

# Value Pricing: What Do Clients Want?

*Note: This article was adapted from the fifth edition of the Legal Project Management Quick Reference Guide, an electronic library of LPM tools and templates. For more information, see [www.legalbizdev.com](http://www.legalbizdev.com) or call 800-49-TRAIN (800-498-7246)*

If a potential client asks you for “value pricing,” what exactly are they looking for?

While the term has achieved buzzword status in law firms, that does not mean that every client who asks for value pricing is looking for the same thing.

In fact, when we interviewed leaders of 50 AmLaw 200 firms for our book “Client Value and Law Firm Profitability,” there was a conspicuous lack of consensus about how to define value. As one senior executive put it (p. 32):

The truth when it comes to value is that I’m not sure what our clients mean. It means different things to different people.

Obviously, in a situation like this, the first step is to ask probing questions such as “Can you tell me more about what you have in mind?”

When you do, the answer you hear is likely to include one or more of these four factors:

1. Alternative Fee Arrangements
2. Lower cost
3. Extra services such as free seminars
4. A radical pricing approach based on clients’ perceived value

## 1. Alternative Fee Arrangements (AFAs)

Experts disagree about many aspects of AFAs, starting with the way they are defined and how they should be categorized. But virtually all agree that the recent growth in law firms’ uses of AFAs has been based on the search for value.



### Editor-in-Chief

LARRY SMITH  
Phone 201-854-3288  
Fax 201-861-6728

### Senior Editor

STEVEN T. TAYLOR  
Phone 503-245-3209

PATRICK J. McKENNA  
Contributing Editor

### Wolters Kluwer

JOANNE MITCHELL-GEORGE  
Editorial Director

MEGAN ROSEN  
Senior Developmental Editor

---

### Editorial Office

2700 Lake Cook Road  
Riverwoods, IL 60015  
Phone: 847-267-7000  
Fax: 847-267-2945

The most widely used definition limits the term AFA to fees that are fully or partly non-hourly. (A few people still use a broader definition which includes blended rates in which a single middle rate is charged for senior lawyers who normally charge more, and junior lawyers who charge less.)

When ALM Legal Intelligence published its survey *Who Really Drives AFA Use—and Why?*, (<http://www.almlegalintel.com/SurveyDescription.aspx?id=VSLYO4Oih00=&type=fEFgIaD+grg=>), they reported that six types of AFAs had been used in the preceding year by at least half of law firms. In order of frequency, they were;

- flat fee
- capped fee
- partial contingency or success fee
- contingent fees
- phased fee
- flat fee with shared savings

The term “value based fees” is often used to cover the same types of categories. When the Association of Corporate Counsel published its “Guide to Value-Based Fees,” the nine groups of fees they listed (p. 6) covered the same nonhourly ground, in slightly different subcategories.

In our opinion, it is unfortunate that the two terms—AFAs and value-based fees—are still used interchangeably by some clients. The simple fact that a fee is fixed or contingent does not necessarily imply greater value. In fact, if a fixed or contingent fee is higher than a traditional hourly arrangement, it could offer less value.

In this context, the important point is that some clients who ask for “value pricing,” are actually looking for an AFA proposal.

## 2. Lower Cost

A number of managing partners and senior executives quoted in our book “Client Value

and Law Firm Profitability” focused on cost, as in this quote:

I think when some clients talk about value, they really just mean cheaper... They want exactly the same service... but they just want it for less. (p. 32)

The most common way to lower costs, of course, is simply to offer a discount on standard hourly rates. And in many cases, clients who start out asking for AFAs end up deciding that they are more comfortable with discounted hourly rates.

When we interviewed 37 managing partners and other leaders from the AmLaw 100 for our *LegalBizDev Survey of Alternative Fees*, several expressed frustration about developing complicated AFA proposals at a client’s request, and then being asked for an hourly discount:

We propose alternative fees, and the clients come back and say, “Gee, that was a really good idea. Thanks for that. Could we just do hourly with ten percent off [instead]?” (p. 33)

What we hear regularly... is, “Wow, that was such an innovative fee proposal. It was really good to see that your firm is thinking outside the box and is willing to take risks and partner up with us, and put skin in the game. Now let’s talk about how much of an [hourly] discount you’ll give us [instead].” (p. 32)

A leader from another firm summed it up like this:

[AFA discussions are] like a junior high dance. There’s a lot more talking than dancing. (p. 37)

## 3. Free Services Such as Seminars

A number of managing partners and others we interviewed for our book *Client Value*

and *Law Firm Profitability* mentioned additional free services, as in this quote:

[Some] clients... are using [value] as a code word for additional benefits. They want seminars, and they want more from the attorney/client relationship—more interaction, advice, access to information as part of the relationship. (p. 32)

Of course, law firms have long offered extras of this type. Client pressure for greater value, however, is forcing firms to take these offers to another level.

