



2020

State of the Legal Market in Canada: Combining Effectiveness & Efficiency



Executive Summary

As we were entering 2020, Canada looked like a growth market for the legal profession, with the largest corporate clients saying they expect to increase their spend in 2020. The strategic priorities these departments were describing revolved around two core areas as spend was growing: being more effective and efficient. It would be easy to assume that the strategic priorities of 2019 are no longer relevant amid the COVID-19 outbreak and the fallout the pandemic has had on the global economy.

However, as we have been speaking to General Counsel throughout the crisis, this is not necessarily the case. Slowly, we are seeing the industry shift from immediate crisis management to short-term planning – some corporates even have their gaze cast further to the horizon and are starting to investigate the opportunities that COVID-19 may bring in terms of both operational growth and resilience.

Currently, it is true, that implementation of some international projects and external transactions have been put on hold, and corporate law departments are

prioritizing their most pressing issues. Nevertheless, for many departments the core strategic priorities remain as they described them, just with differing levels of emphasis. What has not changed, however, is the expectation corporate departments are putting on their outside law firms to support them. Effectiveness is about being fully aligned to the corporate strategy, getting the balance right between minimizing risk and enabling growth while delivering practical, pragmatic support to their internal clients. Efficiency includes speed and accuracy – and not just in terms of cost control, important though that is for many Canadian clients. Again, external legal advisors must match these priorities if they hope to win favour in this evolving landscape.

As well as the traditional pressures, legal teams must accommodate the changes in legal technology and process innovation. Some of these alternative solutions may well become more attractive options as we see clients' appetites for experimenting with new delivery methods grow – a core trend of the last recession.



This in turn will provide more competition for established law firms. Indeed, they will need to pay more attention to their levels of client service and deliver what really matters to their clients.

And to get to what matters, law firms would be wise to focus on the same kind of drive for effectiveness and efficiency that in-house legal teams are pursuing, including these crucial first steps:

- Fostering greater collaboration;
- Applying metrics to daily activities to measure both effectiveness and efficiency;
- Investing in technology; and

- Understanding that clients want legal providers that are ready to innovate, whether that be on processes, technology, or fee structures.

For law firms, the key message from our research is simple: Focus on service. More than anywhere else in the world, Canadian companies prioritize client service over other factors, and the law firms that really understand, respond to, and support their clients' particular needs, will benefit most from this growing market. As COVID-19 brings with it a time of constant change and uncertainty, service becomes even more mission critical for firms to get right.

Background to the Research

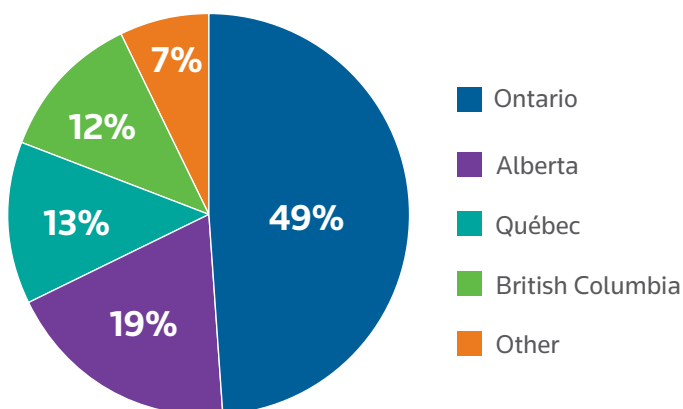
Acritas conducts telephone interviews with more than 2,000 senior legal decision-makers across the globe as part of its annual Sharplegal survey, which contains 50-plus questions about law firm brand, usage, market trends, and more.

This report draws on **251 interviews** conducted between November 2018 and October 2019 within Canada as part of the wider Sharplegal study. This research period took place before the start of the COVID-19 pandemic. However, interviews have continued throughout 2020

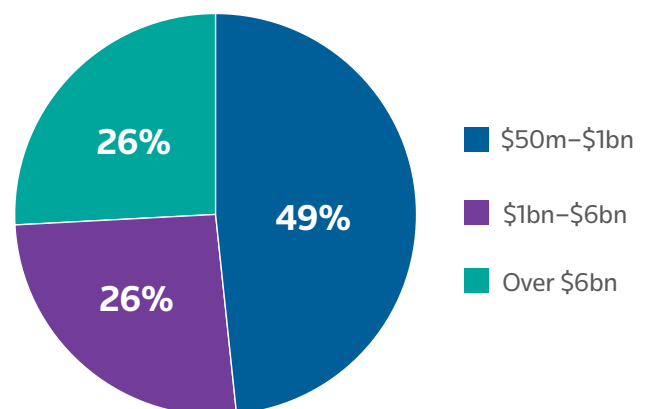
and a review of the latest intelligence from corporate legal departments has been undertaken to ensure the insights shared within this report are still reflective of current market conditions. All organizations interviewed have an annual revenue of more than \$50 million (USD) and the **251** contributors to this report have an estimated combined legal spend of **\$2.1 billion (Can.)**.

Nearly two-thirds of survey respondents were Chief Legal Officers, and a further 30% were in other senior roles.

