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Small and Midsize Law

A GUIDE TO OPERATING A PROFITABLE MODERN LAW FIRM

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Foreword

Lawyers dedicate three years of their lives, hundreds of thousands of dollars, and countless brain cells toward the goal of practicing their chosen profession. After that great sacrifice, and assuming they pass the bar, the state will authorize them to give legal advice for a living. The only thing they will be missing is any idea of how to make money doing it.

Of course, that is a slight exaggeration, but only a slight one. Yes, some young lawyers will find their way into established firms where associates, at least, can take their paychecks for granted much like their cellphones—vitally important things that they choose not to inquire about very much. But at some point in their careers, the vast majority of lawyers will be drawn by necessity, opportunity, or the lure of entrepreneurial challenge to a smaller environment, whether it be a 20-lawyer boutique or a true solo operation. At that scale, it quickly becomes clear—sometimes painfully so—that the lawyer is running a business as well as practicing law. They must learn, for the first time, exactly how that “cellphone” technology works. It is not someone else’s problem anymore; it is their problem. And thus, it is when joining smaller law firm environments—or considering it—that lawyers may realize they have a lot of learning to do.

Perhaps that is why you picked up this guide. It is certainly the reason we wrote it.

A Guide to Operating a Profitable Modern Law Firm is intended as a reader-friendly introduction to the practical side of running a solo, small, or midsize law firm. The topics covered inside are:

- The Basics of Running a Law Firm
- Equipping the Office with Legal Technology
- Developing Business and Marketing Your Practice
- Delivering Client Value
- Understanding Law Firm Finances
- Law Firm Economics
- Improving Law Firm Performance

If anyone feels daunted by topics with “economics” and “finance” in them, let us be clear: they are well within the power of any lawyer to master. (And certainly not as hard as learning the inner workings of mobile communications.)

Let us be clear about another point too: we applaud lawyers who recognize that their practices and firms are business operations and have made a decision to improve the performance of their businesses. With some effort toward that goal, you will very soon notice positive impacts that benefit your clients, your career satisfaction, and your own personal finances.

You will also have the only thing you were missing after you passed the bar.



1 | The Basics of Running a Law Firm

THE BASICS

1. For those running their own law firm, educational and informational resources are plentiful. It is essential to do your research—even on topics you might think you already understand.
2. Technology can be the great equalizer that helps a small or solo law practice compete.
3. The idea of a small or midsize law practice may not carry with it the glamour and grandeur of BigLaw, but there are many advantages to launching a small or solo law practice (see the sidebar in this chapter for more on that).

Whether a solo legal practice, a small law firm (2 – 20 attorneys), or a midsize firm (20 – 100 lawyers), running a law firm is not only not easy, it is often downright baffling. From practice specialization to workflow management, and from technology to accounting and beyond, running a law firm is far more than just hanging your shingle and sitting down to practice law. And while there is no playbook or user's guide for running a law firm, there are plenty of educational resources available to assist you. We hope that this guidebook becomes one of them, helping to demystify several of the more complex issues in law practice operations.

Running a law firm can be at once an enormously challenging endeavor and an incredibly rewarding one. How those challenges and rewards balance out in the end can be surprisingly dependent on the decisions you make early on. But with so many challenges coming at you at one time, how do you ensure that every decision you make is the right one? You do not. Mistakes are a part of every successful venture and for better or worse, there is no better learning tool than good old-fashioned experience.

That said, it is well worth relying on the advice of those who came before you. So, let us start with 12 relatively simple realities of running a law firm:

1. You need money

A law firm is a business, and businesses require a source of funding to keep them going. However noble or high-minded your intentions, there will be items you will have to buy and bills you will need to pay, including some you almost certainly have not considered. Unless you have a wealthy benefactor to bankroll you, the need for income can very quickly sidetrack the best-laid plans.

2. Dream big and carry a buttoned-up business plan

Regardless of your firm's source of funding, you need a business plan to assure the people you are hitting up for financing that you know enough about running a business to someday pay them back. Even if financing is not an issue for you, write a business plan anyway. The time, research, and discipline you devote to creating one will be enormously helpful in ensuring you know exactly where you are now and where you are headed in the future.

If you are a small firm, almost every state bar offers a Small Law Firm Startup Kit with online content that can help move you in the right direction. The state bar Law Office Management Assistance Program (LOMAP) is an invaluable resource that will take you through all the critical steps, from integrating your technology to assisting with trust accounting and from getting and keeping clients to managing your operations. It can also be useful to talk with people who are in the same boat. Join discussion groups and read blogs to pick up insights about what is working—and not working. At minimum your business plan should include the following sections:

- Executive summary
- Industry overview
- Market analysis
- Sales and marketing strategy
- Ownership plan
- Operating principles
- Financial plan

Once you have your business plan finalized, keep it handy and refer to it often. In the coming months and years, it will be well worth revisiting to see how well you stuck to your original plan, whether it needs to evolve, and whether your firm exceeded your initial expectations or failed to live up to your original goals. It may even provide ideas for how to get back on track if you have gone off the rails.

3. Begin with noble intentions (and a marketing plan)

Every law firm begins with the unlimited capacity to help people and make the world a better place. Unfortunately, they also start with the same capacity for failure. The fact is, the more thoroughly you plan for success in your endeavor, the more likely you are to achieve it. Or, on the other side of the coin, there is the old Benjamin Franklin quote, “By failing to prepare, you are preparing to fail.” So, in addition to your business plan, you should also create a marketing plan. Few attorneys have a ready-made client list when they first hang their shingle, so building one can be the most important, and potentially most difficult, aspect of operating the business. And yes, some clients may just happen by and seek your advice because they saw your sign, but in general, those are not the types of clients that are going to bring long-term financial stability to a law firm. That is why taking the time to create a marketing plan is so vital to your success.

We have to warn you, it takes time and discipline to create a successful marketing plan and there are educated decisions you will need to make along the way:

- Who you consider your target market – It is important to be realistic here about the type of client you are likely to be able to attract and the type of work they will hire you to do for them. It may be a good idea to define your target market in a limited scope and then revise it as you progress in the life of your firm.
- What tactics you will use to reach them – Does email marketing make sense for your firm? Digital? Public Relations? Advertising? The answer will likely be a mix of all of the above, and a law firm marketing professional can help you scope your marketing tactics.

- SWOT analysis – This is a strategic planning technique that will help your firm to identify its strengths, weaknesses, opportunities, and threats.
- Your competitive strengths and weaknesses.

The great news – for both solo and small practices as well as for midsize firms trying to take a bite of the BigLaw pie is that technology has done an incredible job of leveling the marketing playing field. Importantly, it has enabled them to compete in the marketing and advertising “arms race,” with Google Adwords, LinkedIn, and Facebook advertising affordable enough for virtually any attorney to utilize.

If you will be creating your own marketing plan, two potential places to start are the Small Business Association website or your local bar association. Another option is to hire marketing professionals with more time and expertise to devote to them.

4. Have an exit strategy

It may seem counterintuitive to create a plan to close a law firm, but as we all know, lawyers have myriad legal responsibilities, but absolutely no immunity to sickness, death, family problems, or any of the other human frailties that can get in the way of representing clients. Better to develop an exit plan now, rather than when you are in the middle of an emotional or financial crisis and incapable of making rational decisions.

Lawyers have a number of ethical considerations to prepare for when closing a law practice. They need to give opposing parties, clients, bar associations, and courts reasonable notice; and they need to destroy documents and advertising that could convey the appearance they are still doing business. It is also important to consider how you plan to:

- Settle open or unfinished accounts, particularly for clients whose flat-fee agreements may be interrupted.
- Form an assumption attorney relationship with a lawyer you trust to take over your cases.
- Purchase tail malpractice insurance for previous cases.
- Store and safeguard client files.
- Alert others that you are no longer in business, through letters, voicemail messages, or a web page.

5. Technology can be your best friend or your worst foe

Law firms have record-keeping responsibilities that would make most accountants cringe. And that is just the practice management side of the business. No matter your firm’s size, you really should not even attempt to operate a law practice without top-drawer practice management software. It does not have to be a big investment. Practice management solutions can make it easier for small firms by combining both practice management and billing and accounting management into an all-in-one package. Or you might consider a similar remotely-hosted solution that offers online matter management for a nominal monthly fee.

Whichever direction you go, practice management software gives you instant searchable access to every tiny detail of every case all together in one place, with no need for paper files. Make sure that your practice management software also helps you capture time that might otherwise go unbilled; integrates with your accounting and office programs; and gives you anytime, anywhere access to calendars, timekeeping functions, and documents from your phone or tablet.

Because of the complex accounting demands imposed on law firms, it is also a good idea to utilize accounting software created specifically for legal professionals or implement a highly specialized program that combines matter management and billing and accounting functions into one integrated package. If you get both your practice management and accounting programs right, you will save yourself a lot of time, not to mention an enormous amount of grief.

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6. Read everything available about the different types of business entities. Then consult an expert.

If you are already running your own firm, you have already determined the type of business entity that is right for your firm. If you are just starting out though, understand that a successful entrepreneur will consume enormous quantities of information deciding which type of business entity to operate, then spend at least an equal amount of time discussing the pros and cons of the different entities with a brilliant accountant and/or business lawyer. Depending on the type of firm you are starting and several other business factors, here are some of the most common options:

- **Sole Proprietorship** – If you are going solo, a sole proprietorship may be an option for you, but beware, this business structure requires the attorney to personally guarantee all business liabilities, which is generally too much risk for even the most confident lawyer to bear.
- **Partnerships** – For attorneys launching a small or mid-sized firm (e.g. two or more attorneys), a partnership is an option. A partnership is an association of two or more people, created to carry on a business for profit. Partners must determine up front how decisions will be made when conflict arises, particularly if they are evenly divided on the resolution. Notice that we said when conflict arises, not if. Count on it and plan for it.

There are two types of partnerships:

- Limited Partnership (LP)* – An LP is created by filing a certificate of formation with the secretary of state. An LP has two distinct groups of owners: general partners and limited partners. Limited partners are not personally responsible for the liabilities of the partnership. General partners are. As passive investors, limited partners do not have control of the partnership.
- Limited Liability Partnership (LLP)* – An LLP is created from a pre-existing partnership or limited partnership and is formed by registering with the Secretary of State. LLPs provide personal liability protection to the general partners, but the partners are still liable for their own malpractice.

7. When choosing a specialty, follow your heart... and the realities of the market

There is a place in this world for all types of people and all types of lawyers. You may well be one of the lucky ones who has a lifelong passion for the type of law you want to practice. If you do, by all means, devote every ounce of your energy to making a success of it. However, if you have not developed a particular affinity for one legal specialty or another, do not worry, you are in very good company. Many of the legal industry's most accomplished attorneys had no idea where they were headed before they stumbled into their specialty either. If you are not sure about your practice focus, it may be helpful to consider the following:

- Look at what is happening in your local market. Perhaps yours is an area where alternative energy companies are exploring, entrepreneurs are flourishing, or technology companies are clustering. If you are not sure about the prevailing direction of business where you live, start exploring the local chamber of commerce website. If you find there is nothing happening in your area that interests you as a lawyer, consider moving to an area that more closely matches the future you see for yourself.

- Look at the economic situation. Strong economies naturally lend themselves to certain types of specialties, including but not limited to real estate, intellectual property, and immigration. And even down economies offer plenty of opportunities (think bankruptcy or small-business start-up law). The trick is not selecting an area that is so ripe for the picking that every other lawyer in your area has already rushed into it before you.
- Honestly evaluate your own skills, talents, and life experiences. Think back to previous matters you have handled that made you feel especially excited by the challenge. Speak with other lawyers about their specialties. Think about what you do when you are not working and how those interests may be turned into a legal business opportunity. It is possible to build a very successful practice in a niche market.
- Do pro bono work in a field you think sounds interesting, or for a cause about which you are particularly passionate. It is a great way to help others while gaining valuable experience and exploring the types of cases that excite you enough to build a firm around.

8. Know what you are good at, and what you are better off hiring someone else to do

You are a lawyer and if one of your intentions is building a successful practice that produces revenue, you will need to start representing as many clients as you can, as quickly as you can. It is easy to fall into the trap of thinking you are saving money by doing non-legal tasks such as building your own website, doing your own accounting, or creating your own marketing plan. In reality, all you may be doing is taking time away from the one thing that other people will pay you to do—practicing law. Not to mention that you are probably not nearly as good at doing those other things as people who actually have that expertise, which will almost inevitably cost you money somewhere down the road. Even if you have a lot of spare time and few clients in the very beginning, it is never a good idea to fall into the do-it-yourself trap. That self-help time would be much better-spent networking. Instead, spend it attending social functions where you can introduce yourself to potential clients, or having lunch or dinner with better-established lawyers who may have more work than they can handle and would love to know someone they can trust for client referrals.

9. There are a number of ways to bill for your services

At one time not many years ago, practically the entire legal community turned up their noses at the very idea of alternative fee arrangements (AFAs). The general consensus among firms was that only clients who were being cheap would ask for set fees, so there probably wasn't any profit to be made from them anyway.

Oh, how times have changed. Early adopters of AFAs very quickly learned to thrive on them. Savvy law firms found ways to work more efficiently (many by leveraging fast-tracking practice management software and other advances in technology) and actually found they were very capable of making as much or more money under AFAs as under the traditional hourly billing model. They were able to do so without the hassles of tracking every minute of their day, and without clients scrutinizing every tenth of an hour billed. And as it turned out, clients who suggested fixed-fee arrangements, particularly the corporate ones, were not necessarily looking for the cheapest price—many were merely looking for more predictability in their pricing, so they could set or meet their budgets.

There remains nothing wrong with traditional hourly billing to this day, but it is important to be aware of the alternative options, and understand that today, AFAs are very much considered mainstream.

