

INNOVATION IN THE AUSTRALIAN LEGAL PROFESSION

ABSTRACT

Summary of 2016 Survey Results

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RESULTS OF THE 2016 SURVEY

Executive summary

In the first half of 2016 a survey attempting to measure innovation in the Australian legal profession was administered to a range of principals in Australian law firms. The key findings from the survey are:

- Innovation was regarded as critical to long term law firm survival with many respondents noting increasingly voracious competition and the necessity to respond more efficiently to client needs.
- The largest sphere of innovation in Australian law firms has occurred in relation to the firms' operational processes, such as new ways of recording fee earner productivity
- A small percentage ranging between 7 and 14 per cent of Australian law firms are engaging in novel innovation; whereas between 9 and 31 per cent of Australian law firms are engaging in non-novel innovation
- The top 3 reasons for innovating were to increase responsiveness to client needs, to increase profit or to increase income. Generally those aims were met when innovation was implemented.
- Innovation is not only driven by profit maximisation. Of the firms engaged in pro bono activities, 54 per cent reported that they innovated in that field
- The major barriers to innovation were the high cost of innovation projects and the regulatory constraints on the legal profession

Introduction

The Australian Bureau of Statistics routinely collects statistics measuring innovation across the economy. However, these have not been undertaken on a sectoral basis and to date there has been no academic study which has attempted to measure the degree of innovation specifically in the Australian legal profession. This survey aims to provide a better picture of the state of innovation in the Australian legal profession than is currently available. By examining patterns of innovation across the Australian legal profession the survey identifies:

- Key drivers of innovation in the Australian legal profession, for example, clients, suppliers such as legal software providers or internal research and development
- Areas of innovation, for example, in pricing, service delivery, firm organisation, marketing, strategy or business processes
- Distribution of innovation, for example, in big established firms, small established firms, small, newer firms or widespread
- Degrees of innovation, for example, efficiency oriented without restructuring business model or radical change of business model
- Impacts of innovation in the market on law firms and their behaviour. 54 per cent of firms have innovated in respect of their pro bono activities

As a result of the survey and further in depth interviews with members of the Australian legal profession, we hope that the legal profession will be placed to make more informed decisions as to

how to maximise efficiency while protecting client interests, the rule of law and the interests of the profession overall. Policy makers will also be better armed with information that may assist them determine how best to shape regulation of the legal profession in relation to such matters as intersecting regulation of the profession across global jurisdictions and fiduciary responsibilities in light of the automated delivery of legal services where there is no lawyer-client engagement.

The survey enables comparisons of the degree of innovation in the Australian legal profession on a State by State basis as well as a firm by firm basis, for example large firms compared with smaller firms.

The survey was conducted jointly by the University of South Australia and the University of Queensland. It used well established methods (OECD, 2005) to elicit an understanding of innovation and the practices and performance of Australian law firms that support the introduction of innovation. A total of 185 law firms responded to the survey - 75 through an online survey and 110 by phone. The survey sample comprised:

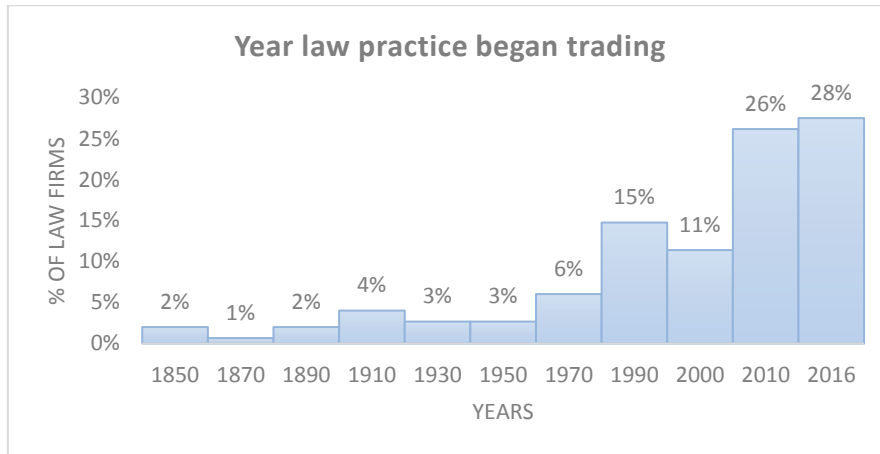
- a. 700 email contacts to Australian law firm principals requesting participation in the online survey
- b. 618 phone contacts to Australian law firm principals requesting participation in the telephone survey.

This report focuses on the 150 responses which contained no missing data to provide a first overview of the state of innovation in the Australian legal profession. The results will be used to influence and inform policy makers to help drive strategic decision making in law firms in the face of challenges such as digitization of services, globalisation and increased competition.

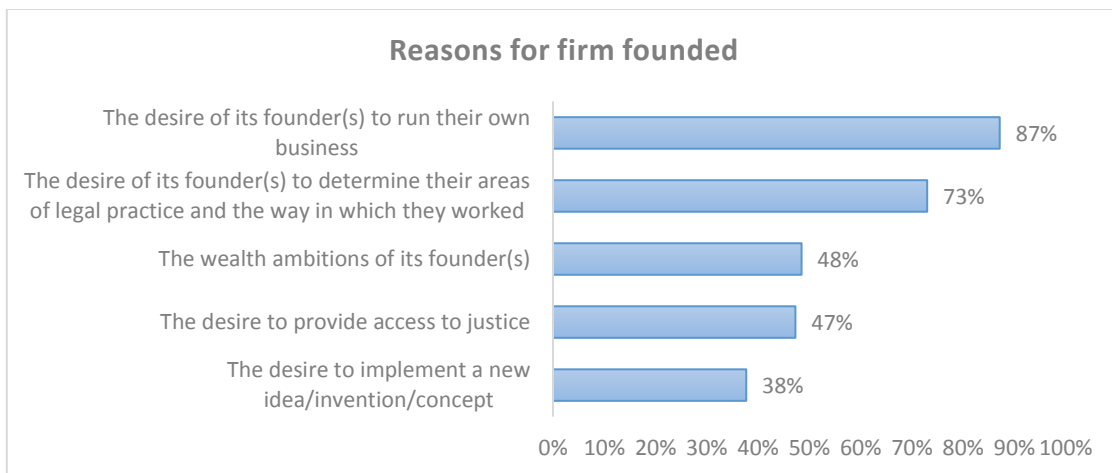
Section A

Characteristics of responding firms

The firms that responded to this survey ranged from older than 160 years to 1 year. The oldest company started trading in 1824. 65 per cent of firms started trading after 2000, of which 54 per cent were formed during the past six years.

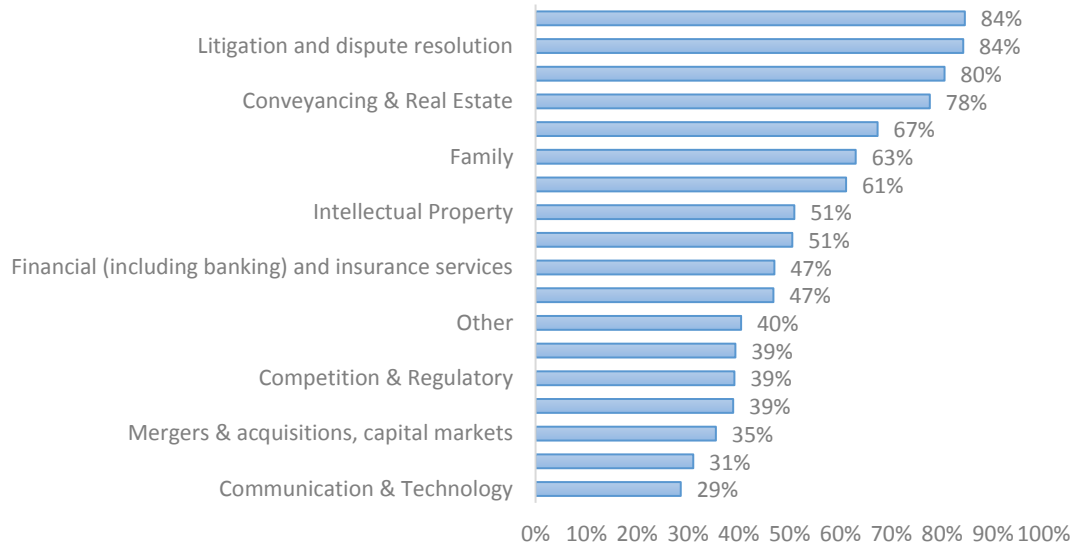


We asked respondents why firms were founded. Most founders (87 per cent in total) had the desire to run their own business, while only 38 per cent started because they had the desire to implement a new idea/invention/concept. These reasons were not mutually exclusive.

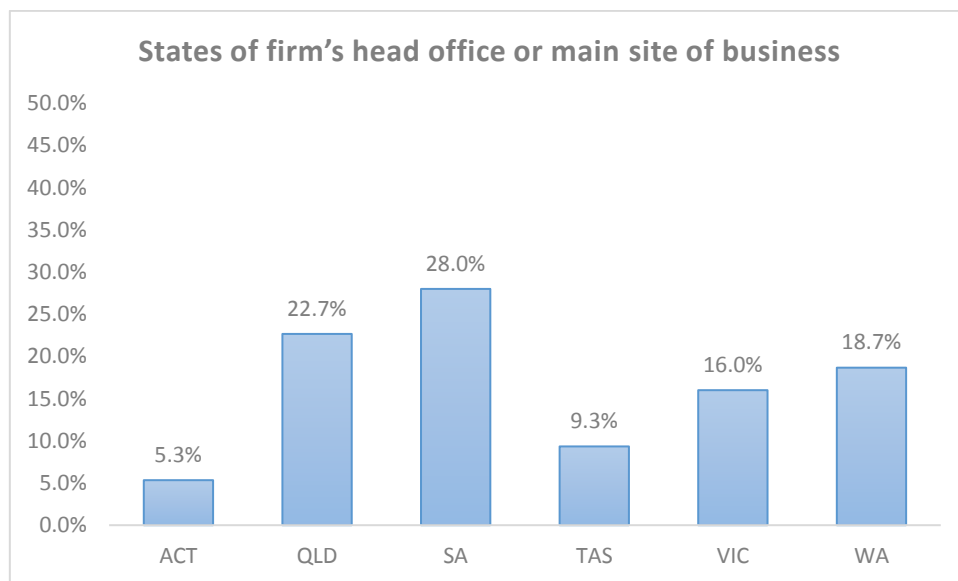
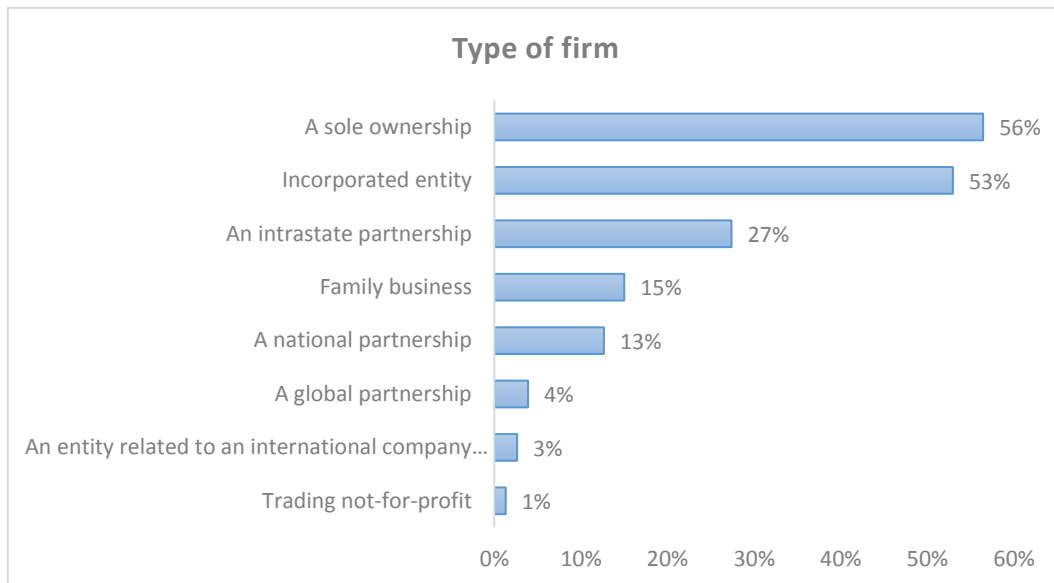


When asked about the areas of law that firms covered, wills and estate practice together with litigation and dispute resolution were the most popular areas (84 per cent), with communication and technology the least popular with 29 per cent. "Other" included personal injury and migration.