Province



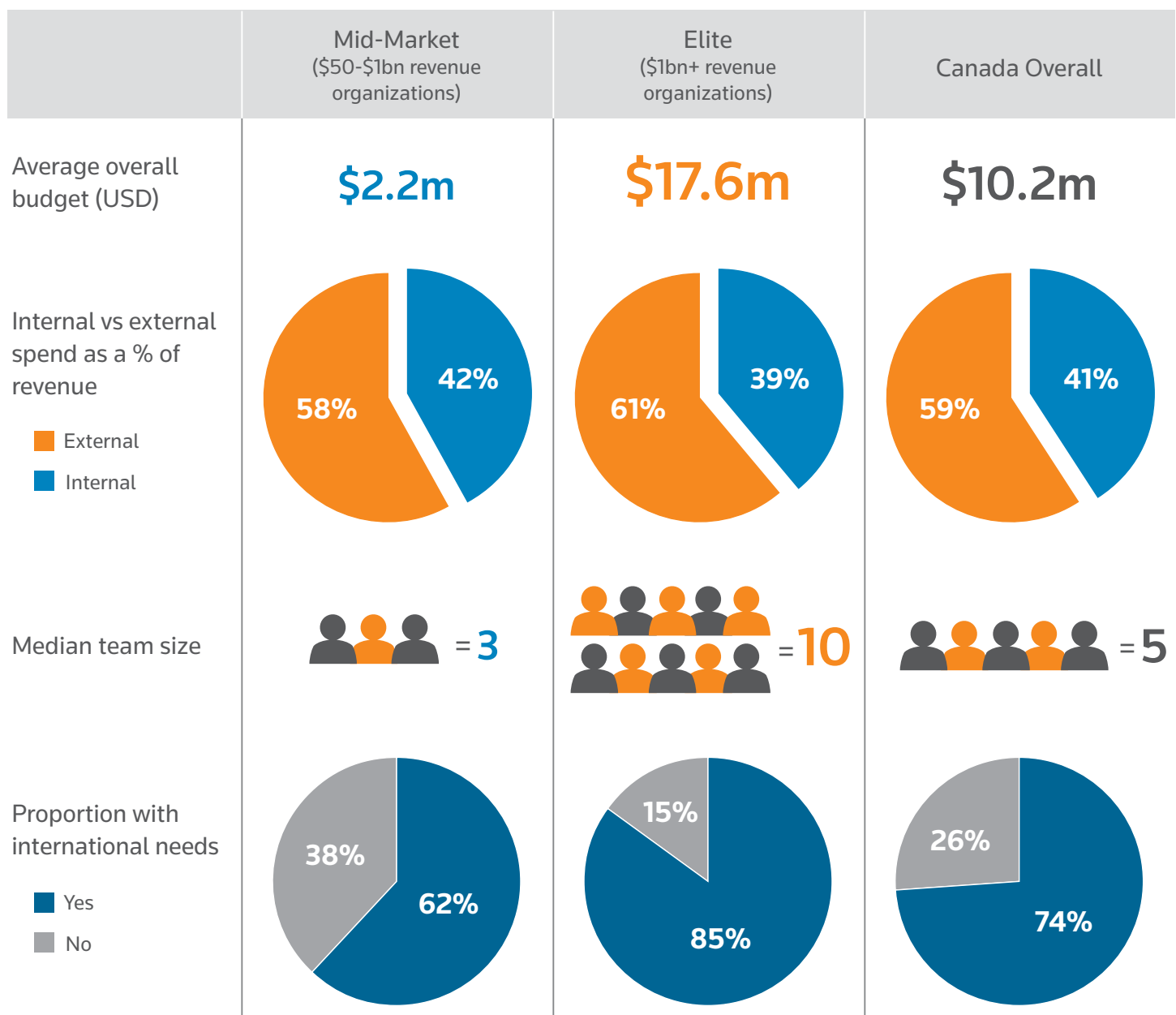
Revenue



State of the Market: The Typical Canadian Buyer of Legal Services

At the end of 2019, in-house teams in Canada were allocating a high proportion of their budgets to in-house resources — and for larger companies, the proportion is higher still. Mainland Europe is the only region which allocates more of their budget internally, on average.

“In-house teams in Canada allocate a high proportion of their budgets to in-house resources...”



Source: Acritas Sharplegal

FINDING THE BALANCE BETWEEN OUT- AND IN-SOURCING OF LEGAL WORK

The larger Canadian clients in our survey — those with revenues over \$1 billion USD — spend more internally than their counterparts elsewhere in the world. Unsurprisingly, those in the mid-market have smaller teams on average than the largest Canadian corporations, but they allocate a similar proportion of their budget toward outside counsel. Though the dollar value of mid-market spend is lower, this dynamic offers an opportunity for law firms and their corporate clients to collaborate to better identify areas where work can be consolidated more effectively across one provider. In this way, law firms can help the in-house legal departments on their drive for efficiency as the law firms develop into a trusted advisor.

The median size of the legal teams within the largest organizations are in line with the global average, but it's worth noting that the “mean” team size has decreased compared with SharpLegal 2018. This could be an indicator that we are about to enter a period of outsourcing for the legal departments for these largest organizations too. Again, there will need to be more conversations around where organizations anticipate their

“This could be an indicator that we are about to enter a period of outsourcing for the legal departments for these largest organizations too.”

legal needs over the next 12 months and how law firms can support those goals, to ensure that the outsourcing does not result in massive overspend for clients.

These proactive conversations — whether instigated by the firm or by the corporate client — should focus on how large organizations and their legal teams can partner with their law firms to create mutually beneficial relationships.



THE INTERNATIONAL OPPORTUNITY

Late-2019, much of the expected growth in the Canadian market is likely to come from international businesses where we see a predicted increase in spend in 16% of cases, on balance. Canadian buyers with international needs spend on average 38% of their external budgets on international advice and support — for those in the largest organizations this increases to 43%. By nature of having operations in many jurisdictions, international businesses will be hard-pressed to compete with the ever changing COVID-19 regulations. The focus of their spending will potentially shift from growth to their more urgent priorities around labour & employment and supply chain management.

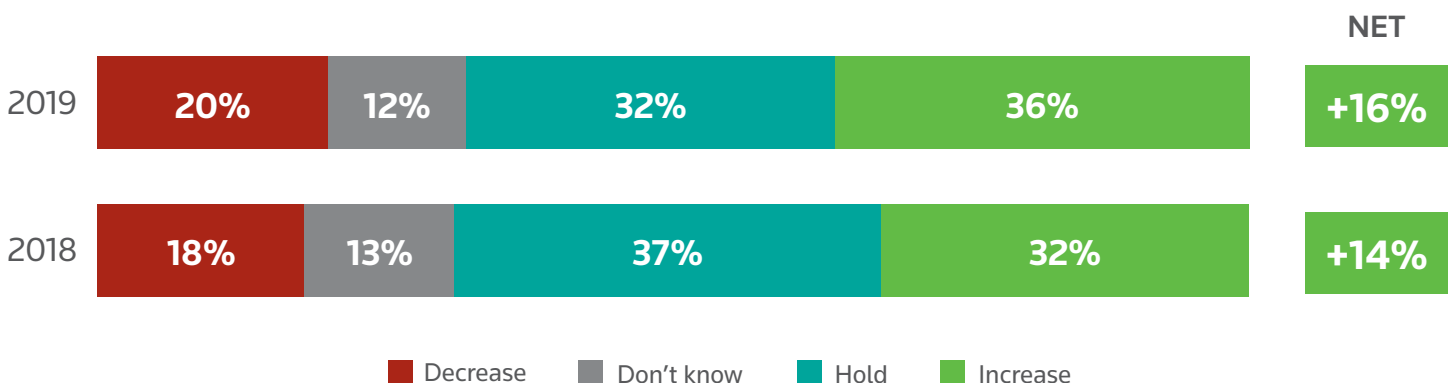
The majority of Canadian respondents to the Sharplegal survey have international needs, although this has slipped slightly from 78% to 74% over the last year, and some are planning to boost their internal capabilities within the various markets in which they operate.

