USING KPIs EFFECTIVELY: IS YOUR FIRM MEASURING WHAT MATTERS?

By Mary Juetten

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I have written before about key performance indicators (KPIs) for the law. My main message has been that like other techniques and technologies, running a law firm is a business and therefore, measurement is critical for success. KPIs are universal and apply to the legal profession regardless of firm size.

Breaking from traditional KPIs that focus on the lawyers' input or time metrics, I believe measurement should start with the client and also zero in on collections rather than only hours. The main reason for business failure is a lack of cash, which is caused by a shortage of clients, poor billing and collections results, or a combination of both.

In June 2016, Thomson Reuters surveyed small law firm customers on KPIs and benchmarking to support my book on *Small Law Firm KPIs: How to Measure Your Way to Greater Profits*. The purpose of the survey was twofold: to better understand if and how small law firms measure and track KPIs and also to gather information on technology usage by those firms.

The survey went to approximately 690 firms. The 62 responses included 10 solo practices. The remaining respondents were divided as follows: roughly 50% had fewer than 10 attorneys; about 25% had between 11 and 20 lawyers; and about 25% had more than 21 attorneys.

More than half, 36 respondents (58%), reported that they do not use KPIs beyond the traditional hours-billed metric. Relying on that traditional KPI is not sustainable because clients are demanding more for less as well as the ability to rate satisfaction with your services. Some of these concepts are new to the legal industry, but not to in-house counsel or consumers, who see KPIs in their business and everyday lives.

Only six firms of the 26 that used KPIs other than hours-billed used more than four different metrics. These alternative metrics included:

- Client experience or satisfaction
- Cost of client development or acquisition
- Pipeline dollar value per attorney
- Aged or overdue accounts receivable
- Collected billings by attorney
- Matter profitability
- Budget versus actual or opened matters

Here's the breakdown of all nontraditional KPIs used by those 26 firms:

- 19 respondents tracked *collected* billings by attorney
- 15 firms measured overdue accounts receivable
- 14 respondents tracked matter profitability
- Three firms (under 5% of total respondents) measured client satisfaction

That last statistic shows the opportunity for firms that start measuring client experience. By moving beyond hours and utilization, you can discover which matters are the most profitable and understand what your clients think about your offerings. Knowledge truly is power when it comes to business metrics, particularly when they impact firm profit.

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When asked whether firm profitability has grown over the past two years, 48 (77%) of the responding firms said yes, with 16 of those firms citing growth of more than 20%. However, of the 14 firms without any profit growth, eight did not use KPIs. Specifically, four of the five firms that had two or three attorneys did not use KPIs and had not experienced any increase in profits.

Finally, the answers for the use of practice management, billing, or accounting software products were also surprising. Fifty firms (81%) responded in the affirmative. Twenty-one (34%) of respondents reported using various time and billing software only. Another 27 (44%) indicated their use of a practice management system which, in some cases, includes time and billing capabilities. Technology adoption is an important step towards simplifying administrative practices and for gathering data for KPIs.

It's clear there's room for implementing a wider range of KPIs, and that's possible without having to adopt new technologies. Many of the newer KPIs that have to do with client experience and firm culture do not require technology beyond Excel®. My next post will address client KPIs that will improve your firm's bottom line.

Lastly, this gap in KPI knowledge and action is not unique to the small law firms – big law is experiencing it, too.

INCREASING REFERRALS WITH HAPPY CLIENTS

The Thomson Reuters 2016 State of U.S. Small Law Firms Report released earlier this year showed that small law firms consider client service ratings to be important along with both matter and bottom-line profits. However, as I mentioned before, you can get some insight from the results of a small firm KPI survey where less than 5% of respondents measured client satisfaction.

I believe that happy clients that refer other clients ultimately generate more revenue in any industry; therefore, I want to focus on client metrics that will in turn increase your firm's profits.

A legal clients' experience should be regarded and measured like any other customer and provider exchange. Not only are law firms of all sizes businesses, but KPIs apply globally, meaning that measurements translate in all countries. In the U.S., law firms tend to focus on inputs or what the firm's lawyers can do for clients, rather than asking the clients for feedback. Anecdotally, lawyers fear that clients may rate them based on the outcome of their case rather than on the service or experience.

However, in our daily lives we are often asked to give feedback on our experience when we purchase hotel rooms, flights, shoes, and so on. Sometimes, it's as simple as indicating whether you were happy or unhappy with the product or service; but at other times, you're asked to rate the experience using a numeric scale. At a recent small law conference, I asked an audience of more than 100 attorneys how many had been surveyed for feedback and close to 100% responded positively. I recommend using the client experience metric Net Promoter Score (NPS) because your clients are familiar with this approach.

An NPS survey asks existing or former clients how likely they are to recommend your firm to their friends and family or colleagues, depending on your client base. The answer to that question is a rating on a scale of 1 to 10 with a 10 being extremely likely to recommend. A 9 or 10 is a promoter; a 7 or 8 is neutral, which is ignored in the NPS calculation; and 6 and lower is a detractor.

