
ALTERNATIVE FEE ARRANGEMENTS: AN IDEA WHOSE TIME HAS COME?

Introduction

Few people, and few sectors of the business world, have been immune from the impact of the economic decline in the United States in recent years. Businesses and individuals alike are looking for new and innovative ways to reduce their expenses, and attorneys and their clients are no exception.

In this new legal economy, many clients have begun to reexamine the concept of alternative fee arrangements (“AFAs”) as an alternative to the billable hour model of legal services. A survey conducted by the Association of Corporate Counsel in 2008 found that 60% of general counsel and chief legal officers believed that the best way for outside counsel to improve relations would be to offer more alternative billing arrangements.¹ Moreover, 77% of those surveyed wanted to increase the percentage of their respective businesses’ spending on legal services which consisted of alternative fee arrangements.²

Although many attorneys and larger law firms traditionally have been resistant to calls for a movement away from the billable hour as the primary measure of the value of legal services performed, recent economic struggles have motivated some to revisit the possible use of AFAs. Frederick J. Krebs, president of the Association of Corporate Counsel, recently opined that the sharp decline in the economy in recent years may have finally resulted in a “tipping point” which will require attorneys to consider other options in terms of legal billing.³ Scott Turow, a well-known author of legal fiction who also works at a large international law firm, has declared that the use of AFAs is essential to law firms’ continuing financial success: “Without alternative billing schemes,” he says, “Lawyers will not be able to maintain the rapid escalation in incomes that big firms have seen.”⁴ As a result, clients and attorneys alike are once again taking a long, hard look at possible alternatives to the billable hour.

I. The Rise Of The Billable Hour

Early in our nation’s history, attorneys’ fees were strictly regulated and limited by state law, and the loser paid the prevailing parties attorney’s fees. Many attorneys earned their living through annual retainers and/or bonuses from satisfied clients. With the overall decline of economic regulation in the U.S. during the 19th century, however, state maximum-fee laws were repealed. By the early 20th century, attorneys charged for their services in a number of different ways, including fixed fees for particular tasks, annual retainers, and various more discretionary methods. The contingency fee also gained widespread popularity with attorneys after it was approved as ethical by the American Bar Association in 1908. Attorneys rarely billed on an hourly basis before well into the twentieth century.⁵

During the late 1930s and 1940s, many state bar associations began to publish “minimum fee schedules” setting standard prices for particular legal services. While these schedules purported to be voluntary, a lawyer whose fees were deemed too low would often be threatened with disciplinary action if he did not raise his fees to meet the applicable schedule. By way of example, the Virginia State Bar, warned that any attorney who “habitually” charged less than the scheduled fees would be presumed guilty of misconduct. Similarly, the ABA’s model ethical code, which was in effect until 1969, deemed it unethical for an attorney to “undervalue” his legal services.⁶

1 Jim Hassett, *The LegalBizDev Guide to Alternative Fees*, July 2009, at 4, at <http://www.legalbizdev.com/files/GuideAlternativeFeesSx.pdf>, citing <http://www.acc.com/legalresources/resource.cfm?show=196674>.

2 *Id.*

3 Jonathan D. Glater, *Billable Hours Giving Ground at Law Firms*, N.Y. TIMES, January 29, 2009, available at <http://www.nytimes.com/2009/01/30/business/30hours.html>.

4 *Id.*

5 Niki Kuckes, *The Hours*, LEGAL AFFAIRS, Sep./Oct. 2002, available at http://www.legalaffairs.org/issues/September-October-2002/review_kuckes_sepoct2002.msp.

