



Alternative Fees are not the Enemy

By Michael W. Davis

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A curious irony in the current discussion of the billable hour is that the popularity and widespread use of the hourly fee arrangement arose from increased client demand. Clients saw clarity, certainty and objectivity in the hourly rate. They also saw a description of the specific services they were paying for, as opposed to the one-line statement: "For services rendered: \$50,000."

The billable hour, over time, has served both clients and law firms alike, and in a great many diverse matters will continue to do so. Billing by the hour is transparent, and firms interested in maintaining or establishing a long-term relationship will not overcharge their clients. Nevertheless, a growing number of corporate counsel and lawyers in private practice argue that the billable hour may reward inefficiency, fail to provide adequate incentive for outside counsel to work cost-effectively and represent a poor method for rationally predicting future costs. Current economic pressures and challenges – and the need for reduced costs for legal services – have increased the demand for alternative fee arrangements that begin to address these perceived shortcomings. Whether one calls these arrangements fixed-fee billing, task-based billing, risk-sharing billing or value-based billing, the time for significant change is upon us. According to the highly regarded BTI Consulting Group, nearly 80% of corporate counsel already rely on some form of alternative billing arrangement. Only 2% of corporate counsel plan to decrease reliance on such arrangements.

Embracing Alternative Fees

The Association of Corporate Counsel (ACC) reports that only 13% of large-company general counsel did not utilize any kind of alternative fee arrangement in 2010. Indeed, the ACC reports that its survey of chief legal officers and general counsel "indicates a continued increase in the use of alternative fee arrangements, regardless of the market rebound, suggesting that practices are becoming institutionalized." Similarly, in an Altman Weil survey of law firms published in *The American Lawyer* in June 2010, nearly all of the 218 firms that responded reported that they offer some type of alternative fee arrangement.

Smart law firms will not lament the passage of the straight billable hour as the norm. They will embrace it. Increasingly, astute law firms initiate consideration of alternative fee arrangements that are tailored to meet specific client needs. By way of example, if we focus on one favored type of alternative fee arrangement – the "value-based" alternative in which clients

compensate their lawyers not for their time but for the value they provide – we can see that this alternative dovetails nicely with a well-run firm’s principles and goals.

Why? Concepts inherent, for example, in “value billing” are hardly foreign to outstanding firms and, in many circumstances, serve to distinguish the few from the many. Value here, and in most circles, embraces more than simply cost reduction. Value includes, among many factors, a deep understanding of the client’s business and priorities, creativity, dependability, efficiency, integrity, reliability of work product, strong communication, success and timely performance. Great law firms have always emphasized these “values.” Accordingly, such firms should embrace this alternative for these and several other reasons.

The billable hour has never adequately captured the benefit that a better idea or insight, which may involve a small amount of time, can produce. One court long ago said it well: “The value of a lawyer’s services is not measured by time or labor merely. The practice of law is an art in which success depends as much as in any other art on the application of imagination – and sometimes inspiration – to the subject-matter.” *Woodbury v. Andrew Jergens Co.*, 37 F.2d 749, 750 (S.D.N.Y. 1930). This value may be particularly significant when a client faces high-stakes or novel legal issues.

Further, the benefit resulting from a highly successful settlement, motion, trial, appeal or negotiation may bear just a small relationship to the time lawyers actually spend securing a strong result. And the law firm that achieves the excellent result should stand to share in the gain from the special benefit to its client that it has helped to produce.

In addition, expanded emphasis on project management and knowledge management allows law firms to do far more efficiently what historically may have taken longer. Legal project management is a more systematic approach to planning and managing matters and produces a wide variety of benefits, including a greater ability to predict and control costs and greater efficiency. Knowledge management allows law firms to capitalize on the breadth of their expertise and experience and, like project management, to control costs and enhance efficiency. Moreover, having invested substantial resources in technology, the best law firms today can deliver services and results with far greater efficiency than years ago.

Change is rarely easy. But the movement toward alternative fee arrangements, particularly “value-based” alternatives, will strengthen the ability of excellent firms to better address their clients’ needs in difficult times, lead to better client relationships and ultimately enhance profitability without perpetuating any notion that a law firm’s profitability can be enhanced only at its client’s expense. When done right and well, alternative fee arrangements create the win/win that insightful clients and law firms seek to achieve.

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