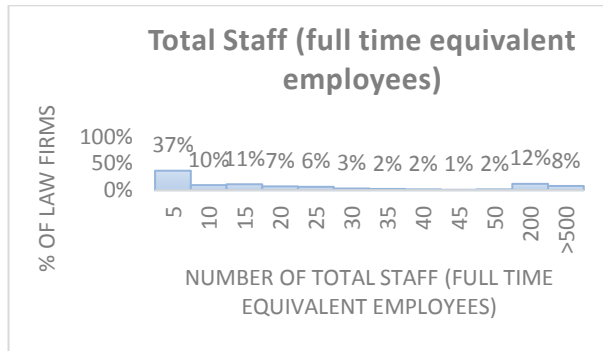
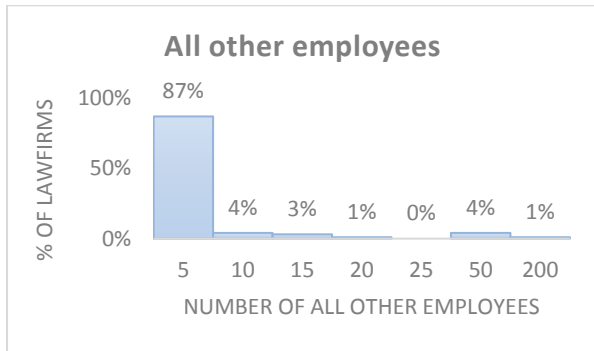
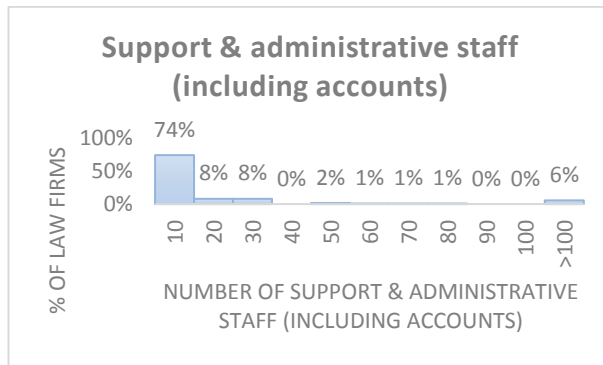
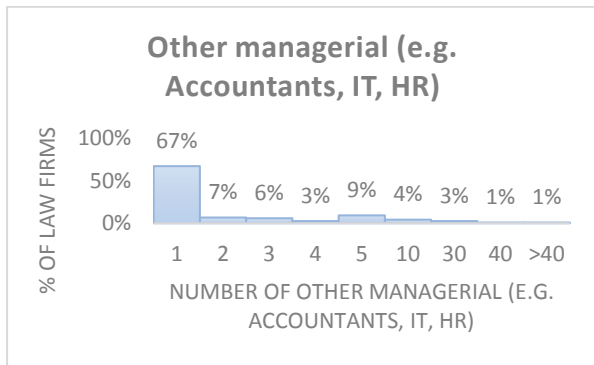
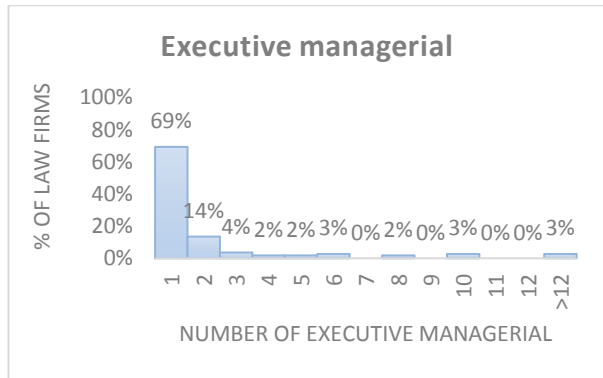
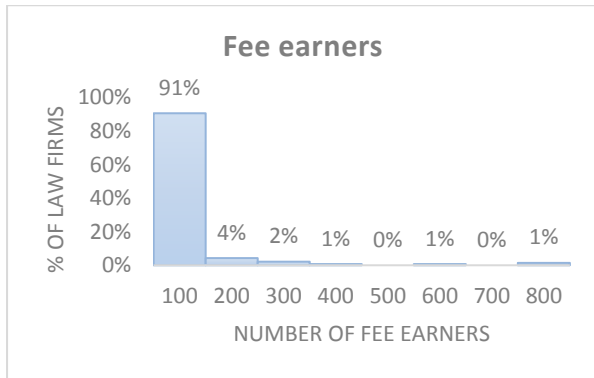
Areas of engagement



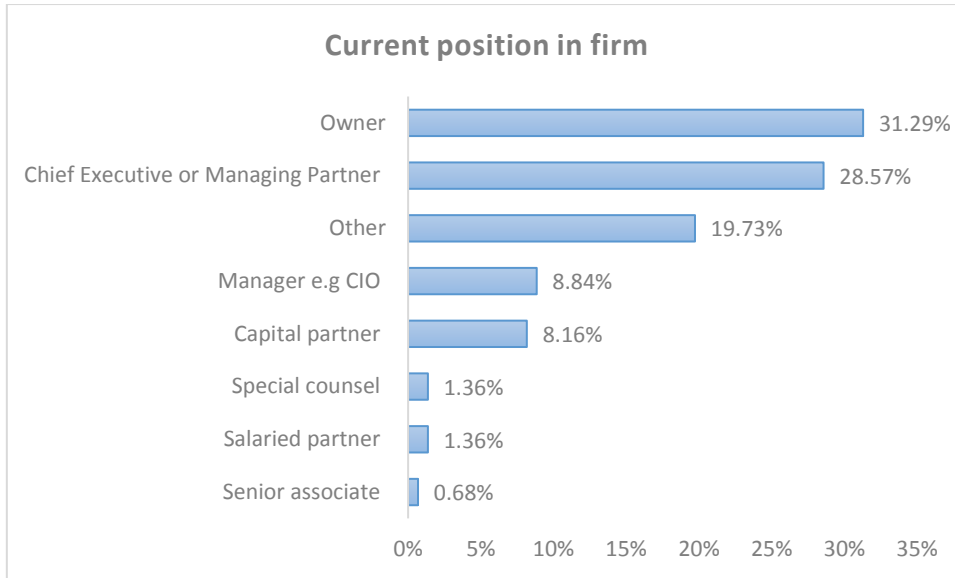
Sole ownerships and incorporated entities were the most popular types of firms. While 13 per cent of firms were national partnerships, only 4 per cent were global partnerships.



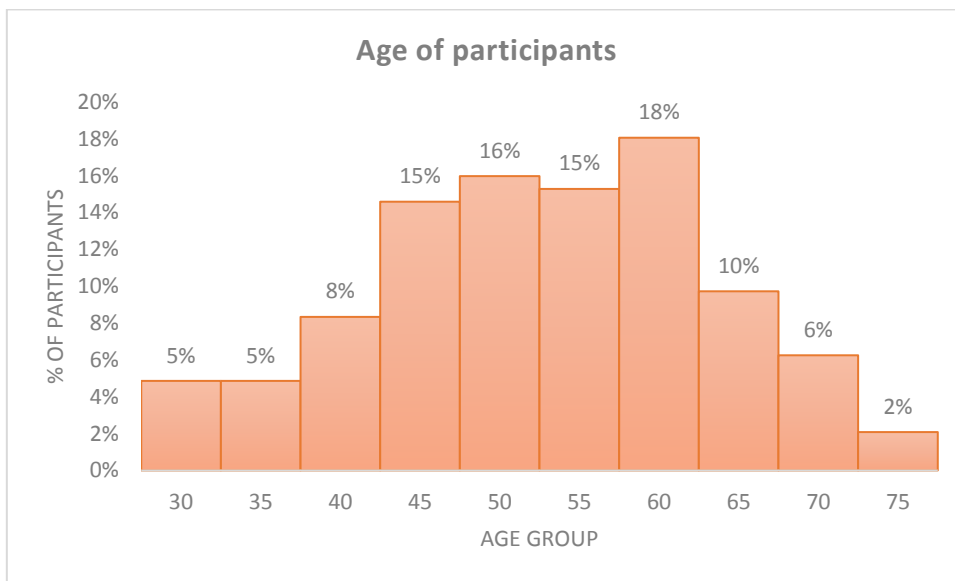
We asked about the different occupational groups in each firm. 91 per cent (127) of the law firms had fewer than 100 fee earners employed. The largest number of fee earners employed was 800. Most firms had 1 executive manager, with 14 per cent 2 and the rest (17 per cent) more than 2. The largest number of executive managers employed was 40. 67 per cent of the law firms had 1 other managerial role. 74 per cent had 10 support and administrative staff. The firm with the most support and administrative staff, founded in 1935, had 800 staff members in this role. A total of 87 per cent of respondents indicated that they had fewer than 5 other staff. In total, 74 per cent of firms had fewer than 30 full time staff. The company founded in 1935 had the most full-time staff with 1480 employees.



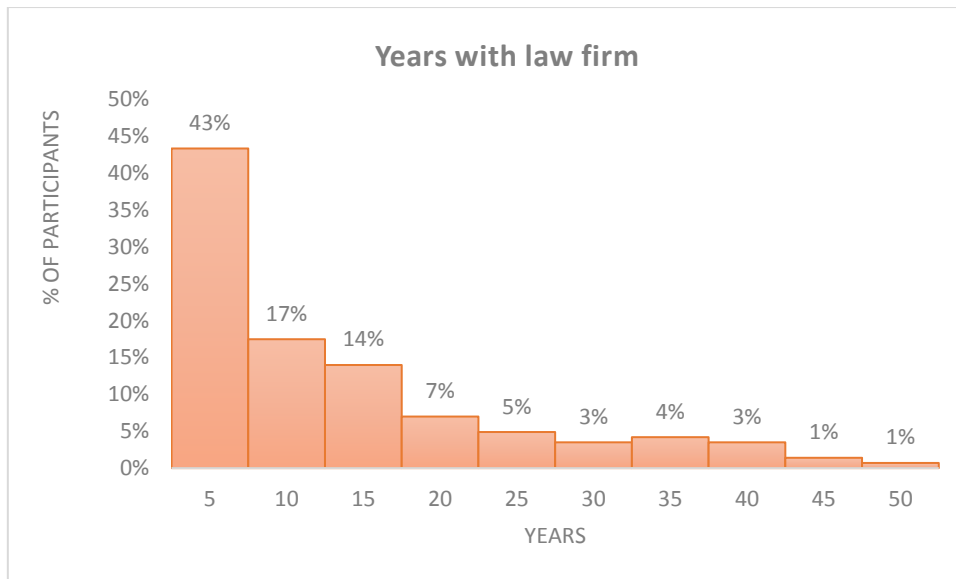
We also asked a number of questions about the demographics of the person who completed the survey. The first asked about the person's current position in the firm. Almost 60 per cent of respondents were owners, CEOs or Managing Partners.



