

ALTERNATIVE BILLING ARRANGEMENTS
IN BUSINESS LITIGATION

C. Neal Pope
Alan G. Snipes¹

Pope, McGlamry, Kilpatrick, Morrison & Norwood, LLP
The Pinnacle, Suite 925
3455 Peachtree Road, N.E.
P.O. Box 191625
Atlanta, GA 31119-1625
(404) 523-7706

1111 Bay Avenue, Suite 450
P.O. Box 2128
Columbus, GA 31902-2128
(706) 324-0050

¹Neal Pope is the founder of Pope, McGlamry, Kilpatrick, Morrison & Norwood, LLP, a regional and nationwide civil trial practice firm specializing in business litigation and traditional tort actions. He has been practicing law for over 40 years following receipt of his law degree from the University of Alabama in 1966. He is a Fellow of the American College of Trial Lawyers, and a member of the Georgia, Florida, Alabama, and District of Columbia Bars. He has been perennially listed as a top 100 *Super Lawyer* in Georgia and in the *Best Lawyers in America* (1991-present).

Alan Snipes is a partner in Pope, McGlamry, Kipatrick, Morrison & Norwood, LLP, and is a member of the Firm's corporate litigation team. He received his B.B.A. degree, *magna cum laude*, from Mercer University in 1993. He graduated from Mercer Law School, *cum laude*, in 1996. He is regularly admitted to practice before all state and federal courts in the State of Georgia and has been admitted to practice *pro hac vice* before numerous other courts throughout the southeast and nationally. His practice focuses primarily on complex commercial litigation.

An Epiphany for a Plaintiff's Lawyer and a Corporate Counsel

Some six years ago, I was sitting on my neighbor's porch at the lake, enjoying a cup of coffee with him as we often do on Saturday mornings. While we had both enjoyed our Saturday morning coffee for years, we had not often talked about business. Looking back, it seems strange that two lawyers with forty years experience each had never talked substantively about business. But, you see, he was the General Counsel of a Fortune 500 company. I was a plaintiff's lawyer. I think both of us thought our law practices were worlds apart and, to some extent, they were. He was accustomed to hiring traditional big defense firms and paying them by the hour. I was accustomed to representing individuals on a contingent fee contract. Those two worlds could never come together, could they? Yet, on that fall morning, they did.

It all started with a stressed look on my friend's face. I couldn't help but inquire what was going on. He said, "Neal, we had to change auditors after Arthur Andersen went under and the new auditors made us change some accounting practices which resulted in a restatement. Now, we've been sued in a securities class action, a shareholder's derivative suit, and a whole host of tag along actions. While we don't think the cases have any merit, it's a bet your company situation in more ways than one. The damages sought are more than we could handle. In the meantime, the lawsuit is holding up a nine figure deal to sell one of our divisions.

This case is absolutely holding us hostage.” Of course, I asked my friend who was representing his company, and was not surprised to learn it was a traditional Atlanta defense firm who had represented my friend’s company for many years. I was surprised, however, to hear my friend’s assessment of their progress: “I just don’t know where this is heading. They have billed us over a million dollars and we just got through a Motion to Dismiss, which we lost. They say we’ll have to go through discovery now which will cost millions more. I’ve got an army of associates in our offices right now gathering documents for production.”

Drawing on my experience, I asked, “If the case is causing that much disruption, why don’t you just settle it?” He replied, “I wish I could. To tell you the truth, we would pay \$20 million right now to get this over with. But our defense firm says there is no way the case will settle until after discovery.” Sitting back in my chair, I had an epiphany at that moment. I said, “if you would pay \$20 million to settle it, would you pay \$10 million to settle it?” With a puzzled look on his face, he replied, “of course, that’s 10 less than I’m willing to pay right now.”²

My friend’s puzzled look would soon fade when he heard my idea. If his company was willing to pay \$20 million to settle the case, why should they continue to pay defense lawyers millions of dollars to defend the case and then ultimately settle the case anyway? Wasn’t that just throwing money away? Right

²The names of the company and the settlement amounts discussed have been altered to ensure confidentiality.

then and there, we made a deal. Our firm would take over defense of the cases at no charge. If we were able to resolve the cases for any amount less than \$20 million, his company would pay our firm a contingent fee based on the amount of money saved. If the cases did not resolve for less than \$20 million, his company would owe us nothing in legal fees.

