

## Project: *Corporate Counsel – Legal Service Providers*

# eLawForum: Aggregating Demand For Fixed Fees In A Competitive-Source Business Model

The Editor interviews **John B. Henry II**, founder and CEO of eLawForum.

**Editor: What has happened since we last talked?**

**Henry:** We have conducted 50 more competitive-sourcing assignments for Fortune 500 corporations. So we have learned a lot more about how to make a market in high-end corporate legal services.

**Editor: What have you learned?**

**Henry:** Our role as a market-maker has gone through 3 stages.

In Stage I, we took the things that law departments do in a sole-source business model and moved them over to a competitive-source business model. We ran competitions for single matters and hourly rates.

In Stage II, we stopped running competitions for hourly rates.

**Editor: What was the reaction to your decision to stop doing hourly rate competitions?**

**Henry:** Our clients agreed that they couldn't be sure they were saving money unless law firms worked for fixed fees. Hourly discounts don't protect you against being billed more hours. The top law firms make 40% margins and give 20% discounts. A 20% discount in hourly rates does not mean a 20% reduction in costs. A competitive-source business model doesn't change this reality.

Fixed fees don't affect the way we conduct quality competitions. The best specialists in the relevant practice area will compete on a fixed-fee basis. They know the risks better than anyone.

**Editor: The ABA recently completed a year-long study of the billable hour, which included a nice description of eLawForum's competitive-sourcing service and a very positive interview with one of your clients.**

**Henry:** The ABA study is an important step forward. There are many lawyers who believe the billable hour threatens the profession. There are many kinds of alternative billing arrangements, but the key factor is who bears the risk of the cost of the service. Fixed fees ensure real savings. Hourly billings don't. Fixed fees allow you to measure savings and put accountability where it belongs.

**Editor: Are there any changes in the way eLawForum runs competitions with the move to fixed fees?**

**Henry:** Our website gets a lot more use. When you shift the risk of the cost of the legal service to the law firm, the corporation must provide more information. This requires more work, but, if you think about it, there is no alternative. The incumbent law firm has what securities law calls "inside information". You can't ask law firms to assume responsibility for the cost of their service if you don't give them the information they need to make an intelligent business decision.

**Editor: What is Stage III?**



**John B. Henry II**

**Henry:** Stage III grew out of our Stage II experience — corporations get the greatest savings when they offer law firms more business. We focus now on deals where we bundle \$10 million, \$20 million or \$30 million of business.

**Editor: So eLawForum is now a deal-maker as well as a market-maker?**

**Henry:** Exactly. We add more value. Stage I taught us how to run first-rate quality competitions. Stage II taught us how to do fixed-fee competitions. In Stage III, we offer law firms more attractive deals.

**Editor: How large can the savings be?**

**Henry:** We focus on deals that can save 50%. We recently saved a client \$16 million in a single competition.

**Editor: It sounds like eLawForum has made a lot of progress.**

**Henry:** It hasn't been easy. We have a lot of scar tissue. We have been patient. We have learned what works and what doesn't work. We are very good at what we do.

eLawForum aggregates demand for fixed fees in a competitive source. That's where you get the power of the marketplace.

**Editor: How long do you think it will take eLawForum to convert the market?**

**Henry:** There is a tipping point, but I don't know where it is.

**Editor: What is the basis for your confidence in a tipping point?**

**Henry:** At some point, the fiduciary argument cannot be avoided.

**Editor: What is the fiduciary argument?**

**Henry:** You can't waste corporate assets.

**Editor: But isn't the result almost always a bigger number than the cost?**

**Henry:** Absolutely. That's why it will take time. Every competition gets us closer. We are patient.

**Editor: What is the argument against the competitive-source business model?**

**Henry:** It is similar to the argument made against fixed fees — that you put the result at risk. We prove this isn't true each time we do a competition. We see a correlation between quality and price — the higher the quality, the lower the price — just the opposite of a sole-source business model where the same firms charge the most. In fact, you are more likely to get a good result if you go through a rigorous quality competition in which the best specialists compete and the winner is on the hook for the cost of its work and can hedge this risk against a large book of business.

