

IS THERE A SEA CHANGE TOWARD AFAS?

IN-HOUSE COUNSEL GIVE IT A SOLID “MAYBE”

WHEN IT COMES TO ALTERNATIVE FEE ARRANGEMENTS, actions speak louder than words. A recent *InsideCounsel/Leader & Berkon* survey of about 140 in-house counsel, suggests just that: Nearly 56 percent of responding in-house counsel believe there has been a sea change in the valuation of legal services that is here to stay.

The time should be ripe. The outside counsel spend is a prime target for companies looking to cut costs in the midst of the recession. One would think the downturn provides just the push needed to move AFAs squarely into the mainstream.

Yet a wide gap remains between the perception of that fundamental transformation and actual practice, as not quite half also report less than 10 percent of their outside counsel spend is structured as AFAs. Fewer than 5 percent of responding law departments employ AFAs for more than half of their outside counsel budget.

In addition, one quarter of the respondents think the status quo is fair or prefer working with incumbent firms so current practice would seem to have a base constituency.

So why the disconnect? Are AFAs truly ascendant, or has the recession merely amplified a decades-old debate?

The answers lie in a combination of the practical challenge of adopting new practices to accommodate a time of tight belts and great uncertainty, and lingering doubts about how to keep both quality and accountability consistent in a new management construct.

For over half of the respondents, quality concerns top the list of the most significant obstacles to expanding AFAs. Close behind are the difficulty of determining a new pricing structure and a belief that it may not be possible to accomplish fees not based on the billable hour without overpaying.

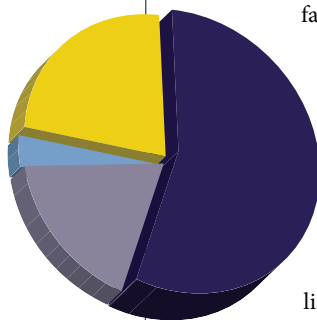
“People are afraid there will be a drop-off in quality in an alternative fee arrangement,” says Gordon Wylie, Vice President and Litigation Counsel at Guardian Life Insurance. “They’re worried that they will never get the best people working on their account – that they will never get the A-team.” Wylie likens it to the anxiety associated with managed health care – you get a doctor that is cheaper, but not better, and generally not the one you want.

Meeting the Cost Predictability and Lower Costs Challenges

The vast majority of inside counsel list cost predictability and lowering costs as by far the most important considerations when contemplating AFAs. On those two points, in-house counsel are of one mind. Wylie

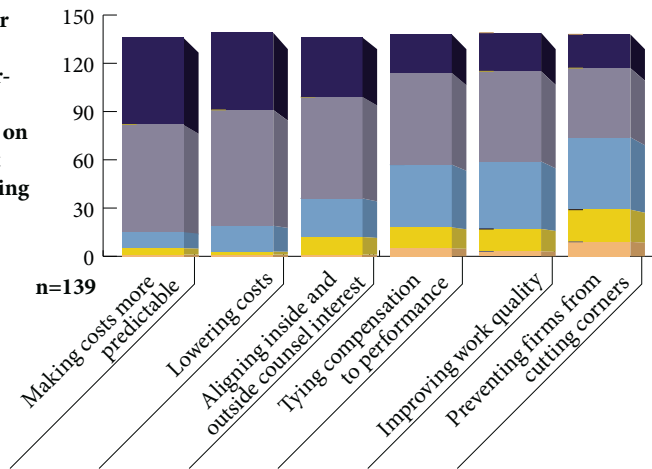
Which statement most closely mirrors your opinion of the alternative fee discussion?
n=138

- There is a sea change in the approach to valuation of legal services that is here to stay = 55.8%
- The alternative fee arrangement discussion will go away when the economy bounces back = 17.4%
- Irrelevant = 3.6%
- Don't know = 23.2%

