



# How Tomorrow Moves: CSX Uses Scorecards to Help Outside Counsel Stay on Track

BY THOMAS I. ANDERSON, KATHRYN D. KIRMAYER AND ROBERT A. LIPSTEIN

Lawyers love grades. Ever the smart kids in the class, for many years, good grades were our favorite reward for hard work, dedication, sacrifice and our stamp of approval. It's in our DNA to rip open the report card looking for the dreaded "B" or to push to the front of the crowd and scan the posted list of grades with breath held (from the top down, of course). Work well done is its own reward, but some of us will admit that good work recognized with a big red "A" is just a little better.

Lawyers can still find grades in the obvious places: the jury's verdict and the judge's decision. But when in-house counsel describe the law firms who have risen to the top of their class — the ones who not only provide outstanding results, but also deliver exceptional value and client service at the right cost — it's clear that lawyers are (and should be) judged on far more than what initially meets the eye. Too often, however, outside counsel are unaware of what — beyond exceptional results and unexceptional bills — their clients truly expect. And that can leave them working on a pass-fail basis, with important opportunities to add real value for their clients going unrecognized. They are left to learn their clients are unhappy only when the next case is sent elsewhere. It's an approach that costs both sides dearly.

This is the story of how CSX Corporation used that immutable trait of many lawyers — the drive to get an "A" — to help redefine its relationship with outside counsel. Performance-based holdbacks, scorecards, annual reviews and the personal touch were used to align inside and outside counsel in an open, constructive and mutually satisfactory partnership that is about more than dollars. It got both sides on track and helped CSX's legal program achieve the railroad's mandate of "Right Results, Right Way."

## The overhaul

In the spring of 2006, each of the 13 core law firms doing work for CSX received an invitation from the law department to send two representatives to a half-day meeting in Washington, DC. The agenda was to improve and modernize CSX's relationship with its outside law firms. As the conference room filled, lawyers from large firms across the United States nodded greetings and spoke quietly. AmLaw 100 was well represented, as were the top regional firms on the eastern seaboard. Some of the pre-eminent names in trial and appellate advocacy nationwide took their seats.

The title PowerPoint slide flashed onto the screen and the room quieted: "Consistent Continuous Improvement." Over the next 45 minutes, CSX's outside counsel learned that changes sweeping through the historic railroad, and its legal department, would be sweeping through their firms as well — or at least those firms staying aboard for the long haul.

Overhaul was a concept with which General Counsel Ellen Fitzsimmons and CSX were familiar. Freight railroads are as old school as industry gets, and for years, CSX and its law department had been no different. But in the early part of the decade, CSX's new management team began making changes. By 2003, CSX had a new vision: "To be the safest, most progressive North American railroad, relentless in the pursuit of customer and employee excellence." With that vision came a set of Core Values including "Right Results, Right Way." That meant, among other things, "how you get there matters."

Vision and values in mind, CSX set about transforming the company from the inside out with a goal of approaching old problems in new ways. That meant a new way of interacting with all stakeholders in the company, including employees, customers, the public, government and suppliers. The new approach emphasized establishing sustainable long-term partnerships, with shared goals and mutual investment in outcomes. For management employees, CSX instituted a new pay-for-performance system designed to align employee goals and compensation with the company's success.

The law department shared the corporate vision and first turned inward, remaking itself. If CSX expected blue-chip partnership from its outside counsel, it first wanted to set blue-chip expectations for its own performance.



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For starters, the law department drafted its own mission statement:

*To protect the people, property and reputation, and promote the businesses, of CSX Corporate and its affiliates by providing quality, cost-effective legal services, while acting at all times with the highest standards of honesty, integrity, courtesy and respect.*

Beyond the mission statement, the law department invested in professional development, expanded non-lawyer staff, developed specific standards and practices for routine legal work, and instituted a periodic internal client survey to gauge its own performance.

