



Show Me the Bill

Alternatives to the Hourly Rate

By Jerome Crawford and Erika L. Davis

Lawyers aren't cheap. That's no secret. For decades, billing clients in hourly increments has been a tradition¹ for attorneys in private practice, without regard to firm size or practice area. Presumably, the underlying justification for the hourly arrangement was to objectively communicate value to the client based principally on the amount of time the attorney spent on the client's matter.

But as with most things in life, financial pressures soon became the driving force in determining attorney compensation. The 2007-2009 U.S. economic recession² brought to the forefront the downsides of the billable hour, as there were fewer legal dollars in the marketplace, and corporate

and for-profit legal consumers began demanding more work for less money. At the same time, individual and nonprofit legal consumers began to look outside the profession for help with their legal needs, turning to the Internet (e.g., Legal Zoom and Rocket Lawyer) and nonlegal professionals such as accountants for legal assistance.³

Despite the growing prevalence of these quasi-legal service providers, people still need lawyers. This change in the marketplace and in client expectations has sparked a conversation about legal fees, specifically regarding the way in which the ultimate fee should be calculated. With increasing access to information, prospective clients are more willing

to question or challenge their attorneys, especially when it comes to billing. To stay competitive, the modern lawyer must be agile to meet these needs—even more than ever before. Alternative fee arrangements are a way for lawyers to receive compensation without relying on hourly billing.

What are alternative fee arrangements?

Alternative fee arrangements, or AFAs, present a unique opportunity for lawyers to receive compensation for services rendered. Simply put, AFAs are agreements between an attorney and client outlining the parameters of compensation using a structure *other than* hourly billing.⁴ The concept of the AFA is not new—at least it shouldn't be. Although the billable hour is heralded in the majority of law firms regardless of size, AFAs have been around for quite some time. As previously noted, however, the ever-changing financial climate of the legal market has contributed significantly to their resurgence and, as more thoroughly covered below, their evolution.

An important point to note is that AFAs are not premised on charging *less than* the hourly equivalent.⁵ They should not represent a better or worse framework for either the attorney or client. Essentially, a well-crafted AFA should provide realistic expectations for both the attorney and client on not just costs, work product, and timing, but, more appropriately, on *value*. The perception of value, of course, is greatly subjective in nature and very much in the eye of the beholder.⁶

AFAs are not about charging more than what an hourly rate might be—they are about charging an appropriate fee based on what **value** the client **receives** and how that client **perceives** value. Alternative billing should be based on what is fair and reasonable both to the client and the lawyer. Keeping track of time should be the lawyer's measure of cost, not necessarily a measure of the value he or she is providing the clients in their legal needs.⁷

FAST FACTS

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What are the benefits of AFAs?

As discussed, over time the hourly arrangement presented challenges both to the client and the lawyer. While the client had some information on which to evaluate the fee—i.e., the hourly rate—the client had no independent way of knowing how much total time a matter would take, and to be fair, attorneys didn't always have this information either. Furthermore, because firms (both small and large) had a way of measuring revenue by lawyer, attorney compensation and advancement decisions were increasingly based on the billable hour.⁸ The hourly system, while intended to create more predictability for the client and the lawyer, led to the incentivizing of inefficiency to the detriment of the attorney-client relationship.⁹

For the attorney, AFAs may be appropriate to cover a task, service, or particular offering in which he or she is well-versed and can control the time spent and process flow; for example, if it is an area in which the attorney can be efficient, an AFA is likely a good idea. For the client, AFAs can make sense for more discrete projects that have a predetermined length or work product, such as patent or trademark filings, estate planning, and baseline corporate filings. A common denominator of value is predictability.¹⁰ Law is uncertain enough; the more an attorney can regulate expectations and potential outcomes, the greater chance for a happy client in the end—even if the desired result is not obtained.

What are some examples of AFAs?

AFAs come in all shapes and sizes. Here are some of the most common examples.

Flat fees

A flat fee is often seen in transactional matters with a clearly defined outcome. That said, flat fees can also be defined for various phases of litigation.¹¹ Routinely, a trial attorney might work a case for a flat fee up until an expected event in the course of litigation, such as the close of discovery or through summary disposition motions. It may be a true flat fee or take the form of a risk collar¹² or subscription fee.¹³ Flat fees are effective because they provide the greatest amount of certainty for both parties.

