

THE RECORDER

TUESDAY, DECEMBER 22, 2009 133RD YEAR NO. 245

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An ALM Publication



CHANGING WITH THE TIMES: Todd Smithline, left, and Raj Jha founded their San Francisco firm in 2004, and started experimenting with subscription-based fees in early 2008.

Month to Month

The bulk of Smithline Jha's revenue now comes from clients who pay a flat subscription fee

By Petra Pasternak

RECORDER STAFF WRITER

When San Francisco lawyers Todd Smithline and Raj Jha negotiate terms with a new client, they never bring up the billable hour anymore. For the last two years, their five-lawyer San Francisco firm, Smithline Jha, has made an almost complete switch from traditional billing to a monthly subscription model.

“We did find all this tracking of hours and dealing with conversations around rates to be distracting, and we didn't think the billable hour was a good way to measure the value of the services we provided,” said Smithline, who

estimates that more than 90 percent of the firm's revenue can now be attributed to such monthly subscriptions.

Alternative billing of all stripes is becoming more popular, particularly given the economic climate — and client leverage — of the last couple of years. But observers say few firms are focusing on monthly flat fees to the extent that Smithline Jha does.

“I don't know of anybody that does it this way to the level that these folks are doing it,” said Thomas Clay, an East Coast legal consultant with Altman Weil who doesn't work with the firm. Clay says that out of all the

alternative billing tools, it's the fixed or flat fee that is taking off the quickest. "One of the biggest requirements of clients now, particularly of big ones, is certainty and predictability." That said, he does not expect subscriptions to catch on widely. "A lot of clients will say I'm not going to pay anything in January through March when there's nothing to do," Clay said. "These things only work if there are measurable amounts of work going on every month."

The pair of firm founders feel that their work — with its focus on IP licensing for software and Internet companies — is particularly suited to flat-fee arrangements because the work is steady and predictable.

Given the steps they go through to set each client's pricing at the outset, and the flexibility that both sides maintain in the month-to-month arrangement, they don't worry about clients taking advantage. "What if they stay with us one more month or one more year?" Smithline asks. "What if they refer another client?"

Earlier this year, executives at San Mateo cloud computing startup Appirio Inc. was looking for a way to cut legal costs. The big firm the company was using wasn't too interested in entertaining flat-fee billing at the time, said Jim Emerich, Appirio's chief financial officer (he declined to name the firm). So the company's work went to Smithline Jha, Emerich said, after a beauty contest that attracted four competitors.

The firm's approach is informed by its partners' years at both big firms and in corporate legal departments. Smithline, formerly general counsel of Marimba Inc., worked as an associate at Latham & Watkins and Gunderson Dettmer Stough Villeneuve Franklin & Hachigian. Jha, a former vice president of strategic transactions and associate general counsel for Ask Jeeves, was an associate at Cooley Godward. In 2004 they opened Smithline Jha.

At first, Smithline said, the firm found it was investing vast amounts of time in new clients at

the onset, getting to know their products, executives, engineers and sales force, much the way an in-house attorney gets to know his or her new company, but was writing many of those hours off. "It was intuitive to us that when you meet a new client, you need all this information," Smithline said. At the time, the partners' hourly rates ranged in the \$400s and \$500s.

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There was another problem: Dips and spikes in the volume of work led to occasional huge bills that scared clients. Jha said that was a particular problem with venture-backed companies, which make up more than half their practice.

So in early 2008, the firm started experimenting by putting a few longtime clients on a flat-fee subscription. They'd estimate what the client would spend with the firm in a year, and divide that by 12 to arrive at a monthly price. (Depending on the client, they say, a month can cost from \$6,000 to about \$30,000.)

They've since come up with a way to set a monthly price for new clients, too, by

negotiating based on what Smithline calls the exploratory month. At first, “You don't know enough about the client and they don't know enough about you.” They charge \$5,000 for that initial month, during which the firm does as much work as the client will give and learns how frequent and complex its deals are. Then, they negotiate a monthly figure.

“People think it's really complicated, but it can be a really quick and friendly discussion,” Jha said.

And if the client's number doesn't match the firm's, Smithline added, “It's not the end of the world; you find a number you can live with. You can revisit it.”

To keep it simple, there are no caps or floors, and neither side is bound legally for more than a month at a time. That way, either party can address major fluctuations in work by requesting an adjustment for the following month, Smithline said. He noted that most client rates are not adjusted more than once a year.

Invoices list the assignments and tasks, but not the time spent, and Smithline says the firm doesn't track time spent internally, either.

Software company BigFix has been working with Smithline Jha since February, paying by month from the start. General Counsel Tom Kennedy said he was looking for help with tech transactions when he was introduced to the firm by a former colleague of Smithline's. Charging a flat fee for repeat advice resonated with him, Kennedy said, and it's worked so well that he now asks other firms he's thinking about

working with to consider handling trial projects on a flat-fee instead of hourly basis.

Of course, Kennedy concedes that if he had any litigation, that would be more difficult to price flatly. “Patent litigation — that can be a rat hole.”

Both partners say bigger and public company clients have been slower to move into the monthly subscription arrangement, something they find understandable given that their billing and budgeting infrastructures are driven by the billable hour. “Some companies are still adjusting to the idea of this,” Jha said.

But almost all of Smithline Jha's venture-backed clients are using the subscription model now, and the firm's lawyers say it's removed some of their own frustrations as well. Under the billable-hour model, for instance, some clients tried to manage costs by waiting to engage lawyers — a practice that was especially common with venture-backed companies that didn't have their own legal department. But that could limit Smithline Jha's ability to foresee potential pitfalls in negotiations. “The client thought they'd reduce costs, but were making our job harder for us,” Smithline said.

Now clients tend to invite them to the deal table earlier, while terms are still being discussed, rather than bringing them in to review a ready-made contract. “They're not afraid to call anymore,” Jha said. “They didn't feel like the meter was running every time they talked to us. The net effect was we got so much closer to our clients.”