

Pricing Is the Future, Billing Is the Past

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RULE 1.5: FEES

(a) A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses. The factors to be considered in determining the reasonableness of a fee include the following:

- (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 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.

(b) The scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation, except when the lawyer will charge a regularly represented client on the same basis or rate. Any changes in the basis or rate of the fee or expenses shall be communicated to the client, preferably in writing.

(c) A fee may be contingent on the outcome of the matter for which the service is rendered, except in a matter in which a contingent fee is prohibited by paragraph (d) or other law. A contingent fee agreement shall be in a writing signed by the client and shall state the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial or appeal; litigation and other expenses to be deducted from the recovery; and whether such expenses are to be deducted before or after the contingent fee is calculated. The agreement must clearly notify the client of any expenses the client will be expected to pay. Upon conclusion of a contingent fee matter, the lawyer shall provide the client with a written statement stating the outcome of the matter and, if there is a recovery, showing the remittance to the client and the method of its determination.

(d) A lawyer shall not enter into an arrangement for, charge, or collect:

- (1) any fee in a domestic relations matter, the payment or amount of which is contingent upon the securing of a divorce or upon the amount of alimony or support, or property settlement in lieu thereof, provided that a lawyer may charge a contingency fee in collection of past due alimony or child support; or

- (2) a contingent fee for representing a defendant in a criminal case.
- (e) A division of a fee between lawyers who are not in the same firm may be made only if:
- (1) the division is in proportion to the services performed by each lawyer or each lawyer assumes joint responsibility for the representation;
 - (2) the client agrees to the arrangement, including the share each lawyer will receive, and the agreement is confirmed in writing; and
 - (3) the total fee is reasonable.
- (f) A lawyer may charge an advance fee, which may be paid in whole or in part in advance of the lawyer providing those services, and treat the fee as immediately earned if the lawyer and client agree in advance in a written fee agreement which notifies the client:
- (1) of the nature of the fee arrangement and the scope of the services to be provided;
 - (2) of the total amount of the fee and the terms of payment;
 - (3) that the fee will not be held in a trust account until earned;
 - (4) that the client has the right to terminate the lawyer-client relationship and discharge the lawyer; and
 - (5) that the client may be entitled to a refund of all or a portion of the fee if the agreed-upon legal services are not provided.

Comment

Reasonableness of Fee and Expenses

[1] Paragraph (a) requires that lawyers charge fees that are reasonable under the circumstances. The factors specified in (1) through (8) are not exclusive. Nor will each factor be relevant in each instance. The South Carolina version of the rule differs from the Model Rule by making the test in paragraph (a)(2) objective rather than subjective. Paragraph (a) also requires that expenses for which the client will be charged must be reasonable. A lawyer may seek reimbursement for the cost of services performed in-house, such as copying, or for other expenses incurred in-house, such as telephone charges, either by charging a reasonable amount to which the client has agreed in advance or by charging an amount that reasonably reflects the cost incurred by the lawyer.

Basis or Rate of Fee

[2] When the lawyer has regularly represented a client, they ordinarily will have evolved an understanding concerning the basis or rate of the fee and the expenses for which the client will be responsible. In a new client-lawyer relationship, however, an understanding as to fees and expenses must be promptly established, preferably in writing. Generally, it is desirable to furnish the client with at least a simple memorandum or copy of the lawyer's customary fee arrangements that states the general nature of the legal services to be provided, the basis, rate or total amount of

the fee and whether and to what extent the client will be responsible for any costs, expenses or disbursements in the course of the representation. A written statement concerning the terms of the engagement reduces the possibility of misunderstanding.

[3] Contingent fees, like any other fees, are subject to the reasonableness standard of paragraph (a) of this Rule. In determining whether a particular contingent fee is reasonable, or whether it is reasonable to charge any form of contingent fee, a lawyer must consider the factors that are relevant under the circumstances. Applicable law may impose limitations on contingent fees, such as a ceiling on the percentage allowable, or may require a lawyer to offer clients an alternative basis for the fee. Applicable law also may apply to situations other than a contingent fee, for example, government regulations regarding fees in certain tax matters.

Terms of Payment

[4] A lawyer may require advance payment of a fee, but is obliged to return any unearned portion. A lawyer may accept property in payment for services, such as an ownership interest in an enterprise, providing this does not involve acquisition of a proprietary interest in the cause of action or subject matter of the litigation contrary to Rule 1.8(i). However, a fee paid in property instead of money may be subject to the requirements of Rule 1.8(a) because such fees often have the essential qualities of a business transaction with the client.

[5] An agreement may not be made whose terms might induce the lawyer improperly to curtail services for the client or perform them in a way contrary to the client's interest. For example, a lawyer should not enter into an agreement whereby services are to be provided only up to a stated amount when it is foreseeable that more extensive services probably will be required, unless the situation is adequately explained to the client. Otherwise, the client might have to bargain for further assistance in the midst of a proceeding or transaction. However, it is proper to define the extent of services in light of the client's ability to pay. A lawyer should not exploit a fee arrangement based primarily on hourly charges by using wasteful procedures.

Prohibited Contingent Fees

[6] Paragraph (d) prohibits a lawyer from charging a contingent fee in a domestic relations matter when payment is contingent upon the securing of a divorce or upon the amount of alimony or support or property settlement to be obtained. This provision does not preclude a contract for a contingent fee for legal representation in connection with the recovery of post-judgment balances due under support, alimony or other financial orders because such contracts do not implicate the same policy concerns.