10. A good technology consultant or legal technologist is a relationship to be treasured

Finding the right technology and software for your firm is very much akin to finding the right spouse. It happens every day, but so do divorces and separations. That is what makes it so important to develop

a relationship with a trusted technology consultant or legal technologist who will take the time to get to know you and your firm's needs before making recommendations, as opposed to selling you on the package they are making the biggest commission from. The fact is, technology changes at a whirlwind pace, much faster than most lawyers are able to keep up with on their own. You do not necessarily want a consultant who is tied to one company, but you do want one with in-depth knowledge of the different hardware and software options that are specifically suited for legal firms. Many companies certify independent consultants who are experts in legal technology. These independent consultants not only have the technical background and practice management expertise to help you make the right choices; they are also expert in law firm processes and can help you manage your practice more efficiently by getting the most out of your practice management software.

11. You need malpractice insurance

No one goes into law intending to commit malpractice. But it does happen, even to the best law firms in the world. It also occasionally happens that a perfectly ridiculous claim of malpractice actually wins. Either way, you need malpractice insurance. We know the struggles of hanging a shingle and getting off to a good start financially. But it is because we are so aware of those struggles that we advocate so strongly for malpractice insurance. While it may seem expensive initially, it only takes one lawsuit, or even the threat of one, to put that cost into perspective. Cut back on the expensive office. Cut back on the high-dollar furnishings. But do not cut corners on malpractice insurance. If you never make use of it, good for you; you have accomplished something. If you do, thank goodness for it; it could very well save your practice from being sued out of existence.

12. Listen to your instincts in new-client meetings

Your gut can be smarter than your head. It is been said that there is nothing less valuable than services already rendered. In the field of law, as in many other service industries, that can mean one very frustrating outcome: not getting paid. And bad debt is just one of a very long list of ways things can go wrong in a client relationship. Bad client relationships can reveal themselves very early on in what you may dismiss as the most harmless ways: an inappropriate comment or look, a quick flash of unwarranted anger, even an attempt to be overly controlling about the way the case should be handled. Trust your instincts. Do not be afraid to respect those hairs standing up on the back of your neck. Instincts are a big part of what makes you a good lawyer and they can save you from taking on a client that you are likely to regret later. If you do not listen and all that happens is the loss of income from one rotten client, consider yourself lucky for the cheap education.

Of course, while your instincts can be a great barometer of client problems to come, it is also important to have a rigorous client-intake process for onboarding any new client. The process will not only help you uncover situations in which a particular client may have caused difficulties for a previous law firm, it is also absolutely essential for helping you avoid potential conflicts of interest that can lead to malpractice suits.

Whether you are a solo or a small or midsize law firm, hanging a shingle is a great option with great potential for good. Enjoy the ride, but do not let it run you over. There is no end to the number of decisions you will need to make as you get your new firm up and running. The fact is, it is easy to get overwhelmed, burned out, or even depressed that you can not control every decision. Do not.

Remember why you got into law and remind yourself of the incredible opportunities in front of you. Every person is different, every situation new, every firm unique. If you start out thinking you are going to do everything perfectly, you are already well on your way to failure. Give yourself a break when things are not going your way and learn from your mistakes. New opportunity is just around the corner. And if you find you need advice or opinions on making your firm a success, remember that your legal industry vendors can be a great resource. Their success depends on the success of the law firms they work with and they can be very helpful in answering questions or offering insights.

TOOLS OF THE TRADE: WHY SMALL LAW?

It is any law school graduate's dream: landing an associate position at a BigLaw firm straight out of school. While there is no doubt a certain level of prestige is associated with a big-name law firm, between a flurry of mergers and acquisitions and BigLaw partners jumping ship, job security is not necessarily a part of the package. And as many who are fortunate enough to secure a BigLaw job right out of law school will attest, it is not always all it is cracked up to be. Which is why after a few years in BigLaw, an increasing number of attorneys are fleeing to either work at or set up their own small or midsize shops.

There are many benefits that practicing at a smaller law firm can offer that their larger counterparts do not. Technology, as we have discussed, has leveled the playing field in recent years, giving smaller firms a real opportunity to compete with the deep-pockets of BigLaw. In addition, practicing at a smaller firm often affords enhanced work-life balance and flexibility that is typically unattainable at a large firm. If you are considering teaming up with industry peers to launch your own small firm, here are a few points that may permanently tip the scales in that direction.

- **Small law is lucrative** – Companies increasingly recognize the value of using smaller or midsize firms for their litigation needs. Some of the larger firms are cost-prohibitive to be able to handle some of their business litigation matters, so companies are looking more aggressively toward alternative options.

"For the most part, industry-wide changes have opened up opportunities for small and medium-sized firms," says Doug Pettit, shareholder and vice president of Pettit Kohn in San Diego. "In the last five to 10 years, mergers have evolved the marketplace and we are seeing a movement toward even bigger law firms. This opens up opportunities for smaller firms. The big firms have gotten almost too big, which allows small and medium firms to step in."

- **Greater efficiencies and a nimble culture** – Commonly, large corporate clients demand greater efficiency and the use of third-party intermediaries to provide their legal services (billing services, document management systems, etc.). Small firms have the ability to pivot more quickly than their larger counterparts.

"Fortunately, as a smaller firm, we are nimble and able to adjust our internal systems to accommodate these demands without too much cost or disruption," said Kellam Parks, managing member of Parks Zeigler in Virginia Beach, Virginia. Smaller firms may also be in a better position to accept contingency fees or alternative fee arrangements that larger firms might not want to commit to.

"There is a potential upside to the firm in handling contingency work and a number of attorneys here enjoy that kind of work," Pettit says. "For some of us, if we were at a larger firm, that might not be a possibility."

- **Interesting work** – Small law practices typically employ generalists who may have a specialty area or two, allowing them to work on several different types of cases, as opposed to large firms, where practice areas are narrower.

"There has been much more flexibility for each of our offices to spend more time in the areas they like rather than focusing on issues they may not have as much of an interest in," notes Rick Rumrell, a partner at Rumrell, McLeod & Brock PLLC in St. Augustine, Florida.

A closer-knit firm culture also means that lawyers at smaller firms may have additional opportunities to work in different areas, offering a chance for less experienced attorneys to work in new areas of the law and focus on matters they may want to specialize in.

- **Work-life balance** – Long hours and all-nighters are part of any attorney's career; there is usually no escaping it. In fact, thanks to the almighty billable hour, the BigLaw culture is known for encouraging overwork, and the solo practitioner has only one person to rely on to generate revenue—not always great for work-life balance. Small and midsize firms, by contrast, can offer the best of both worlds and provide that elusive work-life balance that much of the legal industry is missing. Work-life balance is generally more in focus and alternative fee arrangements may be more commonplace, putting less weight on billable time. Countless surveys show that more hours do not always equate to greater productivity.



2 | Equipping the Office with Legal Technology

THE BASICS

1. Legal-specific accounting, billing, and matter management software will save your firm countless headaches and will benefit your bottom line by saving time and keeping customers happy.
2. Legal practice management software is a must, but there is no one-size-fits-all solution. Get to intimately know your firm's needs and priorities before making a software investment. Maximize your investment by purchasing software you can grow into and by properly training staff.
3. Sharing sensitive documents and confidential information over email is a security concern for a variety of reasons, yet many attorneys still do it—or worse, put this information into free consumer file-sharing sites. Avoid getting into legal trouble by utilizing legal-specific file and workspace sharing software.
4. Have a disaster recovery plan for your data, and always plan for the worst-case scenario. Store your backups online.

Technology has completely transformed the practice of law over the last 20 years. That is no secret. What is less clear, however, is exactly how you and your firm can leverage it immediately to achieve your objectives. Our objective in this chapter is to bring a bit of actionable clarity to that topic.

Technology has created new opportunities for law firms of all sizes. For BigLaw firms, it has fostered opportunities for additional growth, and improvements to client service and cost-savings through new efficiencies and analytics. But despite their smaller scale, many would argue that technology has been an even bigger boon to smaller firms and even solo and duo practices. While the vast majority of these firms will never compete with BigLaw, innovations in legal technology have leveled the playing field considerably between small and midsize firms. Legal tech has become ubiquitous and scalable enough that nearly any legal practice can afford it, meaning firms in small and midsize law are now more likely to compete based on legal acumen and business savvy than by trying to outspend each other on resources.

The fact that technology solutions are so accessible also has a downside, however. The legal tech marketplace is overcrowded and those seeking simple answers on the best solution to buy for a given function are not likely to find them. That said, the following chapter will provide a solid foundation from which law firms can better position themselves to select the tools best-suited for their needs.

FINANCE SOFTWARE FOR LAW FIRMS

Despite an aggressive push toward alternative fee arrangements in recent years, the billable hour remains at the core of most law firms. But firms face a confusing array of options in managing their financial affairs. The objective is always the same: to save time and money by better managing time and money. But not all options are created equal.

Some firms choose to go with generic accounting software (think QuickBooks®), and while these products have many attractive features, they are still unable to easily handle many of the accounting issues unique to attorneys and law firms. Customizing these tools to effectively support these issues can be time-consuming, costly and still yield less-than-optimal results.

Still others can not seem to decide on a single comprehensive product and end up using more than one system to handle their accounting and billing tasks. The drawback of having separate systems for billing and accounting is that there is usually little to no integration between the two systems, so getting a complete view of your firm's financial picture requires separate (and time-consuming) reporting and analysis. Instead, legal-specific software is by far the best choice for firms. Aside from the paramount importance of avoiding legal trouble, there are many other benefits to using legal-specific financial software:

Lawyers trust accounts requirements

Legal-specific software is designed to deal with Interest on Lawyers Trust Accounts (IOLTA) requirements. It is possible for generic accounting programs to maintain IOLTA data, but reports are not automatically generated. Because creating and monitoring reports is time-consuming, these can be expensive to maintain manually.

Legal-specific systems are designed to prepare clear, detailed reports that will keep the auditors from the bar association very happy. An important safety feature typically included is the prevention of overdrafts on client trust accounts, as well as the option to make automatic funds transfers during the billing process.

Find a system that cleanly separates your general operating accounts from your clients' trust accounts. Look for features that show you where the money went, matter by matter, and will keep you apprised of funding levels.

As an extra safeguard, build accountability into your client communications. If you issue billings on a regular basis and a client has a trust account with you, consider including a statement of trust with your invoice. This statement can be a simple transaction list of all trust activity since the last bill to be sure that everyone has the same view.

Legal billing and payroll made simple

Whether your client is being charged on a flat fee, hourly, or contingency basis, legal-specific software is capable of producing any type of legal invoice that may be needed, whereas generic billing systems may not. It is also important to remember that invoice layout needs may also differ from client to client; for example, sometimes bills must be split between clients and insurance companies. Or, perhaps a consolidated bill showing charges across many matters is needed. Customization of bills and their appearance is easily achieved with legal-specific software. Multiple clients can be billed all at once or one at a time, as appropriate. While it is possible to muddle through manual invoice creation, keep in mind that clear, easy-to-understand and visually appealing invoices are conducive to prompt payment.

Law firm accounting can also be complicated, and many classic billing systems are not sophisticated enough to handle the many nuances that legal billing demands. The ability to take payments from clients and allocate fees

by biller, responsible attorney, area of practice or by some variation of these criteria is critical to a firm with more than one stakeholder. Whether staff is paid by the hour or based on the value of the matter at hand, legal-specific systems can produce the correct figures per your preference. Special compensation for things like client origination can also be included in these reports. Because law firms require targets for their staff to bill each year, reports that show the productivity of staff compared to target are important for performance reviews and for employee coaching. With legal-specific software, each employee's activities can be analyzed to see how many hours were worked, billed, and collected. Items like expenses and work-in-process are also factored in, providing a complete picture of an employee's productivity. Additionally, reports on trust accounts, operating and bank accounts, accounts receivable, and work-in-process can all be automatically generated. Legal-specific software is designed to track hard costs and the much more elusive soft costs that clients incur.

Security

There are two basic issues involved in security: granularity and mobility. Granularity refers to confidentiality issues. Which employees should have access to financial information about clients? The firm? Who can submit bills? Who has the authority to make payments on behalf of the firm? Who has access to information about the firm's bank accounts? All of these sensitive access issues can be established and monitored using legal-specific software.

Mobility is the other aspect of security. How will remote data entry be conducted? Will mobile phone access to confidential matters be permitted? By whom? Again, the right software solution can resolve these issues while monitoring all access activity and producing comprehensive reports.

The accountant's perspective

Many accounting firms are familiar with generic accounting software like QuickBooks and reluctant to encourage firms to use legal-specific accounting software. They are often unaware of the advantages to the law firm and themselves that a legal-specific solution provides. Fortunately, some legal-specific solutions can export data for accountants in the QuickBooks format as well as provide a free copy for accountants of law firms to use for the purposes of having a copy at their office to run reports.

The verdict

Generic financial management software simply does not meet the special needs of attorneys and law firms. Legal-specific solutions are abundant, scalable to firm size, and affordable. They also provide so much more in terms of practice management. There is no substitute for software designed with attorneys and law firms in mind.

MATTER MANAGEMENT SOFTWARE

Matter management solutions should be built to meet the specific needs of lawyers. Todd Scott, Vice President of Risk Management at Minnesota Lawyers Mutual Insurance Company, advises lawyers young and old about making good legal software decisions to make their lives easier. He notes that you can expect any good matter management system to provide the same basic capabilities:

- A calendar function that tracks billable time and simplifies scheduling
- Document management that provides shared access to the same files, which are stored in one place
- Contact lists that allow multiple users to share the same up-to-date information
- A shared database that makes it fast and easy to identify potential client conflicts

However, given that most matter management systems do these same basic things, how can you find the best solution for your firm? First, think about how you will do those things. Will you integrate the software with applications that you are already using, or do you want one comprehensive, stand-alone solution that does it all? Will you check for conflicts using Microsoft Outlook and your firm's database or research every outside source available? Do you want front-office and back-office solutions that talk to each other or to separate systems for security reasons? Consider all the ways you will use the system and build a wish list based on your specific needs before you go shopping.

A general office system probably is not your best bet

Prior to his career advising lawyers on malpractice insurance, Scott was an attorney himself. So, when he speaks about the necessity for legal-specific software, he speaks from experience on both sides of the malpractice interview.

“Many companies will simply not cover you unless you have good systems for docket control and conflict of interest,” he says. “You need to understand how important recordkeeping is. Business systems are created for people operating a business. If you are an attorney, each case is an active, open project. You need an enhanced reminder system with triggers and reminders to keep you on track. There is a difference between a statutory reminder and a holiday reminder, but Outlook handles them both the same.”

