Legal Times

WEEK OF NOVEMBER 20, 2006 • VOL. XXIX, NO. 47

ALM

Do the Math on Your Law Firms

Take one $600-per-hour lawyer, multiply by a messy case, and figure out what it really costs.

By Rees W. Morrison

All law departments review their law firm invoices. Few law departments, though, extract management insights from those invoices. In-house counsel mostly view invoices as paperwork to be initialed and processed for payment by someone in accounting.

Yet invoices contain many useful insights, and the effort it takes to reap them is modest. Let's consider what a department can glean from the invoices of a single law firm and what it can learn from the metrics of company invoices taken from multiple law firms. My point is not so much about questionable billing practices, such as those Amtrak may have allowed, as it is about what law departments can learn from invoices.

Management Matters

Start with the invoices from your primary law firm over the past six months on a reasonably sized matter, say, a matter with billings of $10,000 or more a month. How many total timekeepers (lawyers and paralegals) show up on that matter during the period? Of those timekeepers, what percentage of them accounted for 80 percent or more of the time on the matter?

Drive-By Billers

This figure gives you some idea of whether the firm has dedicated certain timekeepers to your matters. That is, does the firm have a core team supporting you consistently, a team that develops familiarity and experience? You usually want the fewest number of people working on your matters and the largest percentage of their time. For example, if a $600-per-hour partner has put in 0.2 hours each month, you might suspect that partner of sprinkling time among his matters. You might even take a tough stand on drive-by billers: "I won't pay for more than two people whose time is less than two hours in a month!"

Next, for those core team members who account for 80 percent or more of the total time, what percentage of a typical level of billing did they work on your matter? If you take 2,000 chargeable hours per year as a rule of thumb, and an associate billed 1,500 hours to you, those hours would be 75 percent of that associate's time committed to your work. A good allocation is between 50 and 75 percent of a lawyer's time, because if the percentage climbs above that, it is likely the associate has no other client projects and perhaps is padding the bills to fill his time sheet. As the saying goes, if you want something done efficiently, ask a busy person.

Admittedly, you can't have it both ways—as few timekeepers as possible, but none of them who are hitting their billing quota just on your matter. Learn from the invoices and then strike a balance.

Another way to analyze six months of bills is to break out the timekeepers by level. What percentage of the time was accounted for by partners? What percentage by associates? By paralegals? Stated very broadly, on typical matters, a plausible pattern would be 30 percent partner time, 50 percent associate time, and 20 percent paralegal or other time.

A variation on this method is to cluster the percentage of the total billings accounted into rate tiers: 30 percent by those who bill between $300 and $350 or more an hour, etc. If you look at the distribution of time by billing rate, you can tell a lot about the differences between law firms. It's not titles that you care about, although they correlate with billing rates, but it's cost per hour, leverage, and distribution of time. Hence, a plausible pattern for a large firm's bills might be 20 percent of the time accounted for by those who charge $500 an hour or more, 30 percent of the time for those at $400-$500 an hour, 30 percent for the $300-$400-an-hour timekeepers, and the remainder for those lawyers billing less than $300 an hour.

Or you can take a look at the ratio of disbursements—covering anything other than what falls under billable hours—to fees. A typical ratio for everything other than lawyers' and paralegals' fees (excluding expert witnesses) is about 10 percent of the total bill, or approximately $9 of fees for every $1 of disbursement expenses. This analysis might suggest how you could substitute your preferred vendors, such as trial consultants or photocopiers, instead of using the firm's vendors, and save money.

A different perspective looks at timeliness. How many days elapsed from the last time entry on a bill until you received the bill? A well-run law firm should get you the bill within 30 days of the period's close.

Another analysis involves creating a table. The table shows the name of each timekeeper on your set of bills down the left side while the columns show each month. Fill in the hours for the timekeepers during the months and you should start seeing patterns of consistency over time. It's a visual way to understand how the law firm has staffed your matter.

Now, Compare the Firms

After you apply these analytics to a single firm's invoices, turn to the invoices of several other primary firms and make the analysis comparative.

With the wider set of data, you can calculate each law firm's effective billing rate. Total the amount of all the bills and divide by the number of lawyer hours on them. That gives you the effective lawyer-billing rate, which includes the time of paralegals and the cost of disbursements. That number can be compared to the cost per internal-lawyer-hour.

Second, calculate the difference between your internal per-hour cost and your firms' rates. Generally, the gap between the in-house lawyer cost and the law firm rate is between 40 and 60 percent.

For a third insight, look at the invoices from your group of law firms to test whether the effective billing rate matches the complexity of the matter. It makes sense that more sophisticated matters take more partner time and thus show higher rates.

A fourth insight comes from correlating the size of the law firm—measured by the number of lawyers at the firm at the end of the most recent year—to the firm's effective rate. Research has shown that the larger the firm, the higher the effective billing rate. You may come to realize that you need to more closely match firms to types of matters.

Finally, introduce yet another element into the invoice review. Match the invoice data to the inside lawyer who is chiefly responsible for the performance of the outside firm whose bills you are studying. Whatever patterns you learn from the bills may be partially a result of the oversight by that inside lawyer. It may be that the in-house lawyer has done a poor job of directing the law firm. That lawyer may not know or care about such notions as delegation, staff focus, and timeliness of billing.

All of this benchmarking is only useful if you speak with your law firms and push them toward more cost-effective practices. Present the comparative data to each firm and point out where they have less delegation, more associates who come and go, a high expense ratio, slower billing, or other indicators of inefficiency. Assess your progress with a similar analysis done six months later. For each measure of law firm effectiveness, you can show by an arrow and its length how much the law firm improved its lagging behavior or maintained its superior behavior. If you couple the message to outside counsel with a corresponding instruction to inside counsel, you will pack a one-two punch.

A sophisticated matter-management system can help you capture and calculate some of these metrics, especially if you use electronic billing to gather detailed data from bills, such as the level of the timekeeper. Otherwise, it does not take much time to extract the relevant data from your set of bills.

Keep in mind that this article is not about the kinds of billing abuses that third-party bill auditors should ferret out—block billing, differences in amounts billed for the same event, days of more than 10 hours billed, and long, suspicious patterns of hours. Trained and motivated in-house lawyers can spot and stamp out these poor billing practices. Nor does this analysis rely on outside guidelines and their restrictions. It is simply about looking at the data available from each invoice in a new light.

Bill review should not be just a drudgery to be gotten through. In fact, bills can tell you much more about the performance of your law firms and your own staff than most law departments realize.

Rees W. Morrison, co-head of law-department management consulting for Hildebrandt International, hosts the blog www.LawDepartmentManagement.typepad. com. He can be contacted at rwmorrison@hildebrandt.com.