CSX then decided it was time to look outward and extend the overhaul to law firms that supported the company in its mission. The key question was how to enlist outside counsel as real partners in

achieving the objectives of the business. With that goal in mind, CSX set about designing a new program to manage its relationships with outside counsel. Even though CSX worked with some of the best law firms in the world, there was still work to be done. In some cases, it seemed the number of timekeepers appearing on bills grew like weeds from month to month. In other cases, it was hard to convince counsel to stay in touch. Budgeting at the outset of a matter was not routine, and sometimes, it seemed outside counsel lost sight of business objectives.

The message to the outside counsel crowded into the Washington, DC conference room was that CSX was changing how it ran its legal work to track its business goals and achieve professional excellence. It was modernizing its practices to become a leading legal organization not just in terms of outcomes, but in its approaches as well. And it wanted more than lip service from its outside counsel. It wanted to employ the right incentives to ensure its firms were focused on "Right Results, Right Way."

## The re-engineered system

The new CSX program had seven interrelated components:

- Outside counsel were expected to support and help in-house counsel uphold the legal department's *mission statement and standards of professionalism*.
- CSX would adopt *web-based billing* for receipt, review and approval of all outside counsel bills. Although some in the audience visibly winced,



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the CSX team explained that this procedure was expected to streamline review and expedite payment, which would translate into lower A/R and less float for the firms.

- The electronic billing system would also be used to help implement a new *staffing policy*, designed to ensure the appropriate level of staffing given the complexity and significance of each matter. CSX intended to focus on ensuring the appropriate level of seniority, and limiting duplication of effort between local and national counsel. Appropriate staffing would be determined at the outset of a matter, in consultation between in-house and outside counsel. Any subsequent changes to staffing required additional approval.
- CSX announced a new *budget policy*: All matters expected to exceed a nominal level of fees required a written budget to include proposed staffing. The budgets would be integrated with the electronic billing system, and on a monthly basis, CSX could determine which matters were running ahead or behind the budget. CSX emphasized that changes in budgets could be expected but would be formalized, and counsel were encouraged to propose alternative fee structures where appropriate.
- CSX designated an in-house *relationship leader* for each law firm, to serve as a liaison for communication between the firm and CSX. Paired with a relationship partner(s) at each firm, the relationship leaders were charged with providing outside counsel information about important CSX developments and company initiatives, monitoring the firm's performance and coordinating the annual evaluation process.
- All outside counsel would go through an annual *performance evaluation* process. This review was comprehensive and standardized — each CSX attorney would complete an online evaluation form for every law firm with which they worked during the preceding year [see sidebar for sample online evaluation form and evaluation guidelines]. Firms were scored on a 1-10 scale across four factors: budget, effectiveness, communication and advocacy. Evaluations of all CSX attorneys were aggregated, written comments were consolidated and a final assessment was prepared. The firms were then compared against each other to evaluate relative performance. A “scorecard” was prepared for each firm, and delivered personally during year-end meetings. The results would be used to make decisions about such matters as future consolidation of work and rate increases.

