



The Birth and Death of the Billable Hour – One Approach for Dealing with the New Reality

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Pick up any legal periodical or business publication today and you are likely to see yet another article on the general dislike of the billable hour. Perhaps driven by the recent economic decline, perhaps driven by years of frustration over a perception of lack of value, clients are demanding alternatives in the way lawyers charge for their services.

Lawyers don't like the billable hour any more than clients do, but they have generally struggled with alternatives that work for both the lawyer and the client. Like any other problem, it's an opportunity for lawyers to distinguish themselves with clients. Given the level of dissatisfaction, the lawyer that discovers a workable solution will be popular indeed.

This article explores the origins of the billable hour, the problems it has caused and one approach for delivering alternatives. The answer that will free the lawyer from the shackles of the time clock is the use of a well-known tool in the scientific community.

Origins of the billable hour

How did we get in the mess in the first place? The origins of the billable hour are relatively recent and come from a surprising source – the head of the nation's first legal aid society for the poor.

In 1914, Reginald Heber Smith took over running the Boston Legal Aid Society, a provider of legal services to the poor. Smith's book *Justice and the Poor*, criticized unequal justice based on wealth, and he sought a better way to allocate the limited resources of the clinic. Smith had graduated from the Harvard Law School and he asked the Harvard Business School to help him devise a system to track and manage the Boston Legal Aid Society's finances.

Out of this arose the then novel procedure that staff lawyers would begin keeping detailed records of their time spent on different cases. This was not for billing purposes, rather it was a management tool designed to make sure that resources were deployed effectively. At that time, the use of time sheets to track a lawyer's time for billing purposes was unknown.

Smith later went into private practice at Hale and Dorr, and took the accounting system he created with him.

The system caught on, but was still not generally used to calculate client bills until much later. Most lawyers in the early part of the twentieth century used the time sheets as one tool to assign values to different legal tasks. Lawyers used a variety of billing methods: set fees for particular tasks, annual retainers, a discretionary "eyeball" method, and contingency fees, which the ABA approved as ethical in 1908. Many local communities published schedules of different services performed by lawyers and they were widely accepted as the "going rate" for different types of services that lawyers would not go below.

The Virginia State bar, for example, warned that "evidence that an attorney habitually charges less than the suggested minimum fee schedule adopted by his local bar association, raises a presumption that such lawyer is guilty of misconduct." The American Bar Association's model ethical code that was in effect until 1969 proclaimed that it was unethical for an attorney to "undervalue" legal services.

The pressure to move away from unit billing came first from clients, and ultimately from the Supreme Court itself.

Clients began complaining about the mystery of how bills were calculated, and demanded time records to support the values

being charged to the efforts. Firms resisted, but ultimately responded.

Finally, in the case of *Goldfarb v. Virginia State Bar*, 421 U.S. 773 (1975), the Supreme Court held that setting minimum fees for legal services amounted to a form of price-fixing that was illegal under the Sherman Anti-Trust Act. The transformation to the billable hour standard was complete.

The Problems Begin

Almost immediately, problems associated with the billable hour began to emerge. It wasn't simply that the billable hour didn't provide a rational way to measure a lawyer's effort, but rather it was having a bad effect on the way the law is practiced.

Treating legal services as a commodity that can be measured in units of time diminishes the importance of the quality of the work and the results achieved. Few other industries would thrive if they measured their value based on the time it took for their workers to produce the product they sell. As one older lawyer advised me when I started practicing law in the mid-eighties, "the billable hour will destroy the legal profession." I didn't know then how right he was.

From the client's perspective, the potential conflict of interest is obvious. It's in the lawyer's best interest to spend as much time as possible, while the client's interest is served by limiting the time spent. Being motivated solely by the hours billed rewards the lawyer for being inefficient. Fantastic results that take little time are under-rewarded, and results that consume a massive amount of resources are over-rewarded.

Most firm's charge by breaking an hour down to 6 minute increments. This method requires a degree of precision that is virtually impossible to achieve accurately. With billable hour requirements as high as 2200-2300 hours a year at some firms (fifty hours a week on average), it does not take a genius to figure out that any person who maintains that level of billing is not recording their actual daily life activities accurately. They are working hard, without question, but one is left with the unshakeable suspicion that following that person around with a stop-watch would reveal massive errors in time-keeping at the client's expense.

