

Financial Fundamentals

The Budget: Your Firm's 'Secret Weapon' for Better Collections

BY ED POLL

All companies do some type of planning. Global multinationals typically have detailed written plans, while smaller companies may have a "plan" in the head of the entrepreneur. Budgets are the essence of a successful plan, and any business can and should operate according to a budget – whether you're making widgets or providing professional services.

Unfortunately, lawyers too often tend to dismiss the importance or even the practicality of preparing a budget. Typically there are three reasons for this:

- Lawyers believe that providing their services depends on too many variables that can't be anticipated – for example, what motions opposing counsel will file, or what problems might turn up when doing due diligence.
- Lawyers want to excel at what they do, whether it's negotiating a deal, drafting a contract, or litigating. They don't want the quality of their services to be constrained by budget limitations.
- Lawyers fear to some extent that budgeting a matter is merely an attempt on the client's part to reduce the fees that the client is willing to pay.

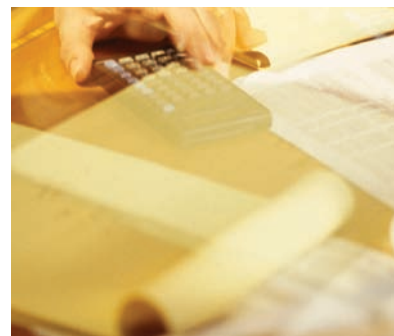
WHAT CLIENTS EXPECT

If clients, and especially corporate clients, ever accepted such reasoning, they certainly don't today. General Counsel clients report to a CEO who understands budgeting and whose life is governed by budgets. General Counsel insist that today's business environment requires budgets for their departments and the matters they handle. That includes every major litigation and transaction. Your firm as outside counsel must understand this requirement, or the General Counsel will get someone who does.

Several years ago, I interviewed a multinational corporation's General Counsel who expressed the corporate perspective quite succinctly: "[We aren't] just looking for a discount. We actually want to pay firms a higher effective hourly rate. We just want [our purchase] conditioned upon the firm's performance. Performance is a factor of many different things: communication, satisfaction of our business objectives, use of technology, overall knowledge. ... Firms should embrace that [because] they live in a world that favors and rewards continuous improvement."

REASONS FOR BUDGETING

In reality, preparing a budget at the start of any matter ensures greater



Failure to communicate often means failure to get paid.



The more information the firm can provide in a bill, the more likely the client will be to understand the value of the work performed, to perceive the bill as fair, and to pay it promptly.

productivity and cost effectiveness for both sides. A budget can only be an estimate of what's going to happen. The lawyer should not strive for the highest possible fee, and the client should not desire the cheapest lawyer in town. Creating a budget shows clients – whether they are individuals, small businesses, or corporate counsel – that you are sensitive to their needs, and it reinforces that you are providing a service of value and not just a block of hourly time. Also, by making a budget that addresses events, time and money as part of every engagement letter, you significantly increase the chances of collecting your fee because the client knows what to expect.

WHERE TO START

A law firm must understand its costs initially before settling on the way it wants to budget for an engagement. The elements to discuss with a client – essential for determining desired outcomes and tracking progress – may include:

- identification of goals to be achieved;
- current status of the project or case;
- complexity of the project or case;
- number of parties involved;
- documents to be generated (drafting responsibility and expected number of drafts);
- extent of travel anticipated;
- extent of work to be done by in-house and outside counsel;
- extent of expected negotiations/discovery; and
- the staffing plan for your firm and other firms that may be involved.

This process aims to secure as much information as possible from the client about goals and expectations. Understanding the client's objectives is essential to defining the budget and payment obligations for the engagement.

A COLLABORATIVE PROCESS

The key here is not just preparing the budget, but

also involving the client in its preparation and allowing the client to formally approve it. Without client buy-in, the process is meaningless. The budgeting process, including all subsequent communication, must be a collaborative effort. If the parties can't trust one another, or if the client and the lawyer behave as adversaries, the representation will likely be unsuccessful, and there will likely be difficulty in collecting the fee. Collaboration means communication. Because a lawyer and client may have unique information at any given time, both must advance the process together.

