 3). This contrasts starkly with Observers, the majority of whom have lower (or no) cost-cutting targets.

Figure 3:
Cost-cutting targets over the next 24 months



Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)

Why do Pioneers, the law departments that have done the most to transform their operating models, have higher cost-reduction targets? It appears that these departments' prior successes with transformation may be the explanation.

As John Knox, EY Global Legal Managed Services Leader, observes: "Many law departments begin their transformation journey with relatively modest goals. Early successes against these goals often leads law department leaders to realize more can be achieved than they initially believed, which leads to more ambitious plans."

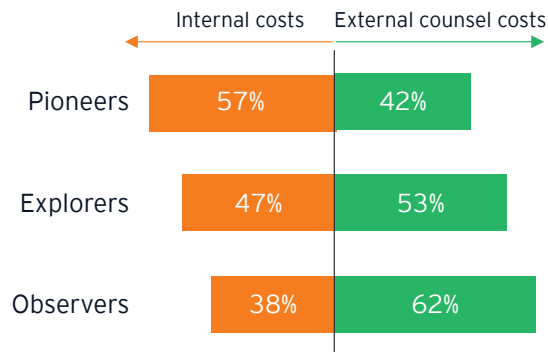
Optimizing internal operations

The data shows that Pioneers are considerably more focused on optimizing internal processes than Explorers or Observers (see Figure 4). At first glance, this focus may seem counter intuitive. At a typical law department, 40% to 60% of total costs lie with outside counsel,¹ with the lion's share of this spend being on law firms. So why aren't Pioneers focused on reducing law firm costs to drive efficiency?

¹ Data from the Association of Corporate Counsel's Global Legal Department Benchmarking Report 2020 suggests that law firm spend as a percentage of overall legal spend varies widely based on the size of the organization and the industries in which they operate.

Figure 4:
Cost-cutting focus

% of law departments by area of cost-cutting focus



Pioneers believe **internal resources** and functions are their greatest opportunity for cost saving

Explorers and Observers believe **external counsel costs** are the biggest opportunity for cost savings

Why are Pioneers focusing on internal cost savings?

Pioneers have already put significant effort into optimizing external counsel costs over the past several years and are now turning inward – focusing on optimizing internal resources and functions.

Many Pioneers have, indeed, put significant effort into reducing and optimizing their use of law firms. However, while work remains in this area, the growth in headcount experienced by many law departments over the past decade may help explain the inward turn.

