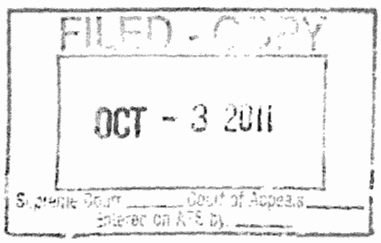
10-3-2011

Bailey v. Bailey Appellant's Brief Dckt. 38760

IN THE SUPREME COURT OF THE STATE OF IDAHO

///

IN THE MATTER OF THE ESTATES OF CAROL BAILEY and FRANCIS ANDREW BAILEY, Deceased,	
F. KIM BAILEY, Personal Representative of THE ESTATES OF CAROL BAILEY and FRANCIS ANDREW BAILEY, Plaintiff- Appellant, v. KERRY BAILEY, KYLE BAILEY, and TAMARA BAILEY SIPE, Defendants-Respondents.	Supreme Court Docket No.- 38760-2011 Bonneville County Docket No. - CV-2006-6496



APPELLANT'S BRIEF

Appeal from the District Court of the

Seventh Judicial District

for Bonneville County

Honorable Jon J. Shindurling, District Judge, Presiding

REGINALD R. REEVES, ESQ.
Appellant's Attorney
Cambridge Law Center
Box 1841
Idaho Falls, Idaho 83403

MICHAEL J. WHYTE, ESQ.
Respondents' Attorney
2635 Channing Way
Idaho Falls, Idaho 83404

IN THE SUPREME COURT OF THE STATE OF IDAHO

///

IN THE MATTER OF THE ESTATES OF CAROL BAILEY and FRANCIS ANDREW BAILEY, Deceased,	
F. KIM BAILEY, Personal Representative of THE ESTATES OF CAROL BAILEY and FRANCIS ANDREW BAILEY, Plaintiff- Appellant, v. KERRY BAILEY, KYLE BAILEY, and TAMARA BAILEY SIPE, Defendants-Respondents.	Supreme Court Docket No.- 38760-2011 Bonneville County Docket No. - CV-2006-6496

APPELLANT'S BRIEF

Appeal from the District Court of the

Seventh Judicial District

for Bonneville County

Honorable Jon J. Shindurling, District Judge, Presiding

REGINALD R. REEVES, ESQ.
Appellant's Attorney
Cambridge Law Center
Box 1841
Idaho Falls, Idaho 83403

MICHAEL J. WHYTE, ESQ.
Respondents' Attorney
2635 Channing Way
Idaho Falls, Idaho 83404

TABLE OF CONTENTS

TABLE OF CASES & AUTHORITIES

CASES

STATUTES

RULES

PERIODICALS

1. "The Billable Hour: Are its Days Numbered?" The American Lawyer, Douglas McCollan, November 28, 2005

2. "Kill the Billable Hour," Forbes Magazine, January 12, 2009

3. "The Hours," Legal Affairs Magazine, Nicki Kuckes

4. 'Billable Hours Giving Ground at Law Firms," New York Times, Jonathan D. Glater, January 30, 2009

5. "The Scourge of the Billable Hour," Washington Post, Lisa Lerer

6. "The Billable Hour Must Die," ABA Journal, Scott Turow

7. "The Time is Up for Outdated System of Charging by the Hour, Chris Merritt, "The Australian," August 20, 2010

8. The Economist, May 7, 2011

9. All Business, August 7, 2010

10. "Billable Hours Giving Ground at Law Firms," New York Times, January 30,2009

11. "Time to Experiment with Alternative Billing Practice." The Lawyers' Advantage, Fourth Quarter 1988.

12. Bargain Briefs, The Economist, August 11, 2011

STATEMENT OF THE CASE

i. Nature of the Case

This is an appeal from the following:

ORDER ON APPEAL
ORDER OF REMAND
ORDER DENYING PETITION FOR REHEARING

ii. Course of the Proceedings.

(a) On June 24, 2009, Respondents filed a Petition for Accounting and Separation of personal representative's attorney fees from estate attorney fees, [**R. Vol. III, p. 405**], which petition was supported by an affidavit of respondents' counsel. [**R. Vol. II, p. 399**].

(b) Appellant answered respondents' motion by filing a responding affidavit. [R. Vol III, p. 407].

(c) The court heard arguments regarding the Petition for Accounting on August 31, 2009 [Tr. p. 143] and "denied the part of the petition which requires or asks that the personal representative and counsel attempt to separate out that which was for the estate and that which was personal." [Tr. P. 154]. The court ordered the personal representative to file a "memorandum of fees and costs in support of any fees which are requested under the statute." [Tr. pp. 154-155].

(d) On September 17, 2009, the Trial Court entered an Order on the Petition for Accounting. [R. Vol. III, p. 431]. The Order commanded the personal representative to file a final accounting indicating all property, income and expenses

to date as well as a memorandum of fees and costs reflecting the work provided for personal representative.

(e) On September 16, 2009, personal representative's counsel filed a Memorandum of Costs, [R. Vol. III, p. 416], which costs (including fees) the personal representative paid.

(f) On September 29, 2009, respondents filed an objection to the Memorandum of Costs. [R. Vol. III, p. 459].

(g) On October 21, 2009, the court held arguments on respondents' request for additional Detail and Accounting and Objection to Memorandum of Costs, and on November 19, 2009, the court issued its order thereon, [R.Vol. III, p.484], finding the Memorandum of Costs to be insufficient, under IRCP 54(e)(3), for the court to determine whether the requested fees were reasonable, and ordering that the memorandum of costs be resubmitted, to comport with IRCP 54(e)(3), to specifically outline the basis for the claimed fees, regarding the value of particular services provided.

(h) On December 1, 2009, appellant filed a Motion for Reconsideration of the November 19, 2009 order, [Vol. III, pp. 490A, 490B], stating that no time records were maintained for legal services, although details confirming the performance of each service had already been submitted to the court. He requested that a determination be made pursuant to IRCP 54(e)(3)(J) and (L).

(i) On December 16, 2009, the court issued its Order Denying Motion for Reconsideration. [R. Vol. III, p. 491]. The court ordered that pursuant to §15-3-720, counsel must show time records for the work performed, in order for the court to determine if the attorney's fees are reasonable and that without such records the court could not grant the request for such fees.

(j) This appeal followed.

iii. STATEMENT OF FACTS

(a) On October 17, 2006, appellant and his attorney entered into an attorney-client contract. [R. Vol. III, p. 574].

(b) The contract stated, inter alia, that "You [Reginald R. Reeves] will use your best efforts on my behalf, for which I [Personal Representative] will pay all expenses incurred, together with a fee to be determined by you, based upon what you believe the services to be reasonably worth, and not based upon an hourly basis."

(c) In accordance with such contract, Mr. Reeves billed on the reasonable worth of his legal services to the estate, not on an hourly basis. No time records were kept.

(d) Respondents moved for a final accounting, which was provided, and the court required time records. [Tr. 172, lines 23-25].

(e) A notice of inability to comply was filed [R. Vol. III, p. 489],

stating that pursuant to such contract, no time records were maintained.

(f) The court then denied the entitlement to the fees set forth in such memorandum.

(g) The court entered an order requiring the filing of a memorandum of costs "reflecting the work provided for the Personal Representative."[R. Vol. III, p. 432].

(h) Two days later, the court entered an order requiring that the memorandum of costs be resubmitted [R. Vol. III, p. 486], "to specifically outline the basis for the claimed fees and specific information regarding the value of particular services provided."

(i) Upon appeal, the rulings of the trial court were affirmed.

ISSUES PRESENTED ON APPEAL

I.

WHETHER THE COURT ERRED IN DETERMINING THAT TIME RECORDS FOR WORK PERFORMED ARE REQUIRED, TO ESTABLISH WHETHER ATTORNEY'S FEES ARE REASONABLE?

II.

WHETHER THE COURT ERRED IN DETERMINING THAT IT CANNOT DETERMINE IF ATTORNEY'S FEES ARE REASONABLE WITHOUT TIME RECORDS FOR WORK PERFORMED?

III.

WHETHER THE COURT ERRED IN ORDERING PERSONAL REPRESENTATIVE'S COUNSEL TO SUBMIT TIME RECORDS FOR WORK PERFORMED DESPITE TERMS OF ATTORNEY-CLIENT CONTRACT WHICH DID NOT BASE FEES ON AN HOURLY BASIS?

IV.

WHETHER APPELLANT SHOULD BE AWARDED FEES ON APPEAL, PURSUANT TO §12-121 I.C., IAR 41, IRCP 54(e)(3)(L), AND §15-3-720 I.C.?

ARGUMENT

I

TIME SHEETS NOT APPLICABLE, WHERE A CONTRACT SETS OTHER CRITERIA

The court erred when it determined that the contract between the personal representative and his attorney is subject to IRCP 54(e)(3)(A). Under I.R.C.P 54(e)(3)(L), a court may award reasonable attorney fees. . .when provided for by. . ..contract." Under IRCP 54(e)(3)(A), "The time and labor required" is but one factor used to determine the amount of attorney's fees granted to a party in a civil action. The Idaho Supreme Court, however, has placed limits upon the applicability of IRCP 54(e) to an attorney fee determination, citing IRCP 54(e)(8) as stating: " The provisions of this Rule 54(e) relating to attorney fees shall be applicable. . .to any claim for attorney fees made pursuant. . .to any contract, to the

extent that the application of this Rule 54(e) to such a claim for attorney fees would not be inconsistent with such . . . contract.'" Zenner v. Holcomb, 147 Idaho 444, 451. In Zenner, the Court ruled that the factors listed in IRCP 54(e)(3) are not applicable if "considering the factors in IRCP 54(e)(3) would be contrary to the language of the contract and, therefore, contrary to IRCP 54(e)(8). Here, therefore, IRCP 54(e)(3) is not applicable. The contract provision does not contemplate the court's involvement in determining whether the fee is reasonable."

In this case, application of the IRCP 54(e)(3)(A) (time and labor required) factor is contrary to the language of the attorney-client contract between the personal representative and his attorney. The personal representative signed a contract with such attorney for legal representation in this action on October 4, 2006. Under the terms of the contract, appellant agreed to "pay all expenses incurred, together with a fee to be determined by you, based upon what you believe the services to be reasonably worth, and not based upon an hourly basis." In accordance with such contract, the estates were billed according to the reasonable worth of the services, not upon an hourly basis.

II

THE CONTRACT WAS VALID

The court and respondent have not challenged the validity of the

contract, personal representative's authority to enter into the contract on behalf of the estates, or counsel's right to form agreements with his clients on the reasonable value of his legal services (not on an hourly basis).

Had the issue involved plumbing services to the estates, billed at an agreed upon flat rate, respondent's should not be heard to complain that some other plumber might have charged less, or completed the work in less time.

As in Zenner, the contract provision governing attorney compensation herein does not contemplate the court's involvement in determining whether the fee is reasonable. In addition, the "reasonably worth" criterion is in direct contradiction with "the time and labor required" factor of IRCP 54(e)(3)(A). The application of IRCP 54(e)(3)(A) violates the attorney-client contract and, therefore, is contrary to IRCP 54(e)(8).

In order to determine the reasonableness of attorney's fees as required by §15-3-720 I.C., appellant requests that the trial court be required to accept the accounting given concerning attorney's fees, as contained in the Memorandum of Costs submitted to the court on September 16, 2009, and use the factors listed in IRCP 54(e)(3) which do not violate provisions of the attorney-client contract and IRCP 54(e)(8).

III

THE COURT ERRONEOUSLY CONSIDERED ONLY TIME INVOLVED

The court erred in its determination that it cannot determine the reasonableness of attorney's fees without time records of work performed. In its Order Denying Motion for Reconsideration, issued December 16, 2009, the court mistakenly ruled, "[a]bsent compliance with the court's order, requiring time records for the work performed, the court cannot determine if the claimed attorney's fees are reasonable and cannot grant the request for such fees." Under IRCP 54(e)(3), "(A) The time and labor required" is only one factor used to decide the amount to grant in attorney's fees. The rule provides many other factors, from (B) to (L), including "(J) Awards in similar cases" and "(L) Any other factor which the court deems appropriate in the particular case." "The time and labor required" factor cannot be used in this case.

If, despite the holding in Zenner, IRCP 54(e)(3) should be deemed applicable, appellant requests that the court use factors (B) to (L) along with the previously submitted accounting contained in the Memorandum of Costs, to determine the reasonableness of the claimed attorney's fees.

IV.

COMPLIANCE WOULD HAVE REQUIRED VIOLATION OF IRPC 8.3

The court erred in ordering the appellant counsel to submit time

records for work performed. Under the Idaho Rules of Professional Conduct, 8.4(c), "it is professional misconduct for a lawyer to engage in conduct involving dishonesty, fraud, deceit or misrepresentation."

In this case, the appellant provided the court with a copy of the attorney-client contract, with the provision that billing would be based on the "reasonable worth" of the legal service, not on an hourly basis. On November 19, 2009, the court issued its Order Re: Requests for Additional Detail on Final Accounting and Objection to Memorandum of Costs and commanded that the memorandum of costs filed by personal representative's attorney be resubmitted, to comport with IRCP 54(e)(3), to specifically outline the basis for the claimed fees and specific information regarding the value of particular services provided. On December 1, 2009, personal representative reminded the court in the Motion for Reconsideration that "no time records were maintained." To comply with the court's order to produce time records, appellant's counsel would have had to guess at and fabricate his claimed hours. The fraudulent time records would constitute a deceitful submission to the court, in violation of IRPC 8.4(c), and therefore, personal representative and his attorney could not comply with the court's order.

V

BILLABLE HOURS – – AN OUTMODED CONCEPT

There is a trend– –nationally and internationally– –away from the

outmoded, unfair practice of determining legal fees based upon the hours (actual or manufactured) involved in the representation of the client.

A

> "For about 50 years now the billable hour has been the dominant feature of the legal profession. And for just as long lawyers have been trying to kill it. A group of litigators who usually couldn't agree that the sky was blue without several footnotes qualifying the shade will gladly sing in harmony about the evils of the billable hour and its partner in crime, the daily time sheet. Yet generations of lawyers have accounted for their work lives in six-minutes increments. Both reviled and ubiquitous, the billable hour is the cockroach of the legal work.
>
> "The basic flaw of the billable hour, say its detractors, is that it puts the financial incentives in the wrong place. Back in a more genteel age, grouse many lawyers, when the practice was more of a profession and less of a business, the cost of legal services was determined not by the amount of time a lawyer spent on a matter but on the value he delivered to the client." Douglas McCollam, "The Billable Hour: Are Its Days Numbered?," The American Lawyer, November 28, 2005, Addendum 1.

B

> "Clients have long hated the billable hour. . ..the hours seem to pile up to fill the available space. The clients feel they have no control, that there is no correlation between cost and quality." "Kill the Billable Hour," Forbes Magazine, January 12, 2009, Addendum 2.

C

". . . 'The billable hour is fundamentally about quantity over quality, repetition over creativity,' Robert E. Hirshon, the president of the American Bar Association, recently observed." Article by Nicki Kuckes, Distinguished Practitioner at Cornell Law School, in Legal Affairs Magazine, p.1, Addendum 3. Mr. Hirshon referred to it as the "tyranny of the billable hour."

