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Value Billing and Alternative Fee Arrangements: What are we Really Talking About?

A Client and a Lawyer Walk in to a Bar.

The client says “we want you to provide us with value billing.” The lawyer says “we’re big believers in alternative fee arrangements and have very sophisticated AFA programs.” The client says, “Okay, how much are you going to reduce your rates?”

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December, 2010**

When it comes to value billing, are clients and lawyers speaking the same language?

In 1985, while still actively practicing law, I defended a claim brought by a diversified Fortune 500 Company against my client, a relatively small manufacturer of fluidized bed heat treating furnaces. These furnaces are, among other things, designed to harden certain ferrous metals for greater endurance. For example, many of the metals in automobiles require enhanced hardening beyond their natural state. This enhanced hardening is achieved by heating the metals above 1,200 degrees Fahrenheit for fixed periods of time. The breach of warranty claim was straightforward: The plaintiff purchased such a machine for \$103,000 and it claimed it did not function as warranted. It wanted its money back. An AmLaw 100 firm prosecuted the case. The lawyer handling the case has since become a federal judge, while I sit from my perch here and jot my musings.

Early discovery in the case and my client’s own engineers’ inspection of the device at the

plaintiff's facility led us to quickly conclude that the problem was that the plaintiff's personnel were simply not properly operating the equipment. Our conclusion was not surprising: In 50 years of business, no customer had ever successfully prosecuted a breach of warranty case against my client. To be sure, this 1,000% batting average was not the result of outstanding lawyering; rather, my client had an excellent product and high quality control standards.

In a very early settlement conference, my client offered to provide the plaintiff's personnel with additional training at no added charge and further offered to refund the full purchase price plus some portion of the legal fees if an independent academic expert mutually acceptable to the parties reported that the device was in fact not operating as warranted. The plaintiff's division head summarily rejected the offer and in an expression of refreshing candor conceded that his division was not meeting net revenue expectations and he needed to get rid of both the machine and the personnel needed to operate the unit if he were to get close to meeting his division's net revenue projections.

Against this backdrop, my client's CEO called me and told me that he could resolve the case quickly. His company had received an order from a different customer that required the purchase of \$10,000,000 worth of refractory brick (that is brick that can sustain consistent high heat, such as you will find in your own fireplace) and that our plaintiff, through a different division, was one of the nation's three largest manufacturers of such refractory. My client was prepared to issue a PO for this refractory to the plaintiff, while still providing the promised additional training.

Sounds easy, doesn't it? The plaintiff would get the full benefit of its bargain and profit from the new order. Yet the plaintiff's division manager refused, since his division would not be credited with the sale and he still needed to trim costs to meet revenue projections. Try as we might, opposing counsel and I, who agreed privately that the proposed resolution was sound and an outstanding commercial resolution, just could not get the plaintiff, even at its highest corporate offices, to buy in on the deal.

We nonetheless settled the case quickly thereafter. My client simply repurchased the machine and resold it within days to the United States Department of Energy for \$135,000. The PO for the refractory was issued to a competitor of the plaintiff.

The litigation costs were far less than anticipated for both sides, and in today's parlance we provided "value billing." We provided efficient professional services and concluded a potentially complex litigation, at a fraction of the budgeted cost. But, did we really provide "value billing?"

This quarter century old case came to mind as I sat through the National Law Journal's Managing Partners Conference in Washington on December 2.

The conference included much talismanic recitations of "value billing." Actually, the repeated catch phrase that captured my ear was the too oft cited "legal spend." The repeated juxtapositions of the two phrases by each presenter, extremely capable law firm leaders, to be sure, was rather straightforward: Corporate clients were slashing expenses for outside counsel

and law firms were scrambling to maintain significant slices of the shrinking pie by discounting prices.