There are many other reasons for choosing legal-specific solutions. For example, clients are becoming more demanding and asking for special billing arrangements, and more attorneys are only taking clients on a retainer, forcing the use of trust accounts.

Define your own technology personality

It can be difficult to choose specific software systems to support your firm's legal needs. So where should a smart firm start? Evaluating yourself and how you (and other stakeholders) learn—even before you start sizing up different products—can save time because you will be more aware from the beginning about types of software that fit your technology personality.

Start by asking yourself a few questions:

- What is your approach to new software? Do you seek out training to learn as much as you can up front, or jump in and learn as you go? Or do you shy away from learning new types of software altogether?
- Do you generally look for the most sophisticated software package, or do you prefer simplicity?
- Are you willing to invest time up front to learn legal-specific software such as practice management if it can increase your productivity later?
- Would you prefer to invest in software up-front, or would you rather pay a small monthly fee to work in the cloud?
- Will you be handling trust accounts that put special demands on your legal software?

These are just a few of the things you will need to think about as you start to define your technology personality and needs.

Do not be afraid to ask for technology advice

It can be worthwhile to ask for advice from more established lawyers or to work with a consultant or legal technologist to help make the right decisions early on. Getting used to a new program takes time, and as important as your legal software can be to your success now and in the future, it is worth investing the time to get it right the first time around.

“Get a program you can grow into,” Scott says. “And go with products that are tried and true. Software products for lawyers come and go. You do not want to put 10,000 names in a new program only to have them go out of business down the road and you are stuck trying to transfer that data.”

Wherever you get technology advice, do not let anyone tell you there is any one right answer for every legal technology situation. They are not just wrong, they are likely trying to sell you something that is right for their pocketbook, not your practice.

No matter how stellar one particular type of software may be, it is not going to be right for every lawyer in every situation. That is why it is important to understand your own technology personality before committing to a program that may not be right for the way you prefer to work.

Insist on seeing all your options in action

Never buy software before you have taken it for a test drive. Most vendors will be happy to demo their software for you. Use this opportunity to “look under the hood.” Ask specific questions that will help you understand how the various product features will adapt to meet your requirements. Do not forget that a demo is a sales opportunity and that the person who is showing the software to you may have his or her own agenda. Keep the focus on what you need, not on what the vendor wants to sell you.

Get buy-in from the top down

The best consultant in the world can not help you unless everyone in your firm accepts and utilizes the new technology. Those at the top can be the worst offenders. You can win hearts and minds by demonstrating the return on investment if the software is used to its full potential and if training is readily available.

Training tips to maximize your software investment

Finding the right practice management solution is just part of the challenge for a small or midsize firm. The next step is mastering it—and that applies to everyone involved. The more you learn – and the faster you learn it – the sooner you will recoup your software investment. Recent studies have proven that people who attend a structured training class are 50 percent more productive during the introductory period of learning a new application than those who do not. Yet many businesses delay formal training or avoid it altogether. The reasons given range from “I can not afford it,” to “I do not have the time,” to “I can figure it out on my own.”

Software that is misused or underutilized can lead to billing snafus that impact cash flow; such issues can even lead to missed deadlines that result in fines or other sanctions, misfiled documents that impair client communications, and other headaches.

Many companies even have consultants that can either come to your office to assist or provide web-based training to further your staff’s knowledge of the application. The investment that you make in proper installation, staff training, and tweaking the implementation of the software you already have should come back to you tenfold.

MINIMIZE DOCKETING ERRORS

Where would lawyers be without calendaring, docketing, and “to-do” lists? Not where they should be. These tools are essential for keeping you on track and out of trouble—like missing a court appearance or a statute of limitations. Calendaring errors account for a significant portion of malpractice claims, especially in solo practices and small firms. Typically, these errors fall into four categories:

- Failure to know or ascertain a deadline correctly (not knowing a limitation, notice period, or filing deadline)
- Failure to calendar properly (knowing the deadline but not having it set in a calendar or tickler system)
- Failure to react to a calendar item (setting the deadline in a calendar or tickler system but missing it)
- Procrastination in the performance of services or lack of follow-up

A moving target

Court rules are complex and subject to frequent changes, such as new timing requirements and rules for calculating deadlines. Compounding the problem, court rules vary by region and, in many states, are county-specific. Varying rules can be a significant headache if your practice area covers multiple jurisdictions, each with their own separate set of requirements.

In spite of the risks, a surprising number of attorneys rely on getting a letter from the court to remind them of pending deadlines. Trusting email notices is an equally bad idea—think of what could happen if that email was unknowingly blocked by a spam filter or just missed in an overflowing inbox.

Set up a dual-entry system

The law states that attorneys are responsible for the ultimate accuracy of their calendaring activities, no matter what system they use. As a best practice for building in safeguards, many firms use a dual-entry system, such as keeping a paper calendar and an electronic calendar, or two electronic calendars. Entering information in two places increases your chances of compliance.

Establish docketing guidelines

A comprehensive docketing system helps reduce the chances of administrative errors. In writing, establish a centralized point of control in the firm and designate who will be accountable for the system, what steps will be followed for entering docket and calendar information, and how it will be made available to all members of the firm. No matter how comprehensive the system, if employees do not understand the system or use it, the system will not work.

Automate due dates and deadlines

An added advantage of electronic calendaring systems is that they often include court rules-based software, automatically adding technology safeguards into the mix. With a court rules database, you reduce the computation risks associated with human error.

Issue multiple alerts

Once your software-based calendaring system is in place, it can automatically generate alerts and reminders—flagging that an important date or deadline is approaching. The alerts can be automatically issued to multiple people in the firm, not just to the lawyer involved.

The bottom line

Your calendaring and docketing practices can impact your firm's liability insurance. Most insurance carriers will ask if you are using court rules-based calendaring, and some will not provide coverage if you are not. As a carrot instead of a stick, some insurance companies will give you a discount with proof of compliance.

EMAIL BEST PRACTICES FOR SMALL AND MIDSIZE FIRMS

You likely spend a significant portion of your day in your email inbox. All attorneys do. The inbox, however, is not (and was never intended to be) a digital “junk drawer” like the ones we all have in our kitchens at home. That is exactly what it will become though if certain best practices aren't followed—and that will lead to major problems for your practice.

Create a retention policy

Develop and implement a pre-established email retention policy that dictates what you need to save and how long you need to save it. Your retention policy will depend on your state bar rules and, in some cases, your practice area. In a typical litigation matter, you may need to keep related emails for five years, but if the case goes to appeal, that could extend to seven or more years. To learn the retention policies that apply to your practice, contact your state bar Law Office Management Assistance Program (LOMAP).

Once you get beyond the legal requirements, you will need to make sure all of your files are automatically backed up throughout the day. The good news here is that most modern email systems, including those in Google's Gmail family and Microsoft's Office 365, already do this for you, constantly backing up your data to the cloud.

Do not use your inbox as a storage closet

Most people create folders on the left panel in their inbox, where they file email and the attachments that come with them. Filing these attachments in an email folder along with the accompanying email message makes it difficult and time-consuming to find that attachment again when you need it. Instead, save attachments into document files as quickly as possible. This reduces email clutter and ensures that all of your files are well-organized and right where they need to be.

If you are using practice management software that connects to your email, as we have already suggested, the job of filing attachments is even easier. These systems will create copies of emails and attachments, and automatically save them to the appropriate files for document management. They will also automatically create a document record for email attachments.

Plan regular purges

To keep all those discarded emails from piling up in your firm's deleted files, schedule a regular time to "take out the trash." For example, make it a company-wide policy to delete or file anything that is been sitting there longer than 90 days. Gmail-based systems automate this task by automatically deleting any items in your trash that are more than 30 days old. If you do need to keep them for longer, this setting can also be turned off.

If you can not keep up with deleting and systematically filing email, ensure that you are at least archiving email so that your inbox stays at a reasonable size. Outlook lets you schedule archiving to any timetable that suits your schedule—every month or every 90 days, for example. It will then automatically execute the task at the appropriate time. If you need anything back, you can pull it from the archive.

TOOLS OF THE TRADE: WHY OUTLOOK IS NOT A REPLACEMENT FOR A MATTER MANAGEMENT SYSTEM

Many law firms use Outlook for contacts, calendar and email, however, law firms must manage many more types of information than a typical business. A matter is like the center of a wheel organizing all the information about a case around one central point. While Outlook lacks the flexibility to organize information in this way, much less tie together complex legal deadlines, parties to a case, case documents,

emails, phone calls, billing slips and so on, practice management systems accomplish this seamlessly. Practice management systems also give everyone a place to share the emails they send and receive on a specific case.



3 | Developing Business and Marketing Your Practice

THE BASICS

1. Your website is the centerpiece of your marketing efforts. Invest in making it polished, informative, and professional.
2. All marketing and business development efforts must start with strong content.
3. A digital marketing strategy can amplify your content, enabling you to target and more easily reach key audiences.

Some lawyers embrace online marketing and do it well, while others make mistakes that cost them clients, money and time—three things that any solo or small law practice can ill-afford to lose. Lawyers may be highly educated and trained to write for the courts where complex legal jargon is expected and well understood but writing strong marketing content in a way that will grab the attention of prospects, particularly in a highly saturated environment, is an entirely different animal. And this much is true: any modern, successful business development and marketing initiative will depend primarily on quality content.

YOUR FIRM'S WEBSITE: THE FIRST IMPRESSION

Your website will be the centerpiece of your online marketing efforts. The digital world we all live in requires firms, regardless of size, to come to embrace the importance of maintaining a professional and engaging digital presence. Your website tells the world who you are, what you do, how you do it well, and why a potential client should choose you to do it for them. If done right, the website will create a favorable impression of your practice while generating quality leads. If not, well, you are very likely to be fighting an uphill battle from the very beginning when it comes to attracting clients. A sloppy, unpolished website sends the same message to visitors that you would send to a potential client if you arrived for an in-person meeting wearing sweatpants.

When evaluating your firm's website, it is worth asking the question: Do non-attorneys find the website easy to navigate and understand? Are the calls-to-action compelling enough to bring in leads?

If a firm's website "checks all the boxes," is professionally designed and clearly describes its capabilities in terms of client needs, but still struggles to generate leads, there are several low-cost ways to provide a noticeable lift in response rate:

1. Your location and phone number should always be prominently displayed on your website. It should include a strong call-to-action that will motivate prospective clients to reach out, such as, "For a free consultation, contact us now." A simple addition like this can make a nervous client feel more comfortable with the idea of picking up the phone.
2. Calling a law firm can be intimidating, so your website should also include a clear, visually appealing contact form for visitors to complete so that you can contact them. This is about as easy as lead generation gets.
3. In the legal services business, in which clients tend to work very closely with their attorneys, personal relationships matter. Your personality matters and your clients and prospects need to be able to decide whether they can trust you with their critical legal and business challenges. Incorporating video on your website will help visitors get a better idea of who they might be hiring. Including at least one high-quality video on the site can help bring a firm to life for prospective clients and increase your search engine rankings, meaning that people will be able to find you and your firm more easily. Adding the video to YouTube, legal directories, and other video distribution sites can also extend that reach.

If these tactics do not adequately lift your response rates, then it may be time to invest in the expertise of professionals to audit your website and examine any data you may have regarding website traffic. Hiring a digital marketing expert to evaluate your website and help you identify and fix problems may feel like a big investment, but the money spent up front will pay for itself once your website actually does what it is designed to do: help you generate new business.

DIGITAL MARKETING FOR LAW FIRMS

Beyond your firm's website, both search engine marketing (SEM) and search engine optimization (SEO) are an important part of any digital marketing strategy. Prospective clients searching for legal assistance need to land on your firm's website, and SEM and SEO will help them do just that.

The term search engine marketing (SEM) generally refers to paid search marketing, a system by which businesses pay Google to display their ads in search results based on keywords searched. SEM also encompasses the ever-popular pay-per-click advertising (PPC), a digital advertising model in which advertisers are only charged when a user actually clicks on the ad. When employing one of these campaigns, it is important to select appropriate keywords that are geographically and topically suited to your firm. This can, at times, be a frustrating and complicated process, as other firms are also competing for the same keywords. A digital marketing expert can help you sort through the challenges and options.

Search engine optimization (SEO) is a bit different from SEM and PPC advertising. It refers to the process by which businesses earn a free spot in Google's search rankings by having the most relevant content for a certain keyword search. We said it before and we will say it again now, it all comes down to content. Assume for example, that you are an estate planning attorney in Florida. If a prospective client does a Google search for "estate planning Florida"—whether your law firm's name appears on the first page of Google's search results is determined by the keywords you include on your website and the context in which they are used.

Law firms should consider hiring an outside agency to help it establish comprehensive digital marketing strategies. Whatever your marketing goals are, experienced writers and digital marketers can help the firm communicate with prospective clients more efficiently and effectively and improve a firm's search engine ranking by incorporating keywords into the website copy that prospective clients are most likely to search. Keep in mind: a few examples of high-ranking websites within an agency's portfolio does not necessarily mean the agency is adept at SEM or SEO. Here are some questions to consider:

1. Are the high-ranking websites ranking for the "best" (most traffic/leads) keywords, or something else?

2. What is the firm doing to drive higher rankings: Is it a breadth of digital work or is it relying on only one tactic, thus putting the firm's eggs all in one basket?
3. Finally, and most importantly: Is the agency employing legitimate and ethical practices to affect ranking? A firm should remember that if it hires the agency, it is representing the law firm's brand: If the agency uses "black-hat" (questionable or unethical) tactics, the firm will have to deal with any repercussions that ensue.

Consider testing an SEM or SEO program on just one area of practice before investing your firm's money in all of them. From there, you can adjust and expand as needed, setting reasonable goals and establishing effective processes to track all inquiries generated from the campaign.

Finally, it is important to learn how success and ROI are measured in a digital marketing campaign. While you do not need to be an expert, you do need to arm yourself with a basic understanding in order to make educated decisions. It is worthwhile to learn the difference between organic and paid search, for example, as well as what defines impressions and conversions.

