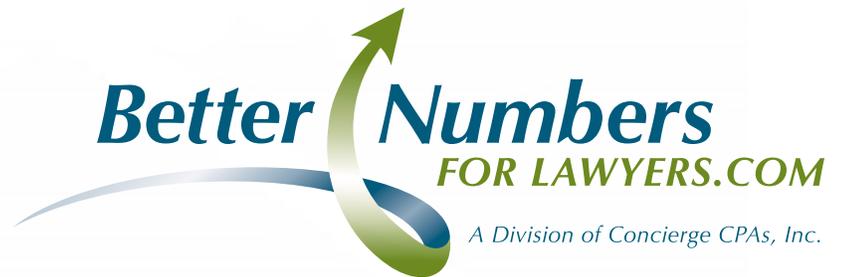


5 BIGGEST FINANCIAL CONTROL MISTAKES

LAW FIRMS MAKE
AND HOW TO AVOID THEM



5 Biggest Financial Control Mistakes Law Firms Make and How to Avoid Them



Do you feel that you're flying blind in your law practice regarding the financial health of your firm?

Do you feel overwhelmed when you look at your financial reports because you're not sure what numbers to really look at, or how to interpret them so you can make better decisions in your business? Do you have a clear spending plan so you know at least how much you need to earn each month to pay the bills and your employees? Are your accounts receivable and cash flow under control? Are you confident you're not overpaying your taxes?

Running a law can be extremely stressful and overwhelming. The day-to-day pressures of keeping up with client work make it difficult to find the time necessary to properly deal with the financial aspects of the business. And when you do finally sit down to think about these things, it seems so confusing that it's just easier to avoid the whole thing altogether.

If you want to take control of the numbers, this report is for you. You'll find out how you can be clear about where you're headed financially and know how to run your business more efficiently and profitably.

The reality is that effective financial management is essential to grow your firm and be more profitable. That might seem obvious, but achieving it can be anything but.

Our mission is to help you demystify financial performance so you can take back control of the numbers. And we're going to start with the 5 biggest financial control mistakes law firms make and show you how to avoid them.

The content of this report is based on our 5+ years of experience helping law firms turn around their financial performance. When you avoid these 5 mistakes you will enjoy greater profits and peace of mind, less overwhelm, more control over your finances and the ability to make more effective management decisions.

Of course, we understand that you may need support implementing strategies to avoid some or all of the 5 mistakes. After all, you're busy running your firm and probably don't love finances as much as we do. Call us strange, but we're passionate about finances and the reason is simple. We've seen how it can change your life. We've seen it happen over and over again with our valued clients.

If you would like to speak with us privately so we can learn more about your business and explore how we can best support you, just go to www.betternumbersforlawyers.com to apply for a Discovery Session.

So let's go through each of these 5 mistakes and show you how you can avoid them to take back control of the numbers.

1 Not Producing Timely, Clear and Reliable Financial Reports

Most small to medium sized law firms vastly underutilize their financial information, using it only to file their tax returns. They don't produce timely, clear and reliable financial reports for their partners. This is a big mistake because without financial reports you can't measure your firm's financial performance.

Most likely your books are prepared using online or desktop accounting software like QuickBooks or the accounting module of your practice management suite. While it's true that running a financial report is very easy using software, the importance of correct and reliable data entry is imperative and a lot of times overlooked. Do you know the old saying "Garbage in, garbage out"? It's certainly true in financial reporting.

Your firm's financial reports should be:

Timely

You would be surprised how many small to medium sized law firms only think about bookkeeping once a year during tax season. Your bookkeeper should finish the previous month's bookkeeping and present you with the financial reports in maximum 7-10 days after the previous month' end. No excuses.

Avoiding even one of these mistakes will make a huge difference, but to get maximum results, we strongly encourage you to avoid all 5 of them.

Clear

As CPAs, we've seen so many firms whose bookkeepers present less than clear financial reports to the partners. It all starts with a clear chart of accounts that is custom-tailored to your firm, but based on industry norms. Do you have multiple revenue streams? They should be tracked separately so you can see how much each revenue stream brings in. Do you use a trust account? Its balance should be presented separately from other operating bank balances. Are the occasional personal expenses that were paid out of the business bank account booked correctly? Do you see them under draws or shareholder distributions (correct way) or as an expense line item on the income statement (wrong way)? You need to have your bookkeeping reviewed by an accountant who specializes in your business, so they can give adequate instructions to your bookkeeper and you can get the clear financial reports you need.

