



Bierce & Kenerson, P.C.

GLOBAL SOURCING PRACTICE GROUP

Introduction to Legal Process Outsourcing

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Infrastructure Services Law

Table of Contents

| | |
|--|----------|
| 1. EXECUTIVE SUMMARY | 3 |
| 2. BEYOND ETHICAL CONSIDERATIONS IN LPO: MANAGEMENT CHALLENGES FOR HIRING LEGAL PROCESS OUTSOURCING SERVICES..... | 4 |
| 2.1 IN-SCOPE LPO SERVICES..... | 4 |
| 2.2 AVOIDING UNAUTHORIZED PRACTICE OF THE LAW..... | 4 |
| 2.3 AVOIDING MALPRACTICE | 5 |
| 2.3.1 <i>Direct Services</i> | 5 |
| 2.3.2 <i>Indirect Services</i> | 5 |
| 2.4 AVOIDING SURPRISES: DUE DILIGENCE..... | 5 |
| 2.5 AVOIDING CULTURAL AND ENVIRONMENTAL GAPS..... | 5 |
| 2.5.1 <i>Individual Lawyers</i> | 5 |
| 2.5.2 <i>Country Risk</i> | 6 |
| 2.6 AVOIDING A SURPRISED CLIENT: THE DUTY OF INFORMED CONSENT..... | 6 |
| 2.7 AVOIDING LEAKS; PROTECTING CONFIDENTIALITY..... | 6 |
| 2.7.1 <i>Avoiding Conflicts</i> | 6 |
| 2.7.2 <i>Avoiding Overcharges and Fee Disputes; Re-working the Law Firm's Fee Agreement</i> | 7 |
| 2.7.3 <i>Avoiding Ineffective Business Practices</i> | 7 |
| 3. BUSINESS MODELS | 7 |
| 3.1 CAPTIVES..... | 7 |
| 3.1.1 <i>Domestic</i> | 7 |
| 3.1.2 <i>Foreign</i> | 8 |
| 3.2 STRAIGHT OUTSOURCING | 8 |
| 3.3 HYBRIDS..... | 8 |
| 4. FURTHER CONTACT | 8 |

1. Executive Summary

In the last fifteen years, the advent of cheap telecommunications, the WTO Uruguay Round of free trade agreements and a landmark American Bar Association ethics opinion on paralegal services has opened new markets. Outsourcing (or “global sourcing”) is a business discipline based on principles of comparative advantage reflected in the “build-vs.-buy-vs.-ally” paradigm in this new global marketplace. By outsourcing, an enterprise hires the services of a specialized service provider, and the provider’s functions integrate into the enterprise’s operations. Like ganglia, this integration creates key interdependencies.

In light of such interdependencies, achieving sustainable legal process outsourcing (“LPO”) requires a new paradigm for corporate legal counsel and law firms. While foreign wage levels might be much lower than domestic “onshore” wage levels, the actual cost savings from outsourcing or offshoring are reduced by the value of ethical risks and the costs of operating a “project management office” (“PMO”) to structure, negotiate and manage the operations. Attrition rates of key employees need to be managed to avoid turnover that could impair business continuity and increase replacement costs. Security, quality metrics, accounting management and audit controls need to be in place. The service provider needs to demonstrate an understanding of the globalizing enterprise’s regulatory environment and strategies for risk management.

LPO requires ongoing hard work and a willingness to take meaningful decisions on such interdependencies and risks. LPO also requires adaptation to change.

Effective LPO requires careful project management. This includes planning and methodologies for management of risks to operations, security, customer relations, legal and regulatory compliance and ultimately brand value. In-house counsel may need assistance from experienced outside counsel to accelerate enjoyment of intended benefits and, more importantly, to provide judgment, strategy and documentation developed through dozens of similar transactions and a focus on this area of legal practice.