D

". . . Treating legal services as a commodity than can be measured in units of time diminishes the importance of both the quality of the work produced and the results achieved. Few other industries would thrive if they measured productivity by the time their workers spent without regard to what those workers created. The standard invites inefficiency, not to mention fraud. The potential for conflicts of interest is obvious– – it's in the firm's financial interest for lawyers to spend as many hours as possible, while the client's interest is best served by limiting the time spent." Kuckes, supra.

E

"The need to bill 2,000 hours a year also means that 'there are bound to be temptations to exaggerate the hours actually put in,' as Chief Justice Rehnquist said. The possibilities for fraud abound, though fraud is often hard to detect. Lawyers can cheat by writing down hours they didn't work or by exaggerating the hours they did." Kuckes, ibid.

F

". . . The system of billing by hour has been firmly in place since the 1960s . . .. In earlier, perhaps more trusting times, firms stated a price 'for services rendered,' without explanation." Glater, Billable Hours Giving Ground at Law Firms, New York Times, January 30, 2009. Addendum 4.

"When not paid by the hour, lawyers' approach to their work changes . . ..

* * * *

"On top of the [fixed] fee. if the case settled for less than what the [client] feared having to pay if it lost in court, the law firm got a percentage of the amount saved. The arrangement made sense when the goal was to resolve the dispute quickly. . ..

"Lawyers on the case negotiated a settlement for much less than the client's worst-case number . . .. 'The effective hourly rate was something like 150 percent of our hourly rates,' he added. 'We made money, the client was happy.' In litigation, firms that charge by the hour can suffer if they are too successful and end a lawsuit– – and the stream of payments from continuing work– – too quickly.

One law firm that recently collapsed, Heller Ehrman, was hurt in part because a number of cases had settled." Billable Hours Giving Ground at Law Firms, by Glator, ibid. Addendum 4.

G

"For years, critics have argued that tracking the work day in six-minute intervals– – the standard billing system used by big law firms – – discourages

creativity and efficiency. Hourly rates are blamed for driving women out of the profession, and for leaving little time for mentoring, pro bono volunteering, or anything like work-life balance. The American Bar Association sounded the official alarm, in 2002. 'The profession's obsession with billable hours is like drinking water from a fire hose,' wrote Justice Stephen Breyer in the forward [sic] to the ABA's report, 'the result is that many lawyers are starting to drown.'" Lisa Lerer, "The Scourge of the Billable Hour," Washington Post. Addendum 5.

H

"In a speech at Northwestern University's law school, [Cisco's general counsel] called the billable hour, 'the last vestige of the medieval guild system to survive into the last century.'" Lerer, ibid.

I

". . . Cisco . . . and several other large corporations have begun to force their law firms into alternative billing arrangements. . .. They say that by eradicating or at least limiting hourly rates, they avoid cost creep, cut their bills, and better predict their expenses." Lerer, ibid, Addendum 5.

J

"[T]here is no more vicious culprit than the practice of basing our fees solely on the time spent on a matter." Scott Turow, The Billable Hour Must Die, ABA Journal, 2011, Addendum 6.

K

". . . I have been unable to figure out how our accepted concepts of conflict of interest can possibly accommodate a system in which the lawyer's economic interests and the client's are so diametrically opposed.

"Looking again to the Model Rules, Rule 1-7 provides in part that 'a lawyer shall not represent a client if the representation involves a concurrent conflict of interest,' which the rule defines as occurring when 'there is a significant risk that the representation of one or more clients will be materially limited by . . . a personal interest of the lawyer.'

"I ask you to ponder for just a few minutes whether that rule can really be fulfilled by hourly based fees."

* * * *

"If I had only one wish for our profession from the proverbial genie, I would want us to move toward something better than dollars time hours. . . .. Somehow, people as smart and dedicated as we are can do better." Turow, ibid, Addendum 6.

L

"Many of you may have heard the one about the lawyer in his early 40s who arrived at the pearly gates and protested to St. Peter that he had been taken too young and deserved to live longer.

"'St. Peter replied that while the lawyer might believe he was only in his early 40s, analysis of his timesheets revealed that he must in fact be in his 90s.'

"[T]he Chief Justice of Western Australia, was making a deadly serious point: time-based billing is a moral hazard." Chris Merritt, "The time is up for outdated system of charging by the hour," The Australian, August 20, 2010. Addendum 7.

M

"Companies . . . are asking for flat or capped rather than hourly fees." The Economist, May 7, 2011, p.14. Addendum 8.

N

"Clients [are beginning] to demand alternatives to the convention of charging by the hour, such as flat, capped or contingent fees. Small and innovative firms began obliging them, and big firms increasingly felt forced to follow suit." The Economist, May 7, 2011, p.74. Addendum 8.

O

"Curbing those long, lucrative hours." Article, All Business, August 7, 2010, Addendum 9.

P

"Billable Hours Giving Ground at Law Firms." New York Times, June 29, 2009. Addendum 10.

Q

"Time to Experiment with alternative billing practices." The Lawyers' Advantage. Fourth Quarter 1988, stating:

> " Recent surveys confirm that, with the exception of individual plaintiff actions relating primarily to personal injuries, well over 90% of all legal fees charged by law firms are still based solely on hourly rates. During the next decade, however, this approach will be replaced on a selective basis with alternative billing practices. For instance: . . . Value-based fees (fees based solely on agreement reached before during, or at the end of the matter, as to the overall 'value' of the services performed." [sic] Addendum 11.

> "Clients are irritated at being overcharged – – through vast hourly fees – – so alternative methods of billing are increasingly being utilized. The Economist, August 11, 2011. Addendum 12.

The time for basing fees upon "billable hours," has passed. The practice encourages inflated time records, and favors the new practitioner over the experienced one.

As an example of the former, consider discovery: typically, the lawyer has the secretary copy the last set of interrogatories (or requests) sent, in a similar case, then bills for several hours, as though each question was painstakingly drafted anew.

As to the latter, the new lawyer might spend hours in researching an issue which the older practitioner has handled dozens (or hundreds) of times. Even at one-half the hourly rate, the new lawyer, then, would be entitled to bill far more than his elder! This system forces the seasoned practitioner to inflate the time spent, as though the hours of research had been necessary.

An experienced attorney could realize upon that experience to cite a decision which could cause her or him to win a $1,000,000 award – – taking all of 15 minutes to dredge up the memory of the case. Should the fee be limited to a charge for only 15 minutes?

An experienced attorney, having honed his skills over a period of many years, might – – in a given case – – negotiate a significant settlement in a period of a few hours, while a neophyte attorney might spend three days in trial, to

achieve the same (or a lesser) result. It would be grossly unfair to hold the experienced attorney to only a token, time-related, fee, for having reached a speedy and more rewarding result for the client.

A defense lawyer, in a $1,000,000 personal injury case, who, in one hour, locates an unimpeachable eye witness, who totally vindicates her client, should not be limited to billing for one hour. With such a restriction the attorney might be encouraged to stretch out the case – – so as to have more billable hours.

VI

QUANTUM MERUIT BILLING APPROVED

In addition, if the client and the attorney contract for payment of fees to be based upon the quantum meruit (as determined by the attorney and agreed to by the client), a billing based thereon should be accepted, regardless of the time required or spent. The Idaho Supreme Court has recently recognized quantum meruit billing, in Farrell v. Whiteman, 146 Idaho 604, 612. See also, Barry v. Pacific West, 140 Idaho 827, 834.

Trial courts are currently allowed to consider "any other factor" deemed appropriate – – which could include quantum meruit contracts – – but typically, they follow IRCP 54 (e)(3)(A), and not (L). In the instant case, the trial court and the district court did not consider IRCP 54(e)(3)(L).

VII

The personal representative is entitled to receive from the estate his attorney's fees incurred at each stage of the proceedings herein (including the appeal).

> "If any personal representative . . . defends or prosecutes any proceeding in good faith, whether successful or not, he is entitled to recover from the estate his necessary expenses and disbursements, including reasonable attorney's fees incurred." §15-3-720 I.C.

In the event of a favorable ruling herein, the appellant should be awarded his attorney's fees on appeal, pursuant to §12-121 I.C.

CONCLUSION

The court below improperly abused its discretion and failed to follow the directive of Idaho statutory and case law regarding the granting of attorney's fees. The matter should be remanded, with a directive to rely upon the contract, and settle the fees as requested, pursuant to IRCP 54(e)(3) (J) and (L), with fees on appeal to appellant.

Respectfully submitted, this September , 2011.

REGINALD R. REEVES, ESQ.
Appellant's Attorney
Cambridge Law Center
Idaho Falls, Idaho

CERTIFICATE OF SERVICE

[IRCP 5(f)]

I HEREBY CERTIFY That on this day I served the foregoing

upon the designated parties, by handing copies, as follows:

RESPONDENT

MICHAEL J. WHYTE, ESQ.
2635 Channing Way
Idaho Falls ID 83404

September , 2011 M. BIRD

Addendum 1

CORPORATE counsel

The Billable Hour: Are Its Days Numbered?

Douglas McCollam
The American Lawyer
November 28, 2005

For about 50 years now the billable hour has been the dominant feature of the legal profession. And for just as long lawyers have been trying to kill it. A group of litigators who usually couldn't agree that the sky was blue without several footnotes qualifying the shade will gladly sing in harmony about the evils of the billable hour and its partner in crime, the daily time sheet. Yet generations of lawyers have accounted for their work lives in six-minute increments. Both reviled and ubiquitous, the billable hour is the cockroach of the legal world.

The basic flaw of the billable hour, say its detractors, is that it puts the financial incentives for lawyers in the wrong place. Back in a more genteel age, grouse many lawyers, when the practice was more of a profession and less of a business, the cost of legal services was determined not by the amount of time a lawyer spent on a matter but on the value he delivered to the client. That model broke down and was replaced by a time-based metric -- which, say critics, encourages firms to overstaff matters, lard their bills with marginally useful services, and draw out cases that might be brought to a swifter conclusion. "Their pricing model follows the production costs instead of following the needs of the buyer," says David Perla, a former in-house lawyer with Monster.com and co-founder of Pangea3, a new company that offers legal services performed by lawyers and scientists based in India at a steep discount to domestic rates. Perla calls the time-based American legal profession "grossly inefficient" and ripe for the competition that companies like his can provide.

Offshoring is only one development posing a threat to the long hegemony of the billable hour. Technology in general has allowed firms to automate certain services for which they used to rack up billable hours. At the same time, as associate costs have soared, so have firm billable hour rates, climbing almost 30 percent during the last five years. That has prodded corporate clients, led by the likes of E.I. du Pont de Nemours and Co. and General Electric Co., to be more aggressive in exploring alternative pricing models for legal services, forcing even longtime outside counsel to bid for the right to represent the company. Fifteen years ago elite firms like Skadden, Arps, Slate, Meagher & Flom could get away with padding charges for photocopies and danish. Today sharp-eyed corporate accountants aren't afraid to put bills from even esteemed outside firms under an electron microscope.

Such aggressive auditing, and a growing recognition of the defects inherent in the billable hour-based system, have led many inside the profession and outside to ask some simple but profound questions. What is it exactly that lawyers are selling to clients? Is it their time or their skill? And, if it is their skill, isn't there a better way to measure that value than by watching a clock?No one has put more effort into trying to drive a stake through the heart of the billable hour than Robert Hirshon, chief executive officer of the Portland, Ore., firm of Tonkon Torp. As president-elect of the American Bar Association in 2001, Hirshon traveled the country taking the collective pulse of the profession. The principal source of dissatisfaction, he says, was the billable hour. Associates complained that outlandish billable hour requirements were ruining their personal and professional lives. Partners resented that the almighty billable had become the single most important measure of their worth to the firm. And general counsel thought the billable hour caused firms to focus more on how much time they could put into a matter rather than to focus on the result obtained for the client. "All these complaints seemed to intersect at the billable hour," Hirshon says.

So Hirshon put together a special commission to examine the impact of the billable hour on the legal profession. The commission surveyed hundreds of law firms and in-house legal departments, quizzing them about their billing practices and reliance on billable hours. The resulting report, issued in late 2002, ran more than 60 pages and fingered the billable hour system for a host of perceived ills in the profession, including bill padding, associate defections and the dearth of pro bono work. The report recommended a host of alternative billing strategies that firms could adopt to replace or augment the billable hour.

But three years later, Jeffrey Liss, co-managing partner of DLA Piper Rudnick Gray Cary and co-chairman of the

commission, admits little has changed. "You do see increased interest in alternative billing arrangements," Liss says, "but the billable hour is still supreme." Liss believes that if firms achieved even the modest goal of moving 30 percent of their work to a non-billable hour basis, the impact on the profession would be profound. But he admits that even within his own firm -- which he sees as at the forefront of the alternative billing movement -- that goal remains distant. And the resistance to innovation isn't coming just from hidebound senior partners. Liss says many clients talk a good game about wanting alternative billing, but when it comes time to do a deal, they get cold feet. "There is a comfort level on both sides with the billable hour," says Liss, noting that it provides an easy metric for measuring and deconstructing fees.

Still, many within the legal industry think the hours are numbered for the billable hour. Joel Henning, a consultant with Hildebrandt Inc., says corporate clients are increasingly aware of the competitive advantages of alternative billing. Henning says his firm is working with a $35 billion company (which he declines to name) on a soup-to-nuts overhaul of its outside legal services. Henning says the ongoing review is clearly showing that even the best firms are inefficient in delivering legal services. "A huge reason is the hourly fee," says Henning. "It simply fosters inefficiency." Henning cites several reasons for this. First, he says, it is inevitable that as associate salaries go up, minimum billing hours go up in tandem. "Partners are going to try to wring every last drop of blood out of associates, and associates miraculously bill whatever number of hours they need to hit bonuses," says Henning. He says that, "as night follows day," firms using this system can't possibly conform to what the client needs. They focus on what the firm needs.

But if the billable hour is such an inefficient system, then how did it come about in the first place? The blame can be traced, as you might suspect, to Harvard University. In 1914 Reginald Heber Smith, a recent Harvard Law School graduate, took over the Boston Legal Aid Society and enlisted the Harvard Business School to help him devise a detailed system to track and manage the organization's finances. One of his innovations was to have the lawyers begin keeping detailed records of their time on different cases. Five years later, Smith, now a well-known figure for his seminal book on legal aid, "Justice and the Poor," joined the new firm of Hale and Dorr as managing partner. He brought his detailed accounting system with him, including a further refinement: the daily time sheet. Recalling his innovation many decades later, Smith wrote that while he thought "nothing could be simpler" than a form on which you recorded the client, the name of the matter and the time you spent working on it, the lawyers at Hale and Dorr hated his new invention. Indeed, Smith wrote, it "seemed to them little better than a slave system."

