

Meat Axe or Tuning Instrument?

Efficiency Not Guaranteed by Legal Bill Auditing Systems

BY STEVEN A. LAUER

Most corporate legal work is billed on the basis of how long it takes to complete. Individual attorneys itemize how they spend time, individual hourly rates are applied and the totals are aggregated to yield a single sum for "professional time."

Unfortunately, that system involves incentives that can be antagonistic to the interests of the clients. A lawyer will be paid more money because more time is devoted to the matter, even if that time is inefficiently utilized. All time is billed equally, even if some is wasted and only a portion results in recognizable benefits.

Clients once took comfort from the professionalism of their law firms and expected that professionalism to restrain inappropriate billing, but they are now less sanguine because examples of abusive billing practices have come to everyone's attention. For example, where the bill formerly could be expected to include support services within the hour-based bill, today the client finds itself purchasing discrete services like legal research, typing, word processing, and messenger charges.

By reviewing invoices in detail, in-house lawyers can identify such egregious practices, as well as routine law firm inefficiencies that result in larger fees. This is a painstaking task, but recent developments in the area of legal bill auditing have provided electronic tools that enable them to do it relatively easily. If properly used, those tools can help manage outside lawyers at the same time they help outside counsel improve their performance.

FORMULAS NOT ENOUGH

There is also a legal bill auditing industry: Third-party consultants and vendors who market their abili-

ties to uncover billing improprieties and assist corporate clients to save or recapture money that otherwise would be spent on legal services. These consultants have made a specialty of identifying overstaffing, excessive staff rotation and similar abuses by law firms.

Whether the abuses that they identify are actually inappropriate allocation of time is not so easy to determine, however. An auditor can formulaically determine that attorneys

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in a law firm spent too much time in intra-firm conferences, or that two attorneys attended one deposition. But can they assess what role each attorney played simply by reviewing the timesheets?

Probably not. If one partner devoted 75 hours to the case in a month, while a second partner spent five hours conferring and reviewing documents with the first, does that mean the second attorney's work was superfluous? Not necessarily. If the second attorney applied a specific but highly developed expertise to a very limited aspect of the case, and that issue was critical to a successful presentation of the client's position, those five hours in fact might be more valuable than the other partner's 75 hours.

Analysis of legal invoices, if it is to answer such questions, must be performed by someone who fully understands the case, and third-party auditors usually don't have that familiarity.

Nonetheless, those consultants

have provided two very valuable services to the in-house legal community: they have refined the task-based billing concept, and they have developed sophisticated software that can analyze a legal bill in many different ways.

TASK-BASED BILLING

Task-based billing requires that when they make a time entry, the lawyers or other professionals categorize the entry according to the task to which that time was devoted. Time spent on research is separated from time spent preparing for a deposition, for example.

The software enables the person who later reviews the invoice to isolate the time spent on each particular task, or to display the data in a variety of other ways. The reviewer can then compare the cost of that task with the cost of similar tasks in that case or another.

Third-party auditors are more likely to review invoices with a "meat axe." They easily can fall into the trap of treating attorneys or other time-billing employees as fungible. ("Two partners spent 10 to 20 hours each on this case last month. Why couldn't one of them - preferably the one who bills at a lower rate - have performed the other's work and avoided some duplication of effort?")

Another problem is that task descriptions can be too imprecise, mak-

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ing it difficult to compare the work of different persons. For example, if several legal assistants (at varying hourly rates) all participate in "trial exhibit preparation" during a month, their tasks may vary considerably despite the fact they all fit within one description. One legal assistant, who is very experienced, very capable, and very familiar with the case actually might have selected the appropriate exhibits from the hundreds of documents received in discovery. A second, much more junior member of the team, might simply have collated and stapled the copies of the exhibits, following explicit instructions from the first.

Could the second employee have properly completed all "trial exhibit preparation," thereby saving hundreds of dollars? No. Such differing interpretations of what the data "revealed" were drawn by a third-party auditor and by me in a recent case. My subsequent discussion with the billing partner confirmed that the same code had been applied to very different tasks, apparently consistently with the auditor's guidelines.

ANOTHER LAYER

Due in part to the limitations to which their auditing role is subject, legal-bill auditors have evolved, with a second generation refining their task. Whether describing themselves as litigation consultants or something else, they are trying to limn a role for themselves that is not simply poring through legal bills in an effort to uncover instances of 30 hour days and other egregious examples of manipulation of legal-billing conventions.

But even with that refinement, when they are brought into individual cases as opposed to helping to design *systems* to manage litigation, they represent an additional layer of activity in a process which already has too many participants.

Likewise in legal-bill auditing, our experience is consultants are most useful to help set up a system which

will then be used by in-house attorneys, who will understand the details and subtleties of the matter at hand, to actually do the auditing.

Legal-bill auditing software can be purchased for in-house use. It is available from some of the third-

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party auditors who pioneered the field, and off-the-shelf as well. The third-party auditors can work with clients to incorporate the software smoothly into the company's own systems.

This is the course Prudential is following. We have retained a consultant with whom we have developed auditing software, which we are in the process of installing in our system. Our expectation is that once we have learned the system, we will do the auditing ourselves.

Auditing software permits faster analysis of the legal invoices by in-house personnel. It empowers the bill reviewers to isolate the fees and costs that correspond to discrete tasks or phases of the assignment, and to review the time of individual billing professionals.

But it is crucial that the reviewer is an in-house attorney or legal assistant who is familiar with the matter. He or she should know the legal issues in question, the size of the assignment, the history of the staffing and billing arrangements that were discussed, and the firm's expectations as well as the client's. The review of the invoice data has to be done with an appreciation for the context.