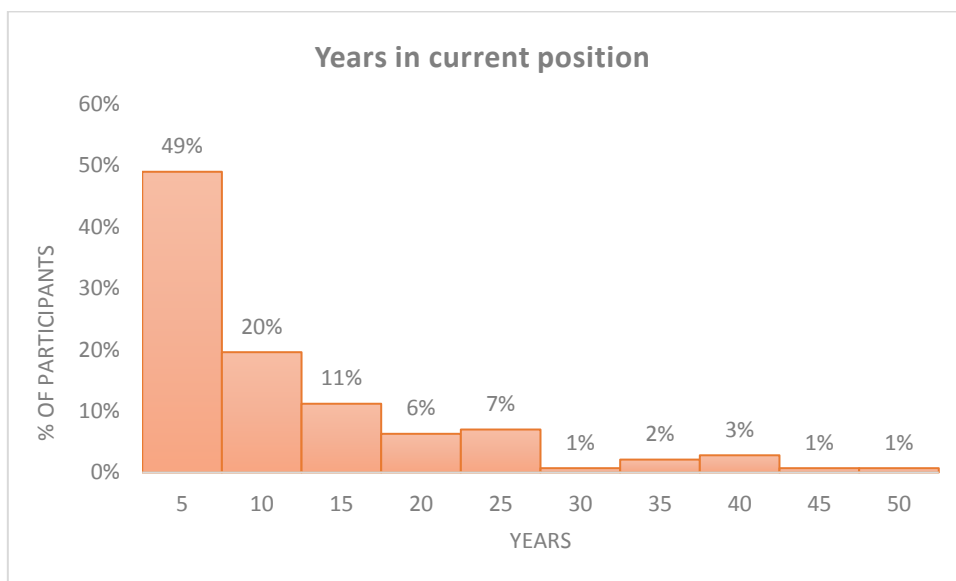
Respondents' ages were well distributed, with 82 per cent between 40 and 60 years. The oldest respondent was 74 years, working as a lawyer for almost 50 years, with the youngest 26 years.



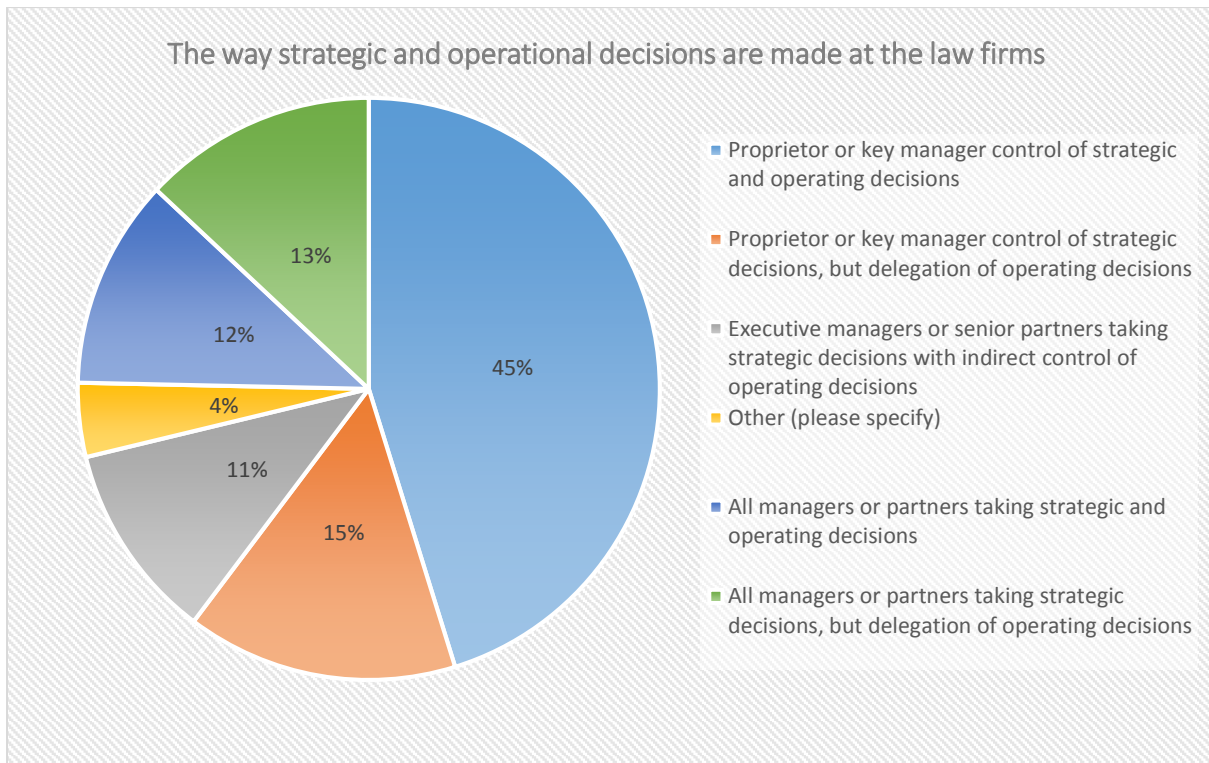
Approximately 82 per cent of respondents had been with the firm for less than 25 years, with 43 per cent there for fewer than 5 years. The respondent who was with a firm the longest was there for 47 years.



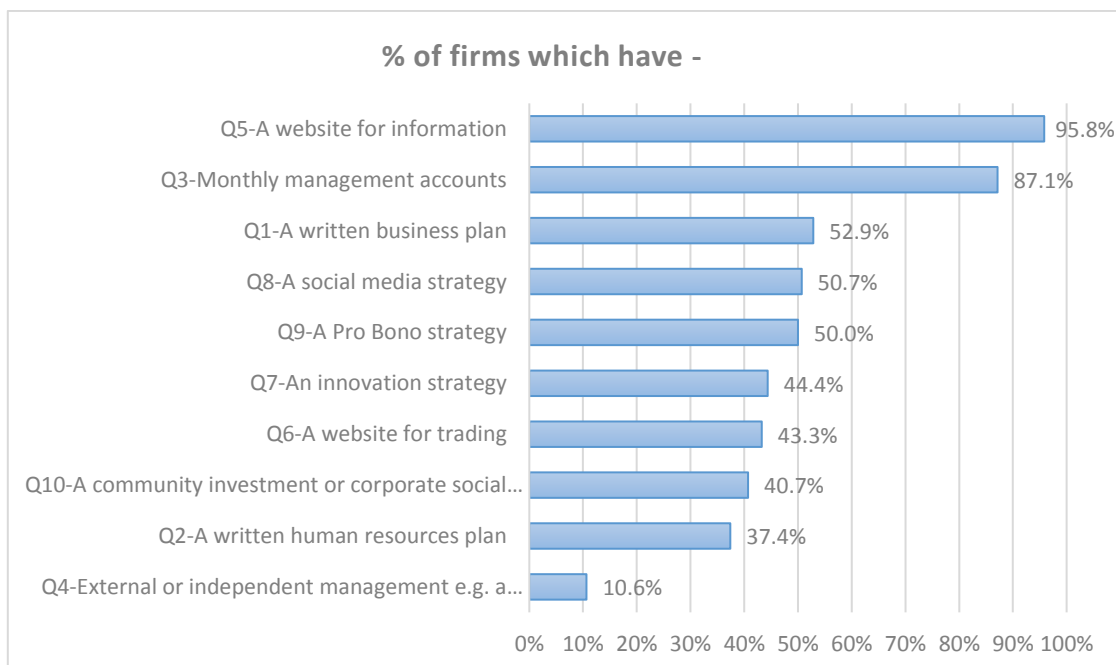
Almost 50 per cent had been in their current position for less than 5 years. The respondent who was 74 years old was also the principal of their firm and had been in the same position for 47 years.



We then asked respondents who was responsible for decision-making in their firms. Respondents to this question reported that 45 per cent of key decisions were made by the proprietor or key manager. “Others” in the figure below included a dependent or independent board that set strategies.



Closely related, we asked about the type of planning in which firms engaged. Almost all firms had a presence on the web (85.8%), with 87.1 per cent using monthly accounts to monitor the financial aspect of the business. Only 10.6 per cent had an external or independent management or board of directors.



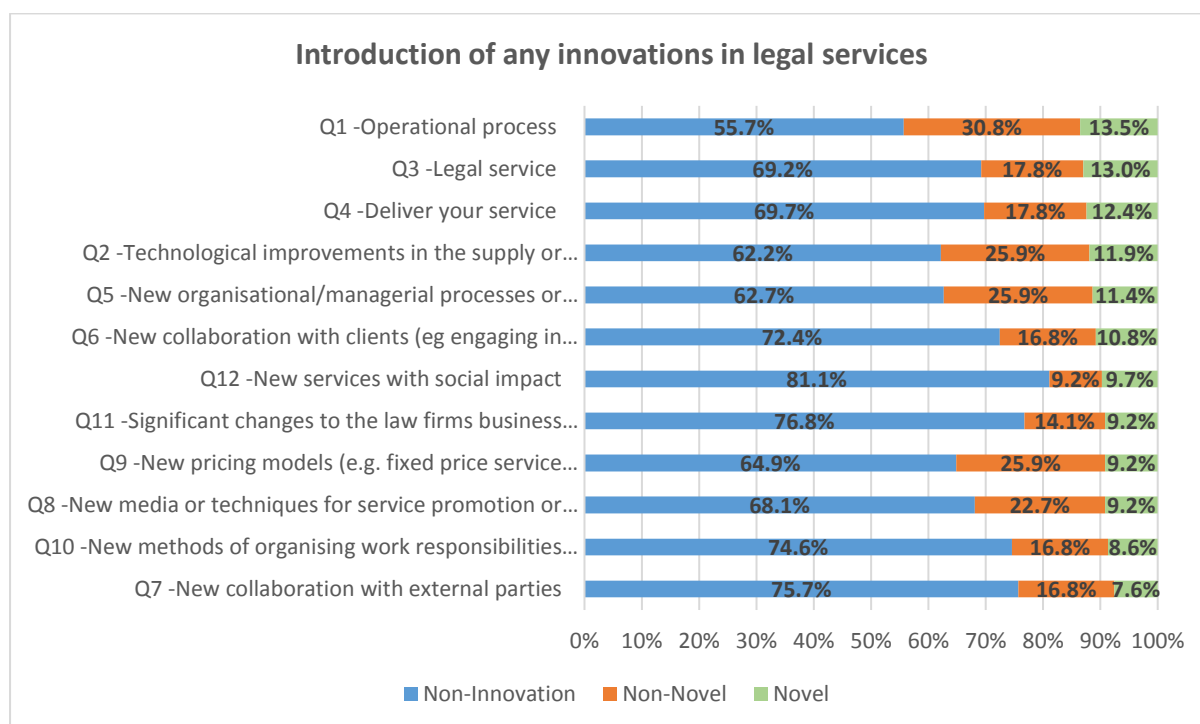
Section B

Innovation

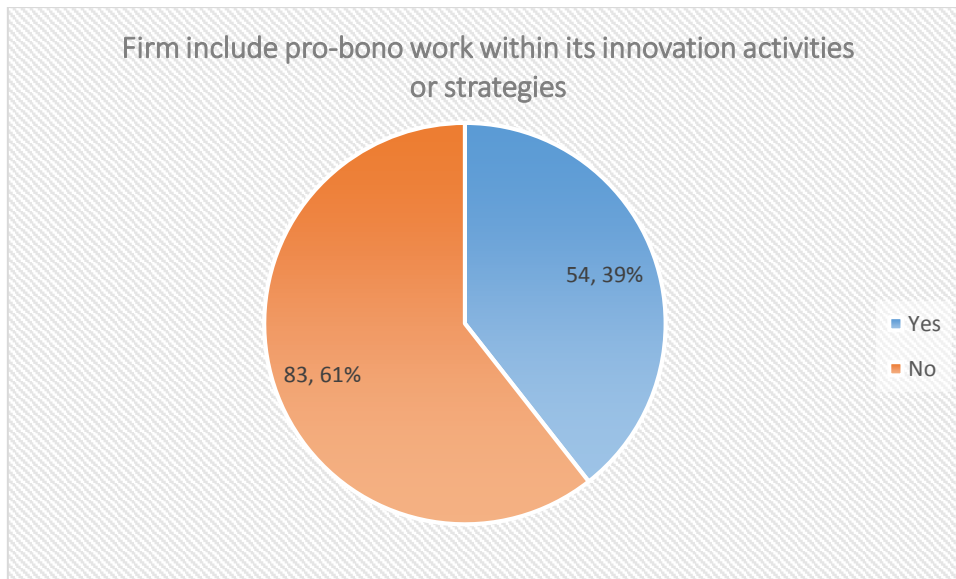
Innovation occurs when a new or significantly improved service or service product is introduced to the Australian legal services market (product innovation), or when a new or significantly improved production, or delivery method, is used commercially (process innovation), and when changes in knowledge or skills, routines, competence, equipment, or practices are required to develop or make the new category of service, or to introduce the new process.

