Getting Your Arms Around Your Firm's Receivables – Better Now Than Later

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With the downturn in the economy, businesses and individuals are experiencing cash flow problems because of a declining need for products and services. Many are holding on to their cash reserves and not paying certain vendors timely because of what everyone seems to agree is an uncertain time, with more uncertainty ahead.

Cash flow problems have always been the number one reason why clients do not pay their bills to law firms. And now because of an uncertain economy, this problem becomes more prevalent. Last to be paid are bills perceived as being non-essential to business operations. The harsh reality is that legal bills typically fall into this category. For many businesses and individuals, paying legal bills does not carry the same urgency as payment to others.

Clients are smart. They know very little will happen if they don't pay their legal bills on time. Law firms have conditioned their clients to pay at their own convenience, without penalty. Clients often disguise their cash flow problems through delay tactics in order to buy more time, or avoid paying altogether.

Law firms should have a sense of urgency to shorten their collection cycle, not only because of the uncertain future, but also because it is critical to determine if and when clients will pay in order to understand how it will affect cash flow within the firm.

These tougher times demand that firms take specific action regarding their overall accounts receivable management. Firms should:

1. Not make the mistake of thinking they can collect themselves out of a receivables problem. Taking steps to collect aged receivables may help cash flow in the short term, but without fundamental changes to prevent collection problems, the lawyers will quickly return to bad habits and the firm will find itself in the same dilemma down the road. The firm must evaluate its client/matter intake process and identify problem receivables early, so they can take action before it is too late. Firms frequently look at their older receivables and admit to having a collection problem. However, the real problem is that the problem has long existed, but they did not take the time to recognize it earlier in the aging process or before the work even started.

2. Establish effective accounts receivable reports. At a minimum, you need to know if an account is actively being pursued, what the payment status is, who is pursuing the collection efforts and whether they are getting results, why clients are not paying, and what needs to be done to get them to pay. Firms that are successful in managing accounts receivable are those that regularly review updated information on the client payment status in order to act quickly. At a minimum, categorize receivables to determine:

- Is it collectible? If so, when can we expect payment
- Is it problematic? How good are the chances we will get paid?
- Is it simply not collectible?

Reviewing various financial reports is essential to managing receivables. However, it is not just reading the numbers, but also using the reports to understand the clients' stories and the relationships behind the numbers.

3. Start digging for information. Begin by running various balance level reports from $5,000 to $50,000 over 90 days to determine where your larger balances are. Check the payment history of these clients, as well as new clients with no payment history. When looking at revenue results or projections, be realistic about whether the firm is underachieving in its collection goals.

Don't depend on historical patterns of bill collections. In economically stable times, you can safely assume that collections increase as the year progresses. An unstable economy can disrupt payment patterns. So measure revenue projections on a monthly basis, and be realistic about whether the firm is underachieving in its collection goals.

4. Have the right leadership and collection committees in place. Effective receivables management starts from the top. The firm needs to put the right people in leadership positions and hold them accountable for making progress on collection efforts. These leaders must have the ability to tell the attorneys to address their collections and, in turn, hold the attorneys accountable for their actions (or lack thereof). Many firms are losing revenue by giving attorneys too much individual autonomy regarding collections. We wonder when such firms will stop tolerating "good clients" who just don't pay their bills. When are they going to stop permitting clients to pay slowly without asking why? When will they start dictating the terms of payment rather than allowing the clients to do so? Additionally, attorneys are given too much leeway in dealing with their clients during the first 11 months of the year, only to have their feet held to the fire during the year-end stretch. With many firms having millions of dollars well over 90 days past due, the traditional culture of forgiveness needs to be replaced with a culture of high expectations to increase revenue through better collection efforts throughout the year.

5. Identify attorneys who have difficulty collecting their receivables – and take action. You know who they are. They are probably the same attorneys who have problems turning in their timesheets and getting their bills done. Take the time to meet with these attorneys on a regular basis and ask them to tell you specifically when bills can be expected to be paid. If they do not meet those dates or don't have a good explanation, make sure others in the firm are available to help them with their collection efforts.

6. Evaluate whether the firm has the right administrative staff in place, and determine whether they are doing the right work in the right way. Are these staff members reporting weekly on the accounts for which they are responsible, the age of the accounts, how much they have collected, and what they have in line for payment? Do you know how much they are working on actual collections, as compared to other duties less important to their primary purpose (i.e., generating reports, sending out reminder statements, providing information that the lawyers request, etc.)? Are they knowledgeable enough to provide the right reports and management information to the firm that will explain the progress of the collection efforts?

Staff must be held to a level of accountability, but for different reasons than the attorneys. If the firm decides to have staff contacting clients directly, the staff must not have too many other responsibilities that keep them from dedicating themselves to this mission. Beware of staff that prefers doing clerical work to making telephone calls to clients.

7. Project realistic time frames for collecting older, more difficult receivables. Be aware that receivables over 120 days have a 50% chance of being collected, and the rate continues to drop as receivables age. If you have any hope of getting paid, these accounts must be pursued diligently; don't wait for a client meeting, a phone call or a letter. Some of these accounts may be difficult to collect if only because no one has made the effort in the past to contact the clients. Work with the attorneys and your staff to figure out if the clients need to be pursued, and, if so, how.

8. Be proactive. Make sure that the attorneys in charge of your collection efforts and those staff involved are coming together on a monthly basis and assessing their progress. Managing accounts receivable is a "roll up your sleeves" effort. More often than not, little attention is focused on collection efforts until the last two months of the year. The effort must be year-round, especially this year. Even if you are unlikely to change old clients' habits of paying at year-end, teach new clients that they are expected to pay timely.

9. Use the services of professionals. Law firms lose clients by doing poor work or by failing to deliver client service, not by asking clients to pay their bills. Managing receivables will not hurt the relationship as long as it is handled professionally. Firms can employ trained professionals in-house who work specifically for the legal profession to perform accounts receivable management functions. Those who specialize in this area have the necessary experience and training, and can be accepted by the lawyers as professionals performing a vital function for the firm. Alternatively, a growing number of law firms are retaining an outside receivables consulting firm with which the firm works closely.

10. Check their calendars. Time is of the essence. Don't wait for the last couple of months of the year to make the year-end push. Start now. Law firms are beginning to react to the adverse economic trends. Many firms are beginning to evaluate how they plan to meet their year-end budget, recognizing that a changed economic landscape has fundamentally changed the rules of the game since the budget was made.

Do you have a question regarding your receivables? Please send your question via e-mail to jakek@clientci.com and our president will respond, free of charge. At Client Connection, we know how to manage receivables, and we would be happy to share a little of our knowledge with you.

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Client Connection assists law firms of all sizes throughout the United States by furnishing accounts receivable management services, developing practical receivable programs, training law firm staff in effective collection methods and executive placement of professional collections managers.

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