Ethical lawyers are often caught in the dilemma recognized by one commentator as the "pull:" "You fumble around on a project feeling like a complete idiot, with time ticking away, and at the end of two and a half hours you've been down half a dozen blind alleys and have half a paragraph of tepid conclusions and realize you don't really understand what you're supposed to be doing anyway. Do you bill that 2.5 hours? On the one hand, great, 2.5 hours, that's a nice big chunk of billable time—great! I hope this will take me a lot longer to finish up. On the other hand, you realize, someone's going to look at this piece of paper and think, "We've hired us a complete idiot! It took her 2.5 hours to do this simple project, and she's still not finished." Maybe you should only write down 1 hour. But where are you going to get the other 1.5 hours? Stay later? What if while you're trying to catch up you're only slightly less clueless?"

In 2001 the ABA performed a study of the billable hour and found that too much emphasis was being placed by firms on billable hour requirements which was leading to bill padding and general inefficiency, as well a damaging the law firm culture. The standard guideline is that it takes at least 10-12 hours to bill 8, so the 1800 to 2000 hour minimums that most firms impose are simply impossible to meet honestly, and are robbing the profession of its joys and satisfactions.

There isn't one of us who does not know all of this by the time we finish our first year of practice, yet we ignore the conflicts and live with the dilemma for lack of a viable alternative.

Alternative Approaches Vary

As the criticisms mounted, firms started looking for alternatives. Just as the billable hour was born because of client demands, it is now dying for the same reason. Clients are demanding a change.

One Boston firm, specializing in labor and employment matters, did away with the billable hour altogether. Instead they charge their clients flat annual fees for giving advice no matter how much or how little they are used. Matters that become litigated are billed separately but in units.

Many other firms utilize a combination of flat fees, contingency fees, blended fees, capped fees, bonus awards, and countless other ways of billing that is not based on the hourly rate.

There are as many approaches as there are firms trying it, but one thing is clear. The only way to successfully move away from the billable hour is to have a very good method in place for calculating in advance how much effort a legal matter is going to take.

All of us could take a case after it is concluded and retrospectively figure out a way of billing that does not require a billable hour. Many of us can also take a routinely handled case and make some general assumptions as to how much effort it will take to complete the matter based on experience. The problem arises with cases that are unique, cases that are outside the lawyer's normal routine, or in cases that inherently and frequently vary greatly in the effort taken to resolve them.

The answer is in devising a system that the lawyer uses on every case that standardizes the way a case is evaluated from the beginning so that the lawyer can more accurately predict the amount of effort a given case will take.

A Surprising Answer Borrowed

Most lawyers understand this, but they overestimate their ability to evaluate a case. The typical lawyer will interview a client, take a few notes, make some initial assumptions about the issues involved, and sign the client up on an hourly rate basis. Under this system, the lawyer can make many mistakes about the case in its early stages, but his inefficiency and lack of forethought will not be penalized, after all, the client is paying by the hour.

If the billable hour is to die, however, a better system must emerge. The billable hour system was borrowed from the business community. The answer to ending the billable hour system might well lie in borrowing from another industry, the scientific community.

Atul Gawande is a professor at Harvard Medical School and practicing surgeon who looked for ways of improving the quality of medicine. The surprising answer he found, outlined in his book, *The Checklist Manifesto: How to Get Things Right*, was to employ relatively simple checklists, like those used routinely by pilots, in the operating room. The results of his study have been nothing short of miraculous.

Dr. Gawande's hypothesis was that the problems in medicine were not caused by ignorance and uncertainty, rather by complexity.

Medicine had gotten so complex that it was impossible for even the superior doctor to keep accessible and useful all that he needs to know.

Dr. Gawande's solution was to employ the simple checklist, routinely used in the scientific community, as a way to eliminate mistakes. He went to the Boeing Corporation and observed how they do things, and noticed immediately that they employ countless checklists to make sure that they do things they same way every time.

Dr. Gawande knew that the way the medical profession historically handled surgery was to make Doctors get 8, 9, 10 years of experience, and then rely on their experience and instinct to handle the complexity.

Dr. Gawande sought to test if there might be a better way. With Boeing's help, Dr. Gawande introduced a very simply checklist to use in 8 Boston area hospitals. The checklist was very simple and took less than 2 minutes to complete. It contained things like "make sure extra plasma and antibiotics are in the surgery room," and "have everyone participating in the surgery announce his or her first name before surgery starts."

