OUTSIDE PERSPECTIVES

# Why Is Budgeting The Hardest Part Of Litigation?

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Each month, we use this space to write about some development in complex litigation that we hope will generate thinking about a particular topic of interest to those reading *Corporate Counsel*. The topics are substantive, borne of our experiences in handling various types of litigation. This month, we digress from a discussion about the substance of litigation to one about the process of litigation.

Last fall, we sponsored an American Lawyer Media seminar for "Litigators and Leaders." The focus of the program was litigation boutiques and other firms with less than 150 lawyers where litigation comprised a substantial portion of the firm's practice. In the course of preparing the programming, I spoke with several in-house counsel about a variety of topics. A top issue with every in-house counsel with whom I visited was litigation budgeting.

Mention the word "budget" to most litigators, and they react like my kids do when I try to pass along some life wisdom—"yea, yea, I know, I know."

The distance between the views of many lawyers and in-house counsel surprised me. But it ought not have. Few lawyers innately appreciate the demands under which in-house counsel operate. The business side of business, including legal departments, is not taught in law school. Few if any firms provide effective training on the topic. I have never seen a seminar designed to teach lawyers about budgeting or about the fiscal demands imposed on in-house lawyers by company executives. One is compelled to wonder about a service industry that so utterly fails to educate and train its members about an issue so important to its clientele.

My colleagues and I just completed a day-long retreat that focused exclusively on litigation budgeting. Jeffrey Carr, General Counsel of FMC Technologies, Inc. and John Rosengren from Gallagher Benefit Services, Inc. provided insight into the demands they face, how those demands are translated into demands on their in-house lawyers and, ultimately, on their outside lawyers. Indeed, FMC Technologies has developed a proprietary system—ACES®[1]—which, among other things, rewards or punishes both inside and outside lawyers for how each performs versus an agreed budget. The clear message was that surprises versus budget are bad.

**Why is effective budgeting alien to litigators?**

Those feeling charitable toward outside counsel might focus on the lack of control over the activities of their opponent, the things the "crazy judge" might order the parties to do, and the general uncertainties associated with litigation. Those feeling less charitable might suggest these as reasons:

- Lawyers have never learned to be accountable for how they spend their client's money.
- Lawyers don't run their practices as businesses.
- The billable hour.

Upon critical review, I vote with those feeling less charitable toward lawyers even though I have articulated to clients on more than one occasion each of the reasons advanced by those feeling charitable to lawyers.

Why have I reached this conclusion? Am I a turncoat? I prefer to think that I have wakened to the coming reality of our profession, but time will tell.

**Lawyers have never learned to be accountable for how they spend their client's money!**

If anything, lawyers are trained to be indifferent to their client's economic interests. Associates are judged on the quality of each piece of work and the concept of "good enough" is eschewed. Lawyers also are compensated on the quantity of their hours, not the quality or efficiency of those hours. So long as firms refuse to break these habits, associates and the partners who judge them will continue to be indifferent to their client's money. And should a client question the firm's efficiency, the most that will

happen is some adjustment will be made to a bill. This remedy is ad hoc, leaving the root problem untouched.

**Lawyers don't run their practices as businesses.**

There is little in the structure of a traditional law firm that is business-like. No business for example, hires new employees every year and pushes every other employee up a notch, save for a few seasoned employees who may not be quite good enough and so are fired. Yet that is precisely how the traditional up or out partnership structure works. Few businesses can be so unconcerned with the cost of producing its product. Yet most law firms have no idea how much it costs to produce their product. Most refer to the old wives tale that "one-third goes to salary, one-third to overhead, and one-third to profit." Yet is there a single businessperson in the real world who believes that the first product costs as much to produce as the last?

**The billable hour**

The lawyer's continued devotion to an economic model that causes their economic well being to be diametrically opposed to their client's deserves special comment. No one would ever dream of a contingency fee agreement that rewarded a bad result. Yet the hourly rate frequently generates more make-work and more "creative timekeeping" than any other economic model. More tangents and issues are explored, regardless of real relevance, because of the billable hour than would ever be pursued under any other economic model. All of these flaws in the system would be sufferable if the system produced superior results. Few really believe it does, however.

But what does this indictment of the billable hour have to do with budgets? It would be easy to conclude these points prove lawyers lack the economic and business sense to develop a real budget. But the problem is deeper. These points really suggest that most lawyers lack the economic discipline to generate a meaningful budget, based upon the cost of doing only that work that is truly necessary to obtain the desired result. We are smart enough to take the upside risk of performing positively versus a budget, but unwilling to accept the corresponding downside risk. It boils down to an "I'm with you, win or draw" mentality that is at fundamental odds with the rigors demanded by a system that depends on tight budgeting.

Of course, all of this is a matter of perspective. Jeffrey Carr, for example, argues that the responsibility for this problem is really the client's. Absent clients that insist on imposing risk on their outside counsel, why should a firm voluntarily assume risk? There is, to be sure, truth in what he says.

**Okay, hotshot, what's the answer?**

Like most problems of consequence, the solution is here is not a simple one for there is no simple way to change the soul of the system. But there are some ways to start the process of change. As an example, any system that aligns the lawyer's economic interests with his or her client's interests will force improvement. FMC Technologies accomplishes this through its ACES® program by rewarding counsel who perform well to budget and effectively punishing those who do not. Another company uses performance to budget as a key factor in deciding whether to use a firm on future matters. Still other companies are at least exploring use of contingent or incentive-based fixed fee arrangements. Because most companies do not publicize "performance to budget" information, it is impossible calculate the benefits these companies have achieved. But those who have employed such systems have become powerful advocates for their use.

Even though some companies are demanding more of their outside counsel, they remain in the minority. The one certainty, though, is that clients will have to drive change. Lawyers will mimic behavior that it rewarded and will push for change in their firms only when their economic success demands it.

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[1] Information about ACES® can be obtained from FMC Technologies by contacting Mr. Carr at 281-591-4585or jeffrey.carr@fmcti.com

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