## All outside counsel would go through an annual performance evaluation process.

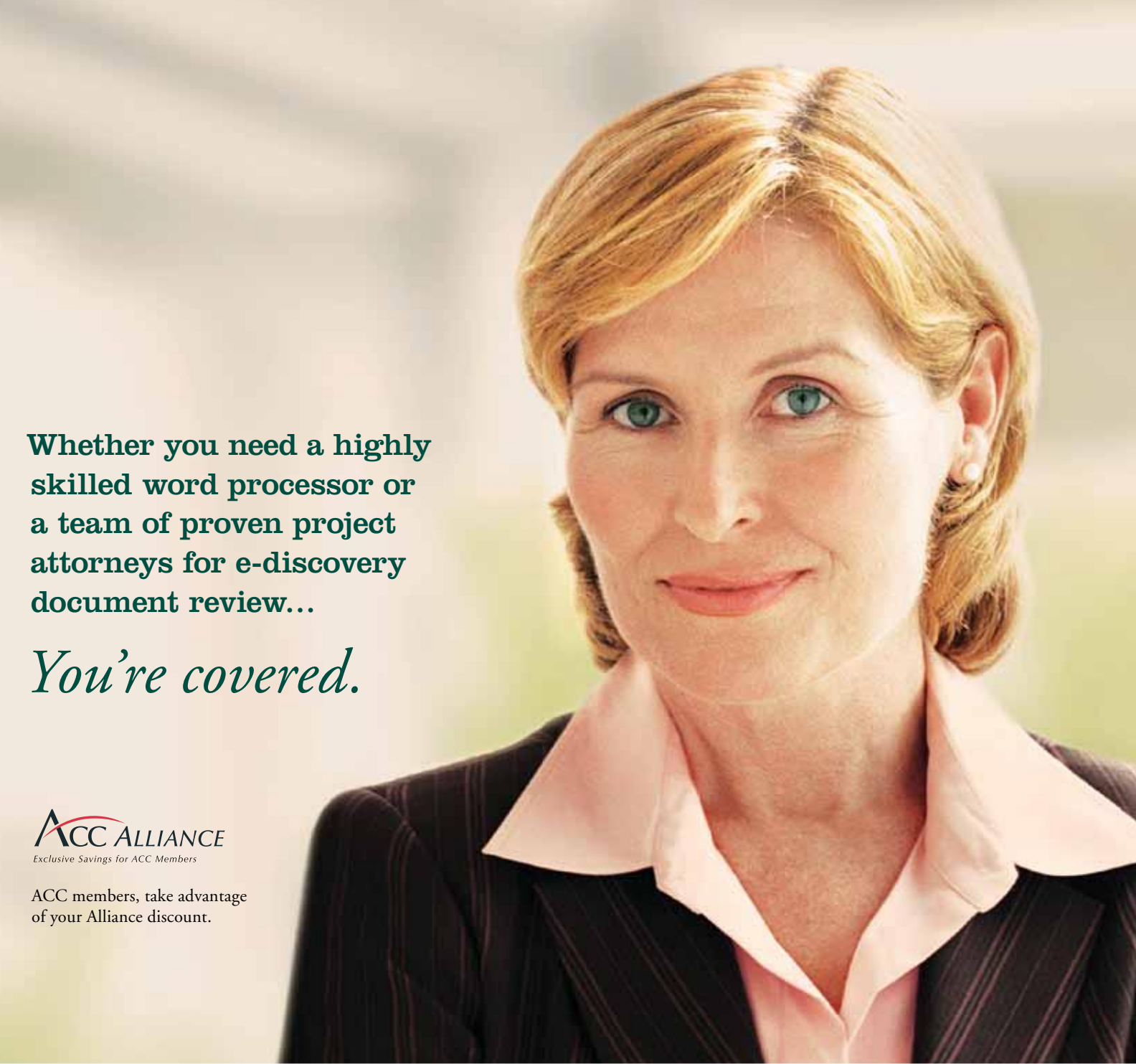
And the kicker:

- All firms would participate in a *performance-based holdback and bonus program*. For all hourly fee work, CSX would pay 85 percent of the total invoice immediately upon receipt and approval, but retain the remaining 15 percent for discretionary payment based on year-end performance evaluation. As an incentive, CSX would offer 5 percent bonus for extraordinary performance. The holdback did not apply to matters handled under alternative fee arrangements (e.g., flat or contingent fees), and did not apply to direct expenses. CSX pledged that any holdback payment would be made to the firms before year-end.

It was important to make clear to the assembled outside counsel what the new program was, and what it wasn't. This was not a program designed simply to reduce legal fees or to reduce the number of outside counsel. It was not about CSX demanding a 15 percent discount. In fact, CSX undertook the effort with the sincere hope of paying out 100 percent or more of the amount it held back. The law department made clear that it would accrue a reserve in the amount of the holdback from every bill, with the expectation that every firm would earn it back. The goal was improving performance and strengthening partnerships, not simply extracting dollars from the firms.