Division of Fee

[7] A division of fee is a single billing to a client covering the fee of two or more lawyers who are not in the same firm. A division of fee facilitates association of more than one lawyer in a matter in which neither alone could serve the client as well, and most often is used when the fee is contingent and the division is between a referring lawyer and a trial specialist. Paragraph (e) permits the lawyers to divide a fee either on the basis of the proportion of services they render or each lawyer assumes responsibility for the representation as a whole. In addition, the client must agree to the arrangement, including the share that each lawyer is to receive, and the agreement

must be confirmed in writing. Contingent fee agreements must be in a writing signed by the client and must otherwise comply with paragraph (c) of this Rule. Joint responsibility for the representation entails financial and ethical responsibility for the representation as if the lawyers were associated in a partnership. A lawyer who assumes joint responsibility should be available to both the client and the other fee-sharing lawyer as needed throughout the representation and should remain knowledgeable about the progress of the legal matter. A lawyer should only refer a matter to a lawyer whom the referring lawyer reasonably believes is competent to handle the matter. See Rule 1.1.

[8] Paragraph (e) does not prohibit or regulate division of fees to be received in the future for work done when lawyers were previously associated in a law firm. Also, when a client has hired two or more lawyers in succession on a matter and later refuses to consent to a discharged lawyer receiving an earned share of the legal fee, paragraph (e) should not be applied to prevent a lawyer who has received a fee from sharing that fee with the discharged lawyer to the extent that the discharged lawyer has earned the fee for work performed on the matter and is entitled to payment.

Disputes over Fees

[9] If a procedure has been established for resolution of fee disputes, such as an arbitration or mediation procedure established by the bar, the lawyer must comply with the procedure when it is mandatory, and, even when it is voluntary, the lawyer should conscientiously consider submitting to it. See Rule 416, SCACR. Law may prescribe a procedure for determining a lawyer's fee, for example, in representation of an executor or administrator, a class or a person entitled to a reasonable fee as part of the measure of damages. The lawyer entitled to such a fee and a lawyer representing another party concerned with the fee should comply with the prescribed procedure.

Payment of Fees in Advance of Providing Services

[10] A lawyer may treat a fee paid in advance of providing services as the property of the lawyer and deposit the fee in the lawyer's operating account, rather than hold the fee in trust, if the client agrees in a written fee agreement which complies with Paragraph (f)(1) through (5), and the fee is reasonable under the factors listed in Rule 1.5(a). The language describing such arrangements varies, and includes terms such as flat fee, fixed fee, earned on receipt, or nonrefundable retainer, but all such fees are subject to refund if the lawyer fails to perform the agreed-upon legal services.

[11] When the lawyer has regularly represented a particular client, the written fee requirement in Paragraph (f) may be satisfied by a single agreement with the particular client that is applicable to multiple current or future matters or files, without the need for the lawyer and client to enter into a new written agreement for each individual matter.

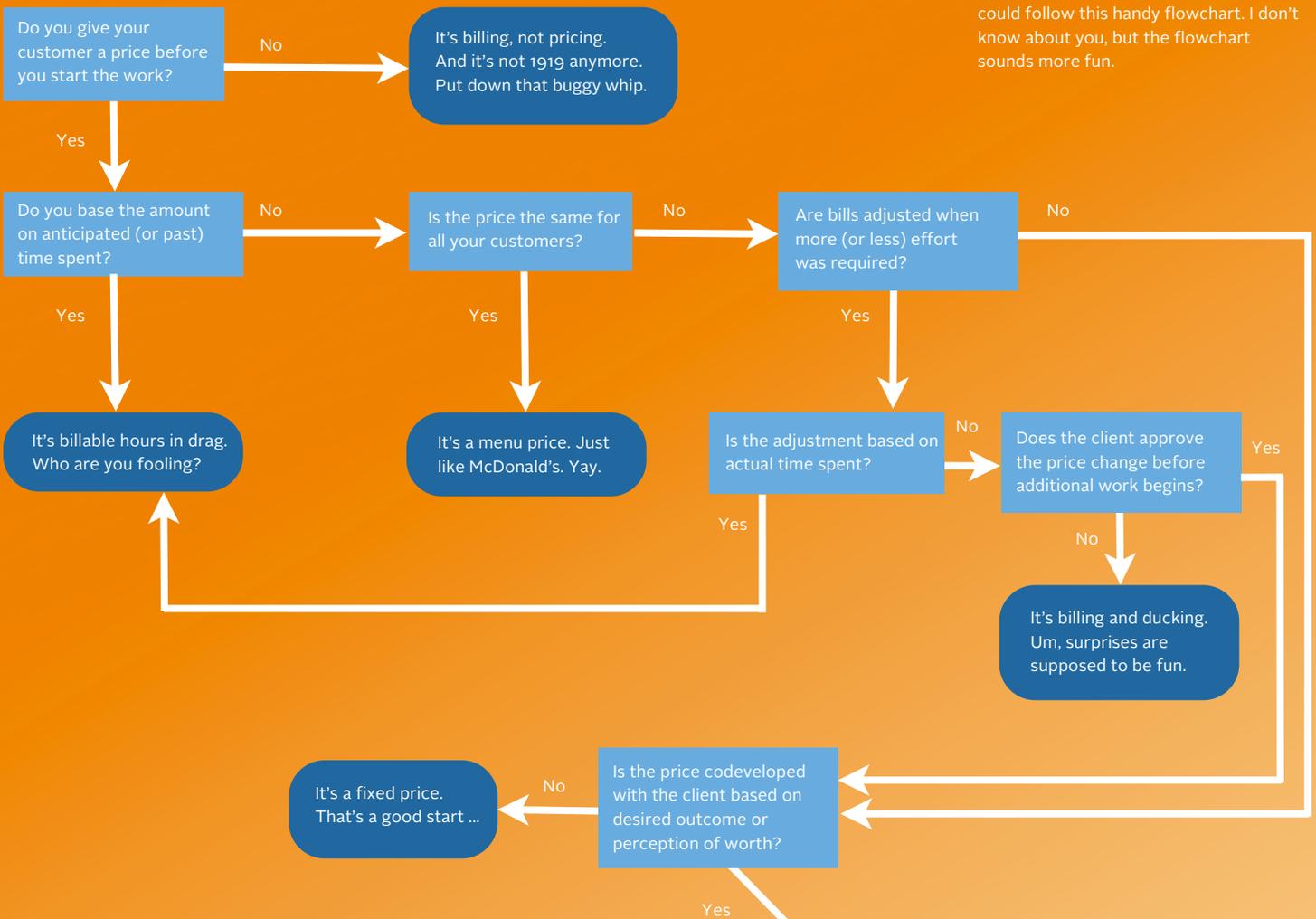
Amended by Order dated July 30, 2012.