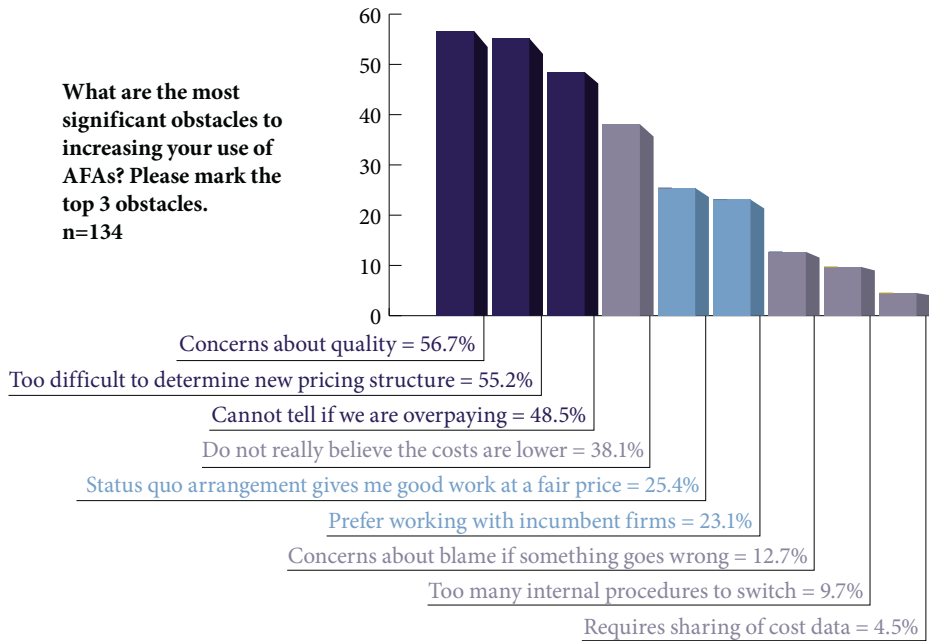


When evaluating whether to enter into AFAs, how would you rate the importance of each of the following considerations on a scale of 1-5 (1 being not important at all and 5 being of critical importance)?

- 5
- 4
- 3
- 2
- 1



What are the most significant obstacles to increasing your use of AFAs? Please mark the top 3 obstacles.
n=134



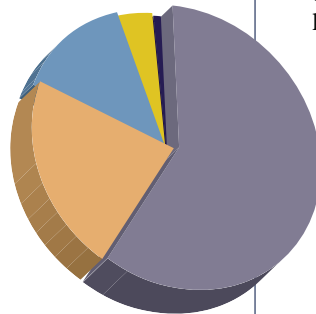
believes that eventually all companies will issue budget report cards to their firms, as success in meeting these challenges often directly affects the in-house leader's compensation.

Leader & Berkon Partner Glen Silverstein sees an opportunity for legal service buyers to take advantage of the competitive legal marketplace to find well-qualified lawyers, with all sorts of incentives to perform, who will accurately bid on legal work through real budgets or even capped or fixed fees. To

Please estimate the percentage of your 2010 outside counsel spend that will be alternative fee arrangements.

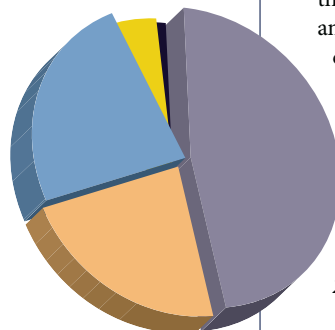
Response - All Respondents
n=123

- 0 - 10% = 59.3%
- 11 - 25% = 22.0%
- 26 - 50% = 13.8%
- 51 - 99% = 4.1%
- 100% = 0.8%



Respondents Who See a Sea Change
n=72

- 0 - 10% = 47%
- 11 - 25% = 22%
- 26 - 50% = 24%
- 51 - 99% = 6%
- 100% = 1%



the extent these costs become disconnected from the billable hour, the better.

"Why shouldn't a law department arrange representation based, at least in part, on competitive bids? After all, there are plenty of excellent attorneys in every jurisdiction," he says. "There are a thousand ways to go wrong in any lawsuit and an enormous amount of time is wasted trying to avoid even small 'mistakes' when the ultimate determination is usually driven by the underlying facts, law, and the lawyer's central theme. From a macro-perspective, it simply would be better to control the overall cost of the litigation."

Evidence of Forward Momentum

The tension many counsel feel over AFAs may merely represent the resistance that greets any significant change. Lawyers on both sides of the corporate fence are hesitant to go against their schooled aversion to any risk, even if it makes more economic sense.

The strongest evidence that AFAs are actually gaining momentum is found in a higher adoption rate among in-house counsel who perceive the sea change. Nineteen percent of all respondents anticipate AFAs will account for more than one-quarter of their overall outside counsel spend in 2010. By contrast, among those who say the value proposition has already shifted and definitive change is here, almost one-third plan to use AFAs for 25-100 percent of their 2010 outside counsel spend.

"I have no impression that this is a temporary thing," says Wylie. "We have a fundamental shift in the way we are thinking. Law firms that don't think this will last are being delusional."

For more information on this survey, please contact Glen Silverstein at 212.486.2400 or gsilverstein@leaderberkon.com.