6 *Id.*

As the practice of law became more complex, fee schedules and other flat-fee arrangements, including retainers, proved increasingly unworkable and were deemed obsolete. In addition, the civil litigation process – most notably, pretrial discovery – was dramatically expanded by the reform of the Federal Rules of Civil Procedure in 1938 and the later incorporation of all or most of the Federal Rules by individual states in the years that followed. As the amount and complexity of pretrial discovery increased significantly in the years that followed, “trial lawyers” became “litigators” who spent much more time exchanging paper and participating in motion practice than they spent trying cases. Another result of these pretrial procedures was that the time expended on a particular matter grew increasingly unpredictable and became subject to circumstances beyond the attorney’s control, making the determination of a flat fee a complex problem for both attorney and client. As this took place in litigation, government regulation of corporations and business activities also increased dramatically, with the result that transactional legal work likewise became significantly more complex and difficult to price in advance.⁷

Before the late 1950s it was uncommon for attorneys to charge by the hour or to furnish itemized time records to their clients; most attorneys’ bills simply stated a total fee “for professional services rendered” on a specified matter. Subsequently, timekeeping was introduced by management consultants, in part as a means for firms to increase revenue. Use of the billable hour spread like wildfire, and by the 1970s, bills increasingly reflected the amount of time spent on clients’ matters, with fees calculated solely on the basis of time spent on a particular matter.⁸

Proliferation of the billable hour was seen as benefiting both law firms and corporate law departments. Law firms viewed it as a “cost plus” arrangement for billing purposes which removed all outcome-related risk from their shoulders, while corporate law departments believed that use of the billable hour and the resultant detailed billing statements provided an accurate measure of whether the client was receiving value commensurate with what it would be paying for the work done. The billable hour thus fit quite well into an accounting-based approach to managing legal service which was well accepted during this time period.⁹

By the 1980s, the billable hour had become the norm, and law firms were setting billable hour goals for their associates. By the early 1990s, those goals had evolved into quotas at many law firms, especially those in major legal markets on the coasts, resulting in a significant increase in the number of hours worked by associates at those firms.

II. Arguments Against The Billable Hour And In Favor Of Alternative Fee Arrangements

The call for use of alternative fee arrangements in place of the billable hour is nothing new. In 1993, the *New York Times* wrote of the increasing use of AFAs as “an accelerating revolution, driven mostly by clients, in the way the nation’s law firms do business. It is, industry analysts say, a cultural revolution that puts a premium on serving clients, not racking up hours, and on producing quality work, as clients define it: work that places an emphasis on timely performance, efficiency, risk-sharing between the firm and its clients, and the firm’s willingness to discuss how cost estimates were arrived at.”¹⁰

Although there have regularly been murmured complaints about the claimed inequities and potential problems of the use of billable hours since at least the late 1980s, however, the movement appeared to gain greater momentum shortly after the turn of the millennium. In 2002, the American Bar Association’s “Commission on Billable Hours” issued a report based on the premise that “many of the legal profession’s

⁷ *Id.*

⁸ Thomas L. Sager and Steven A. Lauer, *The Billable Hour: Putting a Wedge Between Client and Counsel*, LAW PRACTICE TODAY, Dec. 2003, available at <http://www.abanet.org/lpm/lpt/articles/fin12032.html>.

⁹ *Id.*

¹⁰ Margot Slade, *Revolution in Lawyers’ Fees: The Meter is Being Shut Off*, N.Y. TIMES, Oct. 22, 1993, available at <http://www.nytimes.com/1993/10/22/news/>

contemporary woes intersect at the billable hour.”¹¹ The ABA Commission on Billable Hours Report found that an “overreliance on billable hours” tended to have the following negative results:

- Decline in collegiality of law firm culture;
- Increase in associate turnover;
- Discouragement of pro bono work;
- Discouragement of project planning and case planning;
- Lack of predictability of cost for clients;
- Penalizing efficiency and productivity by lawyers;
- Discouragement of communication between lawyers and their clients;
- Encouragement of skipping steps by lawyers;
- Encouragement of excessive “layering” and duplication of effort by lawyers;
- Failure to promote risk/benefit analysis by lawyers;
- Failure to reward attorneys for making productive use of technology;
- Putting lawyers’ interests in conflict with those of their clients;
- Creation of additional risk to clients of paying for incompetency or inefficiency of attorneys as well as associate training, associate turnover, and “aggressive” billing (i.e., padding of timesheets by attorneys);
- Itemized bills which tend to report mechanical functions as opposed to the value of progress made; and
- Competition among lawyers based on hourly rates.¹²

