

FUTURE TRENDS IN THE BANKING INDUSTRY

Impact on Banking Practitioners

Commentary

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Rob's paper is an eloquent reminder to us all that in the old days there were only two things that were constant - death and taxes. Over the last few years we have come to realise there is a third - change.

Of course, the whole of the commercial community has had to cope with an incredible amount of change over the last few years but I suspect that for lawyers, responding to change has been somewhat more difficult because of their natural conservatism and the fact that they had been able to insulate themselves from criticism until the earlier part of this decade.

Rob's paper focuses on the changes which the banking sector seeks from its legal service provider. I want to focus on our response to that. I will confine myself to what I regard as two important issues.

First, I want to make some remarks about the importance of building a strong relationship with our client banks. At the end of the day that, so it seems to me, is the most fundamental thing of all.

Second, Rob has made observations about the increasing use by banks of in-house legal teams. I would like to say something about that.

RELATIONSHIP

I think what must be said at the outset and what Rob has not actually said in blunt terms is that across Australia the "cake" for banking lawyers (in common with other lawyers) is dramatically smaller today than it was in the late eighties.

It may well become smaller still before it grows again. As has been pointed out in the paper, a lot more effort will be put in by the banking sector to standardise its processes. That process will impact adversely on lawyers as he has said. So even if there is growth generally in banks' loan books, legal service providers may not share in that growth.

Competition between us as practitioners has been and will continue to be nothing short of fierce.

Not to put too fine a point on it, that is why at this stage of the cycle our clients have the upper hand. I have said before that in my respectful opinion the commercial community generally and in the context of this morning's discussion the banking sector, has never had it so good. The price paid for legal services across the whole of the business sector is historically lower than it has ever been and the effort put in by the legal community in terms of the quality of that service is extraordinarily high. It does not follow of course that the **quality** is high. But the effort certainly is.

From the perspective of our clients in the financial sector, it means that there is a wide choice available for a high quality product at a low cost.

I have a very strong view that if we are to insulate ourselves from the consequences of our traditional clients in the banking sector being tempted by the cheap prices offered by others, we must focus on building and maintaining a strong and enduring relationship with the institution and the people who work in it.

That is difficult today not only because of the competition but because the restructuring of banks is constantly changing the faces of those with whom we are endeavouring to building our relationships.

I am sure you are all too keenly aware of the problem. But if you do not persevere, I assure you one of your competitors will.

Building a strong relationship with our clients is necessary to achieve at least two things:

- The first is to build confidence in the legal product being supplied. Confidence is largely built on perceptions. If our clients have a perception that we are interested in their business, that we really care whether they are satisfied with what we do for them, that they believe they get value for their money and that we are interested in the outcome - we stand a good chance of holding the work against our competition.
- The second thing a strong relationship will achieve is that it will solve any problems which arise which might otherwise damage the practice. I am not here talking about damage control when things get out of hand. I am talking about solving problems before it is necessary to resort to damage control.

Another response which, in my view, the lawyer ought not overlook is reciprocity. In his paper, Rob has made a particular point that:

"Reciprocity suppliers will be a thing of the past - no longer will banks 'give' some legal work to a law firm as quid pro quo for its banking business, particularly its trust account."

I agree with him that the coarse offer to exchange a trust account for a promise of legal work is not likely to win a client for the lawyer of the nineties.

But I do not think that that denies the proposition that lawyers who currently provide legal services to banks ought not overlook the fact that referral of business is a practical way to signal to a bank that you appreciate a relationship is a two way street: that you are not only interested in the next instruction - you are also interested in supporting your client's business objectives.

There are obviously other ways in which one can give overt support to one's client bank in the context of building a strong relationship. The investment of client's funds is an obvious example.

Whilst I agree with Rob's proposition that "buying" work from a bank in exchange for the promise of favours will not characterise the 1990s and beyond, my experience suggests that banks are and will remain responsive to commercial support where we lawyers can provide it.

One of the problems of the nineties and beyond is what I call the "taxi driver phenomenon". Taxi drivers claim they now drive 20% longer hours for the same money.

But lawyers cannot simply drive for longer. Most of us are working to our limit already. How are we to maintain our incomes when hourly rates and aggregate fees are significantly reduced? I only know of one way and that is leverage. So the response is to manage our practices differently. The trick is to have the work undertaken at the right level (a lot of partners did work in the past that did not justify a partner's rate) yet maintain delivery of a quality product.

And the final point I want to make is obvious enough I suppose. The most successful banking lawyers of the future will be those who get the relationship right and who deliver a top quality legal product. Put those two together, and you have the ingredients for a successful response to this era of change with which we are confronted.

INTERNAL LAWYERS

Rob sees a future in which lawyers in the private profession will be marginalised in respect of a lot of work now offered to them.

He sees an increasing trend towards the use of internal legal teams undertaking certain categories of work, and non-lawyers operating within an interactive computer environment for other work.

He also sees a future in which there will be increasing supervision of external lawyers work by internal legal personnel.

I agree with him.

Even a bank as small as the Bank of Queensland Limited with assets of just over \$2B employs two lawyers, one on the operational side and one on the corporate side. Only significant and difficult matters are briefed to the bank's external lawyers - usually "one off" transactional matters requiring expertise not available to the bank through its internal system.

