

Five Tips to Avoid Common Financial Issues in Law Firms

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There is a lot involved in the financial management of a law firm. Fortunately, with a good understanding of the principles of [law firm finances](#), firms can reap the benefits of a quality time & [billing and financial software system](#) that allows them to handle their firm's management with ease.

Let's dive in.

Trust Accounts

It is common knowledge that improper handling of [trust accounts](#) results in the highest cause of bar issues for attorneys. It is imperative that the firm's trust account be handled by a manager who knows what they are doing and that the managing partner maintains close oversight as well.

Your firm's legal software should have the ability to track each client's trust fund balances. By having your time & billing software and your financial software all on one platform, you can maintain accurate records without the need for double entry into two systems. Each month, the firm's manager should reconcile the firm's trust account with the bank statement, and following that reconciliation, he or she should run a report showing the trust account balances for each client. The total from the client trust listing report should match the total for the firm's reconciled bank balance. These reports should then be provided to the managing partner for full transparency.

A common mistake that leads to bar complaints is when a firm transfers funds to the operating account before the client has been billed. Trust funds should remain in the trust account until the client's regular billing cycle. When funds are transferred to pay an invoice, it is important that the invoice template is clear as to what has been billed and transferred from the client's funds, and that invoice should be provided to the client so that they have a clear understanding of their trust account's status.

The firm should not keep more than a small amount of the firm's funds in the trust account. The sole purpose of keeping firm money in the account is to cover any potential wire fees that may result from an automated clearing house (ACH) coming into the account.

Another common mistake that firms make is transferring funds from the trust account before they have cleared. Gone are the days when a certified check can be treated as cash. Standard protocol is to wait 7-10 days for a deposit to truly clear before drawing on those funds. If the funds are drawn before they are confirmed to be "good," the firm is essentially using another client's funds.

Lack of Written Agreements

It is important that law firms use Engagement Letters (EL) to spell out the agreement between the firm and the client. The EL should define the scope of work, the agreed rates the client will pay for the work, how often the client will be billed, and any interest fees the firm charges for late payments. It should be signed by a partner and countersigned by the client.

Non-representation letters are often overlooked by firms. If a firm discontinues work for a client, or if they provide a consultation to a potential client but do not engage in the work discussed, it is important to send a non-representation letter so that there can be no claim made that the firm was responsible for handling the matter.

Understanding the Cost of Doing Business

Like any business, law firms have a cost of doing business. Do you know what it costs your firm to have an attorney working on a case? You may think it is just a matter of their direct compensation, but there is more to it than that. By using [cost accounting methods](#), you can combine your attorney's direct compensation and their share of the firm's overhead and divide it by the number of hours they typically bill annually to know what their break-even rate is. By calculating this rate, you know what you need the attorney's billable rate to be in order to receive any profit from that attorney's time. Taking the time to perform this exercise is very valuable to your firm.

Accepting Credit Card Payments

Accepting credit card payments from your clients can result in faster payment, improving your [law firm's cash flow](#). It can also result in receiving payments that you may not otherwise receive if you have clients with cash flow issues. It is important to use a credit card processing service that will allow for the separate distribution of your fees to your operating account, in addition to your retainers and settlement payments to your trust account. [Law Pay](#) is an example of a service that can assist with [legal settlement accounting](#).

Many businesses charge their customers a fee for using credit cards. It is important for law firms to understand that the ability to follow this practice varies from state to state. You need to consult your state bar to determine whether it is considered ethical in your state to pass on those fees to your clients. You will also want to consider, even if you are allowed to pass on those fees, whether it is good business practice for your firm to do so. Will passing on those fees leave a bitter taste in the mouths of your clients? Are you better off increasing your rates by \$5 an hour to cover the cost of accepting credit cards?

Understanding Your Firm's Data

Do you know what your [billing and financial reports](#) mean? The best way to have accurate reports that you can rely on and to avoid the issue of having to practice double entry recordkeeping between multiple software applications is to use one software that hosts both time & billing and financial data in one platform. For example, by having everything in one place you should be able to accurately and efficiently run reports that show you things like effective billing rates so that you know if after write-downs and write-offs your attorneys are billing at a rate that is higher than their break-even rate so that your firm will see a profit.