The list of legal markets into which Canadian companies are looking at has changed slightly. The U.S. legal market — predictably — tops the list, followed by the U.K. and China. But Australia and France, ranked 4th & 5th in 2018, slipped to 7th and 9th in our most recent survey, while Germany and Mexico have increased in importance.

“Continue to develop a strong list of experienced service providers, so that every jurisdiction where we’re doing business, we can immediately access high-quality legal advice.”

“For us, it’s really trying to reorganize our function to better serve the geographies in which we work. So, we’re putting internal legal resources in regions of the world where historically we’ve been either absent from an internal perspective, or underrepresented.”

International spending trends

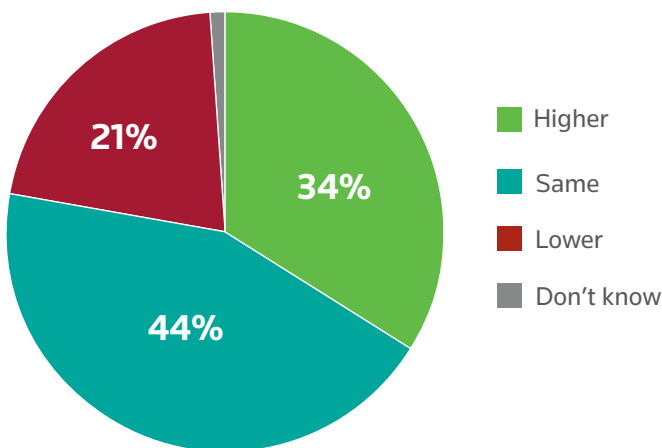


Source: Acritas Sharplegal

THERE'S OPPORTUNITY GOING INTO CANADA, TOO

Sharplegal, as a global study, is also able to identify demand for legal services in Canada from other countries. Thus, we see that 54% of multi-national organizations surveyed by Sharplegal across the globe need legal advice and support in Canada — up from 50% in 2018. And, by the end of 2019, a little more than one third of these organizations expected to increase their spend in Canada over the coming year. As a result of the current pandemic, we may see a shift in what matters this spend is allocated to in the immediate term.

Expected change in spend over the next 12 months into Canada



Source: Acritas Sharplegal

With a presence in multiple jurisdictions, experience of cross-border transactions, and expertise in local markets, large global law firms ought to have a competitive advantage when it comes to this international business. However, particularly as we focus on the U.S.-Canada border, the current preferred choice is to use strong firms *within* that jurisdiction — rather than firms that can practice local law in both.

“...law firms must pay close attention to the strategic priorities of their clients while maintaining strong levels of client service.”

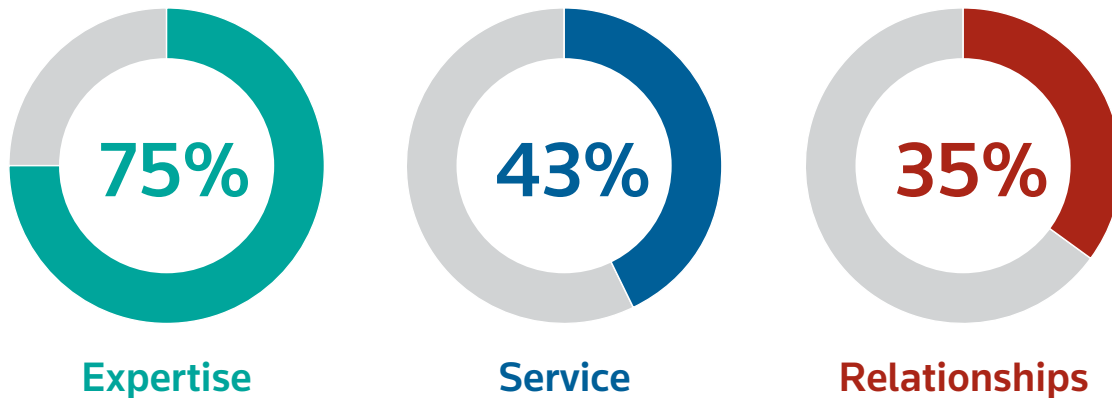
The War on Talent

Private practice lawyers are recognizing this client preference as well. Since Acritas started tracking stand-out lawyers in 2015, we have seen **61** of them change firms. The majority of these **(79%)** moved to a Canadian firm, while just **5** chose to join an international firm within Canada.

Firms that continue to have proactive conversations with clients and develop their international capabilities — even when there is no workflow — will be top-of-mind when advice is required. However, to really benefit from this growth, law firms must pay close attention to the strategic priorities of their clients while maintaining strong levels of client service. Clients in turn must be pushing their law firms to have these conversations outside of the legal work in order to better develop the relationship.

The Client Experience – Service Matters

Top three drivers of law firm favourability in the Canadian market:



Source: Acritas Sharplegal

While expertise is always a strong driver, to really benefit, law firms must convert awareness into favourability paying close attention to providing high-quality client service. This is what sets Canada apart from other markets and should be a law firm's number one priority — and clients should be demanding high levels of service as a minimum standard. In many ways this focus on service reflects the drive for greater effectiveness — in-house teams look to their outside legal advisors to help them add value, and this means going beyond the narrow confines of legal technicalities (where expertise is taken as a given) to a broader level of support that reflects a deeper understanding of the business and the internal pressures the client and its legal team is under.

When asked to more deeply define the service they desire, clients cited speed:

"The turnaround is quick, acknowledgement of when I have an issue [or] when I send my request."

"...paying close attention to providing high-quality client service. This is what sets Canada apart from other markets and should be a law firm's number one priority..."

But just as important, they cited an ability to deliver practical advice that matched the business problem:

"It helps me decide what to do, isn't caveated to the point that it is meaningless. They are also happy to give me advice that I want."

