NERA

Economic Consulting

“2002: Steady State”

2001 NERA Legal Leading Indicators Survey

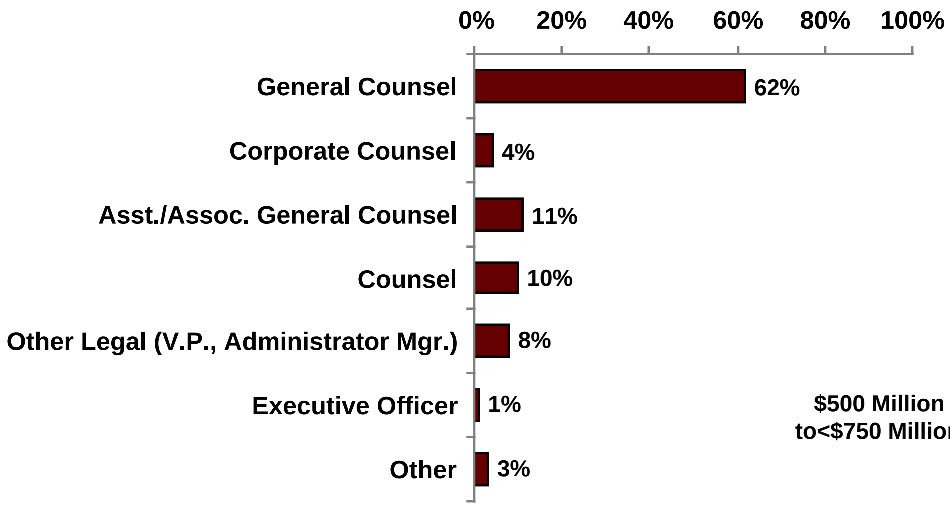
Summary Report

Marsh & McLennan Companies

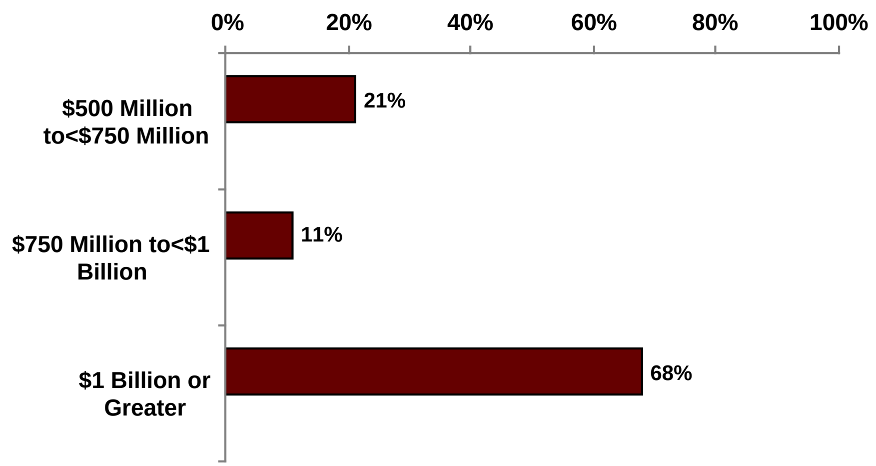
Responses Reflect The Expectation Of Chief Counsel For North America's Leading Corporations

- **68% of respondents represent firms with $1 billion or greater in annual revenues.**
- **62% of respondents identified themselves as their organization's chief counsel.**

Survey Respondent Profile



Annual Revenues of Respondent Companies



Growth In Legal Spending To Flatten In 2002

- **We saw 3% growth in legal spending from 2000 to 2001.**
  - More firms report growth (48%) than decreases (18%).
  - Increases were larger on average (28%) than decreases (17%).

- **Respondents see no growth in legal expenditures from 2001-2002.**
  - Almost equal numbers of firms expect increases (30%) and decreases (25%).
  - Average expected changes are about the same for increases (15%) and decreases (16%).

Total Legal Spending 2000-2002 As a Proportion of Reported 2001 Spending

NOTE: Calculated based on year-to-year growth.

Outside Counsel Expenditures Expected to Slip -- But Not Drastically -- in 2002

- **38% of respondents expect to decrease spending on outside counsel in 2002.**
  - An equal number (38%) expect to hold the line on spending in 2002.