What kind of price is it?

Lawyers, accountants, consultants, and other professionals are under pressure to dump the antiquated billable hour and start pricing like the rest of the world does. But there's a lot of misinformation, especially from so-called practice consultants, on what "value pricing" means.

You could go to a two-day seminar on "alternative fee arrangements" or "alternative billing" and come away stupefied by terms like hybrid fees and risk collars and blended rates and "80/120" (whatever that is). Or you could follow this handy flowchart. I don't know about you, but the flowchart sounds more fun.



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10 Steps to Killable Hours

1. **Commit** — You either know how much your service is worth or you don't
2. **Value ≠ Cost** — Price is about value
3. **Toss the timesheets** — Crutch, measuring the wrong thing
4. **Figure out the value** — the 14 things we do
5. **No menus** — not a restaurant, not commodities
6. **Pricing committee** — Get help; friends don't let friends misprice
7. **Timing** — After meeting, before work
8. **Scope** — not just a brand of mouthwash
9. **Change orders** — Why are contractors more sophisticated?
10. **Learn from mistakes** — not comparing to hourly

14 Factors in Fixed Pricing

1. **Client** — Analyze the client
2. **Importance** — Assess the importance of the situation
3. **Urgency** — Assess the urgency of the situation
4. **Competitors** — Pay attention to what competitors charge
5. **Outcome** — Consider relative values of the outcome
6. **Elsewhere** — Consider difficulty of getting better service elsewhere
7. **Expertise** — Importance of my expertise to success
8. **Past charges** — Consider past charges for similar work
9. **Appropriate** — Were past charges appropriate in retrospect?
10. **More work** — Likelihood of more work from client
11. **Past work** — Consider amount of past work from client
12. **Getting job** — Consider importance of getting job
13. **Capacity** — Do you have the bandwidth to do the work?
14. **Multiple prices** — Consider single price vs. multiple prices

10 Steps to Killing the Billable Hour

BY JAY SHEPHERD

When I tell other lawyers that I haven't billed an hour since 2006, they usually look surprised. When I tell them that I do litigation using fixed, upfront prices, they think I'm crazy.

The most common question I get from lawyers is "How do you do it?" I usually give some short answers accompanied with a mischievous smirk. ("Uh, Jay, what's wrong with your face?") I usually don't give out the secrets of how we do it. But for you, and only you, I will. Just don't tell anyone.

First, a little background: My firm, Shepherd Law Group, is a Boston boutique that defends and counsels employers. I founded it 12 years ago as a solo, and as of this writing we're at four lawyers. For the first eight years, we billed hourly like every other firm. I hated it — I've always hated it — but I didn't know how to do it any other way.

But one of the perks of having your own firm is the ability to do it your way. So I spent those eight years figuring out how to ditch the billable hour. In 2006, we started to fix prices on a trial basis, usually with new clients on discrete matters. As the year passed, we noticed that the clients with the fixed prices were happier. We also noticed that for the most part, we were happier doing the fixed-price work.

So on the last day of 2006, we billed our last billable hour, and we've never looked back. Our

revenue grew substantially, as did our client satisfaction.

How did we do it? The following ten steps will teach you how to kill the billable hour. Follow them, and you'll be on your way to a more-fulfilling, more-successful practice.

Step 1: Commit. This is all or nothing. It's a cop-out to "offer" so-called alternative-billing options while still falling back on the same old hourly rates. This tells the client that you don't actually believe in the value of your services, and either don't have the requisite confidence or knowledge to be able to set a price. It shouldn't be up to clients to determine what your business model should be. When you go to the mall, do the shopkeepers ask you how they should price their wares? Of course not. We are the vendors here. It is up to us to determine our own business models and our own prices.

Step 2: Recognize that value and cost have nothing to do with each other, and that price is all about value. Your clients don't care a whit about your costs. That's your problem, not theirs. All they care about is the value that solving their problem has for them at that instant. If your price equals or is less than that value, then they will be willing to hire you. That's it. In hourly billing, where the

price is kept hidden from the client (and generally from the lawyer, too), the decision to hire is based on guesswork. When the final price ends up being more than the client's value, you end up with disgruntled clients. Hence, lawyer jokes.