In devising the time sheet, Smith was heavily influenced by the theory of "scientific management" promoted by Frederick Winslow Taylor, a businessman and researcher who taught at the Tuck School of Business at Dartmouth. Taylor's theory of industrial management stressed the importance of monitoring the time it took workers to complete certain tasks. He even suggested that supervisors keep a stopwatch handy to take accurate measurements of their observations. Taylor's theories of "time study," developed fully in his 1911 book "The Principles of Scientific Management," were hugely influential in nascent business academia. But they were also controversial. In 1912 Taylor was called to testify about his unorthodox ideas before a congressional committee, and subsequently a law was passed banning the use of stopwatches by civil servants. Taylor's critics said scientific management, with its strict emphasis on time, reduced human beings to little more than machines.

None of that deterred Reginald Heber Smith in his efforts to promote the time sheet. In 1940 he published a short book on law firm management that gave full voice to his theories. "The statement that a law office needs an accurate cost accounting system seems revolutionary," Smith wrote, "but if every business concern has to know its costs, why should the law office be immune?" Smith had little patience with those who argued that the law was a profession as opposed to a business. Moreover, Smith had no doubt what value lay at the heart of the practice: "The service the lawyer renders is his professional knowledge and skill," Smith wrote, "but the commodity he sells is time."

To protect that valuable commodity, Smith gave specific instructions on how the time sheet should be produced, what each line and column should contain, what abbreviations of services should be used and what the basic measurement units should be. "We use the hour and the tenth of an hour because it facilitates not only addition but other calculations. ... For convenience in figuring nothing surpasses the decimal system."

Smith's Law Office Organization was enormously influential, eventually going through 11 printings, but it wasn't solely responsible for the triumph of the billable hour. By the 1940s, bar associations in most states had in place flat-fee schedules for various legal services. Indeed, it was often an ethics violation to charge less than the proscribed amount. But the revision to the federal rules of civil procedure in 1938 fundamentally altered the landscape for law firms. The dramatic expansion of pretrial discovery made it difficult for firms to estimate the amount of work that might go into a case. In tandem, the rise of the trial lawyer and mass tort cases in the 1960s and early 1970s rendered much of the old flat-fee system quaint and obsolete. Finally, in 1975 the U.S. Supreme Court delivered the coup de grâce, ruling that statewide fixed-fee schedules violated antitrust law. The way was cleared for the bastard child of scientific management to dominate the profession.

Inevitably, as firms began to use time as the basic measure of their industry, billable requirements for associates and partners became commonplace. As those requirements climbed above 2,000 hours a year at many firms, lawyers and commentators began to talk and write about how the "treadmill effect" created by such high thresholds was ruining the profession. As a baseline, consider a study by the ABA in 1958 when billable hours were first coming into vogue. It found that there were approximately 1,300 fee-earning hours in a year (that assumption included working half-day Saturdays). Studies show that lawyers need to spend about three hours in the office for every two hours of billable time. Ergo, under

that measure (assuming an hour for lunch), billing six hours means working a 10-hour day, which in turn generates between 1,500 and 1,600 hours of billable time a year. Turn in those kinds of time sheets at most firms today, and you'll get back a pink slip.

The day hasn't gotten any longer, so where do the additional 500 hours that many lawyers bill each year come from? Out of their souls, to hear most lawyers talk about billable requirements. To hit billable targets, they sacrifice their personal lives, their public service and often their physical and psychological health. One of the things Hirshon noticed in his travels for the ABA was how lawyers who had gone in-house rejoiced in being free of the time sheet. It wasn't that they were working any less, Hirshon says, it was that they were liberated from the demeaning ritual of having to account for their professional lives in tenth-of-an-hour increments. Their fate no longer rested on the time they billed, but on the results they achieved. They had been unharnassed from the clock, freed, as Hirshon puts it, from the "tyranny of the billable hour."

The question remains then: If the billable hour is so unpopular, why hasn't it been replaced? For starters, it's a huge moneymaker for firms. To a large extent, reliance upon the billable hour is responsible for the pyramid structure of the modern law firm. With legions of associates toiling away on behalf of a narrow band of partners, the modern megafirm generates huge revenue. Take away the billable hour, however, and the foundation of the pyramid collapses. If the basic commodity sold becomes knowledge, not time, then the modern megafirm suddenly begins to look like an obsolete smokestack industry.

That's certainly the view of litigator Fred Bartlit Jr., whose 60-lawyer litigation shop Bartlit Beck Herman Palenchar & Scott, has more or less done away with the billable hour in favor of flat-fee billing. "I go to these legal conferences," Bartlit says, beginning a well-worn harangue, "and all anybody talks about is increasing profits by taking billables from 2,000 to 2,200 hours. It's all quantity over quality." Bartlit says law firms should radically rethink their business model. "Most firms have 70 percent too many associates and way too much real estate, says Bartlit. "But when the basic metric is 'how long can we take to do something?' that's not going to happen."

But the Bartlit Beck "diamond-shape" model, which features small teams with a partner at the center, would seem to have some obvious flaws. Strict flat-fee billing might work for a boutique firm, but wouldn't it inhibit growth past a certain point? Further, at some point big litigation law firms have to put some wing tips on the ground. Who is going to vet those 3 million pages of documents prior to trial?

Bartlit rejects such criticisms. He says larger firms are actually better able to sustain the occasional miscalculations on flat-fee billing. As for discovery, Bartlit admits his firm needs to team up with larger shops on some cases to handle the workload. And here is where Bartlit's vision meets Pangea3's vision. He says in the near future, firms will be able to rationalize their structure by farming out such labor-intensive tasks to computers and offshore workers. To some extent, that day has already come. Bartlit says that his firm has run blind tests pitting document discovery software against a document review team of lawyers, and the software performed as well or better than its human counterpart. Bartlit concedes the system may not be perfect -- but then neither are associates, and they cost a hell of a lot more.

"All these firms are staffed for the 100-year flood," says Bartlit, "it's just a bunch of excess capacity." He says lawyers should let go of the idea that every last stone in discovery has to be turned over by someone with a J.D. on the wall. "I've never been surprised by a document in court in my life," he says, "but even if you had 100 lawyers working on a case, it's possible it could happen." Moreover, Bartlit says the psychic toll the modern discovery practice takes is huge. "I don't have a single friend who is really happy in a big firm," says Bartlit, "and being a trial lawyer should be the greatest job in the world."

Using his model, Bartlit says, firms wouldn't have to hire 80 lawyers a year, could do proper mentoring and training and could work in small teams that produce higher-quality work. "We do all that [at Bartlit Beck]," Bartlit says, "and it all comes from abandoning the billable hour."

But not everyone is ready to do away with the trusted hourly rate. J. Warren Gorrell, managing partner of Washington, D.C.'s Hogan & Hartson, says his firm is open to alternative billing arrangements, but he doesn't foresee the end of billable hours anytime soon. "That structure may work for more routine stuff, high-volume work or repeat work, but on bet-the-ranch matters, you are going to get a premium." Gorrell says that it is precisely Hogan's ability to muster a big contingent of lawyers over a large geographic area that makes the firm valuable to many of its clients. He notes that Hogan is currently handling a piece of litigation for a client that involves 30 lawyers in ten different offices.

Gorrell does agree, though, that more and more clients are exploring alternatives to the straight hourly billing: "I'd say that the number of RFPs [requests for proposals] on major projects is probably ten times higher than it was five years ago." Clients are looking to cut down on the number of firms they use, consolidate the knowledge base and shift some of the financial risk over to outside lawyers in return for repeat business. Gorrell also says he sees a lot of interest in a sliding scale on fees. "We are seeing a lot of 'we want a 2 percent discount for prompt payment' or 'we want a 10 percent discount if we give you $10 million in business,'" says Gorrell.

That squares with what Liss at DLA Piper Rudnick is seeing as well. Liss says he meets with firm clients often and pitches alternative fee arrangements, but has relatively few takers. Liss says he'll talk about flat fees for an individual case or

transaction, or a flat fee to handle a whole portfolio of business, or a flat fee to do all the client's legal work, or a flat fee with a cap on the high and low end so that both the firm and the client are protected or a flat fee with a performance bonus for positive results. "They always appreciate the offer," Liss says, "but usually they stick with the hourly rate -- with a 5 percent discount."

Why firms remain wedded to the time sheet is understandable. But it's more surprising that corporate clients don't have a bigger appetite for alternative billing. Anastasia Kelly, MCI Inc.'s general counsel, co-chaired the ABA's committee on the billable hour. She thinks alternative billing is great, but admits she hasn't done much of it in her two-plus years of running the legal division for the telecom giant. In part, that's due to circumstances -- MCI has been mired in bankruptcy, and been a takeover target for both Qwest Communications International Inc. and Verizon Communications Inc. Even so, Kelly says that part of the impediment to alternative billing is just inertia.

"The billable hour is easy, that's the reality of life," says Kelly. "It doesn't always reflect the value of the work being done, but it's predictable and familiar." In her former job as general counsel for Sears, Roebuck and Co., Kelly says the company did do value billing on commodity-type legal work, such as certain repetitive contracts and agreements. "Those don't take a rocket scientist," she observes. But for more complex transactional work, she says getting the valuation right for a flat fee would be difficult. "You never know how a transaction is going to go, how long it will last, and what might get in the way," she says. Kelly thinks such an arrangement could work if a company did many small acquisitions, but for big-ticket deals she remains skeptical. Still, she is optimistic about the future of alternative billing. "We had a toe in the waters, and now we are up to an ankle," she says. "In a couple of years we'll be up to our knees. But someone is going to have to dive all the way in [in] order to get a breakthrough."

But before they do that, lawyers need to make sure there is enough water in the pool. The essence of alternative billing is risk shifting. While trial lawyers are used to the vagaries of the contingency system, defense firms remain much more risk averse. So long as they keep submitting time, lawyers are highly paid service workers with little exposure. As soon as they break the bonds of time, they become more independent and free of time-sheet-induced drudgery, but also free to fail. Accepting more risk will entail a basic shift in the relationship between lawyers and clients. For now, relatively few firms or clients seem inclined to make that change. Until they do, lawyers will have both predictability and chronic dissatisfaction. They will have unsatisfying work, but they will have steady profits. In short, they will have the hours.

Addendum 2

On My Mind

Kill the Billable Hour

Evan R. Chesler, 12.18.08, 06:00 PM EST
Forbes Magazine dated January 12, 2009

Lawyers should bill the way Joe the Contractor does.

Evan R. Chesler

I'm a trial lawyer. I bill by the hour. So do the associates who work for me. I have lots of clients, so I can pretty much work, and bill, as much as I want. This needs to be fixed. Yes, you read that correctly.

Clients have long hated the billable hour, and I understand why. The hours seem to pile up to fill the available space. The clients feel they have no control, that there is no correlation between cost and quality.

Addendum 3

legalaffairs THE MAGAZINE AT THE INTERSECTION OF LAW AND LIFE

Reviews

THE HOURS

The short, unhappy history of how lawyers bill their clients.

By Niki Kuckes

Law firms bent on making as much money as possible treat associates "very much as a manufacturer would treat a purchaser of one hundred tons of scrap metal," Chief Justice William Rehnquist observed in the mid-1980s. He explained the firms' attitude like this: "If you use anything less than the one hundred tons you paid for, you are simply not running an efficient business."

The chief justice understood that the modern law firm, once revered as a brotherhood, is now in many ways indistinguishable from the corporate clients it serves. Monthly financial reports, profit targets—these are the fodder of partnership meetings at most large firms. Collegial discussions of cases in progress and debates about the good sense of one legal strategy versus another are largely reduced to hasty e-mails written from the airport.

The product that these law corporations make—and the source of the notion that attorneys are as interchangeable as widgets—is the "billable hour." Both partners and associates are routinely required to bill clients a high number of hours; the current range at most large firms is between 1,800 and 2,000 a year. The benefits of seniority rarely include the opportunity to work less—only the most successful rainmakers are exempt from the pressure to bill time. As one associate puts it, "It's like a pie-eating contest where first prize is all the pie you can eat."

The relentless pressure to turn time into money has robbed the legal practice of many of its joys and satisfactions—those that come from giving good advice, avoiding a lawsuit, preventing a corporate bankruptcy, sparing a client prison time, or negotiating a successful deal. These are the landmarks that lawyers recall when they review their careers, but their value isn't reflected in the way lawyers bill. With good reason, lawyers come to feel that what matters isn't how they do their work but how much work they do. "The billable hour is fundamentally about quantity over quality, repetition over creativity," Robert E. Hirshon, the president of the American Bar Association, recently observed.

Why has the billable hour, uncommon only 50 years ago, become so entrenched and powerful? The answer begins with the corporatization of law practice. As law firms expand or merge, they must search for measures to predict income, expenses, and budget. Billable hours present a ready standard because they can easily be measured, compared, and reduced to "realization rates" (which compare hours worked with the fees collected on those hours). They can be translated into precise expectations that can be used to guide lawyers' performance. It's no wonder, then, that attorneys complain of feeling like piecemeal workers in a factory.

The billable hour's appeal as a management tool is also its greatest threat. Treating legal services as a

commodity that can be measured in units of time diminishes the importance of both the quality of the work produced and the results achieved. Few other industries would thrive if they measured productivity by the time their workers spent without regard to what those workers created. The standard invites inefficiency, not to mention fraud. The potential for conflicts of interest is obvious—it's in the firm's financial interest for lawyers to spend as many hours as possible, while the client's interest is best served by limiting the time spent.

Most firms break billable hours into pieces, typically charging clients for each six-minute increment expended by a lawyer or paralegal. This method of billing requires a degree of precision that is virtually impossible to achieve. Still, the conscientious lawyer strives to record, in his or her daily diary, each telephone call, meeting, letter, memo, draft agreement, research project, and document review. The result is relentless time-keeping from arrival to departure each day, and often at home again at night.

Firms' reliance on the hour as their billing currency emerged in the 1950s. In the country's early history, state law strictly limited legal fees, which were generally paid by the losing side in a case. Lawyers supplemented their income with bonuses from satisfied clients—like tips for a waiter—or with annual retainers. As economic regulation fell out of political favor in the 19th century, however, such maximum-fee laws were repealed. By the early 20th century, lawyers used a combination of billing methods: set fees for particular tasks, annual retainers, a discretionary "eyeball" method, and contingency fees, which the ABA approved as ethical in 1908. They rarely billed by the hour.

In the late 1930s and 1940s, state bar associations eager to hike legal fees started publishing minimum fee schedules that set standard prices for different services. The schedules would "suggest" one fee for handling a contested divorce, for example, and another for drafting a will. While nominally voluntary, schedules were enforced by the threat of disciplinary action against a lawyer whose fees were regarded as too low. The Virginia State Bar, for example, warned that attorneys who "habitually" charged less than the suggested fees would be presumed guilty of misconduct. The ABA's model ethical code, which was in effect until 1969, said that it was unethical for an attorney to "undervalue" his legal services.

But as time passed and the practice of law became more complex, fee schedules and other flat-fee arrangements, like re-tainers, proved increasingly unworkable. The reform of the federal rules of civil procedure in 1938, which were later copied by the states, dramatically expanded lawyers' workloads before civil trials by extensively reworking the pretrial discovery rules. These changes have been credited with transforming "trial lawyers" into "litigators," who spend a lot more time pre-paring cases and exchanging motions with the other side than they do appearing in court. As the work involved in any given case became unpredictable—and subject to vagaries beyond the lawyer's control—it became difficult to set a reasonable flat fee in advance. Over the next few decades, regulation of business activities increased dramatically, which meant that transactional work also increased in complexity and became harder to price.