Do not expect immediate results

We all want immediate gratification and lawyers are not always known for being the most patient bunch. That said, law firm managers shouldn't be discouraged if their return on investment is not immediately obvious a few weeks after implementing digital marketing strategies. If you commit yourself to the program, you will eventually reap rewards. Results from SEM and SEO tactics take time, so patience is key—typically, this means a three-to-six month lead time, during which performance should be monitored and the program tweaked for optimal results.

Leaning-in to the power of reviews

Each month, millions of people visit online legal directory sites to find information and local lawyers who can help them confront a pressing legal concern. That is why a paid profile on one of these sites should be part of a small or solo law firm's marketing strategy. The more information you are able to include about your expertise, the better. In creating your listing, be sure to include information that is critical to prospective clients, such as years of experience, areas of practice, languages spoken, office hours, and payment options.

Ratings are similarly critical to driving new business. Before calling a law firm, many prospective clients now research lawyers beforehand: reading online ratings and reviews that include peer assessments, as well as client feedback regarding a lawyer's legal ability, cost, responsiveness, perceived value, ability to communicate and other factors. If your firm has established a favorable peer-based rating through a credible, third-party ratings resource like Avvo, Findlaw or LegalZoom (there are many reputable lawyer rating sites, but also plenty with less than stellar reputations), you should make sure that rating is featured prominently on your website and encourage satisfied clients to post reviews of your firm's performance on resolved matters. If your firm receives negative feedback through one or more of these sources, it should use that as an opportunity to assess weaknesses in its approach and address the concerns of potentially unhappy clients. Your firm will likely be reviewed whether or not it actively pursues these assessments, so it is best to engage and leverage positive reviews to the fullest, while also responding appropriately and constructively to negative reviews. This illustrates a commitment to client improvement and humanizes your practice—even in the eyes of a negative reviewer.

LEVERAGING SOCIAL MEDIA

Involvement in social media offers limitless opportunities to affordably find, connect, and engage with prospective clients. Though far later to the party than professionals in other industries, many lawyers now leverage social media as part of their marketing and business development strategies. A social media expert can help you decide which platforms you should prioritize (hint: LinkedIn should always figure prominently into that mix) and how to go about reaching the audiences they care about most. Once you do jump in, you should do so in the spirit of connecting with and helping others in the community by providing useful information and establishing yourself and your firm as a trusted resource. Overt sales pitches on social media are often perceived as unpalatable and should be avoided. As you establish trust and credibility with your audiences, business inquiries may come through social

media is simply staying top-of-mind for potential clients and business contacts. Jane Doe may have seen a LinkedIn post on a Tuesday and then contact the firm the following Friday. The firm would only know that Jane is a social media lead by asking her how she heard about the firm.

BLOGGING

In order to maintain a strong voice amongst the chatter of the competition, many attorneys have taken to developing and maintaining legal blogs. Blogs may be used to discuss industry news, legal issues, past cases, and current projects, and to position you and your firm as an expert on certain practice areas. There are, of course, ethical concerns to be taken into account when blogging. State bar associations have regulations that must be obeyed, but many bars also provide guidance on how to use blogs in compliance with their rules. Blogs are another excellent way to stay top-of-mind for your audience and to continually remind people of your firm's expertise.

So, let us jump right in and launch a blog. Not so fast. Before you get started, ask yourself the following questions:

- Do I have a unique idea or an original take on a particular area of law? With the explosion in popularity of legal blogs in recent years, there is a blog (likely more than one) for nearly every practice area you can imagine—and many that you probably have not. While that does not necessarily mean there is no room for you to also author a blog on a similar topic, you will need something that helps you stand apart from the crowd. Perhaps that is an interesting perspective on an often-discussed area. Or maybe it is a granular focus on a particular industry within a practice area. Whatever it is, try to find something that you can “own,” rather than becoming just another voice in the crowd.
- Failure to calendar properly (knowing the deadline but not having it set in a calendar or tickler system) Does my idea have longevity? As great as your blog idea might be, you do not want to launch a blog, only to run out of content after three months. Before moving forward, sit down and map out a content calendar for the first few months of your blog. Were you able to come up with enough ideas? If so, great. If not, maybe this topic is not the most appropriate one for you.
- Am I willing or able to commit to a regular blogging schedule? In order to build a following and be useful as a marketing and business development vehicle, you must provide your audience with new content on a regular basis. Nothing causes an audience to flee like a blog that sits dormant for months at a time. You should ideally post new content twice a week, but as you start out, consider one post per week the minimum threshold. If you can not commit to that now, it is best to save blogging until another time when you can.

If you do decide to move forward with a blog, you can amplify your work via social media. Social media is an excellent place to share new blog posts with your audience. By providing great, consistent content and engaging with your audience on social media platforms, you will attract additional followers and improve your SEO rankings.

CLIENT DEVELOPMENT

The growth of any law firm requires client development skills, which simply means skills by which firms attract prospective clients and manage ongoing relationships with existing clients. In order to generate new business, you need to not only make people aware of your firm's existence but provide information on your services and offer a reason for potential clients to choose your firm over another.

Though the concept of business development is fairly straightforward, many firms overlook the importance of maintaining relationships with existing clients in the pursuit of new ones. It is wise to remember that relationships do not end when a particular matter comes to a close, and that satisfied clients can be an invaluable source of future business either through additional cases of their own or from referrals. Your task is, therefore, twofold: attracting new business and maintaining or expanding existing relationships.

TOOLS OF THE TRADE: THE IMPORTANCE OF THE SWOT ANALYSIS

Your business plan lays out a strategy for successfully running your business and part of that plan will necessarily include a business development and marketing strategy. Without new business, you will have a hard time sustaining your firm for very long. But, of course, it is difficult to successfully develop new business if you do not know what your firm has. And that is where the tried and true SWOT analysis enters the picture. SWOT stands for “strengths, weaknesses, opportunities and threats” and it enables firms to honestly assess where they are and where they should be headed, both internally and externally. Strengths and weaknesses assess your firm’s internal characteristics, while opportunities and threats cover the external forces that may impact your business.

A SWOT analysis typically takes the form of an easy to read matrix and includes the following:

Strengths

- Financial strengths
- Client strengths and relationships
- Growth and professional development
- What are your internal firm strengths?

Weaknesses

- Financial liabilities
- Employee challenges
- Industry dependencies and regulatory risks
- What can your firm improve on?

Opportunities

- Economic and market exploration
- Technological advances
- Resources to use as external support
- What external factors can you leverage for opportunities?

Threats

- Economic risks to your firm
- Competitive concerns
- What external factors threaten your employees and your ability to keep them happy and productive?



4 | Delivering Client Value

THE BASICS

1. If you are measuring firm success by profitability alone, you are missing a huge and critical part of the picture. The delivery of true client value should be viewed as the foundation of your success.
2. There are limitless ways in which technology can help you to drive client value.
3. Obtaining candid client feedback and performing regular, realistic self-evaluations are vital to your understanding of what your clients want and how you can provide it to them.

There is a secret metric that clients will pay attorneys and law firms to improve. It is not a financial metric but performing better on it can vastly improve your law firm's profitability and growth. What is more, it is really not that big a secret if you listen to the clues your clients may already be dropping—trying to negotiate lower rates, taking a long time to pay your bills, or simply “forgetting” to pay bills altogether. The secret metric they all want you to measure and improve on? The value your firm provides to them as clients.

IMPROVED PROFITABILITY AND GROWTH THROUGH CLIENT-VALUE METRICS

Traditional law firm metrics tend to measure success through the eyes of the law firm, with the ultimate goal of improving profitability. Our chapter on law firm performance discusses this in great detail. According to a survey by the Managing Partner Forum, “fully 96% of managing partners said their firms had ‘excellent, highly informative’ financial metrics or ‘solid, reliable financial measures.’” No surprise there. Making money is essential to the long-term success of any business. Contrast that emphasis on tracking financial and other performance metrics with those same firms’ effort to measure “client satisfaction/relationship.” As it turns out, only nine percent of those surveyed firms gave themselves the same “excellent” or “solid” rating in measuring themselves from their clients’ perspectives.

This is a blind spot that can make all the difference for a law firm. Data from the BTI Consulting Group indicates that law firms rated by clients as providing “superior client service” tend to have higher overall growth (35%), rate premiums across all staff levels (19%), and higher profits (33%). How can you tell if your firm is providing the “superior client service” it takes to make your clients loyal to you if you are not regularly evaluating yourself from their perspective? You probably can not. If your firm stops at traditional profitability metrics, you are likely to miss what you need to take profitability and client growth further: client-value metrics.

VIEWING YOUR FIRM THROUGH THE CLIENTS' EYES

Asking the following questions can help your firm begin to view its service through the eyes of your clients:

- How do you manage client expectations? If you do not take time at the beginning of the relationship to understand what kind of outcome each client will consider a success (not having to pay alimony, settling a case for less than a million dollars, not-guilty verdict vs. probation vs. prison time, etc.), how will you know when you have achieved success from their point of view? While complete success may not always be achievable, it is important for the attorney to know what result might be considered acceptable and what would be viewed as a failure.
- How often do you communicate with your clients? Maintaining regular communication is an important element of the client-value equation and one that law firms far too often fall short of in their clients' minds. In fact, inadequate communication consistently ranks as the number-one bar association complaint from disaffected law firm clients.
- How often does your firm update clients about the status of their matters? Do you rush to pass on good news, but keep bad news quiet until the last possible moment? Do you answer client inquiries within a defined period, or are you sometimes guilty of ignoring calls or emails because "I am too busy working for my clients to hold their hands all the time?"

The above measures of value apply to virtually all client types, from large corporations to personal injury plaintiffs. And all of those clients can and do base their law firm's hiring decisions on the above issues. "Many clients assume a high level of legal competence in their encounters with attorneys," says Steven J. Best, Esq., veteran consultant to law firms and founding partner of Affinity Consulting Group. "After that, hiring priorities may vary according to the type of client. Individuals and small business-type clients may hire based primarily on gut feeling and levels of comfort with their first encounter, while corporate clients often prioritize hiring practices by maximizing results while minimizing costs when making the hire."

Even for corporate clients, cost is not everything. With dozens of competent law firms on their rosters at any one-time, other factors come into play. Those factors look remarkably similar to those used by individuals and small businesses: basic communication issues, for instance, or even small niceties that can make a firm more memorable to the people doing the hiring.

"With so much work available from law departments and so many firms vying for each piece, the difference between a first-choice firm and a second-thought firm can seem practically negligible," says Best. "Yet the difference in the amount and value of work sent to both types of firms can be enormous. Anything a firm can do to move up even one or two rungs on the law firm ladder can make a huge difference in the revenue that comes its way."

"Will a card or personal note to the right person make a difference? In all likelihood, no," he said. "But considering the infinitesimal time and money expenditure required for sending out that card or note, even a tiny chance can make the effort pay many times over."

WAYS TO IMPROVE CLIENT VALUE

Client portals

Most of us take for granted the ability to access our bank accounts online, on our own time. And many legal clients would appreciate and benefit from being able to do the same with their law firms, whether it is to check for the latest updates, read documents, respond to requests for information or other similar tasks, all from the comfort of their own computers.

Yet law firm adoption of secure client portals lags considerably behind that of financial institutions. Concerns about security play some role in that lack of adoption, as can the expense of setting up a portal and maintaining adequate data storage, but there are workarounds for both concerns. Beyond offering relief to busy clients who want the ability to update themselves at will, securely storing documents online can also make it easier to fulfill the legal requirements of sharing case information with opposing counsel. Everyone has their own sign-in information and passwords and it is easy to control exactly what each visitor can see once they establish their viewing credentials, so there is no loss of security controls once visitors have signed in to the portal.

Practice and financial management software

Beyond docketing, calendaring, maintaining contacts and keeping attorneys updated about what is coming up, practice management software helps attorneys maintain control over every case detail by storing files electronically. If a client calls, even out of the blue, even five years after matter resolution, you will never again have to utter everyone's most dreaded response, "I will have to call you back after I pull your file." Whether you are in the office or out on the courthouse steps, even files from years back are instantly searchable from whichever device is at hand at the moment.

Advanced financial management software, too, can help improve communication by making it easier to answer client questions about particular invoice charges. Financial management software, for instance, allows firm members to click on individual invoice items to review bills with the client without having to rely on the back office to pull paper copies.

Especially for clients sensitive to potential over-billing, taking even a short amount of time to call and answer questions after invoicing can go a long way toward easing concerns and strengthening bonds with the firm.

Client intake

Beyond docketing, calendaring, maintaining contacts and keeping attorneys updated about what is coming up, practice management software helps attorneys maintain control over every case detail by storing files electronically. If a client calls, even out of the blue, even five years after matter resolution, you will never again have to utter everyone's most dreaded response, "I will have to call you back after I pull your file." Whether you are in the office or out on the courthouse steps, even files from years back are instantly searchable from whichever device is at hand at the moment.

Craig Bayer, founder of Optiable, consults with law firms on streamlining processes to improve productivity. To him, it is important to build client-value measures into the client intake process.

"Smart firms establish certain client-intake processes from day one," Bayer said. "Whether it is conflict searches, sending out engagement letters for signature, setting matters up in practice and financial management software or any of those day-to-day tasks that absolutely have to be done, all are considered standard processes in law-firm client intake."

Law firms can take their performance to another level, Bayer says, by incorporating meaningful client communications into the client intake process as well. "It is so important for law firms to know exactly what each client expects from day one," he said. "That is not to say that client expectations are always going to be reasonable, but it is a starting point for opening the conversation. From there, it is the attorney's job to set realistic expectations for timing, budget, and final result – all within a range, of course – and help the client understand why there may be differences from what they initially thought."

Calendaring

Bayer also recommends that attorneys set up ticklers in their practice management software to alert them to follow through on client communication as promised. "Attorneys tend to think of ticklers only as a way of remembering specific docketing tasks to avoid malpractice," he said. "But there is no reason not to use the same system for prompting attorneys to contact their clients at regular intervals."

“You can set ticklers up in seconds in the practice management software you already use every day. They can be incredibly valuable for helping improve communications. And when you think about it, improving client communications can play an important role in avoiding malpractice, so it all comes full circle anyway.”