- **Growth in 2001 came from maintaining the share of the budget while total legal budgets grew. In other words, the pie may have become larger, but the percentages of spending remained constant.**

- **Despite no growth in 2002, spending on outside counsel is still equal to levels in 2000.**

Outside Counsel Spending as Percent of Total 2001 Legal Spending

	2000	2001	2002
Total Legal Spending Index	97%	100%	100.4%
Outside Counsel Share of Budget	54.0%	53.5%	51.4%
Outside Counsel % of 2001 Total Spending	52.4%	53.5%	51.6%

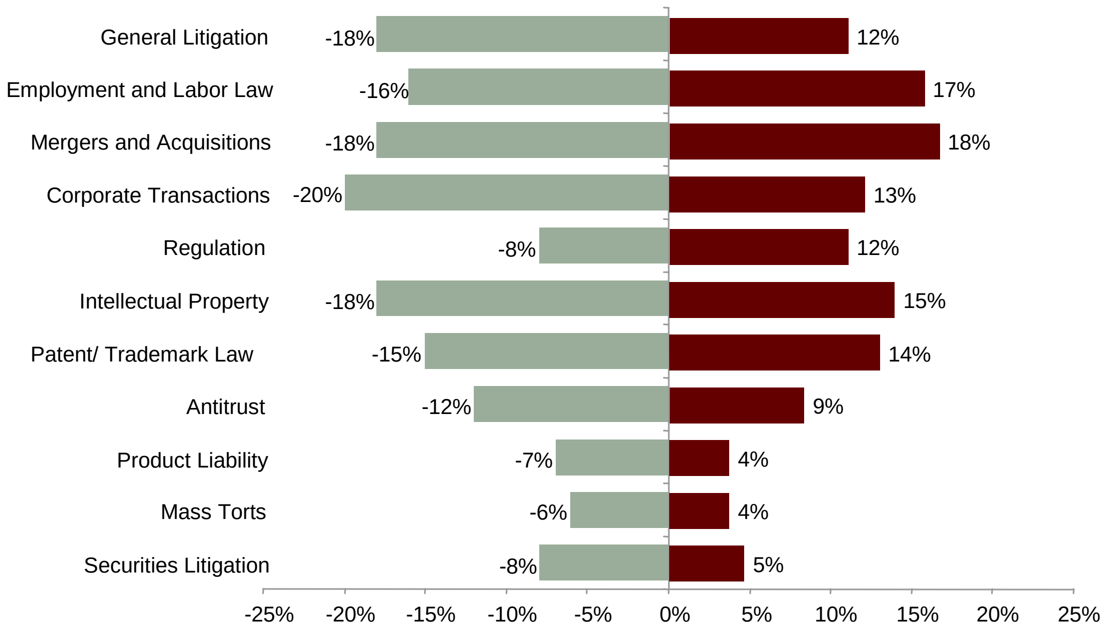
Firms Expect To Make Less Use Of Outside Counsel In Most Practice Areas Next Year

- **The only practice area with a notable expected increase in the use of outside counsel is Regulation, with 12% expecting an increase compared to 8% expecting a decrease (net difference of 4%).**

- **The broadest decline in spending appears concentrated in those areas most impacted by a decline in deal making: Corporate Transactions with a net difference of -7%, and General Litigation with a net difference of -6%.**

Average % of Legal $$ Spent on OC by Area
25%
16%
11%
11%
9%
8%
7%
4%
3%
3%
2%

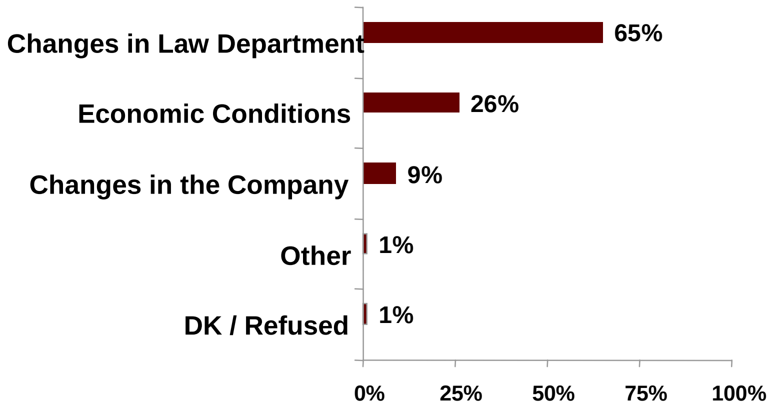
Percent of Firms Reporting Increases & Decreases in Spending on Outside Counsel



