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The Ins and Outs of Law Firm Budgeting

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Forecasting isn't only for your local weatherman—it's an essential legal process too. Fortunately, forecasting income and expenses isn't as complex as predicting where the next hurricane will hit or when the first freeze of the year will occur. But, when you're juggling all the tasks of running a law firm, the forecasting and budgeting process can seem both challenging and overwhelming.

- How do you manage the short term while trying to promote growth in the long term?
- What are your startup costs?
- How do you project revenue accurately?

Law school courses don't teach you the practical aspects of running a business, even though they come up every day in real-life practice at a small firm, especially for solo practitioners.

Creating a solid budget and getting your law firm's finances in order are imperative. This is the only way to stay competitive in the legal market.

The good news is that with the right strategy and management tools, your firm will be off and running. Let's take a look at these critical processes and what steps you can take to create a budgeting plan.

What is budgeting?

A **budget** is an estimate of revenue and expenditures for a specific time period. Basically, it's your law firm's plan for sustainable financial success, and budgeting is the process of creating that plan.

Budgeting provides your law firm with a measuring stick for periodic review throughout the next year. If your law firm is hitting its goals, maybe it's time for an office party! If it's missing your desired milestones, it's probably time to re-evaluate and adjust. Creating a comprehensive budget is the best way to proactively manage your law firm's finances.

What do you need to consider before creating a budgeting plan?

A good budget is thoughtful and aligns anticipated revenue and expenses with goals.

What to include in your law firm budget will depend on the size of your firm, how long it's been in operation, and what practice areas it specializes in. However, there are a few constants for all

practices that you should consider when drafting your firm's budget. Ask yourself these questions.

1. What are your firm's expenses?

Don't start your budget planning in a vacuum. Instead, start by thinking about your firm's mandatory expenses.

- What is required of the legal professionals at your firm?
- What is the cost of bar association dues?
- What do their CLE expenses look like for the year?
- Does your firm maintain malpractice insurance?
- What is the yearly premium?
- What about subscriptions?

Additionally, think about staffing. If firm leadership is planning to add more employees to the firm, you'll need to know whether your firm will have money to cash flow that addition. You'll also want to consider the tangibles: the cost of office space, hardware, and legal and accounting software. What about upgrading to new technology? Or the cost of business cards? Note that some of these expenses will be incurred yearly, some monthly, and some only once.

2. What is your firm's projected profitability?

Once expenses and other overhead costs have been itemized, your next step is to consider profitability (and to do so realistically).

Revenue is the money your firm receives from clients for legal services rendered. When you subtract expenses and overhead costs from revenue, you have net profit (otherwise known as the bottom line).

Think about net profitability in real terms: how many clients will your firm need to service over the next quarter (the next two quarters? the next year?) to bring in the desired level of revenue? Are your firm's rates high enough to support the practice? [What is the required cash flow to keep the lights on?](#) Can improving your invoicing practices improve that cash flow? What about accepting alternative payment methods like credit cards?

[If your law firm is hitting revenue milestones without increasing net profit, it means you might need to cut expenses and overhead costs.](#) Be sure to consider seasonality when it comes to revenue. If you're a tax firm, you're likely booming in April and slow in July. With awareness, your firm can account for these patterns and set aside capital accordingly so that the necessary funds are still available during less profitable months.

3. How will you keep track of your budget?

Keeping track of your law firm budget can be time-consuming and stressful. Many new law firms will opt for Excel spreadsheets or budgeting templates to get started with tracking planned expenses and revenue. However, when your law firm grows and its workflow increases, keeping

track of your law office budget on those tools might prove even more time-consuming and stressful. The right [legal reporting software](#) puts a host of [budgeting and financial reports](#) at your fingertips, each of which will help your law firm organize your finances, optimize your practice, and help you strengthen client relationships.

When it comes to how often to review your budgeting process, we recommend assessing your budget each month. This regularity will provide your law firm with a good idea of whether you need to make any adjustments. Additionally, your firm should review its budget yearly to adjust for goals, new practice areas, or unforeseen circumstances (like a market crash or, say, a global pandemic).

What are some tips and tricks for budgeting?

While budgeting will look different for each firm, we suggest a couple of tools of the trade to get you started on creating or rethinking your law firm budget.

Think short-, mid-, and long-term

Setting your law firm goals is one of the first steps in creating a workable budget. Goals are a benchmark to help you determine where to put capital and where to cut costs.

We recommend classifying your goals into the following categories: (1) short-term goals that you can reach in the first six months of your fiscal year, (2) mid-term goals that can be reached by the end of your fiscal year, and (3) long-term goals that will take your firm longer than a year to reach. Also make sure that each set of goals is specifically laid out, measurable, and realistic.

Work smarter, not harder

Using the right tools and legal tech can transform a firm's profitability and law practice management. While it may seem like just another line item expense, technology can actually help keep your costs low through workflow and document [automation](#), which frees up your lawyers and staff to work on billable matters (i.e., tasks that pay).

The right legal tech will help your firm simplify nonbillable tasks like [client intake](#), [practice management](#), [billing and collections](#), and [time tracking](#). With more time for billable work, your firm can raise its revenues. And with the right tech that [offers a streamlined experience](#) and integrations, your firm will minimize its use of subscription services and administrative time and thus minimize your overhead costs. The result is the perfect recipe for increased profitability.

Keep an eye on trends

We aren't yet out of uncertain times, and keeping a pulse on what's to come is important when setting your budget. If your law firm hasn't yet undergone a full return to the office, your budget may need to include capital for the transition. Or, if your law firm has stayed committed to a hybrid workplace, you might still need to budget for increased tech costs and stipends to employees.

Additionally, many law firms are amplifying their [marketing strategies](#). It's likely worthwhile to consider how marketing efforts can fit into your budget and increase awareness and thus revenue.

What are the differences between forecasting and budgeting? How do they play into one another?

Budgeting and forecasting are both helpful tools that your law firm can and should use to establish a financial plan. As discussed throughout this article, budgeting is the game plan for where firm management wants to take the firm.

Essentially, your budget is an outline of financial expectations and goals. Forecasting, on the other hand, is interpreting whether that plan is working and whether the firm is moving in the right direction by estimating revenue, costs, and ultimately profit that will be achieved at a future date. Generally, forecasting looks at historical data (like last year's or last quarter's profits) and then anticipates future outcomes based on it. It's like a crystal ball, but only better because it's filled with cash.

Forecasting helps firm management make needed adjustments in practice areas by hiring in anticipation of a boom and, more generally, helps you develop an informed business plan. You can then take that informed business plan into consideration when developing a budget.

It's time to start creating your law firm budget

With some critical thinking and [the right tools](#), your firm will be ready for the coming year. Remember that no budget is perfect, but by having one in place and monitoring it regularly, your law firm can forecast big changes and adjust as needed.

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