The Coming Tsunami

Presented by

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LI31

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The Coming Tsunami

How the next 4-6 years will totally change your environment

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Moving out of Old Assumptions

• It’s hard to get
• Your ass in gear
• When you are
• Burdened down
• By an old set of
• Assumptions

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Quality Service Grid
From The Customer-Driven Company

Quality Service Grid
From The Customer-Driven Company

The Cobb Value Curve
Positioning Your Firm

Adapted from Richard C. Whitely’s Book
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The Way to Look for the Future

- Look first at **Events**.
- They will point to **Trends**.
- Trends will point to a new **Era**.

Professor Nadia Thalmann with Nadine
Your next receptionist?
January 15, 2016 Forbes/Tech
The Forces of Change

Adapted from Michael Porter’s "How Competitive Forces Shape Strategy"

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The Ever Increasing Frequency of the Waves of Change

• Wave 1: Industrial Revolution and Process Improvement.
• Wave 2: The Internet.
• Wave 3: Cell Phones and instant transfer of Information.
• Wave 4: AFA’s and the destruction of the Business Model.
• Wave 5: Artificial Intelligence & IBM’s Watson.

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Questions from the Fifth Wave

- Leverage and Specialties?
- Compensation of Partners?
- Training of Associates and Para-Professionals?
- Upgrade of the Client Base?
- Services the firm can and will provide?
- Chunks of work that must be outsourced?
- Mergers and Acquisitions for Market Share?
- Growth or Shrinkage?
- **Where will the capital come from?***

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This Leveraged, Matter Staffing Model *Is Dead*

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The Cobb Value Curve

Positioning Your Firm

HIGH
NUCLEAR EVENT
HIRE FOR EXPERIENCE
BRAND NAME SERVICES
PRICE INSENSITIVE

LOW
PRICE SENSITIVE
COMMODITY SERVICES

RELATIVE VALUE ADDED
VOLUME OF WORK AVAILABLE

Client Power

Degradation in Realization
The Leaks in the Pipeline

Potential W.I.P. A/R Collections
O.H. O.H. O.H. O.H.

90% 81% 72%

P? Discounts
P? Write-Downs
P? Inattention to guidelines

P? Partnership
P? Project Mgt.
P? Arrogance

P? Negotiation Skills
P? Delegation
P? Turnover
P? Intake

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Implications of the Tsunami

• Disintermediation.
• Compensation will be turned upside down.
• Leverage will be upside down.

The Required Foundation
From the Bottom Up

• Collaboration supported by:
  – A supporting vision and core values.
  – Mutual trust and accountability.
  – Supporting vision and core values.
• Create a learning organization that is willing to innovate.
• Demonstrated internal improvement.
• Client recognition of benefits that provides continued recognition and financial results.
Creating a New Business Model
McKinsey Quarterly http://bitl.ly/1QRKD6U

• What are the long-held core beliefs?
• Dissect the long-held beliefs in supporting notions.
• Turn the underlying belief on its head.
• Sanity-test your reframe.
• Translate the reframed belief into your new business model.

The Myths of Change
Moving a Firm From Good to Great
Taken from Good to Great by Jim Collins

• The Change Program.
• The Burning Platform.
• Higher Compensation Will Motivate.
• Fear Driven Change.
• Acquire Into Greatness.
• Revolution.
Creating Permanent Change

- Debrief from this and other sessions. Create a Pareto Chart on the implications.
- Create a sense of urgency.
- Find a core coalition that sees the urgency.
- Have the core coalition create a future vision.
- Communicate with stakeholders.
- Remove petty barriers.
- Create short-term wins.
- No victory celebrations.
- Anchor the changes into the fabric of the firm.

Question? Comments?

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The Coming Tsunami in the Legal Profession
Are You Ready to Adapt?

There have been four waves of change over the last fifty years. We are now entering the fifth wave and this one will be a tsunami. The lawyers who do not recognize the trends will not be able to enter a new era and survive. The fifth wave will turn partnership leverage, compensation systems, and the business model upside down. There is not much time to make the incremental changes that will support sustained profitability in law firms. Many firms will be acquired out of existence.

