

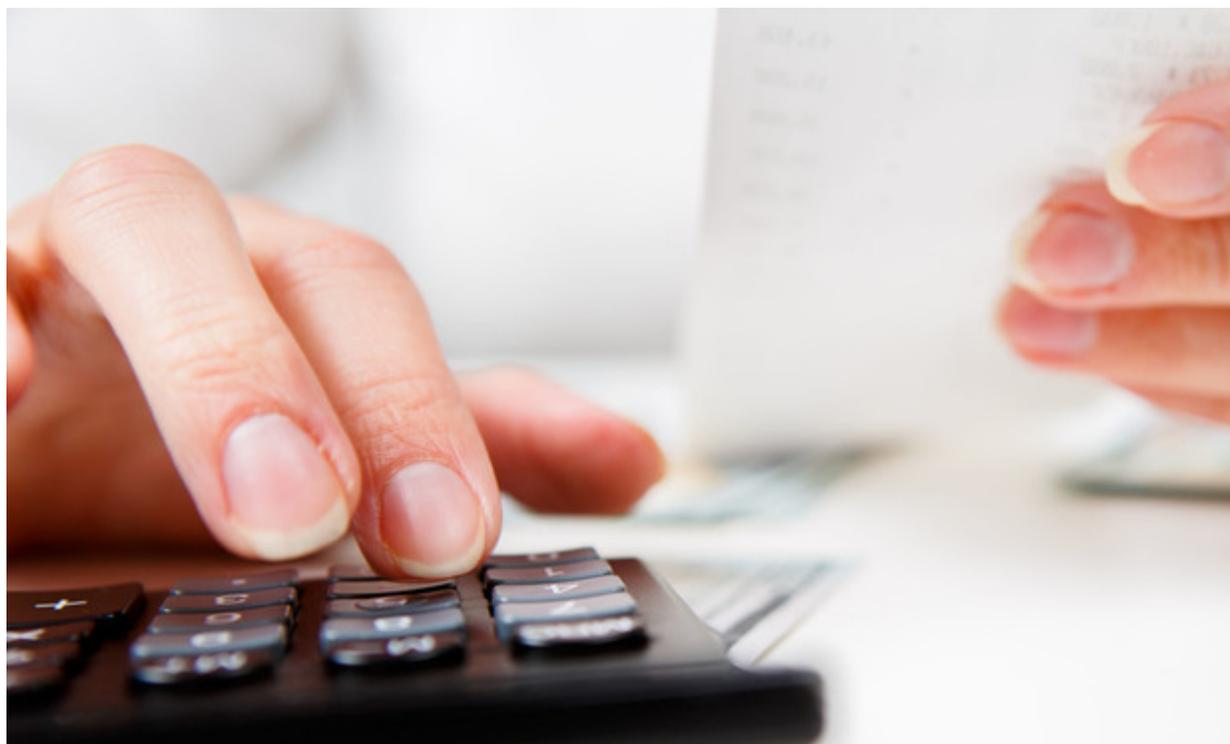
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How Mid-Market Firms Should Pitch AFAs to Clients—Then Actually Use Them

If firms are going to do more alternative fee arrangements, they need good data—and ideally, in-house analysts to examine it, consultants and firm leaders said.

By Hank Grezlak | August 22, 2019



(Photo: Sergey Mironov/Shutterstock.com)

(Editor's note: This is the second part in a series. Last week we examined whether the billable hour gives mid-market firms a competitive advantage and whether they should move away from it. This week we look at how firms should approach their clients about AFAs, and how they should handle moving more away from the billable hour).

The billable hour presents a bit of a dilemma for midsize firms, because in some respects it gives them an advantage against big firms, and the core of their client base may not be asking for anything different. But does that mean these firms should ignore alternative fee arrangements and avoid raising the topic with clients?

Mid-market firm leaders and consultants say, simply, no.

James Goodnow, president and managing partner of Fennemore Craig (<https://www.fclaw.com/>), a 190-plus-lawyer Mountain West firm based in Arizona, admitted that while firms have heard “for the better part of a decade,” that clients will be demanding AFAs, “by and large, that hasn’t happened.”

But he was quick to point out that even so, “that doesn’t mean it should be back to business as usual.”

“Firms that proactively propose alternative fee agreements have a great opportunity to gain market share,” Goodnow said in an email in response to questions. “Any good alternative fee agreement starts with a conversation where you listen to the needs of the client—something lawyers aren’t often good at. Is the client looking for budgeting certainty? Is cash flow the key issue? You and your firm will never know, and you’ll never appreciate which alternative fee agreement to propose, unless you start with that conversation.

“Even if the client doesn’t decide to pursue an agreement, you’ll get points for being thoughtful in your approach—and that may translate into more work in the future.”

Goodnow said his firm has experimented with “many” different types of alternative fee arrangements. He said blended rates tend to be the most common with business clients, and they’ve also used contingent fees on a regular basis.

Many of those interviewed echoed the sentiment that mid-market firms shouldn't wait for their clients to ask for alternatives to the billable hour.

"I believe in being proactive," said legal consultant Marcie Borgal Shunk, president and founder of the Tilt Institute (<https://www.thetiltinstitute.com/>).

Firms need to know what's important to their clients, and their clients might not be all that interested in AFAs, she said.

"If you have a trusted relationship with a client, that's a precursor to an AFA," Shunk said. "But if you have a fixed fee and still get asked to account for the hours, that's not a trusted relationship."