This question of pragmatic advice comes up repeatedly around the world, and in 10 years of studying the legal market, our research has identified the top two skills gaps in external legal counsel as pragmatism and an understanding of their clients' business.

And when it comes to identifying what makes an advisor stand out from the crowd, Canadian clients again focus on the service element — with such factors as practical advice, responsiveness, commerciality, and knowledge of the business all scoring more than the global average. Again, these factors all reflect the client's priorities to be more effective (practical and commercial, really understanding the business) and efficient (responsive).

“...when it comes to identifying what makes an advisor stand out from the crowd...such factors as practical advice, responsiveness, commerciality, and knowledge of the business all scoring more than the global average.”

Many of our survey respondents were very positive about the law firms with which they deal, but as one legal department head explained, there's no room for complacency:

“I think it's how we better use law firms. How they provide more value to us, how we can rein in legal fees and not sponsor lawyer's lifestyles. Manage increases to something that is more in line with inflation and not the crazy amounts that we get requests for every year. That's a big challenge, law firm economics that don't make sense for big institutions like us; [and] big law firms take big institutions like us with a lot of legal spend for granted. There will be a shift to more efficient law firms if they continue to increase fees the way they've been doing. It's bound to happen. There are people that are using technology and passing on those savings instead of increasing their profits per partner and that's what we're interested in and we're exploring. That should be a warning to all of them if you speak to them.”

STRATEGIC PRIORITIES: BE EFFECTIVE, BE EFFICIENT

In common with the focus of the world's legal departments at the end of 2019, Canadian in-house teams were focusing their efforts on two primary goals:

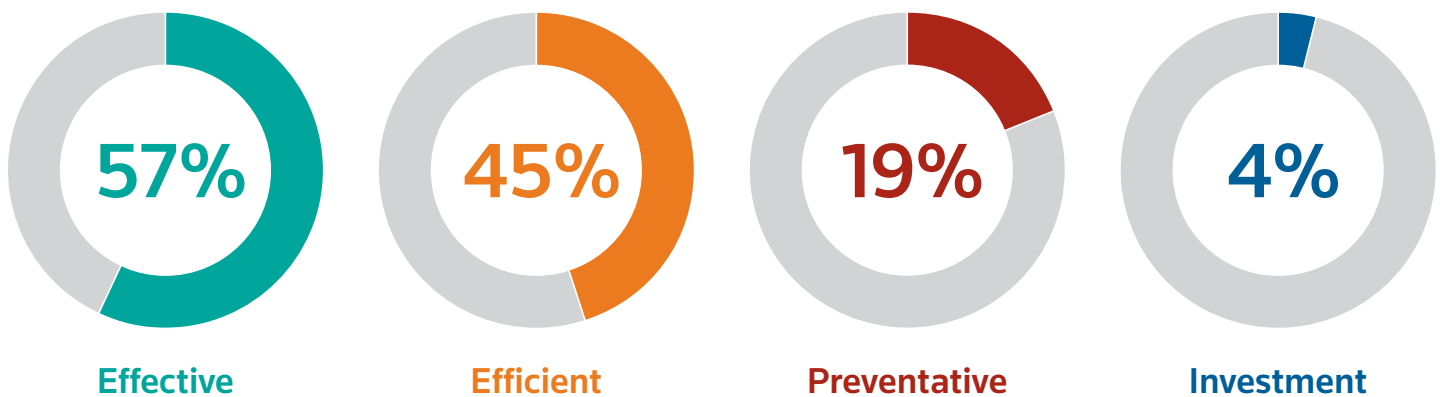
- i) delivering a more effective service to their internal clients; and
- ii) doing so while operating more efficiently.

It would be easy to assume that the strategic priorities of 2019 are no longer relevant amid the COVID-19 outbreak and the fallout the pandemic has had on the global economy. However, as we have been speaking to General Counsel throughout the crisis, this is not necessarily the case. Rather, the focus is shifting as each

priority becomes even more important, in particular the need to return to the *raison d'être* of the legal department – manage and mitigate risks which occur as a direct results of the pandemic.

"We're trying to improve our financial reporting, we are seeking efficiencies in how we deliver our services, we are seeking efficiencies in outside counsel spend."

Legal departments strategic priorities



Source: Acritas Sharplegal

Looking into these goals in more details, cost-control was already the most-mentioned priority before the novel coronavirus truly started to take a grip on the world. But this was still only mentioned by one-quarter of survey respondents, and it was closely matched by other priorities. There is a difference between cost control and cost reduction, of course, and we look at some of the ways in which Canadian corporations might invest more efficiently below.

Even without the context of a pandemic, it is perhaps surprising to see a department's Preventative role being ranked third — after all, most in-house teams would say their *primary responsibility* to the company is to ensure they are compliant with laws and regulations and are protecting the company from regulatory and other risks. But this is a *given* — it's the team's *raison d'être* and underpins everything they do.

For legal departments, the strategic focus this year is on delivering greater value by being more effective and more efficient *even while* they protect the company.

“Help the business to meet goals, protect the organization, mitigate risk to the extent appropriate, and keep cost down.”

“There is a difference between cost control and cost reduction.”

Law firms and their clients can work together to make sure they are collectively and proactively building a mutually beneficial relationship. Proactive conversations should focus on:

- Conducting a portfolio analysis and risk assessment to help prioritize matters and spend; and discuss bulk work for volume discounts and fixed fees.
- Providing tools, checklists, and training to help in-house departments run more effectively and efficiently.
- Offering and requesting secondments for your most strategically important relationships.



Effectiveness

WHAT CONSTITUTES AN EFFECTIVE CORPORATE LAW DEPARTMENT TODAY?

Corporate law departments are being asked to go beyond their traditional focus on compliance and legal advice on straightforward business matters as company boards begin calling for much closer alignment to corporate strategic goals, particularly as companies and industries go through significant changes. This has led in-house legal teams to re-define their own goals.

“The strategic orientation of the organization is a big one I spend a lot of time on myself.”

“Well, job number one is to help the business execute on the overall strategic plan and add value on the way through.”

To support the business properly, corporate law departments need to improve their functional effectiveness in a way that provides value to the company and allows the law department to demonstrate that value. Day-to-day advice, on a par with cost as a priority, must be practical and pragmatic — and so too must be the advice delivered by external law firms.

“Understanding the business and managing changes in the business and the industry.”

“...company boards begin calling for much closer alignment to corporate strategic goals...”

