The Billable Hour is Dead. Long Live…?

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THE BILLABLE HOUR IS DEAD.
LONG LIVE ... ?

By Robert E. Hirshon
As Mark Twain once observed, “the rumors of my death are greatly exaggerated.” Is this the case with the demise of the billable hour?

THE CORONATION OF THE BILLABLE HOUR
For most younger and, indeed, middle-aged lawyers, the billable hour has always been the ultimate arbiter of legal fees and of partner, associate, and paralegal evaluations. There are probably some senior partners (a dwindling group) who may still remember when fees were decided by discussions between a lawyer and a client or were based on a county bar association’s minimum fee schedule. An aggressive approach by the Federal Trade Commission and the U.S. Supreme Court’s decision in Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975), ended the use of minimum fee schedules, however, and forced practitioners to devise different methods of billing clients.

Supported by a relatively new profession (law firm management consultants) and enabled by technology, the billable hour soon became the dominant and most easily determinable factor in figuring out how much a client should pay for legal services. Results and value became significantly less important than “.1s” and “.3s.” Clients did not complain, however, because new billing formats gave them substantially more information than the previously ubiquitous “for professional services rendered.” For a time, everyone seemed happy.
The legal profession, of course, quickly comprehended that pursuant to the hourly approach to billing, two factors were paramount: the total amount of hours it took to complete a matter and the amount of dollars charged per hour. As both transactions and litigation became more complex, law firms found it necessary and easy to justify adding bodies (read: hours) to their clients’ legal projects. With the number of legal projects increasing as a result of explosive economic growth in both developed and developing nations, the demand for top legal talent during most of the 1980s, that clients did not and (even today) still have not completely accepted the value proposition. For many clients, alternative fee arrangements (AFAs) attempting to mimic value meant simply requesting a discount in hourly rates. As such, most law firms used alternative fee arrangements as the preferred billing approach only when forced. Although there are many dramatic success stories involving the use of AFAs, the attempt to align legal billings with value has not completely succeeded, and many clients and lawyers remain skeptical.

Every year, however, more clients and lawyers experiment with AFAs, and some skeptics become converts. A recent report by Altman Weil reveals that in 2009 only approximately 20 percent of the lawyers surveyed thought that non-hourly billing had become a permanent trend within the profession. By 2012 that number had increased to 80 percent.

The report went on to observe that AFAs were being employed by almost all firms responding to the survey. Yet a substantial number of these firms also reported lower profitability when using AFAs. This suggests that law firms and clients have not yet figured out how to turn AFAs into win-win propositions. If they do not, for financial reasons alone, it is likely that the Bar will embrace AFAs only if absolutely required to by clients.

In this economy, at least for the short term, it appears that law firms will be forced to agree to alternative fee arrangements if those arrangements are demanded by their clients. Indeed, because of greater client interest, almost half of the firms surveyed by Altman Weil reported a year-to-year increase in the amount of non-hourly billing, as measured as a percentage of revenues.

Notwithstanding an increased use of alternative billing approaches, the question remains: Is the billable hour dead . . . or at least dying? Clearly much of what is occurring in the pricing of legal services is the result of old-fashioned supply and demand. The truth is that there are too many lawyers chasing too few monied clients. When supply greatly exceeds demand, prices usually go down. Although the ACC Value Challenge was discussed and formulated prior to the Great Recession, it was unveiled during the recession, a perfect time. Accordingly, the Value Challenge helped to create a “perfect storm”: demand from clients for a more rational approach to determining the value of legal services coinciding with a national economic meltdown. These events shifted leverage from law firms to clients in arriving at methods for pricing legal services. Rather than simply requesting discounts based on “most-favored-client” status, companies soon focused on alternative and potentially less expensive models for the pricing of certain legal services.