The Supreme Court killed set fee schedules entirely in 1975, declaring that they were a "classic illustration of price fixing" that violated federal antitrust laws. Meanwhile, clients had grown impatient with "eyeball" techniques of legal billing, which left them unsure how a lawyer arrived at his gross fee. Against this backdrop, hourly billing appealed to clients and lawyers as a more transparent way to value legal services.

Hourly billing allowed clients to "correlate the 'product' that they were buying to the products that they themselves produced and sold," one commentator observes, and fit in well with the move toward business accounting methods. In the process, noted Geoffrey Hazard, a professor of legal ethics at the University of Pennsylvania, "a subtle transformation occurred: The time sheet—created as a control on 'inventory'—now became the 'inventory' itself."

It didn't take the profession long to figure out that the billable hour could be used to turn the practice of law into a more profitable business. In 1958, an ABA committee put out a pamphlet called "The 1958 Lawyer and His 1938 Dollar." The pamphlet lamented the "economic plight" of lawyers and their failure to keep pace with the earnings of other professions, particularly (and gallingly) the income of doctors and dentists. By devoting themselves unduly to the high ideal of "devotion to public interest," the committee concluded, lawyers were flopping as businessmen. The ABA urged them to take a businesslike look at their work habits—beginning with time records, the lawyer's "sole expendable asset."

For the next decade, the bar mounted a nationwide campaign to "preach the gospel that the lawyer who keeps time records makes more money," as one ABA speaker put it. Initially, hourly fees were used as a baseline, and adjusted to account for other factors like a project's success. By the late 1970s, however, pure hourly billing came to prevail. Eventually, it became the standard for nearly every variety of legal work. There have been sporadic efforts to encourage the use of alternative methods like "value" billing (focusing on the value of work performed rather than time spent). But the billable hour has been surprisingly resistant to reform.

To improve productivity, law firms began adopting policies requiring attorneys to bill a certain number of minimum hours each year. It seemed like a harmless enough step—until the number of those hours began to rise steadily beginning in the '80s. Firms raised their hours requirements to maximize the profits of partners and, most recently, to pay for a dramatic increase in associate salaries fueled by the fear of losing young lawyers to the dot-com boom. By 2001, large Washington, D.C., law firms typically asked associates to bill between 1,950 and 2,000 billable hours a year—and in other cities nationwide, most firms reporting minimums required almost as many hours a year.

These standards exert serious pressure, whether they are openly described as "quotas" or euphemistically referred to as "targets." Often, they are enforced with financial incentives or penalties. Associate bonuses are routinely tied to billing a specific number of hours, which means that when a bonus kicks in at 2,000 billable hours, few associates will end the year with less. Partners are also often required to bill a set number of hours, usually slightly lower than those expected of associates. Even where that's not the case, a partner's hourly output still matters for important firm decisions like compensation, hiring needs, and, in a firm with several offices, evaluation of the overall performance of the office where a lawyer works.

It's striking to compare today's expectations to a lawyer's reasonable workday in 1958. In that year, the ABA announced that unless a lawyer worked overtime, there were "only approximately 1,300 fee-earning hours per year." This assumed a five-day workweek plus half-days on Saturday. At that time, the ABA set a "realistic" goal of five or six billable hours a day. Today, a billable hour target of 1,300 billable hours a year would amount to a civilized part-time schedule—the equivalent of a three-day, part-time workweek in most large firms.

Billing 2,000 hours a year may not seem onerous. The total can be reached in just over eight billable hours a day, setting aside four weeks of the year for vacation and national holidays. But studies consistently show that a lawyer must spend three hours in the office for every two hours of billable work. Lawyers can't simply bill time. They have to read and respond to mail and firm memos, go to meetings, read legal publications, and eat lunch—not to mention kib-bitz with colleagues, if not friends.

To do all of this and make the 2,000-hours target, a lawyer must spend the equivalent of 12 hours in the office for each working day. Since the day hasn't gotten longer since 1958, the honest lawyer who commits to working "full-time"—to a schedule of 2,000 billable and thus 3,000 total hours—is giving his life to the firm. This is the "tyranny of the billable hour," as Hirshon of the ABA puts it. Lawyers who have left private practice speak of the relief and pleasure of not having to record their time. The pressure is particularly

acute when a case is in hiatus, or when a firm goes through a downturn in business. However little work the attorney may have to do, the billable-hour statistics continue to be compiled by the firm, day after day.

The loss of collegiality that lawyers bemoan isn't the only casualty of the time pressure. The opportunity to do free work for poor clients or chosen causes—for many lawyers, the most satisfying work of their legal career—gets eaten away. Instead, tedious but hour-consuming tasks like travel, document review, and proofreading corporate reports become valued assignments. An associate who wants to see his kids must pass on taking a course in trial advocacy or running for a position on a bar committee. He also can't find time to write articles or have lunch with business contacts that could help him become a partner. Partners are similarly reluctant to spend time working with associates to help them sharpen their skills, or taking on other non-billable tasks like serving on firm committees dealing with pro bono cases.

The need to bill 2,000 hours a year also means that "there are bound to be temptations to exaggerate the hours actually put in," as Chief Justice Rehnquist said. The possibilities for fraud abound, though fraud is often hard to detect. Lawyers can cheat by writing down hours they didn't work or by exaggerating the hours they did. They can credit themselves for hours worked by paralegals and secretaries. They can bill one client for work already paid for by another, or double-bill two clients for the same hours. The ABA said in 1993 that it's unethical to bill one client for travel time and a second client for work performed en route, but surveys show that the practice has not been eliminated.

Academics tend to see fraudulent billing as endemic; practitioners tend to see it as the exception rather than the rule. The reported cases suggest that most of the lawyers whom the bar disciplines for questionable billing are solo or small-firm practitioners. In many of these cases, the dispute is about such issues as whether a $1,000 fee should have been $500. Recently and notoriously, however, senior partners in major law firms have padded their bills, forcing clients to pay them millions of unearned dollars. When Webster Hubbell, the former high-ranking Clinton Justice Department official, pleaded guilty to defrauding the Rose Law Firm and its clients of $500,000, the charges against him included bill inflation. Billing chicanery has also led to the disbarment or resignation from the bar of partners at such nationally known firms as McDermott, Will & Emery, Latham & Watkins, Mayer, Brown & Platt, and Hunton & Williams.

Some lawyers who have left private practice point to the billable hour as a central motivation for their departure. Patrick Schiltz is a law professor who, along with his wife, left a firm. He gave up a stake in the very large fees earned by his firm from the Exxon Valdez oil-spill litigation. He tells his students that they are entering a profession that is "one of the most unhappy and unhealthy on the face of the earth—and, in the view of many, one of the most unethical." Much of the blame, he has concluded, lies with "the hours." "You should not underestimate the likelihood that you will practice law unethically," Schiltz advises new lawyers. The problem, he warns, will "begin with your time sheets."

The organized bar, which so enthusiastically urged the billable hour on the legal profession 50 years ago, has developed its own doubts in more recent years. In 2001, the ABA assembled a Commission on Billable Hours, and this August it conceded that "required hourly minimums . . . can lead to questionable billing practices ranging from logging hours for doing unnecessary research to outright padding of hours." The commission expressed concern, as well, that the billable hour "penalizes the efficient and productive lawyer" and causes a host of harms, including damage to firm culture, loss of time for pro bono work, duplication of effort, and a disconnect between the value of projects and the legal fees generated.

Still, the commission issued a report that is more pragmatic than crusading. While expressing concern about the weaknesses of reliance on billable hours, the committee bowed to the reality that "many, perhaps most, firms continue to believe in minimum hourly requirements." In contrast to its 1958 conclusion that billing 1,300 hours a year is a reasonable full-time job, the report endorses advising associates that 1,900

hours of billable client work is the amount "sufficient for evaluation and compensation purposes." The commission also recommends making plain to associates that on top of those 1,900 hours, they should generally expect to put in 100 hours of firm service, 100 hours of pro bono work, 75 hours of client development, 75 hours of training and professional development, and 50 hours of service to the profession. That's 2,300 hours a year—many long days and weekends.

What's the alternative? Lisa G. Lerman of Catholic Law School has suggested that the practice of imposing billable-hour requirements be "abandoned." If the ABA Committee considered that idea, it apparently concluded that scrapping the billable hour strays too far from the realities of running a law firm as a business. While the report's model policy for firms ostensibly espouses "no set hard-and-fast minimum levels" of billing, it sends a mixed message, simultaneously giving associates "guidance" about the typical level of effort that the firm "expects in order to meet its revenue and profitability goals." While decrying practices that rigidly tie compensation to billable hours, the report also recognizes the "imperative of rewarding productivity—often measured in billable hours."

Ultimately, the ABA recommends warning associates that deliberate inflation of time will not be tolerated—an important step, but one that puts the onus on associates to put in the time and to do so honestly, without addressing the weariness and dissatisfaction that comes with the billable hour (or the billing practices of law firm partners). The ABA also promotes alternative billing methods, such as fixed fees, contingency fees, and bonus arrangements.

For the foreseeable future, though, the billable hour is likely to remain the bane of a lawyer's work life. It's also likely to provide a shorthand for much of what ails the legal profession. Perhaps the best hope for restoring satisfaction to lawyers in practice, ironically, is that corporate clients will insist on changing the prevailing method of pricing legal services—something that law firms seem to have neither the ability nor the will to do....

Niki Kuckes *is a partner at Baker Botts LLP in Washington, D.C., and is currently serving as a Distinguished Practitioner in Residence at Cornell Law School. This article presents her views and not necessarily those of the law firm.*

Addendum 4

January 30, 2009

Billable Hours Giving Ground at Law Firms

By JONATHAN D. GLATER

Lawyers are having trouble defending the most basic yardstick of the legal business — the billable hour.

Clients have complained for years that the practice of billing for each hour worked can encourage law firms to prolong a client's problem rather than solve it. But the rough economic climate is making clients more demanding, leading many law firms to rethink their business model.

"This is the time to get rid of the billable hour," said Evan R. Chesler, presiding partner at Cravath, Swaine & Moore in New York, one of a number of large firms whose most senior lawyers bill more than $800 an hour.

"Clients are concerned about the budgets, more so than perhaps a year or two ago," he added, with a lawyer's gift for understatement.

Big law firms are worried about their budgets, too. Deals are drying up, and only the bankruptcy business is thriving. Two top firms, Heller Ehrman and Thelen, have collapsed in recent months. Others have laid off lawyers and staff. So cost-conscious clients may now be able to sway long reluctant partners to accept alternatives.

The evidence of a shift away from billable hours is, for now, anecdotal, as few surveys exist. But partners at a half-dozen other big bellwether firms and lawyers at corporations, who sometimes engage outside counsel, say they are more often seeing different pay arrangements.

Mr. Chesler, who is an advocate of the new billing practices, said that instead of paying for hours worked, more clients are paying Cravath flat fees for handling transactions and success fees for positive outcomes, as well as payments for meeting other benchmarks. He said that such arrangements were still a relatively small part of his firm's total business, but declined to discuss billable rates and prices in detail.

The system of billing by the hour has been firmly in place since the 1960s; keeping track of time spent provided a rationale for the amount charged. In earlier, perhaps more trusting times, firms stated a price "for services rendered," without explanation.

But one has only to eavesdrop on a table of law associates comparing their workloads to get a sense of how entrenched the billable hour is, creating a pecking order among lawyers, identifying the best as the busiest and the most costly.

With a sigh that is simultaneously proud and pained, lawyers will talk about charging clients for 3,000 or more hours in a year — a figure that means a lawyer spent about 12 hours a day of every weekday drafting

motions or contracts and reviewing other lawyers' motions and contracts.

"Does this make any sense?" said David B. Wilkins, professor of legal ethics and director of the program on the legal profession at Harvard. "It makes as much sense as any other kind of effort to measure your value by some kind of objective, extrinsic measure. Which is not much."

To be sure, lawyers may be talking a good game but secretly hoping that the economy will bounce back and everything will return to normal, said Frederick J. Krebs, president of the Association of Corporate Counsel, whose members work in the legal departments of corporations and other organizations. He said that lawyers cheerfully lamented the bad incentives created by billable time for years, even as they grew rich from the practice.

"I like to paraphrase Churchill," Mr. Krebs said. "In all these conversations, never has so little been accomplished by so many for so long. It just hasn't happened."

But the crashing economy may achieve what client complaints could not, Mr. Krebs added. "We may well be at a tipping point here."

Greed may also encourage lawyers to change their payment plans. Law firms are running out of hours that they can bill in a year, said Scott F. Turow, best-selling author of legal thrillers and a partner at Sonnenschein Nath & Rosenthal in Chicago.

"Firms are approaching the limit of how hard they can ask lawyers to work," he wrote, in an e-mail response to a reporter's query. "Without alternative billing schemes, lawyers will not be able to maintain the rapid escalation in incomes that big firms have seen."

A recent study released last year by the Association of Corporate Counsel showed a rise in the number of companies paying by the hour — but that covered the spring and summer, before the worst of the downturn.

Many smaller firms and solo practitioners have long offered to perform services, like mortgage closings, for flat fees. Plaintiff lawyers also often work on a contingency basis, receiving a percentage of any awards.

"What we do in our business litigation is charge clients some kind of monthly retainer, which gets credited against an eventual recovery," said John G. Balestriere, a partner at Balestriere Lanza, a Manhattan firm with five lawyers. "It's a lot easier for us to tell a client, 'We want to do this, we want to push for summary judgment,' " he said, and so avoid a lengthy, costly trial.

When not paid by the hour, lawyers' approach to their work changes, said Carl A. Leonard, a former chairman of Morrison & Foerster who is now a senior consultant at Hildebrandt International, which advises professional services firms.

In one case, he said, Morrison & Foerster negotiated a fixed fee for defending a company in court, covering work up to the point of a motion for summary judgment.

On top of the fee, if the case settled for less than what the company feared having to pay if it lost in court, the law firm got a percentage of the amount saved. The arrangement made sense when the goal was to

resolve the dispute quickly, Mr. Leonard said.

Lawyers on the case negotiated a settlement for much less than the client's worst-case number, Mr. Leonard said. "The effective hourly rate was something like 150 percent of our hourly rates," he added. "We made money, the client was happy."

In litigation, firms that charge by the hour can suffer if they are too successful and end a lawsuit — and the stream of payments from continuing work — too quickly. One law firm that recently collapsed, Heller Ehrman, was hurt in part because a number of cases had settled.

That collapse highlights the risk to law firms experimenting with other payment arrangements: If lawyers set too low a price, they lose money. Many lawyers may not be good enough businessmen to pick the right price, said Mr. Krebs, of the Association of Corporate Counsel.

"The difficulty is, we don't really know what it costs us to do something," he said. But the biggest stumbling block to alternative fee structures may be the managing partners at law firms, who will have to overhaul compensation structures to reward partners and associates for something other than taking a long time to do something.

"I don't think law firms have completely come to grips with that issue," said J. Stephen Poor, managing partner at Seyfarth Shaw in Chicago. "But they need to start coming to grips with it very quickly."