“The main priority is adjusting to the new competitive landscape in which the company will now be focusing. We have had a corporate reorganization, we have abandoned some work packages and some types of work, which were not profitable, so I think that the lawyers need to adjust to the organization’s new strategic plan.”

Yet, for many corporate law departments, effectiveness can be an ideal that is under continuous assault by the daily rigours of legal work in a corporate setting. Many of our survey respondents told us that the day-to-day pressures meant they had to be reactive, even though they recognize they need to take a more proactive approach if they are to serve their internal clients better.

“We would like to become more proactive in assisting our internal clients, as opposed to reactive.”

Keeping up with external regulatory change is one challenge; and for respondents in fast-growing companies, this challenge is compounded by rapid internal change that necessitates the team expanding areas of legal expertise to match the expanding areas of business activity. M&A activity in particular brings out two issues: the transactional workload; and also, subsequently, the management challenge of amalgamating teams.

“Balancing aggressive growth with legal requirements — and M&A is our main focus so that will always be a priority.”

“Right now, we are being amalgamated, so it’s to successfully amalgamate our different organizations.”

For corporate law departments, this is an ever-present reminder of the importance of looking beyond the current workload toward what additional transactions will need to subsequently take place. For outside law firms, it presents the opportunity to proactively highlight the other areas a client should be concerned about and position the firm as the support that clients will need. Given the ever-changing risk landscape of the world around us, these issues will require greater collaboration with other functions within the company as corporations take a multidisciplinary approach internally to professional services.

“It is useful in some situations to have that combination of legal services together with accounting services; in particular we use them for immigration-related issues and expatriate assignments.”

How can corporate law departments improve effectiveness?

- Improve collaboration
- Invest in technology
- Define key performance indicators (KPIs) to measure and demonstrate value
- Seek out providers who are ready to innovate, whether that be on processes, technology, or fee structures

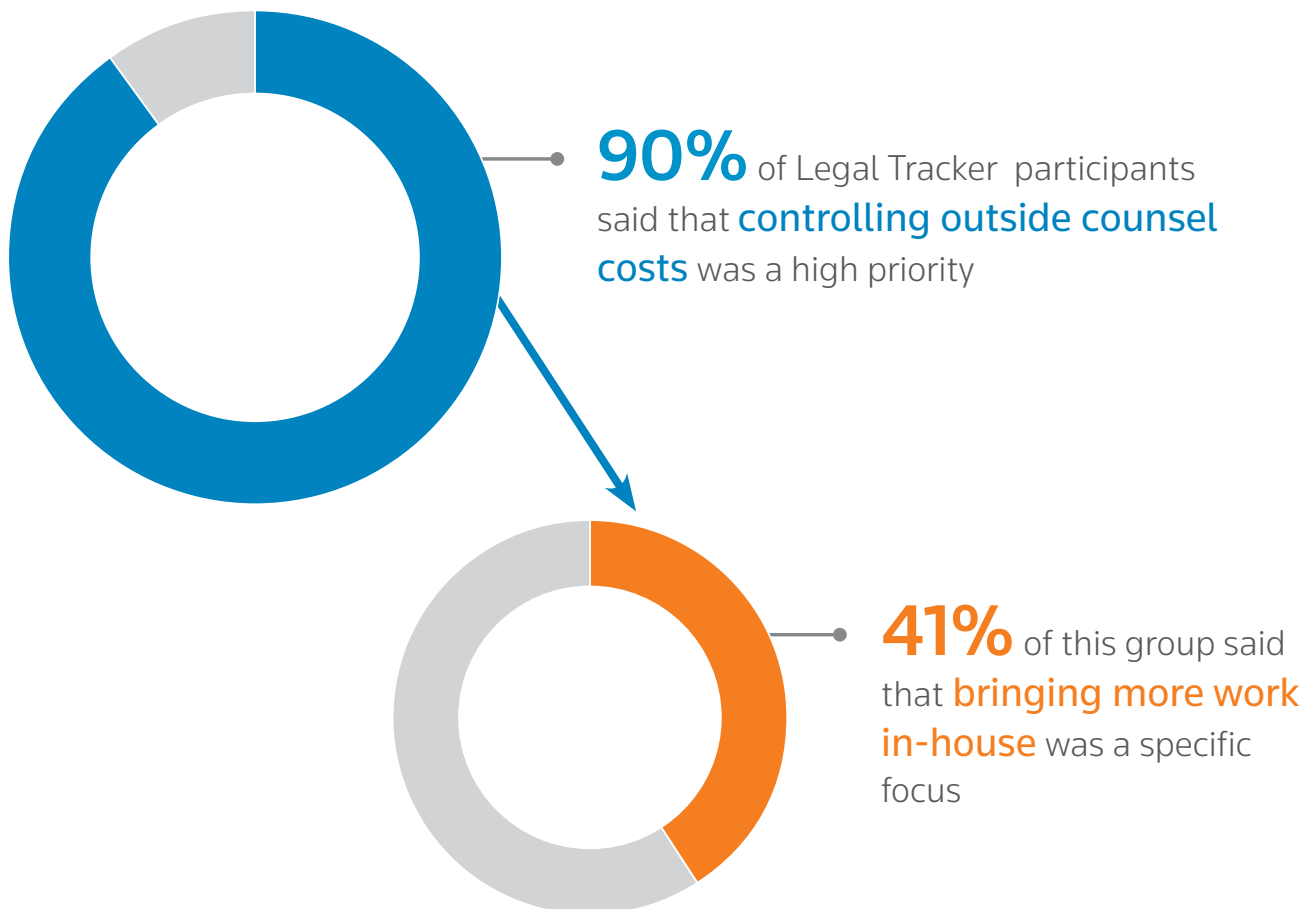
Efficiency

HOW ARE CORPORATE LAW DEPARTMENTS DRIVING EFFICIENCY?

If effectiveness is about what in-house lawyers do, efficiency is about how they do it.

For many, particularly those with smaller legal teams that rely more heavily on outside counsel, a key goal is to reduce external legal spend. This is a consistent story in Canada, around the world, and in the neighbouring U.S. market. Indeed, 90% of Thomson Reuters Legal Tracker participants said that controlling outside counsel costs was a high priority, and 41% of this group said that bringing more work in-house was a specific focus.

"I would think that we are trying to be more mindful of cost and maybe looking at more innovative ways to deliver and work with our external counsel."



