



ATTORNEY'S REPORT

REALIZATION MATTERS

Collecting Your Fee is Still the Key

Law firm realization rates are hitting historic lows. In fact, Georgetown Law School's Center for the Study of the Legal Profession suggests realization rates may have dropped to an unprecedented 85 percent. That means for every dollar billed, some firms are collecting only 85 cents.

Firms have historically aimed for a realization rate of 90 to 95 percent or better. If your firm is not recording and collecting what it is owed, it may be time to give this key performance measure some additional scrutiny.

Who's Not Paying?

When evaluating realization, it's critical to take a hard look at both billing realization and collections realization.

- **Billing Realization:** Billing realization is the percentage of time billed to the time recorded. Or, put another way, billing realization compares what is actually billed to a client to what could have been billed. If billing realization is low, too much time is being written down or written off. For example, if an associate records eight hours of billable time but the relationship attorney deems that only six of those eight hours should be billed, billing realization falls to 75 percent.
- **Collections Realization:** Collections realization reflects the percent of time that clients were billed to what they actually paid. In a perfect world, collections realization would equal 100 percent, meaning your firm collects everything it bills each month. Unpaid bills — whether they are classified as post-facto discounts, write-offs or bad debts — ultimately reflect lost income that could have gone to your bottom line.

The Truth Behind the Numbers

James D. Cotterman, a principal of the legal management consultancy Altman Weil, Inc., notes in a 2012 article that when realization rates start to slip, the problem can usually be traced to one of several common areas:

- **Under-reporting of time** — Less-experienced attorneys have a tendency to flinch at the number of hours it took them to complete a task, chalking it up to their “learning

curve.” They may then balk at recording the entire amount. Sloppy time-capture habits — such as waiting until the end of the day (or longer) to record time — can also result in fewer billable hours being recorded than were actually worked.

- **Inefficiencies** — Perhaps the firm is using ineffective procedures to do the work, or the responsible time biller isn't as familiar with the area of law as he or she should be — or both.
- **Write-downs** — When it comes time to bill, lawyers may fear that the client will not see the value of the work done and balk at paying the full amount. So they write off or discount chunks of time.
- **Client adjustments** — Aggressive and/or complicated billing often results in increased write-offs and discounts. Here, clients may push back on a bill that is higher than expected or contains confusing pricing variations (e.g., different billing rates for various employees, functions and projects that result in a client being charged different rates for similar matters).

Time to Tighten Up

The good news is that realization is an area that can yield tremendous results — simply by tightening up billing practices. Consider these eight tips:

1. **Ensure accurate timekeeping.** An invoice is only as accurate as the timekeeping it reflects. Philosophically, teach all timekeepers to value their time and record it accurately. Follow up with formal training programs for all new timekeepers and hold refresher training throughout the year.
2. **Formalize your billing procedures.** Set aside specific days each month for billing. Require attorneys to submit all bills by a specific date each month, and make monthly billing meetings mandatory. At these meetings, partners should be questioned about larger, unbilled amounts left on work-in-progress.

Collecting Your Fee is Still the Key, cont'd.

3. **Bill while the value is still fresh.** Billing realization is improved by invoicing a client early enough that the value of your services is still perceived (and appreciated!). You may want to require attorneys to bill a specified percentage of unbilled fees every month (at least 70 percent). And bill as the work progresses — don't wait to issue one large bill at the engagement's completion.
4. **Head off surprises.** Keeping clients abreast of the status of their legal matter is critical to heading off surprises in billing and collections. Develop a "value mindset" where you are constantly communicating the value of your services to the client. Also consider showing any adjustments to the pre-bill on the actual invoice. Clients will appreciate your consideration of what an appropriate charge should be.
5. **Watch write-offs.** Establish firm policies regarding billing lawyers' ability to write off unbilled time (e.g., write-offs should not exceed the greater of \$500 or 5 percent of fees, all costs in excess of \$100 should be billed, etc.). Require an explanation from attorneys of all fee write-offs in excess of a specified amount or percentage. This can be reported on a write-off form or in a monthly billing meeting.
6. **Age your receivables.** Age your firm's accounts receivable once a week (i.e., classify outstanding balances according to client and original billing date). Studies reveal that the likelihood of collecting receivables drops drastically as time goes on. Then furnish reports listing clients that are delinquent with their accounts, including the balance owed, by assigned lawyers.
7. **Follow up promptly on past-due receivables.** No lawyer wants to be the "heavy" with clients with whom he or she has spent years developing a solid relationship. But receivables grow harder to collect by the minute. The trick, therefore, is to be responsive — but keep it professional.
8. **Reward billing realization.** Compensate partners based on their realization of standard fees, not on gross billings. Billing frequency and A/R collections should also be a part of your partner compensation guidelines. Periodically, the firm should compute the number of days in unbilled fees and A/R by partner.
9. **Problems in realization can have a big impact on partner profits and compensation.** But if you are doing great work — and communicating the value of that work to your clients — you should have no trouble billing and collecting what you record.