This article has been revised to reflect the following correction:

Correction: February 2, 2009
An article on Friday about some law firms' rethinking the use of the billable hour misspelled one of the names in the law firm of Evan R. Chesler, who favors alternative billing practices. He is presiding partner at Cravath, Swaine & Moore — not Swain.

Addendum 5

PRINT BACK TO SLATE

Slate

JURISPRUDENCE

The Scourge of the Billable Hour

Could law-firm clients finally kill it off?

By Lisa Lerer

Posted Wednesday, Jan. 2, 2008, at 12:17 PM ET

It's a classic, needling lawyer's question: Spend two hours at your daughter's soccer game, or bill the time and pocket $1,400?

For years, critics have argued that tracking the work day in six-minute intervals—the standard billing system used by big law firms—discourages creativity and efficiency. Hourly rates are blamed for driving women out of the profession, and for leaving little time for mentoring, pro bono volunteering, or anything like work-life balance. The American Bar Association sounded the official alarm in 2002. "The profession's obsession with billable hours is like drinking water from a fire hose," wrote Justice Stephen Breyer in the forward to the ABA's report, "the result is that many lawyers are starting to drown."

The criticisms lobbed by academics, associates, and bloggers have had a negligible impact. Making such a significant change takes a more powerful force in law firm life: the client. And now, finally, the companies that pay millions in hourly rates are striking back, forcing their law firms to cut some tough, nonhourly fee deals. If anyone can tame the billable beast, it's the clients who feed it.

Companies are attacking the billable hour out of a growing frustration with rising legal costs. "Put most bluntly, the most fundamental misalignment of interests is between clients who are driven to manage expenses, and law firms which are compensated by the hour," said Cisco's general counsel, Mark Chandler. In a speech at Northwestern University's law school last January, he called the billable hour, "the last vestige of the medieval guild system to survive into the 21st century."

Hourly rates first took hold in the mid-1950s. At the time, they were encouraged by clients, who then saw them as a means to more transparent bills, and by bar associations hoping to gin up profits. A 1958 ABA pamphlet suggested a quota of 1,300 hours a year for associates. By the mid-1980s, large firms demanded closer to 1,800 hours, and top bonuses and making partner in big cities demands closer to 1,800 hours billed (which translates into many more hours worked). The trade-off at top law firms, though not at others, are starting salaries of $160,000 and partner pay of

more than $1 million. Hourly rates have increased annually by 5 percent since 2001, according to ACC data, and for a few partners in the legal stratosphere, reached the $1,000 an hour mark.

Lawyers who work in-house for corporations—making only as much as a third or fourth-year law firm associate—think their companies, when they outsource legal work to firms, unintentionally fund the salary extravaganza. And so Cisco, Pitney Bowes, Caterpillar, and several other large corporations have begun to force their law firms into alternative billing arrangements. The companies push flat fees and volume-based discounts, and ban young associates from working on their business, hoping to avoid paying through the nose for work that could be done more cheaply by paralegals or temp lawyers. They say that by eradicating or at least limiting hourly rates, they avoid cost creep, cut their bills, and better predict their expenses.

Law firms, notoriously risk-averse, are reluctant to go along. Only about a quarter of companies used alternative billing last year, according to a 2006 study commissioned by the Association of Corporate Counsel, an industry group of in-house lawyers.

If this is the future of the legal world, then the business will eventually spilt into three fairly autonomous markets. The top end of the spectrum will remain largely unchanged. Companies will still pay hourly rates to hire white-shoe law firms for specialized, bet-your-company kinds of work. On the opposite end, however, clients will stop taking their rote legal work to law firms altogether. Companies already outsource relatively simple matters like document review to consulting services. And as technology improves, more programs will let companies handle their own contracts online.

In the murky middle between one-of-a-kind advice and dime-a-dozen contracts, the push for alternative arrangements will prevail. Cisco, for example, already pays a fixed fee to law firms for filing patents at the Patent and Trademark Office. The firm's total charge must decrease by at least 5 percent each year, as a firm becomes more efficient; if not, it is replaced with a smaller one willing to take the work.

Smaller, regional firms are slowly starting to go along. If companies continue to snap up the relative bargains on offer, more work will be spread across the corporate law spectrum. And maybe, lawyers will get off the clock and find that they like what they do, when they don't have to do it all the time.

---

sidebar

Return to article

To steal a phrase from a famous ex-lawyer, we live in a world of two legal Americas. Salary distribution data from 2006 neatly breaks out into a two-peaked curve. On one end, grads from top 25 law schools made about $135,000. On the other, graduates from second or third-tier law schools average about $50,000.

Lisa Lerer writes for the Politico.

Article URL: http://www.slate.com/id/2180420/

Also In Slate

- The Reform of "Swipe Fees" Is a Victory for Small Business but Not Consumers
- *Super 8*: Elle Fanning Is Now Officially My Favorite Fanning
- Why Does Everyone Hate LeBron James? Blame Michael Jordan.
- Google Should Invent Google Kids: A Search Engine That Filters the Web for Children
- Help! I Go To Strip Clubs When I Travel for Business. That's Not Cheating, Right?

Addendum 6

Cover Story

The Billable Hour Must Die

It rewards inefficiency. It makes clients suspicious. And it may be unethical.

Posted Aug 1, 2007 3:54 AM CDT
By Scott Turow

Illustration by Jeff Dionise

SIDEBAR: New Routes into the Corporate Door

Three summers ago, my wife and I were driving my two older kids to the airport. The academic year was about to resume. The younger child, my son, was returning to college; the older, my daughter, to law school.

"Say," I heard my son ask his sister in the backseat, "what do you think you'll do when you get done with law school?" My daughter expressed some uncertainty but ended up answering, "I think I'll become a litigator."

I nearly hit the brakes.

"Oh," I heard myself moan, "don't be a litigator."

My advice to my daughter had the usual effect—another demonstration of Newton's third law, the one about equal and opposite reactions, a rule that also applies to parental advice. Before the academic year was over, my daughter had enrolled in a legal clinic and tried her first and second lawsuits. It was those experiences, rather than anything she heard from me, that led her away from the courtroom.

But, candidly, I was shocked by my own reaction. Because for the last 20 years I have chosen to continue my occasional role as a litigator, despite having the option not to do so thanks to my literary career. I have always believed that I've had a charmed life as a courtroom lawyer. When I left law school, I could not imagine becoming anything other than a litigator. The courtroom was where the law was made, where the fundamental struggle to fit the law to facts took place.

The people writing contracts were, in my youthful view, not much different from consultants. Although I have learned to love and appreciate hundreds of transactional lawyers in the years since, I notice, in looking over my novels, that I have not yet had a hero who is any other kind of a lawyer but a litigator. My protagonists have been prosecutors, criminal defense lawyers, a judge, a tort lawyer, a commercial litigator—even journalists. But no deal guys or gals. In the restricted zone of my imagination, it's the litigators who are the real thing.

So why is it—given the satisfaction I've taken from being a litigator—that some piece of my heart shrieked out in

opposition to the idea of my child doing the same?

CONTEMPORARY WOES

I believe what motivated my outcry, in a few words, is that I think it would be hard for someone starting today to have it as good as I have had it. The ratio of pain to pride has grown too high. And the contemporary environment has become much less congenial to aspects of the lawyering craft that deeply pleased me. We all hear the complaints from our colleagues, especially those in my age range who've been doing this now for decades. For too many litigators, our life increasingly is a highly paid serfdom—a cage of relentless hours, ruthless opponents, constant deadlines and merciless inefficiencies.

By now it's obvious that the U.S. Supreme Court's 1977 decision in *Bates v. Arizona*, which invalidated on First Amendment grounds the longtime bar on lawyer advertising, was the opening cannon shot that essentially set off the competitive war in our profession. In doing so, it did no favor to lawyers' lifestyles. The free flow of information about who is making what that soon followed—courtesy of *The American Lawyer*—ushered in the big-firm star system, in which rainmakers rule. Because they are the lawyers who can most easily set up shop elsewhere, the threat posed by that mobility in turn has cued the struggle in every firm to ensure that incomes remain high, especially at the top of the pyramid.

Not that we, in the bar, have any right to complain. The fierce competition that now characterizes the business of being a lawyer is exactly what the market requires. No matter how much we'd like it to be otherwise, lawyers can't claim any privilege to live by different rules from everybody else in our economy.

But I still believe that lawyers in general, and litigators in particular, are yet to confront the realistic limits of that competitive environment. And in this regard there is no more vicious culprit than the practice of basing our fees solely on the time spent on a matter.

Dollars times hours sounds like a formula for fairness. What could be more equitable than basing a fee on how long and hard a litigator worked to resolve a matter? But as a system, it's a prison. When you are selling your time, there are only three ways to make more money—higher rates, longer hours and more leverage. As the years have gone on, the push has continued on all three fronts.

HOURS AMOK

Let me be clear: i don't think there is anything wrong with lawyers making money. There is a unique satisfaction in representing somebody well and being rewarded for it in a manner commensurate with the effort and skill required. I am not engaged here in a jeremiad aimed at getting litigators to join in vows of poverty, or even to agree to make less. I believe enough in the free market to know that if what we ask our clients to pay us wasn't worth it to them, they wouldn't continue to do it. My concern is with the external effects of the system we are now following.

Consider, for example, the consequences of dollars times hours for those entering the profession. When I left the government for private practice in 1986, the hours expectation for young lawyers was 1,750-1,800 hours a year in the large Chicago firms. Today it's 2,000-2,100—even 2,200 hours. And the only real outer boundary is that there are 24 hours in a day—and 168 in a week. Increasingly, if we allow time for trivialities like eating, sleeping and loving other people, it is clear, as a simple matter of arithmetic, that we are getting close to the absolute limit of how far this system can take us economically.

DIMINISHING RETURNS

More tellingly, the prospects for success for lawyers have markedly diminished over the years. Virtually all firms today make fewer partners and take a longer time to do it. And the smaller you make the eye of the needle, the more young lawyers arrive on the job as uncommitted nomads: at best, acquiring skills they'll take elsewhere; at worst, cynically trying to pile up money before the ax falls. But both states of mind alienate them somewhat from the workplace, the colleagues they work with and the clients they serve.

Worst of all, however, is that when somebody is working 2,200 hours a year, he or she has less chance to pursue the professional experiences that nourish a lawyer's soul. Lawyers of all stripes can and should offer their services

for free to the needy, but I find it hard to imagine more satisfying work than pro bono litigation. That is because when you give the poor and powerless access to a just forum, there is a triumph—no matter what the outcome in a case. And the lawyer who is involved in doing that learns an invaluable lesson about the power and goodness that is inherent in being a lawyer.

I don't know many young lawyers who leave law school without dreams of becoming pro bono princes and princesses; nor is there a dream of youth that seems to die faster. In my own firm, we give young lawyers some billable credit for pro bono time and also have a full-time pro bono partner who works hard to engage the firm's lawyers in these projects.

And we are hardly alone in the profession; many other firms make similar efforts. These are noble gestures—and ones fully worth undertaking. But it's still a little like King Canute ordering the sea to roll backward. As long as it's dollars times hours times partners, we know that the tide will always rise.

Let me again make it clear that I am not calling for lawyers to band together to abandon hourly billing. The antitrust division of the Justice Department would be likely to have something to say about that, and well it should. But I am hoping that lawyers, especially litigators, will more often be bold enough to consider offering clients alternative billing arrangements. And I hope clients will be bold enough to accept them.

Many years ago now, I went shopping for a lawyer in Hollywood to represent me in the dealings I have been fortunate to have with movie and television producers in connection with my books. Naturally, I asked each of the lawyers I spoke to about his or her hourly rate. One attorney answered, "We don't bill hourly. We use the fair fee method."

Then I asked, "Pray tell, what is that?"

"Well," he said, "we do the work, and at the end we get together and agree about what's a fair fee." This sounded to me like an invitation to jump without knowing whether there was water in the pool. "Trust me" is not a persuasive motto. A solid economic relationship ought to start out with both sides understanding the scope of the engagement.

One reason that dollars times hours continues to prevail is because it's hard to devise a fair alternative. Columbus setting out from Spain, destined, in some minds, to sail off the end of the Earth, probably had a better idea what he was headed for than either a lawyer or a client at the inception of a piece of litigation.

Whatever alternative arrangements are made have to be flexible enough to adapt to changing knowledge and the unexpected. It will take some education and experimentation on both sides. But I think we have reached the point where that is virtually required.

The widespread practice of billing by the hours exists almost in defiance of the principles that are supposed to guide our profession. Of the eight guidelines mentioned in Rule 1.5 (Fees) of the ABA Model Rules of Professional Conduct, only one speaks directly to the time spent on the legal task. Yet, despite the fact that our profession's guiding ethical rule encourages lawyers to look to other factors, dollars times hours remains the near universal standard of commercial litigation.

A SORRY SYSTEM

But at the end of the day, my greatest concern is not merely that dollars times hours is bad for the lives of lawyers—even though it demonstrably is—but that it's worse for clients, bad for the attorney-client relationship, and bad for the image of our profession. Simply put, I have never been at ease with the ethical dilemmas that the dollars-times-hours regime poses, especially for litigators. And in this regard, I think my views depart from what is commonly acknowledged (including, I hasten to add, by disciplinary authorities, who of course have not disallowed the current system).

But from the time I entered private practice to today, I have been unable to figure out how our accepted concepts of conflict of interest can possibly accommodate a system in which the lawyer's economic interests and the client's are so diametrically opposed.

Looking again to the Model Rules, Rule 1.7 provides in part that "a lawyer shall not represent a client if the representation involves a concurrent conflict of interest," which the rule defines as occurring when "there is a

significant risk that the representation of one or more clients will be materially limited by ... a personal interest of the lawyer."

I ask you to ponder for just a few minutes whether that rule can really be fulfilled by hourly based fees.

It is fair to assume, of course, that sophisticated clients are fully aware of the hazards of being billed by the hour. But we all know that conflict waivers require more than fair assumptions.

When was the last time any of us actually and explicitly set forth the problems of this system for a client, the way we do with other conflicts? Who ever says to a client that my billing system on its face rewards me at your expense for slow problem-solving, duplication of effort, featherbedding the workforce and compulsiveness—not to mention fuzzy math. Does anybody ever tell a client what the rule seemingly requires?

"I want you to understand that I'm going to bill you on a basis in which the frank economic incentives favor prolonging rather than shortening the litigation for which you've hired me." The truth is that even to imagine that conversation would almost necessarily require the lawyer to be prepared to offer the client an alternative.

I understand some of the counterweights to what I've just said. There is more than a little merit to the idea that the market will reward efficient lawyers who labor to hold down their fees in the recognition that this will lead to further engagements. And of course, just like the vast, vast majority of self-respecting practitioners, I can say with conviction that I have never consciously ordered work or labored longer for the sake of increasing my bills. I think that litigators who send out bills are generally as stunned as their clients by the way time piles up.

But let's not assume this is proof the lawyer reasonably believes the representation will not be materially affected. How many times have you heard a lawyer speak mournfully of the case that settled rather than going to trial, with the resulting detrimental impact on that lawyer's economic fortunes?