In the whirlwind of the new economy and alternative fee arrangement buzz, companies in CSX's position might be tempted to throw their economic weight around, demanding huge discounts and treating their outside firms like vendors, fungible and easily replaceable. CSX does not want to drive away talented lawyers and firms by demanding unreasonable rate concessions. CSX realized that over the long term, companies focusing only on rates get what they pay for: cut-rate lawyering by lawyers who are not invested in their client's business success. The CSX program incentivizes law firms to work toward shared goals and mutual success.

An important final key aspect of the CSX program is reflected on the bottom of the scorecard each firm receives in December:



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Reviewer Name:							Date:			
CATEGORY							SCORE			
Budget										
Comments:										
Effectiveness										
Comments:										
Communication										
Comments:										
Strategic Advocacy										
Comments:										
							Total:			
Other Comments:										
Assessment Scale										
10	9	8	7	6	5	4	3	2	1	0
Exceptional		Good		Meets Expectations			Poor		Unacceptable	



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## Law Firm Evaluation Guidelines

### CSX Corporation CSX Transportation, Inc.

#### Outside Counsel Evaluation Guidelines

##### **Evaluation Categories**

There are four evaluation categories, each of which encompasses a range of related professional competencies. A brief description of each category follows:

**Budget:** Evaluates overall performance in managing the cost of matters. Should capture both administrative effectiveness, such as timely submission of budgets and compliance with billing guidelines, and overall productivity, including cost consciousness and appropriate staffing.

**Effectiveness:** Evaluates results of services rendered. Should consider results in light of the goals and expectations of the representation.

**Communication:** Evaluates information exchange between CSX and the firm. Includes responsiveness to requests, understanding of expectations, clarity of written and oral communications, and timeliness.

**Strategic Advocacy:** Evaluates overall partnership in advancing the interests of CSX. Can include seeking creative solutions to complex problems, contribution to tort reform efforts and strategic appellate practice, collaboration with CSX non-legal resources, understanding of CSX business objectives, and efforts to prevent future issues or reoccurrence of past problems.

These categories and descriptions are intended to serve as a framework for evaluation, not to limit the scope of evaluation or provide an exhaustive list of potential subjects.

##### **Assessment Scale**

The assessment scale ranges from 0 (unacceptable) to 10 (exceptional). Scores should be assessed relative to expectations for the particular firm and representation. Generally speaking, performance that simply meets reasonable expectations, given the context of the firm and the matter, should be evaluated as 5 (meets expectations). The highest and lowest scores should be reserved for exceptional circumstances.

##### **Comments**

Written comments are a critical part of the evaluation process. Whenever possible, comments should address both positive and negative performance.



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**Your feedback.** By Jan. 31, please provide a concise written summary of your firm's ideas as to how CSX can be a more effective partner, advocate and user of legal services, and at all times throughout the year, please call with any questions or concerns.

**Your ideas.** In that context, please make an effort to share at least one idea for better handling of legal work that you have observed from your firm or another client.

This is the third rail of lawyer-client relationships: Does the client really want to know what outside counsel think they could do better? Innovation in legal services is constant and all around us, and CSX's outside counsel have exposure to the best — and worst — new ideas at hundreds of in-house legal departments around the world. Why wouldn't CSX capitalize on that depository of knowledge? The "360" review was only possible because the law department worked to create the right environment for it. For example, CSX repeatedly received feedback that outside counsel could be more effective if they had a better understanding of the company's overall business strategy and goals. So CSX began conducting periodic "core counsel summits," gathering together outside counsel to hear from senior business leaders about the real issues that drive performance and results. These summits have strengthened the partnerships with outside counsel while making them better advocates for the company's interests.

### Initial law firm responses

Not all firms immediately embraced the change. We fielded concerns that the electronic billing system would be onerous or that the grading would be subjective and the holdback would be impossible to earn back. All were fair concerns, but ultimately, the proof was in the pudding. The new program was about accepting an invitation to a closer, stronger relationship.