INTRODUCTION

Picture yourself driving up to the office, telling your car to “go park” and then walking into your office in 2020 (just four years from now). You are greeted by Nadine who is a robot tied into social media and into IBM’s Watson. She has already prepared the management reports through yesterday and communicated with the other Nadine robots who work for the partners on the status of each case in the office and updated the files on each client with current events. Your firm has had to let many of the administrative staff, para-professionals, and associates go because all of the work they were doing is now being done by these “nice” robots. (Forbes reported in December 2015 on this quote from Jeff Greene at the Conference on Inequality: “What the global economy did to the blue collar worker....big data, artificial intelligence and robotics will do to the white collar economy.”) This scenario is not as far fetched as you may think. Satya Nadella, CEO at Microsoft introduced a Nadine created by Professor Nedia Thalmann at the World Economic Forum recently. Cancer Centers across the country are using Watson to set up treatments. According to a Wall Street Journal article on March 9, 2016 on page B5, KPMG is using IBM’s Watson to help them examine corporate America’s books. See the Wall Street Journal CFO Journal, “Auditors Count on Tech for Backup.” Linklaters of London created “Blue Flag” years ago to take the place of over 20 lawyers.

I invite you to go back in history and look at the waves (trends) that have turned into eras. Wave 1 was the Industrial Revolution in the early 1900s that propelled your clients to improving the quality of service and the analysis of the processes for manufacturing. The same has come true for evaluating outside counsel. Wave 2 was the Internet. A famous quote from the “Seize the Future” conference in 1997 on the future of law was: “What the printing press did to the monopoly the priests and rabbis had on the interpretation of the Bible, the Internet will destroy the monopoly lawyers have on interpretation of the law.” Wave 3 was the introduction of I-Phones and Tablets has revolutionized the communications and the transfer of information. Wave 4 was the introduction of alternative fee agreements (AFAs) and other pricing models that have created an Industrial Revolution type of scenario, where process improvement and project management has to work.

For example, look at what happened to other professional service providers. Doctors in the 1980s had to go to procedures at a fixed fee to satisfy payers. CPAs in the 1990s
had to go to process improvement with clients asking for a fixed fee for audits. Wave 5: the age of artificial intelligence, big data, and IBM’s Watson doing the work of administrative, para-professionals, and associates. Who will survive? My take? Lawyers must become counselors and not product producers. Firm leaders must take a 1%, step by step change process in the business model of the law firm.

**THE FIFTH WAVE: NEW BUSINESS MODEL**

There are many questions that cannot be answered in this article but I will try to address a sample. For example, here are some questions that come out of the fifth wave. How will a new business model affect the following:

|$\$| The leverage and specialty structure of the firm?
|$\$| The compensation of partners?
|$\$| The training of para-professionals and associates, if there are any?
|$\$| The model employee, who is hired and why?
|$\$| The upgrade of the client base? Can a firm accept just any client?
|$\$| The restructuring of services the firm can and will provide to clients?
|$\$| What chunks of work, typically performed in the firm, must be outsourced?
|$\$| Growth or shrinkage in the firm?
|$\$| Mergers or acquisitions of law firms?

Where will the capital come from to invest in all these changes? We must go through the art of “creative destruction.” We must create something that will change our direction by 1% per iteration. I used to fly and if I was off by 1 percent in my heading, I would have missed a 10,000 mile way-point by over a 100 miles. A 1% change in direction works, one step at a time. A 1% change allows a review of the resulting change and the ability to assess the change and adjust for the future. What are the building blocks for one percent incremental changes? Leaders must manage their culture to create a learning organization. Culture propels the organization - good to success and bad to destruction. The foundation of a successful firm in the new era is driven by the following building blocks. Starting at the base:

1. Collaboration supported by:
   a. Mutual trust and accountability and
   b. Innovation and constant improvement and
   c. Supporting vision and core values that,
2. Create a learning organization willing to innovate and invent new ways of delivering legal services which produce.
3. Demonstrated internal improvements in efficiency and effectiveness that improve the quality of life and experience for partners, employees, and clients. That creates,
4. Client recognition of the benefits in fee predictability and service which provides continued recognition by clients and financial results to the firm.

