

Business of Law

Using Alternative Fee Arrangements to Increase New Business



Contributed by
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In a recent survey, ALM Legal Intelligence found that 62 percent of law firms had increased their use of alternative fee arrangements (AFAs) in the last year, and their top reason by far (91 percent of 194 firms) was to “attract and maintain clients.”

While some firms are just starting down this path, others have been using AFAs to develop new business for quite a while. According to Peter Kalis, the chairman and managing partner of K&L Gates, a global firm with nearly 2,000 lawyers, “We have offered alternative fees for more than 20 years . . . We were dragged there kicking and screaming by a few key clients who led this trend, including DuPont and United Technologies. We found to our amazement that it was a really good way to do business, both for us and for the client.”

Adams and Reese, a firm with 13 offices throughout the southern United States, began offering AFAs for the same reason. The firm encountered several situations “where we wouldn’t get the work unless we agreed to a flat fee or fixed fee,” according to firmwide managing partner Chuck Adams. For example, “We work with one global company that requires standard trademark and patent services in a number of foreign countries, and we do all of their intellectual property work for a flat fee. We trust them, at their full discretion, to pay us a bonus at the end of each year if they think they’re getting value. The agreement gets renewed every year, and they do treat us fairly.”

In addition, Adams says, “we have relationships with some companies that have a large number of fairly similar transactions. We represent entities that buy hundreds of thousands of acres of timberland and they have a volume of fairly similar sales of smaller parcels. When there’s a closing, it becomes pretty much a commodity, a fairly standard transaction. We have arrangements with a number of clients like this to handle things on a pure flat fee arrangement.” These types of arrangements work best when one “has a good prior relationship with a client. We understand how they do business and what they need, and are therefore able to price it in a reasonable way.”

Joseph E. Mais, firmwide chair of commercial litigation at Perkins Coie, a firm with over 850 lawyers in 19 offices in the US and Asia, made a similar point in discussing his firm’s approach to AFAs: “They require a fair amount of trust. They also require significant knowledge of the client’s business to be priced and staffed appropriately.” For this reason, Mais says, it’s easier to offer AFAs to existing clients when there is a mutual understanding than to new clients who are unknown.

Like K&L Gates and Adams and Reese, Perkins Coie first started offering AFAs due to client demands. In fact, Mais identified two categories of work in which “if we weren’t prepared to offer AFAs, we wouldn’t be getting hired for a significant portion of the work” - the representation of policyholders in insurance coverage work, and patent work in which the firm represents defendants who are sued by non-practicing entities. The coverage work is generally done on a partial contingent fee basis - a monthly rate with a success fee. In the patent sphere, says Mais, “the predominant AFA model is a fee cap, hopefully coupled with success fees.”

In some cases, AFAs have also proven useful in attracting new clients. For example: “In multi-party cases, one or more defendants might seek to join forces with a longstanding client, where everyone believes there can be efficiency in having a single law firm dealing with common issues. Here, we have had a fair amount of success bringing in new clients on an alternative fee basis when they weren’t our primary relationship at the start.”

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At Crowell & Moring, a firm with nearly 500 lawyers in eight offices, Kathy Kirmayer, chair of the D.C. litigation group and a member of the firm's finance and AFAs committees, notes, "We have been using AFAs for more than a decade and don't view them as 'alternative' because we think they provide value that far exceeds just the bottom line." The firm has refined another innovative technique for using AFAs to bring in new clients with a type of antitrust proposal that is unusual for a large corporate firm.

When a corporation pleads guilty to some sort of antitrust violation, Kirmayer says, Crowell & Moring lawyers often identify not only firm clients that have purchased significant amounts of the product that has been subject to price-fixing or similar conduct, but sometimes companies new to the firm as well. Those purchasers will usually have the right to sue the antitrust violator for money damages, and verdicts or settlements can run into the tens or hundreds of millions of dollars.

Crowell & Moring's "recovery practice" represents purchasers for a contingent fee - a percentage of the amount it is able to recover for the client. This has been very appealing for new clients of the firm, Kirmayer says, and several clients that established their relationship for this type of work later have grown their relationship with the firm in other practice areas for work on non-contingency matters.

This practice started more than a decade ago when some existing corporate clients sought counsel from the firm, saying they had been victimized by antitrust conspiracies, and asked the firm to represent them. Then Crowell & Moring expanded the practice to serve existing clients and to cultivate new ones, which it sees as an investment in the future.

"We are really in this in order solve the immediate problem for the client and then to develop them into institutional clients of the firm," Kirmayer says. "We want to demonstrate what kind of lawyers we are, beyond these antitrust cases." Although antitrust is the core of the recovery practice, Kirmayer says Crowell & Moring has expanded it for trade and customs duty cases, intellectual property, and tax matters as well.