Established in 1990, Bierce & Kenerson has been supporting service recipients and some select service providers in their quest for effective business operations using key performance indicators (“KPI”) in contract structuring, pricing and renewal. We offer this “Introduction to Legal Process Outsourcing” to help globalizing corporations and their law firms and sourcing consultants understand issues relating to global sourcing, the role of external legal counsel and considerations in the selection of individual law firms to support global sourcing transactions and operations. We believe that our key differentiators are:

- a holistic perspective based on extensive experience;
- a relatively modest cost structure, reflecting a limited hierarchy of team members and thus a “lean team” and collaboration with foreign law firms that either are the client’s existing firms or experienced sourcing counsel;
- a commercial understanding that allocations of risk need to be achieved when defining the scope of outsourced services, but that overall costs (and thus advantageous pricing) might best be managed by not shifting key risks that can be best managed by a client, who retains ultimate responsibility to their customers, suppliers, partners, regulators and shareholders;
- a focus on mid-market clientele that understands the value of money in legal services; and
- a recognition in the industry as savvy sourcing lawyers regardless of size.¹

¹ This brochure constitutes “ATTORNEY ADVERTISING.” This brochure is not intended to constitute legal advice and cannot be relied on as legal advice. Results described here may differ from your experience. Please consult a lawyer on your particular needs. Bierce & Kenerson, P.C. is a New York law firm.

2. Beyond Ethical Considerations in LPO: Management Challenges for Hiring Legal Process Outsourcing Services.

After several state and city bar associations have blessed offshore paralegal services (“legal process outsourcing”), the American Bar Association issued its Formal Opinion No. 08-451, “Lawyer’s Obligations When Outsourcing Legal and Nonlegal Support Services” on August 5, 2008. The ethics opinions frame the minimum standards for lawyers to avoid losing their licenses. Beyond such ethical and disciplinary considerations, the big question is how to make LPO effective and how the global law firm persuades its global corporate clients to stay in the fold. LPO service providers claim to be able to provide better management, better process, faster delivery, lower cost and more effective allocation of resources. This article analyzes the ethical framework and suggests some business management issues that Bierce & Kenerson, P.C. advises on.

2.1 In-scope LPO Services.

The ABA ethics opinion identifies a full range of in-scope services that lawyers may outsource to other lawyers and to paralegals. The list is framed by its extremes:

- Reproduction of documents.
- Creation and maintenance of a data base for complex litigation.
- Preparing a survey of the law in 50 states on an issue of importance to a client.
- Drafting of patent applications.
- Development of legal strategies for preparation of motion papers in litigation.
- Transcription of dictation tapes.
- Business closings.
- Immigration forms and letters.
- Legal research.
- Drafting of standard forms.

2.2 Avoiding Unauthorized Practice of the Law.

Ethics opinions of bar associations generally hold a lawyer hiring or supervising an LPO provider responsible for facilitation, by action or inaction, of the unauthorized practice of the law. In its Professional Ethics Opinion 07-02 of January 18, 2008, approved internally by its Board of Governors on July 25, 2008, the Florida’s Bar Association attempted to provide some clarity to this concept by suggesting a rights-based analysis whether an activity constitutes the practice of law, citing a 1963 Florida Supreme Court decision:

. . . if the giving of [the] advice and performance of [the] services affect important rights of a person under the law, and if the reasonable protection of the rights and property of those advised and served requires that the persons giving such advice possess legal skill and a knowledge of the law greater than that possessed by the average citizen, then the giving of such advice and the performance of such services by one for another as a course of conduct constitute the practice of law. *Florida Bar v. Sperry*, 140 So. 2d 587, 591 (Fla. 1962), judg. vacated on other grounds, 373 U.S. 379 (1963).

The bar opinions generally refrain from concluding that any particular LPO constitutes “unauthorized practice,” leaving that issue open for the attorney and the courts to decide in each case.

2.3 Avoiding Malpractice

2.3.1 Direct Services.

The ABA ethics opinion confirms what has been well known for decades. “There is nothing unethical about lawyer outsourcing legal and nonlegal services.” But to be legal, the lawyer who outsources any legal or nonlegal function must render legal services to the client with the “legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.” *Id.*, p.2, citing ABA Code of Professional Ethics, Rule 1.1 (basic duties of a lawyer). This is sometimes referred to as the “duty of competency.”

2.3.2 Indirect Services.

A lawyer engaging others to deliver non-legal or legal services must make “reasonable efforts” to ensure that the third-party service provider, if a lawyer, conforms to the Rules of Professional Conduct and, if not a lawyer, delivers the services in a manner that is compatible with the professional obligations of the lawyer.

