

### **I-3: Recover 100% of Online Research Costs**

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Cost recovery is but one piece of the larger law firm economic picture. There are two standard accepted methods of improving firm economics: maximize income and minimize expenses. Online research is usually considered a direct expense of doing business.

#### **I. Recovery is a management decision**

The firm belongs to the shareholders. The shareholders are ultimately responsible for what is and is not billed. Management staff, including librarians, is rightly responsible to the shareholders for monitoring and controlling law firm finances. Librarians are the online research stewards and must be actively involved in how much the firm uses, spends, and recovers for online research.

Cost recovery has been an issue of concern for some time. Postings on law-lib, library conference programs, articles in library publications, and vendor presentations attest to the growing interest in cost recovery.

Each firm must determine its own cost recovery goal. Some firms may seek to recover 100% of all online research costs. Others may seek to recover a smaller portion or no online research costs. It does appear from surveys, articles, and discussions that most law firms seek to recover about two-thirds to three-fourths of their online research costs. According to the ABA 2002 Legal Technology Resource Center Survey Report about 43% of firms bill clients at cost while less than 6% mark up (bill clients at cost plus premium). The same survey shows that nearly 22% incorporate the cost of online research into the attorney hourly billing rate while 16% do not bill clients for online legal research. A West survey among 102 AALL attendees in 2004 found that 90% of law firms attempt to recover legal research costs from Westlaw and Lexis. On average, those firms recover about 68% of their Westlaw/Lexis research costs.

Before deciding on your cost recovery goal, it will help to take an honest and complete look at the firm's actual online research costs – including both hard and soft costs. In addition to subscription fees, you may negotiate for content, manage passwords, provide training, purchase additional software and/or hardware, as well as use staff time for processing bills, obtaining missing client numbers, etc. Once you understand the costs, you can decide how much you want to recover.

Some questions that may arise as you determine how much you want to recover include:

- Do you bill the full retail price?
- Do you bill the discounted rate (if you have a "flat rate" agreement)?
- Do you bill any subscription fees (in addition to the regular retail price)?
- Do you allocate costs?

- Do you mark up (or mark down) costs?
- Do you bill for all database research?
- Do you bill for Internet research (not database specific)?
- Do you recover management costs?
- Do billing rates include some or all overhead costs?

There are three primary disbursement pricing methods: retail, discount, and allocated. Kingsley Martin's 2004 "White Paper Cost Recovery for Online Research" contains an excellent discussion of the pricing models realization rate factors.

"Cost-effective" research is only the first step. Most online research bills are complex. Go beyond the first step and educate attorneys and users on the actual "cost" of research. Most attorneys have never seen a Lexis or Westlaw bill or a PowerInvoice or Quickview printout. Show attorneys the actual PowerInvoice and Quickview printouts. Go over these line by line and explain every column and number. Show them an actual statement even if you don't review the hundreds of pages of details.

ABA Formal Opinion 93-379, December 6, 1993, Billing for Professional Fees, Disbursements and Other Expenses states ". . . the lawyer may recoup expenses reasonably incurred in connection with the client's matter for services performed in-house, such as . . . computer research . . . and other similar services, so long as the charge reasonably reflects the lawyer's actual cost for the services rendered. A lawyer may not charge a client more than her disbursements for services provided by third parties . . . except to the extent that the lawyer incurs costs additional to the direct cost of the third party services." The opinion is open to different interpretations. Each firm must review the opinion and determine their interpretation.

Prior to this opinion, many law firm libraries operated as a profit center and marked up the cost of computer assisted legal research. Since this opinion, practice varies although it appears that many firms bill at cost.

Once the cost recovery concept is solidified, it may require a better understanding of the firm's culture before execution of a cost recovery plan. Even though a solid cost recovery plan is critical to success, the execution of the plan may be even more crucial to the firm's bottom line. Execution requires both acceptance and good communication.

## **II. ID validation is necessary for successful cost recovery**

Most research services offer the ability to track online research activity by client-matter number. In the past two years, LexisNexis, Thomson, and ResearchAgent have all released ID validation software. According to Cindy Chick, the Thomson Elite Research Manager product is actually a licensed version of Lookup Precision, previously called Online Lookup. ERM integrates with the Elite accounting system. LexisNexis has a new Cost Recovery Manager product and ResearchAgent has several products to assist with client ID validation and cost recovery. The new generation of products appears to be quite sophisticated – not only do they provide ID validation for research services, but also the ability to track time and activity (similar to the time entry programs such as Time Matters, Carpe Diem, etc.). On the

other hand, these new cost recovery products require the involvement and support of a firm's technical staff as well as library and/or accounting staff. A firm must consider the cost of the "cost recovery" product as well as the ongoing cost of maintaining and using the product. However, I have yet to hear of a firm whose timekeepers will always, without exception, track and bill every online research session without an ID validation program in effect.