Retainers

Even a lay person has heard of retainers. A client pays a specific fee, usually monthly, for the benefit of unlimited access to the attorney (as he or she may be reasonably available) for a specific service or group of services. The retainer has lost its luster over the years, especially with larger firms. However, as corporate legal departments strive to be leaner and control costs better, retainers have regained momentum.¹⁴

Contingency fees

This option is almost exclusively limited to litigation matters. Albeit uncommon, of course, a clever corporate attorney could mold a contingent fee into a transactional matter whereby different compensation would be due depending on the outcome of deal negotiations. Another tweak could be a mixed contingency fee arrangement in which a reduced hourly rate, or capped fee, is combined with a reduced contingency fee for successful resolution of the matter.¹⁵

Blended rate

For a blended rate, you need to calculate the average rate for the timekeeper lawyers on the file and apply that rate across the board, without exception to whether that time is spent by a partner or associate.¹⁶ Naturally, this structure lends itself to larger firms. It is also most beneficial to the firm if the bulk of the workload can be handled by timekeepers with lower billing rates.

Reduced hourly rate with kicker

This unique arrangement is matter specific and regularly used when representing a defendant in litigation; a basic assumption is that it is costlier for that party the longer the case goes on, so the client is willing to pay more if there is an earlier resolution.¹⁷ For example, the effective hourly rate would be higher depending on how long the firm has the file before a satisfactory resolution is reached. Attorneys under this structure are incentivized to wrap up the case as quickly and efficiently as possible.

Conclusion

Regardless of the form, an AFA must comply with the Michigan Rules of Professional Conduct. Specifically, the fee charged under an AFA must meet the standard for reasonableness articulated under MRPC 1.5(a). We hope you find this guidance useful as you consider building a more agile billing structure in your own practice. ■



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ENDNOTES

1. What does (or does not) constitute "traditional" billing is subject to interpretation, depending on time and context. In the early twentieth century, lawyers used a variety of billing methods, including flat fees, success fees, rough budgets, and monthly retainers. See, e.g., Boulden, *The Business of Startup Law: Alternative Fee Arrangements and Agency Costs in Entrepreneurial Law*, 11 J on Telecomm & High Tech L 279, 280 (2013). For purposes of this article, "traditional" billing is the hourly rate.
2. United States Bureau of Labor Statistics, *BLS Spotlight on Statistics: The Recession of 2007-2009* (February 2012) <http://www.bls.gov/spotlight/2012/recession/pdf/recession_bls_spotlight.pdf>. All websites cited in this article were accessed April 29, 2017.
3. Barton, *Lessons From the Rise of LegalZoom* (June 18, 2015) <<https://bol.bna.com/lessons-from-the-rise-of-legalzoom>>.
4. VanPuybrouck & Kurtzman, *The Rise of Alternative Fee Arrangements* (December 11, 2013) <http://www.americanbar.org/content/dam/aba/administrative/litigation/materials/2015_corporate_counselcseminar/Materials/15p_2_the_rise_of_alternative_authcheckdam.pdf>.
5. Ilna Rejeva, Legal Trek, *Alternative Fee Arrangements: A Comprehensive Guide for Law Firms* <<https://legaltrek.com/blog/2015/09/alternative-fee-arrangements-a-comprehensive-law-firm-guide>> (posted September 16, 2015).
6. *Id.*
7. Robertson, *Marketing Alternative Fee Arrangements* (September/October 2011) <http://www.americanbar.org/publications/law_practice_magazine/2011/september_october/alternative_fee_arrangements.html>. (Emphasis added.)
8. *The Business of Startup Law*, 11 J on Telecomm & High Tech L at 280-282.
9. Barnes, *The Real Reason There Are Fewer Law Firm Jobs* (What No Attorney Wants You to Know) <<http://www.lawcrossing.com/article/900042586/The-Real-Reason-There-Are-Fewer-Law-Firm-Jobs-What-No-Attorney-Wants-You-to-Know/>>.
10. Cordo, *Alternative Fee Arrangements: New Ways to Get Paid* <http://www.americanbar.org/publications/law_practice_magazine/2013/march-april/alternative-fee-arrangements.html>.
11. American Bar Association, *Alternative fee arrangements: A primer* <http://www.americanbar.org/news/abanews/aba-news-archives/2013/08/alternative_fee_arra.html>.
12. A risk collar is created using an estimated budget based on an hourly rate. If the firm completes the work under budget, then the client pays a "bonus"; if the work is done under budget, then the client receives a discount. *The Business of Startup Law*, 11 J on Telecomm & High Tech L at 291.
13. A subscription fee is a repetitive flat fee whereby the client pays a monthly subscription for the lawyer's services. The lawyer is required to perform the services included with the subscription, which may vary from month to month depending on the client's needs. *Id.* at 292.
14. American Bar Association, *Alternative fee arrangements: A primer* <http://www.americanbar.org/news/abanews/aba-news-archives/2013/08/alternative_fee_arra.html>.
15. *Id.*
16. *Id.*
17. *Id.*