2.4 Avoiding Surprises: Due Diligence.

The ABA ethics opinion focuses on the challenge of ensuring that the tasks are delegated to competent individuals and adequately and appropriately overseeing the execution of the outsourced project. The due diligence checklist is fairly rudimentary:

- Background checks, including educational qualifications.
- Interviews with the principal lawyers.
- Inquiry into hiring practices, the quality and character of the prospects.
- Security measures for protection of sensitive client data, including physical security of premises, physical, administrative and logical security of the network, and data destruction in refuse and disposal procedures.
- Site visits “in some instances.”

The New York City Bar Association’s Ethics Opinion No. 2006-3 (August 2006) underscores that due diligence continues as an ongoing process of supervision, as a duty to communicate with the non-lawyer to ensure understanding of the assignment and review whether the assignment is being carried out according to the lawyer’s expectations.

2.5 Avoiding Cultural and Environmental Gaps.

The ABA ethics opinion highlighted the risks of hiring foreign lawyers, whose services might not be competent for U.S. legal support due to any one of many cultural and environmental gaps.

2.5.1 Individual Lawyers.

Possible gaps needing assessment include:

- Lack of comparability of legal training to American legal system.
- Lack of cultural inculcation of core American ethical principles.
- Ineffective policing by foreign disciplinary enforcement system.

Where such conditions apply, the American lawyer may still hire the foreign-trained lawyer, but would need to consider the foreign-trained lawyer is just a paralegal for U.S. clients.

2.5.2 Country Risk.

“Country risk” identifies those business and legal risks that arise from the constitutional and geo-political environment where the foreign lawyer (or paralegal) delivers the work. Particular concerns include:

- Susceptibility of confidential documents and records to seizure in judicial or administrative proceedings.
- Susceptibility of client data to “cyber extortion” or inaccessibility if the provider and the attorney have a dispute that local courts cannot promptly resolve (though there may be contractual and technological solutions to this particular risk).

2.6 Avoiding a Surprised Client: The Duty of Informed Consent.

Clients have a reasonable expectation that their attorneys will inform them of “who or what entity is representing them” because LPO involves client confidences that could be put at risk through insufficient supervision or control. In contrast, there is no such supervision and control in “outsourcing,” the ABA concluded. Thus, for the ABA, it “may be” necessary for the lawyer to disclose the outsourcing to the client. Outsourcing and offshoring require “informed consent” when there are risks that a client should be aware of.

Similarly, Florida’s Bar leaves the door open to disclose, or not disclose, a foreign LPO provider’s role, depending on materiality. If a client would think it is material to its decision to entrust the legal services to the law firm, the law firm must disclose the outsourcing.

Informed consent has many threads. Under the Florida Bar ethics opinion 07-02, “The requirement for informed consent from a client should be generally commensurate with the degree of risk involved in the contemplated activity for which such consent is sought.” This means contractual requirements to ensure data destruction, prohibit re-use or sale of client data and contractual gap-filling in case a foreign jurisdiction lacks adequate legal rules on data security, breach notification and identity protection.

In the context of legal services, the level of information necessary for “informed consent” depends on a client’s sophistication. Even sophisticated clients can be expected to demand and receive disclosures of the likely or reasonably possible scenarios of events and the probable impact of each upon the client’s legal rights and remedies.

2.7 Avoiding Leaks; Protecting Confidentiality.

The ABA opinion strongly advises individual confidentiality agreements. The Florida Bar considers that a law firm hiring an LPO provider should limit the overseas provider’s access to only the information necessary to complete the work for the particular client and bar any access to information about other clients. The Association of the Bar of the City of New York (Ethics Opinion 2006-3) recommends “contractual provisions addressing confidentiality and remedies in the event of breach, and periodic reminders regarding confidentiality.”

Confidentiality obligations extend to data collected from opposing parties and third parties, particularly medical and financial records.

2.7.1 Avoiding Conflicts.

Further, the outsourcing service provider should be vetted for possible conflicts of interest in representation of adversaries of the firm’s clients on the same or substantially related matters.