More tellingly, who among us can say he or she has never accused the lawyer on the other side of "running the meter"—of doing unnecessary discovery, filing frivolous motions or foot-dragging before engaging in meaningful settlement talks—all to pad the fee. And that's not just to make excuses to the client. When we say it, we mean it.

Looking at the lawyer on the other side of the v., we can see clearly how the temptation to earn more might impact a representation. If we can see the effects of the dollars-times-hours system so clearly when we look across the courtroom, how can we be so fully confident about ourselves?

Personally, I doubt that greed is the principal motivation for the overwhelming majority in our profession, including my opponents. First and foremost, lawyers want to believe they have done their utmost for their clients—and it would be a rare attorney indeed who took much satisfaction out of thinking of himself as well-paid but incompetent or undedicated.

Like every other conflict issue, the problem is one of appearances and temptations. But how can anyone ever know exactly why certain marginal tasks were undertaken? Anybody who has ever investigated a case or prepared to try one knows there is no limit to the potential issues, avenues for investigations, questions to be researched, or variable scenarios that the courtroom might offer. Dollars times hours subtly influences lawyers not to ask themselves what's most probable. It offers scant rewards for discipline.

The more often lawyers find themselves engaged in wheel-spinning, in running out ground balls rather than focusing on the strike zone, the more isolated they feel from the principal goals of the profession, which will always be doing justice. But again, it's the effect on the lawyer-client relationship that is the principal problem.

FEE FIASCO

As a result of hourly billing, the fee collecting process has grown far more fractious. There are now law firms that specialize in disputing other firms' bills—and in-house nudniks who demand copious details and then flyspeck them.

Other clients search for means, whether it's strict litigation budgeting or task-value billing, to put a finger in the dike.

But what does it do to the environment of our profession, to our perception of ourselves and our clients' perceptions of us, that we are locked into a system in which clients are saying from the start of the relationship: I can't really

trust you to be fair to me. If there is even a grain of truth to that characterization, how reasonable is it to believe that our representations have not been materially affected?

America is ambivalent about lawyers. People are impressed with our knowledge and the power that knowledge gives us, and jealous of it as well. They see us as too often self-seeking, manipulative and greedy. We all know that this is not a balanced picture. Every time I hear about a DNA exoneration on radio or TV, I wait vainly to hear what I know is the rest of the story—about the lawyers, usually an army of them, who worked for years, generally for free, to give that prisoner back his liberty. The story of the lawyer doing good because he or she is committed to doing good is not one of the narrative themes American media are fond of presenting because it's not something the public wants to hear.

But recognizing how far behind the eight ball we remain in the eyes of the public, should we really continue to engage in billing practices that even our clients, who know us best, have been telling us inspire distrust?

If I had only one wish for our profession from the proverbial genie, I would want us to move toward something better than dollars times hours. We have created a zero-sum game in which we are selling our lives, not just our time. We are fostering an environment that doesn't provide the right incentives for young lawyers to live out the ideals of the profession. And we are feeding misperceptions of our intentions as lawyers that disrupt our relationships with our clients. Somehow, people as smart and dedicated as we are can do better.

Sidebar

Read a related story this month, New Routes into the Corporate Door.

Scott Turow, the author of Presumed Innocent and seven other novels, is a partner in the Chicago office of the law firm Sonnenschein Nath & Rosenthal. This article is excerpted from Raising the Bar, a collection of essays by a variety of authors about the modern practice of law, which will be published this month by First Chair Press. For more information, go to the ABA Web store.

Addendum 7

The Australian

The time is up for outdated system of charging by the hour

- **PREJUDICE: Chris Merritt**
- From: **The Australian**
- August 20, 2010 12:00AM

BACK in May, when Wayne Martin was making the case against billable hours, he softened up his Law Week audience with this old saw.

"Many of you may have heard the one about the lawyer in his early 40s who arrived at the pearly gates and protested to St Peter that he had been taken too young and deserved to live longer.

"St Peter replied that while the lawyer might believe he was only in his early 40s, analysis of his timesheets revealed that he must in fact be in his 90s."

Martin, the Chief Justice of Western Australia, was making a deadly serious point: time-based billing is a moral hazard.

Those firms that adhere to this outdated system must struggle continually against a structural conflict of interest that has the effect of disadvantaging their clients.

Martin's rejection of billable hours was a timely reminder to the ethical majority of the profession that the billing system that defines their working day has a deeply flawed basis.

Billable hours and the associated tyranny of the timesheet might not be the root of all evil, but among lawyers it comes close.

How many idealistic young lawyers have fled the private profession, burned out before the age of 30 by the mindless requirement to account in detail for every six-minute period in their working lives?

How much damage has been done to the standing of the profession by the equally mindless minority who demand to be paid for time spent reading documents or organising files?

And for what?

Martin makes the point that one of America's most profitable law firms, Wachtell, Lipton Rosen & Katz, has

never used time billing. And England's Eversheds, which has a large commercial practice, has entrenched that position by using technology to ensure clients sign off on all fees in advance.

For Australian firms, the lesson from Wachtell Lipton and Eversheds is that lawyers need to pay more than lipservice to the need to place the client's interests first.

As eBay's Katrina Johnson explains in these pages, general counsel want practical advice from their law firms. And time-charging provides a built-in incentive for law firms to do the reverse by wasting hours crafting beautiful prose that is simply not required. It is sometimes forgotten that time-based billing is a relatively recent phenomenon in this country. It is an American invention that spread rapidly through Australian firms from the 1970s.

But it is very clear that the billable hour, while still dominant, is past its peak. Firms such as Lavan Legal and Advent Lawyers have seen the writing on the wall and are intent on using fixed pricing to grab market share.

But fixed pricing is not the only option. In its report on access to justice, the federal Attorney-General's Department recorded the fact that when the commonwealth buys legal services it sees advantages in using a system known as event billing, in which a price is negotiated in advance for events such as an initial advice, filing initiating process, discovery and mediation. These alternative billing systems, unlike time charging, give the client certainty over the size of their legal bills.

And that explains why Telstra, one of the nation's biggest corporate consumers of legal services, is leading the charge away from billable hours.

Telstra general counsel Will Irving believes there will always be a place for some time charging. But by disrupting the marketplace with his demand for more fixed-price agreements, Irving has done the profession a huge favour.

The insidious impact of the billable hour is on the wane.

PAGES

Home
Yes, I'm A Lawyer

▶ 2011 (340)
▶ 2010 (750)
▼ 2009 (835)
December (37)
November (42)
October (64)
September (91)
August (84)
July (105)
June (104)
May (56)
April (78)
March (48)
February (51)
January (75)
▶ 2008 (810)
▶ 2007 (690)
▶ 2006 (1192)
▶ 2005 (808)

Colorado Appeals Blog
Eric Goldman Technology and Marketing

26 AUGUST 2009

Against Billable Hours (Or Not)?

Law firms have a business model more like defense contractors creating new weapons systems than like Toyota. The operate on a cost plus basis with results not guaranteed.

This system is called the "billable hour" model. The billable hour system, in addition to being popular with lawyers is also favored by plumbers and accountants.

An important variant on the billable hour model is a system in which lawyers make binding estimates of their charges that cease to apply if surprises come up in the case, a bit like a typical automobile repair shop or a general contractor doing a renovation.

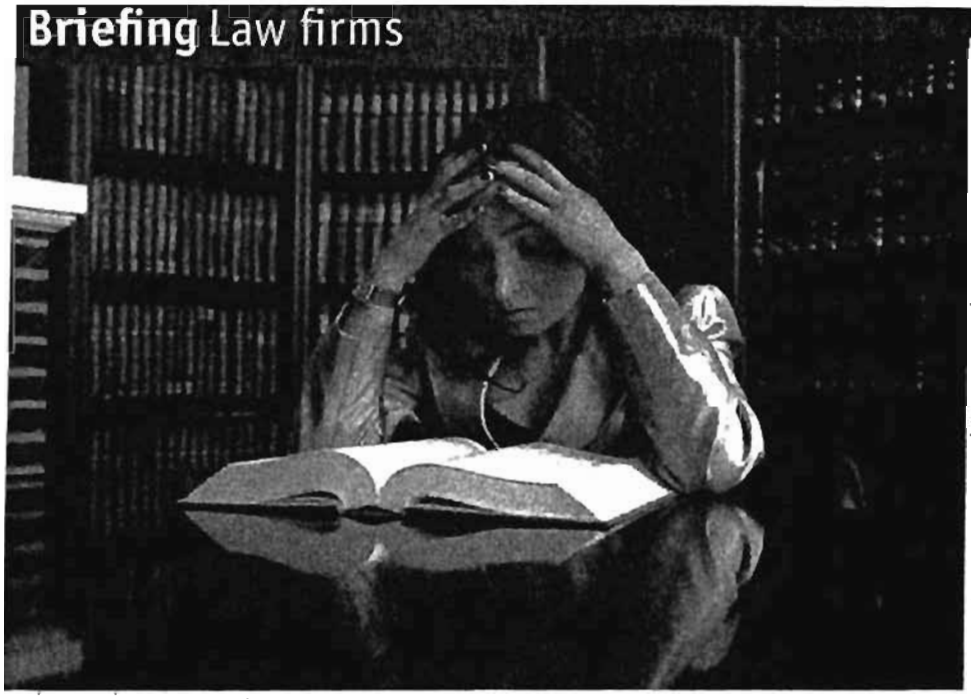
The leading alternatives to billable hours include flat fees and contingency fees. Toyota builds cars for flat fees based on the value of the car. Realtors typically charge a contingency fee based on the sales price (although this is arguably a fee based upon the size of the matter).

Also not unprecedented are fees based upon the size of the matter (common for investment managers), a flat fee per month (sometimes called a "true retainer") like your trash collection bill, and a fee for task model (popular with online advertising agencies and construction subcontractors).

Current Practice

A debate over billable hours, per se, missed the point. In the vast majority of cases, the vast majority of the time, there are ordinary and customary approaches to billing clients for particular types of work that become a stable industry standard. There are many kinds of cases that are almost always handled with alternative fee arrangements. There are other types of cases that are almost always handled on a billable hour basis. Part of the real debate over billable hours is really simply haggling over the size

Addendum 8



A less gilded future

NEW YORK

The legal business has undergone not only recession but also structural change. Ever-growing profits are no longer guaranteed. Nor, for some firms, is survival

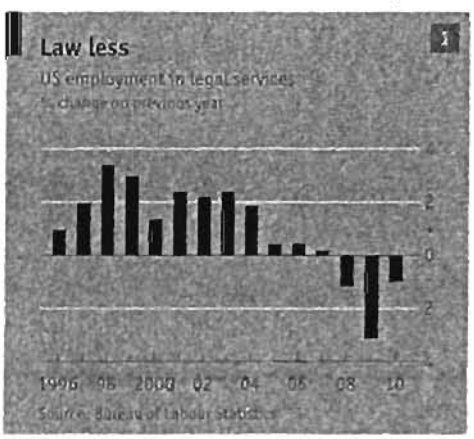
TWO years ago Howrey was one of the world's 100 biggest law firms by revenue, with nearly 700 lawyers in eight countries. Profits exceeded $1m per partner. The American firm, which specialised in intellectual-property suits, had had several spectacular years in a row. But in 2009 profits were much less than expected and angry partners began to leave. Defections continued during the recession. After failed merger talks, Howrey shut its doors this March.

Though Howrey was the only big firm to collapse, the forces that destroyed it hit the whole profession hard. Work on mergers and acquisitions (M&A) dried up and nothing similarly profitable took its place (bankruptcy, securities litigation and regulation were rare bright spots). Clients became keener to query their bills—and to demand alternatives to the convention of charging by the hour, such as flat, capped or contingent fees. Small and innovative firms began obliging them, and big firms increasingly felt forced to follow suit.

All this took a toll on the labour market. After a dozen years of growth, employment in America's law industry, the world's biggest, has declined for the past three years (see chart 1). The 250 biggest firms, according to an annual survey by the *National Law Journal*, shed more than 9,500 lawyers in 2009 and 2010, nearly 8% of the total. Many also deferred hiring, leaving new graduates in a glutted market. Legal-process outsourcing firms, which do not advise clients but do routine work such as reviewing documents, put further downward pressure on the demand for their talents. The pain was felt in Britain, easily the biggest legal market after America, and other countries too.

Lawyers would like to believe that the worst is over and that no more of them will suffer Howrey's fate. Work on M&A and initial public offerings has recovered from dismal levels. And according to *American Lawyer*, profit per partner at America's 100 biggest firms rose by 8.4% last year, having fallen by 4.3% in 2008 and gone up by a measly 0.3% in 2009.

But not all the trends that have hit the legal industry are cyclical. Some are here to stay even as the economy recovers. One is clients' determination to keep their bills down. Feeling that they had overpaid vastly for the work of green trainees, they began refusing to have routine work billed to first- and second-year associates (ie, lawyers who are not yet partners). They see no reason to stand for it again. And alternative fee arrangements continue to grow in importance, albeit slowly: they accounted for 16% of big firms' revenue in 2010.



A second trend is globalisation, which the law is experiencing later than other industries. For lawyers, it holds both promise and peril. Booming emerging markets, especially in Asia, are leading New York and London firms to extend their reach. But the growth of outsourcing to places like India is not lost on money-conscious clients, some of whom are demanding that their lawyers pass certain routine work to cheaper contractors.

A third trend is the growth of technology in an industry long synonymous with trained human judgment. Software that can perform tasks like "e-discovery", sorting through e-mails and other digital records for evidence, is saving firms money. It has also made it harder to sustain a business model in which partners sit atop a pyramid with a fat base of associates who carry out expensively billed work, some of which is routine and repetitive.

Trends that were not part of the recession will not disappear with the recovery. Some will even strengthen. William Henderson of Indiana University points out just how good and how long a run lawyers had. Spending on legal services grew from 0.4% of America's GDP in 1978 to 1.8% in 2003. The legal business grew four times faster than the economy. Now, Mr Henderson says, a "hundred-year flood" is hitting the profession. Job growth had begun well before 2008, he points out, so that the labour market was already out of balance when recession struck. Not all firms will survive, and those that do will not all prosper equally.

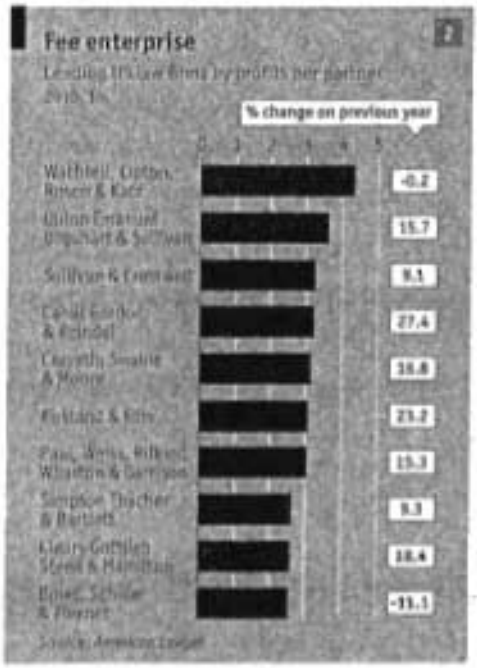
Howrey's boss, Robert Ruyak, blamed two new trends for his firm's demise. Howrey had begun acceding to clients' demands for flat, deferred or contingent fees, causing income to become clumpy and unpredictable. And the rise of specialised e-discovery vendors hollowed out another source of revenue.