My law firm's costs are for the most part fixed, as are yours. I pay fixed amounts for rent, insurance, utilities, office supplies, and payroll. If a particular case ends up involving more work for me or my colleagues, that doesn't affect my costs. There is no such thing as a profitable case or client — just profitable practices. Quit worrying about the costs of a particular matter, and start worrying about your clients' measurements of value.

Step 3: Toss your timesheets. For many lawyers, this is the hardest step. We all use timesheets as a crutch. It gives us something we can measure. Oftentimes, we are afraid that our clients won't trust us. That they will question whether we actually did the work. You need to have confidence in yourself and in the value you provide. You are not in the business of selling hours. You are in the business of selling widgets, and the particular widget you sell is the solution to the client's legal problem.

In the end, you either got the problem solved (or tried to) or you didn't. What difference does it make to the client how much time you spent on it? Are they paying for your time or for your knowledge and experience? As long as you educate the client beforehand about what he or she is buying (a desired solution, not hours), then you will never need to provide a pedantic, Industrial Age recitation of the hours you spent.

Step 4: Start figuring out the value of your services. This, of course, is the real trick. How do you know what the value of your services is in the eyes of your clients?

The first step is to know your client. How serious are they? How sophisticated? Are they experienced users of legal services? How urgent is their problem? How hard will it be for them to find someone else? What will your competition charge? What does the client stand to lose if the problem isn't solved? Or gain if it is solved?

What about you? How much does your particular expertise matter to a favorable result? What have you charged this client in the past? Or other clients? Were those fees light or heavy, in retrospect? How much do you want this particular business?

People often ask if I looked at old bills before setting my prices. I did. We actually analyzed eight years' worth of hourly bills. But not to reverse engineer prices from our past hourly rates. Instead, it was more to see how our past "prices" compared to our retrospective sense of the clients' values. If you don't have eight years of past bills, don't worry about it. You can still figure out what your clients think about their problems.

Step 5: You're not a restaurant, so don't make a menu. A lot of people think that having fixed prices means having the same prices for every client. These aren't Happy Meals, people. They're not commodities. Your services are as unique as you are, and your clients' needs are as unique as they are. How could you possibly set a single price for a single type of matter for any client that comes walking through your door? You can't. Don't.

Step 6: Form a pricing committee. Pricing is difficult, and incredibly subjective. Don't just go on your own gut feelings. Ask your colleagues what they think. Describe the work required and the needs and traits of the client, and ask them what they think is the right price. Even if you're a solo, find people you trust whom you can bounce pricing questions off of from time to time.

Step 7: As in comedy, pricing is all about timing.

One of the biggest problems with hourly billing is that the price (which is merely the rate times the time) doesn't become known until it's too late — after the work is done. You need to set your prices *before* you do the work.

On the other hand, you can't set a price until you know enough about the job. Don't quote a price over the phone. Instead, bring the client in for an interview, learn about them and their problem, and then agree to get them a proposal in writing by the next day.

Step 8: Remember that scope isn't just a brand of mouthwash. When you propose your price, you'll want to put it into a fixed-price agreement. This explains the scope of what you're agreeing to do to solve the problem. Otherwise, you risk "scope creep," an insidious condition where you end up doing more than what you agreed. Spell out the scope of what they're buying, and both you and your client will avoid nasty surprises. And bad breath.

Step 9: If contractors can figure out change orders, why can't you? And if the scope of the job does change, you need a way to be able to price the new work before you start doing it. That's what change orders are for. Contractors use them all the time.

Just don't let the change orders become the tail that wags the dog. As you get more experienced with open pricing, you'll get better at anticipating the scope of the work, and you won't need to use change orders too often.

Step 10: Learn from your pricing mistakes. You will make them, of course. We have. Everyone does. But a pricing mistake doesn't mean

comparing your price to what you would have received had you billed hourly. A pricing mistake is realizing that you probably could have charged more for a job.

The solution is to learn from the mistake. Could you have charged more? If so, remember that, and charge more next time.

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Pricing is an art, not a science. It's hard, and it takes practice. But it is better for clients than hourly billing, and for you, too. Follow these steps, and pretty soon you'll be wondering why you ever billed hourly.

For more information on open pricing, check out my blog on the topic at clientrevolution.com.

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Here's a short collection of articles from *The Client Revolution*, Jay Shepherd's award-winning blog on fixing prices and fixing the practice of law. The *ABA Journal* recently included the blog in its "Blawg 100" list of the top hundred websites for lawyers by lawyers. You can read more at clientrevolution.com

Billable showers

by Jay Shepherd



Vanessa is a senior litigation associate at a large Northeast law firm. She is a hard worker, a good writer, and a very intelligent young woman. She bills at \$575 an hour. She carefully tracks her time.

One afternoon, she is working on a summary-judgment brief. She is focused on a tricky jurisdictional issue that is central to the case. She has just come up with what she feels is a clever approach based on a casenote she just read. She goes onto Lexis and downloads the case. She prints it and reads it carefully. It seems helpful. She then looks up similar cases, finds 24 of them, and reads or skims all of them. She takes careful notes, and she starts outlining this section of the brief. Then, to her dismay, she finds a more-recent case that changes the law in her jurisdiction. This shuts the door to her clever argument. She puts her research and her notes into a file folder, and she deletes the outline she had been working on.

She checks her computer clock, pulls out her timesheet, and enters the 3.6 hours that she spent on this work, along with a careful description of the tasks she performed.

The next morning, well before sunrise, she's taking a shower. After lathering, rinsing, and repeating, she suddenly gets a brain flash on how to solve a different issue in the case. Collateral estoppel! Of course! As the hot water splashes over her, she realizes that she's just come up with a killer argument for her brief. She'll do the research when she gets into the office, but she's certain it will work.