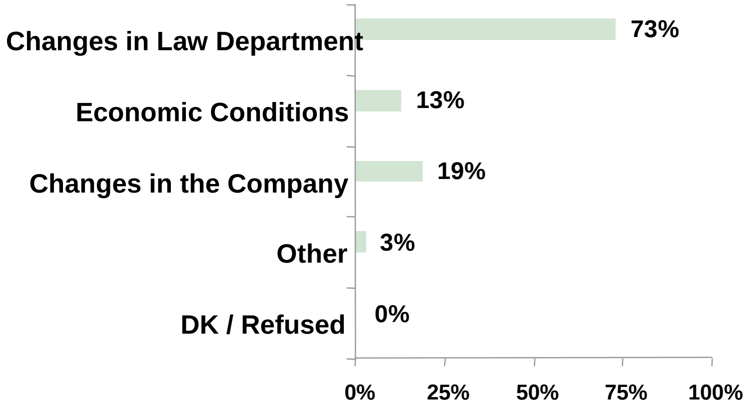
Internal Budget Constraints Drive Decreased Use Of Outside Counsel While Economic Conditions Are More Important To Those Expecting Increases

- **61% of all firms expect changes in spending on outside counsel six to twelve months from now when compared to spending in 2001.**
  - 38% report expected decreases six to twelve months from now.
  - 23% report expected increases six to twelve months from now.
- **Both groups tend to focus first on the corporate legal group itself.**
  - Those expecting decreases tend to mention both the conclusion of specific cases and to an effort to bring work in-house in part to reduce fees.
  - There are also specific mentions of “litigation avoidance” to reduce the need for outside counsel.
- **Change in the company is a more important factor in explaining declines, especially budget constraints that account for half these answers.**
- **Among those expecting increases, economic conditions are a positive force, with most of these reporting a growth in business for their firms.**

Reported Reasons for INCREASES in Outside Counsel Spending 2001-2002



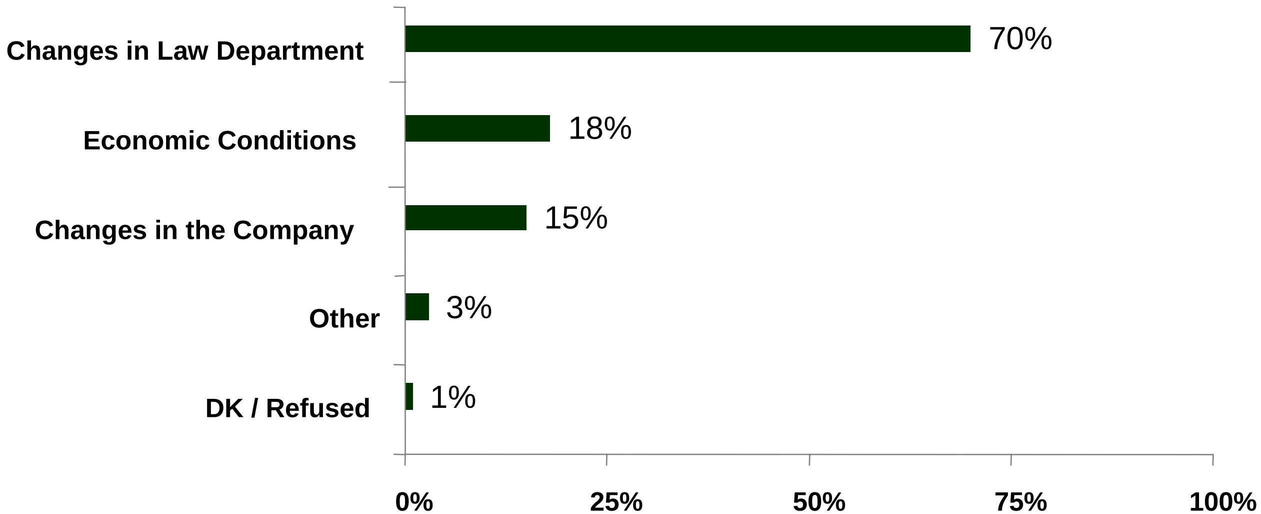
Reported Reasons for DECREASES in Outside Counsel Spending 2001-2002



Expected Change In Outside Counsel Spending Stem From Internal Developments

- **General Counsel give the most weight to factors within the law department, more than either economic changes or changes in the company as a whole.**
- **The largest change expected within the law department is "changes in workload", with one-third of those expecting any change to say it will be a result of workload changes (37%) and then staffing changes (23%).**
- **Both are the internal changes a result of macro-forces – the law department's contribution to cost cutting?**

