

Task-Based Billing: It's about dollars and sense

By Steven A. Lauerⁱ

In the early to mid 90s, a task force of in-house and outside counsel developed the Uniform Task-Based Management System (UTBMS). That system consisted of four sets of codes¹ by which outside lawyers would be able to bill their corporate clients and some guidance on the application of those code sets.

In the years since the UTBMS appeared, the legal profession has continued to rely to a very great extent on the hourly rate as the basis for most billing by outside lawyers to their corporate clients. Surveys of in-house attorneys reflect the survival of fees based on the amount of time devoted to an assignment even though those in-house lawyers voice an interest in fees that more closely reflect the value that the effort reflects for the corporate client.²

The question of how outside counsel fees compare to the value that in-house counsel place on outside counsel's performance has plagued in-house attorneys for some time and in-house and outside attorneys held divergent views in that regard. In 1997, in-house counsel graded their outside counsel at 3.4 (out of a highest possible score of 5) as to whether the charges for legal service were commensurate with the value of those services, while the outside counsel gave themselves a grade of 4.3. In 1998, in-house counsel responding to the same survey gave outside counsel a C, while outside counsel awarded themselves a B+ that same year.³ The gap between the scores awarded to outside counsel by in-house counsel and those that outside counsel awarded themselves on that measure persisted in annual surveys by that same organization.⁴

For quite some time, many authors have explored the idea of using fee structures to create incentives for outside counsel to provide legal service more cost effectively and that create greater direct correlation between the fees paid and the value of the legal service that those fees represent.⁵ The actual use of alternative fee arrangements (AFAs), however, has been much less common than one might expect from the extent of its treatment by consultants and others.⁶ Thus, despite the interest of in-house counsel, the hourly rate persists.

The hourly rate rewards those who take longer to complete a task or an assignment unless the work produced is clearly deficient or the amount of time devoted to that work obviously exceeds any reasonable amount of time needed by a competent attorney.⁷ In-

¹ The UTBMS includes the following code sets: litigation, project, counseling and bankruptcy. See <http://www.abanet.org/litigation/utbms/home.html>.

² See Smith, "Fixating on Fee Systems for Outside Litigators," *The American Lawyer* (December 5, 2005), posted at <http://www.law.com/jsp/ihc/PubArticleIHC.jsp?id=1133517916084>.

³ Lauer, "Maybe Humpty Dumpty Was A Lawyer," *Law Department Management Adviser*, Issue No. 213 (December 1, 2001), p. 5, 6.

⁴ *Ibid.*

⁵ See, for example, Goehl, "How to Boost Business and Profits with Creative Pricing: The Coumadin® Case Study," accessible at http://www.imakenews.com/sugarcrestreport/e_article000121157.cfm?x=r.

⁶ See R. Rawson, L. Cutliff, W. Alderman & R. Donovan, "Fee Arrangements," appearing as Chapter 8 of *Successful Partnering Between Inside and Outside Counsel* (West Group 2000, R. Haig ed.), vol. 1, §8.2, pp. 8-3 to 8-5. See also Smith, note 1.

⁷ McCollam, "The Billable Hour: Are Its Days Numbered?," *The American Lawyer* (November 28, 2005), posted at <http://www.law.com/jsp/ihc/PubArticleIHC.jsp?id=1132653918886>. See also ABA Commission

house attorneys dislike to second guess the amount of time that outside counsel devotes to the representation. During the 90s, insurance companies and some corporate law departments engaged in “legal invoice auditing,” usually by engaging the services of a third-party firm that specialized in that activity. Invoices from law firms included codes⁸ by which the time entries might be sorted with software. The auditing firms subjected law firms’ invoices to detailed review of time entries in an effort to identify excessive time expenditures or inefficient application of resources (such as the attendance by too many lawyers or other personnel at meetings, hearings, etc.).

The insurance industry’s use of invoice audits led to notable dissatisfaction of many law firms with the status of their relationships with the insurance companies. An article in the trade press several years ago described how a number of lawyers who had long represented insurers (including some prominent members of that group) decided to represent plaintiffs against their former client industry. The thrust of the article attributed that trend to the soured relationship between the attorneys and the insurers, at least in part due to the auditing of the formers’ bills by the latter. In the course of the article, the president of an organization of over 20,000 defense attorneys was quoted as saying “[t]here’s been a dramatic drop in constructive dialogue between defense counsel and the insurance industry.”⁹ Since that time, many members of the insurance industry have demonstrated a more nuanced view of their relationship with outside counsel, audits and the use of task-based billing and insurers and their outside counsel have recognized the need to improve that relationship.¹⁰

Since the use of codes for the billing is a prerequisite for auditing the invoices, task-based billing might seem like a step down the road that the insurance industry traveled and toward undermining relationships between in-house and outside counsel, whether in the insurance industry or not. Task-based billing need not, however, lead to that outcome. In fact, task-based billing can permit in-house and outside counsel to improve their relationship by eliminating some contentious issues from their discussions.¹¹ Further, task-based billing can empower them to address issues of concern to all of them more objectively. Once everyone has task-based data about the cost of various types of legal work, clients and firms will be able to negotiate fee arrangements based on solid information, rather than strictly on the basis of economic clout or by making hopeful, but uneducated, guesses. At present, certain large corporate clients, due their market clout or purchasing power, are able to dictate some of the terms by which law firms are paid, such as demanding a percentage reduction from hourly rates or refusing to pay certain costs, whether right or wrong. Better information about the cost of that legal service should

on Billable Hours Report (2001-2002), available at <http://www.abanet.org/careercounsel/billable/toolkit/bhcomplete.pdf>.