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If the firm focuses on financial results without the building blocks that support it, the firm will waste away as if it had a cancer.

**A Few Implications of the Coming Tsunami Wave:**

*Disintermediation* is the elimination of people in the mix because of better process management and replacement of human beings by thinking machines that can perform the same tasks. In business, disintermediation has typically affected the middle managers in the organization. These are the producers who create and manage the product or they filter the information going to the top. In law firms, these are the drafters and reviewers of legal products. The firm must still have knowledge experts and counselors who can deal with the critical issues and expert decisions. But those tasks that fall in the lower half of the Cobb Value Curve will be done by artificial intelligence.

With artificial intelligence and access to vast amounts of world information by computers, where will the people in the middle go? What will happen to law schools and how will their curriculum have to change? Who will be the new professionals? In several IP firms I am familiar with, there are more PhD professionals than there are lawyers and the PhDs make more than many partners. Is this the future for commercial and litigation lawyers?

The new business model will turn compensation upside down. What does your firm value most? If a consultant were to look at your compensation system, it is highly likely that those who have the biggest book of business make the most money. But if some simple return on investment principals are used, they would not make nearly as much. If a calculation of realization (return on time invested) were performed, calculations of performance would be very different. There are three levels of realization. R1 is the percentage of the standard rate that goes into work-in-progress (what the lawyer told the clients the billing rate would be for the matter). R2 is the percentage of work-in-progress rate that gets billed into accounts receivable. R3 is the percentage of the billed rate that is collected and the cost of money for long-standing receivables. A 50 million dollar firm that has an overall realization rate of 90% (R1xR2xR3) loses 5 million dollars of distributable income. There are many articles on realization that can be found in my website www.cobb-consulting.com and other websites.

Leverage will be upside down. With disintermediation, many of the para-professionals and associates will be replaced by artificial intelligence beings and systems. Partners will have to learn how to practice with their new robots. They will have learn how to be efficient in communicating needs and tasks. They will have to create process maps for their matters. They will have to learn how to break up tasks in a process into chunks of work to out-source what should be done elsewhere and what should be done in-house with the firm’s accumulated knowledge base. That will require administrators to create a training process to move one step at a time to process maps for work in the firm.

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The Cobb Value Curve shows the clients’ perception of value added of the overall service and/or the value added of each task in the delivery process. The first step: the recognition that partners need to understand process and process maps. The second step: to create and use the processes. Consulting firms and accounting firms already use process maps to improve realization and reduce the time invested in projects. Pricing professionals can help lawyers create the processes maps. In addition, as many of my clients have found out, project managers from inside a client have the skill set to work within firms to create the process maps and show how to use them.

**Creating a New Business Model**


1. Outline the dominant business model in the profession. What are the long-held core beliefs about how to create value? For example, here are some basic beliefs of the current law firm business model.
   a. Billing rate multiplied by the time invested equals value added. Such a belief promotes inefficiency (wasted time) and ineffectiveness (doing the wrong things). A great defense lawyer once said to his team: “We are not trying to build a Maginot Line here. The client can’t afford that.”
   b. Growth through mergers and acquisitions equals market share, profits, and sustained performance. A firm cannot acquire itself into greatness as we have seen from the Howrey and Dewey implosions. *See Biness Insider, “Eight Most Crushing Law Firm Implosions,” [http://read.bi/1pGDAF3](http://read.bi/1pGDAF3). The second fallacy with this belief is that to acquire market share a firm has to reduce rates or take risks and write-offs. That kills realization.*

2. Dissect the most important long-held beliefs into their supporting notions. How do notions about customer needs and interactions, technology, regulation, business economies, and ways of operating underpin the core belief?
   a. Client needs beliefs: (1) Only lawyers can interpret the law; and (2) clients need to come to the lawyer’s office. We know that neither of those statements is true today.
   b. Business economics beliefs: (1) Associate pay is cheap relative to the production and billing rates they can create. This is becoming more and more a fallacy as clients demand seasoned lawyers for their work. (2) Technology has changed the landscape from FedEx and Fax, to e-mails, text messaging, big data and IBM’s Watson, and artificial intelligence.
   c. Regulations continue to become more and more complex as the growing number of bureaucrats keep creating new ones to justify their existence.