While she's dressing, she grabs her Blackberry and makes a note of the time she just spent working on her case. She puts down 0.3 (including the rinsing and the repeating), because she spent at least 18 minutes analyzing the issue.

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The brainstorm in the shower proved to be the winning argument in the summary-judgment brief, saving the client hundreds of thousands of dollars by avoiding a trial. The 0.3 hours cost it \$172.50, assuming Vanessa did not expense her seaweed conditioner.

The time she spent doing jurisdictional research for her brief proved to be wasted effort. None of that work benefited her client. The 3.6 hours cost her client \$2,070 (plus the marked-up cost of the online legal research).

To all you lawyers who bill by the hour: please explain to me why the online-research work was worth 12 times more than the brainstorm in the shower.

If you are paying attention to the value the client receives, you wouldn't bill by the hour.

You'd bill by the shower.

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Originally published on *The Client Revolution* on 14 January 2009. © Jay Shepherd. Available at <http://bit.ly/bObFm>

A coffee parable

by Jay Shepherd

So it's another gray New England winter afternoon, which means it's time for my caffeine fix. I walk down the street to my usual Starbucks, but for some reason the line is longer than usual and I don't feel like waiting. Then I notice a coffeehouse that I had never seen before. It's surprising because it's bigger than normal and has a very staid, conservative name. More like a string of names, actually, followed by a "P.C." I take this to mean "professional coffeehouse," or something.

The first thing I notice inside is that the décor is heavy on the mahogany and expensive modern art. A sign on the wall

talks about how they have stores in 30 states and eight countries, and that they just opened a location in Shanghai. The sign suggests that they're very excited about this.

I go to the counter and I'm greeted by a tired-looking twentysomething. Her nametag says she's a "Coffee Associate." She asks me what I would like, which I expected, but then she asks me when I need it by, which surprises me.

"As soon as possible," I say. "Is that going to be a problem?"

"Well, it depends," she says. "There are a lot of variables involved. It's hard to say." She then starts talking about arcane developments in coffee production, bean types, and brewing methods. She uses a kind of jargon that I can't really follow, and though I have the sense that it was second nature to her, I'm not sure she really understands it herself.

"How do you want your latte?" she asks. I tell her: triple shot, nonfat milk, extra hot. She writes this all down very carefully on the side of the cup. Then she walks over to a co-worker, whose name is Dave. I notice that his nametag identifies him as a "Coffee Partner," so I assume he's some kind of supervisor. They discuss something — I'm not sure what, but I'm hoping it's my coffee order.



They finish their conversation, and then she walks over to a back corner where there's a desktop computer with the store's logo on the screen. She taps away at the keyboard, all the while taking notes from her research. After a while, she logs off the computer, then delivers her written notes to the supervisor. They have another discussion.

I'm starting to get impatient. "Is my coffee on its way?"

She smiles apologetically and assures me it's coming soon. "I just have to talk to Elizabeth about the extra-hot issue. She's our dairy specialist." And she walks away and confers with another woman who I assume is Elizabeth.

When I'm all but delirious from my lack of caffeine, my barista finally tells me that my latte is ready. It seems well made, and it tastes fine, although I would have preferred to have it more quickly. The young woman thanks me and wishes me a good day.

"But I haven't paid you yet."

"Oh, don't worry," she says. "We'll send you an invoice."

Nearly two months later, I receive an envelope with the name of the coffee company on it. By now, I've already for-

gotten what I had gotten. I open the envelope and nearly faint.

"What the heck?"

Inside is a three-page invoice. The dollar amount is outrageous for a cup of coffee. But what's truly staggering is the level of itemization. First, there's a charge for the young woman's time with the following description:

Conference with customer in regards to customer's preference for beverage. Further discussion with same in regards to size, temperature, and fat content. Online research conducted in regards to same.

The time she spent is tracked to the nearest tenth of an hour.

Next is an entry for the time that she spent speaking with Dave the coffee partner about my order, as well as an entry for his time speaking with her. I notice that his rate is considerably higher. Then there is a pair of entries for the woman's conversation with Elizabeth the dairy specialist, covering both women's time. Again, the dairy partner has a high rate.

Underneath the time entries is a section for expenses. There's a charge for the paper cup, a charge for the cardboard sleeve, a charge for the fancy raw sugar in the brown packets. There was a charge for the stirrer and a charge for the lid. There was also an "online research" charge. And there was an energy surcharge for the additional steam required to make my latte extra hot.

I am livid. I pick up the phone and dial the number on the invoice. I ask for Dave the coffee partner, and after several tries, I finally reach him. I ask him why all this stuff is on the bill.

"Those were the costs of producing your cup of coffee, sir. We have to charge you for the costs, or it wouldn't be fair to the other customers."

"But a charge for the cup?" I ask. "Everyone gets a cup. Why is there a charge for it?"

"We charge you our cost, plus a reasonable markup," he says. "Same with the lid and the sugar and the other client expenses."

I am unmollified. "What about these so-called internal conferences that my barista had with you and the dairy specialist?"

“Well,” says Dave, “she’s just a first-year coffee associate. It’s part of her training. She needs to consult with experienced coffee partners.”

“Hmmpf,” I say. “I’m not sure I should have to pay for her training. Plus, it ended up taking an awfully long time to get my coffee.”

“I understand, sir. But we want our associates to be as thorough as possible.” He pauses. “I’ll tell you what: I can take ten percent off the bill.”