We first asked about the types of innovation in which firms engaged. Each firm was asked to indicate if innovation was new to the industry (novel), new to the firm only (non-novel) or if they did not introduce any innovation in a particular category (non-innovator).

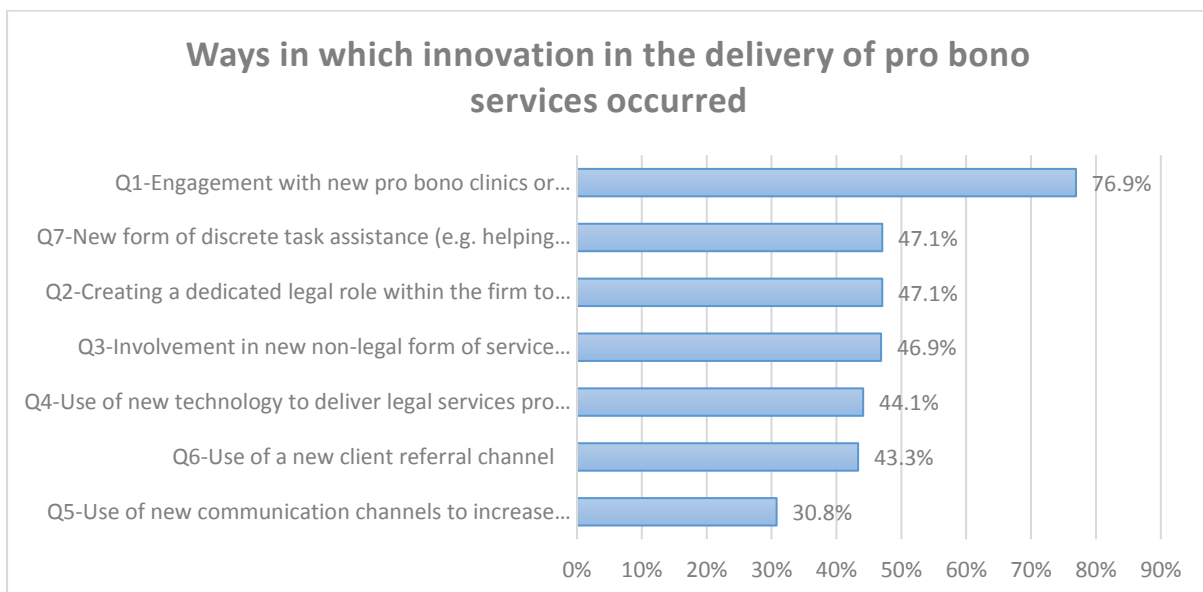
Novel innovation ranged between 7 and 14 per cent in each category and non-novel innovation between 9 and 31 per cent. Most innovation occurred in the category “operational processes (e.g. a new way of recording fee earner productivity)”. The category where the least innovation took place is “new services with social impact” with an 81.1 per cent of firms comprising non-innovators in that category.



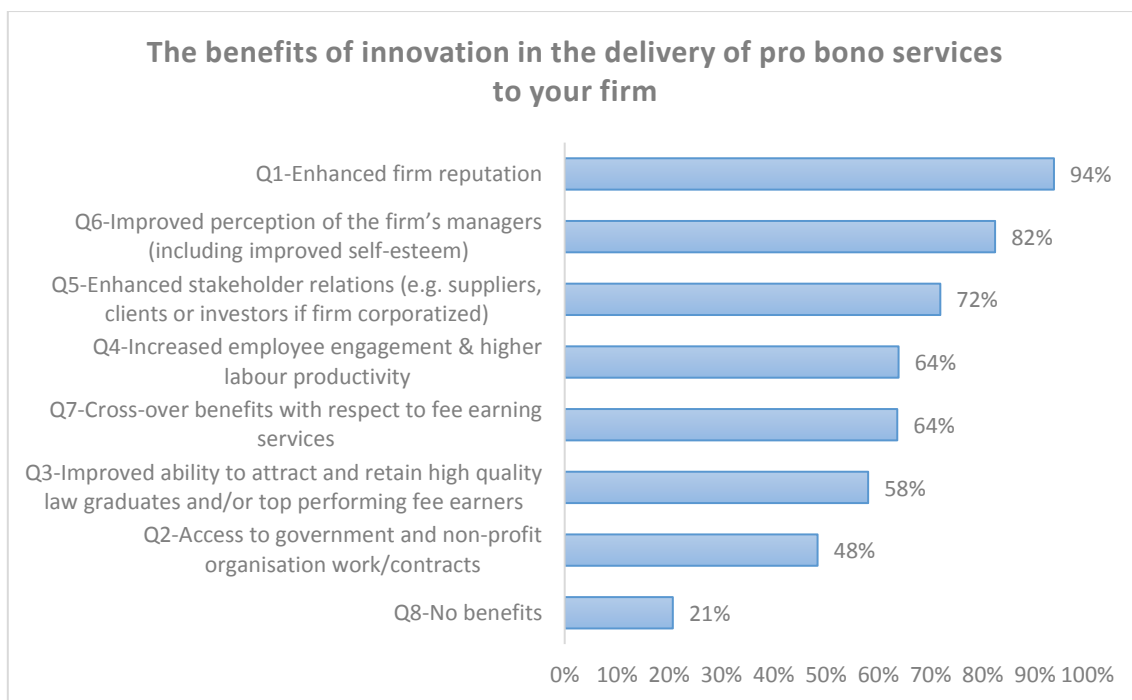
That said, when asked about pro-bono work, 39 per cent of firms reported activity in this area.



Of these firms that reported pro-bono work, 77 per cent engaged with new pro bono clinics or community legal centers involved with direct legal service delivery. Only 31 per cent used new communication channels to increase pro bono clientele.



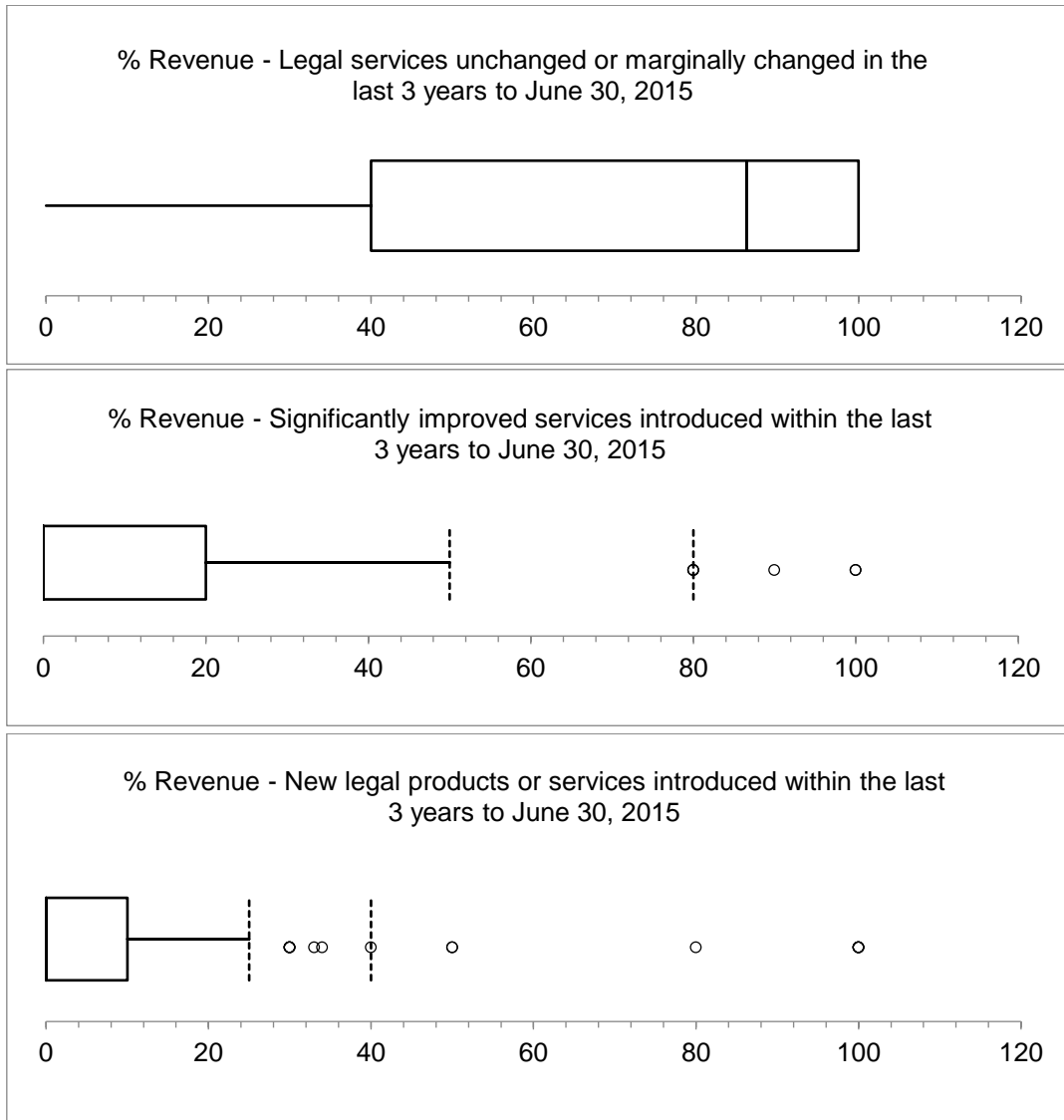
These firms reported a number of benefits when engaging in pro bono services, with 47.94 per cent reporting that they enhanced their firm's reputation, while only 21 per cent did it for no benefit.