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3. Turn the underlying belief on its head. Formulate a radical new hypothesis, one that no one wants to believe - at least no one currently in your firm. For example,
   a. What if there were no para-legal and associate leverage? The primary leverage your firm has is your accumulated knowledge built by the firm and your access to global data bases.
   b. What if the perception of clients to your value added had nothing to do with your work pace or your billing rates?
   c. What if you can get specific tasks done in chunks by accessing a global workforce for small increments? By building process maps for various matters in the firm, you could identify chunks of work that could be performed faster and cheaper by an outside provider. A law firm in New York was able to develop a process map for IPOs that reduce investment of hours by 20%, reduced turn-around by three weeks, and increased realization to 120%.

4. Sanity-test your re-frame. Applying a re-frame that has already proved itself in another firm greatly enhances your prospects of hitting on something that makes business sense. For example, the way accounting firms went to a complex process to manage audits under a fixed fee systems and six sigma six.
   a. In the 1980s, doctors had to go to specific procedures to accommodate the insurance companies. This created whole new processes for rendering medical care in order sustain and improve efficiency.
   b. In the 1990s, CPAs had to develop process maps to determine what was critical and not critical in an audit in order to comply with client demands for fixed fees. Now they are improving the process again.
   c. Law firms like Linklaters developed a way to perform complex financial offerings through a system called “Blue Flag” that reduced the turnaround time from more than three weeks to one day and eliminated the need for 20 plus lawyers per transaction.
   d. If you are persistent, you can find such innovations for every practice area of the firm.

5. Translate the re-framed belief into your firm’s new business model. Typically, once firms arrive at a re-frame, the new mechanism for creating value suggests itself - a new way to interact with clients, organize your business model, leverage your resources and capture income.

Nine Steps for Creating and Sustaining Change

Do you want be reactive and lose the race to 2020 or be proactive and start the incremental changes now?

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Step 1: Start at the end of today and debrief from all you have heard at this conference. List all the changes suggested in this session and others. List all of the old assumptions held by your current business model as they were outlined in the discussion of the McKinsey article above. Then list the implications that will be detrimental to your firm’s future. Create a modified Pareto Chart listing the negative implications on the firm. The X-Axis on the implications chart represents the Impact of the coming tsunami on your firm and your clients on a scale of 0 to 10. The Y-Axis on the implications chart represents the probability that bad things will happen to the firm on a scale of 0 to 10. Any implication that gets a combined score (X times Y) of 160 should be on your take home action list.

Step 2: Create a sense of urgency to show how long it will take to be fully functional in the world of 2020.

Step 3: Find a core coalition of leaders in the firm that see the urgency and want to start the incremental changes to a new business model.

Step 4: Have the core coalition create a vision of what the new business model should be and what incremental steps are required to get to that vision. These incremental steps are measurable and time-sensitive as in 1% changes in direction. Use the Pareto Chart again to identify what steps will move the firm forward toward the vision with the most impact and the highest probability of success.

Step 5: Communication with the core coalition and the clients involved will be critical. Keep the team and the rest of leadership in the loop so progress can be shown along the way.

Step 6: Remove the petty barriers. Blue Flag was only created by taking some lawyers off line for almost two years. One major firm has been working at the changes mentioned above for over ten years starting first with the development of model process maps.

Step 7: Divide up the progress steps into incremental objectives to realize short-term wins.

Step 8: Have no victory celebrations. This is a long-term process with a series of short-term wins. Keep improving the model. The firm that created the IPO process six years ago has continued to improve the model.

Step 9: Anchor the concepts into the fabric of the firm. Once the model works in one area of practice and financial objectives can be demonstrated, have other groups submit proposals to go through process with the support and consultation of the core coalition.

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SUMMARY

The next four to six years will be critical for law firms regardless of size. We know the Tsunami is coming because there are too many recent events that point to a general trend. Once a trend is established, a new era will begin for law firms. If not prepared, law firms will find that they will go the way of the guilds of the 1800s as processes and artificial intelligence takes over the analysis and production effort. Efforts must be started now. Every newspaper report I see on the accomplishment of a major change in law firm management or delivery of services began at least four to five years before the reported success.

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