Innovation the next frontier for law firms

In the first of a three-part series, Nick Humphrey considers innovation, what it is, why it is important and why he believes lawyers have generally been such poor innovators.

Innovation is crucial for modern law firms, but it is often misunderstood. The concept involves finding a new way of doing something. It is about:

- using fresh ideas to create more effective processes, more dynamic products or better ways to deliver your current services;
- ‘thinking outside the box’ and challenging the accepted way of doing things; and
- lateral problem solving and maverick thinking.

Innovation means more than simply generating a new idea. It is the ability of the organisation to convert the new idea into value and ensure that the value is utilised throughout the different parts or divisions of the organisation.

Why is innovation important?

Innovation can be an important catalyst for growth and help a firm to evolve and adapt to a rapidly changing and increasingly complex marketplace. As the diagram below suggests, it can deliver a range of benefits, including allowing firms to differentiate from their competitors and potentially contributing to higher profitability and better client service.
Over time, almost all goods and services, no matter how pioneering, will become a commodity or perhaps even obsolete. In the music industry, for example, the introduction of CDs was revolutionary at the time and made tapes and records obsolete, but they have now been replaced by MP3 players and other devices.

In a similar vein, the legal profession is now bracing for changes to its business model that most partners or practice leaders could not have anticipated a decade ago. Until recently, many firms did not need to innovate to survive, and innovation was thought to be the sole preserve of high-tech and pharmaceutical companies. However, the past few years have seen dramatic changes in competitive environments for most, if not all, industries, including legal services. The convergence of globalisation, rapidly evolving technologies and the prevalence of outsourcing has significantly increased the need for firms to improve their efficiency.

Not only must they control costs and improve productivity; legal firms must also innovate to deliver better products and services or risk being supplanted by offshoring, insourcing or brave new providers who embrace integrated technology solutions or multidisciplinary teams.
With regard to offshoring, countries such as India, Thailand and Vietnam have enormous populations of highly educated professionals. In India alone, there are more than a million university-educated lawyers, accountants and consultants, with salary levels at 80 per cent less than their counterparts in the United Kingdom or the United States.¹

Professionals who think those countries will only provide labour-intensive or low-skill services should be wary as the nature of processes outsourced in the past five years has transitioned to encompass not only back-office work but value-added work and more highly skilled tasks. It is now reasonably common for large accounting firms to use offshoring when preparing audits of their major clients. As a consequence, law firms must be prepared to react and innovate.

In this rapidly changing environment, three main drivers are increasing competitive pressure on lawyers.

1. The first is the ‘more for less’ challenge.² Clients, especially corporate clients, are all demanding far better service for a lower cost. Since the global financial crisis, clients are far more cost conscious.

2. Another key factor is ‘liberalisation’, meaning that non-lawyers are permitted to deliver certain types of services that in the past were provided only by lawyers.³ These services can be provided by paralegals, law clerks or non-lawyers and we even see documents automatically generated by software in response to questionnaires.

3. Rapid technological advancement is playing a highly disruptive role within legal firms. There are three categories of transformative technology:

   - The internet and advanced telecommunications have dramatically changed professional services. They make geographic distance far less relevant, so work can be quickly and easily transmitted across large distances.
   - A plethora of websites are now offering a range of legal services and advice for consumers. LegalZoom, for example, is a website which helps consumers create basic customised legal documents.
   - Automation allows lawyers to automatically generate documents based on client questionnaire answers, reducing the need for laborious formatting and ‘grunt work’.

**Why are lawyers such poor innovators?**

Against this background of change and the requirement for law firms to rethink how they do things, the truth is that lawyers have not typically been seen as ‘innovators’. Some potential reasons include:
Lack of requirement: Until the global financial crisis, many lawyers had not really needed to innovate; they simply increased their hourly charge-out rate at the beginning of each financial year and continued to operate in the way they had for many decades before.

Risk aversion: Lawyers are also typically highly risk averse. They have been trained to analyse the risk or downside in every situation. Risk aversion is deeply engrained into everything they do and their heuristic style is designed to reduce or eliminate risks.

Indoctrination: The rigorous training of professionals may indoctrinate a narrow perspective on problem solving and a systematised preference to rational thinking over creativity.

Some commentators argue that the entire education system – from school through university, as well as the system for professional accreditations – is designed to focus on a very narrow range of skills, styles and talents. British education advisor Sir Ken Robinson argues that our education system “kills creativity” as it not only stigmatises failure, but narrowly focuses on mathematics and sciences and “exiles the arts and humanities”. From an early age, we are told there is no point in studying any creative subject as you will not be an artist/actor/dancer/novelist when you finish school or university.

In the battle between efficiency and innovation, meanwhile, many professional service firms have built cultures of efficiency. Management drives financial performance and sets target metrics, which in most law firms are measured in billable hours and reported real time. Partners are judged on team utilisation, realisation, hourly rates, billable units, daily profit targets, WIP lock-up and fee-to-salary ratios. Increasingly sophisticated financial recording and reporting systems are implemented and, more often than not, the primary or sole criteria for financial reward and promotion for partners and staff are those financial metrics.

Many law and accounting firms require their producers to record 6.5 hours of billable time a day, measured in six-minute increments. Some New York lawyers pride themselves on doing 2500 billable hours per year or more. In this culture, where is there time left for creativity? Who would dare to do anything other than billable work if that is all that is tracked, recorded, celebrated and rewarded.

The focus for many managers and management teams in this environment is often on left-brain rationality, whereas innovation typically comes from right-brain creative processes. As the following factors reveal, there are often competing forces at play:
• **Hemisphere of brain:** The efficiency culture requires ‘left brain’ activities. Productivity is driven by logical, rational styles of thinking. Innovation, however, requires ‘right brain’ activity. The right hemisphere governs conceptual, intuitive, imaginative types of thinking. It is the domain of creativity and lateral thinking.

• **Measurability:** Efficiency is measurable and objective. It can be tracked and legislated by management: you will produce six billable hours a day, 1500 billable hours a year and so forth. It is hard to measure innovation and its attainment is fairly subjective. Furthermore, you cannot legislate for more innovation. Imagine management saying: “Please produce another 10 units of innovation today.”

• **Management styles:** Efficiency is driven by a command and control mentality. Strong management is needed to legislate and track targets. Efficiency flourishes under micro-management. In contrast, innovation is a result of strong leadership, which engenders trust and collaboration (aspects typically stifled by management and their metrics and tracking tools). Innovation requires leaders to be inspirational, infectious and communicate their vision in a way which is relatable and empowering.

• **Motivators:** Efficiency responds well to incentives tied to meeting the metrics. There is, however, evidence to suggest that financial incentives simply will not work to encourage creativity and may, in fact, hamper intuition. This type of thinking responds less to financial rewards and more to autonomy and the intrinsic rewards of problem solving.
Perspective: Efficiency is primarily an introspective culture, whereas innovation is more likely to flourish when you take a client-centric and external mindset.

So it is clear that while innovation is important, achieving it can be complicated given the pressures on modern law firms and the traditional way in which lawyers approach their work. Yet embracing change and innovation must be on the agenda for firms if they hope to prosper in the years and decades to come. With that in mind, the next part of this series examines ways in which lawyers can learn to innovate.

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Sources:
1 Austin Chambers, Casey Lekahal, Katie Nelson, Jean Pyun and Gavin Wolny in their article, “Transformative Change: Outsourcing the Practice of Law”, University of Colorado, 2013.
3 Susskind, ibid, page 5.