

It's Time to Collect

Getting clients to pay legal bills is harder than ever this year, due to cash-flow problems.

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Management

The No. 1 reason why clients don't pay their legal bills is cash-flow problems. This year has seen an increasing number of clients with cash-flow problems as a result of the weakening economy. These problems have become even more prevalent since Sept. 11 as a result of the declining stock market and a reduction in consumer spending.

The problem that law firms are facing is actually twofold. First, businesses are experiencing cash-flow problems because of a decline in demand for products and services. Second, businesses are holding on to their cash reserves instead of timely paying certain vendors because of the uncertain economic future. Even the largest companies are feeling the effects of reduced cash reserves and trimming expenses.

As a rule, businesses have always prioritized payments of bills to vendors. Businesses that are having cash-flow problems are forced to take prioritization much more seriously. This includes companies with historically strong balance sheets.

Their first priority is making sure that payroll, taxes, communication costs, utilities, and office space leases are paid monthly. Next in line are vendors that provide continuous products or services, such as equipment leasing and office supplies. These payments can be delayed for a period of time without an interruption in services.

Last to be paid are bills for services perceived as nonessential to the operation of a business. Whether lawyers like it or not, this includes legal bills. For many business clients, legal bills simply do not carry the same urgency as others. What's more, clients have come to expect that they will suffer no consequences for not paying their legal bills on time.

Firms have conditioned clients to believe that they can pay at their convenience without penalty. Many firms do not remind clients on a monthly basis that payment is expected.

Therefore, clients do not feel obligated to pay promptly. The problem is compounded when lawyers fail to recognize the point at which they should stop doing work for a client in arrears, and instead let the meter keep running.

Clients often hide their cash-flow problems with delaying tactics in order to gain more time to pay their legal bills or avoid paying them altogether, such as:

- Misplacing bills and requesting additional copies,
- Saying that others in their organizations must review the bills and approve payment,
- Questioning services provided, and
- Requesting backup documents.

Noninstitutional clients, too, are often unprepared to pay large legal bills. For individuals, household budgets have become even tighter and, like institutional clients, they must pay what they see as their fixed costs, such as mortgages and car payments, before tending to other bills. The average person doesn't understand the time and process that a legal matter requires. These first-time buyers of legal services often have sticker shock when they receive bills for legal services, and are unprepared to pay them.

SHORT-TERM SOLUTIONS

Now is the time to make sure that 2001 turns out to be financially rewarding for your firm, even though it's been tougher for most firms this year. One way, of course, is to keep the new work coming in. Equally important, though, is making sure that the firm gets paid for the work it has done.

Where do we start? First, to ensure strong collections for the rest of the year, identify attorneys and practice areas that traditionally have particular difficulty collecting their receivables by year-end, and determine if the soft economy will add to the problem this year. Ask all attorneys to candidly classify receivables as collectable by year-end, problematic, or not collectable by year-end. If accounts are going to be paid by year-end, require attorneys to specify how much their clients are prepared to pay, along with dates that payment is expected for each account.

What kind of information should we be looking at, going into year-end? Aged accounts receivable is a moving target and must be reviewed weekly to ensure that progress is being made. Although attorneys should be frequently looking at their aged accounts receivable report, it is more important for them to understand the payment trends of their clients. To help, firms should generate a list of clients that typically pay their bills during the last 60 days of the year, and find out if these clients are again anticipating paying in full this year-end.

Also, get your arms around your receivables by determining which clients make up the largest dollar amounts of all accounts. Then get the payment history of these clients to find out how quickly they have paid previous bills throughout the year. For those clients that normally pay over 45 days, cash flow may be even tighter and therefore require more frequent collection efforts.

REACHING OUT

What's the best way to approach clients about payment? Whether it's the first or last month of the year, the best results will be obtained by using the telephone. Unlike phone calls, letters can be ignored. Collecting receivables from law firm clients requires direct contact. Remember, clients are not offended by tactful inquiries. You can be sure that they are receiving phone calls from other vendors to whom they owe money.

When talking to clients about payment, attorneys should be prepared to discuss additional work to be performed up to year-end and the expected timing of payment for that work. Getting clients to pay is a process that must be approached in a diligent and timely manner.

LONG-TERM SOLUTIONS

More and more law firms are beginning to prequalify new clients by reviewing their credit reports and detailed financial information. Firms must learn to evaluate prospective clients to determine if they can and will pay their bills. Many clients simply do not have the income to pay even relatively small legal bills. Others can handle the initial costs, but don't have enough cash flow to pay later, when fees and expenses grow larger than

anticipated. Then there are those who have the means to pay, but are unwilling to do so in a timely fashion. If the matter will require a significant amount of time and out-of-pocket expenses, it is especially important to get a credit report.

What is a good strategy to make sure receivables don't age past 60 days?

- Provide clients a range of legal costs for the initial stage of the engagement. Make sure the lawyer and client share expectations about the amount and kind of work that will be done and the anticipated costs.
- Learn how to use a retainer and don't continue to perform work unless the client pays timely. An attorney who requests a retainer and then applies it to the first bill is not using a retainer properly. All retainers should be held until the end of the engagement, with payment of invoices expected upon receipt. Also, a good test of the client's ability and willingness to pay for your services is whether they can and will pay a retainer.
- Establish credit thresholds: How much time and expenses can a client incur before work is stopped?

Don't make the mistake of thinking your firm can collect itself out of receivables problems. Taking decisive action to collect aged receivables will help cash flow in the short term, but without fundamental changes to prevent collection problems, lawyers will quickly return to their bad habits and the firm will find itself in the same dilemma down the road.

Solving collections problems requires long-term remedial changes. The first and most important steps are to evaluate your client/matter intake process and identify problem receivables early on. Although a weakening economy can hurt law firms in many ways, it will especially hurt those firms without proper client intake procedures, efficient billing methods, and timely collections.

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