Another pair of critics wrote in December 2003 that the billable hour pits attorney against client in a billing war which has caused substantial deterioration in attorney-client relationships:

Another significant effect of the hourly rate is that it means that the financial component of the relationship between the client and the outside lawyer is a zero-sum game insofar as the client wishes a lower fee and the lawyer prefers a higher one. A client that tries to control the costs represented by the fee can only do so by reducing the number of hours for which it pays or negotiate a reduced hourly rate. Each of those means of reducing costs leads to less reward for the lawyer without changing the dynamics of how that lawyer works and the effort devoted to the assignment by that lawyer. In short, either the lawyer or the client “pays” for the lawyer’s time.¹³

Alternative fee arrangements, by contrast, are often said to be geared more toward providing value to the client, as the lawyer may not be required to track his time, and the amount paid by the client is not tied to the number of hours worked by the lawyer. In addition, AFAs allow clients to obtain a greater degree of control over their budgets for legal fees, which has been shown to significantly improve the attorney-client relationship; surveys routinely show that clients tend to be unhappier about surprises and unexplained costs in the billing context than they are about high-cost bills themselves.¹⁴

Some critics of AFAs are concerned that they may go too far in failing to compensate lawyers for work actually done, especially in the situation where a legal matter becomes significantly more complex or time-intensive than initially expected. In response, they propose a middle ground in which the billable hour is not the primary measure of compensation, but an allowance may be made for the work done where it turns out to be materially more than either party anticipated.

¹¹ ABA Commission on Billable Hours Report, Aug. 2002, at ix, available at <http://www.abanet.org/careercounsel/billable/toolkit/bhcomplete.pdf>.

¹² *Id.* at 5.

¹³ Sager and Lauer, *supra* note 8.

¹⁴ Ed Poll, *How to Make Alternative Billing Part of Your Marketing Strategy*, LAW PRACTICE TODAY, Oct. 2009, available at <http://www.abanet.org/lpm/lpt/articles/fin10091.shtml>.

Before entering into an alternative fee arrangement, a law firm must carefully examine its costs of providing client services to determine whether costs can realistically be cut without diminishing the value of service provided to the client. For example, can an associate, rather than a partner, perform more of the work on a particular matter? Are there parts of a particular matter which can be handled more efficiently by either in-house or local counsel? By determining the total costs to handle a particular matter and then determining where steps or costs can be trimmed, a law firm can establish a viable range in which to negotiate a fixed fee with the client with appropriate contingencies.

It is likely that firms will have a difficult time traveling back and forth between traditional hourly and alternative fee arrangements. This is because firms embracing AFAs necessarily will focus more on results than on process and hours, and these firms will become less attuned to the necessary description of time required by client auditors. Similarly, there will be less flexibility within such firms for hour-intensive work as they trim the fat from their workforce and internal budgets. There will also be less room for error, as the amount of time expended on discovery in some litigation matters is significantly reduced. While we all analyze and weigh the need to take specific depositions and written discovery, attorneys anxious to eliminate too much risk may be prone to undertake too much discovery in the way that a doctor may order a number of tests to eliminate improbable illnesses. The law firms which succeed with AFAs will have to learn to evaluate risks and rewards with sufficient precision to both effectively and efficiently handle the matters entrusted to them.

In essence, clients want their attorneys to become better project managers. As a group, attorneys lag behind the rest of the business world in terms of both project management and utilization of technology. The use of AFAs goes hand-in-hand with more efficient use of resources, whether in terms of staff members, time, or technology. Clients increasingly want to understand where their legal dollar is being spent, and the use of AFAs forces attorneys and law firms to examine this as well.