Self-evaluation

While client input provides the most important measure of how valuable your services are, you can not always count on every client to participate. Fortunately, there are metrics your practice can use to evaluate itself. That way, you still have ways of measuring success from the client’s point of view without having to rely entirely on client feedback.

One such measure is by maintaining statistics on your firm from the Client-Value Metrics Self-Evaluation. The self-evaluation creates a checklist/check-back system for making sure that firms always cover certain subject areas before contracts are signed. These include topics that many attorneys would prefer not to discuss, but absolutely should.

“Clients absolutely need to know whether they can afford your services and it is definitely in your firm’s interest to know whether they have the money to pay you,” Bayer says. “After all, your firm has a lot more to lose by getting involved with a client that can not afford you than the client does. The same attitude can also relate to how much time a matter will take. While attorneys’ hesitation in locking themselves into hard-and-fast estimates may be understandable, it can not be allowed to get in the way of open and honest conversation.”

While self-evaluation metrics may not be a perfect measure of how clients feel about your firm, they are a good way of making sure attorneys spend the time necessary to understand and discuss client expectations from day one, a giant leap forward for many firms. In addition, they allow attorneys to maintain a record of “successes” and “failures” on particular client communication metrics and see patterns they might otherwise miss in order to make improvements in the future.

Besides the client-value metrics self-evaluation, another way in which law firms can better understand the value they provide clients is by tracking repeat business and referral statistics, both of which can be easily noted/measured in your firm’s practice and financial management programs.

The higher the percentage of your business that comes from repeat business and referrals, the better you can assume you are performing on the measures that matter to your clients. It is also important to keep regular checks on reports such as aged accounts receivable from your financial management software as another potential measure of client-value perception.

While overdue client invoices are by no means always the result of dissatisfaction with the firm, they can be used as a “canary in the coal mine” alert that a client may not be 100 percent happy, either with your legal services or with charges out of line with their expectations.

Since good practice suggests that any type of business – law firms being no exception – should contact customers about overdue invoices anyway, a personal call from the attorney making sure everything is okay can be the perfect opening for that conversation.

Client-satisfaction surveys

Traditional client satisfaction surveys – whether by email, phone or through the mail – are a relatively easy, low-cost way to help measure how well your firm met the minimum standards your clients expect from you. While that is not exactly a ringing endorsement of such surveys, there are still firms that feel they have some value. Given their limitations, if your firm thinks it has something to gain from client satisfaction surveys, make sure any survey you send out is as short as possible to ensure you are not bothering busy clients.

Besides setting a very low bar for defining the value you provide as a law firm (satisfaction), be aware that what you learn from such surveys can be skewed by the fact that the most dissatisfied clients are the least likely to take time to fill them out. So, while your satisfaction scores may look good on paper, they will not always help you understand why your client list may be dwindling. That is not to say that learning what your clients think

you might be falling short of expectations. If clients want to help you, and that may depend on how helpful you were to them, your firm has the most to gain from a one-on-one client conversation, in person or on the phone, preferably with the attorney in charge or a firm principle.

While such conversations require more effort on the firm's part and may not always get the level of response you would prefer, every successful conversation can be a goldmine for discovering what the firm is doing well and what they should be doing better. Not to mention that many clients will appreciate the extra attention from important firm members.

Both phone calls and one-on-one meetings are far superior to emails for gauging how the client feels about the value the firm delivered. According to Bayer: "Emails are fine for gathering information and sending brief status updates, but they are horrible at gauging how your client is really feeling. It is too hard to pick up on emotions such as frustration from words on a computer screen.

"Make it a priority to call every so often just to ask how your client is doing," Bayer says. "And especially when you are trying to gather client-value metrics, phone calls are much less annoying than emails because they take real effort on the attorney's part and clients appreciate that."

What is more, for those matters that did go wrong in some way, nothing beats a sincere, personal apology from someone in a position of power.

One other way of learning more about how clients feel about your firm is with net promoter scores or NPS. NPS divides customers who respond to the question "How likely is it that you would recommend (your firm) to a friend or colleague" into one of three categories according to how they rate you:

- Promoters (score 9-10)
- Passives (score 7-8)
- Detractors (score 0-6)

Scores are determined by subtracting the percentage of detractor scores from the percentage of promoter scores, so the higher your firm's score, the better. Like other survey types, you will only gain information from clients who care enough to take time to rate your firm, but unlike most surveys, the NPS system offers two great advantages:

- There is only one question, so it can be completed in an instant.
- The NPS measurement goes past the "client satisfaction" metric that sets the bar so low for client value, to instead measure "client loyalty," which can be a much better predictor of return and referral business in the future.

TOOLS OF THE TRADE: CLIENT-VALUE METRICS SELF-EVALUATION

Timing Expectations for Matter Resolution: _____ (days/weeks/months)

- 0 No timing was discussed for resolving the matter
- 1 Timing range was discussed, but never agreed on with the client
- 2 The matter took longer to resolve than was discussed
- 3 The client was informed as soon as we realized the original timing couldn't be met and agreed to an extension
- 4 The matter was resolved by the agreed-on time range or sooner

Budget Expectations for Matter Resolution: \$ _____

- 0 No budget range was discussed for the matter
- 1 A budget was discussed, but no range was agreed on with the client
- 2 Firm invoice was more than the agreed-on range
- 3 The client was informed as soon as we realized the original budget couldn't be met and accepted the additional cost
- 4 The final invoice was the same as or less than the agreed-on range

Client Outcome Expectations: _____

- 0 No client outcome expectations were discussed
- 1 Client outcome preference was discussed, but no expectations were ever agreed on
- 2 Outcome expectations were missed
- 3 The client was notified as soon as we realized their expectations were unlikely to be met and agreed to accept the likely outcome
- 4 The client's outcome expectations were met or exceeded

Client Updates During Matter Resolution: _____

- 0 Client was not updated about their matter status until late in resolution
- 1 Client was updated about their matter status once during the work
- 2 Client was updated about matter status only when responding to their inquiries
- 3 Client was updated about their matter status infrequently
- 4 Client was updated about their matter status on a regular basis

Client Inquiries Responded to: _____

- 0 Firm failed to respond to at least one inquiry
- 1 Firm responded to all inquiries within one week
- 2 Firm responded to all inquiries within three days
- 3 Firm responded to all inquiries within two days
- 4 Firm responded to all inquiries within 24 hours



5 | Understanding Law Firm Finances

THE BASICS

1. Strong, consistent billing practices are critical to producing the revenue your firm needs to survive and thrive.
2. As a best practice, learn how to read your accounting reports line by line to fully understand and control your firm's financial health.
3. Maintaining your financial records month-by-month will save you time, money, and other hassles at year's end.
4. A good CPA is an absolute must for any law firm, regardless of size. Your CPA can save you countless headaches and dollars in tax liabilities.

Lawyers are expected to learn what they need to know about practicing law in law school. Looking at the course offerings from any law school you will find Criminal Law, Torts, Administrative Law, Business Law, Family Law and so on. What you will not find are courses on accounting or the financial administration of a law firm. This very important part of managing a law firm (regardless of size) is left for on-the-job training, yet it is one of the most critical components of a successful law practice.

THE BASICS OF LAW FIRM BILLING

There is only one way to have revenue flow into your law firm. You have to bill your clients for the legal work you are performing on their behalf. Many attorneys think of bills or statements as entirely financial transactions, when in fact, they should be thought of as detailed reports on matter progress – a way of communicating to your clients the value that you have provided. Whether you choose to bill your clients on an hourly basis or use one of the alternative fee arrangements (AFA) that have steadily grown in popularity, regularly billing your clients is both essential and need not be a complicated, multi-day process.

"If the thought of sending out regular statements seems overly complicated, it is time to take a hard look at upgrading both your processes and your software," Bayer says. "There are always better solutions out there, especially if you are still using the general business accounting software you bought when you first started out."

Creating bills or statements should not be a long process, not if you have very good legal-specific software that takes care of everything from timekeeping and billing to accounting and reporting in one fully integrated

program. With billing and accounting solutions, the entire process should never take more than a few hours at most. These tools will allow you to set up individual billers along with their standard and alternative hourly rates; accounts for each client that factor in hourly, flat fee or other billing arrangements; billing codes for different client matters; and standard language for describing the legal tasks being performed.

Regularly invoicing your clients, besides giving you an opportunity to report on your progress and communicate your value, also sets an expectation – much like a monthly electric bill or mortgage statement – that your bills need to be paid.

Now that we have hopefully convinced you of the importance of regularly billing your clients, let us now also convince you (hopefully very easily) that when it comes to your firm, anything worth doing is worth doing right. This particularly applies to billing—without billing you have no revenue.

Billing Best Practices

Proper billing practices compel the client to pay by making the invoice easy to read and ensuring that it communicates the value of the services rendered. To that end, all invoices should be written in language that the client understands, in line with your client fee agreement, and delivered in a timely manner while your work is still fresh in the client's mind. You should also be able to answer client questions about specific invoice items without hesitation. If your billing program does not allow you to drill down to answer questions on the spot, it is time to upgrade. Hedging on an immediate response may raise a red flag with your client: If you are unable to answer such a simple question about an invoice, your clients are likely to wonder if you are the right attorney to represent them.

Do not Be Your Client's Bank

It is also important to take a careful look at the legal fees and other costs you are advancing your clients – this is sometimes overlooked but often substantial and can significantly impact your practice's cash flow. Think about amending your standard engagement agreement and asking for retainers to pay client-specific costs from a trust account to decrease the amount you are financing on behalf of your clients.

Similarly, law firms must evaluate how much money they are leaving on the table by not managing their billings efficiently enough. Variations in billing practices inevitably results in inaccurate rates, lost billable hours, and late billing. For any law firm, managing and capturing more billable time will lead to higher profitability.

Let us take this oversimplified but illustrative example:

An attorney, a partner in a law firm, works on a simple case for a client. The firm's standard rate is \$300 an hour but the attorney has agreed to handle the case for \$200 an hour. He works 10 hours, which at the standard rate would net \$3,000. However, at the reduced rate, the net is only \$2,000.

Now the attorney gets busy with his other cases and is slow to bill the client. When he finally gets around to billing, he discounts the bill \$200 because he is so late in sending the invoice. When the client receives the bill, they point out a discrepancy, and the attorney knocks off another \$150 off the bill.

Total net on the case is now down to \$1,650 – that is just \$165 an hour, nearly half the standard rate of \$300 an hour. And that comes right out of the bottom line.

This points to the importance of better billing management. Unbilled time and other charges cost money, as working capital is needed to cover related expenses. Unbilled time can also accrue to higher levels than

perceived if not recorded properly. Without accurate records, a firm will never really have a clear picture of who is billing what, where errors may be taking place, and how to correct any problems.

While these types of discounts cost firms money, so too does inaccurate timekeeping. While accurate timekeeping is essential to accurate billing, it is not on the top of the list of priorities for an attorney on any matter. Timekeeping is – no pun intended – time-consuming, and that time is better spent on billable work.

Once again, this is where technology enters the picture. We will discuss the plethora of robust time and billing solutions available to firms of all sizes later on, but suffice to say, with all of the billing technology available, no firm should be tracking time on Excel spreadsheets or in other dated software not optimized for lawyers. These solutions make timekeeping a less tedious task, increasing the likelihood of it being performed by staff members. That increases billable hours and reduces the amount of client work performed but not captured. This, of course, increases firm profitability.

THE BASICS OF LAW FIRM BILLING

If you are running a law firm, you should better have at least a basic understanding of how to account for the money flowing into and out of your business. Even if you have someone who produces your financial statements (i.e., a bookkeeper, accountant, or firm administrator), as a stakeholder in a law firm this understanding is critical to knowing how their recommendations impact your business in the short- and long-term. Financial statements are the Rosetta Stones for law firms, as they hold all the answers about the financial health of your business—how much you have earned, how much you owe others, and how much you can spend:

The Balance Sheet

One easy way to remember the balance sheet and what is on it is by a simple formula: $\text{Assets} = \text{Liabilities} + \text{Owners' Equity}$. At any given moment, your balance sheet will provide you with an accurate snapshot of how much equity you have in the firm at that point in time. The balance sheet includes your bank balances; assets, such as the property and equipment you own; your law firm's debt, i.e., bank loans, lines of credit, and vendor payables; and an equity section that shows shareholder or partner capital as well as accumulated profits or losses.

The Income Statement

Your income statement displays revenue, expenses, and a profit or loss. Most law firms report on a cash basis and, therefore, the revenue that is reflected shows what has actually been received. If your firm is reporting on an accrual basis, your income statement will reflect what is earned but not necessarily received. Similarly, for expenses, if you are reporting on a cash basis, the expenses shown on the income statement reflect what you have actually paid for, whereas on an accrual basis, it would reflect expenses that have been incurred during that period, but not necessarily paid. Your firm's revenue minus the expenses result in a positive or negative number, i.e., profit or loss.

Cash Flow Statement

One common misconception in reading an income statement is that the profit at the end of the statement should be equal to the amount of cash in the bank, which shows up on your balance sheet. This is not true. Cash flow is not easy to see or manage using only a balance sheet or income statement. What you will not see on the balance sheet is a record of where your cash is going. That is why a cash flow statement is important; it combines the income statement and balance sheet and shows the detail of the activity by period.

Taxation Issues

If you have a large case and are spending money for things like filing fees, court recording fees, and an expert witness, you can not claim these as your law firm's expenses because they are considered reimbursable costs and the client will eventually pay you back. Essentially, you are loaning this money to your clients, which means these expenditures are not tax deductible. Loans to and from your firm do not show up on the income statement, they show up on your balance sheet.

As Jim Trippon, an expert tax CPA in Houston, points out: “Law firms and solo practice attorneys are a specialty area of corporate and partnership tax that requires skill in identifying when income becomes taxable. This can be a challenge due to the use of trust accounts for fees and litigation settlements, as well as the requirement of court approval of fees in some matters. Equally challenging can be the determination of what expense can be deducted during the case and when.”

