

Outsourcing your General Counsel – When is it appropriate?

By Gregory L. Phillips

The concept behind “general counsel outsourcing” is that a business organization may not need to hire a full time in-house lawyer to perform the services and functions performed by a general counsel. Some business organizations may be able to contract outside the organization, resulting in improved efficiencies and profit.

The concept of outsourcing certain business and services functions is not new. It has been used for years. For example, most companies do not maintain their own payroll function, they outsource it – there are specialists outside contractors who can manage the function more cost-effectively. For the same reason, many companies outsource most non-strategic functions – the annual report preparation; staff recruitment; insurance; public relations; advertising; internal audit; staff training; and information services.

When considering a task or job function, a two-question test can be applied as follows:

- *Strategic:* Should this be done in-house?
- *Cost Benefit:* If not, can it be done outside as well, or better, and as cheaply?

So what is new about outsourcing?

What is new is that outsourcing has become a major response to the profit pressures on many businesses. Using a medical analogy, many companies are going through major surgery. There are several favored surgical procedures that have new titles but are familiar in reality. There is “reengineering” (going back to basics); “restructuring” (re-allocating resources); and “down-sizing” (shedding surplus operations and staff). Outsourcing, on the other hand, seems to be the favorite post-surgical procedure.

In the past, companies have outsourced mostly functions considered non-strategic to the company, such as some of those listed above (e.g., staff recruitment and training; public relations; advertising; and internal audit). However, due to increased pressures on profits and accountability issues with respect to corporate governance, there is a trend towards outsourcing “*strategic*” functions of business organizations, such as the general counsel and corporate development/strategy.

The potential application of outsourcing is now such that one has to assume that no aspect of the company is safe from outsourcing. We may come to see a company outsourcing entire departments and functions such as accounting, sales and distribution, human resources, corporate affairs, and even manufacturing.

In each case, the directors and senior management will need to be satisfied that the essence of the business remains intact, even if most of the functions are contracted out. Come to think of it, why not also contract out the directors and senior management? We may then be left with shareholders owning a company whose only non-cash asset is a

brand name and whose only staff and functions are those which are required by law to remain in-house; and, of course, those required to stay around to manage the outsourced contractors and suppliers (or, could that function also be outsourced?).

Outsourcing the general counsel legal function.

Where does the outsourcing of the general counsel legal services sit in the outsourcing question?

It is important to understand that for some business organizations not all functions should be outsourced. The strategic and cost-efficiency test provided above should be applied in each case. Modified to apply to the general counsel legal services function, the test may be posed as follows:

- Are there strategic reasons why the general counsel legal services function should be delivered in-house?
- If not, can general counsel legal services be delivered from outside as cost-effectively?

There is not space in this article to go through the detailed analysis that may be required to arrive at final answers to these questions. It generally comes down to the following principles.

Due to business reasons and company culture, some companies may not want to entirely entrust certain functions to outside contractors – strategic planning, operational planning and control. However, the legal services typically performed by a general counsel that includes the legal analysis, planning and other input, that needs to go into such strategic planning process, and the operational planning and review process could be outsourced to a lawyer who understands the company's business and culture who, in essence, becomes a part-time extension of the company's senior management team.

On the other hand, once a company has made a strategic decision, the legal services involved in the implementation of such decision may need to be handled by a legal specialist in an outside firm. As a general rule, these transactions that implement the strategic decisions may include the buying and selling of businesses and other assets, financing arrangements, applications for regulatory consents and licenses of all kinds, and litigation and dispute resolutions in all forms. It simply may not be cost-effective for an outsourced general counsel to duplicate such specialized legal services, unless they are strategic to the company; but, the outsourced general counsel can manage the services to be performed on behalf of the company by outside counsel to ensure cost efficiency and quality of work.

Most companies recognize that they need legal resources at a senior level to perform this strategic legal function to ensure that the company's major assets and rights are suitably protected and its major exposures and obligations are suitably managed. In practical

terms, this involves an on-going legal risk and opportunities audit, and an ongoing legal compliance program.

