

# OFFSHORE OUTSOURCING: WHITE ANT OR VALUE DRIVER?

*Like it or not, business development and professional services marketers may soon be forced to broach a subject that some firms have so far been reluctant to embrace – outsourcing. Mark Phillips reports on how outsourcing is rapidly transforming the legal sector and the implications it could have for all Asia-Pacific professional services firms.*

Ten years ago Baker & McKenzie took a punt that paid off big time. It decided to embrace ‘offshoring’ and established a small team of employees in Manila whose job was to type and edit dictated copy sent from Baker & McKenzie offices around the globe. Today, Global Services Manila handles not only back-office work but also a raft of higher value services, saving the entire Baker & McKenzie organisation a reported US\$25 million per year.

As more organisations look to global delivery as a means of reducing costs, an increasing number are turning to outsourcing. Last year the miner Rio Tinto outsourced document review, legal research and contract review and drafting to multinational services provider CPA Global in a bid to improve internal teams’ responsiveness to business needs. This also allows internal teams to focus on more complex legal matters that might otherwise have been sent – at significant cost – to external counsel. According to Eve Johnson, CPA Global Senior Manager Asia-Pacific, the process has already saved Rio Tinto more than US\$14 million.

In April this year Microsoft expanded its relationship with India-based legal process outsourcing (LPO) provider Integreon, which delivers services such as document and contract review, as well as e-discovery. Even more recently,

boutique Sydney firm Advent Lawyers announced that it had aligned itself with Mumbai-headquartered outsourcing firm Pangea3.

## **Cost and efficiencies**

Speaking to *PSF Journal*, Advent Lawyers Managing Director John Knox would only divulge ‘off the record’ the hourly cost differential between the rate charged for work done at a junior level within a big law firm, compared to that charged by Pangea3. It suffices to say that the two are not even in the same ball park. However, he stresses that outsourcing is not always about cost.

“Cost is really just a by-product of response time and efficiency,” Knox says. “We were talking to one of the big banks about a project that involved thousands of documents every year. The lead time for their internal legal team to turn those documents around had blown out to six to nine days. While they appreciated the cost saving, more important was the fact that through Pangea3 the documents could be turned around in 48 hours.”

But not all professional services firms are keen to talk about outsourcing. Some refused point blank to discuss with *PSF Journal* whether they use the process at all, let alone if it factors into their business development and marketing strategies.

“The reason they’re not talking is because it cuts into their own lunch,” Knox says. “Traditionally clients approached law firms and asked if they could do something and, of course, the firms said they could do it all. And they’re still doing the lower-end process work



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*Outsourcing is a direct threat to the big business firm model. It will happen anyway through competitive pressure, but like most change in professional services it will be slow and grudging.*



and getting away with charging \$260 an hour for it. If they were to promote outsourcing they would be giving away a very profitable slice of business.”

Michael Bradley, Managing Director at Marque Lawyers and former Gadens Managing Partner, agrees.

“Low-level work is ideal for outsourcing – discovery, due diligence, small debt recovery and basically anything routinely done by paralegals in high volumes,” he says. “Firms could operate on a much lower cost base if they didn’t maintain

change in professional services it will be slow and grudging.

“Logically, lawyers should only be doing the things that only they can do,” he adds. “Everything else is always going to be done better and more cheaply by someone else. One of the principal drivers behind the massive size that professional services firms have now reached is that they have so much of their business committed to work they shouldn’t be doing. Therefore, in the end, they will have to outsource it. It will just be a long time



large teams of low-skilled people for that kind of work, but outsourced it and charged it on at cost or a small margin.”

An interesting parallel emerges when we look at what happened with non-professional services around 20 years ago. All photocopying used to be done in-house by law firms and represented a major profit centre for most of them. Some had whole floors of photocopiers. Then it gradually dawned on clients that it didn’t make sense to keep paying a dollar a page to their lawyers when there were outsourcing providers that charged around seven cents for the same service.

“It took a while but eventually everyone had to give up and outsource all bulk copying,” Bradley says. “The same will happen with low-skill professional services, which are often carried out by non-lawyers anyway.”

However, he adds that to date, professional work has been outsourced as little as possible. This is because work that can be easily outsourced is precisely the work for which firms collect the highest margin when doing it themselves.

“Outsourcing is a direct threat to the big business firm model,” Bradley maintains. “It will happen anyway through competitive pressure, but like most

coming, because the necessary consequence is that the firms will get smaller and have to be structured differently.”