Trippon has identified three typical trouble spots:

- **Constructive receipt** – Your fees are subject to tax when you have earned, billed, and can access them, even if you leave them on deposit in your law firm IOLTA account.
- **Advance expense payment** – This is a huge issue for plaintiff attorneys working on contingency. Often a successful case means a huge tax liability. Firms can moderate that liability by pre-paying law office expenses within certain IRS guidelines.
- **Employee benefit plans** – Tax can be reduced by employee benefit plan expenses. This includes pensions, healthcare plans, tuition reimbursement, and others. But be careful! Taxes will not be reduced if you violate any of the anti-discrimination rules, or affiliated group rules, the IRS places on benefit plans.

Work with your CPA or accountant to understand what reports you have available and identify the ones that help you make effective business decisions.

MAINTAINING FINANCIAL RECORDS

In many states, keeping your financial records up-to-date and accessible is really not an option. State bar associations mandate attorneys keep their trust accounts current and accurate. Firms must be able to prove they are properly managing their clients’ trust funds without commingling them with the firm’s general account, as doing so could lead to disbarment. Many bar associations perform random audits to test compliance. Handing over disorganized or incomplete files is not only embarrassing but risky.

Having your trust accounts audited is not the only reason why keeping clean books is important. Here are a few more:

- **Better money management and business decisions** – Printing periodic financial statements for the firm let you compare your firm’s current performance to previous periods in time. Having your bank reconciliations complete is one of the most critical criteria required before printing financial statements. Also, if your firm uses budgets to anticipate and plan for the future, having current financial statements tells you whether you are on track. And at year-end, being on top of your numbers can lead to a faster path to knowing what is available to determine the distribution of profit.
- **Better lending profile** – Knowing how much money you have puts you in a better position to borrow more. Messy books are red flags for lenders.
- **Lower accounting costs and hassles** – At the end of the year, all you have to do is close out the last month and send your statements off to your CPA. With everything in order, there is no last-minute rush or paying exorbitant fees for hour-intensive catch-up work.

The case for monthly close-outs

Closing a month means finalizing accounting entries for that month. Applicable journal entries are posted to the general ledger and the account balances are frozen to prevent further changes to the financial statements for that period. A month does not have to be closed immediately, though there are certainly advantages to reconciling and closing months on a regular basis.

For starters, do not discount the effort it takes to recall activity several months back that went into making up a balance. Some firms might be tempted to think “if we record activity throughout the year then it is no big deal to wait until the end of the year to do all of our bank reconciliations at one time.” This can be an overwhelming task, even if all your information is in order. And what if you find an error or something else, like a trust check that was recorded and billed as an entry and never cashed? Many issues could arise at the last minute and you would have little time to respond.

As a best practice, choose financial management software that has built-in processes for closing out months and protecting that data, ensuring that nothing can be changed once the month is reconciled and closed. (While freezing the month's data may seem overly final and nerve-wracking, it does not prevent you from accessing the data. It merely keeps entries from being backdated to a month that is been closed, protecting the integrity of your financial data.) Making it possible for someone to adjust the numbers after the fact will throw off your initial conclusions. Also, using different systems – one for billing and one for accounting – can lead to needless woes. Often this method requires double data entry, which is difficult to reconcile and prone to human error.

Move along in little bites, reconciling one month at a time. Catching things as you go along will keep you from having to scramble in January or February. And, since you have to keep up with your trust accounts every month, why not make it a practice to do your general accounting at the same time? Choose integrated billing and accounting software that will help you through the process.

Accurate end-of-year closeouts

When all data entry is complete for the previous year, it is time to close the books for the year. This process occurs in two stages: closing the individual months and closing the year itself.

The end-of-month process should occur throughout the fiscal year; we have covered that already. When the last month of the fiscal year is closed, the end-of-year can be run, zeroing out income and expense accounts while updating the capital/equity accounts for the new year. End-of-year should not be performed immediately when the calendar year ends. Often, year-end adjusting entries prescribed by the firm's accountant are required. Upon receiving these entries, you will need to back-date the adjustments to the last day of the fiscal year.

Before closing a year, the following conditions must be met:

- All bank accounts have been reconciled
- The accountant's adjusting entries have been received and entered
- Financial statements have been printed and compared
- The last month of the fiscal year has been closed

If a discrepancy exists between the general ledger bank balance and the bank journal, find the date when the two reports last balanced, then isolate the day the reports no longer reconcile. Run both reports for a period, compare the totals, then re-run the reports for half of the period. Repeat this process for the period half in which the totals do not match. Continue until you narrow down the discrepancy to a single day. An adjustment must be made on that date.

Here is a list of best practices that will help you prepare for – and properly close – the end of your fiscal year.

1. The last month of the fiscal year has been closed

- Running a backup month-by-month provides you with a record of your entries at the time of the backup and allows you to restore your system if you experience any issues in the end-of-year process.
- Check with your local bar association—external backup might not be regulated, but it is always a good idea.

- When you use an external backup program, verify that your files have indeed been backed up. Have your IT support person check on a regular basis, testing the validity of the backup by restoring.
- Whether you are using discs or tape, move your year-end backup files offsite, to a safety deposit box or other secure location.

2. Reconcile all financial reports and transactions, month to month

- Compare the statement you receive from your banking institution to reconcile bank accounts for the various months in the fiscal year.
- Submit financial statements to the firm's accountant to check for posting errors or reclassification changes.
- Make sure your billing journal reconciles with your general ledger. Basically, reconciling what is been billed and received and that it is properly recorded and reflected on your financial statements.
- Enter general ledger adjustments from your accountant dated the last day of the fiscal year.
- Use budgeting features from your financial software to analyze and prepare budgets and make adjustments for the following year.
- Close the last month of the fiscal year.
- Close the year.

3. Produce 1099 forms

- Make sure you have accounted for all of the expenses that the firm has incurred and paid to a vendor. Setting up your vendor with the right criteria will enable your accounting software to automatically create 1099s for vendors, including law firms you have hired during the year.
- Review your 1099 listings for the year and produce 1099 forms for all vendors by January 31 (U.S. only).

How to use your accountant at year end

It is customary to have your accountant review your firm's financial statements at the very beginning of the year-end process. One reason is to spot and correct classification errors – rent posted as telephone, for example. Another equally important reason is to take advantage of your accountant's expertise in finding reclassifications to help reduce your tax bill and to ensure compliance with all tax issues.

You might also consider meeting with your firm's accountant intermittently through the year, perhaps quarterly or even monthly if your goal is to take some of the chaos out of year-end, or to fully take advantage of your accountant's expertise without the pressure of year-end bearing down. Many firms spend dearly in added accounting costs each year because every piece of the year-end puzzle is pushed out to the frantic final weeks, days and even hours of the year-end procedure when rush charges can accumulate rapidly and leave your firm with an extra expense you never planned for in budgeting.

If you are well-prepared at end-of-year and have closed the books each month, your accountant charges likely will not be much different for end-of-year service than they have been for getting help with end-of-month closeouts. It is even possible you will save money over the year.

You are also more likely to have your accountant's full attention if you are not loading him or her down with everything at one time at the very last minute (never mind that your own attention span will be longer if you are not worried about every other detail still to be completed for year-end).

How to use your accountant at year end

To protect your firm from potential year-end hassles, it is important to collect 1099 vendor information at the very beginning of a relationship. Each vendor should complete and provide a W-9 form. Not only will it protect you from year-end hassles tracking down missing information, it also ensures that every vendor is properly set up in your firm's accounts payable software from the very beginning. That makes issuing 1099s push-button easy if you are using legal-specific programs like financial management software.

When producing vendor checks from anywhere inside your financial software, be sure to select the vendor from the vendor list rather than typing the entry individually. You will save yourself the hassle of having to consolidate vendors under different or misspelled names when you are creating 1099s at year-end while ensuring that checks written outside of accounts payable will be included in 1099 reporting.

The following are some stress-saving tips to keep in mind in connection with 1099s:

- If in doubt about whether you need to send a 1099 to a particular vendor or client, send a 1099.
- If your firm is reasonably certain that you are making a one-time payment to a vendor or client, you can save the end-of-year hassle by issuing and sending 1099s along with the check, no matter what time of year it is. Particularly in the case of a class-action lawsuit where the firm involves itself in sending out settlement checks to large numbers of plaintiffs, it will also save the firm an extra mailing later.
- Law firms come under special scrutiny by the IRS for 1099s and may face more complications than other types of businesses. On the recipients' end of client payouts, the IRS also singles out law firms for special consideration, requiring every company hiring lawyers to report those payments on 1099s.
- If your firm changed accounting software at some time during the current year, make sure you have complete vendor information from both programs before closing the books on the year's 1099s. You will also need to include payments from your prior system in the current calendar year.

The case for legal-specific financial software

Generic financial software is a life-saver for small businesses. It is intuitive. It is easy to use. And it is relatively inexpensive. Unless your small business happens to be a law firm. If you are using generic small-business software to manage the finances of a law firm, it is exactly the opposite of easy or inexpensive. And never more difficult or expensive than at year-end. Reconciliation is a great example. If you are using separate programs for billing and accounting, entering numbers into both is not only time-consuming, it can be the worst possible nightmare at year-end. Every double-entry throughout the year doubles your risk of human error bringing year-end to a dead-halt before you even get started.

With legal-specific programs, every step of your firm's financial organization is fully integrated – from billing to accounting to reporting and even analytics – so the numbers flow seamlessly from one step to the next. No double entry. No extra entry point for human error.

Generic small-business accounting programs also create problems for law firms because they are most often configured for businesses using the accrual basis of accounting. Unless the settings are customized (more lost time), all accounts receivable will be reflected in income and accounts payable in expenses.

Producing the correct reports for year-end can also be more difficult with generic software. Law firms are not like any other business in some of the specific reports that can help you get through end-of-year, and on to a more profitable year next year.

Perhaps most problematic for off-the-shelf software, though, is trust accounting. National and local bar association rules leave little room for error for law firms that handle their clients' money or other valuables in trust.

And there are several ways that generic programs – even those with trust plug-ins – do not adequately support your firm:

- Generalized accounting can not account for money or valuables in trust by matter, nor provide detail by matter number the way legal software can.
- Reconciling aspects related to trust are far more difficult with generalized software.
- Generic programs require that firms set up separate companies for trust accounts, complicating the 1099 process. That can mean having to create 1099 forms for trust vendors separately, or worse yet, neglecting to create and send trust 1099s at all.

Legal-specific programs will automatically prevent your firm from making errors that violate trust rules and can lead to sanctions.

TOOLS OF THE TRADE: HIDDEN ADVANTAGES OF MONTH-END CLOSE OUTS

Closing months in a timely manner creates several advantages for law firms, and not all of them are about making end-of-year less taxing:

- Users are prevented from backdating entries in previously reconciled months.
- Entries that have exceeded their allowable retention periods (stale checks) can be purged.
- Federal and state taxes are made easier to prepare in a timely, organized manner.
- Organized and accurate trust account records are mandated by your local bar association. Many bar associations perform random audits to test compliance.
- Bank reconciliations must be complete before your firm can print financial statements. Financial statements allow your practice to:
 - » Compare your firm's financial standing against budget.
 - » Determine what is available for-profit distribution.
 - » Present a better lending profile to your bank.
- Updated month-ends may also help your firm save on end-of-year accounting fees. At year-end, all you will have to do is close out the final month and send financial statements off to your accountant for adjustments. Once adjusting entries are made, the final month can be closed. With everything in order, there is no last-minute rush that can cost your firm excessive rush fees for time-intensive catch-up work.

MONTH-END CHECKLIST

This checklist provides general guidelines for the financial reports you will need to reference for end-of-month (and end-of-year) accounting. Check with your accountant for any additional recommended

or those that may be required by regional governing bodies:

- General Bank Journal (for each general bank account check register)
- Trust Bank Journal (for each trust bank account check register)
- Write-Up/Write-Down Journal (for costs that have been adjusted)
- Client Costs Journal
- Client Trust Listing
- Client Summary (detailed)
- General Journal
- Receivables by Client Report
- Sales Tax Journal (if applicable)
- Collections Report
- Revenue collected by required parameters (for partner compensation calculations)
- 1099 Listing
- All relevant Payroll reports cost your firm excessive rush fees for time-intensive catch-up work.

For firms using accounts payable, the following reports should also be used:

- Purchases Journal
- Payment Listing
- Payable Listing

Financial statements you will need:

- General Ledger
- Trial Balance
- Income Statement
- Balance Sheet

Best Practices:

- Produce separate general bank journals and/or trust bank journals for each affected bank account. A separate report should be present in any report group for each bank account.
- Two versions of the Client Summary should be included as part of month-end reporting procedures—one to display retainer balances, and the other to display totals for the firm.



6 | Law Firm Economics

THE BASICS

1. Attorneys do not need to raise their fees or work more hours to improve profitability.
2. It is critical to understand the “five gears” that impact law firm profitability and how they all work together.
3. Matter management, accounting, and billing software can improve profitability by streamlining processes, providing an accurate picture of the firm’s finances, and ensuring that all billable time is captured.

No matter the size of your law firm, as a firm stakeholder, you affect your firm’s profitability every day, with every move you make. Maybe more importantly, you affect it with every move you do not make, which is actually much better news than you may realize. Once you understand that you impact your firm’s financial picture even by doing nothing, it becomes easier to take positive action instead of sitting back and hoping good things happen.

Every equity partner within a firm can directly improve their firm’s profits without asking clients to pay higher fees or asking employees to work more hours. All that is required is a fine-tuning of three business metrics – realization, leverage, and margin – that dictate the economic picture of every law firm.

- **Realization** – Realization rate measures the percentage of a firm’s billed legal work that is collected. Any number of factors can affect a firm’s realization rate including how work is billed, how many months of work are waiting to be billed (that is, how quickly bills go out the door), and the average length of time between billing a client and receiving payment. When you can improve any of these factors; e.g., getting paid faster by sending bills out more efficiently, decreasing write-offs by staffing the right talent on a matter, or reducing delinquencies by putting a good collection process in place, you can bring more money into your firm. For every \$100,000 a year you bill, improving your realization rate by five percent means an extra \$5,000 in receipts for the firm. That is significant for a practice of any size.
- **Leverage** – The next business metric you can adjust is leverage, i.e., the extent to which you delegate work to associates or support staff. Many firms, regardless of practice area (and even solo practitioners with productive paralegals or other timekeepers), have found that a good strategy is to delegate as much work as possible to lower paid staff, providing more time for the experienced partners to seek more business and to work on existing client relationships. Giving your staff more challenging tasks will keep

them motivated and interested and make them feel like they are truly part of the team. And paying your associates less to do the same work as partners do will increase your profitability through leverage.