**HEIRS TO THE THRONE**

As a result of this change in dynamics, law firms and clients have created numerous alternatives to the billable hour when pricing legal services. The most common are outlined below:

**Contingent fees.** First up is the “old standby”: contingent fee billing. It has long been an alternative for hourly billing. A contingent fee is dependent on the results obtained. This obviously requires a clear understanding of what the results are. In personal injury cases, this determination is usually easy. It is a percentage of the amount recovered for the injuries...
sustained by the client. Accordingly, it is
tied both to value (the amount received
by a lawyer will increase/decrease in
tandem with the amount received by
the client) and risk sharing (if the client
recovers nothing, the lawyer will charge
nothing). In other types of cases, how­
ever, defining successful results is often
problematic, and contingent fee billing
is not frequently used.

**Reverse contingent fees.** Recently,
defendants and their counsel have ex­
plored contingent fee arrangements
known as reverse contingent fees as a
way of pricing legal services. A reverse
contingency allows for compensation
based on an avoidance of exposure to
liability. Although in some cases it may
be difficult to determine the amount of
exposure escaped, it is clearly not im­
possible. Most lawyers know how to place a
value on their cases, and defense counsel
relying on both personal knowledge and
public reports of damage awards in their
jurisdiction have become adept at assess­ing
the likelihood of both liability and
the amount of damages.

**Fixed fees and flat fees.** In addition
to contingent fees and reverse contingent
fees, fixed or flat fees are often-used al­
ternatives to hourly billing. A fixed or
flat fee is the price that a law firm charges
no matter how many hours its lawyers
spend on the matter. A fixed fee may be
the total fee for the engagement or may
apply to discrete components of a mat­
ter, such as fixed fees for discovery, for
pretrial motions, and for the actual trial.
Because clients and law firms recognize
that flat fees can disincentivize the pro­
duction of quality work and often lead to
representation by more junior lawyers,
many believe that fixed fees are more ap­
propriate for simple or commoditized
legal work. There are some notable ex­
ceptions, however, to this thinking.

**Blended rates.** Blended hourly rates
apply to all hours billed on a matter. The
blend includes the lower rates of associ­
ates and the higher rates of partners. A
blended rate often works best for high­
risk and complex work. It can, however,
lead to over-representation by junior
talent. And unlike capped fees or fixed
fees, it does not provide the client with
budgeting predictability.

**Percentage fees.** Another popular
alternative fee arrangement is a percent­
age fee, either constant or graduated and
based on the amount of the transaction.
Some courts allow fees to be determined
by the value of the estate being probated.
The fees for many bond issues are like­
wise determined by the percentage of the
amount of bonds sold.

**Combined approaches.** Many alter­
native fee arrangements combine various
approaches. Thus, some firms create fee
schedules based on a low blended hourly
rate plus a contingency. Other firms base
their fees on all the factors set forth in the
ABA Model Rule of Professional Con­
duct 1.5. Alternative fee arrangements
may even include an amount retrospec­tively set, based on the value received
by the client.

**The kingdom of tomorrow**

Ultimately, whether alternative fee ar­
rangements supplant the billable hour
will depend on the level of trust between
attorneys and their clients. Both buy­
ers and sellers of legal services have
become comfortable with the billable
hour. Change comes hard. Law firms
that increasingly rely on alternative fee
arrangements report that selecting the
switch from billable hours is difficult
and often takes a lot of hand-holding.

Creating a law firm billing model
based on AFAs is not impossible. Bartlit
Beck Herman Palenchar & Scott, LLP,
a Chicago litigation boutique, has dem­
onstrated that the billable hour can be
killed. No cases accepted by Bartlit Beck
are billed by the hour. Recognizing the
need for additional hand-holding, how­
ever, the firm states: “starting with day

Many firms report spending more
time discussing ongoing matters with
their clients in cases that are billed with
AFAs than they do in cases that are billed
by the hour. These firms report that cli­
ents know the “clock is no longer run­
ing” and are pleased with the increased
communication about their cases. These
firms also report that there is “no turn­
ing back.” They believe that the billable
hour will die.

Admittedly, the firms that rely com­
pletely, or mostly, on AFAs are unique.
Bartlit Beck’s novel paradigm has yet
to be replicated. But alternative fee ar­
rangements are being increasingly used
by more and more law firms. Clearly,
the billable hour no longer rules the
kingdom alone. Whether it fades away
into oblivion, however, is not yet a
certainty. ■

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