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Lawyers: if you’re using cost-plus pricing (to wit, billable hours and marked-up expenses), keep in mind that your clients are probably just looking for a fast cup of joe.

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Originally published on *The Client Revolution* on 3 January 2009. © Jay Shepherd. Available at <http://bit.ly/cSDE4l>

What’s my time worth?

by Jay Shepherd



I can name six different companies that would have been shut down if it weren’t for my law firm.

Now, that’s not just me bragging or exaggerating or taking more credit than we deserve. In each of the six cases, the company had been founded by someone who

had gone into competition with his or her previous employer. In each case, the old company had sued to enforce a non-compete agreement and had asked a court to shut down our client. In each case, we successfully defended the new company, allowing them to stay in business.

Now compare that to other work I’ve done as an employment lawyer. For example, I’m often asked to write or revise a company’s personnel handbook. These handbooks often include provisions that I consider ridiculous. What most drives me crazy are bereavement-leave policies, where employers make hyperlegalistic rules about whose funeral an employee can go to without having their pay docked. Needless to say, I’m not a fan of helping an employer decide whether an uncle or a niece is a close-enough relative to justify an employee being allowed time off for the funeral.

As many of our readers know, my firm, Shepherd Law Group, hasn’t billed a single hour since 2006. But we used to, and for some of the work I described above, we did.

Hourly billing values equally all the time I spend working for clients, regardless of the project I’m working on, and regardless of the value the client receives.

Is there anyone out there who believes that the work I did to save those six companies from court-ordered extinction was equal in value — on a minute-for-minute, or rather six-minutes-for-six-minutes, basis — to the time I spent tweaking stupid bereavement policies?

If you can honestly say that you think the work was equally valuable, then you are a true defender of the billable hour, and we’d love to hear from you. But I won’t hold my breath.

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An alternative to “alternative billing”

by Jay Shepherd

Words matter. What we call something matters. The name we give something usually provides people with the first opportunity to form an opinion about that something, so it’s important that the name fits.

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I hate “alternative billing.” (If someone quotes me on this, make sure they include the quotation marks.) It’s a terrible term; one that does injustice to the concept. As I’ve said before, it has a seamy connotation to it,

like “alternative lifestyle.” It seems vaguely Berkeley or Brookline or (gasp) Vermont, which makes tradition-bound lawyers very uncomfortable. We need an alternative for “alternative.”

And I don’t like the “billing” part any better. First, it makes it seem like the issue is about invoice styles, which makes it more boring than the Tax Code or, say, professional soccer. (“Woo! Another one-nought blowout!”) Second, it places the focus on the law firm and its administration, rather than on the client and the value it is getting.

The intellectual godfather and guru of this ill-named field, the Verasage Institute’s Ron Baker, has long advocated “value pricing” as the preferred term. [Update: Ron points out in the comments that he prefers “fixed price” when talking to the customers themselves; “value pricing” is more of a behind-the-scenes term.] It’s definitely an improvement, and it is far more descriptive and accurate. The main idea, of course, is that lawyers should price their services based on their value to the client. (Gee, it sounds so obvious when you say it like

that.) But my quibble is that the word “value” has Walmart-y connotations. People often connect “value” with “discounted,” and that’s missing the point entirely.

I propose a different approach:

Open-price lawyering.

What we’re talking about here is legal services where the price is known to the customer ahead of time, so that the customer can make an informed decision about the worth of those services to him or her before actually agreeing to buy them. In other words, the price is out in the open. There is a fair exchange between lawyer and client with the client having as much knowledge about the price as the lawyer.

And what’s the opposite of open-price lawyering?

Hidden-price lawyering.

The price is hidden from the client (and, often, even from the lawyer). I’m not saying that in a judgmental sort of way, like the lawyer is intentionally hiding the price from the customer. Well, maybe I am. But even if it is unintentional, that’s no excuse for doing it.

Clients of the world: which would you rather have — open-price lawyering or hidden-price lawyering? Try out the term, and let me know what you think.

Or offer an alternative.

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“How do you set your prices?”

by Jay Shepherd



This is the question I hear the most. (It isn’t, sadly, “How did you get to be so flippin’ handsome?” That’s second.) Unsurprisingly, I get this question mostly from other lawyers, and sometimes from in-house counsel. They ask this ques-

tion because my firm, Shepherd Law Group, hasn’t billed a single hour since 2006. We work for employers lowering their workplace risk and charging fixed prices for our services. So lawyers are always asking this question.

The question is at the heart of lawyers’ hesitation to break their addiction to hourly billing and make the leap to fixed pricing. It is the root of lawyers’ fear that they will make a mistake in setting their prices.

As if. The funny thing is that lawyers don’t seem to have any trouble setting their hourly rates. And just to be clear: rates are a form of pricing, albeit an unsophisticated, rudimentary one. Ask a lawyer (we’ll call her “Monique,” because that sounds French and sophisticated and I’m about to make fun of people who try to sound French and sophisticated) who’s just hung out a shingle how she set her hourly rate:

Well, I used to charge \$525 an hour when I was a seventh-year associate at my BigLaw firm. I figure people will expect me to charge less because my firm is so much smaller. On the other hand, my practice is very specialized, and I really own my niche. [It’s pronounced “nitch,” by the way; it does not rhyme with quiche. Saying it that way does not make you sound French and sophisticated. But I digress ... Told you.] On the other other hand, my office is in the suburbs instead of downtown. So I’m charging \$425 an hour.”