- **Margin** – In addition to improving realization and leverage, firms are also deeply affected by how they spend money. Finding ways of doing things more efficiently will help you cut costs, which in turn will increase your profit margin. Although it requires an up-front investment, technology is often a key to working more efficiently, and as a result, improving margins.

THE ECONOMICS OF SMALL AND MIDSIZE LAW

Think about the movement of gears in a well-oiled machine. While they are all working together toward a common purpose – driving the machine forward or backward – adjacent gears are actually moving in opposite directions. The same goes for the primary gears driving law firm profitability. Instead of the individual gears moving independently, they're all interdependent with each other. You can not move one gear without affecting the others, sometimes in the most unintended ways. So, it stands to reason that getting every gear moving in sync with the others is a process of constant adjusting, then analyzing the numbers after each adjustment to understand where to make the next tweak.

Before we get ahead of ourselves, though, let us start at the beginning: identifying the gears that make a law firm go. We have already defined three of them above. Small and midsize firms are impacted heavily by two additional factors, which deal with the usage of timekeepers. The full list of five “gears” is as follows:

- Production Value – The number of hours or fees timekeepers are expected to bill
- Utilization – The actual amount of billable time a timekeeper logs
- Realization – How much money a firm is paid compared to how much it bills
- Leverage – Generating revenue through the work of non-partners
- Margin – The difference between the money

Getting back to the interdependent movements of the five gears, let us look at how a singular focus on one of them – margins – can affect the total profitability picture of a firm, with possible unintended consequences. Specifically, we're going to consider a firm that has set out to improve its margins by cutting costs. There are a couple of obvious targets for such an initiative, either or both of which can set into motion the law of unintended consequences:

1. **Employee layoffs** – With a grim economic outlook in the Great Recession years after 2008, many firms worked fiercely to increase their profit margins by cutting costs. That meant layoffs for thousands of lawyers and cuts to benefit programs. As a result, short-term margins improved. But extreme cost-cutting is a temporary bandage, one that eventually has to be ripped off. And when it is, it generally reveals more painful challenges for the future. With a singular focus on cost-cutting, both leverage and margins end up taking a hit:
 - The layoffs, other departures, and stalled hiring left fewer employees for partners to leverage work from. Less work gets done, decreasing revenue.
 - Lower-level tasks have to be performed by higher-level employees at a higher cost, eventually eating into the profit margin cost-cutting was supposed to increase.

That is a painful result however you look at it. The effect can be even worse when firms slash costs by delaying technology investments.

2. **Technology cutbacks** – In an ideal world, firms looking to increase profitability in the face of layoffs would balance out the productivity loss by making smarter investments in technology, allowing the remaining employees to get more done in less time. But in their zeal to cut costs, some firms also brought technology spending to a grinding halt. The result? A one-two productivity hit that made it near impossible for firms

The moral of the story: Profit margin is important, but it is just one of five gears. If you are betting your firm's profitability entirely on cost-cutting, you will bring other profitability gears to a grinding halt.

Now let us consider the alternative: making small adjustments to individual gears one at a time with a longer-term goal of fine-tuning the entire profitability movement.

Production value: Creating a billable hour target for each timekeeper

From the time employees begin work at a law firm, they have billable hour targets on their backs. It is how they are expected to carry their weight in the firm and how partners measure the worth of each employee. But just billing the required number of hours does not answer the question of how long any given matter will take or how much it will cost to service the client.

Do you ever wonder if the amount you are charging for a particular matter or case is profitable? How many hours of partner time, associate and paralegal time, and admin time will it take to resolve the matter, and how many had to be written off? What about outside costs and expenses, which should include both the costs incurred to resolve the matter and some portion of the firm's overall costs? If you consistently estimate all the different factors correctly, you will net a profit. If you occasionally get it wrong, accept it and go through the reporting and analytics process to learn why. No one is right all the time. But successful firms learn from their mistakes, make adjustments and move forward. Less successful firms, on the other hand, may be less particular about tracking the profitability of individual jobs or even write off losses as the price of doing business, putting revenue on equal footing with profitability. While it may occasionally make sense to bring in less money on a matter, as a long-term business strategy, it is a better fit for running a charity.

Utilization: How much of your employees' time is billable?

Firms do not make money from the time their employees do not bill. So, unless you are dealing with rainmakers and partners, whose time may be better spent capturing new business, increasing timekeeper utilization can be a prime candidate for increasing profitability. But what about the non-billable tasks that are essential to firm performance? How can you convert the hours spent on those tasks to billable time?

You cannot manage what you can not measure, so you will need to start by requiring timekeepers to track both billable and non-billable time, which will help you divide non-billable tasks into two categories:

1. Non-billable tasks that should be delegated to admin employees, and
2. Non-billable tasks that require some timekeeper involvement

Reducing timekeeper hours from the first category is easy: Require timekeepers to hand off tasks such as making copies or chasing down files to admin staff. This may require a little bit more planning, but it pays off in the long run. For the second category – non-billable tasks that require timekeeper participation – your goal should be to reduce the time required to complete them. For instance, you may be able to make a one-time investment in technology that will reduce the time required for non-billable tasks. If so, it is likely to pay off in multiples over the lifetime of that investment.

Better document management through practice management software

Electronic file copies have been around since computers and word processing programs were adopted by law firms in the 1980s. So why are there still so many paper copies in file cabinets weighing law firms down? Why are there still firms not taking advantage of practice management technology to organize, search and retrieve documents electronically instead of hunting for the printed version?

Two good questions. But unfortunately, no good answers. In addition to keeping files organized for everyone in the firm to reference when needed, centralizing electronic documents in practice management software helps lawyers be more responsive to their clients. If a client calls with a question about an event six weeks ago – or even six years ago – any employee in your firm can respond on the spot, without the dreaded, "Let me call you back after I pull the file".

Having easy access to electronic files also makes timekeepers' workdays more productive, with less reliance on admin staff – so you can utilize their time more effectively in other ways, or perhaps even get by with fewer admins. Either way, better document management creates another potential bonus to your firm's bottom line.

Realization: How much of your firm's potential income actually reaches its potential?

Law firm economic survey models typically group law firms into four categories:

- The top 25% of law firms, which have the highest earnings per partner
- The bottom 25%, with the lowest earnings per partner
- And the middle 50%, divided into two groups

As a general rule, there are two reasons why the top performing law firms reach the top:

- They understand the value of what they do and bill accordingly.
- Their clients realize the value of what they do and pay accordingly.

However you look at it, it is worth taking the time to understand why your firm may be lower on the realization ladder than you deserve in spite of your hard work and sacrifice. There are a number of reasons your firm may not be realizing its potential. Here are just a few:

1. ***Poor billing practices*** – For some firms, it may be less about the amount of the bill than it is the bill itself. Make sure that every client bill is:
 - Written in plain English
 - In line with the fee agreement
 - Sent in a timely manner (when the matter is still fresh in your client's mind)
2. ***Poor client communications*** – Barring regular communication from their lawyers, the best way for clients to get their firm's attention is by holding legal bills hostage. One of the most efficient ways to improve communication is with client portals, which allow clients to access relevant files and messages at their convenience, even when your office is closed. For most clients, getting regular updates through portals is enough to reassure them that their matters are getting the attention they deserve.
3. ***Regular credit memos and write-downs*** – Understand the value of what you do and bill accordingly. Discounting your firm's work not only creates the expectation of more discounts; it devalues the importance of your work in your clients' minds.
4. ***Unrealistic expectations*** – Use your experience to realistically assess each client's matter in the beginning, but make sure they understand the difficulty of predicting outcomes. It should go without saying, but it will not: Never promise an outcome, no matter how open and shut the case may seem.

Having easy access to electronic files also makes timekeepers' workdays more productive, with less reliance on admin staff – so you can utilize their time more effectively in other ways, or perhaps even get by with fewer admins. Either way, better document management creates another potential bonus to your firm's bottom line.

Leverage: Working for profit vs. profiting from the work of others

There is an old saying that you have to have money to make money. We think it is truer to say that you have to spend money to make money. Leverage is one of the least-understood profitability gears because it requires just that: spending money on associates, other employees, and technology to make more money.

The fact is, the most profitable law firms are usually the most highly leveraged: Fewer partners with more associates, and often with a greater emphasis on increasing productivity through technology. Firms with more partners and fewer associates, on the other hand, almost inevitably generate less revenue and have more people taking slices out of that smaller pie.

PROFIT MARGIN: HIGH-VOLUME DISCOUNT STORE OR EXCLUSIVE SPECIALTY BOUTIQUE

It may seem counterintuitive, but your firm can make profitability gains by moving the profit margin gear in either of two opposite directions. Just consider the case of two highly successful companies: Walmart® and Tiffany & Co®. Walmart has created a successful business model on a low-margin, high-volume strategy; Tiffany profits from selling exclusive jewelry and accessories at high margins in low volumes.

The key to success is making a decision about which type of business you are going to be, then driving all your efforts in that direction. In general, being successful with a high-margin strategy requires unwavering attention to detail and service, while following a low-margin strategy requires having the systems and processes in place to get your product out quickly and efficiently, with a minimum of wasted time and effort.

Whichever strategy you are following in your law firm, there are certain ways to reduce expenses without hampering either productivity or client service:

- Use financial software with automated reporting and analytics to look for patterns of excessive spending.
- Get more work from fewer employees with software that helps improve productivity at the support staff and professional levels.
- Establish systems and controls to maximize reimbursement of client expenses.

ASSESSING TIMEKEEPER'S PRODUCTIVITY

Many law firms consider themselves profitable if they are able to pay all of their expenses and put money in their own pockets during the year. However, that is not the only measure of profitability. A successful law firm or lawyer understands how he or she is actually making money. A number in black at the bottom of an income statement does not mean you are seeing the entire picture.

Profitability is measured not just on the income statement, but by analyzing matter and timekeeper profitability. In order to control growth and increase bottom line profits, it is imperative to evaluate profit on a case-by-case basis or at a minimum by a particular type of law. How many hours were required to derive the fees generated? Not all cases are winners and it is important to understand which ones are worth pursuing and which ones are draining profits.

The same is true of timekeepers. Obviously in smaller firms where only principals do client work, it is easier to follow the productivity of the timekeepers. As firms grow and additional timekeepers are hired, it is important to be sure that each timekeeper is generating enough revenue to substantiate his or her employment. Are certain timekeepers entering a large number of billable hours that have to be reduced at the time of billing? The real success of a law firm or lawyer is the result of a strong understanding of the firm's total financial picture.

It is wise for law firms to develop an objective way to gauge and compare the profitability of individual producers, all the way from paralegals to partners. For obvious reasons, most firms attempt to measure individual profitability, but many end up including overhead expenses in their calculations, which puts lower-level timekeepers at a disadvantage in calculating their profitability contribution. The fact is, if a law firm generates sufficient revenue to cover overhead, there is no value gained in allocating overhead expenses to individual timekeepers.

It is preferable, instead, for law firms to determine each producer's profitability ratio using only his or her direct expenses. At the end of the year, any producer who generates revenue equal to or greater than twice his or her direct expenses are contributing to overhead, meaning that everyone in the firm is earning net income from that person's work.

What do we consider direct expenses? Just as it sounds, any benefits directly attributable to one producer, including all types of employer-provided insurance:

- Payroll and payroll taxes
- Insurance, including health, dental, vision, disability, long-term care, and other insurance regardless of tax deductible status
- Retirement
- Other benefits directly attributable to one timekeeper, such as education, travel, seminars, and any other expenses other than those attributable to overhead

For any firm that wants to make sure all of its producers are profitable, this is a great way to easily compare the entire firm without getting muddled into the whole “how do we allocate overhead” trap. It also helps overcome the often-incorrect ideas law firm partners develop as to who their strongest performers are.

Once the proof is in the numbers, even the most overlooked paralegal can prove his or her worth amongst the firm’s top producers. Reaching that two-to-one ratio may also mean that producer is worthy of a bonus, no matter how high or low on the organization chart.

TOOLS OF THE TRADE: CAPTURING MORE BILLABLE TIME WITH PRACTICE MANAGEMENT SOFTWARE

No one wakes up in the morning looking forward to keeping track of every minute of the day. But timekeeping is just one of many jobs that can be made dramatically easier and more efficient with legal-specific practice management software. Besides providing multiple ways to capture time – including on the go – look for software that reminds timekeepers of work performed, but not yet billed.

Some practice management solutions, for example, have features that help capture billable time that hasn't yet been recorded. If employees log phone calls or appointments on their calendars, or save email to a matter, for instance, Time Entry Advisor makes a note of that billable time, then sends out daily reminders of time that hasn't been recorded. From there, it is a simple matter of a few clicks on the timekeeper's part to record the time that would otherwise be lost. At \$300 an hour – a conservative estimate of a law firm's average billed rate across all timekeepers – capturing just thirty more minutes a day can put an additional \$37,500 per year in your firm's bank account. And that is just the increase in revenue from one timekeeper, so the savings keep multiplying by the number of billable employees you have. What is more, timekeeping is just one of the many ways the right practice management software can rev up the profitability machine.

THE ECONOMICS OF SOLOS

Many solo attorneys are convinced that either: 1) Money issues are beneath them, or 2) They're just not good with money and that somehow, everything will work itself out. Unfortunately, the attorneys in the first group often end up buried by the very money issues they feel are beneath them, and those in the second group find that their money troubles have "worked themselves out" by becoming large tax liabilities, burdensome loans, or other business-destroying financial problems. Do not fall into either of these traps.