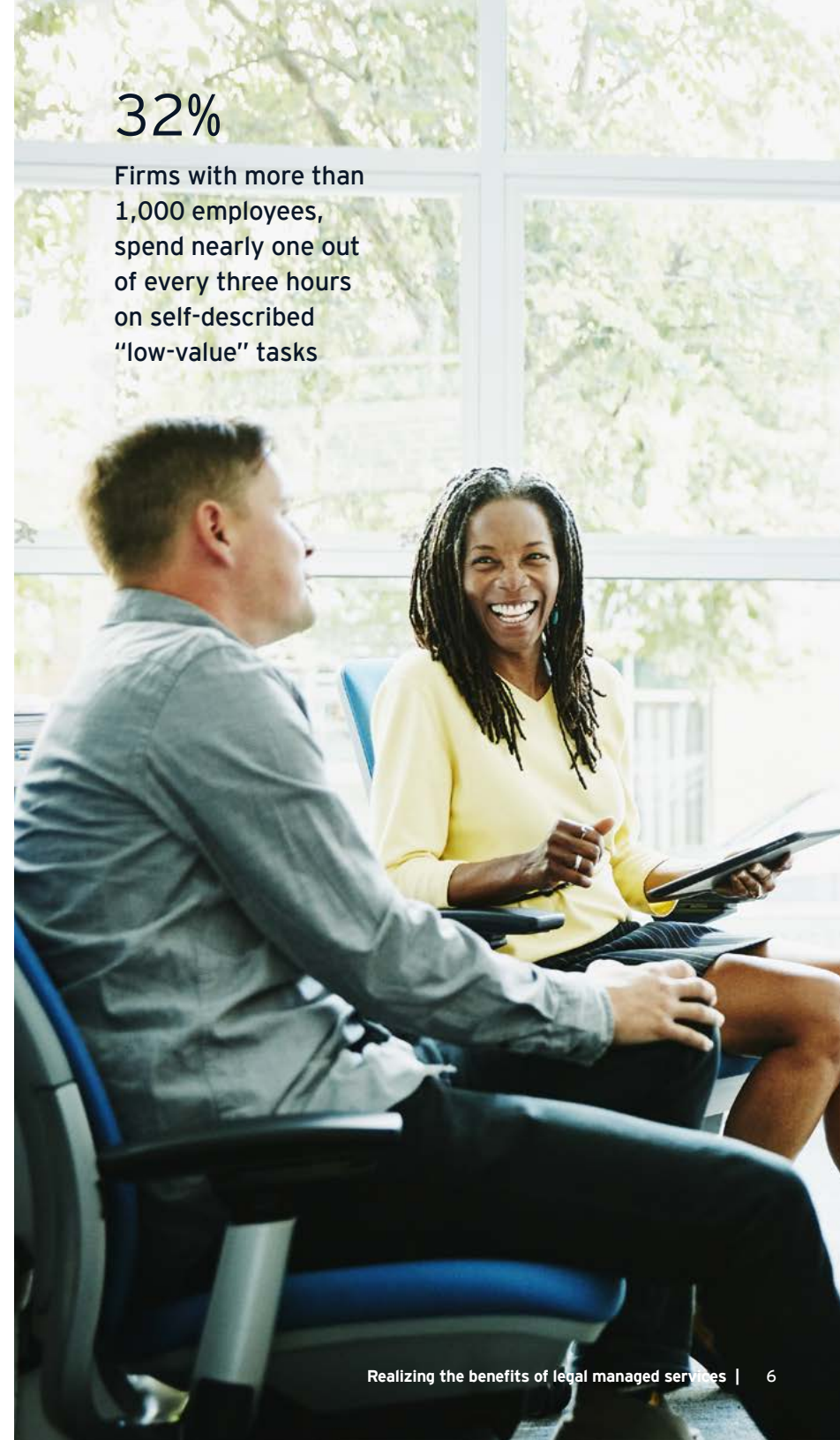
After the 2008 global financial crisis, many law departments hired aggressively. This was a natural reaction to the options they had at the time. In this period, alternative service providers were in their infancy and few had the necessary scale to partner with large law departments. General counsel were faced with the choice to either buy from law firms, with their high and rising costs, or build their own capabilities in house. Many chose the latter option.

Yet, while insourcing saved money, it created challenges. Many law departments are now the size of medium (or even large) law firms. Managing these departments has become a full-time task for senior department leaders. Additionally, insourcing flooded departments with new work. Many legal functions are now spending an increased amount of time on high-volume work. The EY *Reimagining the legal function 2019* report found that large law departments, those with more than 1,000 employees, spend nearly one out of every three hours (32%) on self-described "low-value" tasks.

These factors have led law departments to a broader rethink of their operating models and sourcing strategies.

32%

Firms with more than 1,000 employees, spend nearly one out of every three hours on self-described "low-value" tasks



Note: For simplicity, the response "Other" which accounted for <2% of responses was omitted

Source: EY *Reimagining the Legal Function Survey Data* (Survey Size = 1,058 Law Departments)

As Peter Krakaur notes: “When law departments acknowledge the need to optimize the work that people are doing internally, they tend to rethink their entire process to understand who is doing what. Once you start doing that, particularly from an aggressive cost-reduction perspective, it opens the door to managed services because of the need to look at different ways of sourcing the work beyond the in-house law firm paradigm. The result is that internal optimization often leads to external optimization and greater use of managed services.”