Our firm immediately took over defense of the cases. When we received the file, we found a typically litigated case. The plaintiffs had requested hundreds of thousands of pages of documents. Defense counsel had objected, and numerous discovery motions were pending. These, of course, would have required months to resolve and hundreds if not thousands of hours of attorney time.

We chose a different approach. We immediately hired a third party consultant (so as to minimize in house disruption to our client) to give us a quote on compiling and imaging every single document the plaintiffs were requesting. We then made an offer to plaintiffs' counsel we knew any judge would approve: we would produce every single document they were requesting (with the exception of privileged documents), provided that they would agree to pay the costs for the third party consultant to compile and image the documents. You would be amazed at how reasonable a plaintiff's attorney can be when he faces the prospect of having to put upwards of \$50,000 into a case. Needless to say, the documents that

were ultimately produced were far less than originally requested and the numerous pending discovery disputes were resolved in a matter of days.

On our end, we likewise began defense of the case, but not in the traditional sense. In most securities class actions, months if not years are spent with the defendant producing documents and the plaintiff taking depositions of the defendant's witnesses. Meanwhile, numerous pretrial motions are litigated. Discovery related to the class representatives is typically an afterthought that takes place only at the end of discovery. As traditional plaintiff's lawyers, however, we knew that class representatives are often the weakest link in a class action case. Because of that, we decided to start there, and aggressively pursued documentary discovery and depositions of the class representatives.

Plaintiff's Counsel were puzzled at our approach and, at first, resisted. We insisted on our discovery plan. Instead of facing that prospect, Plaintiff's Counsel offered to settle. Within a matter of months of our firm taking over defense of the cases, all of them settled for far less than the \$20 million my friend was willing to pay on that fall morning when we first spoke. The distractions to his company were gone, as were the legal bills. Needless to say, he was very pleased. He was even more pleased two years later when we were able to recover every penny paid to settle the case in a later case we tried to verdict against the company's insurance carrier, which was again handled on an alternative fee basis.

Since my epiphany six years ago, our firm has represented corporations in numerous actions, all on an alternative fee basis. In fact, we now have a department of our firm dedicated to that work. These cases have involved, and continue to involve, a number of fee arrangements including contingent fees, reverse contingent fees, flat fees, incentive fees, and blends of all of these. Through these last few years, I have found that the attorney-client relationships in these cases are perhaps the best I have enjoyed in my forty years of practice. When the attorney's interests and client's interests are aligned in an alternative fee arrangement, an inherent trust develops. That trust leads to better efficiency in the litigation, better results, and a happier client. This paper discusses some of these arrangements.

History of Attorney's Fees

The American Bar Association's Model Rules of Professional Responsibility had their origin in the 1908 Canons of Ethics, which included Rule 1.5 entitled "Fees." Rule 1.5 sets out the following factors to be considered in determining a reasonable fee:

- the time and labor required, the novelty and difficulty of the questions involved, and the skill required to perform the legal services properly;
- the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;

- the fee customarily charged in the locality for similar legal services;
- the amount involved and the results obtained;
- the time limitations imposed by the client or by the circumstances;
- the nature and the length of the professional relationship with the client;
- the experience, reputation, and ability of the lawyer or lawyers performing the services; and
- whether the fee is fixed or contingent.

Although the amount of time involved has always been a factor, it was not traditionally a significant factor. While some lawyers kept notes or general time records, billing by the hour was not prevalent until the early 1960s. During that time, law firm consultants increasingly began advocating that attorneys who kept accurate time records and billed by the hour made more money. Predictably, by the late 1960s, most firms had shifted to hourly billing. Over the course of the last 40 years, that has been honed down to even the tenth of the hour.

Once firms shifted to hourly billing, the practice of law notably changed. Because billing could be tracked by the hour, it could be budgeted. As we know, that led to firms setting billable hour and rate targets for both partners and associates. As competition among lawyers increased and the economy fluctuated, many lawyers could not increase their rates enough to cover expenses. As a result,

the number of billable hours increased. Over time, the billable hour “targets” became billable hour “commitments.” Associates were judged as partnership material based on billable hours. Partners remained at law firms based on billable hours.