What kind of firm is likely to thrive in the environment in which Howrey failed? On one answer, many experts agree: a group of elite New York-based firms that cover a wide spectrum of legal work. These include Davis Polk & Wardwell; Sullivan & Cromwell; Cleary Gottlieb Steen & Hamilton; and Simpson Thacher & Bartlett. Though associated with Wall Street, they have become internationalised, through longish histories in Europe and recent moves into Asia and Latin America. That said, they don't try to be everywhere, covering mainly the leading financial centres. Nor do they try to do everything, but offer the range of services on which their New York businesses were built: M&A, fi-

, white-collar defence and so forth.
n & Cromwell is one of seven firms
rican Lawyer's list whose profits per
r top $3m (see chart 2).
other bunch likely to do well are
focused firms that concentrate on
few fields. Some ("monolines") spe-
in only one. They typically do not
span the globe, but their work is so
hat clients will keep paying hand-
y for it. Wachtell Lipton, for example,
w York firm focused on M&A. It is
e world's most profitable, with pro-
partner of $4.3m last year. Cravath,
& Moore, also known mainly for
oined the $3m club in 2010 after pro-
partner went up by one-sixth. Out-
merica, this group is represented by
ter and May, one of the "magic cir-
five London firms that compete
ne leading American outfits. Rather
etting up shop abroad such firms
artnerships with local leaders, such
ice's Bredin Prat or Spain's Uría Me-
, to gain reach without establishing
wn offices and hiring staff.
vath and Wachtell have boosted
in the past two years without shed-
ny lawyers. Many other firms in
an Lawyer's top 100, lacking their
power, maintained profits only by
headcount. Even equity partners
ot been spared. Firms cut 0.7% of
2009 and 0.9% last year.

ing, anywhere

nue is not growing as quickly as it
, more firms must not only employ
awyers but also compete for market
s never before. With the American
hardly booming, a third class of
as rushed to expand globally. These
and well-known, but do not have
tering reputations of the first two
. Their promise is that wherever cli-
ant to do business, they will deal
seamless entity. Jones Day, which
in the American Midwest and is
19 countries, exemplifies the type
s slogan, "One Firm, Worldwide".
per, product of a three-way Anglo-
an merger (and technically a "ve-
n association of partnerships under
aw) aims to offer global clients a
te service while keeping prices
y working out of cheaper cities.
er & McKenzie, another verein, has
gest history of globalisation of any
. It was in Latin America as long ago
950s and in mainland China in 1993.
o the world's biggest firm by rev-
ulling in $2.1 billion in 2010, half of
clients that use the firm in ten or
laces. Baker & McKenzie likes to call
global", not "international", mean-
not a firm that has simply grown
m New York or London. Its new
luardo Leite, a Brazilian, is the first
from one of the BRIC economies



(Brazil, Russia, India, China) to lead such a big firm. But continuity worldwide remains a priority: Mr Leite says that the firm works constantly to co-ordinate its efforts, with regional and national managing partners regularly travelling to audit each other's work for quality, for example.

If groups like Baker & McKenzie and lower-cost DLA Piper are doing well, offering anything, anywhere has pitfalls for more expensive integrated firms with a global spread such as Allen & Overy and Clifford Chance, both based in London. During the recession they had to lay off some partners, cut the equity shares of others and thin their layers of junior lawyers. Some pin Howrey's demise on its rush to spend on foreign offices while betting heavily on antitrust law just as M&A was falling off a cliff. There is money in globalising, but not enough for everyone.

In addition, some countries protect their turf. It is virtually impossible for a foreigner to practise Indian law. Only locals can practise Chinese law. Although flotations and cross-border mergers involving Chinese companies have been good to many firms, the mass rush into China has led to competition on prices. Chinese clients are even more accustomed than American ones to asking for alternatives to the lucrative billable hour. And local firms are becoming more sophisticated. There is no reason to expect they will yield business tamely. Brazil presents similar obstacles to foreign lawyers.

Ultimately, lawyering is becoming more of a business than a profession. Some lawyers decry this. Others welcome it. Few deny it. Because the American market cannot grow as it used to, firms will have to find new strategies and make use of sophisticated branding to stand out.

Mr Leite suggests one way lawyers can guarantee themselves work: by becoming experts in other industries, not just areas of legal practice. Young lawyers can learn from being seconded to clients. And American law schools are slowly trying to instil some business acumen into future lawyers, though in Europe and elsewhere law remains distressingly academic.

Another much-discussed solution for teaching lawyers to be businesspeople is the creation of all-in-one professional-service firms, combining lawyers, management consultants and accountants. But this looks unlikely to succeed for many; the three professions are simply too different in their traditions, training and incentives. A liberalisation of the legal market in England and Wales will allow more non-lawyers to own parts of firms or offer certain services, but at first this is likely to affect mainly the cheaper end of the market, not the richest pickings of corporate work.

Many bosses of law firms realise that the profession is changing in ways that will be uncomfortable for some. They are adjusting to this, but Howrey's fall shows just how fragile even a 55-year-old firm can be. Since a firm's only real assets are its partners, when a few departures turn into an exodus, the end can be shockingly quick. ■

Sound career advice

Canada's general elec

Harper

Ho

tively, they are a useful contri-
l struggling to grow.
bigger that contribution might
ble to process the applications
t. There are more than 700,000
ventors wait for two years un-
considered. Ten months more
hether they have been success-
ion, the American economy is

Patents pending

The backlog extends the uncertainty that the process causes to businesses, applicants and competitors alike, slowing investment and constraining the economy. It may also push back the launch of the new product for which a patent is sought, depriving customers of the benefits. Entrepreneurial small businesses, which are increasingly recognised as an important source of new jobs and often need a patent to raise the capital they need to grow, tend to be hit particularly hard. The delay may also cause firms to seek alternative methods of protecting their intellectual property, especially through trade secrets. That may in turn impose further costs on the economy by slowing the dissemination of knowledge which the pate system helps to bring about.

On April 26th a scheme to process applications more quic ly for an additional fee was put on ice by David Kappos, tl head of the Patent Office, who blamed this on its new spen ing cap. Even in today's difficult fiscal circumstances, it shou not be beyond Congress to find the money to allow the Pate Office to introduce this reform. Simply letting it keep all its fe would do the trick—even if this comes at the expense of son other programme that contributes less to the economy.

Congress should also hurry up and pass the patent reforn that it has been considering, mostly favourably. Certain, there are things to quibble about in the proposed legislatio Not everyone is convinced by its bias towards the first app. cant to file for a patent rather than (as now) the first applicai to have the idea, nor by its lack of an easier way to challeng patent awards. Yet, overall, it makes sense. Most sensible of a is the part that would let the Patent Office determine its ow fees and keep all the money that it collects. That would pr sumably enable it to reduce the backlog of applications. Th sooner Congress passes this legislation, the easier it will be t take seriously the claims of America's politicians to be doin all they can to foster innovation. ■

The price of legal services

How to curb your legal bills

They fell during the recession, but not nearly far enough

LAWYERS are less than 1% of American adults, but they are well-represented in government. Both the president and the vice-president trained as lawyers. So did 55% of senators and 100% of Supreme Court justices. There are advantages to having a bit of legal expertise among those who write and execute the nation's laws, or assess their constitutionality. But there is also a potential conflict of interest. If florists had such a lock on the levers of power, you might expect subsidies for weddings, a campaign to beautify cities and the addition of Godmothers' Day, Aunts' Day and Librarians' Day to the calendar. Lawyers, alas, are no more selfless.

The American legal system is the most lawyer-friendly on Earth. It is head-thumpingly complex. The regulations that accompany the Dodd-Frank law governing Wall Street, for example, are already more than 3m words long—and not yet half-written. Companies must hire costly lawyers to guide them through a maze created by other lawyers. They must also hire lawyers to defend themselves against attacks by other lawyers on a playing field built by lawyers. The cost—roughly $800 a year for every American—is passed on to consumers. The benefits are hard to detect. Americans are probably no less likely to be injured or cheated than the citizens of countries that spend a fraction as much.

So it is hard to muster sympathy for lawyers facing a tighter labour market. America's 250 biggest law firms shed more than 9500 people, nearly 8% of the total, in 2009-10. Law students ed after graduation. One big law firm even went bust (see pages 74-75). None of this is nice for the people concerned, especially those with large student debts. But a squeeze was lon overdue. The recession forced corporate America to look har for savings, and the people who were being paid hundreds o dollars an hour to nitpick were an obvious target. Some lawyering requires exceptional skills and deserves high pay. Bu law firms were often charging stiff rates for routine work done by trainees. Clients are right to demand better value for money Law firms can increasingly oblige them with the help of technology and globalisation.

Lawyer, meet my accountant

Companies are insisting that their lawyers outsource basic or repetitive tasks. They are pressing them to use software, rather than expensive eyes, in the collection of vast amounts of information for anyone who files a semi-plausible suit. They are asking for flat or capped rather than hourly fees. American lawyers are not the only ones recalculating their bills. London firms with a global spread are also facing competition and more demanding clients. Firms at the cheaper end of the British market nervously await liberalisation at home.

Yet no one should underestimate lawyers' ability to adapt. In America members of the plaintiffs' bar search constantly for ingenious ways to make whoever has the deepest pockets pay for whatever goes wrong. That benefits defence lawyers too, because firms facing ingenious assailants need ingenious protectors. It will take more than market forces to make the system fairer for non-lawyers. America needs fewer and simpler laws, and stricter curbs on frivolous suits and outlandish damages.

Addendum 9

Print Page

AllBusiness

Powered by LexisNexis

Curbing those long, lucrative hours

The billable hour is not dead, but many people would like to kill it

LAWYERS hate keeping track of their billable hours. Clients hate them even more; each month they receive bills showing that their legal representatives have worked improbably long hours at incredibly high rates. Billing by the hour often fails to align lawyers' interests with their clients'. The chap in the wig or the white shoes has an incentive to spin things out for as long as possible. His client would rather win quickly and go home. Since there is clearly a demand for an alternative to the billable hour, you would expect someone to supply it. And indeed, this is starting to happen.

Many legal tasks, although not quite easy, are variations on a theme. The production of a certain document (such as a trademark registration) does not differ vastly from one instance to another. So more firms are using "document assembly" software such as that made by Basha Systems; Seth Roland, the company's founder, says that his company's software reduced the time needed to put together a certain type of real-estate lease from 40 hours to one. Automating the automatable stuff allows lawyers to spend more time talking to the client. Everyone wins (including Basha, which Mr Roland says has grown by between 15% and 20% a year for more than a decade).

More and more firms' in-house lawyers, who typically hire and manage outside lawyers, have turned to alternatives to the billable hour since the beginning of the global recession in 2008. According to a survey by the Association of Corporate Counsel (ACC), which represents companies' in-house lawyers, 44% of members asked their lawyers for alternative billing to cut costs in 2009, more than any other cost-reducing measure. Susan Hackett, the ACC's general counsel, says that just a few years ago what she calls "value-based" billing was only 3% of her members' legal spending. Now, she says, surveys show the average client laying out between 15% and 30% of their legal spending this way.

Evan Chesler, the presiding partner of Cravath, Swaine & Moore, one of the world's largest law firms, wrote an article in 2009 called "Kill the Billable Hour". It has not been killed, but he is confident that clients will continue to ask for alternatives. The recession may have boosted this trend, he says, but it was not its primary cause. Clients are not merely trying to screw down fees, but rather are aiming for predictability and fairer, not just lower, bills. This means lawyers must sit down with clients at the start and discuss what exactly they want to achieve, and how much success might be worth to them.

Different needs call for different billing structures. Repeatable documents are one thing; complex litigation is another. Lawyers often remind their clients that litigation (and hence the bill) is unpredictable. But even litigation can sometimes be billed in ways other than by the hour. A "bet the company" case, in which price is no object, will probably still be billed by the hour. But many cases are settled, and companies can try to figure out how much they want to spend on, say, depositions while trying to prepare themselves to sue or settle. Since the time and money needed for a deposition can be relatively predictable, says Ms Hackett, the client can decide how many are needed.

That still leaves many hours being billed the old-fashioned way. Experts and surveys estimate that between 10% and 30% of hours are never billed by tired and overworked attorneys who cannot keep track of every piece of work they do. A firm called Chrometa addresses this problem by producing a software programme that automatically tracks a lawyer's computer usage, showing how much time she has spent on which e-mail, document or spreadsheet. These can easily be filed by case and client, so the client gets a more detailed invoice. This may not result in many more hours billed, but it saves strain on both lawyer and client in keeping track. Both sides can then focus on the case at hand, rather than the bill.

Addendum 10

Billable Hours Giving Ground at Law Firms

Published: January 29, 2009

A recent study released last year by the Association of Corporate Counsel showed a rise in the number of companies paying by the hour — but that covered the spring and summer, before the worst of the downturn.

Many smaller firms and solo practitioners have long offered to perform services, like mortgage closings, for flat fees. Plaintiff lawyers also often work on a contingency basis, receiving a percentage of any awards.

"What we do in our business litigation is charge clients some kind of monthly retainer, which gets credited against an eventual recovery," said John G. Balestriere, a partner at Balestriere Lanza, a Manhattan firm with five lawyers. "It's a lot easier for us to tell a client, 'We want to do this, we want to push for summary judgment,' " he said, and so avoid a lengthy, costly trial.

When not paid by the hour, lawyers' approach to their work changes, said Carl A. Leonard, a former chairman of Morrison & Foerster who is now a senior consultant at Hildebrandt International, which advises professional services firms.

In one case, he said, Morrison & Foerster negotiated a fixed fee for defending a company in court, covering work up to the point of a motion for summary judgment.

On top of the fee, if the case settled for less than what the company feared having to pay if it lost in court, the law firm got a percentage of the amount saved. The arrangement made sense when the goal was to resolve the dispute quickly, Mr. Leonard said.

Lawyers on the case negotiated a settlement for much less than the client's worst-case number, Mr. Leonard said. "The effective hourly rate was something like 150 percent of our hourly rates," he added. "We made money, the client was happy."

In litigation, firms that charge by the hour can suffer if they are too successful and end a lawsuit — and the stream of payments from continuing work — too quickly. One law firm that recently collapsed, Heller Ehrman, was hurt in part because a number of cases had settled.

That collapse highlights the risk to law firms experimenting with other payment arrangements: If lawyers set too low a price, they lose money. Many lawyers may not be

Addendum 11

Time to experiment with alternative billing practices

Recent surveys confirm that, with the exception of individual plaintiff actions relating primarily to personal injuries, well over 90% of all legal fees charged by law firms are still based solely on hourly rates. During the next decade, however, this approach will be replaced on a selective basis with alternative billing practices. For instance:

- Contingent fees.
- Modified contingent fees (reduced or guaranteed hourly rate, with additional fee calculated as a percentage of the result).
- Flat fees.
- Standard hourly rate plus bonus (based on result).
- Piecework fees.
- Value-based fees (fee based solely on agreement reached before, during, or at the end of the matter, as to the overall "value" of the services performed).