For example, Perkins Coie, a firm with over 1000 lawyers, has developed a program for their biggest clients called the *Client Advantage*<sup>TM</sup>. When Law.com published an article about this approach, the title was “The Law Firm Disrupted” (<https://www.perkinscoie.com/images/content/1/9/v2/192793/Law.com051418.pdf>) and the program was called a possible “template for future relationships between Big Law and corporate clients.” The article went on to quote several Perkins Coie clients, such as Lisa Konie, the Senior Director of Legal Operations at Adobe Systems Inc., who described the way Adobe’s law department “truly worked together [with Perkins Coie lawyers] as if [they] were an extension of [our] legal team.”

For example, when one large client was interested in improving their document management systems, Perkins Coie provided access to their own employees who had been involved in installing the firm’s document management systems. These employees passed along all the valuable lessons they had learned in this process.

Another example of the way the *Client Advantage*<sup>TM</sup> program is “stay[ing] a step ahead of trends,” is the fact that Perkins Coie is using their license to this online fifth edition of *Legal Project Management Quick Reference Guide* (<http://www.legalbizdev.com/projectmanagement/index.html>) to go beyond internal use. They also offer these templates to key clients who want to improve LPM within their departments.

Of course, there is no charge for any of the services offered within the *Client Advantage*<sup>TM</sup> program.

## 4. A Radical Pricing Approach Based on Clients’ Perceived Value

The fourth and final approach that clients may be thinking of when they request “value pricing” is far more radical, and has led to an enormous amount of discussion.

In his book *Implementing Value Pricing: A Radical Business Model for Professional Firms*, CPA Ron Baker offers this narrow definition of value pricing:

The word value has a specific meaning in economics: “The maximum amount that a consumer would be willing to pay for an item.” Therefore value pricing can be defined as the maximum amount a given customer is willing to pay for a particular service, before the work begins. This is not to suggest we can capture one hundred percent of maximum value, but rather that we have the potential to access some of it utilizing strategic pricing (Ronald J. Baker, *Implementing Value Pricing: A Radical Business Model for Professional Firms* (Wiley, 2010), 233).

Accountants refer to hourly billing as a “cost plus” pricing model, because the price is ultimately based on the cost of providing the service, including overhead and profit.

In cost-plus pricing, cost is estimated before you set the price. In value pricing, you start with the price the customer is willing to pay, then control your costs to meet that price. Baker summed up the difference in these two diagrams:

*Cost-Plus Pricing*

Services » Cost » Price » Value » Customers

*Value Pricing*

Customers » Value » Price » Cost » Services

Baker feels strongly that value pricing should replace hourly billing. In fact, his Web page bio begins with this statement, in bold and italics: “Mission: “To, once and for all, bury the billable hour and timesheet in the professions.”

Similarly, Chapter 17 of Baker’s book *Implementing Value Pricing* is titled “The Deleterious Effects of Hourly Billing” and describes numerous disadvantages, including misaligning interests, focusing on effort instead of results, hoarding of hours, leaving money on the table, and diminishing the quality of life.

When Baker spoke at a law firm conference entitled “Can ‘Value’ Pricing Replace the Billable Hour?” (<https://biglawbusiness.com/can-value-pricing-replace-the-billable-hour-perspective/>), he began by saying:

“I am here to bury the billable hour and the time sheet. The only place time should count is in prison... Time is a constraint, that’s all it is. You can’t hoard it or buy and sell it. (For knowledge workers) it’s like plunging a ruler into an oven to get the temperature.”

Like a lawyer’s bill, he said, “we can measure labor pains in six minute intervals. But instead of focusing on the result — *here’s the baby!* — we bill for the contractions. These measurements obscure reality. A client always buys to satisfy a want. A client buys value.”

Adopting a value-based approach promises, in his view, better alignment with clients and hence a better relationship. Also it will take the discussion from the impoverished arguments over efficiency to one he thinks that lawyers and other professionals should be having: how efficacious is our work? Are we providing the maximum desired impact? We don’t care if our heart surgeon is efficient. We want him to be efficacious. Same with lawyers.

In *Implementing Value Pricing* (p. 160), Baker has also emphasized that value pricing can sometimes produce far more revenue than the hourly approach. He gave the example of an accounting firm that was engaged to develop an exit and management succession strategy which produced substantial tax savings. Initially, the CPA billed at standard hourly rates, but at some point he said to the client,

“I don’t believe hourly rates [are]... appropriate [in this case]... You tell me what all the value of this is to you.... I know I will be happy with whatever you come up with.” Ultimately he was extremely happy because the total payment was “a little bit over \$1 million.”

By then, the CPA had stopped tracking time on this engagement, so it is impossible to say exactly how much he would have gotten on an hourly basis. He, however, did say his prices had “skyrocketed” and reading between the lines of Baker’s account our guess is that hourly rates would have totaled less than \$100,000 instead of the \$1 million the CPA actually billed.