The results were a "massively better result" in surgery. The last suggestion alone – introductions made before surgery--resulted in 35% fewer mistakes because the doctors observed that those who spoke up once by announcing their names were more likely to speak up if a problem arose.

The resistance to the use of checklists was predictably fierce in the beginning. Even Dr. Gawande himself resisted their use – after all he was a Harvard trained surgeon that did not need the extra help. Yet, to avoid being called a hypocrite, he used the checklist and discovered that his own performance dramatically improved.

Among the doctors he tested, he found that even with the improved results known, only 80% of the doctors wanted to continue using the checklist – these doctors thought it was too simplistic. Yet, 94% of these same doctors admitted that if they were required to have an operation, they wanted their doctors to use them.

Dr. Gawande believes that the resistance is caused by smart people having to admit to having a weakness so easily solved. But, the results are undeniable. Not a week of surgery goes by without the checklist preventing a problem in Dr. Gawande's work.

Dr. Gawande was also convinced by the real-life proof in the value of the checklist with the "Miracle on the Hudson," when Captain Sullenberger successfully landed the plane on the Hudson saving 155 people after it was hit by geese over Manhattan shortly after takeoff. Sullenberger was lauded as a hero, and he is, but he himself credits the checklist as the answer. Dr. Gawande was struck by Sullenberger's comments time and time again that "there was nothing that hard about the physical navigation of this plane – it was teamwork and adherence to protocol that saved the day."

The use of a Checklist in the Law

While the use of checklists would undoubtedly improve the quality of legal services in the same way it improves the quality of medicine, it could also provide the key to developing a workable way to price legal services outside of the billable hour format.

The problem that Dr. Gawande sought to solve was too many mistakes in surgery. The problem that lawyers need to solve to free themselves from the billable hour is a systematic way to analyze a case upfront to accurately predict the effort needed to solve the legal problem.

The answer is to turn the case acceptance method on its head. Instead of accepting a case once it is determined that no conflict exists, and then performing research into the issues as they arise, the "checklist" method would start with an in-depth case analysis first – before the case is even accepted. Only after all of the potential issues are identified would the decision to take the case – and how to bill the case – be made.

An Example Checklist Case Analysis

Step One: Meet the Client

The initial case meeting would not result in accepting the case as it often does today. Instead, it would be the opportunity for the lawyer to obtain in-depth information about the facts of a case in as much detail as possible, and would likely require multiple sessions. The client will undoubtedly press the lawyer

for an answer as to whether the lawyer will take the case, but the lawyer should resist this until all facts are known and the check list can be completed.

The temptation to conduct this meeting over the phone should be avoided. The meeting should occur in person. So often, in this day of instant communications, bad decisions are made because of distraction and a lack of time. How many of us have received the hurried call by a client who is calling from a public location with a legal problem that he or she believes requires immediate response? The temptation is to accommodate the client and "launch into" solving the legal problem, yet so much is gained from cool reflection and the non-verbal communication that comes from a face-to-face meeting that the phone should be avoided for this checklist item.

Step Two: Identify a Goal

This will be the second checklist item and it must be articulated in writing. In the context of a litigation matter, the goal is often expressed as "to win," but that is way too simplistic.

To be useful, the goal must be as detailed as possible. For example, in a case involving employment discrimination, the goal might be to obtain reinstatement rather than damages. In a breach of contract case, the goal might be to "buy some time," or it might be to obtain injunctive relief, or it might be to obtain damages.

The point is that the goal should be something that is carefully discussed in light of realistic legal obstacles as well as cost considerations. Once the goal is arrived at, it must be written down. Just like any good checklist, it is not enough to simply discuss it. The act of memorializing the goal will help to focus the effort of the lawyer and client. The important thing to recognize is that the goal will likely change as the other checklist items are completed.

Step Three: Prepare Written Issue Analysis

This is the most difficult and most important checklist item. This is the analysis that will allow the lawyer to develop an accurate cost analysis to be able to propose a reasonable fee structure that is not based on the billable hour.

The written analysis will first contain a statement of the facts in as much detail as possible and with reference to exhibits.

Putting this in writing will force the lawyer to investigate the case carefully and make sure that it “tells a story”

It will next contain a very detailed discussion of every issue that can be identified, liability and damages, with citations to case authority. The importance of this section cannot be overemphasized. Without this section, the lawyer cannot possibly determine in advance the effort that will be necessary.