This process, to some degree, can be seen in the data. It is well documented that leading law departments have made significant efforts to upgrade their systems and processes in areas such as matter management and workflow management, thus giving them access to detailed and timely information. When examining how confident they felt in that information, we discovered that Pioneers had considerably more confidence when it came to understanding not only the cycle time of cases but also the costs of external firms and the productivity of internal and external resources (see Figure 5).

Through this access to better quality information, Pioneers are more clearly able to define what work their departments should and should not be doing – indeed, they are almost twice as likely to be able to do this as the other two groups. Better quality information also allows these departments to define the best delivery model for different types of tasks. For example, Pioneers are twice as likely to have identified which tasks should be self-served by the business.

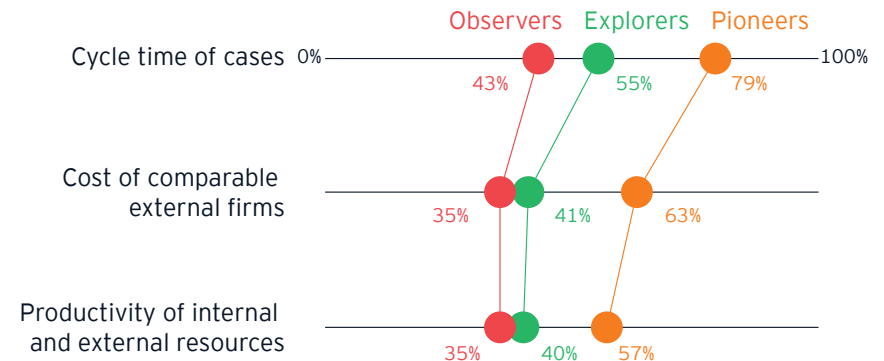
In summary, Pioneers have high cost-reduction expectations that have pushed them to rethink the way their departments work. Having been on a transformational journey for some time, many have already redesigned their relationships with their law firm partners to reduce cost and are seeking new approaches to continue saving money and increase efficiency.

Having put significant effort into upgrading their systems and internal processes, Pioneers have better data on the productivity of internal and external resources, allowing them to more efficiently diagnose their problems and identify solutions, including using external non-law-firm providers and managed services more extensively. This process explains why Pioneers are outsourcing more than their peers.

Figure 5:

Law departments’ access to detailed and timely information

% of law departments that are very confident in their data in the following areas:



Pioneers report having better access to a broad range of management information

Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)



Why do Pioneers have better access to management information?

Many leading law departments have spent significant effort over the past decade upgrading their systems and processes (examples: matter management system and workflow systems).

The multilayered benefits of managed services: going beyond just cost savings



EY research on the use of LMS by leading law departments reveals a broad range of benefits. These include cost savings, increased efficiency and the ability to shift a department's focus to the most important tasks.

These benefits don't exist in isolation, however. Subsequent benefits can also be gained, including:

- The ability to shift funds toward building new capabilities
- Improvements in talent – across morale, recruitment and retention
- An improved ability to manage complex high-value tasks

EY research confirms that law departments using managed services more extensively are enjoying many of these benefits. However, the results also revealed another significant factor: those that are more engaged with – and are actively using – LMS have more confidence in their operations, their ability to manage costs and in the future of their departments.

Increasing efficiency and managing cost

Pioneers are almost twice as confident as other law departments in their ability to manage third-party providers. Given that external costs typically make up a significant portion of overall spend for law departments, managing them is incredibly important to increase the efficiency of the department.

Indeed, the data shows that 62% of Pioneers reported being very confident in their arrangements with third-party providers, compared with 34% of Explorers and 25% of Observers. The wide difference between these groups provides strong evidence that managed services models, and the savings they provide, allow Pioneers to increase the overall efficiency of their departments.

Furthermore, Pioneers feel more confident that their vendor relationships provide them with greater access to data and technology. Given Pioneers' greater use of technology-savvy alternative services providers, their confidence in these areas seems understandable. Managed services providers tend to bring significant data, technology and process expertise to the table. The way they work, in close partnership with clients, also allows for knowledge transfer between the service provider and the client.