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The survey can be done at the close of an engagement but it is not limited to that timing and must not be done anonymously to allow for follow-up. SurveyMonkey or Google® documents can be used to email the survey, and follow-up can be done by administrative staff. An Excel spreadsheet can track the firms' results.

In the example from my book, *Small Law Firm KPIs: How to Measure Your Way to Greater Profits* (Figure 1), in one month we had 22 responses and the results were 9 promoters, 8 neutrals, and 5 detractors. The calculation is simple math as outlined in the chart below, taking the percentage of promoter responses and subtracting the percentage of detractor responses.

NPS CALCULATION		
Promoter (9 or 10)	9/22	41%
Neutral (7 or 8)	8/22	N/A
Detractor (1 to 6)	5/22	23%
Promoter – Detractor		18%

Figure 1

The NPS in the chart above is 18%, but note that the NPS could be a negative number if you had more detractors than promoters. What does the 18% mean? Some may wish to know how that stacks up against competitors' results. In research done by survey firm Inavero, the average NPS for the legal industry in 2016 is 23. It's interesting to note that many think of success as being above 50% or an NPS target of 75% or above. Remembering that you are working with a possible result from negative-100% to positive-100% helps to put the 23 in perspective. However, the number alone may not be enough. Instead, consider asking the client "why or why not?" along with the NPS survey question.

Collaborating and working well with a client requires soft skills like communication and project management. Clients desire polite, timely communication and efficiencies through technology. No one wants a surprise either in terms of outcome or billing. The NPS survey with the "why or why not?" follow-up question gives a law firm the opportunity to check how it's doing and make needed changes based on the feedback. Another complementary measure to NPS is to track the source of your new business by measuring new clients that come from referrals as a percentage of total new clients. It's easier to either sell additional services to existing clients or potential customers who are referred.

Finally, measuring client experience applies equally to big law, and today several large law firms are gearing up to measure NPS. As mentioned in my first post, these newer KPIs around client experience and client acquisition costs do not require sophisticated technology solutions.

IMPROVING THE BOTTOM LINE

Previously we explored key performance indicators (KPIs) for measuring client experience with legal services. Satisfied clients increase revenue but many firms still fail because they do not pay attention to the business of timekeeping and billings. Recording hours, billings, collections, and cash flow are all critical to business and therefore, to a firm's survival. Now, I would like to focus on KPIs around collections that could increase your firm's profitability.

Small law firms consider both matter and bottom-line profits to be important according to the Thomson Reuters 2016 State of U.S. Small Law Firms Report. However, as outlined in my first post in this series, the majority of firms surveyed on KPIs rely on bank balances or take-home dollars at the end of the month to measure profitability. Based on this information, I infer that a majority of firms are looking backwards when it comes to results.
Not only is it too late to take corrective action if you wait to see how the month turns out, but a bank balance does not accurately measure profitability. Digging a bit deeper, we see that 18 of 31 law firms surveyed – which includes firms from all size groups – do not track KPIs. However, there is still time to set up your firm's KPIs to measure and improve collections for 2017.

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Traditionally, a firm pays staff and bills with some type of regularity, all likely within 30 days. Therefore, a firm's accounts receivable (A/R) collections need to be at least within the same time frame to avoid running short on cash. Using an example [from my book, *Small Law Firm KPIs: How to Measure Your Way to Greater Profits*], we calculate the average lockup days, which is a measurement of how long your cash is tied up from the date of time-recording to billing and ultimately to collections. The period between the time being recorded to actual billing is work-in-progress (WIP) lockup and the period from billed to collected is accounts-receivable (A/R) lockup. The law firm in the example below (Figure 2) has cash locked up for a total of 41 days on average, with 21 as WIP and 20 as A/R.

PROF PI 2016	JAN
4-PROF(g)WIP Lockup Days (#)	21
TARGET – WIP Lockup Days (#)	30
Input – Total Unbilled Time for the period*	$407,500
Input – WIP balance beginning of the period	$320,000
Input – WIP balance end of the period	$275,500
*Includes the outside costs and fees	

PROF PI 2016	JAN
4-PROF(h)A/R Lockup Days (#)	20
TARGET – A/R Lockup Days (#)	15
Input – Total billings for the period*	$500,000
Input – A/R balance beginning of the period	$125,000
Input – A/R balance end of the period	$531,250

Figure 2

Alternatively, you can start with a KPI that looks at the aging of both the WIP and A/R in total to check whether you have an excessive dollar value outstanding over 30 or 60 days. Although target lockup days vary by firm, best practices would be to bill out as much WIP as possible within the same month as it's recorded, and collect A/R immediately or within 30 days. Remember, your bills are due within a similar time frame and borrowing money incurs interest payments that will only eat into your profits.

Also, a final word on collections and compensation. In the KPI survey mentioned earlier, 18 of the 58 firms surveyed are looking at some metric of cost vs. budgeted or expected revenue, which is a good start when measuring profitability. However, when the same firms were asked whether all the timekeepers had financial goals, only half answered "yes." It's hard to measure and reward profitability if there's no accountability.