One issue that comes up at times when discussing AFAs, she said, is that "lawyers have a certain discomfort," with discussing certainty, even though clients want predictability. Lawyers are trained not to take risks, Shunk said.

"If they aren't 100% certain, they are reluctant to say it," she said.

Courtney Paulk, president of Hirschler (<https://www.hirschlerlaw.com/>), a 77-lawyer firm based in Richmond, Virginia, said her firm is proactive with exploring alternative fee arrangements "where we think it makes sense for clients."

"We take time to think through ways we can be more efficient with a representation and create more predictability in a client's legal spend," Paulk wrote in an email in response to questions. "This is accomplished through AFAs as well as careful budgeting (particularly for litigation)."

Paulk said fixed fee arrangements have been successful when the work was predictable in scope, and blended rates when there has been "a sufficient volume of meaningful work." Contingency fee arrangements can be "alluring," she said, but also present the most uncertainty and risk.

Joel Carpenter, managing partner of Sullivan & Worcester (<https://www.sullivanlaw.com/>), a 136-lawyer firm based in Boston, said the important thing is to be attuned to your clients.

“I think you absolutely have to be attentive to your client’s concerns over costs,” and be prepared to offer options to address those concerns, Carpenter said. “We don’t raise it with a client unless it’s something that can benefit both of us mutually.”

Patrick Fuller, vice president of ALM Intelligence

(<https://www.alm.com/intelligence/solutions-we-provide/business-of-law-solutions/legal-compass/>) (a division of ALM, which also owns the Mid-Market Report), said that while he generally believes it’s better to be proactive rather than reactive with using “fee engagement strategies,” whether the firm raises it first with the client or waits for the client to broach the topic can depend many factors.

“If the firm can handle the matter efficiently and effectively, it could be worth a conversation with the client,” Fuller wrote in an email. “While attorneys should always ask their clients how they evaluate outside counsel performance, they should also ask their client how [the in-house attorney’s] performance is evaluated internally and what KPIs impact their bonus. Every client is a bit different, and firms should always be engaged in conversations with their clients on how they can better serve them.”

Starting the Conversation

If mid-market firms want to move away from the billable hour, how should they approach it? Breaking down the processes for various matters and having data are key, according to firm leaders and consultants.

“Most lawyers rely on their ‘gut’ or ‘experience’ to make alternative fee pricing determinations,” Goodnow wrote. “It turns out that lawyers’ gut feelings on pricing tend not to be very good. We’ve pushed hard into data analytics technology that helps us understand the actual cost of a piece of work. With the help of the technology, we’re able to get rational pricing that can have us earn collected rates that are higher than rack rates and lead to happier clients.”

Fuller said it should go deeper than just the process for the legal work. Even the compensation structure should be examined, he said.

“In my opinion, the first move should be to adjust the compensation structure accordingly to ensure that it is incentivizing the desired behaviors,” he said. “After that, it’s about understanding the costs to deliver the service, if there are opportunities internally to increase the efficiency, such as the use of technology, lower-cost basis resources, and improved processes.

“I feel it’s critical for any matter, but especially fixed-fee deals, to be extremely well-scoped in order to hit the matter profitability target.”

If there’s going to be an AFA for a client, Shunk said, a firm should get people involved in the work into the room “and ask: ‘What does this process look like? How long does this take?’”

Firms need to “approach it systematically,” she said. “Lawyers are analytical and good at breaking things down incrementally.”

But Shunk added that having hard facts is key.

“You need data capture,” Shunk said. “Many firms don’t have clean, organized, data. They aren’t capturing the data in ways that allows them to analyze. They need financial analysts and project managers.”

Get the Right Pros

Firms of any size would benefit from having financial analysts in-house, she said, to ensure profitability and properly compensating people, among other things.

Goodnow also emphasized the importance of data—and people to analyze it. Firms that don’t use “analytics technology” and hire “number crunchers,” do so “at their own peril,” he said.

“Using data and relying on financially-minded people who understand the technology can help firms come up with a suite of pricing offerings that will enable them to stand out and earn more business,” Goodnow said.

“Operating without full information, lawyers may be tempted to cut deals that undervalue their services,” Paulk said. “An experienced and well-informed pricing professional—trained internally or hired from outside—can help evaluate risks and ensure profitable work.”

Fuller said it wasn’t necessary for firms to have in-house analysts. He pointed out there are good consultants in the market who specialize in things like “recalibrating,” compensation structures, process improvement and project management.

A critical piece, he said, is a “real-world matter scoping exercise to account for all potential costs, delays, changes, etc.”

While Shunk said she thinks firms of virtually any size would benefit by having their own business analyst, she said firms can rely on consultants or train folks internally to take on those tasks.

Carpenter said that his firm doesn’t have any business analysts or pricing individuals in-house. The reason? He said they don’t have enough matters involving an AFA to justify it.

“We are a little on the small side for that,” Carpenter said. “The lawyers will do their best to estimate. We’ll do the engagement letter in such a way as to protect ourselves from any gross miscalculation. [But there’s] not enough value add in our system to justify [hiring internal analysts.]”

In general, when it comes to the debate over the billable hour and AFAs, Carpenter said that “nobody has broken the code.”

“In the end, it comes down to whether the client thinks they’re getting value for what they’re paying,” he said.

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