On the other hand, while low level work can be effectively sent almost anywhere, higher level work is much more relationship-sensitive.

“Thinking you can obtain the same result from getting research done overseas is probably a bit naïve,” Bradley says. “The answer will be the same, but that ignores the essence of professional service relationships.”

#### **An accelerating trend**

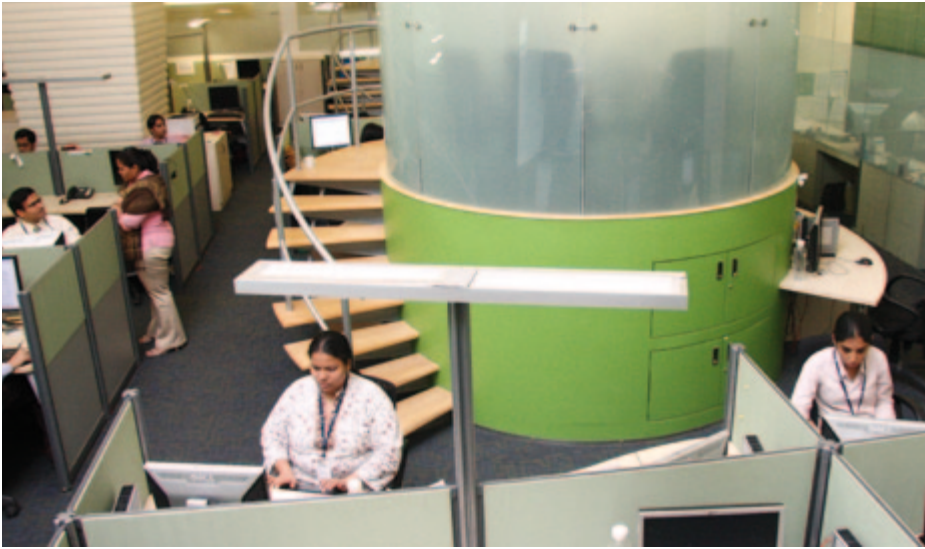
Even so, a recent poll of 200 corporate law departments in the United States found that about half the respondents were considering LPO for legal research. Other work areas under consideration included (in order of likelihood) contract review and drafting, document review and e-discovery, and intellectual property and patents drafting and filing

Indeed, the LPO industry is one of the fastest growing segments of the outsourcing market, thanks to companies aggressively cutting their operating costs, even in areas once considered sacrosanct, such as the legal department. On the supply side, revenue is predicted to hit

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Outsourcing provider Pangea3's facility in Mumbai, India.

US\$4 billion (\$4.57 billion) by 2015, up from just US\$60 million in 2006.

Already LPO providers are offering services at the higher end of the 'judgment chain'. "There is a lot more sophisticated work that can be done offshore and far more cost-effectively," Knox says. "This is proven by the fact that Pangea3 now has 20 per cent of Fortune 500 companies on its books." The provider currently employs around 500 fully qualified lawyers. In four to five years it expects to have close to 4,000. Such growth could concern many professional services firms.

"All indications are that the professional services sector is growing globally, but that growth is going to be picked up by outsourcing providers," Knox says. "I don't see massive downsizing, but I do see companies becoming smarter in how they do things. If you're a General Counsel in a big company, you now have choices. The glory days of the big law firms being able to charge whatever they want for anything are gone. They won't be able to grow at the same rate any more, if at all."

CPA Global's Eve Johnson is in no doubt that the outsourcing market is evolving. "It started out as 'legal process outsourcing', with a lot of volume; process-driven

work that was easily commoditised," she says. "However, we are now being increasingly asked to take on more sophisticated, strategic and highly customised work – hence the change we're seeing in terminology to 'legal services outsourcing'. The 'process' element is still vitally important, but more in the context of how we work rather than what we do. Quite simply, as outsourcers, we're bringing in levels and quality of process management and performance measurement that have been unheard of in the legal industry. It means clients not only know how much they're paying, but exactly what they're paying for and when it will be delivered."

According to Johnson, some law firms have introduced outsourcing as an active way to be seen to be helping clients meet their challenge of controlling legal expenditure, while others use outsourcing providers to make internal savings. The law firms act as project managers and charge for this 'management' time and, of course, for the time spent on the high-end, advisory aspects of the matter.

