
Summary: Is your law firm bringing in as much profit as possible? Take these steps to improve your law firm's profitability.

As if lawyers, be they associates or partners, aren’t under enough stress, as these attorneys practice inside large, prestigious law firms, they have to be aware of, and at times are dictated by law firm profitability.

According to Law Practice Today, law firm profitability is a critical management task that influences strategic management decisions. However, while profitability is easily defined, traditional law firm partnership financial reporting models are not easy to analyze or compare within the legal industry.

As convoluted as this definition may seem, partners nevertheless understand that a good part of law firm profitability depends upon how much business they bring into their law firm. Or, if there’s a large financial influx into the firm from a won case, that as well would contribute to that firm’s profitability.

Most businesses define profit as assets gained after its expenses are subtracted. The corporate world measures profitability through a system of a price-to-earnings ratio in which the stock price is divided by earnings per share.

As direct as this is, particularly to individuals who own stock in a company, this type of profitability model is not what law firms use. That’s because law firms are traditionally structured as partnerships and are privately held. Additionally, law firms don’t come under the same profit-oriented regulations and investor reviews as corporations. This is because law firms are not:

- Publicly held entities.
- Not invested into by investors.
- Are not corporations in the traditional sense.
Conversely, law firms are:

- Led by legal partners within the firm’s partnership.
- Privately held.
- Entities that gain profit from ongoing business and retainers.
- Entities that gain profit via large legal settlements.

**Who benefits from law firm profitability?**

In most cases, partners are the first people inside law firms who share in the firm’s profit. The profit is first divided among the partners while associates may or may not share in the firm’s profits by way of bonuses.

The law firm itself can also benefit from a law firm’s profitability through:

- Created value.
- A greater ability to cover costs.
- The firm can now assume greater risk.
- The law firm overall makes money.

Law firm profitability further proves that firms have evolved into true businesses, even though they don’t operate in any way like a business. There’s no product other than the lawyers themselves and how they represent a client or case. Even so, having clients can in ways resemble a large corporation that has public stock investors.

While investors buy increasing numbers of shares in a company, a law firm’s investors are the clients themselves who pay for the firm’s legal services. In fact, as that client’s legal work grows, leading the client to put one or more of the firm’s attorneys on retain, this, in a strong way, can resemble traditional corporations as on a monthly or quarterly basis, that firm bills the client for its “standby status” that is associated with retained attorneys.

**How is law firm profitability calculated?**

According to Law Practice Today, law firm profitability is calculated this way: A law practice with 20 attorneys and $10 million in revenues, where one firm has ten equity partners, while the other firm has limited their partner rank to only the five leading partners with the other five considered non-equity partners (reported as expenses before net income), will have drastically different expenses and net income even though every single person in the two firms could earn the same amount. The law firm with ten partners may have net income of $5 million while the firm with five partners may only report net income of $4 million.

**Which firms are most likely to benefit from law firm profitability?**

To be sure, all firms benefit in some way from law firm profitability. Law firm profitability can help retain important partners as well as those partners’ clients, which benefits the entire firm.

High-yield profitability can also attract outside attorneys who themselves have a strong book of clients.

But the firms who are most likely to benefit from law firm profitability are the large and prestigious firms simply because they are the ones that are getting higher-margin cases such as wealthy estates, or large ongoing corporate-related legal issues for which attorneys are more than likely retained.

**If a law firm has fewer partners, are there more profits to go around?**

Law firms with only a few partners don’t necessarily mean that the firm’s profitability will be distributed more evenly. This is because within most legal settings, the fewer partners a firm has, the larger slice of profit pie those attorneys will take for themselves.

If a law firm has many more partners, the formula remains the same, but the slices of pie are thinner than if the firm had fewer partners.

As for associates, they might still get a bonus, but much depends on the law firm’s politics and cultures. More likely than not, an associate will simply be left to share in the firm’s new-found glory.

**Law firm profitability seems like it is highly leveraged?**

While partners control how a law firm’s profits are distributed, it’s part and parcel to think and believe that the system of law firm profitability is highly leveraged – because it is.
Like a pride of lions in which the biggest and most ferocious male eats the kill first, the biggest and most important partner, usually a founding partner, receives the largest cut of a law firm’s profits.

**So how do most law firms increase their profitability?**

There are several ways law firms can increase their profitability. Listed here are the most popular methods that leading law firms utilize to broaden their bottom line.

- **Improve your law firm’s systems.** Document your law firm’s routine for each case its attorneys handle. Then use this system to safeguard against potential snags and mistakes that can limit the profits your law firm can make. Having the correct systems in place will not only allow you to get more done, but it will also make it easier to delegate work to an associate or other employees.