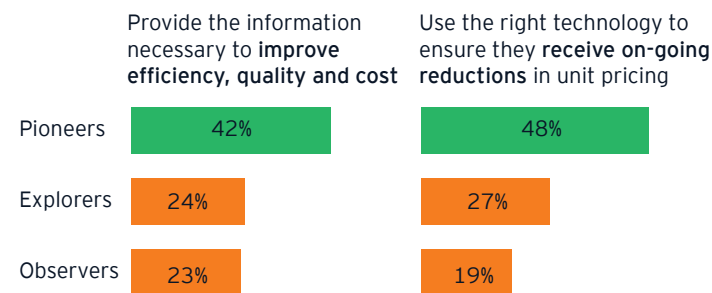
Heidi Stenberg, EY Americas Legal Function Consulting Leader, notes: "Data, technology and process improvement is a key aspect of every LMS engagement. LMS providers bring a lot of technology expertise and data to their engagements. Clients typically want LMS providers to identify the appropriate technology for their situation and then to implement that technology in a way that embeds it into the day-to-day working of the department. While this has immediate impacts on efficiency, it also has longer-term impacts on the department's openness to future technology and process automation initiatives."

The LMS working model and the data in Figure 6 suggest that managed services providers' impact is twofold. Not only do they deliver benefits now, but also they allow law departments to continue increasing efficiency and reducing unit costs in the future. This is significant as most departments seek constant improvement rather than episodic gains.

Figure 6:

Law department's confidence in their service providers

% of law departments who are very confident in their service providers



Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)

Focusing on what matters most

It has long been recognized that law departments are spending an inordinate amount of time on high-volume routine tasks. As noted earlier, the EY *Reimagining the legal function 2019* report found that large law departments, those with more than 1,000 employees, spend nearly one out of every three hours (32%) on what they described as "low-value" tasks. This focus on low-value work lowers morale and has a negative impact on recruitment and retention. Similarly, it diverts energy and resources away from tasks that matter the most.

Managing high-volume work efficiently and effectively requires process, project management and other skills that traditional legal providers do not necessarily offer, have the expertise in or the desire to handle.

By using LMS to handle specific tasks, Pioneers report that they are more able to focus on the key issues. As a result, they report being significantly more confident in managing the complex risks facing their organizations, including new privacy and disposition rules, investigations and major regulatory events, such as IBOR and BEPS (see figure 7).

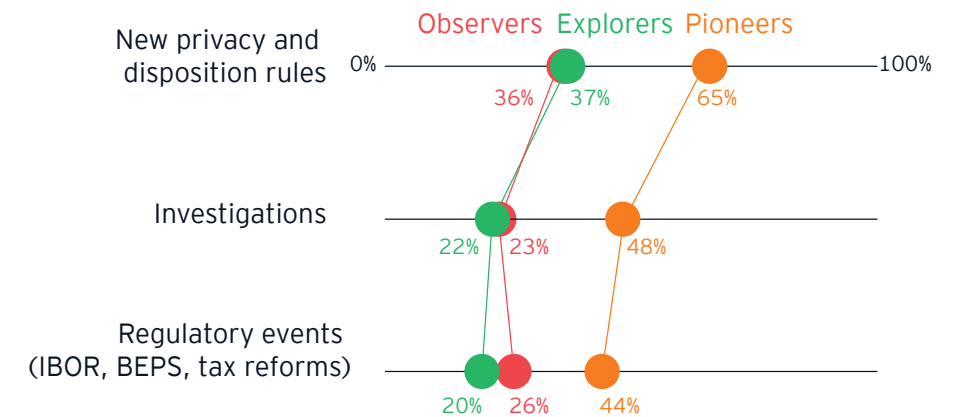
"The importance of this finding should not be overlooked. These events are likely to impact almost every part of a law department's organization and pose significant financial and nonfinancial risks," notes Peter Krakaur. "The fact that Pioneers report significantly higher confidence in these areas is important. Increasing focus on and confidence in the management of these high-value, high-risk events should be the goal of every law department. If managed services can assist in this goal, as appears to be the case from the data, it makes a compelling argument for any law department considering new sourcing models."