Law firms insisted to clients that paying for legal services by the billable hour was the most fair and efficient way to do business. But was it really? Of course, it was great for the law firm because the firm could project their revenues with a high degree of confidence. They could project their withdrawals as partners based on how many hours they were willing to work. What everyone failed to mention, however, was that the billable hour model created an inherent potential conflict between attorney and client with regards to efficiency. The ugly truth behind the billable hour model is that the longer the lawyer works on a matter (whether necessary or not), the more the lawyer is paid. What incentive, then, does the lawyer have to resolve a matter quickly and efficiently?

The corrosive impact of emphasis on billable hours has led to widespread issues in the practice of law. *See, e.g.,* ABA Commission on Billable Hours Report, 2001-2002. As noted by the ABA Report, the overreliance on billable hours by the profession:

- results in a decline of the collegiality of the law firm and an increase in associate departures;
- discourages taking on pro bono work;

- does not encourage project or case planning;
- provides no predictability of cost for the client;
- may not reflect value to the client;
- penalizes the efficient and productive lawyer;
- discourages communication between lawyer and client;
- encourages skipping steps;
- fails to discourage excessive layering and duplication of effort;
- fails to promote a risk/benefit analysis;
- does not reward the lawyer for productive use of technology;
- puts the client's interests in conflict with the lawyer's interests;
- runs the risk of the client paying for (a) the lawyer's incompetence or inefficiency; (b) associate training; (c) associate turnover; and (d) padding of timesheets;
- results in itemized bills that tend to report mechanical functions, not value of progress; and
- results in lawyers competing based on hourly rates.

While all of these issues may not be relevant to corporate counsel, many of them certainly are. Hourly billing arrangements do not require, or even encourage, the lawyer to prepare a project plan or case plan at the beginning of a client engagement. Hourly billing arrangements likewise do not reward efficiency. Indeed, the inefficient and less productive lawyer ends up billing more hours and making more money. And, without a risk/reward analysis, there is no way to

determine whether the work performed is necessary, or whether it is premature or at a cost that is not justifiable.

Hourly billing arrangements likewise generally result in higher costs. It is no secret that financial challenges for law firms result in higher billable hour requirements for partners and associates. While reputable lawyers do not pad their timesheets, high hourly requirements can put subtle pressure on lawyers to be aggressive rather than conservative in recording their time. Likewise, as hour requirements increase, the amount of time available for partners to interact and teach associates, as well as the time available for associates to train, decreases. Clients therefore end up paying for associate “on the job” training. To prove this point, take a look at your last legal bill on a substantial lawsuit and see how many attorneys are working on your case.³

Perhaps the worst problem with hourly billing is that it discourages true and open communication between the lawyer and client and instead hinges the value of a case on a mechanical formula. Every case has an intrinsic value to the client.

³Several years ago, our firm took over defense of a declaratory judgment case in which all of the officers and directors of a company had been sued. Upon looking through the pleadings index from previous counsel, we were surprised to see the number of lawyers working on the case and how much unnecessary work was done. Collectively, they had filed fifteen separate, but identical, answers on behalf of each of the officers and directors (as opposed to filing one consolidated answer). Sure enough, when we looked at the billing records, the client had been charged for every one of them.

That value may be greater than a fee based on the hours billed, or it may be less. Hourly billing never considers the value to the client. It instead produces a result that is either unfair to the client, the lawyer, or both. All the while, the client may be discouraged from even discussing the value of the case with the lawyer because they are concerned that such actions will merely start the billing clock. Without effective communication between the lawyer and client, what is there?

The Shift to Alternative Billing Arrangements

Very few foresaw the gravity of the economic downturn we have experienced over the last several years, but all of us have suffered its effects. Corporate earnings have dropped, in some cases dramatically. Law firm earnings have likewise fallen. Across the board, the economic downturn has led to a renewed emphasis on cost control. Budgets have been slashed, notably including the budgets of in-house counsel.