To illustrate the necessity of alignment between timekeeper and the law firm's financial goals, we have an associate "Allan" who is recording hours and billing well above 100% traditional utilization, and thinking that he is deserving of a bonus at year's end. However, some of his billings have to be written off at the end of the year as shown in the chart below (Figure 3). Allan has missed his target by 12% which, at a billing rate of $160, translates into about $41,000 of write-offs or lost cash. If Allan understands that his performance will be scored based on *collections* rather than *utilization*, then he will not be surprised when his bonus is negatively impacted.

ALLAN	$160
S-PERF(a) Billings Collected by Attorney	88%
TARGET – Billings Collected by Attorney	100%

Figure 3

One important caveat is that I am not suggesting that timekeepers should stop recording hours – that information is invaluable for pricing, including determining billing rates and flat fees.

It's clear that there is room for implementing a wider range of KPIs for profitability, and that's possible using existing software solutions regardless of firm size or geographic location. In fact, many of the newer KPIs do not require technology beyond Excel.

CREATING AND TRACKING METRICS

We have come full circle in this white paper on the best use of key performance indicators (KPIs) by returning to client metrics, this time with an emphasis on client development KPIs. Often attorneys do not believe that prospecting and marketing to potential clients is the same as sales and marketing efforts that occur outside the legal profession. Other than important ethical advertising considerations that should not be ignored, there is much to be learned from business development practices outside the law.

In our example above, we discussed a KPI survey of 62 firms, where 36 measured hours, collections and billings, but only 25% of those firms tracked the number of new clients. New clients bring in new revenue, so collecting that data allows you to best evaluate your marketing and business development efforts. In addition, only about one-third of the firms tracked pipeline value per attorney and cost of client acquisition. There is room for more KPIs within legal, and that's possible without having to adopt expensive technologies. Many of the newer KPIs discussed here do not require software beyond Excel. Now, we will examine creating and tracking some client development metrics, including the potential client pipeline.

First, it is important to take a holistic approach to the metrics because KPIs are interdependent within an overall framework that follows the workflow and processes within a firm. In the same survey mentioned above, only six of the 26 firms that used KPIs for measurement other than traditional utilization, used more than four KPIs. Therefore, while a pipeline KPI is important, there are other measures such as client conversion and referral rates that monitor client development efforts. In a similar fashion, client development KPIs are not the sole client metrics. Client experience and the cost of client acquisition KPIs should also be tracked to optimize use of limited firm resources. Measuring the effort to attract new clients and their value to the firm is fundamental to profitability. Also, it's risky to focus only on one KPI area.

We look to the business world for an example of using a sales pipeline for monitoring the amount of incoming client business to ensure that overall firm revenue targets or budgets will be met. An overall caveat is that creating and maintaining a client pipeline is more of an art than a science because of the estimates that must be made.

Below is an example of a family law firm pipeline from my book, *Small Law Firm KPIs: How to Measure Your Way to Greater Profits* (Figure 4). Note that it is built up using Excel. Some customer relationship management (CRM) systems produce a pipeline, but it's helpful to understand the basics. Using Client 6 to illustrate: The *$ Value* is the projected fees to be earned which are set at $25,000. The *Go* represents the likelihood that Client 6 will actually go forward with the matter and the *Get* is your chances of getting the work. The *Adjusted Value* is the $25,000 multiplied by the 25% Go and the 100% Get.

PIPELINE EXAMPLE – MARCH 2016

Family CD	$ Value	Go	Get	Adjusted Value
Client 1	$1,500	50%	50%	$375
Client 2	$5,000	75%	100%	$3,750
Client 3	$5,000	75%	50%	$1,875
Client 4	$10,000	100%	100%	$10,000
Client 5	$1,500	100%	25%	$375
Client 6	$25,000	25%	100%	$6,250
Total	$48,000			$22,625

Figure 4

While the math for Adjusted Value is simple, arriving at $Value, Go, and Get can be challenging. If you do not have a discrete menu of different services, flat fee packages, or an estimate of how much revenue each client will bring in, do your best to make some estimates based on past history. For Go and Get, limit the options to 25%, 50%, 75%, and 100%. Think of Get in terms of the number of others competing for the work. If the competition is between two firms, but you think the competitor has a better chance, then use 25%; or, if it's a draw between the two firms, 50%. Again, these are estimates. The objective is to compare the Adjusted Value to your budgeted revenue for the upcoming period to see whether you need to adjust your client development efforts.

It bears repeating that you cannot look at just one measure, even within a KPI category like client development. Tracking metrics such as which potential clients retain your firm in comparison to the total clients that you are prospecting will give you information to refine your pipeline and also direct your scarce marketing resources.

Lastly, KPIs are not limited to small law firms or only to the United States. The small law principles and framework can be applied to all sizes of firms everywhere.

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Mary Juetten is founder and CEO of Traklight and has dedicated her career for more than 30 years to helping businesses achieve and protect their success.

Juetten is an international writer, speaker, and mentor. In 2015, she cofounded Evolve Law, an organization for change and technology adoption in the law. Juetten was named to the ABA's Legal Resource Technology Center 2016 Women in Legal Tech list and serves on the Group Legal Services Association (GLSA) board.

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