III. Selected Types Of Alternative Fee Arrangements

There is no single accepted form of alternative fee arrangement; the number of potential varieties of AFAs is limited only by the imagination and innovation of attorneys and clients. Nevertheless, several broad types of AFAs have begun to see wide use in the United States.

The AFAs discussed in this paper are as follows: (i) Fixed/flat fees and “project” billing; (ii) Discounting; (iii) Blended billing rates; (iv) Contingent fees; (v) Capped Fees; (vi) “Success” Fees and “Premium” Pricing; (vii) Retainers; and (viii) Hybrid fee arrangements.

A. Fixed/Flat Fees and “Project” Billing

The concept of a “fixed fee” or “flat fee” is simple and nothing new. In such an arrangement, an attorney or law firm commits to handle a particular task, suit, or matter for a predetermined total fee. A flat fee may either be a fixed amount of money, or a fixed, but not contingent, amount involved in a particular matter. Financial and real estate transactions may be paid based on a percentage of the amount financed or the value of the “deal” being consummated. In recent years, some transactional clients have negotiated fixed fees below that typically charged in the legal market using volume or other incentives. Fixed fees are also being pushed by some institutional clients involved in a high volume of repetitive litigation.

The obvious advantage of fixed or flat fees to the client is predictability: the client knows from the inception of the representation precisely how much the attorney’s services will cost. Flat fees are also said by some to encourage the use of technology by attorneys to streamline the provision of legal services.¹⁵ The disadvantage to the attorney is that he bears the risk of any unforeseen developments or complications which would materially increase the amount of time spent beyond that estimated for the matter. The primary risk to the client is that an attorney who is “upside-down” on a case may lose interest in the prosecution

¹⁵ *Id.*

or defense of the case, with potentially serious consequences in the outcome of the case. One major benefit to lawyers from flat fee or per-project fee arrangements is elimination of the need to keep detailed, incremental records of time spent on a particular matter.¹⁶

Given the nature of these risks, flat fee arrangements have proven most useful for routine legal services and those involving repetitive issues and limited risks; accordingly, flat fees are far more common in the context of repetitive transactional legal services than in aggressively-disputed or otherwise complex litigation.¹⁷ This distinction arises from some fundamental differences between typical transactional work and litigated disputes. First, transactional matters arguably are more easily limited to and broken down into specific, discrete tasks (e.g., drafting or reviewing a single contract). Litigation, by contrast, may involve a lengthy, complex, and unpredictable sequence of pleadings, discovery, court appearances, hearings, trial, and appeals, during the course of which clients typically prefer to be, and generally are best served by being, represented by the same attorneys or law firm. Most obviously, the often unpredictable nature of litigation may render the number and complexity of the issues arising in a particular case unpredictable and difficult to forecast. Unlike the typical transactional matter, in which everyone involved plans to make money, litigation generally consists of parties seeking diametrically opposed results. Indeed, the recent collapse of the prominent international law firm Heller Ehrman has been blamed in part on an unforeseen decrease in revenue due to the settlement of a number of cases.¹⁸

These complexities do not mean that litigated matters cannot be handled under variants of this form of AFA. Some attorneys and clients have negotiated fixed fees for individual stages of the litigation process.¹⁹ For example, a particular attorney or firm might negotiate a set amount to prepare interrogatories, a different set amount to prepare a dispositive motion, and yet another set amount for trial. For such a system to be sustainable over time, it is likely that a firm would need differing schedules of fees for the various stages of litigation in different types of cases – e.g., one schedule of set per-stage fees for slip-and-fall or other types of “standard” premises liability cases, another schedule of fees for auto accident or other simple personal injury actions, and a third schedule for simple insurance coverage actions. Additionally, a contingency can be added to the terms of the billing arrangement to provide the lawyer with protection in the event that a particular matter lingers, moves from pre-litigation to active litigation, or becomes significantly more complicated than either attorney or client forecasted.²⁰ Even so, it remains questionable whether such a system can be effective over the long term for more complex litigation, such as products liability and wrongful death cases.²¹