The emphasis on cost control has quickly led to a shift away from the billable hour model. An April, 2009 survey conducted by the Association of Corporate Counsel found that a stunning 77% of members would like to consider alternative billing arrangements in work handled by outside counsel. When asked how outside counsel could improve their relationships with in-house lawyers, 60% said they could offer alternative billing – by far the most popular answer among

respondents. This growing trend is borne out by the actions of major corporations throughout the country:

- On January 1, 2008, Pfizer announced that it was giving almost all of its U.S. labor and employment work to Jackson Lewis for the next two years in exchange for an agreement from the firm on an annual cap on its fees – no billable hours or even flat per matter fees.
- Tyco International has announced that it has outsourced all of its products liability work to a single firm who has agreed that at least a portion of the billing will be on alternative arrangements.
- Honeywell International, Inc. has announced its adoption of the single firm model, with billing done on an alternative basis.
- Late last year, Levi Strauss & Co. announced that it had selected two firms to handle all of its legal matters and that it was using alternative billing arrangements for 100% of its routine outside counsel spending.

Proof of a trend, of course, is always in the bottom line. According to BTI Consulting Group, the market is tracking for an increase this year of more than 50% in corporate spending on alternatives to the traditional billable hour model. The BTI survey of 370 lawyers who work for Fortune 1000 companies found that money spent on alternative billing arrangements totaled \$13.1 billion through November, 2009, versus \$8.6 billion for the same period in 2008, and produced average cost savings for those corporate law departments of 15%.

Common Alternative Billing Methods and When to Use Them

Ultimately, clients want to pay for results, not time. They want predictable costs, not surprises. And, in the event of a poor result or cost overruns, they want their lawyers to share some responsibility. As set forth above, the billable hour model does not address these concerns. Depending on the particular situation, the following alternatives may:

1. Flat Fee

Description: Law Firm will perform the specified legal work related to the litigation for a set fee.

Example: With litigation threatened against the Client, Law Firm was retained by Client to renegotiate a supply contract. Client communicated its goals for the contract with Law Firm, including lower costs, joint marketing efforts, and better service, but timely resolution was the overriding factor. Client and Law Firm agreed to a flat fee arrangement to negotiate the contract terms as specified by the Client.

Litigation Note: Having a respected trial litigator negotiate a contract may achieve better results. If your negotiating partner senses

that you are willing to litigate, your negotiating posture may improve.⁴

Advantages: Fee is not based on time and both the Client and Law Firm know at the outset what the fee will be. This allows the Client to budget accordingly and avoid billing surprises. It allows the Law Firm to leverage its experience and efficiency. It requires both the Law Firm and Client to document with specificity what services will be performed for the fixed fee. It gives the Law Firm an incentive to improve workflow, make better use of technology, and pay closer attention to the way in which it staffs matters.

When to use: High volume, routine work where costs are easy to predict and surprises are rare. Client is comfortable assuming the risk of a bad outcome and Law Firm is comfortable assuming the risk of cost overruns. In every instance, alternative fee arrangements should include safety valves or “reopeners” that allow both the Client

⁴These Litigation Notes are all based on examples of representations our firm has provided, and illustrate the benefits and cost efficiencies of alternative billing strategies.

and the Law Firm to revisit and revise the agreement should unforeseen circumstances occur.

2. Contingent Fee

Description: Law Firm will perform the specified legal work with no guaranteed fee. Instead, Law Firm is entitled to a percentage of recovery if the litigation is successful.

Example: Competing company tortiously interfered with Client's contractual rights. The Client communicated its goals to the Law Firm, foremost of which was to prevent such an occurrence in the future. Law Firm was retained, on a contingent fee basis, to bring tort action.

Litigation Note: After extensive discovery, and just prior to trial, the litigation with competing company settled for a sizeable amount. During the lengthy discovery period, Client paid nothing in attorneys' fees. If the case had been unsuccessful, Client would have owed no legal fees.

Advantages: Client only pays when Law Firm achieves successful results. Client does not pay for time. This approach allows the Client to pursue litigation without costs during the pendency of the litigation. It allows the Law Firm to

fully leverage its efficiency and expertise. It perfectly aligns the interests of the Client and Law Firm as they are both interested in one thing only – success.