Reliable

Is your bookkeeping comprehensive? All bank accounts, credit cards and cash transactions should be booked each month. Also, all your bank accounts should be reconciled and reconciliation reports presented to you each month so you can be sure that the books tie to the bank statements. There are certain adjusting entries that your bookkeeper might not be comfortable making and they need to be entered by your accountant or CPA at review-time and book closing. For most reliable financial reports your bookkeeper's work should be reviewed monthly, or at least quarterly, by an accountant who is intimately familiar with your business.

2 Not Having a Spending Plan and Not Knowing Your Break-Even Point

Your goal in setting up a spending plan is to create an environment that promotes the financial health of your firm. A well thought-out spending plan helps you maintain control over expenses. It can also track how close your revenues are compared to where you would like them to be.

Your spending plan doesn't have to be fixed. It's not a set it and forget it kind of thing. In fact, it should be flexible and adjusted throughout the year so you have more control over your business.

Putting together a spending plan sounds complicated and overwhelming, but in fact it's pretty simple. Most accounting software gives you a super easy way to set it up. You can start at any time of the year, but the best is to have one for the whole year. December and January are a great time to think through your goals for the New Year and put them in a spending plan.

A goal-clarifying exercise will result in higher control over your finances.

Let's say you have a goal to reach \$750k in gross revenues by the end of the year. What does that mean in monthly goals? If you start with \$50k income in January, how much do you need to grow every month to get to \$750 by year end? Will you be able to grow an additional \$10k without a new marketing campaign? At what point in time will you need an additional employee to support your growth? These are just examples of questions that come up when you work on your spending plan. Setting it up is a great goal-clarifying exercise that will result in higher control over your finances.

Here are a few tips on how to set up a spending plan for your firm. Generally you can estimate your expenses with greater accuracy compared to your revenues, so let's start by determining the following:

- Identify the monthly draws that you would like to take out from your law firm. You can start with the minimum that you absolutely need to take home to cover your personal expenses, and as time goes by, and if your cash flow permits you can adjust your draws.
- List all known business expenses, such as office rent, utilities, insurance, payroll, dues and subscriptions. Don't forget to budget some flexible expenses, such as marketing and advertising expenses.

After listing your likely expenses by month, you will know what your firm's **projected monthly break-even point** is. You will need either revenues or a credit line to fund your monthly expenses.

Once you know your likely expenses and break-even point, you can focus on revenues. If you've been in business for a while you can analyze your previous revenues, and using your historical information combined with your goals you can set your revenue goals for each month. If this is your first year in business, your first revenue goal is to cover all your expenses plus your minimum draws that you require.

Setting up a spending plan is great, but it's just a beginning. Each month you need to **analyze your actual activity compared to your spending plan**. Your bookkeeper should be able to run this report for you and most accounting software will generate it easily as well. Did you achieve your income goal for the month? If not, what happened? What caused your insurance expense to double compared to the spending plan?

You can tell your whole firm's story from the spending plan versus actual report. It's a goldmine of information, when you know how to interpret it. Ask for expert help on how to create your budget and how to interpret it so you can reach your financial goals.

3 Not Projecting Cash-Flow on a Consistent Basis

Cash-flow is becoming an increasingly bigger problem for many law firms. According to our benchmarking survey, 40% of firms are experiencing more cash-flow pressures than in previous years.

As a business owner, you understand and strive to make a profit. If you bill a client \$3,000, pay your employees \$1,000 to complete the engagement, and incur \$500 filing fees along the way, you just made a \$1,500 profit.

But what if the client is slow to pay his or her bill, and six months pass before the bill is paid? Your business still shows a profit, but what about the bills you have to pay during the six months that pass? You will not have the cash to pay them, despite the profit earned on the engagement.

