

Taking an Alternative Approach:

AFAS

How moving beyond the billable hour can
benefit both inside and outside counsel

In the Beginning: the Billable Hour

According to [**"The Hours" by Niki Kuckes**](#), which explored "the short, unhappy history of how lawyers bill their clients," in the early 20th century, lawyers rarely billed by the hour. Instead, they employed set fees, annual retainers, a discretionary "eyeball" method and contingency fees.

Then in the 1930s and '40s, state bar associations rolled out minimum fee schedules in order to raise legal fees.

By the 1950s, the billable hour had emerged as firms' top billing choice. As Kuckes stated, "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."

While hourly fees were initially used as a baseline, with adjustments made according

to project success, by the 1970s, billable hour billing became the standard. It ascended in the '80s.

In 2002, when Kuckes published her article, she believed that the billable hour was here to stay for the foreseeable future.

She also prophetically wrote: "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."

Corporate counsel driving change, including shifting from billable hours to alternative fee arrangements, is exactly what happened.

The Arrival of AFAs

The financial crisis of 2007-2009 turned the pressure on corporate counsel to initiate a change in billing.

Weary of overbilling and inefficiency of the billable hour, plus the added demands from internal management to cut costs, corporate counsel turned to AFAs or value-based fee arrangements.

In the 2010 article [**"Alternative Fee Arrangements: An Idea Whose Time Has Come?"**](#) the authors referenced the results of a

2008 Association of Corporate Counsel survey in which 60 percent of general counsel and chief legal officers expressed that the best way for outside counsel to improve relations was to offer more alternative billing arrangements.

Altman Weil and Norton Rose's 2015 surveys reflect the trajectory of AFAs. It's crucial when adopting AFAs, that you measure and analyze the effect on success and cost-savings achieved from their implementation.

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A subtle transformation occurred: The time sheet — created as a control on 'inventory' — now became the 'inventory' itself.

-Geoffrey C. Hazard, Jr., Penn Law faculty member

AFA Adoption: Past, Present and Future



What Are Corporations Using AFAs on?

Here's what corporations reported using AFAs on in a recent survey, "The State of the Legal Industry," conducted by LLM.

 LITIGATION

54%

 EMPLOYMENT

37%

 INVESTIGATIONS

24%

 M&A

15%

 CONTRACTS

41%

 INTELLECTUAL PROPERTY

30%

 REGULATION/ COMPLIANCE

24%

 REAL PROPERTY

11%

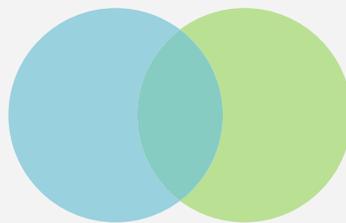
The Value of AFAs

AFAs can be used for various types of matters, such as contracts, M&A and litigation, benefiting both client and firm.

Corporate Counsel

(GC, CLO, CFO, in-house attorney)

AFAs not only help keep costs down and offer a high level of predictability for budgets, they also help mitigate risk and maintain the company's bottom line.



Both

AFAs assist in clarifying goals, fostering communication around budget and status, thus increasing trust in the firm's project staffing and strength of the client-firm relationship.

Firms

(Partner, Associate)

AFAs encourage communication about expectations, strategy and scope, which empowers proactive firms to showcase project management skills and prevent surprises for clients. An additional benefit is increased payment predictability.

As shown, AFAs can help make firms and corporations more successful in a variety of different areas. It's imperative, however, that counsel uses metrics to both measure the AFA benefit and plan for future matters.

The AFA Glossary: Pros, Cons and Goals

While the following pages define some of the more commonly used AFAs, it's not an exhaustive list. Get to know seven AFAs, what specific goals they accomplish, and their respective pros and cons.



Fixed/Flat Fees

(optional collars)

A predetermined total fee that's paid in advance for all covered work.



To gain cost predictability



- High-volume, repetitive work, sometimes commoditized work, like employment litigation, or contracts

- There are defined limits or historical knowledge of project costs



- Offers cost predictability to both client and firm

- Eliminates need to maintain detailed, incremental hourly billing

- Can encourage a firm to streamline legal services by standardizing knowledge, processes and incorporating technology



- An attorney who is "upside-down" in a case may lose interest

- Firms may put less-experienced resources on project to save costs



- Encourages communication between inside counsel and firms to handle any early surprises that arise

- Optional collars act as risk buffer for unexpected developments

Capped Fees

(optional collars)

An hourly rate for attorney time up to a determined maximum amount.