No lawyer wants to lose control and direction of an assignment, but accepting informed client judgment can sometimes be essential for effective budgeting. Several years ago, an in-house counsel for a major multinational corporation told me that once she saved her company nearly half a million dollars in one litigation when she suggested that the budget reduce by almost 50 percent the number of depositions that outside counsel wanted to take. The law firm was concerned about potential accusations of negligence or malpractice if one of the canceled depositions proved to be a key information source. The client responded by accepting responsibility for the reduced depositions if something went wrong, calling it a reasonable business risk. The result was agreement, lower costs, and a successful engagement – the objectives of any budget.

PARAMETERS OF TIME, MONEY, AND FORM

The client's objectives should define three crucial budget parameters: time, money, and form.

- **Time.** Use common sense, be realistic, and communicate accurately about the amount of time it will take to complete any work. Err on the side of caution, and be sure to build in more than adequate time. Except when you are dealing with statutory or deal-making deadlines, the client is less concerned with exact time and more concerned about being hit with surprises.

- **Money.** Clients should have in mind how much money they want to spend to resolve a problem, just as they know what they want to spend on a piece of equipment. In either case, a higher initial cost may be acceptable if the long-term return on investment justifies it. Sometimes a legal problem is large enough that spending a big sum is justified. Most issues, however, involve everyday costs of doing business. It makes no sense to budget spending \$2 million to try a case if a \$100,000 settlement will meet the client's objectives.
- **Form.** It's important to know the physical form in which a client wants to receive and monitor a budget. Some clients may prefer an Excel spreadsheet, others a simple text document. A good rule of thumb is to find out how the client's operating budget is set up and then try to integrate with it. Providing budgets and budget communication in a format that's difficult for the client to use defeats the collaborative nature of the process.

THE IMPORTANCE OF COMMUNICATION

Once the client formally approves the final budget, all subsequent communication about it must continue to be collaborative. Because a lawyer and client will possess unique information at any given time, both must be in constant communication about developments to keep the budget on track. The budget document should be periodically reviewed, with the client being told how much it has already spent and being asked to approve any necessary changes.

Failure to communicate often means failure to get paid. A large law firm once engaged me to help end its write-offs of litigation fees for two clients. I suggested creating a flowchart of the litigation process to determine where and how much the client had really been involved. Ultimately, there were very few points at which these clients were informed about what was happening in the case. When the final bills came, they were shocked at the large amounts and refused to pay. The lawyers defended themselves by saying, "I talked with the client frequently. We were preparing for depositions and constantly asking for documents." But, that's not the kind of interaction that gives clients the understanding of where their budgets stand. Honesty, openness, and candor will make the

budget understandable and the entire representation easier and more successful.

THE BUDGET AND THE BILL

Ultimately, the greatest benefit of budgeting an engagement is that the budget provides a benchmark for the firm's work as it is completed and billed. Although the main purpose of your bill is to make sure you get paid, there is a secondary purpose that lawyers often miss: to inform the client with a favorable impression of the services received. In other words, your bill is another tool for client communication.

A bill that shows work performed in the context of constant budget communication is one that speaks clearly and directly to clients. The more information the firm can provide in a bill, the more likely the client will be to understand the value of the work performed, to perceive the bill as fair, and to pay it promptly. A bill that describes promises made and kept, complete with examples of value and service as defined by both parties in the budget, will be most meaningful.

Too many lawyers make the mistake of brevity when billing – for example, "work on motion for summary judgment, 20 hours." Break any such charge into its basic elements, with the amount of time needed for each: review key documents and deposition testimony, draft statement of uncontested facts as required by court procedure, research precedents in four similar cases, and so on. Such itemization does not try clients' patience; rather, it helps them understand just how much you did on their behalf and relate them to the budget. Clearly indicating the specifics of what was accomplished closes the budget loop and helps clients appreciate the effort required for success. *

about the author

Ed Poll is the author of 11 books, including *Attorney & Law Firm Guide to The Business of Law, 2nd ed.*; *Selling Your Law Practice: The Profitable Exit Strategy*; and his newest, *Disaster Preparedness & Recovery Planning for Law Firms: A LawBiz Management Special Report*. Contact him at edpoll@lawbiz.com or (800) 837-5880. Visit his Web site, www.lawbiz.com, to subscribe to his free monthly newsletter, *LawBiz Tips*, or his blog, www.lawbizblog.com.