**Editor: Let me repeat what you said to make sure I understand it: In a sole-source business model, high quality and high prices go together because the seller sets the price. Put the same firms in a competitive source for a large block of work for a fixed fee and the best firms have the lowest prices.**

**Henry:** Exactly. As long as corporations buy outside legal services matter by matter on a hourly basis in a sole-source business model, there is no accountability for costs, only results.

**Editor: But what keeps law firms from cutting corners?**

**Henry:** The best specialists can handicap the assignment better. Their income and reputation are on the line. The interests of the corporation and the law firm are properly aligned. The incentive to boil-the-ocean is gone.

**Editor: What is different about the eLawForum experience from corporations who have gone through convergence on their own?**

**Henry:** We didn't invent demand aggregation any more than we invented the Internet, fixed fees or competition. What we have done is put them all together in a unique combination.

DuPont went from 300 to 30 law firms. Fred Bartlit left Kirkland & Ellis to offer fixed fees. These innovations, however, were still within the context of a sole-source business model. You don't get the full power of the marketplace until you aggregate demand for fixed fees in a competitive-source business model.

**Editor: Does the buyer always select the lowest bidder?**

**Henry:** No. The highest quality firms are best able to handicap the assignment. In one competition, we saw a \$40 million spread — the highest bid was \$56 million and the lowest \$16 million. Price was only one of twelve categories the firms were graded on.

**Editor: It makes sense that law firms are more attracted to large deals than small ones.**

**Henry:** eLawForum alleviates one of the biggest problems law firms face in a sole-source business model. Nobody knows for sure how much spare capacity there is. Keeping everyone busy all the time is not a small challenge. The economy is always changing. So are practice areas. Selling hours matter by matter is an uncertain way of doing business. It's very hard to plan.

eLawForum's deals give law firms a steady source of income for five years. They know how much money they are going to get for the next 20 quarters.

**Editor: eLawForum is giving the corporation the same certainty.**

**Henry:** Exactly. The law department can plan better too. It has a much better idea of what its budget is going to be.

**Editor: Is there any relief for the firm if a particular case turns out to be a problem?**

**Henry:** That's the beauty of the way eLawForum does business. There are many hedges. Only the most qualified law firms win. They know the risks better than the corporations. They get a lot of work over a long period of time so the risk of any one case is less and is built into their fixed fee. They are not being asked to take the risk that there will be more cases. If something highly unusual happens, the corporation can always change the deal.

**Editor: Are the incentives different?**

**Henry:** It is well known that about 95% of all litigation gets settled. Incentives talk to when settlement occurs. In the sole-source business model, where corporations assign cases one at a time and law firms bill by the hour, the law firm doesn't have the same incentive to settle as a corporation does. Their incentive is to boil-the-ocean. When you shift the risk with fixed fees, the law firm has an economic incentive to resolve the matter earlier. So fixed fees not only move the cost upfront, they also move the result up in time.

**Editor: So aggregating demand for fixed fees in a competitive-source business model has real implications for ADR.**

**Henry:** I have learned a lot working with Jim Henry, Howard Aibel and George Frazza on our advisory board. Each competition shows us more clearly that changing the rules of compensation changes the rules of the game. eLawForum makes mediation and arbitration skills more valuable. The optimal world for ADR is aggregating demand with a flat rate in a competitive-source business model. Law firms have a greater incentive to practice those skills.

**Editor: Are fixed fees adjusted for success or failure?**

**Henry:** I believe the market is going to go that way — reward for the best results, less compensation for poor results.

**Editor: I think I now understand why law firms are reacting as positively to eLawForum as corporations.**

**Henry:** We finally figured out how to solve their problem. We're giving law firms a better deal than the sole-source business model can give them. Long-term contracts are more certain than matter-by-matter relationships. Inside information formerly only known to an incumbent firm is being shared with the best specialists. Our competitions are fair and offer law firms something they can't get anywhere else.