When to use: When Law Firm is highly confident in its ability to achieve successful results through legal expertise. When Client wishes to fully align its interests with Law Firm and pay no attorneys' fees unless the case is successful.

3. Reverse Contingent Fee

Description: A Reverse Contingent Fee is useful in a limited number of cases. In essence, the Client has expressed a dollar amount that it would be willing to pay, or it believes is reasonable to pay, to resolve a pending suit against it. The Law Firm receives its compensation based on a percentage of the amount it is able to save the Client off of that amount.

Example: Client was prepared to settle a pending securities action for \$20 million. Law Firm was retained to defend the Client. Law Firm agreed to receive a percentage of any amount less than \$20 million the Client ultimately paid to resolve the action. If Client was required by settlement

or judgment to pay in excess of \$20 million, Law Firm would receive no fee.

Litigation Note: The pending cases resolved within months of Law Firm being retained. Law Firm later recovered all amounts paid in settlement in an action against the Client's insurance carrier, which action was handled on a contingent fee basis by Law Firm.

Benefits: As with a Contingent Fee, the Client does not pay any legal fees unless the litigation is successful. Again, the Law Firm has the dual motivation of resolving the litigation as quickly as possible while obtaining the best financial results for the Client.

When to use: When Law Firm is highly confident in its ability to achieve successful results through legal expertise. When Client wishes to fully align its interests with Law Firm and pay no attorneys' fees unless the case is successfully resolved.

4. Incentive Based Fees

Description: An Incentive Based Fee is just what it sounds like. The Law Firm is compensated based on achieving agreed

upon goals in litigation. This can be calculated in a myriad of ways before the litigation. It can also be determined at the conclusion of the case through a retrospective agreement on value.

Example: Company purchased competitor and included in the purchase agreement a non-compete clause with the owner of the company. Upon discovering that the former owner had started another competing business, Law Firm was retained to enjoin former owner's conduct. Law Firm's compensation was structured based upon the results achieved with an agreed upon fee for: (1) obtaining a temporary restraining order; (2) obtaining a permanent injunction; and (3) obtaining a monetary judgment.

Litigation Note: With the threat of litigation, the company and former owner reached a business arrangement financially beneficial to both parties.

Benefits: Shifts focus from time spent to the value of the results. The Client does not pay any legal fees unless the Law Firm achieves one or more of the various goals agreed to prior to litigation. This facilitates staying within a

budget, with the caveat that excesses are explained by results. The Client is also able to obtain certainty as to future legal fees which are valued prior to litigation based on their importance. The Law Firm is motivated to achieve the Client's stated goals as early in the litigation as possible.

When to use: When Client and Law Firm know and trust each other, and when the value to the Client of the results achieved can be fairly and accurately calculated.

5. Volume Discounts and Discounted Fees

Description: Law Firm reduces its hourly rates in return for Client guaranteeing a certain volume of legal work.

Example: Client agrees to send Law Firm all of its North American products liability work in exchange for a 10% reduction on all hourly rates.

Benefits: A good alternative billing start. Guaranteed work for the Law Firm saves business development costs. Reduced rates give the Client an incentive to send more work to the Law Firm.

When to use: High volume, routine matters when cost is the Client's primary concern.

6. Hybrid Fee

Description: A Hybrid Fee is a combination of a Flat Fee, a Contingent Fee, a Reverse Contingent Fee, an Incentive Based Fee, and/or a Volume Discounted Fee.

Example: Client retains Law Firm to pursue commercial litigation action for a flat fee up front, plus future fees based on the achievement of stated goals in the lawsuit.

Litigation Note: While the case is pending, the Client does not receive monthly bills for attorneys' fees. It also potentially allows the Client to pay the up front fees in installments to provide flexibility in budgeting.

Benefits: Easy to negotiate and administer. Shifts focus from time spent to the value of results. The amount of the fee is based on the value to the Client as defined by the Client. The Client is able to obtain certainty as to legal fees which are valued prior to litigation based on their importance. The Law Firm is motivated to achieve the Client's stated goals as early in the litigation as possible.