Outsourcing provides Pioneers with greater access to information and technology, allowing them to continue increasing efficiency in the future.

Figure 7:

Law departments' confidence in their readiness plans

% of law departments reporting they are **very confident** in their readiness in the following areas:



Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)

Pioneers are more confident about managing the complex risks facing their corporations

Furthermore, the shift to outsourcing certain tasks appears to have positive impacts on Pioneers' ability to recruit and retain talent. The reason for this is straightforward. As Pioneers have shifted high-volume work to managed services providers, in-house counsel are able to focus on higher-value work, improving morale and the attractiveness of the business to future hires. Notably, the data shows that Pioneers are the only group where a majority of respondents report that recruitment and retention is not a challenge.

Additionally, the use of LMS has benefits on law departments' ability to invest in new capabilities. Pioneers are twice as confident that they have the appropriate non-legal competencies as the other groups. They also are twice as likely to report they have the necessary technology and process automation skills.

Why are Pioneers more confident in these areas? One hypothesis is that Pioneers' relationships with technology-savvy LMS providers are yielding benefits. Another explanation is that Pioneers' use of outsourcing has freed up time and resources, allowing the department to identify and invest in the skills it needs to manage the department and tackle its most important tasks. Given the increasing importance of technology and process automation, such an outcome is significant.

As Rutger Lambriex, EY EMEA Legal Managed Services Leader, points out: "We had anecdotal evidence about many of the benefits of using LMS, but this report confirms what we had long suspected. If you free up lawyers' time for more sophisticated work and if you have access to technology and information to improve efficiency, you can demonstrate the value of the legal function to the business. This can fundamentally change the position of the law department."

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We had anecdotal evidence about many of the benefits of using LMS, but this report confirms what we had long suspected. ... This can fundamentally change the position of the law department.

Rutger Lambriex
EY EMEA Legal Managed Services Leader

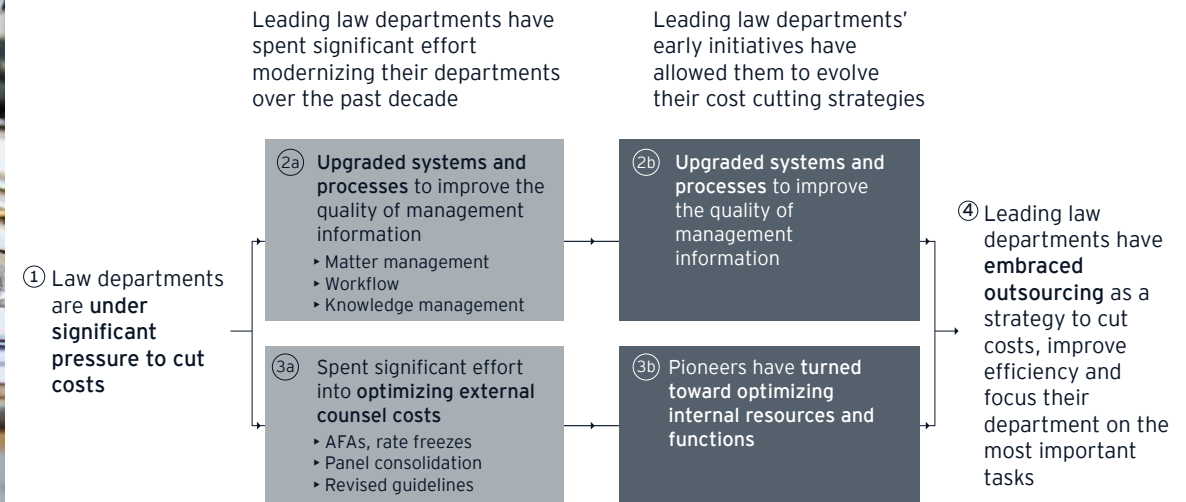


Conclusion



This report highlights three distinct attitudes to the transformation of the in-house law department and the use of LMS- providers. It also highlights that the forces driving law departments to use these services vary significantly and extend beyond simple cost reduction.