B. Discounting

Another form of billing sometimes considered an alternative fee arrangement is “discounting,” which consists simply of applying a discount to a lawyer or firm’s standard hourly billable rates. Discounting is sometimes used as a manner of attracting additional business from reliable clients, or as a way of rewarding the loyalty of clients for repeated and long-term referral of new matters.²² Unless the discounting is used in conjunction with some other fee arrangement, such as a contingency fee, or a reward for specifically achieved objectives or benchmarks, a straight discount to an hourly fee is not fairly considered a legitimate AFA.

¹⁶ Wendy Werner, *Alternative Billing Practices Beyond the Billable Hour*, LAW PRACTICE TODAY, Sep. 2004, available at <http://www.abanet.org/lpm/lpt/articles/fin09041.html>.

¹⁷ ABA Commission on Billable Hours Report, *supra* note 11, at 16.

¹⁸ Glater, *supra* note 3, at 2.

¹⁹ *Id.*

²⁰ Werner, *supra* note 16.

²¹ *Id.*

²² ABA Commission on Billable Hours Report, *supra* note 11, at 16

C. Blended Billing Rates

A “blended billing rate,” by contrast, is a system under which the client pays the same rate for attorney time spent on a particular matter, regardless of the classification or rank of the attorney performing the work.²³ While the client pays the same amount for an associate’s time as a partner or senior partner’s time, the firm should be able to charge a lower effectively hourly rate for the client services because it is free to most efficiently use its human resources. The firm may arrive at a blended rate based on the average rate of two or more attorneys who are expected to work on a particular matter.²⁴

D. Contingent Fees

Contingent fees typically consist of a percentage of the amount of funds recovered or saved for the client by an attorney in a particular matter.²⁵ The key feature of a pure contingent fee is that the client does not pay anything unless the attorney achieves a successful outcome. The contingent fee can be a particularly useful tool for an attorney who is skilled at analyzing cases and determining at the outset which cases have a high likelihood of success.²⁶

Clients generally like the idea of a contingent fee because it requires no outlay of funds from the client, and the attorney is only ever paid out of funds received by the client in the context of the particular matter. The contingent fee may also represent an “alternative to give corporate firms a bigger payoff on ‘bet-the-company’ matters for large clients, and to give those clients the assurance that their lawyer has some ‘skin in the game’ in exchange for the predetermined percentage payout.”²⁷ Contingent fees are most common in plaintiff’s personal injury cases, class actions, and business salvage, indemnity, or subrogation claims. Corporate and institutional clients typically look closely at the issue of contingent versus hourly fees when they find themselves in the position of a plaintiff attempting to recover large sums of money. If they believe they have a very strong case and can fund the effort, they will almost invariably want to pay an hourly rate. If the case carries significant risk of loss, however, the client may want to pay some or all of the fee under a contingency arrangement.

Contingent fees are similar to, but not the same as, so-called “success” fees, which are discussed separately below. The primary difference between these two types of alternative fee arrangements is that contingent fees have become well accepted in the U.S. in recent years and now are generally excluded from the otherwise broad prohibitions against an attorney acquiring a pecuniary interest in a client’s case.²⁸

E. Capped Fees

Under this arrangement, the client pays an hourly rate for the attorney’s time, but only up to a defined maximum amount. Capped fees can be advantageous to law firms which understand their efficiencies and expertise and are capable of effectively leveraging them. Clients may prefer capped fees, especially where budgets are tight, because they enable the client to predict the maximum cost of a particular legal matter while shifting some potential financial risk to the law firm. As a result, capped fees tend to work best with high-volume, routine commodity work, where costs are easier to predict and surprises less likely. It is wise for any attorney using a capped fee agreement to include a stop-loss provision in the agreement in case the matter takes an unpredictable turn.²⁹

²³ *Id.*

²⁴ Susan Van Dyke, *A Marketer’s Guide to Alternative Billing Methods*, Dec. 8, 2009, available at <http://www.lawmarketing.com/pages/articles.asp?Action=Article&ArticleCategoryID=7&ArticleID=917>.

