Litigation Portfolio Risk Transfer

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Litigation cost is a heavy burden on Fortune 500 corporations. (See *Fortune 500: The Total Cost Of Litigation Estimated At One-Third Profits, The Metropolitan Corporate Counsel* February 2008, p. 28.) As one industry after another is targeted, corporations use their balance sheets to absorb the growing cost, only buying insurance against catastrophic litigation risk.

Traditional cost accounting hides the magnitude of self-insured litigation cost. The defense cost of the entire litigation portfolio is expensed annually to the law department, while the liability cost of individual cases is expensed to business units when incurred. Annual budgets are not an effective tool for managing litigation cost. *Ad hoc* case management dissipates corporate buying power. Hiring lawyers case by case and arbitraging different hourly rates creates the wrong incentives. The traditional approach rewards inefficiency and encourages delayed resolution, leading to higher total cost.

Litigation is best managed on a portfolio basis over three- to five-year periods. Total cost accounting determines the full cost of the litigation portfolio. (See *The First Step in Reducing Litigation Cost: Widen Focus to the Portfolio with a Litigation Scorecard, The Metropolitan Corporate Counsel* March 2008, p. 26). With a Litigation Scorecard, the General Counsel and law department can be compensated for reducing the total cost of the corporation's litigation portfolio. Outside counsel is also best compensated for delivering results measured against a Scorecard. Law firms are eager to manage portfolios of litigation. Portfolio management reduces total cost by rewarding efficiency and encouraging early resolution.

Transferring Risk To Law Firms

When eLawForum was founded in 2000, the idea of selecting counsel through professionally managed competitions was novel. Today competition is an increasingly accepted method of retaining counsel. While competition is critical to cost reduction, it must be combined with a portfolio approach to achieve measurable cost reduction and risk transfer.

Over the last dozen years, the average profits of the AmLaw 100 have grown from $50 million to $250 million. *[See Chart 1.]* The explosive growth of U.S. law firms has created the capacity to take risk. As a result, the best law firms will share risk on large portfolios.

Over the last six years, eLawForum has developed substantial expertise in structuring portfolio engagements to take advantage of this new risk-taking capacity. Unlike "beauty contests" among a short list of firms well known to the law department, eLawForum invites a sufficiently large number of highly-qualified law firms, incumbent and non-incumbent, to create a market for the portfolio. Firms compete to be national coordinating counsel ("NCC").

eLawForum harnesses law firm risk-taking capacity in two ways. Fixed fees comprise one-third to one-half of law firm compensation, transferring defense cost risk to outside counsel. The other one-half to two-thirds of the compensation is paid out of liability cost savings. Law firms share one-third of the reduction in the liability cost of the portfolio. Increasing performance-based compensation transfers more liability risk (as well as defense cost risk) to law firms. *(See Chart 2.)*

eLawForum's proprietary Fortune 500 database yields the ratio of liability cost to defense cost in important practice areas. The higher the ratio, the more potential exists for risk transfer. For example, in product liability cases, the liability to defense cost ratio is four dollars to one dollar.

Chart 1. Emergence of Risk-Taking Capacity

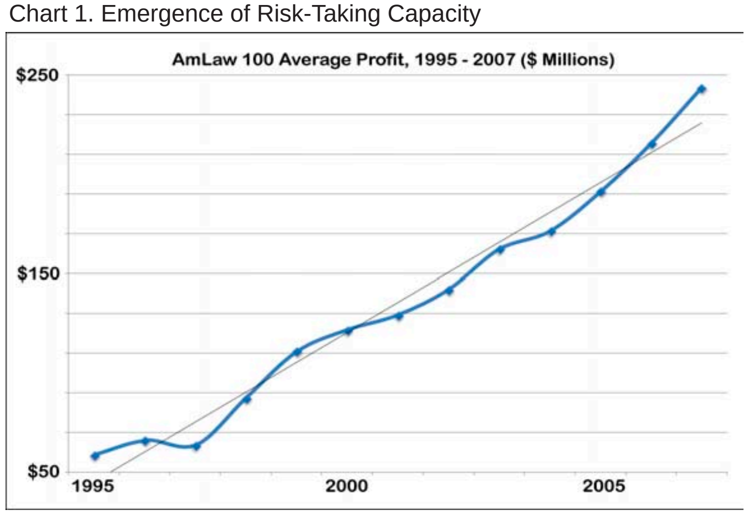
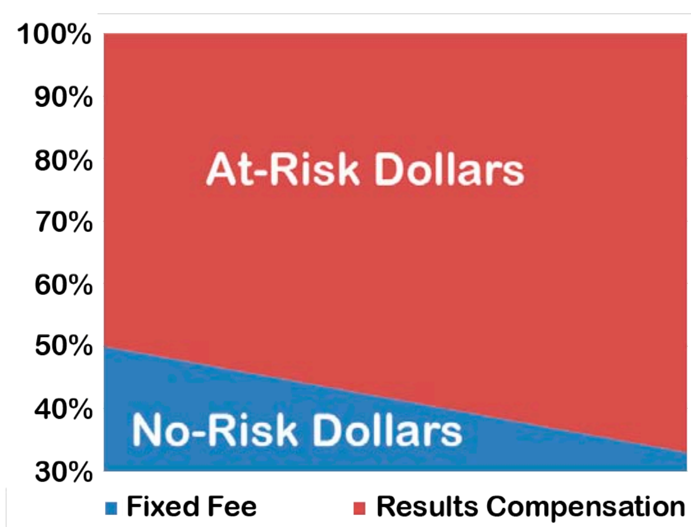