An ABA Committee on Corporate Counsel survey revealed that many problems between corporate counsel and outside lawyers stem from billing based on the traditional hourly rate method. Responding to the question: "What one factor concerns you most about outside counsel's billing practices?", over 75% of corporate counsel expressed mistrust of private law firms' hourly billing procedures.

Still, this attitude doesn't preclude recognition of the merits of paying a premium for outstanding work. Quite the contrary: two-thirds of the corporate counsel agreed that a bonus arrangement tied to the outcome will, in their view, provide lawyers with a greater incentive to obtain superior results.

Approximately 70% of the responding corporate counsel indicated they would be willing to agree to a contingent fee, a modified contingent fee, or a flat fee in cases where the company is a plaintiff. In cases where the company is a defendant, an alternative billing method received majority approval (a smaller 52% of the respondents) and, in their view, this should generally be a flat fee.

About one-third of corporate lawyers expressed a willingness to experiment with a piecework basis for fees. Nearly 60% felt that flat fee arrangements would cause outside lawyers to work more efficiently and institute cost-cutting measures. And, interestingly, 52% felt flat fees for consultation time would encourage "preventative maintenance."

Business and individual clients see many advantages in alternative billing practices. Why not, then, make more of an effort to institute such approaches? Clients will view their financial interests as better protected—more easily budgeted. For the law firm, it can result in an enhancement of revenues for the same number of lawyer hours.

Hints for moving work-in-process to the bottom line

Even though the accrual method of accounting is an essential tool for measuring the economical performance of today's law firm, common sense indicates that only cash meets payrolls, supports the overhead and permits those periodic distributions from "profits" to supplement partners' regular "compensation."

It may be satisfying to a law firm to show a profitable picture and an adequate balance sheet on the accrual basis. But, if these perfectly proper financial statements are heavily made up of receivables and work-in-process, the cash flow may suffer. Increased borrowing or "tightening" will occur.

In today's legal environment, where overhead costs and salaries of employed lawyers are rising, where client resistance to fee increases is on the ascendancy and where partners want to maintain a higher rate of distributions, cash management is probably of critical concern in the financial administration of a law firm.

A number of law firms face difficulties with cash flow because of their unwillingness to confront increased unbilled time and delinquent accounts receivable.

Responses to accelerating collections once billings have gone out to clients deserve special attention. An overlooked cash-flow resource for law firms is the increasing amount of work-in-process (the value of unbilled time).

One dramatic indication of the extent to which this potential reserve of cash has been ignored by law firm managements is that, in the recent Altman & Weil 1988 Survey of Law Firm Economics, only 60% of the 700 participating law firms could answer the question, "What was the value of unbilled time at your regular hourly rates at the close of the fiscal year?" Apparently, this one aspect of financial information was unavailable to many.

The extent to which work-in-process is not billed represents an extension of credit to clients—money that law firms are lending on an unsecured and non-interest-bearing basis.

The firms that did answer the question about the value of unbilled time at the close of their fiscal year showed an average of $41,172 per lawyer. (The upper quartile of this unbilled time per lawyer is $55,849, and the ninth decile is an extraordinarily high $78,444). The average annual cash generated per lawyer for these firms is $178,623.

Therefore, the average law firm now has tied up in work-in-process an amount equal to 25% of the gross receipts of each lawyer in the firm, or the equivalent of three months' cash revenues.

Aggravating the situation is the extent of the value of disbursements outstanding, but not billed or repaid, at the close of the fiscal year. This amounts to an average for all firms of $5,163 per lawyer, or, approximately, an additional 11 days of cash revenues.

Rapid "inventory turnover" is essential to the profitability and liquidity of

(Continued on page 4)

Presnell, Gage & Co.
Certified Public Accountants

1150 W. State Street
P.O. Box 1693
Boise, Idaho 83701
(208) 345-2350

1216 Idaho Street
P.O. Box 555
Lewiston, Idaho 83501
(208) 746-8281

First Bank of Troy Building
609 S. Washington, Suite 202
Moscow, Idaho 83843
(208) 882-2211

The Lawyers' Advantage
for America's Lawyers
Fourth Quarter, 1988

Law firm borrowing requires careful consideration

The failures of several law firms—including one of the nation's largest—during the last 12 months should move the management of law firms that borrow from banks (often for the purpose of "accelerating the realization of receivables") to review the implications and alternatives of such transactions.

Many administrators and managing partners take refuge in the fact that their "good" receivables are several times the amount of their borrowings. It is reasoned, therefore, that the obligation is somewhat "moot," since the firm has "more than adequate coverage." No doubt such borrowings are, in the majority of instances, rational, reasonable and justified. Still, this kind of debt should be examined carefully.

Most law firms increased their distributions to partners in fiscal 1987. About half did so by more than 20%. All of this seems very good economic news for the professional. But, at the same time, many also increased their bank borrowings or experienced a degree of cash-flow tightening. Law firms require timely, carefully prepared financial studies to evaluate the relationship between distributions, borrowings and cash flow.

Borrowings by law firms—made in reasonable proportions for all kinds of purposes including start-up needs, acquisition of equipment, space improvements and even short-term working capital infusions—are one thing. It seems that the most questionable borrowings, however, are those that are done solely for the purpose of continuing a pattern of larger and larger distributions to partners.

It could be argued, and argued persuasively, that money borrowed—no matter what and how much the assets on the other side of the column—for purposes of fulfilling partnership distributions is fundamentally returning a partner's capital to him or her.

Yet, it should also be conceded that large numbers of law firms have for many years successfully repeated this kind of borrowing prior to or just after year-end without future problems. Regardless of the widespread success of such experiences, though, complacency about the seriousness of these borrowings can sometimes lull a firm into further borrowings of increasingly larger amounts.

When this scenario emerges, the ratio between current assets and current liabilities can narrow to a point where short-term loans must become

(Continued on page 2)

What's Inside

Addendum 12

Alternative law firms

Bargain briefs

NEW YORK

Technology offers 50 ways to leave your lawyer

CONVENTIONAL law firms charge vast hourly fees and then hand the work to underlings while the partners play golf at clubs their clients are too poor to join. At least, that is how it seems to many clients, whose irritation at being overcharged turned to fury during the recession.

Some clients are switching to unconventional law firms, which claim to offer equally good lawyering for much less money. Take Clearspire. The firm's 20 or so lawyers work mostly from home, collaborating on a multi-million-dollar technology platform that mimics a virtual office. A lawyer checking in on a colleague automatically sees a picture of her on the phone when she is, in fact, on the phone. Clients use the platform too, commenting on and even changing their own documents as they are being drawn up. Conventional lawyers are far less open.

From the start, Clearspire offers cost estimates for each phase of a legal job. Employees who underestimate how long it will take cannot simply jack up the bill—they must take the hit themselves. But if a lawyer finishes his work faster than promised, he gets a third of the savings. The client also gets a third, as does Clearspire. This gives everyone a stake in making the process more efficient and predictable.

Bryce Arrowood, the founder, notes that law firms reward partners who bring in business, and not necessarily the most brilliant lawyers. Yet clients' priorities are exactly the reverse. So Clearspire has an unusual dual structure. American law firms cannot have non-lawyers sharing fees with lawyers. (Britain used to be the same, but will ditch this pointless rule this year.) So Clearspire must be two entities: a law firm, with salaried employee-lawyers rather than partners, and a second company that focuses on bringing in business and supporting the lawyers.

The discount for clients is sweet. George Kappaz is a private-equity boss who recently gave a complex job to Clearspire (structuring an equity package for Astrata, one his fund's firms). He estimates that it cost a quarter of what he would have paid the big firms he used before, and Clearspire's work was just as good. (Many of its lawyers come from top-notch law firms.) Mr Kappaz predicts that the Clearspire model, or something like it, will revolutionise the legal business.

Perhaps so, but for Clearspire it is early days. Can it make money? A company like 11-year-old Axiom proves that clients have an appetite for alternative models. Axiom either seconds some of its hundreds of lawyers to a company, takes on a whole chunk of a client firm's legal work (such as commercial contracts), or performs "discovery" (reviewing documents for litigation). Rather than charging by the hour for each lawyer, it asks for a single flat fee, or charges for a team by the week or the month. Expenses are kept low by having headquarters in SoHo, a chic bohemian bit of New York, and by stashing many lawyers in even cheaper places such as Houston and Hyderabad.

The recession was good to Axiom. After it sent its consultants, recruited from the likes of McKinsey and Accenture, to clients to help them trim their legal spending, the clients gave Axiom more work. Revenue grew from $55m in 2008 to $80m in 2010. This year the firm expects to rake in $120m. Companies were always under pressure to cut their legal bills, says Mark Harris, Axiom's boss. But "fake pressure" before became "real pressure" during the downturn.

Axiom and Clearspire serve some of America's biggest companies. Other entrepreneurs are aiming at small-business clients. These would normally take a chance on finding the right sole practitioner or small firm. But on LawPivot, a year-old social-networking website for lawyers and those who need them, potential clients post questions (up to three a month), and lawyers provide free, brief answers. The lawyers make nothing, but use the service to drum up custom. Clients can test a lawyer's skill before opening their wallets.

LawPivot is a social-networking site, not a law firm—it will make its money initially by charging lawyers to upgrade their profiles (similar to the networking profiles on LinkedIn). Google Ventures is a backer, and Apple's former top lawyer for mergers and acquisitions is a co-founder. This kind of heft will bring it up against LegalZoom, the biggest seller of online forms and easy, repeatable legal services for small businesses and individuals. LegalZoom now wants to put more of its contract lawyers to work directly for clients at a flat rate.

It is more than a decade since the internet made book-buying cheaper and more convenient. If technology now helps cut gargantuan legal bills in America and elsewhere, it will be better late than never. ■

Tour operators

Horrible holidays

The holiday business is in trouble. Firms are merging like Brits in Benidorm

EUROPE'S travel industry has had four terrible years: a recession, an Icelandic volcano, unrest in the Middle East, costly oil, a weak dollar and a widespread sense of malaise. People want to get away from it all, but worry that they can't afford to.

Airlines, hotels and cruise ships have all suffered, but the worst-hit are the tour operators. To survive, they have merged and cut costs. In 2007 Thomas Cook, a German-owned travel firm, took over MyTravel, a British rival, to create Europe's second-biggest package-tour firm. A couple of months later Hanover-based TUI, Europe's biggest travel company, merged its travel business with First Choice, another British package-holiday company, to create TUI Travel, a company based in London and listed on the London Stock Exchange. Both ▸▸

Alternative law firms

Bargain briefs

NEW YORK

Technology offers 50 ways to leave your lawyer

CONVENTIONAL law firms charge vast hourly fees and then hand the work to underlings while the partners play golf at clubs their clients are too poor to join. At least, that is how it seems to many clients, whose irritation at being overcharged turned to fury during the recession.

Some clients are switching to unconventional law firms, which claim to offer equally good lawyering for much less money. Take Clearspire. The firm's 20 or so lawyers work mostly from home, collaborating on a multi-million-dollar technology platform that mimics a virtual office. A lawyer checking in on a colleague automatically sees a picture of her on the phone when she is, in fact, on the phone. Clients use the platform too, commenting on and even changing their own documents as they are being drawn up. Conventional lawyers are far less open.

From the start, Clearspire offers cost estimates for each phase of a legal job. Employees who underestimate how long it will take cannot simply jack up the bill—they must take the hit themselves. But if a lawyer finishes his work faster than promised, he gets a third of the savings. The client also gets a third, as does Clearspire. This gives everyone a stake in making the process more efficient and predictable.

Bryce Arrowood, the founder, notes that law firms reward partners who bring in business, and not necessarily the most brilliant lawyers. Yet clients' priorities are exactly the reverse. So Clearspire has an unusual dual structure. American law firms cannot have non-lawyers sharing fees with lawyers. (Britain used to be the same, but will ditch this pointless rule this year.) So Clearspire must be two entities: a law firm, with salaried employee-lawyers rather than partners, and a second company that focuses on bringing in business and supporting the lawyers.

The discount for clients is sweet. George Kappaz is a private-equity boss who recently gave a complex job to Clearspire (structuring an equity package for Astrata, one his fund's firms). He estimates that it cost a quarter of what he would have paid the big firms he used before, and Clearspire's work was just as good. (Many of its lawyers come from top-notch law firms.) Mr Kappaz predicts that the Clearspire model, or something like it, will revolutionise the legal business.

Perhaps so, but for Clearspire it is early days. Can it make money? A company like 11-year-old Axiom proves that clients have an appetite for alternative models. Axiom either seconds some of its hundreds of lawyers to a company, takes on a whole chunk of a client firm's legal work (such as commercial contracts), or performs "discovery" (reviewing documents for litigation). Rather than charging by the hour for each lawyer, it asks for a single flat fee, or charges for a team by the week or the month. Expenses are kept low by having headquarters in SoHo, a chic bohemian bit of New York, and by stashing many lawyers in even cheaper places such as Houston and Hyderabad.

The recession was good to Axiom. After it sent its consultants, recruited from the likes of McKinsey and Accenture, to clients to help them trim their legal spending, the clients gave Axiom more work. Revenue grew from $55m in 2008 to $80m in 2010. This year the firm expects to rake in $120m. Companies were always under pressure to cut their legal bills, says Mark Harris, Axiom's boss. But "fake pressure" before became "real pressure" during the downturn.

Axiom and Clearspire serve some of America's biggest companies. Other entrepreneurs are aiming at small-business clients. These would normally take a chance on finding the right sole practitioner or small firm. But on LawPivot, a year-old social-networking website for lawyers and those who need them, potential clients post questions (up to three a month), and lawyers provide free, brief answers. The lawyers make nothing, but use the service to drum up custom. Clients can test a lawyer's skill before opening their wallets.

LawPivot is a social-networking site, not a law firm—it will make its money initially by charging lawyers to upgrade their profiles (similar to the networking profiles on LinkedIn). Google Ventures is a backer, and Apple's former top lawyer for mergers and acquisitions is a co-founder. This kind of heft will bring it up against LegalZoom, the biggest seller of online forms and easy, repeatable legal services for small businesses and individuals. LegalZoom now wants to put more of its contract lawyers to work directly for clients at a flat rate.

It is more than a decade since the internet made book-buying cheaper and more convenient. If technology now helps cut gargantuan legal bills in America and elsewhere, it will be better late than never. ■

Tour operators

Horrible holidays

The holiday business is in trouble. Firms are merging like Brits in Benidorm

EUROPE'S travel industry has had four terrible years: a recession, an Icelandic volcano, unrest in the Middle East, costly oil, a weak dollar and a widespread sense of malaise. People want to get away from it all, but worry that they can't afford to.

Airlines, hotels and cruise ships have all suffered, but the worst-hit are the tour operators. To survive, they have merged and cut costs. In 2007 Thomas Cook, a German-owned travel firm, took over MyTravel, a British rival, to create Europe's second-biggest package-tour firm. A couple of months later Hanover-based TUI, Europe's biggest travel company, merged its travel business with First Choice, another British package-holiday company, to create TUI Travel, a company based in London and listed on the London Stock Exchange. Both ▸▸