SYSTEM REQUIRES FOLLOW-UP QUESTIONS

I have used one version of auditing software that permits the display of billing data in several potentially useful ways. But in the final analysis

the utility of a system depends on who is using it.

In this system, the number of hours (and fee) billed by each billing professional in a firm during a billing period can be arrayed in a tabular format. Each billing person's time is displayed in a vertical column, with each entry in that column representing time devoted to a type of task (e.g. "research," "intraoffice conferences," "deposition"). The same software can display various pie charts, with the time and fees billed shown

by category of billing professional (partner, associate, legal assistant, etc.).

In this example, a senior and a junior associate of a law firm, both working on the same case, billed time in the same month for similar tasks as follows:

<u>Described Task</u>	<u>Senior assoc. time</u>	<u>Junior assoc. time</u>
Prepare for trial	35.5	48.4
Research statute of limitations	3.5	15.3
Prepare for depositions	15.4	5.3

These categories are too vague to permit a reviewer to assess the roles filled by the two attorneys. Someone not familiar with the case might easily conclude that much of the senior associate's work could have been performed by the junior associate. But the work performed by the senior associate may have required the greater experience level of that attorney and been totally inappropriate for the junior member of the team.

The labels in this example can't convey that. "Prepare for depositions" might have been shorthand for "review evidence, review same with senior executive (deponent)" for the senior associate. But for the junior associate, the meaning might have been "identify documents written by, addressed to or containing name of prospective deponent (senior execu-

tive) for use in preparing executive for deposition."

Similarly labeled research can be performed at very different levels of detail and difficulty by senior and junior associates. In order to determine if this analysis is indicating problems, follow-up questions must be asked by someone familiar with the case.

The reviewing process can be improved by greater precision in the entry. The software must be introduced with appropriate instructions to the law firms, including proper definition of the task codes. This requires careful thought about how much detail you want to be able to recapture in reviewing bills. A balance must be struck. The codes can be wordy and too narrow in scope or so terse and broad that they are of little analytical use.

Close collaboration between in-house counsel, the auditors or designers of the software and the technical staff who install it on the company's hardware can avoid many problems.

BENEFITS FOR BOTH SIDES

By selectively using what the legal-bill auditing industry offers, clients can get help in identifying the firms that not only do good legal work, but do it efficiently.

It's a short step for clients to then reduce inefficiencies in the firms that do their work, a process which often ends up strengthening their relationships with those firms. Law departments discover issues they want to discuss with their legal providers, and these discussions can improve the quality of communication generally.

They also can help the law firms discover management problems of their own, problems that they may not have recognized. For example, data might reveal that two individuals with similar backgrounds doing similar tasks are very different in terms of their efficiency. The firm might then undertake training to eliminate the problem.

ECCR

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PITH HELMETS AND CROWBARS

IMCERA then decided to retain our firm, the Insurance Archaeology Group (IAG). We had a successful track record and by the early 1990's had documented billions of dollars in past coverage for dozens of companies throughout the United States. IAG was familiar with the history of mergers and acquisitions of the insurance brokers, which was important in view of fact that some of the former brokers were no longer in business. Other promising ideas for contacting third parties, such as additional insureds and companies that may have received evidence of insurance, were submitted in a written proposal along with suggestions for prioritizing the research to meet IMCERA's budgetary requirements.

The search began in IMCERA's corporate storage facility in suburban Chicago and moved next to the mine in Carlsbad. The storage area in the mine was so pitch black that the IAG researchers had to use lamps mounted on pith helmets. Some records had to be pried out of crates with a crow bar.

Because IAG's criteria for potentially relevant records was so broad, hundreds of boxes were examined in both locations. Eight original policies along with secondary evidence for twenty-one other policies dating back to 1960 were found in these document reviews. All of this information pertained to previously unknown policies and added many millions of dollars to the pre-acquisition coverage available for the Santa Clara site. The value of the primary policies that were found actually exceeded their face value, because unlimited defense costs were covered in addition to the policy limits.

Other important leads, such as names of former employees, former brokers and information regarding lawsuits and contracts, also developed in these reviews. The search was then expanded to these outside sources.

IAG knew from previous work for another client that the earliest CSC broker had been acquired many years before by a major New York

firm. Through contacts at the successor firm, IAG researchers were successful in gaining access to three boxes of records pertaining to CSC's third party liability coverage prior to 1975. These records contained ten original policies dating as far back as 1966, as well as a wealth of secondary evidence for numerous other missing policies. Crucial information about intermediaries, such as excess and surplus lines brokers and brokers in London were also identified in these records.

Many of these other brokers had also merged over the years, but knowledge of their respective corporate histories enabled us to contact their successors. Twenty-nine excess policies along with secondary evidence for eight other policies were then obtained through contact with four other brokers in Boston and in London.

Once this phase of the research was complete, there were still gaps involving several years during which the primary policies had been purchased directly from the insurance carrier without the involvement of a broker. However, secondary evidence had been located.

We then researched the standardized policy language and obtained copies of policies issued to other insureds in the relevant time periods. This enabled us to establish the terms and conditions for the missing policies.

In all, IAG uncovered evidence of \$250 million dollars in cumulative policy limits covering nearly two decades prior to the CSC acquisition. These valuable historic assets were then safely preserved not only for the Santa Clara litigation but for any future environmental or products liability problems.

COVERAGE DISPUTES

IMCERA notified dozens of insurers, and events entered another phase. As the refusals, disclaimers and reservations letters mounted, it became obvious that serious legal issues had to be addressed just in tendering the claim to the carriers.

IMCERA turned to Sidley & Austin in Chicago. IMCERA had a long-