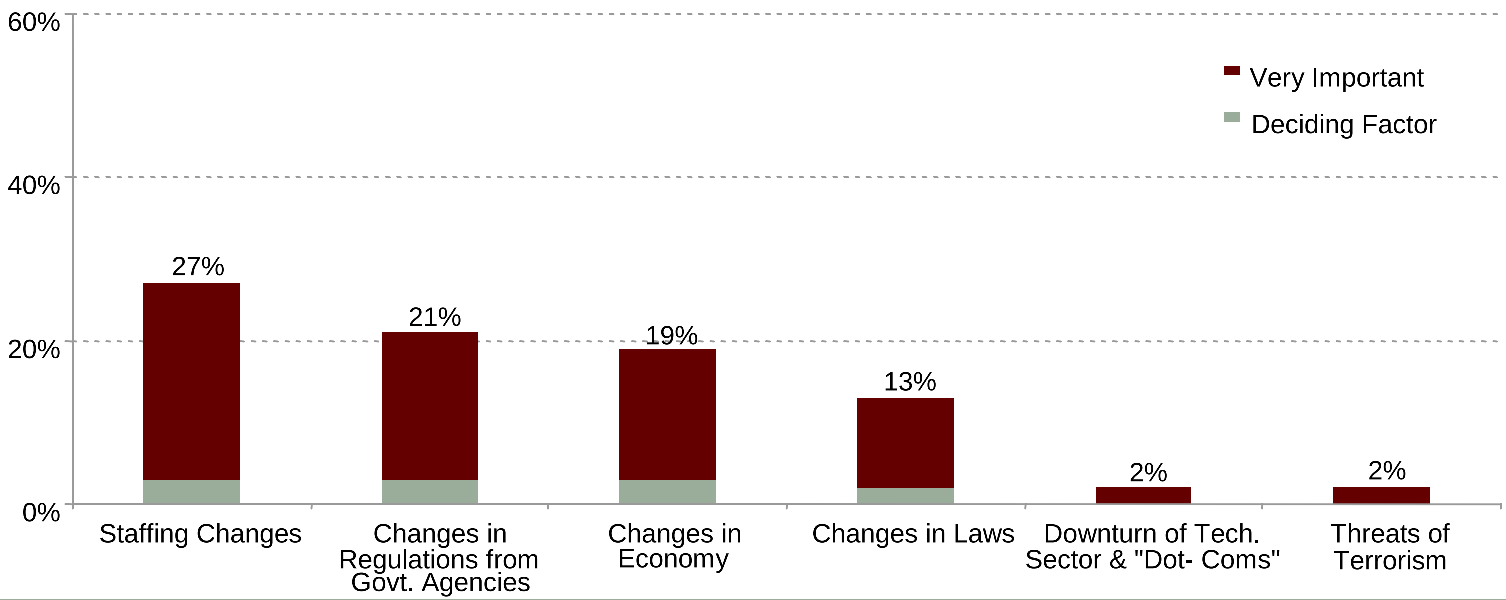
Reported Reasons for Change in Outside Counsel Spending for 2001-2002)



Companies Are Most Likely to Rate Internal Factors As Key To Their Use Of Outside Counsel Next Year

- **Staffing changes were rated as having the most impact on plans for use of outside counsel next year.**
- **When asked directly about its effect on their use of outside counsel, General Counsel rate the impact of the economy as less important than staffing changes and about the same as the impact of changes in government regulations.**
- **Only 2% of firms say that the downturn of the technology sector and the "dot-coms" or continuing threats of terrorism are important to their expected spending on outside counsel next year.**
- **Law department focus tends to be much more case oriented (e.g. what's in the pipeline) than product, market and/or industry focused (e.g. what is happening to my company).**