As you can see, **profit and cash flow are two different concepts**, each with entirely different results. The concept of profit only looks at income and expenses at a certain point in time. Cash flow, on the other hand, is more concerned with the timing of the money moving in and out of a business.

Other than being able to pay your bills, and keep your firm running, you also have to consider your own cash draws from your business. My guess is that you also want to pay your mortgage, car loan, and finance the life of your dreams, right?

For most firms the cash-flow projection is the most important report to analyze on a consistent basis. It just happens that this is also the report that most bookkeepers have the hardest time generating without initial setup by expert help, because most accounting software can't generate this report with a push of a button.

The idea of the cash-flow projection is fairly simple: estimate how much income you will collect or harvest during the next month and add that number to the balance already in your bank. Then estimate the bills you have to pay during the same period and see if you have money left over at the end.

If your projected bank balance at the end of the month is in the red, than you either need to start calling some clients who owe you money or postpone paying some bills. If you project to be in the green at the end of the month than you might decide to leave the money in the bank, pay yourself a bonus, or maybe invest in increased marketing.

You always want to project out several weeks or months ahead, as you might have a positive cash flow one period and red the next. **This is a management exercise that all successful firm owners take very seriously.**

Profit and cash flow are two different concepts, each with entirely different results.

4 Not Knowing Your Most Important Numbers

Do you know that 95% of law firm owners do not know off the top of their head how much their year-to-date revenue is? But I can guarantee that the most successful ones do! Don't become a statistic — know your numbers!

95% of law firm owners do not know, off the top of their head, how much their year-to-date revenue is.

The list of the most important financial numbers can be long and overwhelming, but you can start with identifying the top three that are the most important for your firm at this time. Your expert advisors can help you identify the top three based on your business's health and help you analyze them.

You should look at these numbers regularly: at least monthly, but the most successful firms do it semi-monthly or weekly. While it's human to want to avoid looking at the numbers, especially in hard times, tracking them consistently will provide you with the information you need to make better management decisions.

Here are some of the financial numbers that law firm should track:

- Monthly and year-to-date gross revenues
- Monthly regular expenses and extraordinary expenses
- Monthly and year-to-date net income or loss
- Cash balance in the operating account
- Cash balance in the trust account that can be harvested
- Accounts receivable that can be collected in the next 30 days
- New client work that can be completed & collected in the next 30 days
- Monthly payroll expense
- The variances between planned versus actual for #1-8 above.
- Monthly break-even point.

You will need to request the following financial reports from your bookkeeper:

- Monthly and year-to-date Income Statement
- Balance Sheet
- Spending Plan
- Spending Plan Variance Report
- Cash Flow Projection
- WIP (Work in Progress) Report

5 Overpaying Your Taxes

Most business owners think that their tax preparer is also doing tax planning for them, but let me ask you this: When was the last time your tax preparer called you up and said: “Here is a tax strategy that I think will save you money?”

You want to maximize available tax strategies based on your firm’s situation. For instance, paying taxes on your profit as self-employed on a Schedule C might have worked well in the beginning, but as your business grows, it might not serve you the best.

The mistakes and missed opportunities might be costing you thousands in tax. You might leave money on the table by not having a Medical Expense Reimbursement Plan in place, or by not asking the IRS to tax you as an S-Corp. Do you know if your current retirement plan allows you to maximize your contributions?

Is your tax accountant running quarterly tax projections for you based on your big family tax picture so you can be sure that you don’t under or over-pay your quarterly estimates? This is especially important in the case of a growing firm. Everybody hates surprises at tax time!

You need to ask your tax preparer if he or she is taking a truly proactive and comprehensive tax planning approach. He or she has to look at every angle of your tax situation not just one time, but every time there is a change at your end or in the tax laws.

A recent client, who will save around \$7,000 a year in taxes, told me that he will use that money to take his entire family on a nice vacation every year. I’m sure his wife and kids will thank him for that and they’ll make lifelong memories!

You want to maximize available tax strategies based on your firm’s situation.

NEXT STEPS

We hope these 5 biggest financial control mistakes law firms make have given you some insight into how you can improve your firm's financial control and performance. If you want to talk with us privately so we can learn more about your business and explore how we can best support you, just go to www.betternumbersforlawyers.com to apply for a complementary Discovery Session.