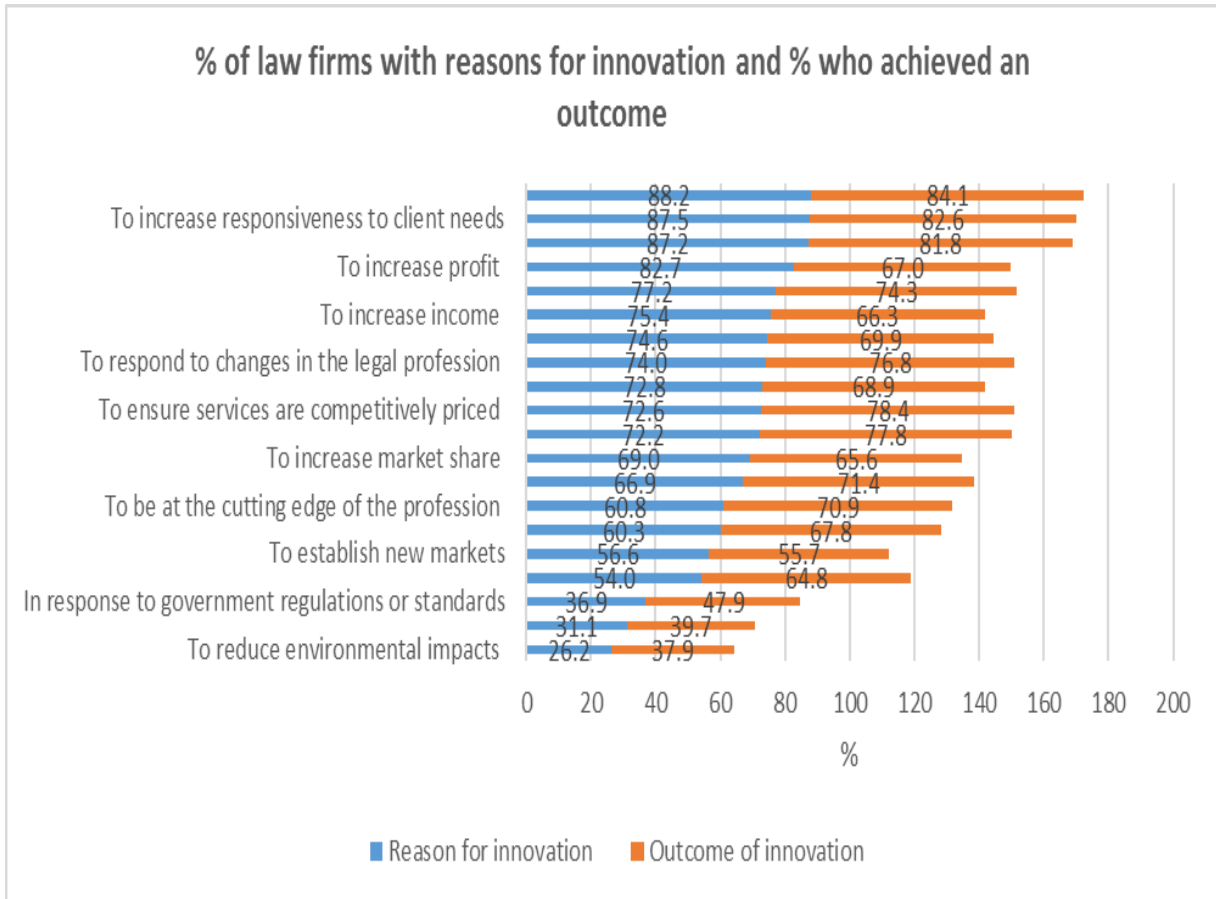
We then asked about revenue from different types of services during the last financial year.

	<i>Legal services</i>	<i>Significantly improved services</i>	<i>New legal products or services introduced</i>
# Respondents	138	138	138
mean	69.33	12.51	9.53
sample variance	1,396.66	457.45	392.52
sample standard deviation	37.37	21.39	19.81
minimum	0	0	0
maximum	100	100	100
range	100	100	100
1st quartile	40.00	0.00	0.00
median	86.25	0.00	0.00
3rd quartile	100.00	20.00	10.00
interquartile range	60.00	20.00	10.00
mode	100.00	0.00	0.00
low extremes	0	0	0
low outliers	0	0	0
high outliers	0	3	7
high extremes	0	3	7

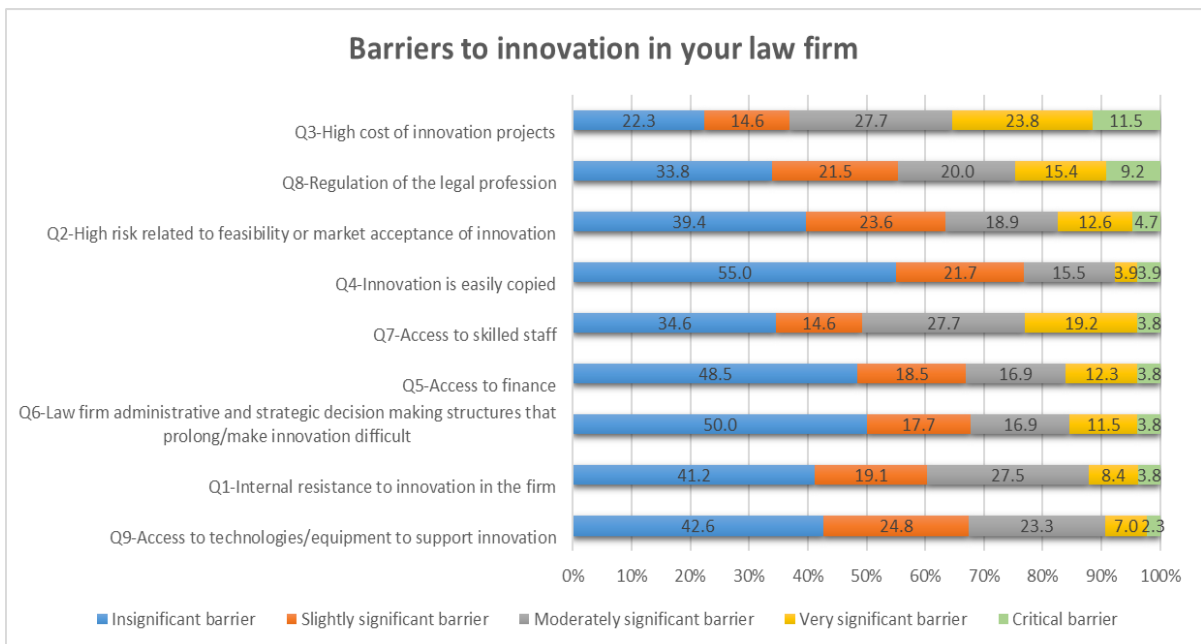
The box plots below show that between 40 and 100 per cent of the percentage revenue was distributed across legal services unchanged. Between 0 per cent and 20 per cent for legal services significantly improved and not more than 10 per cent for new services introduced. This correlates well with Question B1.



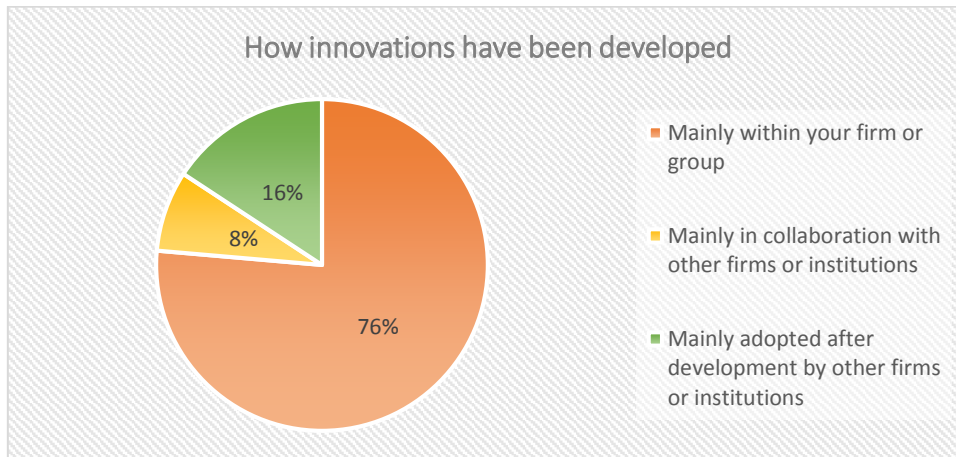
Respondents reported that the main reason for innovation was to improve quality of service. This correlates well with an open ended question on why firms would innovate. Most said that the market is competitive and to survive they had to improve their service, they had to increase responsiveness to client needs and increase efficiency of service delivery. However, while a high percentage of respondents reported that they innovated “to increase profit” (82.7 per cent), only 67 per cent achieved this.



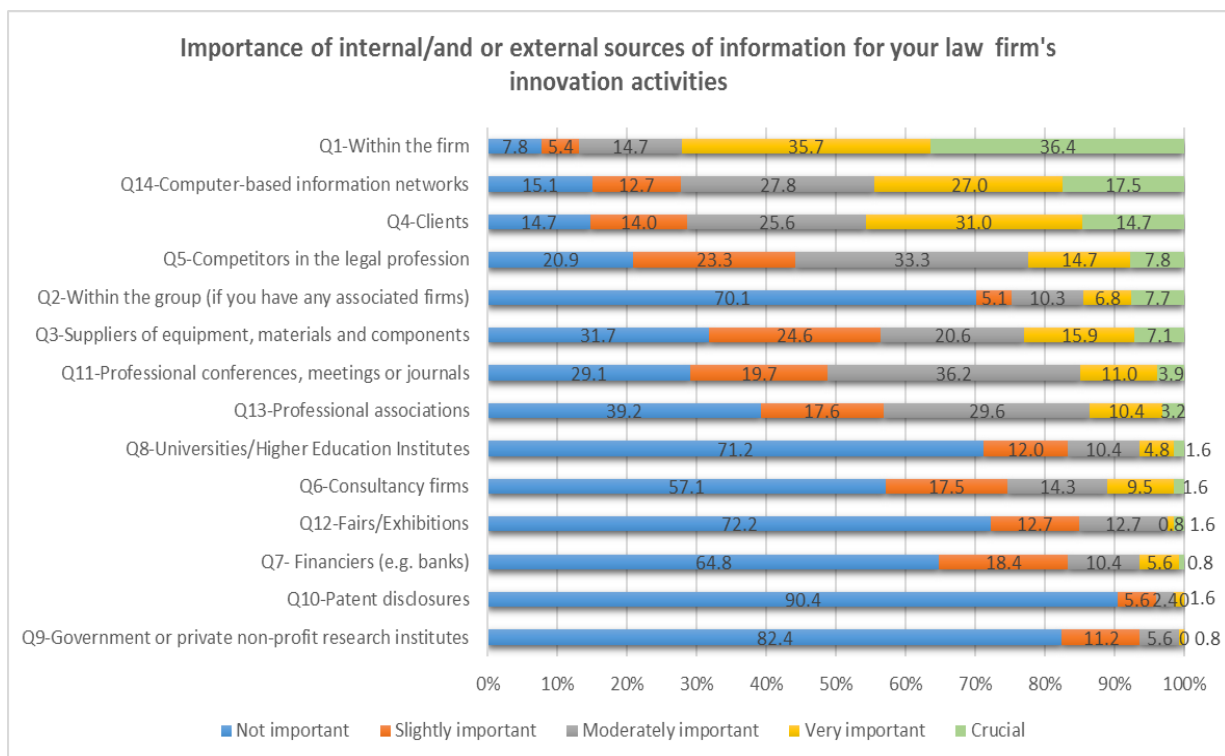
A critical barrier to innovation was the “high cost of innovation”. Access to skilled staff also seemed to be a significant indicator, while the category “innovation is easily copied” had the least significant influence.



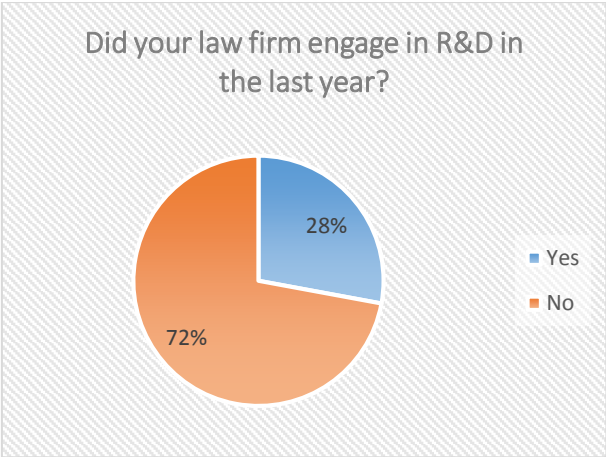
We then asked how innovation was developed and most firms reported that they innovated internally.



