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Advice and Insight into the Practice of Law
Managing Risk by Managing the Revenue Cycle

By Jack Eagles

Suing for fees significantly sharpens the risk that you will face a claim for professional liability. Almost always, a motivated client can develop an argument that at least some portion of your services fell below some reasonable expectation and standard of care. A lawsuit against the client can be just the motivation the client needs to pursue that argument rather than just walk away without complaining. Fee suits place you and your firm at risk for ethical challenges, professional liability claims, and business losses in the form of litigation expenses and lost attorney time that may very likely outweigh any potential recovery in court.

Fee disputes and lawsuits are avoided through communication with the client, good billing and collection practices, and timely, prudent business decisions on the part of the lawyer and law firm. Effective management of the entire "Revenue Cycle," from client intake through payment or collection, can virtually eliminate the need to engage in the types of recovery actions that trigger malpractice suits, and also enhance your cash flow and profitability. Let's examine the issues in turn.

Client Intake When firms look for long term solutions to improving cash flow and minimizing loss potential, they should start by focusing on client intake. usually, lawyers talk much more about evaluating new clients and checking their credit than actually doing so. Lawyers have traditionally tended to shy away from discussing money matters with clients. Apparently, attorneys feel it is somehow "unprofessional" to request financial or credit information from prospective clients. However, these same lawyers would never suggest that a client extend credit to someone without first getting a clear understanding of the person's ability and intention to pay. Yet, ironically, that is exactly what they are doing themselves. Unless you are paid a replenishable retainer, you are in effect making an unsecured loan to any client for whom you perform work and bill later.

Do check potential clients' credit history. If they are switching firms, ask about their previous attorneys and why they are moving their legal business to you: you may be the next firm they plan not to pay. Don't assume that the client will be offended by such inquiries. Businesses and individuals are asked for this information on a regular basis. If someone balks in the face of your questions, that may be a good indication that you ought not to do business with them.

Engagement Letters Attorneys can make a profound long term impact on cash flow by being more up front with new clients regarding the firm's expectations about fees and payments. Helping the client to understand up front what is expected and what may happen if problems arise may in turn help you avoid litigation over unpaid fees later on. The more you can guide clients' expectations, the less likely it is that they will be surprised by the size of a bill on your insistence on payment at appropriate times. This is especially true for clients with little or no experience with legal representation.

An engagement letter or fee contract should define the costs and scope of the firm's services. It should lay out the billing and payment practices and procedures and make clear that you expect to be paid on a timely basis. It should also explain what you may do should the client fail to comply with those procedures. Have the client acknowledge that the payment terms are reasonable and evidence their understanding with a signature.

Timekeeping Another way to enhance firm cash flow and avoid fee disputes is to adopt rigorous timekeeping procedures and require compliance from all timekeepers. Most importantly:

Make sure everyone turns in time reports daily. Half hours lost here and there when timekeepers try to reconstruct a week's worth of work on Friday afternoon can add up to big dollars when multiplied by the total number of individual billings in any given week, let alone an entire year.

Require sufficient detail in all time entries so that invoices may be appropriately descriptive and itemized. Several one-hour entries of "reviewed file" can prompt a client to wonder if the lawyer isn't just trying to grab a few extra billable hours where she can. On the other hand, an entry of thirty minutes during which the lawyer "analyzed deposition testimony" or "read court ruling and planned next steps" explains just what the client is getting for the money.

Billing Process Law firms tend to experience substantially more investment in work in process (WIP) and accounts receivable than they seem to realize. The degree varies, but it is not unusual for firms to have 30 percent or more of their total receivables over 120 days. WIP often exceeds 40 to 60 days of firms' activity as well.

All time in WIP should be billed out on no more than a monthly basis, no matter how small. This keeps the cycle moving, maintains a predictable pattern for the client which allows for the development of a payment routine, and helps keep the billings to a relatively reasonable size, making payment easier and more likely. Long delays between bills, or between work performed and bill for that work, increase the possibility that the perceived value of the work will diminish as other events unfold, making a reasonable charge appear unreasonable and possibly prompting dispute. The time to bill for drafting a summary judgment motion is immediately after the motion is drafted and delivered to the client, not six months later when the judge has denied the motion, the client is disappointed, and hindsight seems to suggest you should never have made the motion in the first place.

Often, firms end up with tight cash flow because their internal controls and procedures to motivate partners to actually get the bills out are inadequate or nonexistent. The key to helping billers to maintain a steady billing cycle is to make the process as smooth and efficient as possible. The key to that is to standardize as much of the process as possible. The less time a biller needs to spend on the billing process, the more likely she will do it. The better the systems, internal reporting, and support the biller has to work with, the more successful the bills will be.

Invoices For many firms, a simple retooling of their invoice format is enough to significantly improve cash flow. Too often, legal bills look too much like a letter "informing" the client of the current balance rather than a "demand" for payment.

Bills should look like the invoices they are. They should have invoice numbers and a title that says "Invoice." And they should clearly show a payment due date (ten days beyond the date of issue is a good rule of thumb). This format clearly communicates that payment is expected upon receipt of the bill and makes it easy for the client to comply on time.

If you are being paid a retainer, try to include in your agreement the right to issue an edit report when your combined accounts receivable and WIP equals 75 percent of your retainer. This allows time to issue a new retainer billing and replenish the balance before it reaches zero and avoids the circumstance where you are essentially advancing credit to the client by continuing to work while the client's account is dry. Another alternative is an "evergreen" retainer, in which the initial retainer amount is designated for application to the final invoice with the client paying current invoices directly. Once the representation is over, the retainer is used to satisfy the final remaining balance. Such a set up provides a lawyer with some protection should the client fail to keep up with mid- representation invoices. Whatever approach you choose, the goal is to be able to stay ahead; once billings surpass the retainer received it is extremely difficult for the lawyer to recover the advance position a retainer is intended to create.

Collection Despite all your best efforts, there will be times when a client falls behind on payment. Every law firm has to consider how best to collect delinquent fees. In most firms, the duty falls to the attorney who sent the bill in the first place. But this is frequently ineffective., Attorneys tend to have a problem taking time to work on collections. And when they do pick up the phone to talk to the client, the conversations tend to focus on the meat of the representation and the request for payment gets substantially downplayed.

Firms that give the responsibility to a firm administrator often do not fare much better. Sometimes the reason is because the lawyers are not willing to fully support the administration's efforts. For example, if a client calls the billing lawyer after the administrator has made a collection call, some lawyers will be almost apologetic about the collection attempt. Clearly such exchanges can only undermine the administrator's chances for successful collection. Other firms undermine the benefit of referring collection to administration when the billing lawyers choose to keep the big accounts or especially important clients to themselves and pass along only the smallest outstanding bills.

When lawyers or firm managers don't have the knowledge, skills, interest, or time to effectively manage the firm's receivables, small delinquencies can grow into serious enough outstandings that a fee suit could appear to be potentially cost effective. Collection is generally most successful -- and least risky -- when done by those with specific training and experience to allow them to understand the sometimes sensitive dynamics of a collection interaction (see Collection Call Basics). If you find that your firm frequently considers or institutes fee suits, or that fee delinquency is more the norm than the exception, your best course of action may be to collaborate with consultants specializing in professional service firm cash management and collection.