The Crowell & Moring attorneys returned from the meeting realizing this was an opportunity, not a threat. And it was a sign of more change to come as other companies adopted the model. The firm has always been strong in client service, but the CSX model provided a meaningful way for the firm's lawyers to measure that service against what really mattered to one of its most important clients. It meant the firm lawyers could expect to be rewarded for client service in a concrete way — assuming the firm could perform consistently across the wide variety of matters it handled.

All Crowell attorneys working on CSX matters — across all practice groups — met together to hear about the new system and to be briefed on the evaluation criteria. Quite

## Not all firms immediately embraced the change.

predictably, the firm was determined to get all 10s. The team of lawyers discussed mechanisms to ensure they measured up. With CSX's scorecard in hand, Crowell could manage its matters to make sure those needs were met. For example, the firm designed its own "staffing template" form for internal use, to be completed by the responsible partner for each CSX matter, tracking proposed staffing. When Crowell saw that CSX would actually award credit for creativity, it freed team members to propose unusual strategies or innovative approaches to working with in-house colleagues. It was as if the CSX scorecard gave the lawyers new permission to check on their progress and service throughout the course of the engagement. The scorecard became a tool for a dialogue on client service that carried new meaning and clarity.

### Beyond the grade: Tracking value

As the program has evolved, CSX doesn't merely use the scores to give feedback to outside counsel and administer the holdback program. It also incorporates the scores into its own internal analyses of value, weighing volume of work, average per-hour rate and quality score to analyze how core firms array on the twin axes of quality and price. These analyses help the law department decide where to direct new matters and which firms truly offer the most value per dollar. The analysis is fed into a bubble chart that provides a unique glimpse into the performance of CSX firms.

### The verdict

So, five years down the road, how has it all worked out for CSX and its core firms?

The feedback from both in-house and outside counsel has been very positive, and the results have exceeded our internal expectations. CSX has successfully managed its legal spending over the past five years, but it has done so while still employing top-notch counsel and still taking on difficult problems for the company. The performance evaluation process has evolved from an uncomfortable undertaking for many involved at the outset to a routine part of our business process. Our experience is that most professionals value frank feedback on their performance when they get it, and by providing a routine process where that can occur, CSX has loosened some of the barriers of human nature that might otherwise stand in the way.

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For Crowell & Moring, the scorecard provided an incentive to focus on areas of client service that, just 10 years ago, might not have warranted as much attention. Pre-approval of timekeepers and a focus on appropriate staffing has changed the way the firm works. Now, if a sudden research project comes up that requires additional staffing, Crowell lawyers call and describe the need and the proposed new team member in advance, and the CSX attorneys have the chance to say yes, no or later. As a side-benefit, Crowell's core "CSX team," comprised of attorneys who spend a high proportion of their time on CSX matters, has been able to become better acquainted with the company and its in-house attorneys. The scorecard creates a framework for them to initiate focused and frequent communication with CSX. And because individual attorneys are included in the written comments on the scorecard sheets, Crowell attorneys are rewarded for their good work by both the client and members of the firm when the scores come back.

Some clients want their outside counsel to identify opportunities to be creative or to suggest partnering on new ideas — but until they assign a tangible value to those inputs or provide outside counsel with the information they need to be effective in those areas, those ideas don't shape up.

### **"Continuous" means continuous: Next generation**

What's next for CSX and its outside counsel? With a solid group of core firms and five years of collective experience with the mutual-gains approach, CSX is redoubling its efforts to find appropriate billing models beyond the hourly fee structure. The law department is encouraging its core firms to experiment with alternative fees, with the explicit understanding that the partnerships forged over the past several years will allow both sides to honestly appraise the results and make equitable adjustments as necessary.

Crowell & Moring has taken its relationship with CSX to the next level. In response to CSX concerns about the overall legal budget and predictability of fees in some of the largest matters, Crowell proposed a portfolio flat-fee billing arrangement for all of its work. A single annual fee covers both counseling and litigation across a variety of subject areas. This arrangement requires a high level of trust and a long-term commitment from both sides. CSX needs to trust that Crowell will continue to see its best lawyers, at all levels, dedicating the same time and attention to CSX matters as they always have. And Crowell needs to be able to trust that if the unexpected happens, CSX will find a way to protect the firm from a serious economic hardship. The increased trust built through the performance program paved the way for that new fee model to come about. And both firms were willing to take risks.