Figure 8:
The forces driving greater use of LMS



Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)

Ultimately, the report demonstrates that progressive law departments utilizing managed services – those that we define as Pioneers – benefit in ways that others miss out on. Not only are they more efficient today, but also they are more confident about future efficiency. They have more faith in their ability to respond to geopolitical and regulatory changes and are more confident that they have built the right capabilities within their departments. Importantly, they also are better able to attract, retain and appropriately deploy talent.

These Pioneers have been on a longer transformational journey with regard to optimizing their operational models and, having made necessary changes to internal resourcing, have often been early adopters or first movers when it comes to shifting toward managed services. This journey has been marked by innovation and collaboration.

“Some general counsel are ahead of the game when it comes to the use of the new generation of legal services providers,” says Peter Krakaur. “Indeed, I’d say the Pioneers have played a role in helping define these services. They have come to managed services providers with a challenge that needs addressing and have often played a role in co-developing solutions. They’ve effectively been partners in the ecosystem.”

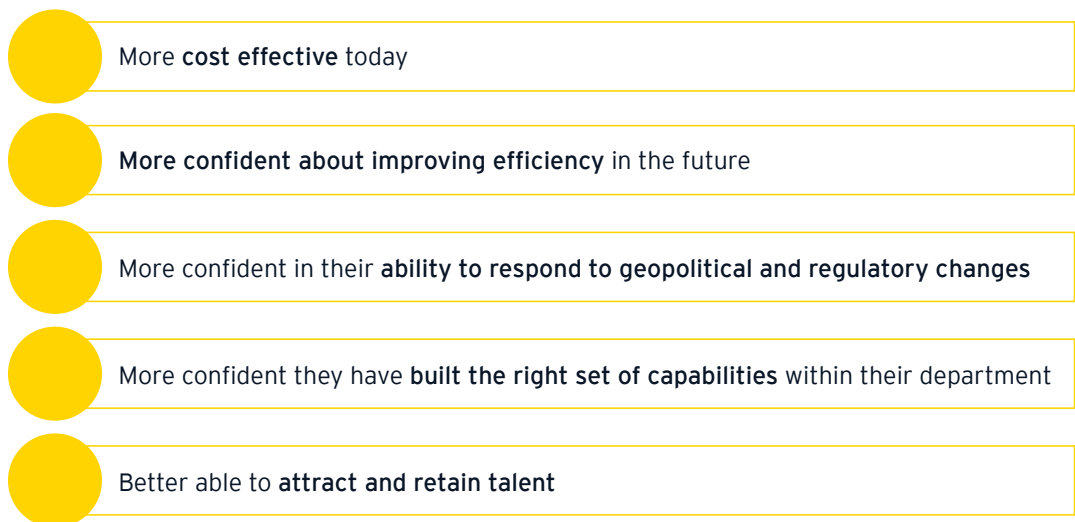
Considering the benefits that are realized from the use of LMS, as clearly demonstrated in this report, it is our expectation that this deep partnering is likely to continue.

As John Knox notes: “Pioneers will keep innovating and working with managed services providers to come up with new ways to push this model. In the next phase, we also expect to see that managed services models will become even more defined – more ‘plug and play.’ This will help the Explorers that are looking to take their next step on their journey.”

It also will help the Observers. As shown in this report, those legal departments are generally smaller and need ready-made products that they can implement from day one. Indeed, in some respects, the collaboration between LMS providers and the Pioneers may well have paved the way for Explorers and Observers.

As Rutger Lambriex concludes: “In this exploration of how law departments are using LMS, this report has uncovered the drivers and revealed compelling reasons for the use of those services as part of operational transformation. Significantly, it has also pointed to how they may develop from this point.”

EY research shows that law departments which use LMS more extensively are ...



Source: EY Reimagining the Legal Function Survey Data (Survey Size = 1,058 Law Departments)





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EYG no. 004082-20GbI

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