In this session, we will:

- get a clear picture of your financial goals and how you will get there
- discover the financial performance areas that need improvement
- explore some easy steps you can take for better profitability and efficiency

We look forward to getting to know you and helping you reach all your financial goals!

ABOUT THE AUTHOR



Borbala went to law school in Europe and moved to the United States two weeks after graduation with the idea of challenging herself to make it in a place where nobody knew her. As a business manager for a high-tech startup she recognized the power of understanding and interpreting financial information and the clarity and peace of mind this knowledge gives business owners.

After starting her own business and focusing on law firms, Borbala was invited to serve as the CPA and virtual CFO of one of the leading law firm management coaching firms in the United States.

She believes in forging close relationships with her clients and becoming their most trusted advisor by using both her expertise as a certified public accountant and over 15 years of business management experience.

She is the founder of Better Numbers for Lawyers, a business advisory and certified public accounting firm bringing turn-key financial control solutions to law firms. The firm currently serves clients in 17 different states.

She can be reached borbala@betternumbersforlawyers.com

Rave Reviews and Case Studies (Cont'd)

“I could not only understand my books, but I could use them to make decisions about my business.”

“I had worked with two bookkeepers before Borbala. The first one was able to balance my books, but she couldn't generate reports. So I turned to a certified QuickBooks Pro who although she had no expertise working with law firms, assured me that books were books, regardless of the type of business. Big mistake! She was non-responsive, over three months behind, and blamed me for not giving her the “tools” she needed to do her job.

By the time I handed my books over to Borbala, they were in complete disarray. I was at my wits' end, but I had no illusions that she would be any better than my previous two bookkeepers. Boy, did she prove me wrong and restore my faith in the idea that I could not only understand my books, but I could use them to make decisions about my business.

In less than a week, Borbala had reconciled the first five months of the year, correcting my old bookkeeper's numerous mistakes. Suddenly, the numbers started to make sense! In another week, she had balanced the three months' worth of delinquent accounting. When she originally gave me the timeline, I was extremely skeptical, as my last bookkeeper had never met a deadline she found worth keeping, but Borbala delivered. I was thrilled, and it took no further thought whatsoever to hire Borbala as my accountant, CPA, and CFO.

Borbala consistently gives thorough, detailed instructions of what she wants and why she wants it. She never asks for extraneous information, and she knows exactly what I need from her. What I especially like is that she's the expert, guiding me, and making my life easier. With my last bookkeepers, I always felt like they were waiting on me to make decisions without the information I needed.

Now, I feel much more confident about my present and future financial picture. She holds me accountable to managing costs, maintaining a budget, and monitoring my accounts receivable. With Borbala's help, I can make smart strategic decisions about my business without fear of causing financial harm.

Cristin M. Lowe, Esq.
Law Office of Cristin M. Lowe, San Ramon, CA
www.cristinlowelaw.com

Rave Reviews and Case Studies (Cont'd)

“She has changed my life.”

“Before working with Borbala I was a mess. I did not have a budget, had no idea how to plan for tax time, had never even heard of a budget variance report, and was basically flying blind in my law practice when it came to the financial health of my firm. I did not have a bookkeeper, and I basically had a stack of papers that at some point before my tax returns had to be filed each year I “organized” into some type of financial report that I would use to file my tax returns. Within a few weeks of working with Borbala, I had my very first budget. It was so freeing to know that this is what I needed to shoot for each month, and I had an idea of where I was heading. Now, I know where I am going financially and have a plan for getting there. I highly recommend Borbala. She has changed my life. ”

Amber James, Esq.
James Family Law Firm, P.C. Huntsville, AL
www.jamesfamilylaw.com

“I now have a yearly budget in place and a realistic picture of what I need to earn to reach my financial goals.”

“Before working with Borbala, I was just flying by the seat of my pants and simply working month to month with no set financial goals and without a realistic picture of what it cost to run my law firm. After working with Borbala for a few short months, I now have a yearly budget in place and a realistic picture of what I need to earn each month and each year to reach my financial goals. It also helped me determine what fees I should be charging since now I know what it costs to run my firm. I highly recommend working with Borbala so you can have a clear vision of where you are in order to meet your financial goals.”