To set a maximum cost of a matter



Work similar to fixed-fee or phase-based work that can be scoped to a maximum threshold but may require less work based on certain outcomes



- Guarantees client that fees won't break internal budgets

- Firms still get paid for actual billed hours up to a point, encouraging well-managed allocation of resources



Risk to firms if time billed exceeds cap



- Firms that know how to leverage their efficiencies and expertise will be a good match for this AFA.

- Like in fixed fees, caps with collars can help buffer risk to firms if higher than expected costs.

Phase-Based Fixed

A specific fee is designated for anticipated work for each phase of a matter, similar to fixed fee.



To achieve cost predictability



Early phases of litigation or investigation matter that are more predictable



- Requires better scoping and budgeting
- Allows flexibility of implementing different fee arrangements for later, more volatile phases



Because fees for the early stages of the AFA are decided on in advance, it can require significant assumptions and analysis.

Success Fees

The firm charges a base fee at the beginning of a matter and can earn an additional fee for a successful outcome. If unsuccessful, the firm retains the original base fee, but it doesn't earn any additional reward.



To reward favorable outcomes and quality work



Variety of work where success can be defined either as monetary (contingency) or a milestone (patent validity/invalidity, finding of summary judgment or limiting damages below a threshold)



- Shares reward, not just risk, to both parties
- Aligns interests



Requires both defining what a successful outcome entails and actually reaching that outcome

Blended Billing Rate

Whether a partner or junior talent performs the work, the client pays the same rate for attorney time.



To achieve a lower hourly rate



High-risk, complex work



- Offers client a middle-of-the-road approach with potential for savings
- Client can gain senior-level work for lower rate



- Can lead to over-representation by junior talent
- Does not provide client with budget predictability

Collars and AFAs

Collars can be added to different types of AFAs as a way to mitigate risk for both parties. They work as a buffer in the event the work is less or greater than anticipated. If the amount of work falls within the collar, the agreed-upon fee is paid. If it falls outside the collar, whether more or less, clients and firms share the costs or savings.

Contingency

This is dependent on the outcome of the matter and is usually a set percentage. The client doesn't pay anything unless the attorney achieves an agreed-upon outcome.



GOAL

To have both parties share a mutual investment



BEST USED FOR

Certain types of insurance or litigation work with potential for monetary reward, clients with limited resources to finance litigation (startups)



PROS

- The client doesn't pay anything unless there's a successful outcome with monetary recoveries.
- The client can use this AFA to incentivize firms.



CONS

Firms potentially receive no payment in unfavorable outcome

••• OTHER

- Firms that are skilled at analyzing a case and determining their likelihood for success will do well with this AFA.
- Can also consider bundling together multiple litigations on contingency to increase opportunity for a reward

Volume Discounts

A client receives a discount on the standard hourly billable rates in exchange for a promised volume of work.



GOAL

To reduce costs on large amounts of work and/or reduce the number of firms



BEST USED FOR

Larger volume work that's often, but not exclusively, transactional



PROS

- Can help a client streamline number of firms it uses
- Guarantees law firms a certain quantity of business and can help in planning for resources
- Can help firms attract more business from reliable clients



CONS

Firms not incentivized to reduce hours billed

••• OTHER

If using it to consolidate firms, it can create efficiencies by having each firm become more knowledgeable about specific business needs of volume work, i.e., no reinventing the wheel with each engagement.



While this is not an exhaustive list, it does include some of the more commonly used AFAs. Based on the end goal, it can also make sense to combine different AFAs. When a more tailored arrangement is called for, a hybrid fee arrangement is possible, which can be periodically revisited for potential modification.

On the Way to AFAs: Shared Priorities and Goals

The Greatest Focus for the Next Year

Corporations and firms are in agreement on the top two greatest areas of change they're asking for.

1

Cutting costs

2

Increasing the efficiency of legal service delivery model

Legal Department's Top Budgeting Priority

To save money and for greater predictability and transparency, more departments are using AFAs for non-transactional work.



