Alternative fee arrangements in IP cases

Billing by the hour is an outdated model says Robins, Kaplan, Miller & Ciresi's **Marla R Butler**. But are law firms ready for new creative alternatives?

For most of my career as a patent litigator, I have observed or participated in discussions about doing away with the billable hour. It is a law firm lawyer's dream. When our colleagues go in-house and we ask how things are on the other side, often time the first response is, "I no longer have to record my day in six minute increments and I love that!" When I hear such gloating, I am envious.

Yet after so many years of discussion, I still record most of my day in six minute increments and I still bill most of my clients by the hour. And I still don't like it. As business owners and as practitioners of the art that is the law, we can and should, be doing better. But the concept of billing by the hour is so engrained in our collective law firm DNA, and so engrained in corporate legal departments, that we have not found a way as an industry to break away from this outdated model.

Breaking away from the billable hour model starts by developing a comfort level with fee arrangements that vary by some degree from the strict pay-by-the-hour arrangement. This article will present reasons why moving away from the billable hour is preferable and will present options for such alternative fee arrangements ("AFAs") in assessment and litigation of IP matters.

Why move away from the billable hour model?

The goals in any attorney-client relationship are more easily met when there is enough flexibility to allow for a fee arrangement that is appropriate for the particular circumstances.

Trust

We want the attorney-client relationship to be a trustful one. The client's trust is diminished when she feels that she has been charged more for a matter than the result appears to warrant. The client's trust is diminished when she feels that a matter is staffed with more lawyers than appears necessary or when more lawyers tend to a task, eg, a deposition, than the client understands to be necessary. Similarly, a lawyer's trust is diminished when her client expects her to leave no stone unturned in litigation, but expects to pay for only the most essential of litigation tasks.

The best attorney-client relationships, the ones that provide both attorney and client with the highest levels of professional satisfaction, are those relationships in which there is trust on both sides. Implementing creative alternative fee arrangements can help us establish attorney-client relationships built on trust.

Certainty

My clients want certainty in their legal spend. I have been told by clients that it is preferable for me to come in at budget rather than under budget. This was a surprise at first, until I understood that dollars budgeted for legal expenses that go unspent are dollars that could have been spent elsewhere. I get that. And certainly coming in over budget is a problem. In other words, clients need to budget for legal spend and they generally need that legal spend to precisely match that budget. Our clients need fee arrangements that allow for the certainty that their budgeting processes require.

Skin in the game

I have learned (the hard way) that a full contingency arrangement in which the client pays no fees or expenses along the way can turn out quite poorly for the lawyers. It is easy to take risks with someone else's investment. On the other hand, when clients are paying at least some portion of the fees or expenses – and therefore have 'skin in the game' – they tend to be remarkably more reasonable in deciding on strategy, including settlement strategy. And I am sure that clients feel that lawyers are more efficient and strategic in their approach to litigation when the lawyers have fees at risk. When both client and lawyer have 'skin in the game', it is more likely that there will be a meeting of minds on strategy.

Value

Law firms are, generally, for-profit entities. So even if the client is pleased with reduced legal spend, if the work does not result in profit for the firm, the relationship has not been a successful one and is not likely to be a repeat one. And clients need to feel that whatever their legal spend is, it was worth it. So we need

to look to fee arrangements that leave firms with acceptable profit and clients feeling like they got their money's worth.

AFA options for IP assessments and cases

AFAs can modify the hourly billing model or abandon it altogether. The examples discussed are not intended to be exhaustive. They can be combined with one another so that, for example, an assessment of the client's case is done on a flat fee and the case is litigated for a partial contingency. We should be creative in finding fee arrangements that work for a given situation.

Contingency

Among the simplest of alternative fee arrangements is the contingency fee, where the attorney only gets paid when the client is paid. A problem with pure contingency arrangements in IP cases, however, relates to the fact that IP cases, especially patent cases, tend to be very expensive. When a law firm takes on a patent case under a contingent fee arrangement, the law firm generally places significant fees at risk. The client, on the other hand, faces no direct monetary risk. As a result, the client and the law firm can find themselves on different pages in the litigation. For this reason, contingency arrangements should be modified, if possible, to ensure the client has skin in the game.

