

# The Rise of Alternative Fees Against the Historic Billable Hour

## Is There Room for Both in the New Legal Landscape?

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In the not-so-distant past, people owned the things they used in their daily lives. They went to stores, purchased products, and brought them home, where they stored them in their closets or inside their garages. Some people reading this may be saying to themselves, “This is not a thing of the past at all; I still own my ‘things.’”

But do you?

For a little over a decade now, the United States has seen a steady increase in the number of people who choose to lease their personal automobiles.<sup>1</sup> People who lease the cars they drive do not own them, the banks do. Most people also do not own the books they read or the shows they watch. Instead, rather than purchase DVDs of our favorite movies or TV shows, CDs from our favorite artists or books from a particular author, we subscribe to services such as Netflix, Spotify and Amazon’s Kindle Unlimited for unlimited movies, music and e-books. In fact, on July 1, 2018, the American multinational consumer electronics retailer Best Buy stopped selling CDs in its stores, citing the main reason behind its decision as the popularity of subscription streaming music services like Spotify and Apple music.<sup>2</sup> For some people, even owning clothing and accessories is optional. Companies like Rent-the-Runway and Le Tote allow people to subscribe to a service in which you rent, rather than own, the clothing that you wear on a daily basis. These trends in pricing show, at least, a willingness to turn to subscriptions as a way to pay for the services that we use and enjoy in our everyday lives.

## EFFECT OF INCREASED CONSUMER CONFIDENCE IN SUBSCRIPTION-BASED PRICING MODELS ON LEGAL BILLING

Staggering proof of the rise of subscription-based pricing models is clearly apparent in Credit Suisse’s finding that consumers spent \$420 billion on subscriptions in the United States in 2015, which is up from \$215 billion in 2000.<sup>3</sup> Should we as attorneys be concerned about the clear uptake in interest that the subscription-based pricing model appears to be enjoying? The short answer to this very complex question is, of course, and not because it will eclipse the prominence of the main way that attorneys bill for their time – the infamous billable hour – but because subscription-based pricing may be an alternative fee arrangement that provides real value to some of our clients.

Further, in the current climate, where there is an ever-emerging willingness and interest among consumers to pay subscription fees for services that they want or need, attorneys should, at a minimum, be able to knowledgeably discuss this alternative fee arrangement with their clients. In this way, attorneys will be prepared to address the needs of their clients if we begin to see the same willingness and comfort-level for subscriptions. This is not

to diminish the billable hour, which may always be the preferred method of billing for some clients. The billable hour, however, should be considered one of the tools in our pricing toolbox, rather than the only option.

## BRIEF HISTORY OF THE BILLABLE HOUR

Before considering how a subscription-based pricing model provides an effective alternative to the billable hour, we must briefly consider the climate during which the billable hour came to be the accepted form for billing legal services. From the early practice of law in the United States up until 1975, attorneys did not bill their clients by the hour. Instead, lawyers sold their services at fixed fees for various tasks, such as \$100 for drafting a will and \$500 for a simple adoption, which would be more expensive since it might require a court appearance.<sup>4</sup> Up until the early 1930s and 1940s, states codified reasonable fees for these services and made it illegal to charge more than the minimum fee for a legal service.<sup>5</sup> Then, with the goal of wanting to increase attorneys’ income, state bar associations began publishing “suggested” minimum fee schedules that created standard pricing for a variety of legal services.<sup>6</sup> Due to the irrefutable laws of supply and demand, and the state bar associations’ unwillingness to restrict supply (the number of attorneys allowed to practice) or mandate pricing, this change resulted in a race to the bottom, where attorneys undercut each other by offering their services for less than the minimum. As a result, this guidance, originally conceived as a way of setting a price floor, actually created a price ceiling.

In 1969, the American Bar Association addressed this issue and stated that it was unethical for attorneys to charge below the minimum fee. The American Bar Association’s guidance essentially did away with the ability for clients to “shop around” or negotiate fees because all attorneys charged the same thing – the minimum established fee. This created, in effect, a cartel of lawyers all working to keep prices stable. In 1975, the Supreme Court settled this issue in *Goldfarb v. Virginia State*, in which it held that minimum fee schedules violated antitrust law by eliminating competition among law firms.<sup>7</sup> Out of this climate, the billable hour became the predominant method of compensation for legal services because it provided a clear way for attorneys to charge their clients for the work that they were hired to perform. The billable hour is in stark contrast to the minimum fee model because attorneys were now compensated for the time and effort it took to achieve their client’s goals, rather than a minimum fee that likely was set to drive business to a particular firm. In doing so, attorneys who were able to successfully complete work at a rate faster and as effectively as their competition were able to be rewarded for their efficiency.