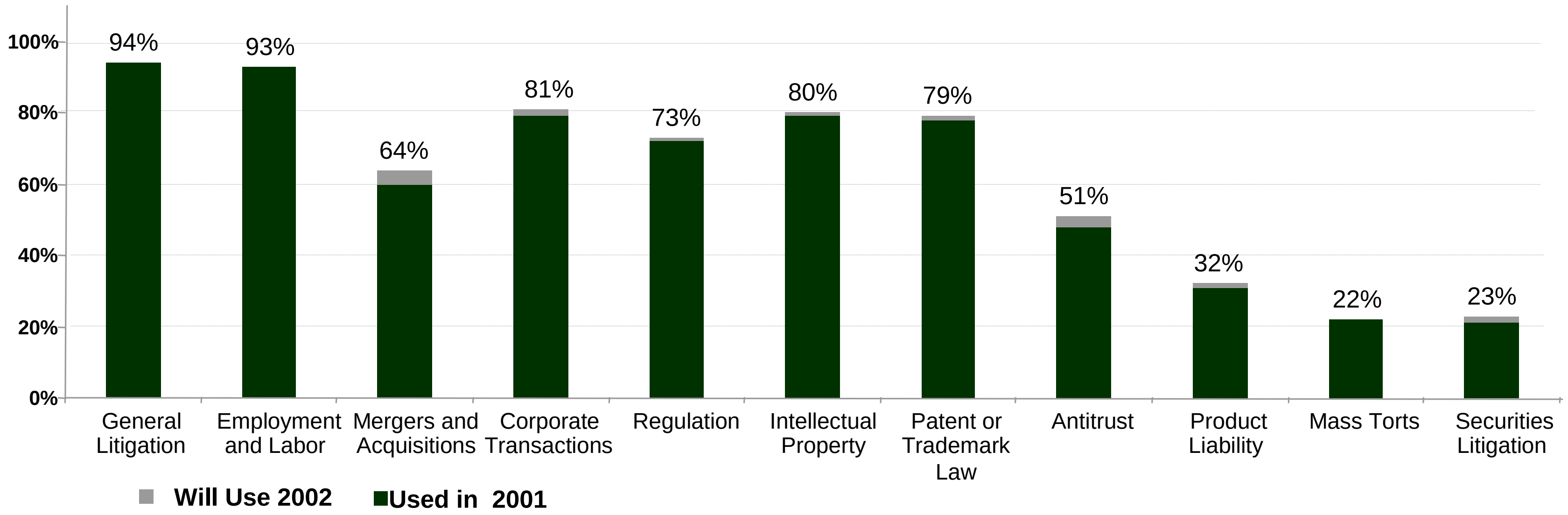
Importance of Factors in Changes of Use of Outside Counsel in Six to Twelve Months



Use Of Counsel Expected To Increase In The Areas of Mergers And Antitrust

- **Use of outside counsel in Antitrust and in Mergers is expected to rise in 2002.**
- **More firms also report using outside counsel for Employment and Labor Law than for any other single specialty practice area in 2001. Does this reflect the growing pattern of disputes over wage and age discrimination?**

Percentage of Surveyed Firms Using Outside Counsel in 2001 or 2002 By Practice Area

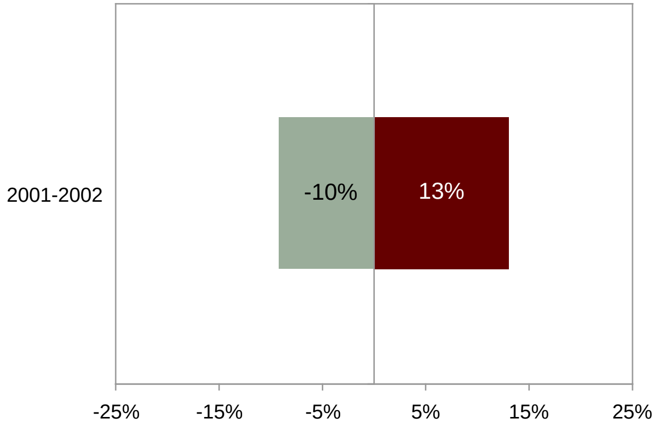


NOTE: Practice areas ordered by average spending on outside counsel.General Litigation represents a collection of practices including bankruptcy, fraudalent conveyance, contract disputes, etc.