Source: Thomson Reuters 2019 Legal Tracker™ LDO Index

CONTROLLING COSTS: LESSONS FROM THE U.S.

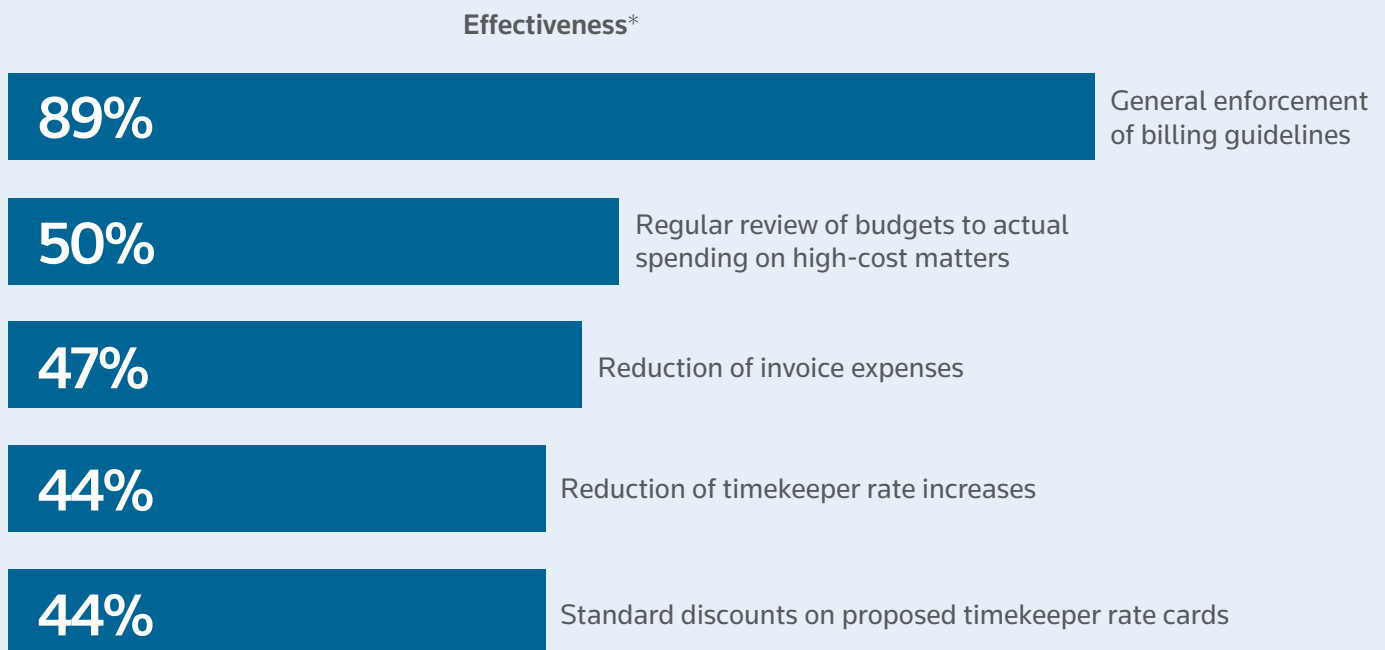
Controlling cost is an issue for legal teams all over the world, and our research shows that, unfortunately for many corporate law departments, they have limited ability to reduce external counsel spend further than they already have. Indeed, some survey respondents suggested the cutbacks their departments have experienced were not sustainable as the business continues to grow. The most they can aim for at this time, is perhaps to keep strict control at current levels.

Given the increasing demands on these law departments for greater effectiveness, more collaboration, and further expansion of the legal role into other areas of the business, the

leaders of corporate law departments face a big challenge. U.S.-based research from the Thomson Reuters Legal Tracker LDO Index shows how law departments there are tackling this problem.

The single most effective cost control measure, according to Legal Tracker participants, is general enforcement of billing guidelines which can result in the reduction of invoice fees and expenses. Clear, consistently enforced billing guidelines compel external legal advisors and suppliers to submit fewer non-compliant expenses. This also enables law departments to more proactively manage unanticipated or escalating costs and simplify the invoice process, further improving efficiency.

Top 5 cost control methods



*% identifying each as an effective measure

Source: Thomson Reuters 2019 Legal Tracker™ LDO Index

Enforcing Billing Guidelines

Law firm data from Thomson Reuters Peer Monitor™ indicates that the collected rate realization by firm — as measured against worked (or agreed upon) rates fell steadily between 2007 and 2010, from around 94% to just 89%, as corporate law departments began to implement stricter billing guideline enforcement. This figure has, however, remained stable at around 89% since 2013.

It appears that, despite almost universal agreement on the impact of billing guideline enforcement on cost control, law departments can no longer make substantial efficiency gains through this method. The practice remains crucial, however, to ensure that costs do not escalate, but it does not offer the chance to significantly reduce external expenditure further.

Reviewing Cost-Effectiveness of Suppliers

In addition to swapping out expensive law firms for their lower-cost peers, corporate law departments are increasingly turning to ALSPs (or new law companies) that often can offer cheaper and more technology-enabled services for certain legal matters, often at a fixed price. But increasingly, law firms themselves are innovating their offerings to take advantage of new types of flexible resources, low-cost centers, and technology enhancements, to better provide these services to clients themselves with more price certainty.

Corporate law departments should have discussions with their incumbent law firms to see what their outside firms can offer by way of new innovative processes or practices. And if law department leaders don't find what they're looking for, it may be time for them to cast the net wider and see what else is out there.

“Corporate law departments should have discussions with their incumbent law firms to see what their outside firms can offer by way of new innovative processes or practices.”



METRICS: WHERE EFFECTIVENESS MEETS EFFICIENCY

A number of survey respondents talked about reorganizing their law departments and their processes, and as part of this, introducing metrics to track performance. For example, some departments are surveying their internal business partners on the quality of the work provided or are tracking their turnaround times on contracts. This effectiveness push also brings with it the challenge of speed — speed of distilling data and information and then offering concise business-ready advice.