PREDICTABILITY

70%

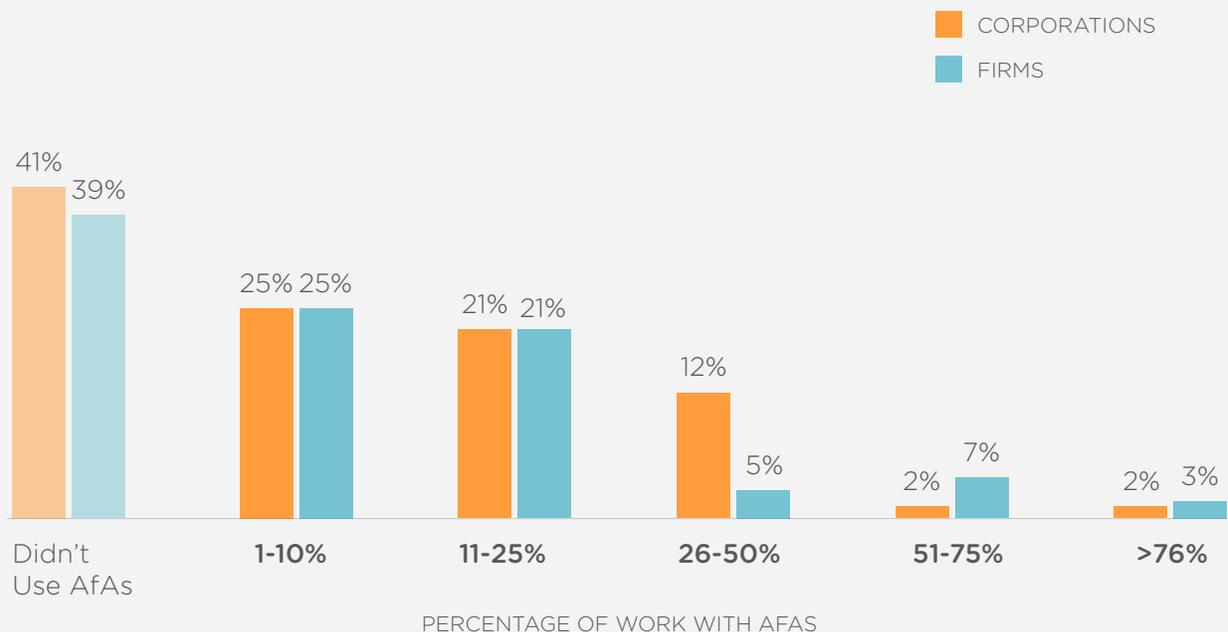
Listed as their No. 1 budgeting priority in LLM's 2016 survey, "The State of the Legal Industry."

AfAs provide the lower costs, high predictability and increased efficiency firms and corporations are asking for.



The Percentage of AFA Use for Non-Transactional Work in the Last 12 Months

(Corporations vs Firms)



LLM's 2016 survey, "The State of the Legal Industry."

Next Steps: Measuring Success



Once AFAs have been implemented, it's absolutely imperative that counsel measures their success by tracking and measuring different types of AFAs against each other and more traditional billing models.

As a result, success of implementation, effect on win/loss, whether the quality of contracts has changed and more depending on specific goals will all become clear. It also serves as a starting point for scoping and budgeting future AFAs.



Final Words



Where to begin with AFAs? With metrics!

The most immediately important metric is whether the selected AFA model will be an improvement (decrease costs, increase predictability, etc.) to the current model. Along the way, capture metrics that inform future decisions on which AFA model to use.

Counsel can also use data collected in real time to ensure the AFA continues to best serve ongoing needs, meets goals and leads to productive client-firm discussions.

For detailed information on considerations for measuring legal work, download our latest white paper, "[Cut Costs and Increase Profits with Legal Metrics.](#)"

AFAs are the alternative approach to the billable hour. By fully understanding and embracing AFAs, both client and firm can harness them to increase cost savings and profits, and improve communication and trust.

Resources



LLM, Inc.

[Cut Costs and Increase Profits with Legal Metrics \(white paper\)](#) »

[Better Budgeting Analysis, Better Predictability \(webinar\)](#) »

[Cut Costs and Increase Profits with Legal Metrics \(infographic\)](#) »

[Making it Count: Budgeting Success for General Counsel
and Legal Departments \(white paper\)](#) »

General

[“Alternative Fee Arrangements: An Idea Whose Time Has Come?”](#) »

[“The Billable Hour Is Dead. Long Live . . . ?”](#) »

[“Types of Legal Services Pricing: Fixed Fee and Retainer”](#) »

[“Alternative Fee Arrangements”](#) »

Learn how AFAs can increase predictability and save you money.

Contact Us »

About LLM, Inc.

LLM, Inc. unifies the legal process by combining legal holds, case strategy, matter and budget management, review and analytics in a single, web-based platform. We connect legal strategy to tactics in a way no one else can, so every part of the process is actionable. Our product scales to help corporate and law firm teams gain cost-savings and eliminate inefficiencies.