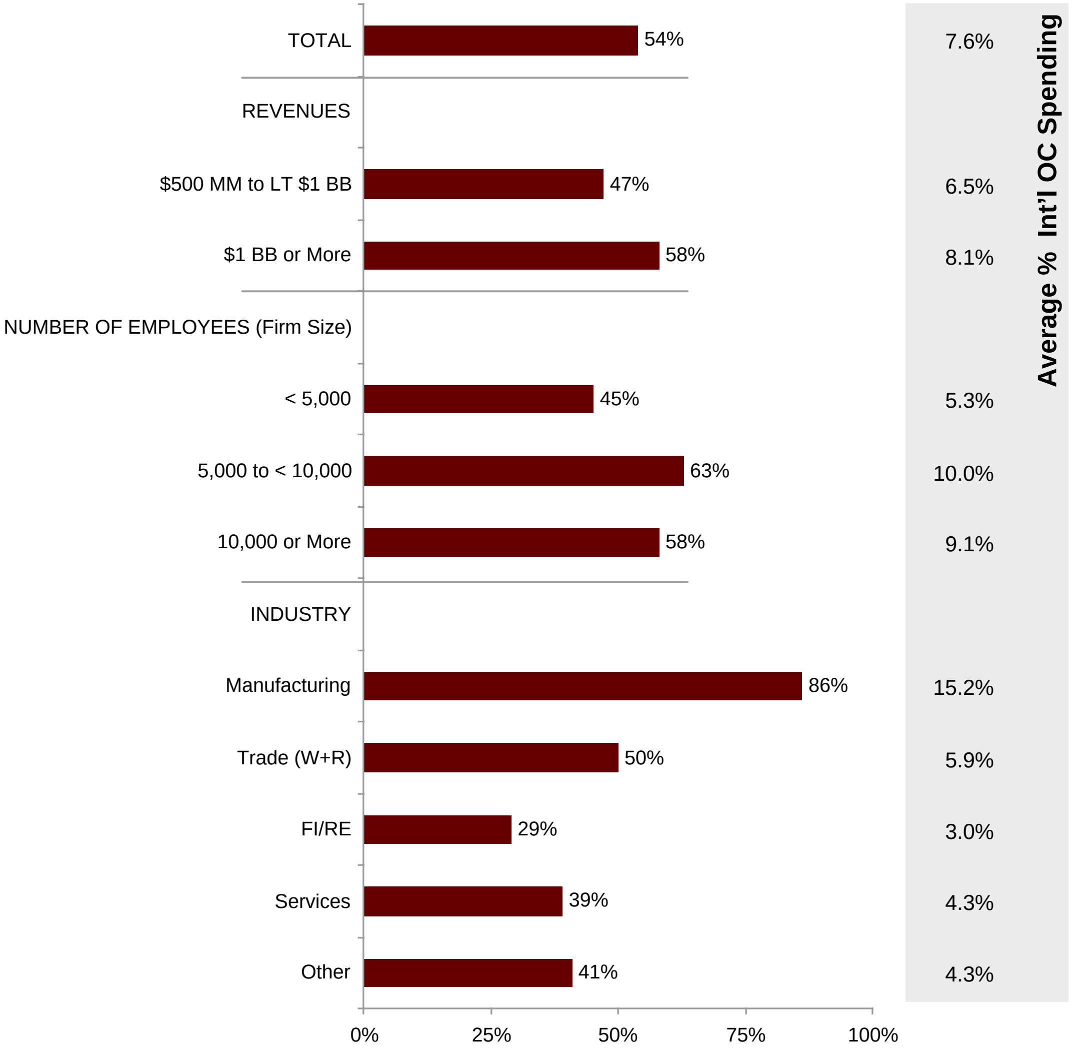
Growth Expected In Use Of Outside Counsel For Matters Outside The U.S.

- **54% of all firms report using outside counsel for matters outside the U.S. in 2001.**
- **Unlike overall legal spending, there is a slight tendency to expect more use of outside counsel for matters outside of the U.S.**
- **Manufacturing firms are notably higher than firms in other industries in reported use of outside counsel for matters outside the U.S. as a result of their more global activities.**

Percentage of Firms Reporting Increases or Decreases in International Spending on Outside Counsel in 2002