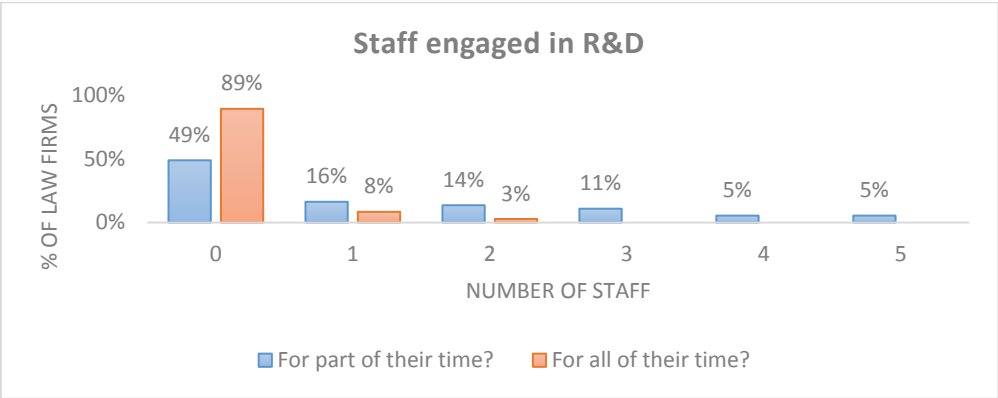
When asked about the sources of information for innovation, more than 70 per cent of firms felt the most important source of information for innovation activities was in the law firm itself. This is confirmed by information from the graph above. In addition, computer-based information networks and listening to clients also mattered. Patent disclosures were unimportant in this industry.



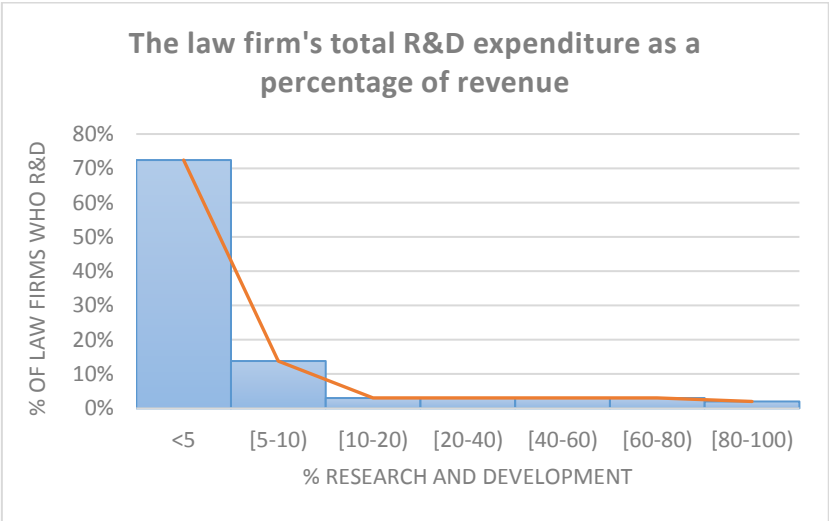
However, while firms found innovation from inside, only 28 per cent of law firms engaged in research and development (R&D) in the last financial year.



Of the firms that engaged in R&D, most did it as a part-time activity.



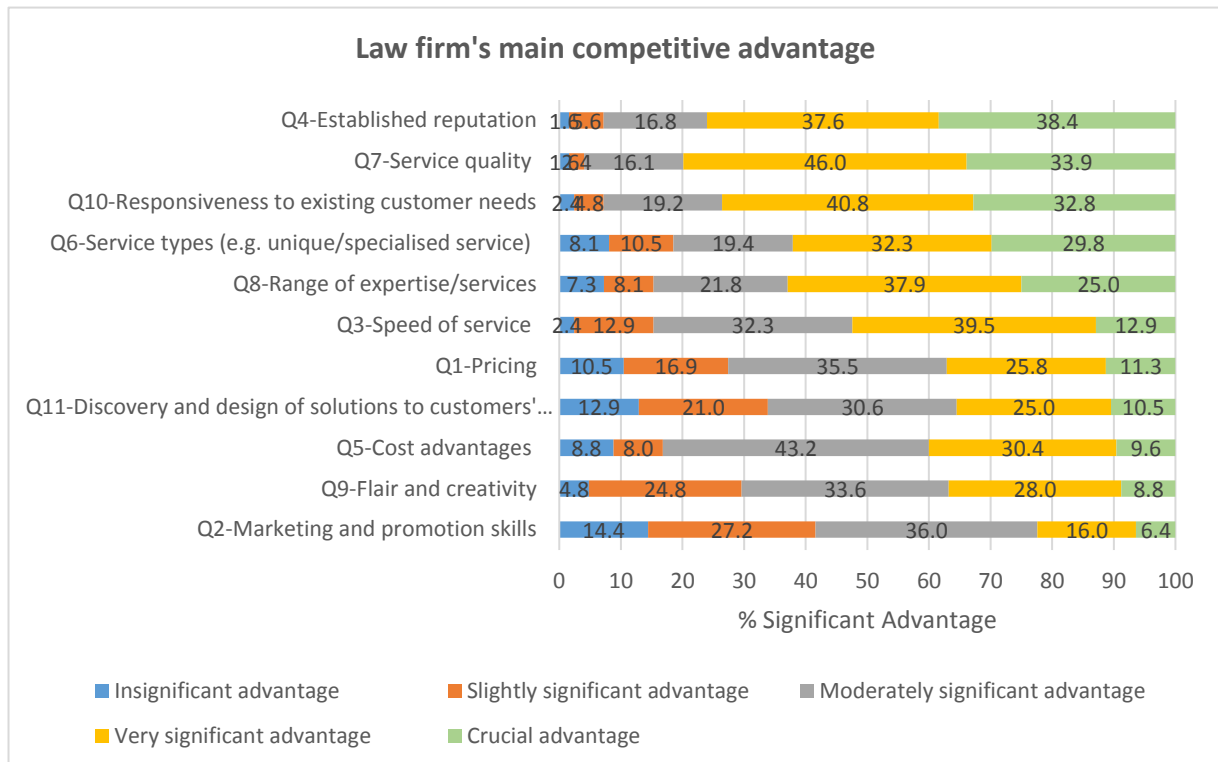
This was reflected in the percentage of turnover spent on R&D, with 70 per cent of those who engaged in it spending fewer than 5 per cent of turnover.



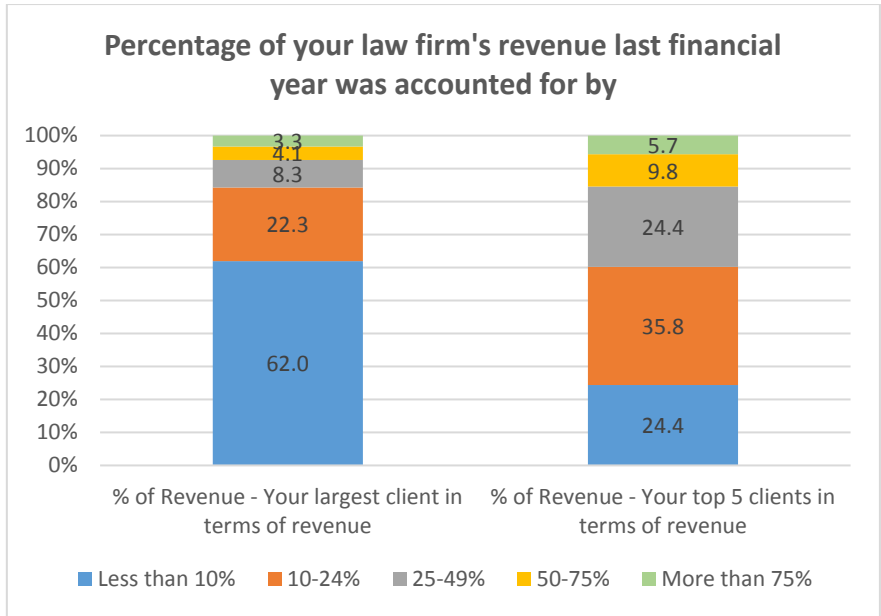
Section C

Competitive Situation and Collaborative Activity

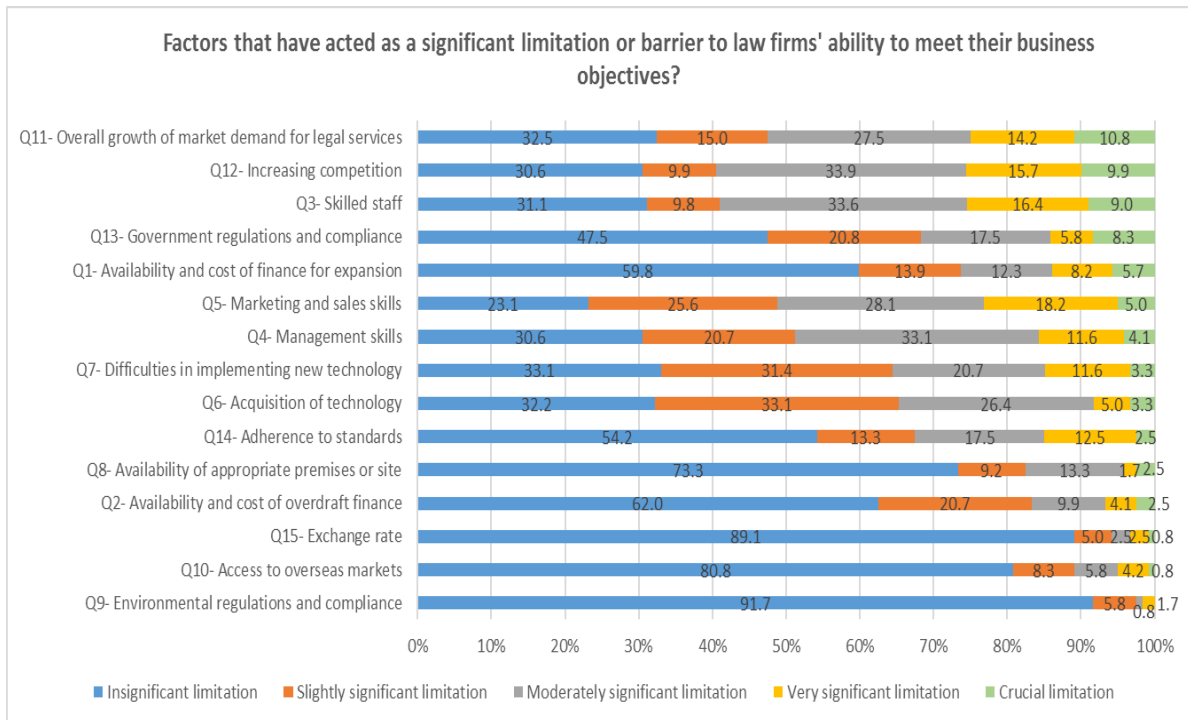
The competitive nature between law firms is epitomized by the fact that “established reputation” was the most important form of advantage, followed closely by “service quality” and “responsiveness to existing customer’ needs”. Marketing and promotion was the least favourable form of advantage, which underlines the fact that law firms prefer to build a relationship with their clients.



The first stacked graph below illustrates that 62 per cent of firms received fewer than 10 per cent of their income from their largest client. The other 90 per cent of their income was earned from their other clients. The second stacked graph illustrates that 60 per cent of the law firms received less than 24 per cent of their income from their top five clients. This represented a healthy spread in revenue.