### **III. Client education and communication**

In the winter of 1990, Altman Weil Pensa completed a study on the productivity and quality of work product with computer assisted legal research. Based on the results of the study it was concluded that computer assisted research was less costly and less time-consuming than manual research on a relevant case basis, for identical research tasks. Firms can replicate this study and make their own determination as to the cost-effectiveness of online legal research. Librarians can offer billing seminars for firm clients, detailing the advantages of online research. Billing seminars for clients would be presented in partnership with attorneys and management.

The "Research Trail" and "History" can be used to justify charges to clients (and provide more detail on billing invoices).

### **IV. Managing information expenses through cost recovery best practices**

According to a Thomson West Law Librarian Relations MBA workshop on Law Firm Economics (February 2005) the four top best practices are:

- Attorney education and communication
- ID validation
- Client education and communication
- Team effort/Company buy in

Law firm partners assume primary leadership for setting and managing online cost recovery policies 26% of the time. Attorneys must become more involved for any cost recovery program to succeed. Attorneys and managers who understand the cost of online research and who have participated in a cost recovery CLE/discussion are best suited to shape the firm's cost recovery policy. If they have been part of the process they will buy in because it is *their* policy. One who has been intimately involved in the birth and growth of a policy has an investment in said policy. That attorney understands and cares about cost recovery. S/he ensures cost recovery success.

Attorney education is the top "best practice" in managing information expenses through cost recovery. Billing for online research is a logical part of an ethics continuing legal education class (as well as a research class). A cost recovery CLE works well as part of a series of online legal research CLEs for attorneys and paralegals. An argument can be made for incorporating the cost of research into every legal research CLE.

### **V. Outline for a "cost recovery" CLE**

1. Provide a background history of law firm's online legal research billing.
2. Review the ABA opinion (ABA Formal Opinion 93-379, December 6, 1993).

3. Present the current status of your firm's billing procedure/policy.
4. Look at the bills. Specifically, look at an individual attorney's online legal research expenses and a client's online legal research bill. Analyze the research and the resulting bill.
5. Present different scenarios. Have attorneys decide the correct course of action. Ask them to argue the other side.
6. Collect results. Present findings to upper management.

## **VI. Sample Scenarios for a Cost Recovery CLE**

**Scenario A:** For XYZ Service, we pay \$150 per month in subscription fees. There is a charge for each research transaction (either hourly or per search). We bill the client for the research transactions. We do not allocate any portion of the subscription fee to the clients.

**Question: Should clients be billed for a portion of the subscription fee? Why or why not?**

**Scenario B:** Most of our ABC Service research is covered by a "flat-rate" pricing agreement. The pricing agreement is confidential and may not be disclosed. If it costs the firm \$25 for research, the client is billed \$25.

A portion of our monthly fee consists of the cost of retrieving documents with a citation. This comes to \$100,000 annually. During the past year, the firm decided to allocate the cost of getting such documents to all clients for whom online research was performed. This is done in the accounting department by running a software program on the monthly electronic invoice. For example, if the cost of the client's research was \$25 the final bill to the client might show a charge of \$28.

**Question: Is it appropriate to allocate charges for retrieving documents with a citation to client research charges? Why or why not?**

**Scenario C:** Much of the computer-assisted research that is performed is for pro bono clients, charitable and civic activities, speech writing and presentations, marketing and business development, and for clients who simply refuse to pay research charges. The firm would like to recover some of that expense by allocating some of the nonbillable research to paying clients. Thus for example, the client above whose actual research cost was \$25 might be billed \$32.

**Question: Is it appropriate to allocate charges for nonbillable research above to paying clients? Why or why not?**

**Scenario D:** Clients want to know in advance how much research is going to cost. Therefore, after our best analysis the firm has decided to charge the following rates for online legal research:

\$5 per case pull

\$100 for a news search

\$50 for a company or financial search

\$200 for a public records search

\$160 for a caselaw search

\$90 for a trademark search

**Question: Is it appropriate to use a rate adjustment or surcharge when the actual cost may vary slightly? Why or why not?**

**Scenario E:** The firm can use an automatic process (allocation or rebalancing) to optimize the pricing of online research libraries within preset parameters. This will drive increased recovery by boosting prices on databases that clients have demonstrated a high level of willingness to pay for in the past while decreasing prices on databases that historically have had lower recovery. Such rebalancing constrains price increases and decreases within user-defined ranges to minimize excessive price swings. It balances to the actual online research costs so as not to add a premium over the firm's actual cost. This model yields a 20% increase in chargeback realization and offers the potential for the firm to increase recovery even further through aggressive manipulation of the algorithm, if we so desire. (The rebalancing model forces some client bills to increase while causing others to decrease.)

**Question: Do you agree to implement the rebalancing model? Why or why not?**

## **Conclusion**

After completing the cost recovery CLE and debating the merits of different methods of billing for online research, attorneys will reach a consensus on the appropriate cost recovery methods for their firm. With attorneys and management in agreement, a viable cost recovery plan can easily be developed and implemented.

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