Any lawyer would love the concept of value pricing if it meant that they could get paid 10 times what they would earn for billing hours. Also, some law firms see this type of value pricing as a ray of hope in a challenging marketplace, an opportunity to increase profitability at a time when there are unrelenting competitive pressures to charge less.

At the end of the story of the CPA whose profits skyrocketed, Baker went on to say that while lawyers should not expect to earn 10 times their normal rate very often, his approach to value pricing will usually increase profitability, and should be the standard approach for most lawyers.

Companies like Apple have become very profitable by creating consumer perceptions of value, and pricing products like the iPad and iPhone accordingly. But there is only one Apple, and there are dozens of companies like Samsung, Lenovo, Hewlett Packard,

Sony, Dell, and Microsoft who compete with various Apple products, and often find themselves competing on price.

A small number of the most profitable law firms in the world have been using value pricing for years, just as Apple has. They, however, are at the top of the profession and specialize in “bet the company” work. If a client is defending a multibillion dollar lawsuit, acquiring a powerful rival, or being accused of a white-collar crime, they will care much less about the price than about the results. However, only a very small percentage of the legal marketplace falls into this “bet the company” category.

Most legal work falls into two other categories:

1. “Important” where price matters, but is only one factor in selecting a firm, or
2. “Commodity” in which price is the single most important factor in selecting among qualified bidders.

By definition, if in the commodity category value equals the lowest price, then Baker’s approach does not apply.

Lawyers sometimes deal with matters that could justify the kind of premium billing that Baker describes. For example, trusts and estates lawyers will generally find that most of their practice falls into the important or commodity category. But in a few cases they may add much more value than their hourly rates. For example, they might save an estate tens or hundreds of thousands of dollars by renegotiating debt. In these cases, it would be a good idea for the lawyer to consider Baker’s type of value-based billing and charge a premium for that work.

While such situations may be relatively rare, this type of value pricing is a good concept for lawyers to keep in the back of their mind. When situations like this arise, lawyers should call attention to the value they are delivering, and consider utilizing innovative pricing strategies to capture it.

If you are interested in applying Baker’s approach, his books and articles also include a significant amount of legal project management (LPM) advice, since Baker sees LPM as necessary to maximize value. To go beyond LPM and actually set the best price Baker offered this advice in a post entitled and “How to value price: Just do it”:

Stop analyzing, stop looking for a checklist, a formula, or detailed instructions like this was a piece of IKEA furniture—there aren’t any.... Just do it. ([http://www.verasage.com/index.php/community/how\\_to\\_\\_value\\_price\\_just\\_do\\_it/](http://www.verasage.com/index.php/community/how_to__value_price_just_do_it/))

Unfortunately, we believe that in the current marketplace, Baker’s definition of “value pricing” can backfire by creating an expectations gap. Law firms want to believe it can lead to higher prices and profits, but clients want to pay less.

In its 2018 *Law Firms in Transition* survey of 398 managing partners and chairs from US firms with 50 lawyers or more, Altman Weil reported that 74% of firms said their associates were “not sufficiently busy” and 49% said the same about equity partners. That’s one of the reasons 96% of these law firm leaders predicted that “more price competition” is a permanent trend in the legal marketplace.

The result can be some very aggressive bidding. Here’s what managing partners from two different AmLaw 200 firms had to say about the implications in our *Client Value* survey:

It’s kind of like an airplane. An empty seat gives you no revenue. So when we’re evaluating bids or contingent fee cases, we look at the actual and predicted workload of the people who expect to be working on a matter. And we may make a different business decision if someone’s well is pretty dry. (p. 80)

Sometimes we know a matter is not going to be profitable, but we take it

anyway because we've got overcapacity that we're not going to be able to get rid of quickly. It's not profitable, but it's more profitable than zero. (p. 80)

Therefore, in our opinion, it would be a mistake to follow Baker's radical suggestion to "trash your timesheets." In today's legal marketplace, you're going to need all the data you can get to determine your costs, and decide just how low you are willing to go.

It is important to note that this article focuses on pricing tactics rather than changes in the way lawyers practice which increase efficiency. However, all of the experts quoted in this piece—the Association of Corporate Counsel, the managing partners we interviewed in our surveys of value and AFAs, and Ron Baker's books on value pricing—emphasize that that all value pricing

assumes that lawyers also increase efficiency through LPM. Whether a client is interested in AFAs, lower cost, free services, or Baker's type of value pricing, it all starts with LPM.

But what does this all mean to a lawyer whose prospective client raises the idea of "value pricing"? Only the client knows for sure. And even they may be a bit uncertain, until you ask probing questions, and listen very carefully to their answers. ■

—Jim Hassett and Tim Batdorf

*Jim Hassett (jhassett@legalbizdev.com) is Chairman and Tim Batdorf (tbatdorf@legalbizdev.com) is CEO of LegalBizDev which helps law firms increase client satisfaction and profitability by improving project management and business development. They can be reached at 800-49-TRAIN (800-498-7246).*