The truth is, solo practitioners do not need an accounting degree to properly deal with their financial issues, but it is essential that you at least know the basics of your business. You should be reviewing the following financial reports on a regular basis:

- Profit and loss statement – Monthly
- Cash flow report – Weekly
- Aged accounts report – Weekly
- Balance sheet – At least quarterly

The good news is that the best legal accounting programs today make it extraordinarily easy to get a big-picture view of your firm's financial statements at just a glance and allow you to "drill down" on individual items to better understand the numbers behind the numbers. It is your responsibility as a firm owner to know enough to spot potential problems that could put you in danger of malpractice or even worse, put you out of commission as an attorney.

No one became a lawyer to get saddled down with small-business chores, but solo practitioners should make certain they are not focusing only on legal services to the exclusion of the business side of their practices. As a practice owner, it is simply too easy to wake up one day and discover that you are tens of thousands of dollars in debt without ever having seen it coming.

In addition to reviewing the above financial reports, here are a few management duties that solos should stay on top of:

- Know your realization rate. A good rule of thumb is that you should aim for a billing realization rate of 90% or higher.
- Do not let accounts receivable get beyond 30 days without a personal phone call to the client, followed by increasingly urgent dunning letters on a regular basis if payment is not forthcoming. If you have

after billing, you need to have a serious conversation with each one personally to determine if there is a problem. Reach agreement on a payment plan to bring the account current before ending the conversation.

- Develop a budget for your practice, then figure out what you need to do each day to meet that budget (given the number of potentially billable hours/days in the year).
- Know how much time you spend on initial consultations. Many attorneys perform such consultations free of charge, but keep in mind that attorneys give legal advice during these consultations, even if it is to say, "you do not really have a case here, so there is

nothing on which to take legal action." For those who feel they must provide free initial consultations, it is wise to limit them to a maximum of 30 minutes, after which the meter should start running.

- Make sure client bills are sent promptly, and that they are highly detailed and accurate so that your clients understand exactly what they're paying for.
- Understand which types of clients and cases are more profitable for you and start working toward attracting more of them to your firm.
- Maintain an annual plan.



7 | Improving Law Firm Performance

THE BASICS

1. Profitability, not revenues, is the best measure of law firm performance.
2. A business process improvement offers opportunities to improve law firm performance that every attorney can and should leverage.
3. When implemented appropriately, performance benchmarking and measurement are invaluable tools.

Let us be honest with ourselves for a moment. When all is said and done, we are practicing law for one primary reason – to make money. The underlying reasons for needing to run a profitable law firm may differ from lawyer-to-lawyer and firm-to-firm. Some are truly in it for the love of the work or view it as a noble means of helping those less fortunate. Some may be pressured into it by family expectation, while still others are driven purely by the prospect of earning a good living and supporting themselves or their family. Stripping these and other reasons away though, no matter an attorney's or firm's underlying reasons for existence, the universal truth is this: To accomplish their objectives, they must operate a profitable, stable legal practice. And in order to do that, they must perform.

Most law firms typically focus on revenues as a measure of a practice's performance and financial health. But there is a growing trend among law firms large and small to analyze profitability in order to measure business effectiveness. Profitability really is a better way to gauge a firm's financial position. In most areas of the country, law firms are ranked by revenues, so, it is not surprising that attorneys generally concentrate on increasing revenues. However, firms that rely only on revenues to define firm performance are overlooking critical information that significantly impacts the bottom line.

Profitability, not revenues, are the best bellwether of firm performance. Unfortunately, law firms continually find their profits squeezed by client price sensitivity and technology-enabled commoditization of legal services. So, while enhancing profitability should be priority-one for law firms, it is becoming more and more difficult to achieve. The most obvious way of growing profits, of course, is to develop new clients and grow existing business. If you are running a legal practice of any size, we assume you understand this and refer you back to our earlier business development and marketing chapter. Our focus here will be business process improvement – streamlining and adding efficiencies to key operational functions, which go directly to the bottom line.

THE BUSINESS PROCESS IMPROVEMENT

Let us consider two law firms that are mirror images of each other. Same size, same approach to business development, same practice focus, a very similar client base, similar record of success in client matters, and similar revenues. Yet one law firm consistently outperforms the other and is far more profitable. How is this possible? It is not a difficult answer, really. When all other factors are equal, the practice that is more operationally sound will always win. For that reason, even the smallest law practices are well-served to regularly take a close look at business process improvement.

While process improvement is a vast, all-encompassing category, we will focus on two of the opportunities most critical to small- and mid-sized law firms: billing and records management.

Records management

Records management has come a long way since the days not so long ago when documents were stuffed in file cabinets. Today, records management systems must account for both desktop and cloud-based documents, including:

How to use your accountant at year end

To protect your firm from potential year-end hassles, it is important to collect 1099 vendor information at the very beginning of a relationship. Each vendor should complete and provide a W-9 form. Not only will it protect you from year-end hassles tracking down missing information; it also ensures that every vendor is properly set up in your firm's accounts payable software from the very beginning. That makes issuing 1099s push-button easy if you are using legal-specific programs like financial management software.

When producing vendor checks from anywhere inside your financial software, be sure to select the vendor from the vendor list rather than typing the entry individually. You will save yourself the hassle of having to consolidate vendors under different or misspelled names when you are creating 1099s at year-end while ensuring that checks written outside of accounts payable will be included in 1099 reporting.

The following are some stress-saving tips to keep in mind in connection with 1099s:

- Emails
- Calendars
- Electronic documents, spreadsheets, and filings
- Timekeeping software
- Other proprietary and specialty software

That is not to mention whatever traditional paper documents still persist.

While we discussed records management solutions in greater depth in our technology chapter, it is important to note here that law firm size is no longer a barrier to effective and efficient records management. Affordable, scalable records management solutions now exist, and any legal practice would be foolish not to use one of them. That is because managing all of these records – even for one matter – can be time-consuming. A good deal of such record-keeping is non-billable time. Inaccurate records and missing data can mean billable time is overlooked or underbilled. And that affects profitability.

ULTIMATELY, It is ABOUT COLLECTIONS

We think we have provided plenty of sound guidance so far but here is the harsh truth. No matter how good your technology, no matter how good your business processes, no matter how great a lawyer you are, none of this will truly make your law practice profitable. Only one thing will. Your ability to collect on the work you perform.

One common experience for small and midsize law firms is the growing number of receivables. Usually, there are two reasons why bills do not get paid on time or at all. First, there might be something wrong with the bill itself.

Perhaps it is unclear or incorrect. Maybe it was sent too long after the work was performed or was not what the client expected. Second, the client may want to pay but is experiencing financial difficulty. For many firms, the result of this increasingly serious situation is refocusing the staff on collecting outstanding invoices, renegotiating or financing clients' accounts—impacting the firm's profitability. Here are some best practices that can help you avoid or resolve collection issues.

Build “payability” into your billing process

To ward off trouble at the onset, bill quickly – people will pay for a service that is fresh in their minds. And bill frequently – large bills received months or years after a matter began or at the conclusion of the engagement are more difficult to pay and often create client relationship problems. It is also a good idea to offer your clients flexible options, such as scheduled credit card payments to support more frequent billing.

Make inroads with your invoices

Choose a billing format that is easy to read. Keep your bills clear, informative and free of legal jargon. Be consistent and correct. While five different people may provide billing input, you want the end product to look like it came from a single source. Create and adhere to a list of standardized terms, abbreviations, naming conventions, etc. Anyone who enters data should spell check in the moment. Appoint a vigilant reviewer to check each bill before it goes out the door.

In addition to including the amount due, your itemized list of charges (whether based on an hourly rate or a fixed fee) should also clearly project the value you delivered to the client. Even if you haven't personally been in touch with them during the month of service, use your invoice to connect with the client, indicate what you have been doing gratis – such as the phone calls you have made on their behalf – and express your gratitude for their business.

Ask for the check

Unfortunately, flexible payment options and timely, well-crafted invoices are not always enough. When bills go unpaid in spite of your efforts, follow up with your clients to ask if something is wrong and how you can help. Based on numerous interviews with small and midsize law firms, the consensus is that a multi-touch collection process works best, i.e., a letter, then a telephone call, and perhaps an email with a note and a copy of the bill. The timing of each client touch should be structured into the process, as well as determining who the most appropriate staff member is to carry out each client touch.

BENCHMARK AND MEASURE PERFORMANCE

It is true for athletes and attorneys: measurement improves performance. You set your sights on the best and then continually compare and improve what you are doing to reach that pinnacle of success. This process is called benchmarking.

Benchmarking basics

Benchmarking reports are critical to helping law firms make informed decisions about increasing effectiveness and profitability. Collection realization metrics and reports list billing transactions that were completed during a year and compare the original value of the fees to what was ultimately collected. These reports can illustrate your lost opportunity, for example, by comparing your actual realization per your fee agreements versus what it could have been had you billed at your standard rate.

For a complete reporting system that gives you a 360-degree view of your financial position and prospects, look for reports that make it easy to understand these critical factors:

- How long it takes to convert a billable entry into a bill and how quickly that bill is collected. The older an hour is, the harder it is to collect.
- The life cycle of the bill – the number of days between the first day worked and the day the bill was paid.

- Important indicators that help you run your business on a day-to-day basis. These include work in progress, cash receipts, and comparisons of this information to another period in time, like last week, last month, or last year.
- The expenses of the staff who are working on the matter and other overhead expenses such as office space. The client you bill the most may not be your most profitable client.
- Hours worked by a timekeeper in comparison to target hours that you can use in conjunction with a staff leverage report to assign workloads.

Avoiding benchmarking traps

Performance measurement traps to avoid include:

- Measuring only against your own firm, which keeps you from gaining broader insights for productive change.
- Looking backward and making the same decisions year after year that lead to the same mistakes.
- Putting your faith in numbers without clearly understanding what those numbers mean.
- Gaming your metrics by over-emphasizing the importance of billable hours.
- Sticking to your numbers too long that it stifles your firm's potential for growth.

How can law firms avoid these traps? The best practice for productively gauging your firm's progress is to pick benchmarks that are relevant, timely, flexible, nonrestrictive and open to change. Comparing your firm's financials to firms that practice in the same region or areas of law will be helpful. You do not, however, need to stick with companies in a similar earnings category. Also, many industry studies indicate that law firm profitability is about the way you manage and leverage key business metrics – including margin – so do not base your benchmarks on billings alone.

Rigidly trying to match the firm's financials from this year to the last one is another common mistake that many firms make. Be flexible so that you can tweak your course along the way if a decision you made previously is not working now. Change your criteria as necessary and look for numbers that lead, rather than lag, the profits in your business.

Another way to assess your firm's performance is to ask your clients. But make sure you understand what the client feedback numbers are really saying. Performance measurements are not just about figures on a financial statement or billing report. Studies have shown that employee and client satisfaction scores can directly impact the profitability of a company. Firms collecting client feedback should remain cognizant that the way they obtain such information can affect the value of the data being collected. One way to encourage an honest response is to hire a third-party vendor to conduct the survey for you.

And while you want to optimize your employees' time, using performance metrics to measure your staff may invite unwanted gaming by them, such as padding their hours to meet expected billable goals. If you are going to set billable hour or fee targets for your lawyers, you also want to set metrics like realization rates that measure how much they collect versus how much they billed, as well as measurements for soft skills like respect for and mentoring of colleagues, excellent client service, integrity, and community service.

Perhaps the stickiest trap of all is complacency. Do not be afraid to grow. Actively benchmark your firm's performance to others and use that information to chart an aggressive plan for increased success. If you are stuck in survival mode, consider taking your partners to an offsite retreat with a law firm expert who will help you develop a plan to higher profitability.

TOOLS OF THE TRADE: THE VALUE OF PERFORMANCE ANALYTICS

If you are running a law firm of any size—even a solo shop—you already have everything you need to analyze firm performance at your disposal. That is the good news. The bad news? It is likely spread out over several separate software platforms, databases, and spreadsheets. Sure, you can analyze cash flow, revenue and profitability from your accounting software. And you can analyze attorney and client billings and attorney utilization from your billing platform. But getting a solid picture of these and other metrics will require you to navigate different systems with different interfaces and click through various screens just to get to the data that you want to see.

It is far more efficient to create a single database—it can even be a simple spreadsheet or Google doc, that you set up to track your firm's key performance metrics over time. These documents can be updated each week or at the close of each month to help you identify historical trends that will enable you to run your firm more effectively. Alternatively, your firm may choose to invest in robust reporting systems that bring all KPIs (key performance indicators) under the same view. But what KPIs should you be tracking for your firm? Besides the obvious revenue, profitability, billings and

utilization, consider these lesser-known but equally important metrics:

- **Lockup** – The combined time it takes your firm to bill and collect on client's invoices.
- **Billable Hours per Full-Time Equivalent Timekeeper** – How many billable hours are worked per full-time theoretical lawyer. This KPI can illustrate a law firm's capacity or lack thereof.
- **Leverage** – The ratio of associates to partners, which is key to maintaining firm profitability.
- **Client growth rate** – The ratio of clients the firm handled in its first few months versus the number of active current clients.
- **Business development ratio** – The ratio of the business development spends for the year versus total fees billed during the year.

ABOUT PCLAW | TIME MATTERS™

“Dedicated to you in the past, here for you now, committed to you in the future.”

PCLaw | Time Matters™ LLC, a joint venture between LexisNexis® and LEAP Legal Software, is a global provider of practice management software solutions for law firms. For more than two decades, our practice management solutions have been used by lawyers to make better business decisions, improve profitability, and enhance client relationships.

PCLaw® and Time Matters® technology has been developed and refined to meet the needs of law firms. Whether you are looking to earn more, work more efficiently or spend more time on practicing law, PCLaw | Time Matters™ has the practice management solutions and resources to support your personal success and your firm's performance.

With our people, products, and partners, we are dedicated to innovating the business of law.

PCLAW

PCLaw is an all-in-one billing, accounting, and matter management solution for small to mid-size law firms. PCLaw allows firms to manage their finances, client information, billing and timekeeping in a secure, easy-to-use, central location, giving attorneys the ability to focus on serving their clients.

TIME MATTERS

Time Matters is an adaptable case, client, and document management solution that helps foster collaboration on matters, streamlined internal processes and increased profitability allowing attorneys to have more available billable hours and increased efficiency.

To learn more about PCLaw | Time Matters™,
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