BECAUSE I'M WORTH IT

Sally Dyson reports on the proceedings of a recent Professional Services Marketing Group Directors' Breakfast where discussion of alternative fee arrangements and the difficulties that professionals face in justifying their fees was the order of the day.

Early on an inclement January morning, I joined a gathering of business development heads at a PSMG Directors' Breakfast kindly hosted by law firm, Winckworth Sherwood, in their meeting rooms overlooking the Thames. As the sun struggled to rise over St Paul's, I led the participants through a session entitled "Facing down the fear of alternative fee arrangements".

The presentation began with an appraisal of the changing popularity of different fee types since 2011. Relying on research from Winmark, in the legal sector, I was able to report that, of the buyers of legal services surveyed, 56 per cent had decreased their use of hourly rates, whilst 83 per cent had increased their use of fixed prices. A further 50 per cent had upped their use of success fees and 42 per cent were availing themselves more of value pricing. (Numbers add up to more than 100 per cent as many survey participants had used law firms multiple times, on a variety of different bases.)

In one year, 58 per cent of clients had decreased their use of hourly rates, whilst 83 per cent had increased their use of fixed prices.

Having acknowledged the key drivers of such changed buying behaviour; notably client activism, economic pressures, technological advances and competition from offshore and outsourced service providers; we moved on to an exploration of the attitude to alternative fee arrangements ("AFAs") commonly exhibited by professional services firms. I highlighted four commonly seen behaviours. Type A firms, try to **avoid** AFAs at all costs but often wind-up in the undesirable position of having to give up-front discounts to their hourly rates in order to win business. They are then forced into offering further discounts in order to get their bills paid. Type B firms **begrudgingly** concede to client pressure and offer AFAs without being properly equipped to do so. Unsurprisingly, such firms struggle to operate AFAs profitably as they suffer from budget over-runs and unchecked scope creep. Type C firms fare little better. These firms exhibit **conflicted** behaviour. Senior management will have invested in systems and processes to enable fee earners to operate AFAs but most of their fee earners fail to make use of the systems and support available to them. This is generally because the firms' reward systems do not incentivise fee earners to change their behaviour. If billing targets remain supreme, then fee earners are not motivated to adopt the efficient working practices essential to making a success of AFAs. Finally, there are type D firms which effectively **deliver** AFAs and reap the rewards in terms of enhanced profitability, improved cash flow, better client relationships and competitive advantage.

Unsurprisingly, amongst firms finding themselves in categories A, B or C described above; there is a mis-perception that AFAs cannot be operated profitably. This is hardly surprising in firms making piecemeal attempts at AFAs without the necessary financial understanding or business tools to predict, with accuracy, the likely cost to the firm of conducting a matter. In fact, firms which have successfully adopted AFAs have found that in some cases, they make greater profits than they would have done employing hourly rates. This may have been due to the firms winning work because of their creative fee proposals; or it might have been that the discipline of working with AFAs has forced them to adopt more efficient working practices. The final explanation, which, without doubt, drew the attention of the breakfast delegates, was that some firms, operating AFAs, are able to earn a significant uplift on what they would have earned by billing only in accordance with time on the clock.

We proceeded to put such firms under the microscope. How did they do it? The essence of our discussion, distilled here, is that a firm must persuade its clients that it is **"worth it"**. When charging on the basis of hourly rates; firms are charging for their effort. But most clients are uninterested in how hard a firm has to work. Instead, clients concentrate on the value or utility of the services that they will receive

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The (quite literally) million dollar question becomes how to capture that value and charge for it? Firms often do not find it easy to enunciate the value that they provide to individual clients but this skill is absolutely central to justifying the firm's charges. The reason that value seems so ephemeral is that it is totally subjective. Firms must be able to convey to their clients the value that they provide in terms that are meaningful to each client.

The only way to do so is for firms to engage directly with their clients.
It is often not so simple as posing a direct question to a client such as "what does value mean to you?" Few clients are able to conceptualise value without some intelligent prompting and guidance from the firm. Firms are best advised to tease out the answer by

asking pertinent questions. One American head of pricing likes to ask clients: "what is your pain?"

If, for example, the client complains of pressure of work then the firm can emphasise the ways in which it will ease the client's burdens by acting autonomously on the client's matters whilst at the same time operating simple billing processes requiring minimal client effort. The firm should always be cognizant of the client's objectives when instructing the firm. Service providers are inclined to think only in terms of their work products such as drafting a contract. The underlying objective for the client however will be related to the purpose of that contract. Completing a lease on a new office building for example may mean that staff who have been scattered across several run-down offices in sub-prime locations will be united in one convenient location with consequent increases in morale and productivity. Timely completion of the lease may actually increase the client's profitability – which is something worth paying for!

A regular refrain from firms (which was repeated at the breakfast meeting) was that clients often ask for "creative pricing proposals", when in reality they appear only to want to slash their spend. When clients ask for creative proposals it is often because they don't know exactly what they want. If the firm can put a number of options on the table (each of which will be a desirable outcome for the firm) then the client will recognise which option provides the best value for their current needs.

The lessons of the morning were therefore threefold:

- Fond hopes in some quarters that hourly rates will be restored to favour look likely to be dashed as the year on year data show ever increasing up-take of AFAs by clients.
- Firms that merely dabble in AFAs are likely to get their fingers burnt but firms that harness budgeting tools and understand their own worth will be rewarded.
- Value billing can be a very lucrative method of charging. To succeed in this sphere, firms must recognise the difference between price and value; establish what value means for each individual client at the time of the engagement and then be prepared to offer a range of alternative fee structures which will all deliver the financial returns sought by the firm.

This article was originally prepared by Sally Dyson for PSMG magazine. Sally has written in greater depth on fees and value billing in her book "Budgeting and Negotiating Fees with Clients: A Lawyer's Guide" available from http://www.mpmagazine.com/bookshop/