Monique’s (made-up) monologue accurately reflects the thought process — explicit or just intuitive — that most lawyers undertake to set their rates. Think about it. Layered beneath the *I-was-a-big-firm-lawyer* pomposity and the *now-I’m-on-my-own-what-do-I-do?* abject fear is some pretty sophisticated market analysis. The legal marketplace often does put a lower value on work done by a lesser-known firm. The legal marketplace usually does place a premium on the skills of a specialist. The legal marketplace does place some value on a law firm’s location on Wall Street as opposed to Maple Street.

My point is: Monique did not come up to me and meekly ask how she should set her rates. (In part, on account of her being imaginary.) So why should it be so different when we’re talking about real (that is, fixed) prices instead of rates?

The answer is: because lawyers seem to think that the price has something to do with the (perceived) cost of providing the service. Something to do with the hours spent on doing the work.

As if. (This is my new favorite sentence.) Look, genius: let me first dispel the notion that legal work that takes more time costs more. You pay your associates an annual salary, right? Very few firms pay their lawyers by the hour. So the firm's "costs" do not rise when a motion takes six hours to write instead of three. Yes, yes. I know. "It's the opportunity cost. The extra three hours means that lawyer can't be working on something else, and that adds up over time." Sorry — I'm not buying that. If you have more work than you have lawyers available to do it, then congratulations — and hire more lawyers.

But more importantly, as I have said before, your customers don't care about your costs. The price they will pay is less than or equal to the amount that they value your service at that time. Period. What Monique did in her rates analysis is estimate how her potential clients would value the suburban small-firm nichework she has to offer. She did not wonder how much providing that work would "cost."

So ask your question again:

"How do you set your prices?"

I'll tell you. (Just promise not to tell anyone else.)

- I analyze the client.
- I assess the importance of the situation.
- I assess the urgency of the situation.
- I pay attention to what my competitors charge.
- I consider the relative values of the different possible outcomes.
- I figure out how hard it would be for the client to get better service elsewhere.
- I determine how important my firm's expertise is to the likelihood of a successful outcome (in other words, is this going to be easier because of our particular skills, or could any trained monkey use the Interwebs to find the answers?)
- I consider what we've charged other clients in the past for similar work
- I consider whether those charges were heavy or light in retrospect
- I consider the likelihood of getting more work from this client
- I assess how much work we've done for this client already

- I wonder how important getting this particular job is to our firm (if it isn't, I might raise the price)
- I decide whether to do a single price for the whole gig, or whether (and how) to break up the job into minigigs with separate prices
- and then I say, "This is our price."

Simple, right? No, it's not. Price things too high and you don't get the work. Price things too low and you get work you don't want, or clients you don't want, or you just don't make enough money.

But it's not that hard. You don't hear car manufacturers and watchmakers and restaurateurs and baseball players and movie stars whinge about how hard it is to set a price. They set the price. If people buy at that price, great. Increase the price. If they don't, *zut alors*. (Oh, so sophisticated.) Lower the price and try again.

That's how I set my prices.

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A one-question test for your law firm

by Jay Shepherd



To figure out how good your lawyer is, give him or her the following test. It only has a single question, so it will only take about three seconds to administer. On the other hand, it will take considerably longer to answer. And it should.

Here it is:

Question One How much will this cost?

That's it. Five words only, but it's the whole ballgame. If your lawyer can't correctly answer it, then you've got the wrong lawyer.

Now for the Teacher's Guide:

- Every case, every matter, every job will have a different answer.
- The answer your lawyer gives you won't necessarily be the same as the answer he or she gives another client.

- “It depends” is not an acceptable answer. Neither is “Well, there are variables”

One of the commonest complaints I hear from CFOs and general counsels is that law firms pitching their wares always talk about how good they are and how experienced they are. Unlike other vendors, they never talk about how they’re going to save the company money. That’s because the law-firm business model doesn’t provide a means for doing that. In the billable-hour system, costs are passed on to the client, meaning that there is no incentive to reduce them. Meaning that they won’t.

A fixed price avoids that problem, and requires the law firm to be efficient. But a fixed price also requires the law firm to know and understand the value of its services, something it can only do well if it really knows its business.

Many lawyers have insisted to me that you can’t put a fixed price on litigation. There are variables, they whinge. We can’t control the costs. What if the other side hits us with a bunch of discovery? What then?

What then indeed.

If your law firm knows its business well, then it should know the value of the service it provides. Hiding behind a fear of variable costs is an admission that you don’t really know your business. An airline doesn’t say “there are variables” when charging you for your ticket. And yet headwinds, storms, airport congestion, and overtime can dramatically increase the airline’s cost of a particular flight. But your ticket price won’t change after they sell it to you.

The Red Sox won’t say “there are variables” when selling you a ticket for tonight’s Yankees game. Yet Sox-Yankees games tend to be much longer than other games; plus it’s raining lightly with more weather expected. A longer game, especially one with rain delays, means increased costs for the Red Sox in wages, overtime, electricity costs, and so on. But your ticket price won’t change after they sell it to you.

The Red Sox know their business. The airline knows its business.

Does your law firm? Give it the one-question test.

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Lexis, coffee filters, and associates: law firms’ overhead

by Jay Shepherd



My law firm pays the same amount for LexisNexis online research every month. For a fixed price, we get unlimited access to the caselaw and statutes that we use in our practice. Now don’t get me

started on the absurdity of paying money for free, public-domain, governmental content; that’s a topic for a different post. Instead, let’s talk about how we handle this expense.

