



## SHOVELING SMOKE: BETTER GOVERNANCE—DITCH THE LEGAL BUDGET?



**Ronald F. Pol** is president of the **Corporate Lawyers' Association of New Zealand (CLANZ)**.

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*In this column on professional issues, legal department management and relations between in-house and outside counsel, Mr. Pol discusses elements of managing lawyers, sometimes likened to herding wild cats, or as he prefers, shoveling smoke. Here he applies a provocative view on one of the most time-consuming processes employed by legal departments in managing outside counsel, and themselves—budgets.*

The most pressing issues facing legal departments today? No surprises here. An in-house counsel survey<sup>1</sup> confirmed the two top issues as “reducing outside counsel expenses” and “too much work for too little resources/legal budget.”

So, how do most legal departments traditionally address these issues? Ironically perhaps, and pretty much the same way most corporations do, with ever-increasing budget pressure.

But do budgets really help reduce outside counsel expenses? Or reduce the ratio of time spent on administrative rather than strategic tasks?

The pressure to meet budget is often intense—bonuses and even jobs sometimes depend on it. Yet some of the activities they promote can be counter-productive. For example, if you're running over budget a

few months out from year-end, you might freeze some new instructions to outside counsel or slow the discovery process in major litigation. What's the harm? Sometimes, the ‘catch-up’ might prove more expensive overall, not just in monetary terms, but also in the less effective management of legal issues.

Some managers are beginning to realize that it's not just what they spend that's causing problems, but the annual budget round itself—and its behavioural and governance impact.

A new paradigm has recently been proposed<sup>2</sup>—for more effective use of sophisticated, yet simpler and more pragmatically focused, technology tools, and for improved customer focus and better governance.

Jeremy Hope and Robin Fraser advocate abandoning the annual budget process as currently practiced. They suggest replacing it with a series of rolling forecasts. These might still look 12 or 18 months out, but can be updated regularly—with ‘always on’ technology tools enabling managers more quickly to collect, analyze, and share financial information across key stakeholders within the organization.

The problem they suggest is not so much budgets themselves—they still offer a valuable forecasting tool—but the link between the budget process and performance targets. The authors advocate abandoning fixed performance, budget-based targets,

in favor of relative incentives based on factors genuinely connected to organizational strategy, such as profit ratios, performance relative to competitors, and customer profitability.



Another problem is that the budgeting process takes so long (often many months) that by the time the year begins, the entire basis on which the budget was created may have changed. Moreover, the information is seldom aligned with strategy: Budgets focus on internal divisions such as departments, functions and products, whereas strategy focuses on meeting customer needs.

The authors quote studies<sup>3</sup> indicating that up to 90% of managers think the traditional budgeting process takes too long and adds little value, with 85% finding they don't focus enough on key strategic issues. From a direct governance perspective, 75% think that traditional budgets cause dysfunctional and sometimes even unethical behaviour.

At its core, abandoning fixed budgets and decision-making based on arbitrarily imposed internal targets is

about realigning decision-making towards customers' dynamically changing needs.

The outcome for legal departments may be for lawyers to focus directly on the central purpose of their role—to meet ‘customer’ needs profitably, and work more collaboratively with key corporate service functions and business unit managers to meet organizational goals.

Put another way, it's about whether you ask where you are against budget, or whether you ask if you are delivering better client service at less cost than your competitors. In short, are you managing the department's numbers, or are you managing the organization's legal business?

*Ronald F. Pol is President of the Corporate Lawyers' Association of New Zealand, general counsel of a start-up software company, member of the governing Council of New Zealand's Law Society, director of a company connecting strategy with key motivating factors of people, and sometime adviser on improved connections between inside and outside counsel. He is available at rfp@xtra.co.nz.*

### NOTES

1. *Serengeti-ACC Managing Outside Counsel Survey 2005.*
2. BEYOND BUDGETING: HOW MANAGERS CAN BREAK FREE FROM THE ANNUAL PERFORMANCE TRAP, JH Hope & JRT Fraser, (Harvard Business School Press 2003).
3. Surveys quoted at the *Beyond Budgeting Round Table* website: [www.bbrrt.org](http://www.bbrrt.org).