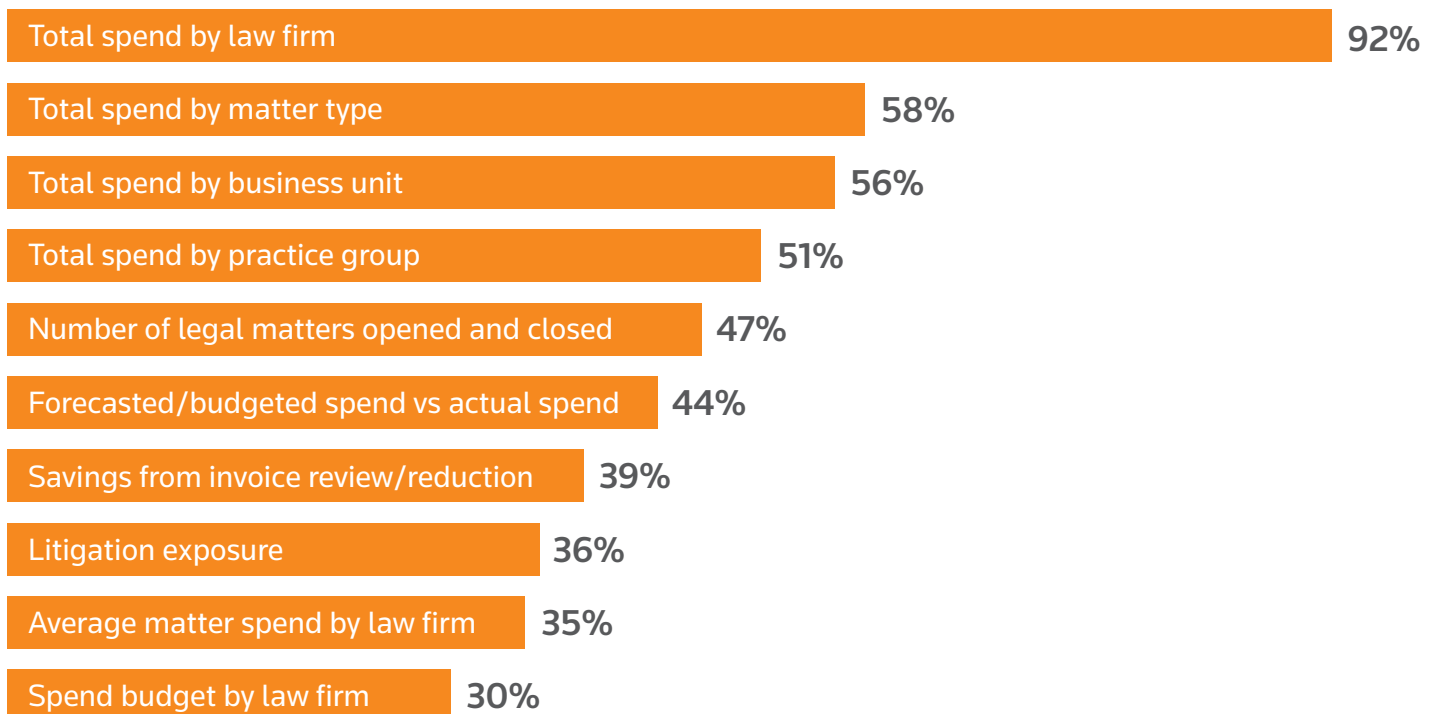
This approach has the advantage of not only measuring efficiency but also enabling teams to demonstrate their effectiveness to senior colleagues elsewhere in the company. However, this still appears to be a minority approach, all over the world. The increased use of metrics to measure law department initiatives, efficiencies, and performance would go a long way toward changing how the department is perceived within the company.

“To adopt an effective legal transaction management system so we can track our incoming work, the workflow status, and the results. A comprehensive one. We have those systems, but we want to consolidate them into one system.”

“Controlling costs, ensuring work is done at the right level, ensuring it is done efficiently and effectively. Being able to measure results.”

Top 10 law department metrics being used

Utilization Rate



Source: Thomson Reuters 2019 Legal Tracker™ LDO Index

Technology, Innovation & ALSPs

WHERE CAN TECHNOLOGY HELP MOST?

In many parts of the world, corporate law departments are applying new technology and innovative ways of getting legal advice in their drive for greater effectiveness and efficiency. Not so in Canada, where companies spend on average 20% less than their American counterparts on technology. In fact, technology remains a small proportion of legal buyers' overall budgets.

Automation of routine tasks remains a prime opportunity for many law departments to increase efficiency and, ultimately, reduce costs. It is unsurprising that, for 70% of Legal Tracker participants, using technology to simplify workflow and manual processes is a high priority.

Top 5 ranking of legal department technology solutions in order of importance

1. E-billing / Spend & Matter Management

2. Legal Hold / Litigation Hold

3. Document Management

4. Legal Research

5. Contract Lifecycle Management

"...there's no real consensus on what is most important to clients as far as innovation is concerned."

Automation is an area where Canadian businesses could invest more as they seek to improve effectiveness and efficiency. The more that corporate law departments can start to digitalize their legal portfolio and workflows, the more they can use data to measure and report on workload, turnaround speed, and exposure — and to do this in a way that measures outputs, which are important to their companies' priorities. Not only does this enable law departments to work smarter and more transparently, it provides a data baseline for improving effectiveness over time as well.

The desire for technology in the legal ecosystem reflects that clients are looking for new ways of working. This is the primary driver for innovation in the legal industry in Canada and throughout the world.

The pursuit of legal innovation has created a highly fragmented market with plenty of opportunity for differentiation for the legal services provider — whether tech firms, ALSPs, or law firms — that gets it right. While e-Discovery and document management are the most demonstrated tech solutions, there's no real consensus on what is most important to clients as far as innovation is concerned. In the absence of specific direction from clients, legal providers need to re-visit their clients' strategic priorities and find solutions that meet clients' business challenges.

Source: Thomson Reuters 2019 Legal Tracker™ LDO Index

But innovation is not just about technology. Some survey respondents talked about taking a *different* approach to problems, while others highlighted the potential for innovation on fee structures.

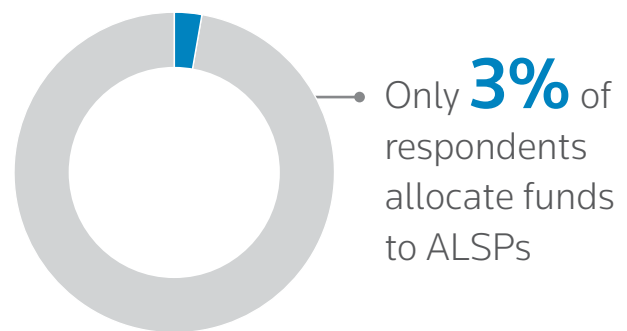
“One of the things that they do that is interesting is design-thinking. They do a survey where they have clients identify common problems, and then clients do their design-thinking around that problem; and then build solutions that target a range of clients.”