²⁵ *Id.*

²⁶ Poll, *supra* note 14.

²⁷ Edward Poll, *Flat Fees and Contingency Fees – Do They “Fix” Hourly Rates?*, LAW PRACTICE TODAY, June 2007, available at <http://www.abanet.org/lpm/lpt/articles/fin06071.shtml>.

²⁸ See RESTATEMENT (THIRD) OF LAW GOVERNING LAWYERS, § 36(1).

²⁹ Van Dyke, *supra* note 24.

F. “Success” Fees and “Premium” Pricing

The “success” fee model is designed to pass on to the attorney some of the risk that the client may not receive a positive outcome.³⁰ Under this AFA, the attorney typically charges a base fee at the inception of the matter and has an opportunity to earn an additional fee for a successful outcome in the matter – e.g., winning at trial or closing a business deal on time. In the event of an unsuccessful outcome, the attorney retains the original base fee, but does not earn anything further at the conclusion of the matter.

Success fees are sometimes lauded as incentivizing attorneys to obtain a successful result for their clients. As Evan Chesler, a presiding partner at the prestigious firm of Cravath, Swaine & Moore, LLP wrote pointedly in a recent article in Forbes magazine:

Quality insurance should come in the form of a success fee. If I win, I should be rewarded. That’s not only fair, it places the incentive where it belongs. It doesn’t suffer from the soft idea that effort, even unsuccessful effort, should get an A. Winning is what deserves an A.³¹

Although success fees are mostly unheard of in the United States, they are a way of life for lawyers in Japan.³²

Under the similar method known as “premium pricing,” either an hourly rate or a flat fee may be used as the base cost for an attorney’s services, and the lawyer has the ability to earn an additional “premium” if the attorney’s results exceed the client’s expectations.³³ Unlike the “success” model, however, an attorney is not penalized for failing to obtain a successful result; he simply does not receive an additional “premium.” Premium pricing is said to give an attorney a stake in the outcome of his client’s legal matter while maintaining the assurance of a minimum fee for even a “bad” result.

The use of success-based fee arrangements may help an attorney establish his role as a trusted adviser, focused on the client’s needs and success, rather than appearing as a merely a detached service provider who sends monthly invoices. Success-based fees can be seen as a more palatable analog to the contingent fee for defense attorneys, who have traditionally viewed contingent fees as reserved for plaintiff’s attorneys.

G. Retainers

This well-known fee arrangement consists of a fixed fee for a set period of time (e.g., monthly) on a recurring basis over a designated period (often one year).³⁴ This fee arrangement provides a level of predictability in terms of the dollar amount of fees to be billed which is unsurpassed by other billing arrangements. At the end of the designated period, the attorney and client can reassess the relationship and determine whether it should be renewed and whether the rate retainer amount should be altered. In some instances, a retainer is used as a one-time payment to guarantee the attorney’s future availability for a particular matter.³⁵

H. Hybrid Fee Arrangements

A “hybrid” fee arrangement can consist of any combination of one or more of the other types of fee arrangements. Evan Chesler has suggested the use of a hybrid of the flat-fee, retainer, and success-fee models in litigation matters. Specifically, he proposes that a fee be set in advance for a particular period of time (e.g., three months), based on the client’s objectives and a measurement of possible contingencies.³⁶ The client and attorney would then periodically revisit the arrangement to determine whether the price should be modified for future time periods, and when the matter is concluded, the attorney would receive a

³⁰ Poll, *supra* note 14.

³¹ Evan R. Chesler, *Kill the Billable Hour*, FORBES, Jan. 12, 2009, available at <http://www.forbes.com/forbes/2009/0112/026.html>.

³² ABA Commission on Billable Hours Report, *supra* note 11, at 18.