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### **Tips to create your own performance program**

For in-house counsel contemplating a performance-based hold-back arrangement, whether for a single matter or for a group of matters, here are some tips for getting the most out of it.

#### ***Keep the signals straight: Frequent, clear and honest communication.***

Communication is a two-way street, and it is critical to invest all in-house counsel with the authority and responsibility to engage in a consistent dialogue with outside counsel about the company's goals and expectations for representation. Inside counsel need to embrace the concept that our success depends on having engaged effective outside counsel who know when they are doing well and how they can improve.

Once a performance-based compensation program is operational, periodic communication regarding the law firm's performance prior to the annual report card is essential to prevent system breakdown. Once a year is too little, too late to learn about missteps or miscommunications. As part of the CSX program, each firm gets an informal, mid-year debriefing from its relationship leader designed to eliminate surprises and trigger mid-course corrections. And throughout the year, in-house and outside counsel are encouraged to thoroughly evaluate performance and results against goals and expectations to find opportunities and lessons learned. The law department also routinely conducts in person *post mortem* ses-

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## Most of all, don't overlook the phenomenal opportunity you have as a corporation to cultivate healthier relationships with your outside counsel.

sions with internal clients and outside counsel to recognize success and identify areas of improvement.

### *You get what you measure.*

The scorecard criteria communicate loud and clear to your outside firms what you want and what you value, and in what proportion. It may seem obvious, but not all clients value the same things to the same degree. So the process of developing the criteria, and deciding how to score and weigh them, is a critical one. CSX began framing its evaluation process by conducting group sessions in the law department — drawing on the accumulated experience of its in-house professionals — to identify the criteria that can make an outside firm successful and a representation effective. Once those criteria are identified, it is important to design an evaluation program that will elicit qualitative comments and specific examples in addition to numerical scores. CSX's experience has been that numerical scores can vary significantly from person to person and year to year, but written comments add the most value to the evaluation process, both for the in-house team and the outside counsel. It has also proven important to include internal clients in the evaluation process, as their experience interacting with outside counsel can often provide a different insight. At year-end, numerical scores and qualitative comments for all firms, along with other factors, are reviewed together by the CSX law department leadership to determine performance-based compensation.

From the law firms' perspective, it's important that the scorecard be credible and fair. Even though numbers are used, the scoring is subjective. That's why it is critical for the scores to be reviewed to be sure they reflect a fair sample and the consensus of those who dealt with the firm. The great thing about the CSX program is that there are so many evaluators that the scores have a greater chance of being perceived as fair.


The specific comments are often more valuable than the numbers, because the comments tell firms what drove the number and give firms the information they need to do better next time. It is a delicate balance because anonymity is important to ensure candor, but sometimes it's hard to be specific and retain that anonymity.

Also, keep in mind that the scorecards are a powerful tool inside the law firms. Firms do pay attention to the criteria. Firms do "work to the test," and they do take action in response to scores. At Crowell, annual report cards are distributed to everyone on the client team and to the firm's leadership. There can be implications — for future staffing and even compensation — for attorneys who are singled out, for good or ill, in the evaluation.

### *Make it personal.*

Recognize another important driver of good behavior: personal relationships.

Meet face-to-face with your partners and other key attorneys at each firm to deliver their scorecards and go over their results. Use these meetings to share with outside counsel your company's business outlook and plans. This is a critical component of the process. It communicates to the firms that you are truly personally invested in the program and are making the time at the highest levels of the company to work on those relationships.

Most of all, don't overlook the phenomenal opportunity you have as a corporation to cultivate healthier relationships with your outside counsel. The investment in a good performance program appeals to the over-achievers in all of your law firms who want to do better and gives them better tools to help you succeed. If your lawyers don't get it, they shouldn't get it. 

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