## BENEFITS OF THE BILLABLE HOUR

While much has changed in the last 40 years, the billable hour's predominance, especially in the realm of billing an attorney's time in litigation, has not. Its obvious benefit is that billing hours provide attorneys with a straightforward way of charging their clients for their service, and clients have a clear understanding of what work the attorney has done for them. In the context of the Supreme Court's 1975 decision in *Goldfarb*, it is clear why the pendulum swung from flat minimum fees for specific services to the billable hour.

Even in the current era, where subscription-based pricing is increasing in popularity, the billable hour pricing model still remains valuable for certain clients, especially those whose legal service needs change from year to year, with little to no predictability when it comes to assessing how much or how little legal assistance they will require during a given time period. Alternatives to the billable hour, however, may be especially helpful for clients who engage the services of attorneys with some regularity.



## SUBSCRIPTION-BASED PRICING FOR LEGAL SERVICES

In the context of legal services, subscription-based pricing will likely look a lot like a fixed-fee arrangement, where a client pays a flat fee for the law firm's work over a specific period of time. The fee would be agreed upon beforehand and perhaps allow for some flexibility if the work needed by the client exceeds expectations.

Subscription-based pricing models in the legal industry can be structured in a variety of ways to ensure that the clients' needs are met, and the arrangement is financially viable for the attorney or law firm. Some subscription-based pricing models include charging clients a flat fee for unlimited work during a specific time period, such as a quarter of a year, an entire year, over the course of several years or even for a specific "book of business" (i.e., in the case of insurance companies, for cases that originated from occurrences during a specific policy year). Such arrangements may be most useful for litigation attorneys and can include additional incentives for performance,

including bonuses for quick resolution of cases or successes at trial or during settlement negotiations. Since litigation is unpredictable, attorneys must carefully evaluate their practice to quantify the capital needed to fund these types of flat-fee arrangements and should seek to employ safety gauges to ensure fairness. One such safety gauge is a "price collar," which allows law firms to receive partial compensation if their actual fees rise considerably above an agreed-upon amount.<sup>8</sup>

Alternatively, attorneys engaged in transactional work, such as real estate closings, business incorporations or even the drafting of divorce settlements and wills, may wish to charge their clients a flat fee to prepare and file any and all documents necessary to complete the transaction or series of transactions over a period of time. In this context, the law firm may charge a flat fee for each transaction, regardless of the time it takes to complete it, or may charge a flat fee to be "on call" for the client if and when these transactions are needed. Under the latter arrangement, the client may pay the attorney an initial retainer fee and then an additional amount per completed transaction.

Assessing an appropriate fixed-fee amount is not a perfect science. If the law firm has worked with the client for a number of years, data from previous years should help to inform what this "fixed-fee" or subscription fee should be, such that it is mutually beneficial for both the client and the law firm. With new clients, who have no history of billing in a prior year,

applying a subscription-based pricing policy may be more challenging.

Aaron George, who wrote *How to Start A Subscription Based Law Practice (And Why You Should Consider It)*, recommends creating the pricing model for new clients by

add[ing] up the total amount of revenue you generate from a sampling of clients over the course of a year. Try to include some higher value clients, and some lower end ones to get a complete spectrum. Then find the median, and divide it by 12 to determine a monthly subscription rate.<sup>9</sup>

As with preexisting clients, George's pricing model also uses the data law firms already have to assess possible pricing arrangements for clients interested in this fee arrangement. It is clear that this billing approach requires economic analysis, which lawyers must be willing to learn and implement in the context of billing for legal services. A subscription-based pricing model will be most successfully implemented by those law firms that understand that law is a business, where "a product" of sorts is being

sold. Lawyers, like manufacturers, must understand the importance of pricing when it comes to driving sales and increasing profitability.

## **BENEFITS OF SUBSCRIPTION-BASED PRICING MODEL**

Clients benefit from subscription-based pricing models because they are able to (1) budget for their legal costs since they will be paying a pre-established rate for the services within a specific time frame, (2) establish a trusting relationship with a particular law firm since they will be working together throughout this period of time, and (3) respond more efficiently when legal services are required

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since the attorneys will come to know and understand the client's concerns, goals and specific needs. While client relations can be fostered under a billable hour arrangement, it is less likely because clients may not have the same scope of interaction with their attorneys. Repeat interactions between the client and the law firm may also ensure continuity in cases or transactions, which may be particularly beneficial for those clients who wish to establish certain precedents during litigation or settlement.