James P. Whalen, Esq.
Whalen Law Office, Dallas, TX
www.whalenlawoffice.com

Case Study

Subject: Rapidly growing consulting firm

Issue: Although profitable, it seemed there was never enough cash to pay current bills and invest in resources that would generate more growth.

Resolution: We determined that we need a weekly cash projection report, estimating income and expenses for 6 weeks at a time. Revenues from clients were collected in the middle of the month, so the cash flow projection helped the owner determine what expenses to pay each week so the cash would last till the next collection cycle. We run a new cash flow report every week, based on the bookkeeper's report of new bills that came in and new income estimates for the month. This was a great tool for the owner to have control over his business' finances.

“She helped take the fear out of the financials.”

“I was completely lost about how to measure the financial health of our company. I stepped into the CFO role out of necessity and had very little experience with accounting practices or bookkeeping. My husband and I took over a family law practice that while having huge potential, it needed a complete financial overhaul. (...)

Within three months of working with Borbala, we had a completely different outlook on the health of our company and we were able to measure our successes in all the important financial categories. She was able to help us clear up the confusion and to put metrics in place to measure our success and to keep us honest and accountable moving forward.

Now we're able to see a clearer picture of our financial health and make course corrections when necessary. She helped take the fear out of the financials. (...)

Rebecca Goodman, CFO
The Goodman Law Firm, Brooklyn, NY
www.nygoodmanlaw.com

Rave Reviews and Case Studies (Cont'd)

“She takes a palpable interest in my practice and how it can be more efficient, productive, and profitable.”

“Before working with Borbala, my business was “running,” but I didn’t know how well or even why, not to mention what it was capable of doing. I’m not an accountant, and frankly, I don’t like thinking about the numbers side of my divorce and family law practice.

With Borbala’s help, I now know what my budget should be, how much I can and should pay my associates and staff, how to plan for maximum tax savings, and how to set and reach goals for increased profits.

Borbala loves this stuff and it shows. She doesn’t just “do her job,” she takes a palpable interest in my practice and how it can be more efficient, productive, and profitable. Each month we meet to review my books, analyze the data, and use that to ensure I stay on track. And I mean on track to go from \$500,000 last year to \$750,000 this year.

I have a bookkeeper (who loves Borbala too). I have an accountant. They do a great job, but their job isn’t the same as Borbala’s. Borbala helps me make the most of my resources. Because she is herself a CPA, she knows what my bookkeeper can and ought to be doing. She provides me with a knowledgeable, neutral second opinion on my accountants’ work too.

From an ROI perspective, Borbala has been and remains an easy choice. She’s careful, accurate, creative, and engaged. I cannot recommend her more highly.”

Eric K. Johnson, Esq.
Utah Family Law, LC, Salt Lake City, UT
www.divorceutah.com

“It’s given me great peace of mind knowing that she is a watchdog over the tax situation of my business.”

“Before working with Borbala, I was working with an accountant that didn’t understand how to project my tax burden and help me plan for the year. As a small business, it’s really important to me to understand what my quarterly taxes should be based on my current income and what I should be putting away for an end-of-year retirement contribution. With Borbala, there are no unpleasant surprises come April, and it’s given me great peace of mind knowing that she is a watchdog over the tax situation of my business. (...)”

Malissa Bodmann, Principal/Owner
Compelling Communications, LLC, Shaker Heights, OH
www.compellingcommunications.com

Rave Reviews and Case Studies (Cont'd)

“Now, our firm is less stressed and more confident that we are making the right decisions.”

“Before working with Borbala, we did not have a budget in place; we were not analyzing our financial reports to make financial decisions – because we didn’t have financial statements.

Within the last few years of working with Borbala our firm has been able to make day-to-day and long-term decisions that have affected our tax liability, and our ability to grow in smart ways. Now, our firm is less stressed and more confident that we are making the right decisions for us and for the clients we serve.

I highly recommend working with Borbala because she is extremely knowledgeable and responsive in a way that most vendors are not. Returning calls or emails the same day and for a consulting firm like us makes all the difference.”

Lori D. McClung, President
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www.advocacyandcommunication.org