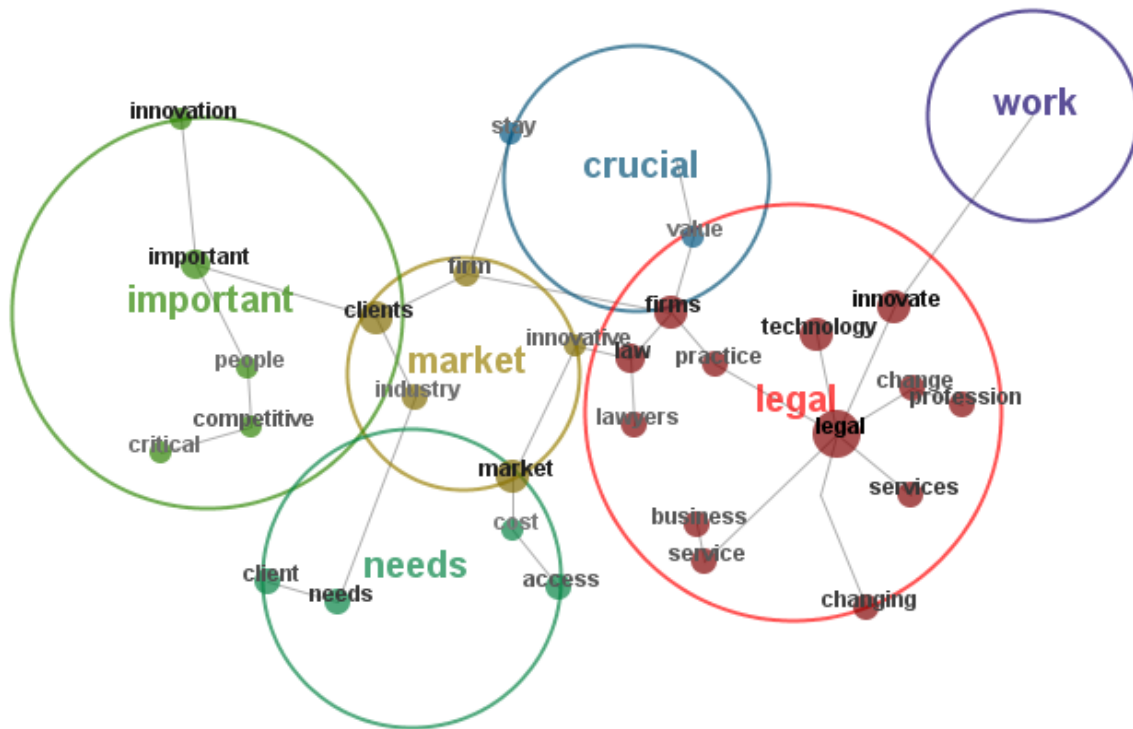


The three top crucial limitations to law firms' ability to meet business objectives were "overall growth of market demand for legal services", "increasing competition" and "skilled staff" (See B7 had skilled staff as a barrier for innovation). "Marketing and sales skills" also seemed to be an important barrier whereas "environmental regulations and compliance" were not important at all.



We asked an open ended question about law firms' perceptions of the need to innovate to address existing or potential changes in the Australian legal services market. To analyse these responses, we use software called Leximancer (www.leximancer.com) that identifies the most important themes

from data and the links between those themes. These are summarized in the concept map, produced by the software, below, with concepts highlighted in red in the text below.

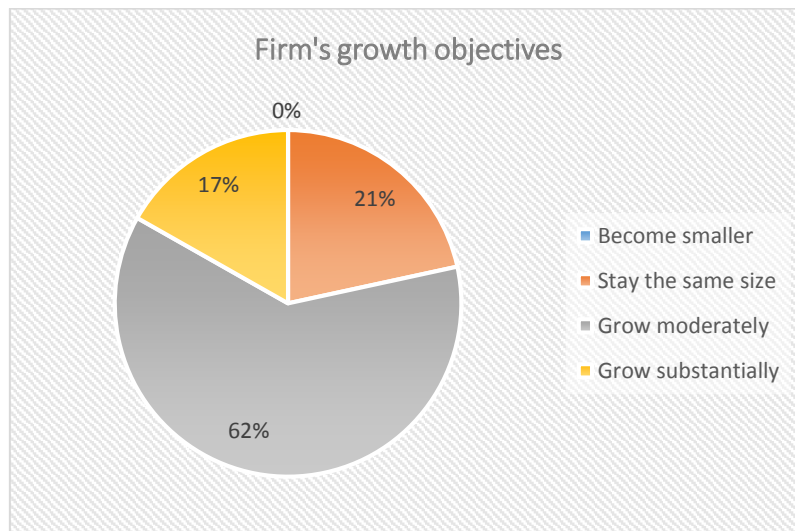


Theme	Connectivity	Relevance
legal	100%	<div style="width: 100%; height: 10px; background-color: red;"></div>
firms	57%	<div style="width: 57%; height: 10px; background-color: brown;"></div>
clients	33%	<div style="width: 33%; height: 10px; background-color: olive;"></div>
market	31%	<div style="width: 31%; height: 10px; background-color: green;"></div>
important	29%	<div style="width: 29%; height: 10px; background-color: green;"></div>
business	18%	<div style="width: 18%; height: 10px; background-color: green;"></div>
needs	17%	<div style="width: 17%; height: 10px; background-color: green;"></div>
crucial	13%	<div style="width: 13%; height: 10px; background-color: teal;"></div>
changing	08%	<div style="width: 8%; height: 10px; background-color: blue;"></div>
innovation	06%	<div style="width: 6%; height: 10px; background-color: blue;"></div>
stay	05%	<div style="width: 5%; height: 10px; background-color: blue;"></div>
work	03%	<div style="width: 3%; height: 10px; background-color: purple;"></div>

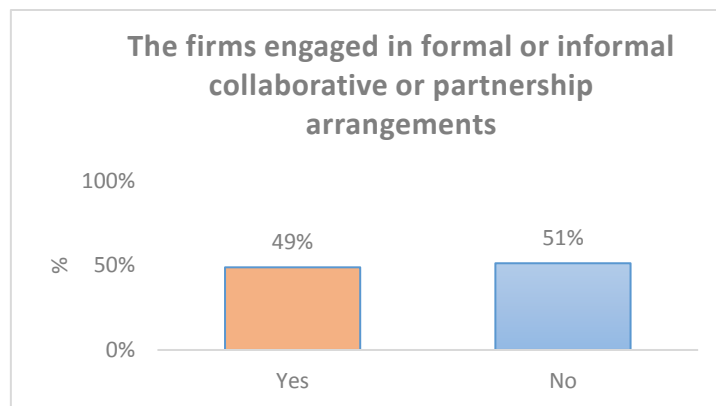
The **legal profession** and **law firms** will **need to change** dramatically over the next ten years to **survive**. Like any industry you **need** to adapt to **changing needs**. **Innovation** is **critical** to survive. It needs to be a **part** of your everyday **business**. The legal **market** is more **competitive** than it's ever been. It is **important** to meet the **client's** needs. Innovation needs to be focused on the client rather

than ideas, so what we think our client wants is **crucial**. People expect availability due to **technology** therefore law **industry** should keep up to date with **technology**, social media and networking in this area. In summary, law **practices** have to innovate as it is crucial to improve and differentiate the **service** to clients, and to improve efficiency to remain competitive.

We then asked about growth objectives over the next 3 years. While no firms planned to shrink, 62 per cent planned to grow moderately in the next 3 years.

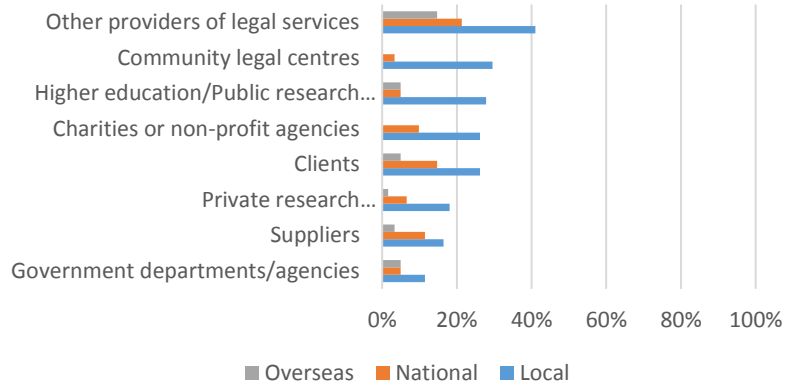


When asked about formal or informal collaborations with other firms over the last 3 years, just under half of respondents said yes.



Of the firms that did collaborate, most engaged with other local firms (41 per cent), with only a few engaging with overseas partners. The collaborations were mainly with other providers of legal services and least with government departments and/or agencies.

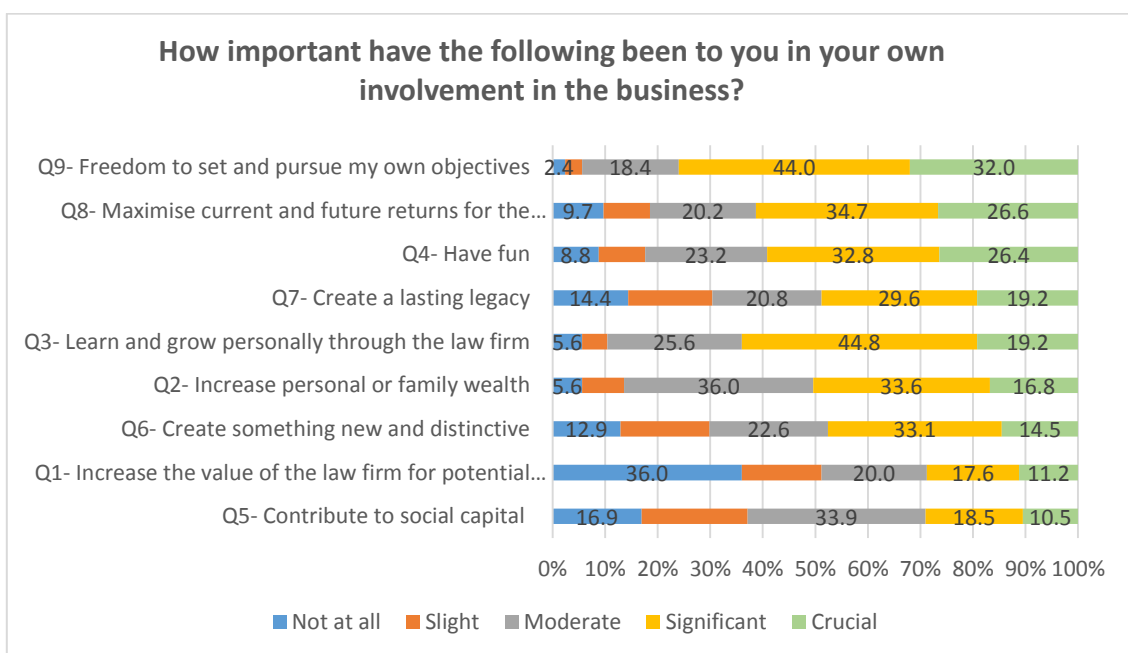
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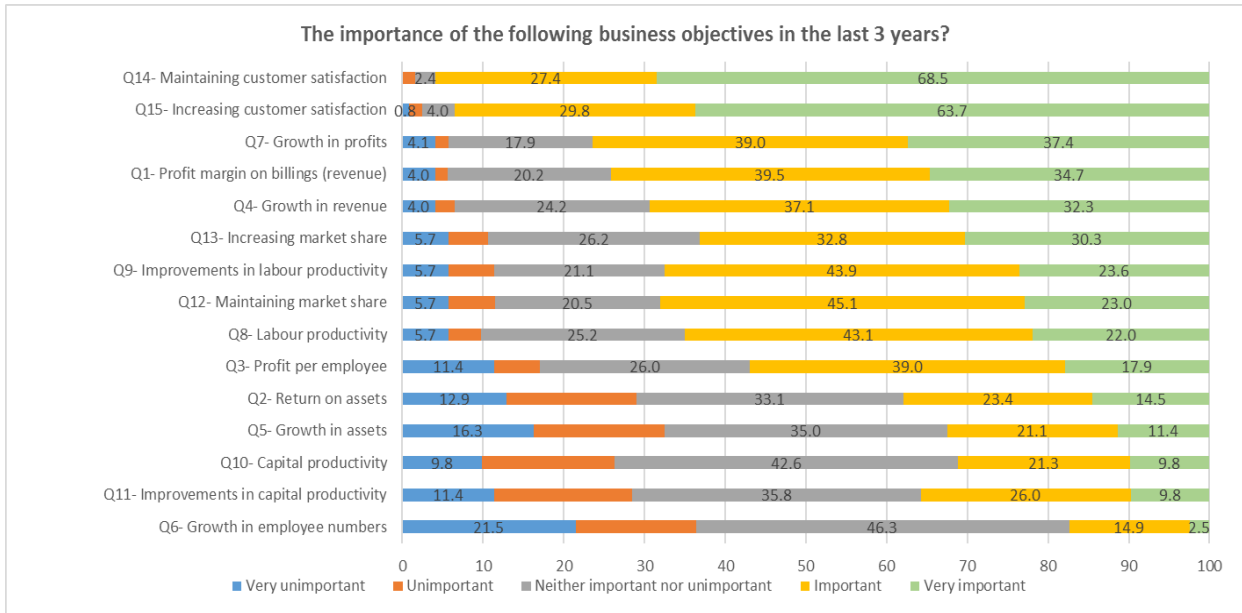
Section D