⁸ The codes referred to typically were developed by individual insurers, corporate law departments or the billing auditors, not those developed as the UTBMS, which were not released until 1995 and later.

⁹ See Brennan, “Driven to Defection,” *The National Law Journal*, (May 18, 1998), pp. A1, A27.

¹⁰ See, for example, “Recommended Protocols For the Relationship Between Insurers, Insureds and Retained Defense Counsel,” posted by the Association of Defense Counsel of Northern California and Nevada at http://www.adcnc.org/docs/06_recommended_protocols.pdf.

¹¹ See Lauer, “Task-Based Billing as a Strategic Component of Client/Firm Relations,” *Bottom-Line Management* (Altman Weil, April 1988), pp. 9, 11.

allow everyone to make more-informed decisions on fees and some large corporations recently have begun to experiment with and to implement alternative fee arrangements.¹²

Task-based billing offers considerable benefits when applied in the context of budgeting, especially for litigation. If lawyers can accumulate information as to the effort needed for each aspect of a case (measuring the same aspect in multiple cases so as to identify a norm or average), however, they will be much more able to estimate the costs of future litigation. They will be able to take into account similarities and differences between cases with greater assurance.

Task-based billing will allow invoices to be added together in such a way that both in-house and outside counsel can understand the actual costs of a case as compared to the previous estimate in more specific detail. It should become possible for them both to learn whether budget overruns are in fact due to the excessive discovery demands of one's opponent, or whether they result from too much research for a particular case or because of overstaffing or other tactical decisions by inside or outside counsel. That distinction might lead to very different decisions upon learning of an overrun, since efforts to control "defensive" discovery could lead to undesirable impacts on one's litigation prospects.

Whenever discussing billing and fees, you must remain aware of the potential adverse impacts that any decision you make might have on the relationship between the client and outside counsel. The insurance industry failed to do so during the heyday of legal bill auditing and insurance companies' lost credibility with some of their outside law firms and ultimately the services of some of those firms. Better data from task-based billing should enable clients to avoid such pitfalls.

An alternative fee arrangement can and should improve the relationship between the law firm and its client. An alternative fee is defined by virtue of what it is not – a fee based on the amount of time devoted to the work and calculated as a multiple of a rate that applies to a unit of time (typically an hour). The goal of in-house attorneys in their quest for alternative fees is a closer alignment of the interests of corporate clients and their outside counsel because the hourly rate's inherent incentive is to reward more time devoted to a task regardless of the contribution that such time makes to the success or value of the work.

How does task-based billing accomplish this? When itemizing his or her time in an invoice, outside counsel who uses task-based billing must break that time into the specific tasks completed and apply to each entry a code from the UTBMS.¹³ By unambiguously identifying how each step in the work performed relates to the activities expected, task-based billing enables the reader of an invoice to more fully understand the relationship between the work and the hoped-for result. As law departments and law firms work with task-based billing and accumulate data on the legal work done for the former by the latter, they likely will find that they can more effectively discuss and design alternative fee arrangements that take into account the needs of the matter in question, the needs of both the firm and the client and the most effective means of handling the legal needs of

¹² Smith, note 1.

¹³ While other sets of task-based codes exist, including those developed by individual corporate law departments for use by their law firms and in-house lawyers, the principle stated in the text pertains regardless of which set is applied. Use of the UTBMS, however, conveys the opportunity to benchmark across multiple clients and multiple law firms because they use the same "language" for their billing.

the client. See “Using the Uniform Task-Based Management System: Survey Results January 1998,” Law Firm & Law Department Consulting Group, Price Waterhouse, pp. 5-6.¹⁴

Conclusion

After much discussion and debate, alternative fee arrangements have become somewhat more prominent than they had been only recently. The interest of in-house attorneys in alternatives to the hourly rate seems to have reached a point that law firms, including some prominent firms,¹⁵ have engaged in serious discussions and arrangements that shift some of the process- and cost-related risk of the matters for which corporations retain them. Since at least some of the willingness to enter into such arrangements and the likelihood that such an arrangement will be successful¹⁶ depends on the client’s and firm’s ability to “monitor expenses against budget,”¹⁷ task-based billing could provide the factual basis on which to move forward.

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¹⁴ With respect to the hourly rate and alternative fee arrangements, see also Lauer, “What Do Law Firms Sell? What Do Clients Buy?,” Law Practice Today (American Bar Association), January 2004, posted at <http://www.abanet.org/lpm/lpt/articles/fin01042.html>.

¹⁵ The article cited above lists Howrey & Simon, Shook Hardy and Morgan Lewis as firms that have agreed to work on the basis of alternative fee arrangements with Unocal, Tyco and Cisco, respectively. See Smith, note 1, *supra*.

¹⁶ “Success” in this context means something specific to each client/firm engagement, of course, but presumably reflects an arrangement that in fact meets the two parties’ disparate needs and offers each of them a benefit.

¹⁷ See Smith, note 1, *supra*.