A partial contingency arrangement in which the client pays costs (which can be considerable in patent litigation) and/or a percentage of the law firm's hourly rate, can help align the goals and strategy of the client and the law firm. For example, while a client that has spent nothing on the litigation and is not committed to spend anything as the litigation progresses may have little incentive to agree to a reasonable settlement offer short of trial, a client is more likely to accept that reasonable offer if it too has money at risk. Similarly, if the client is participating in the financing of the litigation, it is more likely to be reasonable in only pursuing specific strategies that are likely to be fruitful, rather than insisting that every stone be turned.

While contingency arrangements are most often agreed to in representation of a plaintiff, a contingency arrangement can be applied to representation of a defendant also. The fee can be tied to the amount the defendant ultimately pays the plaintiff in the litigation. For example, in a case in which the plaintiff is seeking $20m, the fee agreement might set one fee if the client pays more than $10m, a higher fee if the client pays more than $5m but less than $10m, and a still higher fee if the client pays $5m or less. Such an arrangement allows for attorney and client to be more aligned in goals and strategy, even in defence cases.

Caps

Caps provide a not-to-exceed dollar amount for each phase of the litigation, for the entire litigation or both. Caps give the client certainty for budgeting purposes and force the law firm to be very deliberate in its strategy. Except for the rare bet-the-company case, gone are the days when every lead can be followed and every possible defence fully litigated. Caps require a plan up front, with certain assumptions about how the case will be litigated and how much time it should take to do so.

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To be effective, caps also require good communication on the front end. A law firm must be clear as to what assumptions are built into its proposed caps. For example, if the proposed caps assume that one liability expert and one damages expert will be retained, this assumption needs to be explicit. If the caps assume that certain defences will be pursued and others will not, these assumptions need to be explicit. Capped fee agreements usually include a provision that allows the client and the law firm to revisit the caps if something unexpected occurs that materially changes the litigation and disrupts the assumptions.

Fixed/flat fees

Under the fixed or flat fee arrangement, the firm essentially agrees to do whatever work the client sends its way for a fixed monthly or annual amount. It requires trust between law firm and client and, ideally, that trust is reinforced throughout the relationship. To work best, the law firm will perform a large volume of work under a fixed or flat fee arrangement and will feel fairly compensated for that work.

Like with the contingency arrangement, however, there is risk of misalignment of strategy and goals. To help avoid this misalignment, the client and law firm can agree to a monthly hourly goal, and if that goal is regularly exceeded, the parties to the agreement will know it is time to reassess. That means, however, that the billable hour is still factoring into the arrangement in a significant way.

To avoid this, the parties might agree to a finite team that is dedicated to that client, eg, two partners, two junior associates, two senior associates and a paralegal. That team will do whatever work the client sends with no collective billable hour expectation. This is, perhaps, the ultimate rejection of the billable hour model.

Are law firms ready?

Law firms may be the biggest impediment to AFAs. Often, law firms measure their success by comparing firm revenue to firm capacity, where capacity is billable hour expectation (eg, 1900 hours) multiplied by hourly rate. Where the measure of success is built on the billable hour, there is little hope of moving away from the billable hour model.

On the other hand, where a firm measures its success simply in profits-per-partner, there is significantly more room to move away from that billable hour model. So many other factors affect profits-per-partner, including the number of non-partners, salaries and other overhead expenses. When law firms begin to measure success a bit more like their corporate clients, and with little to no regard for billable hours, we will be less confined to the billable hour model. Lawyers will be driven more by the quality of work than the quantity. The level of professional satisfaction we envisioned when we went to law school might actually come within reach. And we might even hang onto to some of those really good lawyers who would otherwise go in-house to escape recording their lives in six minute increments.

Author

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