You and Your Business

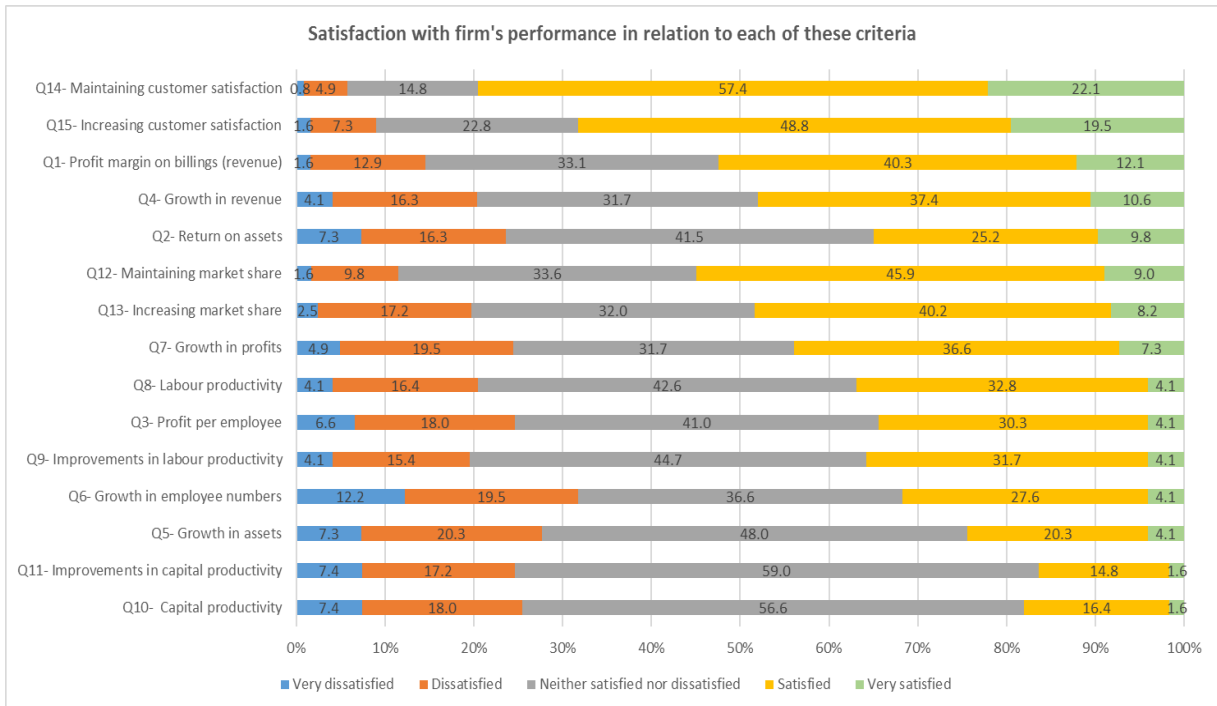
In this section we asked about the aspects of their business that respondents valued. We first asked about the importance of a range of business objectives, and found that most respondents valued the “freedom to set and pursue my own objectives” with 76 per cent indicating that it was crucial and significant. Second most important was the ability to “maximise current and future returns for the investors/partners/owners”. Most lawyers felt that to “increase the value of the law firm for potential capital gains” was of lesser importance.



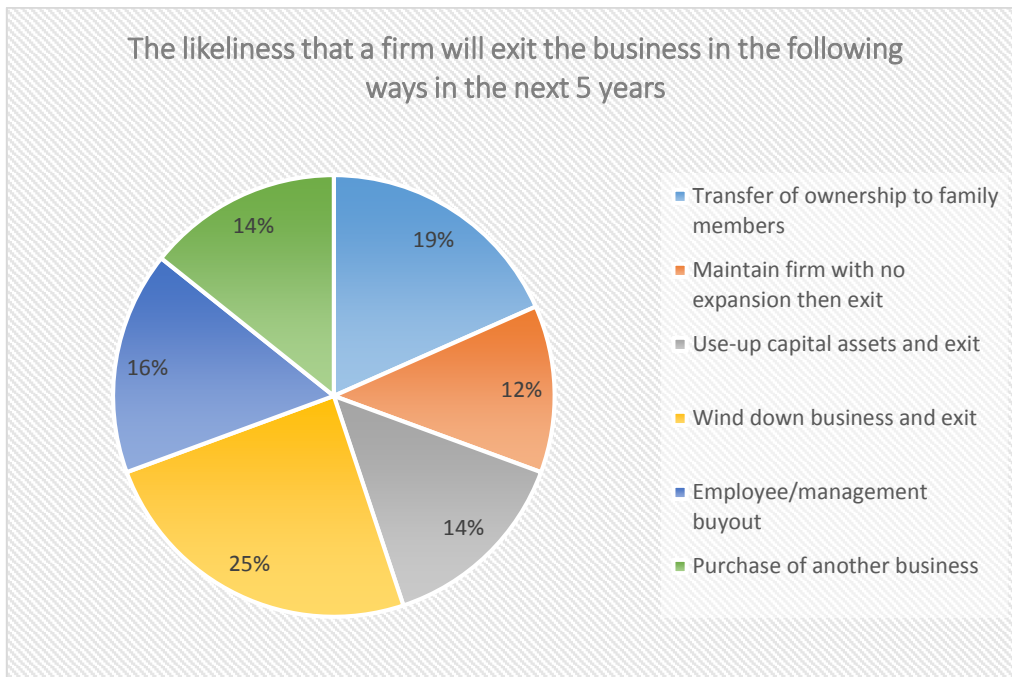
We next asked about the importance of a range of business objectives over the last 3 years. Maintaining and increasing customer satisfaction was at the top of the list followed by financial objectives such as “growth in profits”, “profit margin on billings (revenue)” and “growth in revenue”. Surprisingly, “growth in employee numbers” was the least important. This is particularly interesting seeing that “skilled staff” was seen as a significant barrier for firms to meet their business objectives.



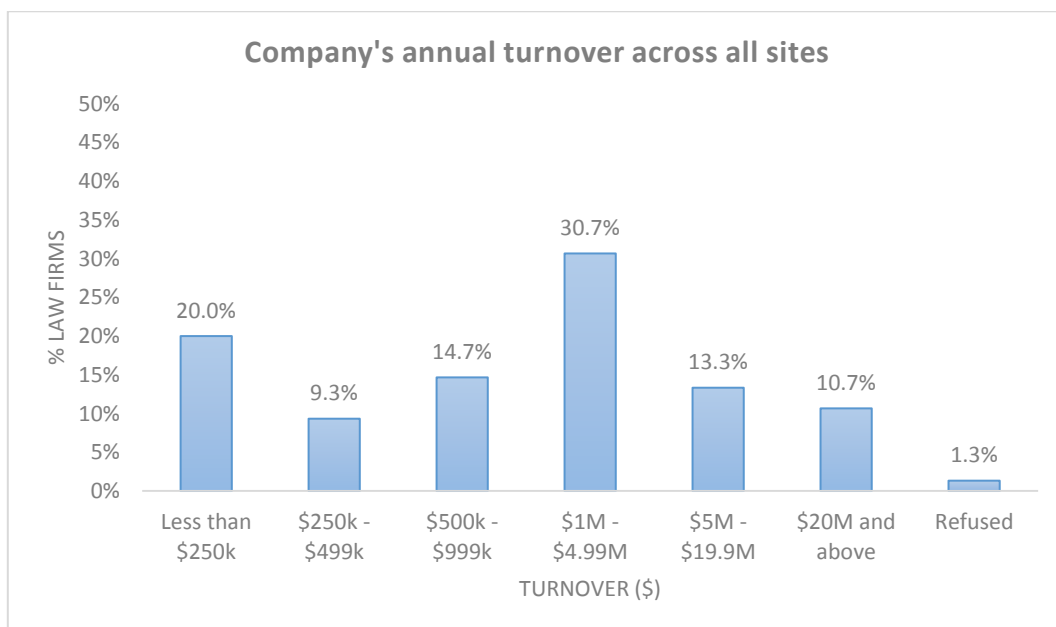
Firms were asked about their satisfaction with their performance in relation to the same criteria. We saw that, in general, firms were much less satisfied with these criteria than the importance that they attached to the same criteria. While “maintaining and increasing customer satisfaction” was once again rated as the top-most important objective for law firms, it seems as if the financial indicators such as “profit margin on billings (revenue)”, “growth in revenue” and “return on assets” scored a stronger dissatisfaction rate. “Growth in assets”, “improvements in capital productivity” and “capital productivity” rated the highest in dissatisfaction. Law firms were also the dissatisfied with “growth in employment numbers”.



Only about a third of firms responded to a question about potential exit. From the chart below it is evident that law firms are divided on this question, with 25 per cent indicating a preference to “wind down and exit the business” in the next 5 years.



About 54 per cent of the firms had an annual turnover of more than \$A one million. The older, larger firms fell into the category of \$A20 million and above.



We asked how financial indicators had changed over the last 3 years. Regarding the percentage change to *turnover*, 31.7 per cent of firms indicated they had had no growth, while 54.8 per cent had had up to 50 per cent growth. The State with the most movement was Victoria, followed by South Australia and ACT. We then asked about the change in the size of the *geographic market*, and 66.9 per cent of law firms had had no growth, with 27.6 per cent law firms with up to 50 per cent growth. 2 law firms had had more than 300 per cent growth. When asked about the change to *pre-tax profit*, South Australia showed higher losses, but also had had high pre-tax profits. ACT had recorded no losses and had had steady growth (65 per cent of ACT's firms recorded pre-tax profits). Last we asked about changes to *full time equivalent employees*, and Tasmania was the only State with no decrease in staff (0 out of 7). Western Australia led the way with a 57 per cent increase in full time employees.