2.7.2 Avoiding Overcharges and Fee Disputes; Re-working the Law Firm's Fee Agreement.

The most controversial element of the ABA opinion lies in its conclusion that the fees charged by a lawyer hiring outsourced LPO services must be reasonable and, if the services are hired by a law firm, the law firm may not mark up the costs of the outsourced service provider if the firm elects to pass along the costs as a disbursement. However, some markup would be allowed for overhead expenses (such as office space, support staff, equipment and supplies) and "a reasonable allocation of the cost of supervising these services if not otherwise" included in the firm's fees. The New York City Bar and Florida Bar generally concur in this approach, which is based on a 1993 ABA Formal Opinion 93-379 on the subject of pass-throughs of expenses for non-legal services.

In contingent-fee cases, outsourcing costs cannot be included as a disbursement if it covers work that is customarily provided by attorneys, according to the Florida Bar opinion.

2.7.3 Avoiding Ineffective Business Practices.

None of the ethics opinions cited asks whether it is unethical for a lawyer to follow the business practices and work flows recommended by the LPO provider. Aside from malpractice worries, this issue is largely an open book.

Adopting effective LPO business practices requires an understanding of project management, competitive bidding procedures in complex services, filling gaps in implicit and explicit assumptions about instructions and cost-benefit analysis.

Further, extensive experience with offshore outsourcing suggests the use of strategic tools for in-house counsel and law firms to deal with the business of non-legal services ancillary to legal services. LPO agreements should adopt key clauses on such topics as:

- Price benchmarking and competitive pricing throughout the term.
- Security, data protection and remediation of suspected identity theft.
- Intellectual property and trade secret rights (not just protecting client data).
- Audit and control issues.
- Relationship governance.
- Termination rights and portability of the operations to insourcing or re-sourcing to a third party provider.

Law firms and corporate counsel may know how to manage paralegals, but legal process outsourcing requires a more holistic approach to client protections. Achieving effective outsourcing may require hiring experienced legal and business consultants to accelerate benefits, reduce risk and provide a clear framework for effective supervision and evolution of the LPO relationship.

3. Business Models

Law firms and corporate legal departments have traditionally adopted a branch model for distributing service providers based on jurisdiction or proximity to lines of business. In LPO models, service delivery is centralized, requiring management tools and procedures for management across time zones.

3.1 Captives

3.1.1 Domestic

A "captive" can consist of a branch or subsidiary where "legal process" services are delivered from a "center of excellence" or other specialized service delivery center.

Domestic captives have been established by a number of law firms seeking local control, proximity and domestic hires. The ethical issues are minimal, but so are the cost savings. Advantages include access to locally admitted attorneys, local cultural compatibility, visibility, relatively easy management and proximity. A domestic captive may also extend a law firm's reach and be particularly effective where the firm has already developed a multi-disciplinary practice.

3.1.2 Foreign

Foreign captives represent an attempt to extend the enterprise or the law firm as an integrated global enterprise. A foreign captive requires a global-services approach to standardization and service automation. As in any global services model, a foreign captive requires distribution of service providers, a global leader and liaisons. Ethical risks are increased because foreign-trained personnel might not have the same culture of confidentiality and concerns about "the appearance of an impropriety" as American or British lawyers. Such concerns can be overcome through a robust program of training, supervision and audit.

3.2 Straight Outsourcing

Straight outsourcing involves assigning responsibility to an external service provider for performing a defined scope of responsibilities. Sometimes scope can be vague, so the supervision needs to be effective, persistent and visible. Further straight outsourcing needs to deal with issues of process efficiency, transparency and ongoing management rights and opportunities to change directions as needed.

3.3 Hybrids

Hybrids offer an opportunity for cost savings while relying to some degree on the management services of a third party, though such reliance cannot ethically displace the attorney's duty of direct supervision. Hybrid models involve a combination of captive model with an outsourcing model. Under a hybrid, for example, the captive can be established, owned and legally governed by the law firm or the corporation law department, but a service provider could provide management services to achieve quality targets ("service levels"). Under a second hybrid model, the captive can serve as procurement department for legal services.

Hybrid models involve some added complexity involving laws and procedures relating to taxes, transfer pricing, governance, intellectual property, process control, licensure and employment. In a forward-looking strategy, the models can shift from one to another over time.

4. Further Contact

Bierce & Kenerson, P.C. has extensive experience in structuring, negotiating and implementing business relationships involving outsourcing, global services and shared services. For further information, please contact:

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For Further Reading, see:

- www.outsourcing-law.com
- www.biercenerson.com/portals
- Introduction to Outsourcing and Offshoring, White Paper (available on request)