- **Maximize your law firm’s profitability.** Explore every route possible to find out where you can maximize profitability. Make certain all your firm’s billable hours are being properly submitted and billed in a timely fashion.

- **Make certain your attorneys don’t leave billable hours on the table.** In some cases, billable hours are lost to a lack of accurate billing. Require your attorneys to occasionally review their billing process to make certain they’re properly charging for their work.

- **Look into new practice areas if possible.** Some law firms simply can’t see the forest for the trees. In large law firms, attorneys who specialize in niche practice areas can easily be overlooked by others in the firm. Maximize the potential of all your attorneys to make certain each is either bringing in business or billing within their practice area.

- **Recruit attorneys who specialize in practice areas that aren’t your firm’s specialty.** An interesting method to increase profitability is to expand your law firm’s practice areas. Keep an eye out for new and emerging practice areas that your law firm can involve itself in and make an increased profit from.

- **Have your attorneys market themselves as well as your law firm:** The best way to increase profits is to let the consumers know you’re in the game. hone and extend your marketing efforts with better brand advertising. Also, consider showcasing your attorneys at special events and meetings.

- **Avoid bad clients.** There can be many ways a client is so-called bad. They don’t pay their legal fees on time or put a law firm on retainer just to keep them available, yet not supply the firm with ongoing work that can be billed.

- **Raise your rates.** Sure, rates can be a touchy subject for both an attorney and a client, but sometimes it’s necessary to maintain profitability. Do not leave money on the table. Going years without increases to their fees, which can eventually have an ill-effect on their businesses. Remember, the last thing you want is to put your law firm in financial risk. If you need to raise your rates to keep your doors open, then do so.

- **Bill accurately and often.** Billable hours are the life’s blood of a law firm. Without billable hours, you may as well pack up and hit the rails. Set up a system in which your lawyers don’t fall behind on their invoices. Encourage them to send out their invoices on a monthly basis to keep a constant flow of assets coming into your law firm.

- **Be vigilant about billable time.** Encourage your attorneys to stay on top of their billings. Have them note down every half-hour they spend with a client and his or her case. It’s face-to-face, on the phone, by email or any other interaction. It’s only fair to do this, particularly if your attorneys are involved in strenuous cases.

- **Ask for client feedback.** Are your attorneys’ clients happy with the service they were provided? Will they return if they have more legal issues and will they recommend your law firm to other prospective clients? You will only know this if you ask your clients for feedback.

- **Double check your expenses.** Is there wastefulness inside your law firm? Is someone not holding their end up, costing you both time and money? Do you, your lawyers and your law firm a favor by identifying wasteful portions of your law firm which you should immediately eradicate.

- **Have new and existing clients pay in advance.** This might be awkward for some. However, it is very important to keep money coming into your law firm. After all, you have expenses too, such as paying the attorney who just asked his new or existing client to pay in advance.

**Metrics that should be followed while going forward.**

Now that a baseline has been established for you to follow as you attempt to increase your law firm’s profitability, you should keep an eye on the following metrics which can reflect the financial health of your law firm. These are:

1. **Cost of servicing a client.** How much did Client A, B, and C cost you? Have your attorneys keep detailed records of every single bit of effort they put into a client’s case. You don’t want to lose out on any finances owed to your firm because your attorney forgot to bill for a portion of the services rendered.

2. **Measures of profitability.** How well your practice areas are doing. If one is inordinately low in profitability, maybe it should be analyzed a bit more closely. Also look into the following:

   - Firm profitability
   - Profitability by practice area
   - Profitability by partners
   - Profitability by client
Profitability by timekeeper (all levels)

Some say the profits measure in law firms is meaningless: If they say this to you, wholeheartedly ignore them.

It’s been long since established that law firms are more businesses than establishments where the law is practiced.

This is true.

As law firms evolve into entities that give financial and estate advice, as well as the usual corporate and litigation support, they’ve seemed to spring up a partnership with consumers that haven’t run this deep in the history of law.

But since law firms are, in a strong sense, businesses, those businesses need to have income, or they’ll very quickly die off.

While all law firms are different, and depending upon their practice area, cannot follow the same business model as another law firm, the guidelines above are still very broad, and can be applied in almost any legal practice.

Follow the guidelines above to ensure your firm has enough incoming profitability to keep the associates and partners happy, but most importantly, the doors to your law firm open to whoever needs legal assistance.

See the following articles for more information:

- The Sources Of Revenue And Profit For Attorneys And Legal Firms
- Pay to Win—How to Make Your Law Firm's Compensation System an Asset
- Self-delusion among Law Firms