³³ Poll, *supra* note 14.

³⁴ *Id.*

³⁵ *Id.*

³⁶ Chesler, *supra* note 31.

success fee if the client receives a positive result. “The point should not be to achieve a ‘gotcha’ for me or the client. The point is to devise a rational system that puts the incentives where they should be.”³⁷

Other forms of hybrid fee arrangements may be used in commercial litigation. For example, the client may pay an hourly rate with a total cap for the law firm to evaluate the merits of the client’s position, and report their conclusions to the client. Based on this report, the client may elect to abandon the case, proceed with other counsel, or negotiate terms with the same firm to proceed with the handling of the matter. At that point the parties may agree to proceed on a straight contingency; a contingency with tiers of recovery; a reduced hourly rate and a reduced contingency; and/or any other combination of incentives, caps or rewards with whatever contractual triggers to which the parties may agree.

Likewise, on transactional engagements, the parties may agree to an hourly rate to a specified point in the transaction, with an opportunity to negotiate a fixed fee from the specified point forward. These are only examples, and it seems certain that the future will bring new and more innovative alternative fee arrangements as clients continue to demand more – or at least a greater degree of predictability – for their legal dollar.

IV. Ethical And Practical Considerations In The Use Of Alternative Fee Arrangements

The perpetuation of the billable hour among lawyers is not due entirely to the preference or custom of individual attorneys and law firms. Rather, ethical standards and considerations often substantially limit the degree to which lawyers and firms can explore and implement alternative fee arrangements. Thus, it is important to remember that even when the client is a sophisticated consumer of legal services, is fully informed of and comprehends the details of the fee arrangement, and seeks the advice of independent counsel prior to entering into an agreement for legal services, any alternative fee arrangement must comply with applicable ethics and professional responsibility rules, which can vary substantially from state to state.³⁸

As a general rule, attorneys are prohibited by applicable rules of professional responsibility from sharing legal fees with non-lawyers.³⁹ Indeed, in at least some jurisdictions, an attorney may not even be a member of a partnership, professional corporation, or association in which any non-lawyer holds an interest or any right of control.⁴⁰ Some argue that such rules “stifle innovation by denying firms a way to offer more flexible services at lower cost,” thereby severely limiting the ability of lawyers and law firms to create and utilize innovative business structures and fee arrangements.⁴¹ Nevertheless, until this prohibition is modified or eliminated, its violation can lead to attorney disbarment and it must be honored.

Similarly, ethical considerations are a significant concern in any success-based fee arrangement, inasmuch as attorneys typically are prohibited from sharing in a client’s financial success. Specifically, a lawyer generally “may not acquire a proprietary interest in the cause of action or subject matter of the litigation that the lawyer is conducting for a client.”⁴² Such arrangements may well be deemed sufficiently contingent on the outcome of the matter as to trigger the specific professional responsibility rules governing contingent fees.⁴³ Attorneys must always be on the lookout for this trigger as contingent fees are subject to specific contractual requirements and limitations in almost all states.

³⁷ *Id.*

³⁸ James D. Shomper and Gardner G. Courson, *Alternative Fees for Litigation: Improved Control and Higher Value*, ACCA Docket 18, no. 5 (2000), at 21, available at http://www.dupontlegalmodel.com/onlinelibrary_detail.asp?libid=96.

³⁹ See, e.g., RESTATEMENT (THIRD) OF LAW GOVERNING LAWYERS, § 10; GA. RULES OF PROFESSIONAL CONDUCT, Rule 5.4.

⁴⁰ *Id.*

⁴¹ Knowledge@Wharton, *New Fee Structure for Law Firms*, FORBES.COM, Apr. 29, 2009, at <http://www.forbes.com/2009/04/29/billable-hour-retainer-entrepreneurs-law-taxation-wharton.html>.

⁴² RESTATEMENT (THIRD) OF LAW GOVERNING LAWYERS, § 36(1).