Percent of Firms Reporting (Any) International Outside Counsel Spending

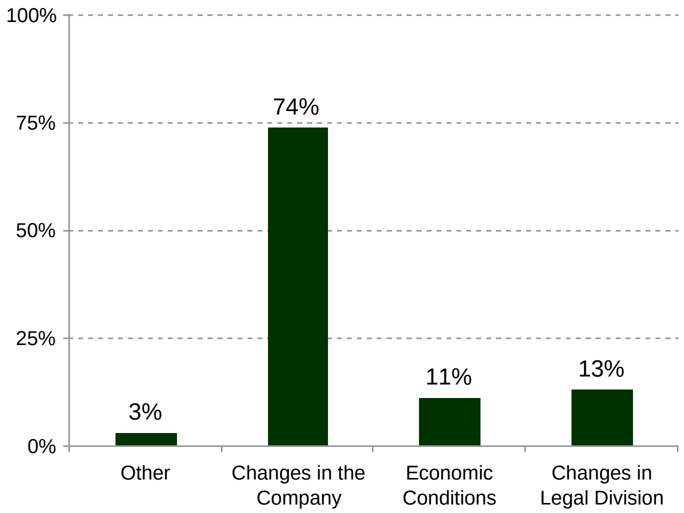


Strategy Changes Drive Use Of Outside Counsel Abroad

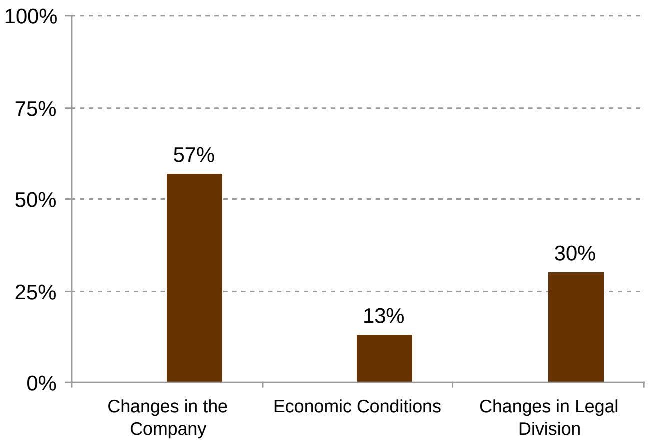
- **77% of all firms report use of outside counsel to increase as a result of changes in corporate strategy.**
  - Use of outside counsel for matters outside of the US has more to do with strategy (e.g., expanding international business (74%), or general corporate reorganization (3%) than with law department budgets.
  - Changes in the law department, including specific new transactions or projects, are secondary to these corporate strategy changes (13%).

- **Corporate strategy is also the most important factor influencing a decreased spending on outside counsel, with the main factor being withdrawal from foreign markets or business ventures.**

Reported Reasons for INCREASES in Outside Counsel Spending Abroad 2001-2002



Reported Reasons for DECREASES in Outside Counsel Spending Abroad 2001- 2002



The Voice Of The Respondents On Outside Counsel Spending

On Decreases in Spending….

- “Our litigation philosophy has changed to one of litigation avoidance.”
- “Current litigation will be completed, and will not have additional litigation at the same level coming up to take its place.”
- “Level of activity this year that will not be duplicated next year, we are not doing as many deals because of the economy.”
- “We will be bringing in higher level in-house talent.”
- “We are trying to limit what we send outside. More [use] of in-house counsel, more focus and closer review of outside billings.”

On Increases in Spending…

- “The amount of litigation and threatened litigation, amount of patent activity, amount of employee complaints or likelihood of complaints; higher insurance deductibles, general growth of business.”
- [“We will need to spend more on outside counsel because] we have eliminated 2 positions and 4 paralegal positions.”
- “The maturity of the entity. The longer you are around the more [work] you have.”
- “We will have more litigation matters and more corporate transactions due to the growth in our underlying business.”

Final Thoughts

- **Business forecasting isn't a science; all the survey can do is improve our intuition.**
- **When earnings decline in a recession, law departments are expected to control or shrink spending.**
- **It's natural for them to try to diminish the use of outside law firms in hard times.**
- **Overstaffed law departments get downsized.**
- **All this happens with a lag; last time the market crashed in '87; law firms suffered most in '90-'91 and recovered in '92.**
- **Law departments tend to be more focused on internal case load than external forces that may impact the business at large.**
- **It seems that our respondents believe that next year's contraction will be mild for both law departments and their outside counsel:**
  - Legal spending to flatten, not collapse.
  - Some spending increases on outside law firms and decreases expected to be moderate.
  - Transaction work has already shrunk around the country; surveyed law departments expect litigation to slow next year as well.
  - A puzzle: respondents seem to say "It's not the economy, it's what's going on inside our departments" Hard to understand outside the context of the macro contraction.
  - Moderate growth to continue on U.S. firm spending on lawyers abroad – continued impact of globalization.
- **In sum, if the economy rebounds in 2002 as forecast, law departments and their outside law firms could escape without major damage. Why? Possibly because of leaner staffing and continual expense control even during the good times.**
- **A forecast…or a wish?**

Appendix A: Survey Methodology

Sample Design

302 firms with annual revenues of $500 Million or more from a national sample of firms selected from D&B. Interviews conducted October 31st through November 20th, 2001.

