

## Kirkland Expands Use of Special Fee Structures

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In an effort to keep cash-strapped clients in the fold, **Kirkland & Ellis** is expanding its use of alternative-fee arrangements -- discounting rates and extracting promises of future work from corporate players.

During the past three years, the firm says it has given away more than \$100 million worth of billable hours, but it hopes to make the revenue back through follow-up work from those clients. Reed Oslan, the Kirkland partner who is leading the firm's alternative-billing efforts, says that it hopes to expand the program. "It's been a mutually successful program for both the clients and the firm," Oslan said.

Though \$100 million represents a very small percentage of the firm's fee income -- last year Kirkland grossed \$1.4 billion, according to *The American Lawyer* -- the effort may be one of the most extensive at a major firm. Pamela Woldow, a consultant with Altman Weil who specializes in alternative-billing arrangements, said Kirkland is the largest firm by revenue or head count making the most of such arrangements.

Others that are aggressively pursuing alternative arrangements are Morgan, Lewis & Bockius; Alston & Bird; and Holland & Knight, said Woldow. "In the last two years, all four of those firms began digging into alternative-fee arrangements, so they're way ahead of the curve," said Woldow. "They have figured out how to make it profitable."

Smaller firms also making headway in the area include Butler, Snow, O'Mara, Stevens & Cannada of Jackson, Miss.; Saul Ewing of Philadelphia; Lewis and Roca of Phoenix; and Parker Poe Adams & Bernstein of Charlotte, N.C., she said.

The firms are pursuing more common alternative-billing arrangements such as fixed fees, capped fees and contingent fees. But Kirkland is also offering hybrid approaches: Under one arrangement signed in March, the firm agreed to handle two dozen of a longstanding client's defense cases at a discounted monthly fixed fee in exchange for the first right of refusal on all the client's plaintiff cases during the next three years, with the firm taking one-third of the recovery in the plaintiff matters.

At a meeting on alternative billing arranged by Kirkland last month, the firm said that the benefits of the arrangements for clients are a greater degree of certainty with respect to the cost of litigation, an ability to shift more risk to the law firm and less need to track billable hours and supervise staff. The firm stands to gain if it can perform the work so efficiently as to allow a premium in the final payment. It may also lose money if it miscalculates or meets an unexpected hurdle.

The firm and the client benefit from the structures, which are determined on a case-by-case basis for either defense or plaintiff matters, because their incentives are more closely aligned, Oslan said. Oslan wouldn't specify what kind of premium above its standard fee Kirkland sometimes reaps from the arrangements, but said that the firm occasionally takes multimillion-dollar write-offs when it bets wrong. He also declined to disclose what percentage of the firm's revenue derives from such arrangements, but said it was "meaningful."

Although the firm doesn't want to lose money, it also doesn't want to make so much as to damage a relationship with a client, he said. "It allows the client to take their guard down somewhat when they know that the law firm's fee is tied to delivering a success in the matter," he said.

## ACCELERATING ARRANGEMENTS

Kirkland has entered into 49 of the arrangements during the past three years, accelerating its use of the arrangements after logging just 32 in the prior 12 years. The number of attorneys working under such arrangements nearly doubled to 242 last year, up from 147 in 2006, Oslan said.

At its meeting last month, Kirkland hosted about 150 clients on the topic at the firm's Chicago office. The firm plans to host two more meetings in New York and San Francisco later this year as it tries to fan interest in the deals, said Oslan, who is based in Chicago. The firm is trying to build up use of the arrangements after first experimenting with the approach 15 years ago.

Firms have become more amenable to the arrangements as corporate clients clamor for relief from standard billing rates amid a recession that has forced their companies to slash spending, including the law department budgets. In an Altman Weil survey of law firms in March and April, 93 percent of the 208 firms that responded said they use some type of nonhourly billing, but the majority said that those revenues accounted for 10 percent or less of total revenue last year. All six of the firms with more than 1,000 lawyers that responded to questions about alternative-fee structures fell into the 10 percent-or-less category, but 14 percent of those with 500 to 999 lawyers said that from 11 percent to 20 percent of revenue came from the pacts. The percentage of revenue stemming from the arrangements rose as the size of the firm declined, with all firms of fewer than 100 lawyers deriving at least 30 percent of revenue from the arrangements.

## LEADING THE WAY

Some of the smaller firms have been among the biggest innovators on the alternative-billing arrangements, Woldow said. Butler Snow, which has 150 lawyers, earns about 20 percent of its revenue through such pacts with about 50 clients, including international pharmaceutical and medical-device companies, said Charles Johnson, a partner at the firm who helped pioneer the arrangements at his firm starting back in 1989. The firm has increased its use of the structures in the past two years as more general counsel have become interested in discussing them, he said.

"Everybody's budget is getting greater scrutiny, and they see it as a way to add certainty to their budget," Johnson said of clients who gravitate to the arrangements. "It's on the agenda of all GCs to explore."

In one arrangement, Butler Snow is handling all contract matters for an international pharmaceutical company on a fixed-fee basis and is performing litigation work for the same company at a fixed fee for each stage of the work or in some cases for a "blended rate" that allows a single rate to be billed by all attorneys regardless of seniority.

Still, some sophisticated clients are reluctant to negotiate the nontraditional payment plans because they don't have the historical data they need to determine what is and isn't financially advantageous, Johnson said. In those cases, the firm will try to reassure the client by offering a review of the arrangements six months into the transaction to make sure that initial assumptions are on track, he said.

The firms surveyed by Altman Weil also said they expect to earn more from the arrangements this year. Of the six firms with 1,000 or more lawyers, one expected to boost its income from nonhourly work to the 11 percent-to-20 percent range this year; of the firms with 500 to 999 lawyers, 36 percent expect to be in that category; and 43 percent of the firms with 250 to 499 lawyers expect to end up there.

Three firms with 1,000 or more lawyers said the arrangements tend to be "less profitable" than hourly fees, and two said they were "more profitable" or "as profitable" as the more traditional fee method. Smaller firms mainly said the arrangements were "as profitable."

"I have not seen a huge uptick in the use of alternative fees across the entire industry," said Woldow. "I have seen specific firms adopt and adapt it to their clients."

At Kirkland, partners say they are primarily responding to clients' demands for the arrangements, which are attractive largely because they allow flexibility based on a particular client's needs, said John Desmarais. Desmarais sits on the firm's management committee and has used the arrangements with the intellectual property group that he leads. The firm has a special committee that reviews the arrangements and is glad to enter the agreements "as long as there's an appropriate reward for Kirkland if it performs well," he said. "It's a better solution than just giving a discount."