Chart 2. Increased Results Compensation Means More Risk Transfer



In employment cases, the ratio is one-to-one. Therefore, it is easier for a law firm to accept more risk transfer in a portfolio of product liability cases than an employment law portfolio. *(See Chart 3.)*

Portfolio management is the key to risk transfer, spreading both defense and liability cost risk over many cases. At-risk compensation transforms the relationship into a joint venture with the corporation. By reducing total cost, firms can earn more than under the billable hour.

Winning NCC are confident they can reduce defense cost and payout by resolving the majority of cases earlier at a discount. This does not mean a formulistic approach of settling every case. Each case must be priced realistically at the outset. If a case has merit, NCC make reasonable early settlement offers and convince plaintiffs that holding out will not increase the settlement. Going all the way to judgment when necessary establishes their credibility, reduces unrealistic demands and deters frivolous claims. NCC profit based on their skill and judgment rather than hours billed. Managing the portfolio rather than individual cases, NCC present a united front and eliminate the ability of plaintiffs' lawyers to exploit inconsistent positions.

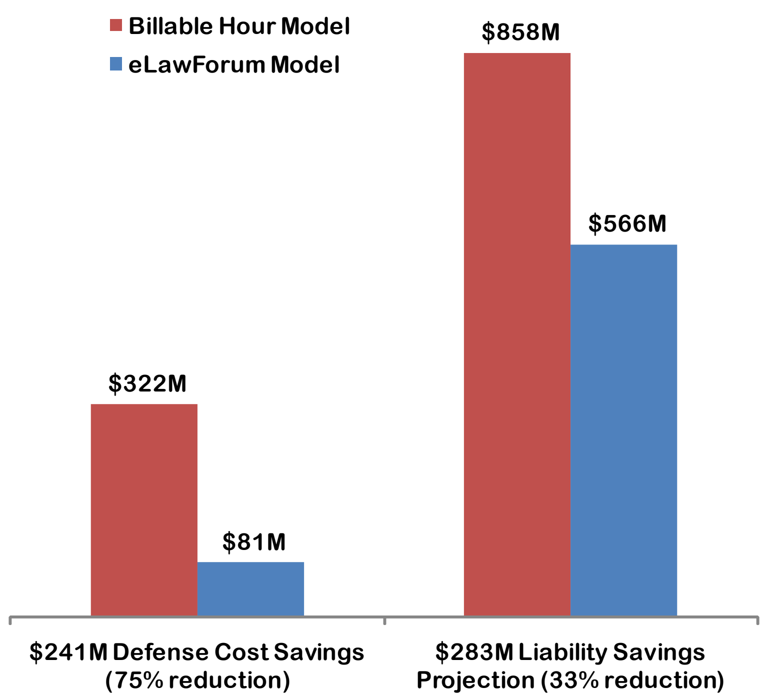
Client Savings

eLawForum's portfolio approach to managing litigation is phenomenally successful. eLawForum saved a quarter billion dollars in defense cost in six competitions across a wide variety of practice areas and industries. For three- to five-year periods, eLawForum's clients purchased 3,200 cases: 1,500 personal injury cases, 800 employment, labor and ERISA cases, 650 asbestos cases, 200 environmental cases, and 100 commercial cases. *(Chart 4.)* The six winning law firms based their fixed fees on the expectation of reducing aggregate liability cost by one-third.

***John B. Henry** is President of eLawForum. Further information about eLawForum can be found at www.elawforum.com.*

Chart 3. Liability To Defense Cost Ratios

Chart 4. eLawForum Client Savings



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