- **General Counsel names developed from multiple sources including**
  - Aspen Law and Business Directory of Corporate Counsel
  - Martindale web site
  - Marketplace, Inc.
- **If no listing found in the above sources, screened for General Counsel among firms with 10,000+ employees or $1 Billion+ in revenues.**

Data Collection

- **Respondents interviewed by phone, with average interview length of 14 minutes.**
- **Respondents were sent a pre-alert letter explaining the purpose of the study and offering a copy of results.**

Additional Information About Firms Surveyed

NUMBER OF EMPLOYEES

- **43% Less than 5,000**
- **23% 5,000 to less than 10,000**
- **35% 10,00 or more**

OF LAWYERS IN-HOUSE 2001

- **36% Less than 4**
- **34% 4 to 9**
- **29% 10 or more**

APPENDIX B: Survey Questions

RESULTS FROM PAGE 2:
F3: What is your title?

Revenue data matched by D&B.

BASE: 302 General counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 3:
Q1a/Q1c: Compared to the year [2000/2001], has your firm's full year legal service expense, including inside staff and cost and outside legal fees, increased, decreased, or stayed about the same?

Q1b/Q1d: By what percentage did your firm's full year legal service expense [increase/decrease]?

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 4:
Q1a/Q1c: Compared to the year [2000/2001], has your firm's full year legal service expense, including inside staff and cost and outside legal fees, increased, decreased, or stayed about the same?

Q1b/Q1d: By what percentage did your firm's full year legal service expense [increase/decrease]?

F1: How many lawyers do you have in-house this year?

Industry data matched by D&B.

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 5:
Q2a/b/c: In the year [2000/2001/2002], what percentage of your total legal budget was/will be spent on outside counsel?

RESULTS FROM PAGE 5 (cont.):
Q5a: How do you expect your overall level of spending on outside counsel to change in the next six to twelve months? Do you expect your spending to be substantially lower, somewhat lower, about the same, somewhat higher, or substantially higher?

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 6:
Q2a/b/c: In the year [2000/2001/2002], what percentage of your total legal budget was/will be spent on outside counsel?

F1: How many lawyers do you have in-house this year?

Industry data matched by D&B.

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 7:
Q3a: In the past six months or so, did your firm use outside counsel in [AREA]?

Q3b: In six to twelve months from now, do you expect your firm's use of outside counsel in [AREA] to go up, go down, or stay about the same?

Q3c: Do you expect to use outside counsel for [AREA] six to twelve months from now?

Q4: Approximately what percentage of your total legal spending on outside counsel was spent for [AREA]?

RESULTS FROM PAGE 7 (cont.):
BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more that use outside counsel in 2001 or 2002.

RESULTS FROM PAGE 8:
Q5c: What has changed your expected spending on outside counsel?

BASE: 185 General Counsel that expect increases or decreases in spending on outside counsel from 2001-2002.

RESULTS FROM PAGE 9:
Q5c: What has changed your expected spending on outside counsel?

BASE: 185 General Counsel that expect increases or decreases in spending on outside counsel from 2001-2002.

RESULTS FROM PAGE 10:
Q6a-f: How important is each of the following factors in your expectations about the use of outside counsel six to twelve months from now?

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 11:
Q3a: In the past six months or so, did your firm use outside counsel in [AREA]?

Q3c: Do you expect to use outside counsel for [AREA] six to twelve months from now?

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 12:
Q7a: What proportion of your total legal spending was for matters partially or entirely outside of the U.S. this year?

Q7b: Six to twelve months from now, do you expect your firm's spending on outside counsel for matters outside of the U.S. to go up, go down, or stay about the same?

BASE: 302 General Counsel from a national sample of firms with revenues $500 Million or more.

RESULTS FROM PAGE 13:
Q7b: Six to twelve months from now, do you expect your firm's spending on outside counsel for matters outside of the U.S. to go up, go down, or stay about the same?

Q7c: Why do you expect your spending on outside counsel for matters outside the U.S. will [go up/go down] six to twelve months from now?

BASE: 68 General Counsel from firms that expect to increase or decrease spending on outside counsel for matters outside the U.S. in 2002.

RESULTS FROM PAGE 14:
Q7c: Why do you expect your spending on outside counsel for matters outside the U.S. will [go up/go down] six to twelve months from now?

BASE: 68 General Counsel from firms that expect to increase or decrease spending on outside counsel for matters outside the U.S. in 2002.