For us in the private profession, to challenge the wisdom of this move towards the increasing use of internal lawyers is arrogant and not particularly helpful.

What might be helpful is to focus on some aspects of the role of the internal and external lawyers, their relationship with each other and some strengths and weaknesses of each.

1. Commerciality

Rob has reported complaints about the lack of commerciality on the part of some external lawyers. Whilst it is true that many lawyers in private practice lack the experience of working within the four corners of a commercial organisation, I am personally not convinced that generically the internal lawyer is more commercial than his counter-part in the private profession. Nor am I convinced that working within a commercial organisation necessarily enables him or her to acquire that attribute to a greater degree than his or her counter-part in the private profession.

My observation is that lawyers in private practice have had to learn this lesson the hard way and that those who succeed have a high degree of recognition that a commercial approach to legal problem solving is a given if the client base is to be maintained.

2. Objectivity

It has often been said that an internal lawyer is too close to management and that over time he will lose independence and objectivity. I have noticed an increasing trend towards the creation of separate legal "firms" within the corporate structure. The rationale for this is probably to preserve legal professional privilege. But a consequence is that it tends to create a relationship between line management and the in-house legal team which is something akin to the relationship between the organisation and its external lawyers. It enables the internal lawyer to "keep his distance" as it

were from management. Nonetheless, it must be recognised, I think, that internal lawyers are more likely than private lawyers to lose objectivity. That is an advantage which those of us in the private profession should not lose sight of.

3. Skillbase

The internal lawyer was once regarded as a second class member of the profession. The perception and the reality are now well and truly outdated. In general, private practitioners have a healthy respect for the professional skill base of their internal colleagues. Nonetheless, I believe that the internal lawyer suffers a disadvantage in terms of the development of generalised legal skills in that he is denied the interaction with colleagues in a large legal office where partners are engaged in complex legal work across a range of specialties. That environment tends to keep each lawyer up-to-date with leading edge developments in the law and generally up-to-date with what, in commercial terms, the clients of the firm are doing.

4. Cost

Rob has made reference to the perception amongst some line managers and internal lawyers that it is more cost effective to employ a lawyer internally than to brief out. That generalisation does not stand scrutiny. The flaw is that apples are not being compared with apples.

The first point I want to make is that the commercial community generally insists upon its legal service providers bringing to bear on its problems leading edge professional expertise. That does not come without cost. The infrastructure costs of a large law office including the cost of sophisticated computer systems, the maintenance of skill levels by rigorous training and continuous legal education, and the labour intensive nature of legal work are enormous. For good reason, internal legal teams do not generally need and in any event do not have the same level of investment in such facilities. It should not be overlooked that large law firms only exist because large corporations need that level of service.

It is not surprising therefore that a person in such a firm will command an hourly rate well in excess of his counterpart of similar experience working in an internal legal environment. But that does not mean that the aggregate fee (cost to the client) will be greater. It never ceases to amaze me that we in the private profession seem unable to persuade perceptive commercial clients including banks that they are more likely to contain the aggregate fee if they deal with a recognised expert or, in the case of transactional work, they out-source to a highly experienced team of lawyers who are not reinventing the wheel.

It is not only the fact that the job is done more economically notwithstanding the hourly rate differential: the **quality** of the product is likely to be higher which means that the client can have much more confidence in the outcome.

I think the cynicism with which the commercial community meets that argument is to some extent a product of the indulgent manner in which we behaved during the buoyant 1980s. We largely squandered the opportunity to build trust into discussions about fees. We behaved as if all we were interested in was a fat premium bill. The fact that premium billing is largely a thing of the past underpins a remark I made earlier - that in the last few years our banking clients have never had it so good. In the present environment I argue that the value of expertise and experience to a bank in the context of difficult advisory or transactional work, including litigation, will almost always justify the out-sourcing of the work at a necessarily higher hourly rate.

5. Efficiency

Prima facie communications between an external legal service provider and internal lawyer whose task is very largely to "manage" the transaction will be easier than communication with non-lawyers at line management level. There are inherent efficiencies involved here. First, the external

lawyer can “talk in shorthand”, leaving it to the internal lawyer to explain things to management. Second, a “sign off” by an internal lawyer of the appropriateness of advice provided by the external lawyer contributes to the confidence of management in the advice. Third, the interpretation of an internal lawyer sometimes enables a client to avoid mis-instructing the external lawyer because the internal lawyer has a greater ability to identify the relevant and discount the irrelevant.

CONCLUSION

I congratulate Rob on a perceptive analysis of the issues that confront us in the decade ahead. I have restricted myself to comments upon two of the issues which seem to me to be important. There is no doubt that in an environment of fierce competition, diminishing work available to the profession and an ever increasing population of lawyers, the good times are probably gone for the foreseeable future. But there will always be work available to the private profession which can return a reasonable profit if managed correctly. That is the real challenge for us. Those who succeed in meeting it will, in my view, be those who focus on delivering a product perceived by the client to be of value to it in the context of a strong solicitor and client relationship. Lawyers who continue to disregard that injunction are the lawyers who are likely to be marginalised.