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Guest article: Post-Recession Strategies: Controlling Financial Leakage

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If there is anything that the Great Recession has reminded us, it is that cash (not debt) is king and that organizations serve themselves best by keeping a steely-eyed focus on free cash flow. For a law firm, this cannot be done without a detailed profitability analysis by practice area, by client and even by matter. And with billing rates getting squeezed – and not likely to rebound soon, it is important for firms to take into account all expense data at all times.

Some expenses, such as client lunches and business development costs, are clearly the firm's responsibility but must be considered when calculating the profitability of a client or matter. Expenses related to photocopies, scans, faxes and phone calls are historically the client's responsibility, but some firms and attorneys find these expenses are an easy write-off for the sake of client satisfaction and goodwill. Although firms find these costs easy to write off (or bury in the hourly rate), they are not always fully tracked and sometimes not tracked at all. Other expenses that are typically the responsibility of the client are not recovered when if they are incurred outside of the firm's systems. Examples might include overnight charges or online research. It is imperative to capture information about all expenses, no matter where and how they are incurred.

For example, imagine a matter that requires one thousand photocopies in a given month. The attorney's administrative assistant may make most of the copies, but say the partner himself made 200 on a Saturday. Uninterested in looking up a client/matter code, the partner simply enters "9999." If the firm doesn't have a good mechanism for managing exceptions, it loses track of 200 copies. Then when reviewing a pre-bill, the engagement partner writes off another 200. The client receives the bill, complains a bit, and receives a credit for a further 200, never even realizing that it was not billed for the delivery of the documents by FedEx or for the online research that went into creating those documents. The firm recovers for less than 40% of its expenses – and because the "leakage" was at multiple places, firm managers don't even realize it. That favorite client that the partner thinks is so valuable may not be so profitable after all.

The AmLaw 100 reported a reduction in profits per partners of 4.3% in 2008, and no one expects the 2009 numbers to be any better, so these days even a small loss in profitability can make a big difference to a firm. The key to remaining sound in and after the recession is to collect good data throughout the firm and then apply that data to sound profitability analyses. Firms account for all hours worked, even those that are not billable, and it is also crucial for firms to collect all expense data. This includes copies, faxes, prints, phone calls and scans, as well as travel, court fees, research, overnight, courier and credit card charges. The key is automation: make sure information is collected as these expenses are incurred, rather than asking attorneys and administrators to recreate it after the fact.

Once all data is collected, use it to get a full idea of your profitability. Analyze by matter, by partner, by client and more. Make sure all write offs are accounted for and make sure they provide value; reducing the bill for an already unprofitable client does not serve the firm.

Furthermore, expense data can be used to optimize operations within the firm. Are multifunction devices placed properly based on data, or based on squeaky wheels? Are the right projects getting outsourced? Is the firm being properly compensated for all it does?

The Great Recession has taught us to focus on profitability, but many firms developed questionable habits during the upswing. The best way to ensure a happy future is to promote discipline in collecting and using data to the best effect.