⁴³ Shomper and Courson, *supra* note 38.

Most importantly, all fees must be “reasonable” and all fee arrangements must be fully explained to the client. Regardless of the manner in which an attorney’s fee is calculated, the attorney obviously must represent his client zealously at all times, even if the arrangement becomes unprofitable at some point during the representation. Although professional responsibility codes generally permit modification of fee arrangements, changing an arrangement on the eve of a trial or at some other critical juncture during a particular matter could result in a charge of duress by the client. As outlined above, attorneys also must follow applicable rules regarding fee-splitting, doing business with clients, and acquiring an interest in litigation. Such potential issues are alleviated to some extent by recording all fee agreements in written form.⁴⁴ Whether required or not, written engagement letters and agreements clearly setting out the attorney’s undertaking and method of calculating compensation is of particular importance in any hybrid fee arrangement.

Attorneys also must be mindful of and follow applicable state ethics rules governing the handling of client funds. Unless a particular payment qualifies as a true retainer (i.e., the payment is made to secure the attorney’s availability, in which case it would be considered earned immediately upon being paid), any amount paid for future work must be placed in the attorney’s trust account, and the funds may be withdrawn by the attorney only as earned under the terms of the parties agreement.⁴⁵

Law firms must be particularly careful to remember their obligation to zealously represent their clients under AFAs which may actually remove incentive for some firm members to work. For example, blended-rate systems are said to incentivize law firms to assign less experienced attorneys to a particular matter so that the firm can actually charge higher rates than it normally could for those attorneys’ time. In response, some have raised concerns that under a blended-rate system, more senior attorneys will not be sufficiently motivated to work on the matter.⁴⁶

Another element of the movement towards AFAs has been the client-driven trend towards outsourcing, which has been met with limited success. Thus far, outsourcing of legal services to other countries, including India, appears to have been limited mostly to document review. Such outsourcing brings potential ethical, practical, and quality concerns which likely have yet to be realized in their entirety.

Contingent fees come with their own concerns, most notably issues regarding attorney compensation. First, while a matter taken on by a firm on contingency remains open, how is the firm to determine the proper amount of salary, bonus, or other compensation to pay the attorney working on that case, let alone generating the actual funds to pay that attorney?⁴⁷ Because it can take several years to resolve complex litigation matters, these issues represent very real concerns which could even threaten the firm’s financial stability. If a successful result is realized in the matter, how are the proceeds split between the firm and the attorney who actually handled the matter? If the client does not succeed, and the firm, therefore, is not paid, how will the individual attorney’s compensation be affected? All of these questions must be resolved in detail and in advance of accepting any contingent fee arrangement, or else significant problems may arise between lawyer and firm.

Conclusion

It is far from certain that the current push to unseat the billable hour as the primary method of pricing legal services will have significant long-term success. One need only look as far back as the early to mid-1990s, when the nation was in the grip of a relatively significant economic recession, to find desperate calls for a broad shift toward AFAs and away from the billable hour. In late 1993, the New York Times boldly predicted the impending death of the billable hour as a means of charging for legal services:

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ Van Dyke, *supra* note 24.

⁴⁷ Poll, *supra* note 27.

But now the ground is shifting in response to increased competition among law firms and to diminished revenue among law firms and clients alike. And that shift, particularly in corporate law, has begun to bury the hourly rate.⁴⁸

The years that followed, of course, represent what may well be the most successful period of time ever for the use of the billable hour among lawyers and law firms.

Regardless of whether the recent death knell of the billable hour once again proves to be premature, it is certain is that some clients will continue to demand a greater level of flexibility and value in the legal services they purchase. Even if many clients continue to accept hourly billing, there no doubt will be others who will approve of, or even require, the use of alternative fee arrangements. To remain competitive and to develop new business, attorneys and law firms will be best-served by developing and considering innovative, creative fee arrangements which go beyond the billable hour.



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⁴⁸ Slade, *supra* note 10, at 1.