Jonathan Cooper, a partner at the Cleveland office of Tucker Ellis, also reports that AFAs have been an excellent way to attract new business for his firm.

One technique that Tucker Ellis has used is to bill a fixed sum on a quarterly or monthly basis for all legal work of a given nature such as tort defense or employment litigation. These arrangements often include a risk collar. If the actual hourly cost proves to be less than the agreed upon fee, the client and the firm split the savings 50/50. If the actual hourly cost exceeds the fixed price, the client pays half of the overage, and the firm pays the other half. "This mitigates both risk and reward and provides incentives and openness between the lawyer and the client," Cooper says.

For example, Tucker Ellis used this type of arrangement to get some mass tort work from one large state by agreeing to a fixed quarterly payment with a risk collar. "The client's associate general counsel was dissatisfied with her previous law firm because of

uncertainty about the fees," Cooper recalls. "She loved this new approach. Many clients think lawyers are just trying to bill as much as possible to rip them off, and this clearly wasn't the case with us."

In another type of arrangement, Tucker Ellis approached a client that had been on the wrong side of a multi-million dollar verdict, and asked to handle the appeal in exchange for a percentage of the amount that the client would save if the appeal were successful. "This worked well. We thought there was a high chance of winning the appeal. The client got a top-flight appellate lawyer, and the incentive was running the client's way," Cooper says.

At Warner Norcross, senior partner J.A. Cragwall Jr. has found that AFAs have been equally attractive to their clients. In one case, the Michigan firm was competing for a large chunk of national business litigation for a Fortune 500 manufacturer. Also in the running, Cragwall says, were other major firms from money centers such as New York, Chicago, Cleveland, and Milwaukee.

Cragwall reports that Warner Norcross was able to get the work, and develop an ongoing relationship with this major company, by "working up a budget, and then proposing to bill the client for a portion of the budget each month." If the matter were resolved earlier than planned, the law firm would split the savings with the client. That way, Cragwall says, "the client may get a surprise, but it's a good surprise."

This particular client, Cragwall explained, felt that the best way to get a handle on spiraling legal costs was to "control cycle time - the time that it takes to finish a matter." The firm's alternative fee proposal responded directly to that concern.

At the Jackson, Mississippi, office of Butler Snow, partner Charles Johnson III says alternative fees "have become a standard way of doing business for us. We have some clients who prefer hourly billing, but more and more of our clients want and expect predictability."

Johnson says that in the past five years, for example, Butler Snow has begun to do all the nationwide product liability work for a global top 20 pharmaceutical firm by offering alternative fees. In addition, the firm has been able to land a considerable amount of transactional and contract review work for that client by using its experience to accurately estimate how much time each task will take.

"For these deals, we are now able to offer a fixed fee for due diligence and advance work, another fixed fee for the drafting and negotiating process until closing, and another fixed fee for closing and post-closing work," Johnson says.

All of the firms described in this article, and many others, have found that AFAs can help bring in new business.

Some firms aggressively promote AFAs. Others, like K&L Gates, describe their approach as "agnostic." According to chairman Peter Kalis, "For some clients, it's a requirement to use AFAs. For others, it's an arrow in our marketing quiver. We shoot it a lot, and some clients duck and others welcome it . . . We're happy to offer AFAs and happy to go hourly . . . We truly don't

have a preference Our historical client base consists of extraordinarily sophisticated consumers of legal services. When they are able to engage in an informed dialogue with a provider of legal services on a subject near and dear to them, that is always a positive step in the relationship.”

In general, Kalis says that the AFA movement has been “a healthy development in our profession. I think it’s a sign of the maturation of the industry, that law firms and clients are having more informed discussions about the cost of legal services than they did ten years ago.”

In addition, “AFAs are a great tool for helping law firms meet client needs in a way that furthers the relationship,” according to Chuck Adams of Adams and Reese. “But the most successful ones develop from existing client relationships because clients and lawyers must be in synch. It is critical to understand clients’ expectations, their philosophical approach. Do they want to turn over every rock, for example, or just the basics? Lawyers can eliminate inefficiency, and staff and price AFAs best when they understand this and there is a relationship of mutual trust.”

“It can be complicated to work these things out,” according to Perkins Coie’s Mais. “But my guess is that AFAs will grow as big companies continue to converge on using fewer law firms and developing deeper relationships with their lawyers.”

The 194 law firms in the ALM Legal Intelligence survey agree: 82 percent expect the volume of AFAs to increase over the next five years.

To assure that this trend works out for both clients and their firms, Mais says: “The most important core principle for AFA success is to align the firm’s interest with the client’s interest.”

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