What Realization Might Say About Your Rates

A hard look at your billing realization can provide insight into your rates. For example, assume that you've established a target realization in the 90 to 95 percent range. If your realization exceeds 97 percent on a regular basis, your rates may be too low. Conversely, if billing realization is dipping much below 90 percent, your rates could be too high.

Ultimately, your billing rates and other fee arrangements should be covering your costs and be cushioned with targeted profit. Run the numbers and make sure the economics support your billing.

Realization issues can endanger your bottom line. Contact your Mueller Prost today at 314.862.2070 to learn how our advisors can help you establish sound policies and procedures.

CRITICAL CONTACT

Three Collections Calls You Should Be Making

Accurately recording your time and then billing what you are due (see the page 1 article) is only half the battle — collecting your fee is the other half. Unfortunately, many law firms struggle with collections.

Three Critical Contacts

One of your best collections tools might just be sitting right on your desk. Consider these three critical phone calls (or e-mails) that you should be making to clients:

1. The Confirmation Call. Make a call or send an e-mail to uncover any objections before the invoice is sent (especially if the bill is higher than the client may be expecting), rather than waiting for issues to surface at 60 days past due. Also confirm that the invoice is going to the person who has the power to approve it and get payment made.

2. The Follow-up Call. The next most critical contact occurs about 30 days after the date of the invoice, if you haven't received payment yet. Try to find out if the client is experiencing cash flow issues that are delaying their payables. This is also the time to reiterate your payment terms (you'll certainly have some leverage if you've included service charges on the original invoice).

3. The "Cut-Your-Losses" Call. Finally, if payment is still languishing after 45-60 days, there is a third call you should make: a call notifying the client that you will be forced to stop work if you don't get paid. Don't make the mistake of continuing work if huge sums are owed. Remember, your first loss is your smallest loss — continuing to work for a non-paying client only increases the size of your potential loss.

Standardize Your Calls

When it's time to start working the phones, it helps to have a standard protocol that's followed for every client. For example, automatic account statements are sent to clients every 30 days and telephone follow up is made after 45 days.

Keep in mind that clients usually prefer speaking to someone other than their attorney about payment issues. If you delegate this call to someone else, make sure he or she has the experience (and personality) to represent the attorney well.

Ultimately, law firms usually lose clients by delivering poor work or service, not by asking clients to pay their bills. Most clients will not be offended by friendly, professional inquiries about payment status. In the end, frequent phone and email contact may make the difference between getting paid ... or getting ignored.

Collections dragging? Consider involving your accounting professional. Call Mueller Prost today at 314.862.2070 for the help you need.

A Word About WIP

Work in progress (or WIP) is work that has been started but not yet finished. As such, it has already incurred a capital investment from the firm. WIP is accrued as the work is performed. It is recognized as an asset on the balance sheet and as revenue (unbilled) on the income statement.

Problems often occur at small law firms because most of them operate on a cash basis, accounting for cash as it comes in and goes out — rather than for billings or work in progress. By contrast, accrual accounting reflects WIP (completed but not yet billed) and accounts receivable (work billed but not yet collected) as line item assets on the firm's balance sheet.

The bottom line is that WIP is an asset that has to be managed. For example, if a matter involving 10 billable hours at a rate of \$200/hour shows up as an unbilled receivable of \$2,000 on your firm's balance sheet, it would be much more likely to receive the attention it deserves.

Ultimately, it's a matter of discipline to make sure every attorney is billing his or her WIP on a weekly basis. Doing so could entail generating a weekly WIP summary by attorney. Another key indicator to monitor is the firm's trailing 12-month average, which calculates the average days of WIP for the prior 12 months.

The Fine Art of Cultivating Referrals

Most satisfied clients are more than willing to make referrals. But soliciting client endorsements can still be tricky business.

The key is building a “referral consciousness” and imprinting yourself in clients’ minds so that you are always top-of-mind when the subject of legal representation comes up. Consider these referral cultivating tips:

- **Remember that competence always beats nice.** Don't even broach the subject of a referral until you've done a great job — a stellar job, in fact — for your client. The best referrals sound more like this: “He might be a little expensive, but he's worth it” ... “My attorney did an amazing job” ... or, “My lawyer kicked butt!”
- **Make the memory linger.** Make sure clients remember you after their cases are resolved. A handwritten thank-you note — maybe with a Starbucks gift card — can go a long way (be sure to include a few business cards that list the practice areas you handle).

- **Teach your clients to make the right referrals.** Of course, you want to remind clients that your business depends on referrals from satisfied clients, but also teach them what a good referral looks like. That means educating clients about your practice, areas of expertise and what kind of client is ideal for your practice.
- **Practice some quid pro quo.** If you're referring clients to other attorneys, make sure they know that you did so. If they don't remember, then maybe you need to move on to other lawyers who do!
- **Do it now.** It may be a non-billable activity, but developing a strong referral base is just as important as short-term production and billable hours. David Maister says it best: “Your billable time is your current income ... your non-billable time is your future.”

Give your Mueller Prost advisor a call at 314.862.2070 to discuss ways to generate referrals and cultivate repeat referral sources.

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