It is also the one that the lawyer will likely try to avoid as he or she gets more experienced. Just like the experienced surgeon who thinks that checklists are too simplistic to do them any good, a good lawyer with years of experience will likely assume that he or she “knows the law” in his or her area of expertise making a written memorandum unnecessary.

Step Four: Detail the necessary procedural steps

Once the facts and legal issues are anticipated, the lawyer then lists out every step in as much detail as possible that will be necessary to prosecute or defend the case. This will include every witness that will have to be interviewed or deposed, the pleadings that will need to be filed and defended, and the paper discovery that will be necessary.

Step Five: Estimate the Cost

In this section, the lawyer will attempt to estimate the cost of each identified step, based on his or her hourly rate. Often, the identification of the legal issues will drive this. Where a particular issue is a close legal call, or will require a significant amount of expert proof, the cost estimate will be necessarily adjusted. The interesting thing to note in this step is that using time records in this way is exactly how the use of time records started. As discussed above, time records were used as a tool to measure efficiency, not as a billing method. The checklist method returns time records to their proper use.

Step Six: Discuss Battle Plan with Client and Agree on a Fee

This is the entire point of this exercise. Once you have written down the first five steps, you will be ready to discuss, in exquisite detail, the merits of the case, the effort that will be required, and the basis for a fee. The lawyer will know whether the case is a “six month case” or a multi-year odyssey, and will

know the steps that will require routine work, versus significant investments of time and resources.

Will this method eliminate errors? Of course not. But, its habitual use will allow the lawyer to make better decisions at the beginning of the case and lessen costly mistakes.

Example Six: Step Application: Case of Legal Malpractice

A real life example of how this can work is a case involving a potential claim for legal malpractice that our firm recently accepted.

The client was an extremely educated and naturally intelligent developer of cutting-edge technology for mining, valuing and utilizing intellectual property. He started a company with the help of his long-time lawyer, only to have the lawyer steal the company from him.

He contacted us and was quite anxious to sue, pressing us for an answer. Instead, we led him through the six steps, which took almost four months to complete.

During the process of factual analysis, several surprises that the client had forgotten were discovered. Some of these discoveries helped his case, some did not. All were important to our analysis.

During the checklist steps, it was learned that while the client had an excellent case on the merits, his case for damages was weak.

The client was ultimately very persuaded by the in-depth legal and factual analysis. Because the damages issues made the case less valuable, the fee basis was adjusted to account for the increased risk vs. reward. Ultimately, the low damages made a pure contingency fee not a good bet for the firm and like an increasing number of clients today, a pure hourly rate with a hefty retainer was not something the client was willing to do. In the old days, this case would have been turned down, or the client would have agreed to pay it. But this is the new reality.

The careful analysis convinced the client that we were being reasonable in our analysis. Ultimately a blended fee arrangement with a \$6,000 per month flat fee together with a contingency bonus became the fee basis. Given the difficulty in damages,

it was determined that experts would be needed early, and the client agreed to escrow \$30,000 in advanced costs. Again, because of our in-depth analysis, the client was convinced that we were the firm to handle this case, and that our opinions were sound.

Postscript

The six-step “checklist” will not eliminate all mistakes, but it will lessen the amount and make case analysis more precise. Most important of all, it will allow the lawyer to make an informed decision about accepting a case under a fee arrangement that is something other than a pure hourly rate.

In the case of the legal malpractice case, we haven’t anticipated every issue in advance, but we’ve accurately predicted most of them. We have shortened our response time to each motion the that defense has filed. We have streamlined our discovery,

eliminating some discovery that we would probably have done automatically without a careful up-front case analysis, and we have been better at identifying the areas that we need to concentrate on. So far, our estimate has been profitable as well. The monthly amount of flat fees has exceeded in every month but one the amount that would have been charged by the hour, and we still have the opportunity to collect a bonus from the contingency fee at the end of the case.

Finally, it has made litigation of the case more enjoyable. The flat fee arrangement has completely removed the economic motivation to litigate the case “hour by hour.” Sometimes we spend a lot of time making sure that a unique legal issue is completely resolved without any concern of the time we spend on it, sometimes we omit certain discovery as unnecessary based on our analysis. Most important of all, the case is proceeding as planned and the client believes they are getting value. ■

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