Unlike many firms, we don’t pass this cost along to our clients. For one thing, it’s impractical to do so. Who wants to bother with dividing up the total monthly nut for all our Lexis research and then apportioning it by client? What if we reuse research originally done for one client in another client’s case? Who pays?

Who cares?

Online research is overhead. It’s the cost of doing business as a modern law firm. We don’t apportion our rent, insurance, taxes, coffee, or legal pads (actually, who even uses legal-sized legal pads anymore — it’s an eight-and-a-half-by-eleven world, kids). Yes, it’s possible that in a month where we do a ton of research for one massive case and an unusually small amount of research for all our other cases, it could seem fair and appropriate to have the research-heavy client bear the expense of the legal research. But why would we? Again: I’m not going to have that client pay its “fair share” of rent for that month. So why is online research different?

It’s not as if my online-research expenses go up as a result of this heavier usage. As I mentioned, I negotiated a fixed fee with LexisNexis. (And your firm should, too, unless you’re too ill informed to understand the value of your monthly legal research. In which case, get better informed.) If I do a ton more research in June than in May, my expense isn’t going to go up. So why should I bother to “pass along” (or worse, pass along and mark up) these costs to the client. Overhead is overhead.

My costs are my costs. They don’t change much month to month. I pay our rent, payroll, insurance, taxes, fees, supply costs, and so forth every month, and it comes out about the same each time. This is the cost of doing business, and as long as we can bring in enough revenue to cover it, then we’ll remain in business.

Which brings me to associates and their time.

Why do law firms feel the need to “pass along” the cost of the associates? How are associates any different from LexisNexis or coffee filters or photocopy toner? Most law firms pay their associates an annual salary, divided up into monthly, semimonthly, or biweekly pay periods. As with LexisNexis, insurance, and coffee filters, the firm knows what its monthly payroll nut is going to be. Whether they work harder or less hard, for one client or fifteen clients, the associates’ pay isn’t going to change from month to month. The law firm’s cost isn’t going to change either. So why feel the need to apportion this cost to clients?

Associates are overhead. Just like coffee filters.

(Partners are too, but that gets more complicated. Let’s stick with associates for now. And coffee filters.)

Law firms don’t apportion and pass along their rent, insurance, taxes, coffee-filter expenses, or fancy-artwork costs to clients. Why not? Because it’s all overhead, and clients wouldn’t tolerate it. Send a client a bill for some portion of your month’s rent and see what kind of reaction you get. You’ll have clients marching in with rulers and floor plans to make sure they’re not getting ripped off. (That’s not actually true; the clients would simply fire you.)

So why do they tolerate it with associates’ time? Habit. And a sense that they have no other choice.

Now folks at other law firms will whine that they need to know how profitable an associate’s work is, and how profitable a particular matter or client is. Without tracking and billing for time, they can’t possibly tell.

Nonsense. Take an accounting class. Profit is revenue minus expenses. The question is whether the firm is profitable, not whether an associate or a client is profitable. The relevant question for a client is whether you’re delivering enough value to the client to justify the best price they would pay. The relevant question for an associate is whether he or she does good work for your clients.

The whining continues: But if we don’t track associates’ time, how do we know if they’re working?

After your accounting class, take a management class. You know by *managing* your associates.

Bottom line: Overhead is overhead. Clients don’t want to pay for overhead.

They want to pay for *value*.

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Scope + Value

S T A T E M E N T

PROBLEM TO SOLVE

Client Sample LLC
Matter ABC v. Sample LLC
Date October 11, 2010
Problem ABC has filed a third-party claim against Sample for tortious interference with the contractual relations between it and a former employee who has sued ABC for unpaid wages. Our job is to make this litigation go away as favorably as we can.

SCOPE OF WORK

RESPONSE TO COMPLAINT

- Research claim, review pleadings in underlying lawsuit, advise client, communicate with opposing counsel, draft and argue motion to dismiss.
- Price 5,500
- Due before we file in court.

DISCOVERY

- Conduct and defend written discovery and remaining depositions.
- Price 55,000
- Due now: 30,000
Due 10/15: 15,000
Due 11/15: 10,000

SUMMARY JUDGMENT

- Move for or defend against summary-judgment motion, including motions and hearing. Only if necessary.
- Price 25,000
- Due 30 days before scheduled hearing

PRETRIAL PREPARATION

- Prepare case for trial in federal court. Includes preparing witnesses and exhibits
- Price 55,000
- Due 90 days before scheduled trial date

HOW WE WORK

SERVICE GUARANTEE

We don't just guarantee our prices; we guarantee our service. If you're not delighted with the service we've given you, all we ask is that you tell us and give us a chance to fix it. If we can't, we'll refund our fee for that service.

OPEN PRICING

Hourly billing makes for hidden pricing, as the client doesn't know how much the service will cost until after it's completed. Instead, we use Open Pricing for all our matters. By giving you an Open Price for our work and a detailed description of the scope of that work, we'll ensure that there aren't any surprises.

CHANGE ORDERS

Our prices are not estimates — they're prices. If it takes us more work than we anticipated, that's on us, not you. On the other hand, if developments require us to do work beyond this plan, we will first send you a change order describing the work and giving you an Open Price for it.

EXPENSES

Unlike other law firms, we do not charge you for routine photocopies, faxes, FedExes, online legal research, telephone charges, postage, or automobile expenses. We consider these expenses to be our overhead costs. We will pass along to you — with no markup — expenses that we incur on your behalf for major items like deposition transcripts, computer forensics, outside copying jobs, court costs, and out-of-state travel.