Small to middle market companies must make tough decisions when addressing such strategic legal resources. Such companies are constantly seeking ways to obtain the strategic legal resources that their business requires while at the same time trying to save money and increase efficiency. Many such companies find that traditional methods of retaining counsel are not cost effective because traditional law firm overhead costs, for office space and support staff, limit a firm's flexibility in fee-setting. When outside counsel fees climb, emerging companies consider hiring an inside counsel as an employee. With all the benefits that employee status entails, hiring someone to be an inside counsel can also be costly; such companies simply may not have the justification or the resources to hire a full-time in-house general counsel.

Outsourced general counsel services offer an attractive option to such companies. For a specified fee, the company contracts with an experienced and well qualified attorney to provide strategic in-house counsel legal services. The outsourced general counsel is an independent contractor, not an employee. He, or she, works at the company's site and uses company offices and services for typing and copying. Thus, the attorney reduces his or her overhead, while providing the same high quality, high level of service of law firms or employee counsel. The outsourced general counsel becomes an extension of the company's senior management team.

In no event, should any company buy the idea that the outsourcing of general counsel legal services decision is an all or nothing choice. Certainly, some legal services are best delivered externally, from law firms that offer specialized legal services. However, other legal services such as certain legal day-to-day corporate governance issues and strategic functions, can be performed effectively by the company with the help of an outsourced general counsel who understands the company's business.

As in most things, it is a matter of balance and the result of informed and objective analyses. The key issue of determining whether outsourced general counsel services are proper for a company is a question of balancing the delivery of the company's needs for legal services between inside and outside legal providers to ensure an ultimate advantage for the company.

The important thing is to have resources of the correct caliber in the right place to deliver each aspect of the company's legal requirements.

Standards of legal services.

What qualities are required of the lawyer who performs the strategic legal services provider role for the company in an effective way? Most companies who have addressed this question would agree with many of the following:

- the ability to operate at a senior level in the company's organization;

- a close understanding of the company's policies, strategies and objectives;
- a close understanding of the company's operating methods, processes, products, suppliers and customers;
- the ability to manage legal risk, to analyze the company's strategies and in order to identify legal issues, and to develop plans and programs to manage and, if possible, to avoid legal problems that arise;
- the timely delivery of work of high technical quality that also provides practical solutions which meet the company's business goals;
- the ability to work closely and co-operatively with company personnel, suppliers and customers as may be required;
- the ability to add value to the efforts of internal clients, whether this is by saving money, avoiding losses, solving problems, achieving their business objectives, by using knowledge and skills to improve the way the company manages its legal risks and pursues its legal rights and opportunities; and
- the ability to manage external legal services for extraordinary legal issues that arise (e.g., litigation; public/private securities offerings; bankruptcy) in a cost-effective way that achieves optimum benefits for the company

Almost by definition, these qualities can only be performed by someone inside the company, who has absorbed the company's culture and become part of the way the company does business. An outsourced general counsel can provide this level of service and resources for the company.

A classic example of this is the legal compliance area. In recent years and with the recent corporate scandals, there has been a proliferation of laws directed against businesses. Higher standards of compliance are required and stiff penalties threatened. As a result, businesses are coming to see the need to introduce formal legal compliance programs. However, many limit their efforts to the issuing of a manual, which does little more than recite, at great length, the relevant laws affecting the company. The typical manual is usually thick, and while it looks handsome on a shelf, it is seldom consulted by employees. The manual represents a raising of awareness about compliance but is not, of itself, compliance. Compliance only occurs when the relevant legal compliance obligations are reflected in company culture, policies and procedures, agendas, minutes, reports, guidelines, price lists, terms of trade, and so on. Compliance must be embedded into the way the company does business externally and in the way it operates internally.

The only way such compliance will be achieved and maintained is through the disciplined, determined and unglamorous efforts of lawyers and managers. This is a very detailed and time-consuming job. Experience has shown that this work can only be done effectively by lawyers who understand the company's culture and business strategy. Even if outside lawyers tried to do the same job, they could not provide the same quality program as an outsourced general counsel, and their fees would be beyond what most companies would be willing to pay.

By following the approach as set forth in this article, a company will ensure that it has the correct mix of internal and external legal resources to meet its legal services

requirements, and the outsourcing of general counsel services may be one avenue to provide the company with confidence that they have arranged their legal resources accordingly.