Where cost savings have been made through outsourcing, Johnson says law firms are generally upfront and transparent about it. At the end of the day, though,

it's in-house counsels who have been the real drivers behind the use of legal services outsourcing. "As the cost-saving eye of company boards turns to their legal departments, in-house attorneys have realised that it's no longer acceptable to pay hundreds of dollars per hour for a junior associate to carry out tasks that provide little clear added value," Johnson says. "This has forced them to look at the value provided by their law firms, and as a result many have turned to outsourcing providers to handle significant elements of their legal work."

This trend has created a new legal model, in which there is a tripartite relationship between the corporate in-house legal team, their external counsel and the legal services outsourcing provider.

"The outsourcing providers can help corporates to clearly define this relationship and map out which work should be undertaken by which party," Johnson says. Notably, CPA Global is working with some firms that believe offering outsourcing to clients will differentiate them in the market, and their business development teams are actively involved in the process.

"With the rapid growth of legal services outsourcing in the US and Europe,

I believe more Australian companies will be looking to outsourcing as a means of controlling legal spend and bringing operational efficiencies, particularly given the increasing focus on regulatory and compliance issues,” Johnson says. “Law firms can either ignore this and leave their clients to look into the benefits on their own, or they can take a proactive approach by talking to their clients about how outsourcing might be used to add value.

“Most corporate clients want their outsourcing firm to work in partnership with them and their law firms. Those that cooperate with their clients’ decision to outsource and help them to structure how legal work is allocated gain greater trust and, with it, more instructions.

“Business development and marketing executives have an influencing and educational role to play within this process. They should be exploring whether outsourcing is something their clients are going to expect and ensuring their firm is ready to have these ‘trusted adviser’ conversations with clients.”

#### **Quality and security**

Inevitably, any such conversations will have to address questions about quality and security, around which there is still some concern.

“The security risks are pretty obvious. There is also substantial reputational and relationship risk,” Bradley says. In Gartner’s recently released report, *10 Leading Locations for Offshore Services in Asia Pacific and Japan for 2010*, Gartner research vice president Jim Longwood noted that “The link between lower risk and higher cost holds true”.

Others express different views. “Feedback we’ve had from clients is that the quality is as good, if not better, in some cases than what they’re getting from junior people in big law firms,” Knox says. “Lack of quality is a myth, and so is document security and storage. You only have to go to the offices of firms like Pangea3 to realise that in terms of security, the major international law firms could actually learn something. There are guards at the door, every room has biometric fingerprint access, there are cameras in the ceiling and all the computers have disk drives disabled. It’s world class and the large law firms are not anywhere near that point.”

Not surprisingly, Johnson agrees. “One of the biggest myths in the legal services outsourcing market is that low cost means low quality and security.

That’s simply not the case. Legal services outsourcing firms such as CPA Global are acutely aware of this concern, and put in place robust quality assurance and security measures. The fact that we have major international companies such as Microsoft and Rio Tinto as our clients speaks for itself.”

As, perhaps, does a comment by a *Law Society Gazette* journalist on the security in CPA Global’s Indian operations, who wrote “it is easy to feel like an extra in a *Mission Impossible* film rather than a tourist in a Delhi outsourcing centre”.

#### **Changing views**

At the end of the day, the trend towards greater outsourcing of professional services seems inexorable.

“There are instances where there is reluctance to move lower-end work to external providers, but such instances are increasingly few and far between,” says Antony Alex, Vice President of Legal Services at Pangea3.

“In fact, our view is that the Australian market is ready to explore alternative methods of delivery of high quality legal services, as well as accounting. It’s true that confidentiality of information and quality are two areas that Australian corporates are concerned about, but when we explain that we are an ISO 270001 certified organisation and that most of our attorneys hold a Six Sigma Certification, the concern falls away.”

Why, then, the reluctance among so many large professional services firms to talk about whether or not they outsource? Is it because they don’t want their clients to know they are outsourcing work offshore, or because they themselves are still making up their mind about it?

“It’s probably a combination of both,” Alex says, “although some of these firms have started to realise that they will be able to deliver far greater value to their clients if they are open to outsourcing. We are starting to see more inquiries from professional services organisations and believe that it is only a matter of time before they start sending a lot more work to organisations such as ours.

“Certainly the delivery of legal services is fast changing – so much so that in the very near future most legal services will be delivered out of India by a company like Pangea3.” ■

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