## **IDENTIFYING THOSE CLIENTS WHO MAY BENEFIT FROM SUBSCRIPTION-BASED PRICING AS AN ALTERNATIVE FEE ARRANGEMENT**

To identify those clients who should consider subscription-based pricing attorneys should first address preexisting clients who have expressed interest in alternative fee arrangements. Legal practitioners understand that it has been increasingly important for clients to carefully focus on their bottom lines and reduce risk. In the context of litigation, for example, many attorneys have observed a noticeable increase in settlements to achieve these goals. Sometimes, this phenomenon is the result of courts with limited resources that simply cannot try every case. It is, however, also driven by clients who value minimizing their risks. While trials present unavoidable risks to clients, the unknown amount of their legal fees does not have to compound this uncertainty. Subscription-based pricing allows a client to pay a sum on either a monthly, quarterly, or annual basis. This cost will not change and, therefore, will provide some consistency for the client's profit and loss statement. Likewise, law firms can benefit from this consistency because they will be able to plan for a certain amount of revenue and work and subsequently

hire the appropriate amount of attorneys to handle the workload.

## **KEYS TO SUCCESS WHEN USING SUBSCRIPTION-BASED PRICING**

As with any deal, careful preparation and negotiation are important when entering into a subscription-based pricing arrangement. This includes research regarding the clients' needs, expectations and objectives to properly assess the amount of work that will be needed to achieve their goals and present a realistic fee structure that ensures both the attorney and client feel they have received the benefit of their bargain. Likewise, to avoid

the feeling that the deal is one-sided, it is necessary for the client and law firm to "establish a relationship of mutual trust based on a true partnership between the law firms and their clients."<sup>10</sup> Such a relationship is cultivated by frequent and open communication with your clients to encourage a team-oriented approach. Both the law firm and the client should work together to devise and follow the strategy to achieve the desired outcome of the case or legal transaction.

## **ETHICAL CONCERNS**

While law is a business, the Supreme Court made it clear in *Goldfarb* that different rules govern businesses and professions, particularly the legal profession, as lawyers are considered officers of the court. In fact, in *Goldfarb*, the Court specifically stated that "forms of competition usual in the business world may be demoralizing to the ethical standards of a profession."<sup>11</sup> Therefore, while we should continue to be creative in the billing methods that we offer our clients, we must consider our ethical obligations when doing so.

The ABA Model Rules of Professional Conduct provide us with general guidance when it comes to assessing the appropriate legal fee to charge our clients. Specifically, Rule 1.5(a) states that "a lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses." ABA Model Rule 1.5 tells attorneys to consider the following eight factors when assessing whether a fee is "reasonable":

1. the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;

2. the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;
3. the fee customarily charged in the locality for similar legal services;
4. the amount involved and the results obtained;
5. the time limitations imposed by the client or by the circumstances;
6. the nature and length of the professional relationship with the client;
7. the experience, reputation, and ability of the lawyer or lawyers performing the services; and
8. whether the fee is fixed or contingent.

New York has adopted the model rules. Under Rule 1.5(a) of the N.Y. Rules of Professional Conduct, “a lawyer shall not make an agreement for, charge, or collect an excessive or illegal fee or expense.” A fee is excessive when, after a review of the facts, a reasonable lawyer would be left with a definite and firm conviction that the fee is excessive. The factors to be considered in determining whether a fee is excessive mirror those of the ABA Model Rule listed above.

Lawyers must be mindful when determining whether to employ an alternative fee arrangement, including a subscription-based pricing model, that specific attention is devoted to ensuring the arrangement complies with all ethical standards and rules. In this regard, we must consider the type of work needed and the likely issues raised by this work. We must also consider the type of attention

and time the work will require, including court appearances and discovery obligations, such as depositions in the case of litigation work. We must also consider when entering into an alternative fee arrangement, the skill of the attorneys who will be assigned to assist the client during the prescribed time period. Finally and most important, attention must also be paid to how much the work would have cost the client under a traditional billable hour arrangement, since ethical rules require attorneys to consider “the fee customarily charged.” If we are seeking to evoke a subscription-based model, which is not customary, then consideration of a customary model is essential. The latter requirement should not provide additional onus on the law firm since, as stated above, costs for hourly rates will likely already have been taken into consideration when assessing the subscription price to ensure that it is mutually beneficial for both parties.

## FINAL THOUGHTS

It is clear that in an increasingly competitive legal market, attorneys should consider the various tools in their metaphorical toolboxes because pricing, including flexible billing methods and arrangements, can drive new business and help cultivate preexisting relationships with clients. The billable hour is one such tool and still is likely to be the one most often used by attorneys. However, to ensure that attorneys are adapting to our clients’ needs and the current consumer climate, we must be prepared to consider and, when appropriate, adopt other billing methods. A subscription-based billing approach is one such popular method that we may see infiltrating the legal billing world, as it has in movie, book and music sales and even the sale of everyday items such as clothes. Attorneys who want to succeed in this new frontier should be prepared to consider both alternative and hourly fees or risk missing out on financially rewarding opportunities.

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