It's now been two years since the Association of Corporate Counsel issued its ["Value Challenge"](#) and perhaps it's now time to reconsider the concept and perhaps re-define re-think what legal "value billing" really should mean. [I readily admit to be a value billing junkie.](#)

A principal problem in the ACC Corporate Challenge is its rather wholesale reliance on defined metrics. Professor Steve Harper, a former [Kirkland partner, recently reported that reliance on metrics is frequently misplaced.](#) I long ago joined a chorus of others in raising the issue of the "mother" of all metrics; the much touted annual AmLaw 200 [report on law firm profitability is slightly less than gospel.](#)

The National Association for Legal Placement, which has a key part of its mandate issuing reports on the metrics of recent law school graduates issues [reports on that are nothing more or less than picture perfect portraits of opacity.](#) NALP and its constituents are unwilling or unable to answer a simple question: "If I decide to go to law school, work my butt off for three years and incur \$200,000 in debt, what is the likelihood that I will get a well paying job? If the law schools let me know how their recent graduates managed, I could make an informed decision." An Indiana Jones inspired group, [The Law School Transparency Project](#), embarked on a good faith search for this holy grail of metrics and short of an extremely unlikely national labor strike there is very little likelihood that actual metrics will ever be found.

The point here is that metrics are ephemeral, misleading, quixotic, enigmatic and too often of little assistance in getting the full measure of quality.

All of which brings me back to my original questions: exactly what is value billing, how is it measured (or even recognized) and how should it be rewarded?

Indeed, even with the ever rising crescendo demand by corporations for Alternative Fee Arrangements over the past 30 months, [corporate general counsel are still expressing confusion and uncertainty regarding the concept](#) while law firms, eager to satisfy a dwindling client base believe they have risen to and met the Alternative Fee Arrangement challenge, [remain perplexed about why they are having so much difficulty marketing AFA's.](#)

Metrics are simply just but one, and only one, variable in a far more complex algorithm by which value is measured.

I think we all need to get back to basics and view the issue in the context of law school: Classroom participation counts.

Let's posit the query in a Socratic hypothetical: Assume a sophisticated client believes it has perfected the alchemy to turn dross in to gold. All that it needs is the capital to finance the R&D and the assistance of regulatory specialists to gain required governmental approvals. At a networking event at law firm or through some [blog postings by a law firm](#), the client makes the connection to obtain financing and is introduced to scientists who can serve as Scherpas through

the regulatory gauntlet. Clearly, the client has already obtained value (of the most prized, sort, since it came at no cost) but now it needs to engage counsel to handle the lawyering. Corporate counsel, guided by his or her own Sherpa, the purchasing agent, issues an RFP and circulates it among the usual suspects, including the networking event host and blog poster. Five acceptable proposals are submitted, with network hoster and blogger proposing a fee schedule placing it as the second most expensive bidder in a tight race. As John Belushi asked, “who are you going to call?”

General Counsel: How do you answer Belushi’s question? Hit the comment section at <http://kowalskiandassociatesblog.com/2010/12/07/alternative-fee-arrangements-value-billing-metrics-in-a-dwindling-marketplace-for-legal-services-are-we-all-marching-to-the-beat-of-the-same-drummer/> and share your thoughts.

The Law Firm and the Lawyer as a Marketplace for Value

Lawyers who have achieved marketing successes have done so because they intuitively comprehend that they add value because they have developed a network of contacts and that this network is a constant work in progress. Whenever such a lawyer is in contact with a member of his or her network, his or her first instinct is to calculate in nanoseconds which of his or her other network contacts can add value to that contact. The primary skills for achieving this result is listening to the speaker and then instantaneously calculate how value can be added to the speaker by hooking him or her up with another network member and for each to develop synergies, business alliances, business solutions and more spokes attached to the hub of the marketplace for value. No direct metric can be attached to this activity nor will immediate revenue derive from having a lawyer or a law firm function as a marketplace for value. But the simple fact is that clients will flock to lawyers who regularly add value, even if no invoice can be rendered for the value received by the client in having commercially enjoyed the benefit of this marketplace for value.

As for law firms, it is your job to demonstrate the entitlement to a higher grade by touting your own classroom participation and the real value (not the metrics) you added to the client:

- **During your own [marketing calls to your clients](#), show how you added real value, not just a lower bill.**
- **In responding to the RFP, don’t be shy as to expressing a willingness to meet the competition (*But only meet the competition after you have first assured yourself that you can manage the engagement at a reduced fee which still yields profitability; as more than ever, risk assessment and project management are the elixirs for survival in the AFA world*).**
- **Just as the swallows head south for Capistrano at this time of year, so too does the annual debate concerning the value of client surveys fill the air. Does your client survey ask the simple question “other than lowering our fee structure, how else can we add value?” In your client survey submission, cite instances in which your firm added *real value* to a client’s business (other**

than simply by reducing fees); solicit suggestions from clients regarding how your firm can add *value*, not just reduced metrics.

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