When to use: When various elements of other alternative billing arrangements collectively make sense for the Law Firm and the Client.

The list of alternative billing arrangements above is by no means a comprehensive list. Depending on the particular case, any combination of them may be applicable.

IMPLEMENTING ALTERNATIVE BILLING STRATEGIES

Now that you have decided you may want to implement alternative billing strategies, how do you do it? The simple answer is to talk to the lawyers you currently work with to see if you can negotiate an alternate agreement. The answer may not, however, be that simple. The empirical data suggests that corporate counsel are far more willing to discuss alternative billing strategies than outside counsel. Indeed, in a 2009 study by Altman Weil, Inc., only .6% of corporate counsel surveyed responded that outside counsel were “doing everything they can” to change their legal delivery service model to provide greater value to clients. A whopping majority (74%) found their outside counsel’s efforts in this regard to be less than average.

Given these statistics, implementing alternative billing arrangements may well require a look into hiring new counsel for certain kinds of cases. If that is an option, consider the following suggestions gained from our years of experience:

1. Hire local. No matter the magnitude of the litigation, there is likely a law firm in Georgia that can help your company. When litigation stakes are high, companies often tend to hire a New York, Washington, or Chicago firm. More times than not, that is a mistake. A Georgia firm brings many intangibles to the litigation (including knowledge of the local court and the judge) that are priceless to your case. Hiring a Georgia firm will also help control litigation costs.

2. Bigger is not always better. Larger firms generally possess greater resources in terms of manpower. The important question, however, is not what resources a law firm has, but what resources a law firm is going to dedicate to your case. In this regard, you may find that a smaller firm may better serve your litigation needs. According to a 2009 Altman Weil study, smaller firms are also much more likely to offer alternative billing arrangements.

3. Experience matters. More than perhaps any other area of the law, experience is critical in litigation. The litigation of your case is not a cookie cutter venture that follows the same path to reach the same result that a firm has used time and time again. An in depth analysis of the case is required to effectively shepherd your case to the optimum result.

4. Interview the lawyers thoroughly. Who will actually be handling your case? How much experience do they have? Will the case be staffed primarily by partners or by associates? Who will formulate the legal strategy? Who will be

responsible for research and writing? Who will be responsible for depositions? Who will be responsible for hearings and trials?

5. Formulate a strategy with your counsel. Too often in litigation, strategy tends to be a moving target that is set only by outside counsel with little input from the client. Make sure you understand the options and your counsel understands your expectations. Recently, we looked at a case for a disgruntled corporation who had been charged a substantial amount of legal fees in an arbitration proceeding that had been in discovery for over a year. As it turned out (but apparently unbeknownst to the corporation because they had blindly relied on counsel), the arbitration clause in the contract between the parties called for the arbitration hearing to be held within 60 days after the demand was filed. The attorneys for the plaintiff and the defendant (who were both being paid by the hour) had agreed to waive the timing provision to conduct discovery. Obviously, the lawyers' interests were not the same as the clients' interests in this case.

6. Monitor the progress of the case and your costs. Just because a lot of work is being done on your case does not mean a lot of productive work is being done on your case. Several years ago, we took over a case from a billable hour attorney who had the case for over a year but had made no real progress. When we received the file, we were shocked at the size of it given that nothing had really happened in the case. When we opened it, we found out why. Most of the file

consisted of “research” and “memos.” Hundreds of hours had been spent researching and writing memos on generic issues of the law (*i.e.* contracts are construed against the drafter, contract terms are given their ordinary meaning, etc.). Don’t let this happen to you. Monitor your cases and make sure the work being done is necessary.

7. Communicate with your outside counsel. Let them know your expectations up front and let them know if they are not meeting them down the road. Remember that the key to any successful partnership rests on open and fluid communication between lawyer and client.

CONCLUSION

The billable hour model may not yet be dead, but it is clearly under attack. Corporate counsel are increasingly concluding that more and more cases could and should be handled on alternative billing arrangements. Utilizing some of the strategies discussed herein may lead to decreased costs to your company, a better relationship with your outside counsel, and, most importantly, better litigation results.