“They could charge less and be more innovative in their alternative fee arrangements. They should not wait for us to ask about it; they should take the initiative and make proposals to us.”


Other respondents pointed to relying on ALSPs as a way to infusing more innovation into how their law department works.

Currently, Sharplegal respondents in Canada are allocating only 3% to ALSPs, which is below the global average of 6%. But this relatively low figure may underestimate the impact these ALSPs are having. A 2019 survey by Thomson Reuters* on the ALSP market showed a 12.9% compound annual growth rate, with the larger ALSPs expecting to grow at 24% a year.

The survey also found that corporate use of ALSPs will continue to expand significantly, and it suggests that within three years more than half of Canadian companies will be using ALSPs for some legal work.



The ALSP market showed a **12.9%** annual growth rate 

Larger ALSPs expect a **24%** annual growth rate 

Source: Thomson Reuters 2019 Alternative Legal Service Providers report on US, UK, Canada

Why Corporate Law Departments go to ALSPs

- Access to specialist expertise
- Free up in-house teams to work on higher value-add or strategic issues
- Drive efficiency and reduce costs
- Meet peak demand without increasing headcount

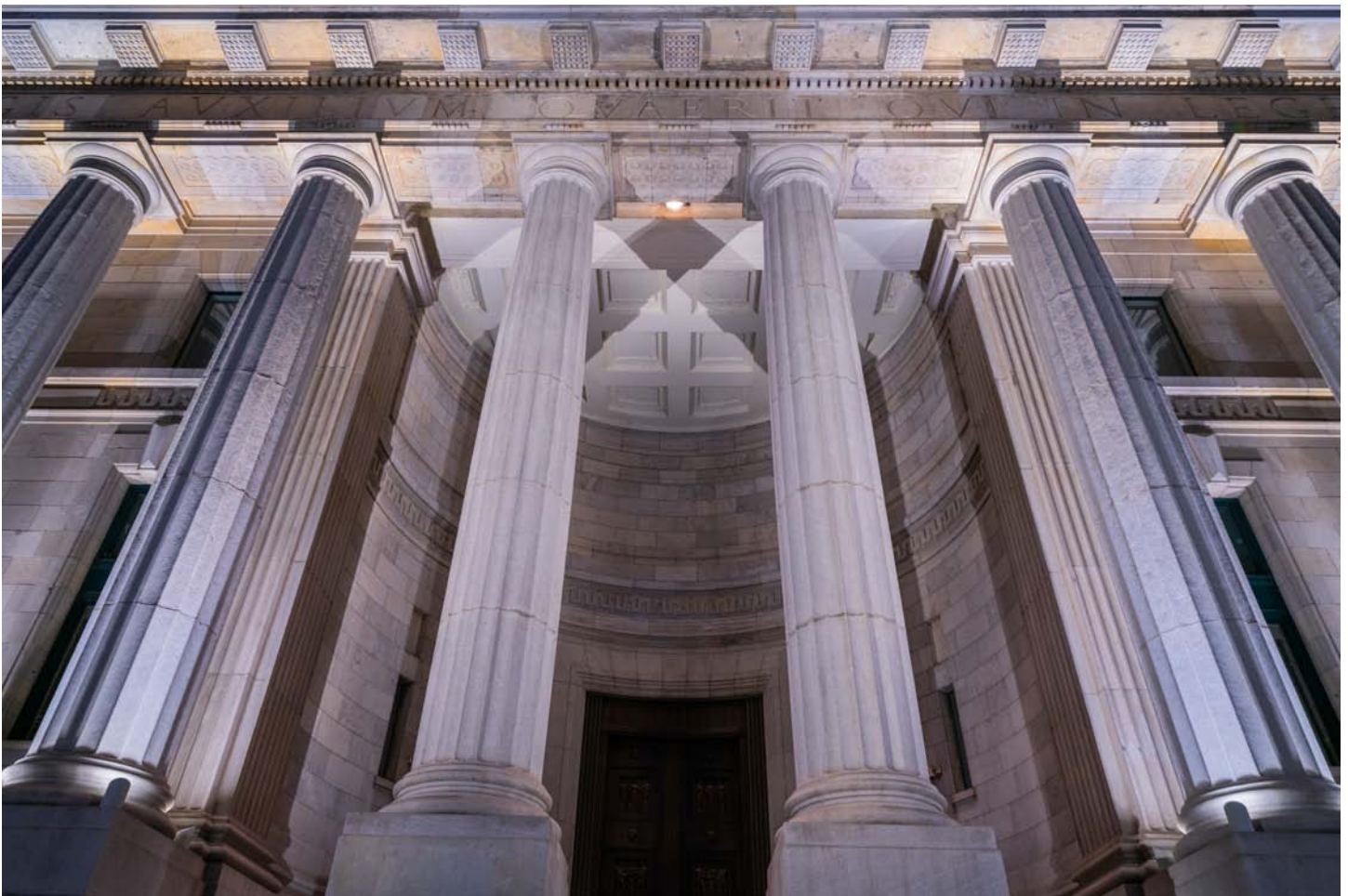
Conclusion

Canada is a strong legal market with growing international demand that sits next door to the world's largest market for legal services, and boasts a client base that values relationships and service as much as cost control. It's an attractive proposition for Canadian legal professionals, but it's not one they can take for granted.

The global trends that are disrupting business models elsewhere will bring their own pressures to the Canadian market. Indeed, domestic clients are already expressing interest and enthusiasm for new, more efficient ways of running their legal services.

As we look beyond the current pandemic, for Canadian law firms – and other legal service providers – that client pressure means they will need to combine high levels of service with innovative ways to improve effectiveness and reduce costs.

If they succeed, the opportunity is there to gain a greater share of a growing legal market – and that is an attractive proposition indeed.



Acritas

Acritas, now part of Thomson Reuters, is the leading provider of market research in the global legal industry. Its annual market studies with in-house legal departments and top law firm talent provide a bedrock of data to help law firms and legal services providers develop strategies which will enable them to gain competitive advantage. In addition, Acritas provides custom research and advisory services from its offices in the UK and the US.

For more information, go to acritas.com

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