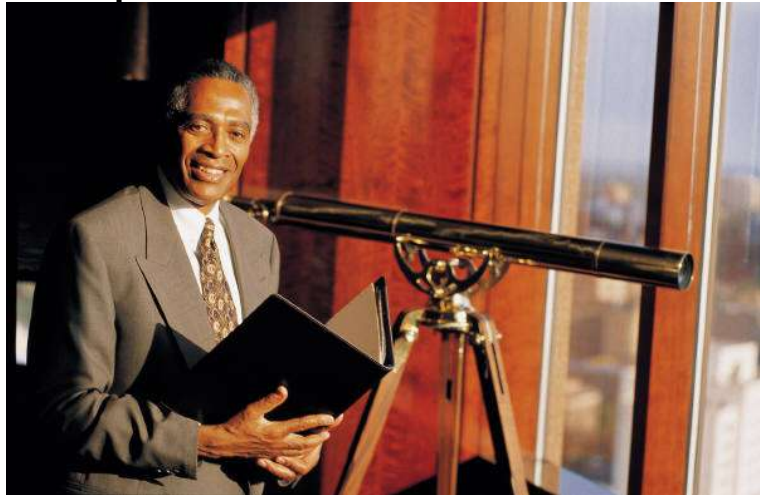


Frequently asked questions about

Starting your own law firm



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At some point in their careers, most lawyers seriously consider solo practice or starting a new firm. Each lawyer approaches this opportunity with a unique set of talents, aspirations, and resources. There are several critical questions that every lawyer should consider before taking this big step; and here are some general answers that Walker Clark consultants frequently offer.

How do I develop realistic financial expectations for my new firm?

There are two simple, reasonably reliable models to project the financial performance of a new firm:

Revenue-based model

This model starts with your expected fee billings and uses standard benchmarks to estimate operating costs and the net income to be distributed among you and your partners. The resulting point of analysis is “Will I be satisfied with the remuneration that my fee billings are likely to produce?”

Circumstances vary from location to location, as well as among various legal practice specialties. However, our firm’s experience worldwide and published law firm economic surveys suggest that the financial performance of a new law firm can be predicted with a reasonable degree of precision. We advocate a very conservative approach to cost budgeting, which will depress somewhat the take-home expectations for the partners of the new firm. On the other hand, careful cost management during the first year might also produce some pleasant year-end surprises, even after only one year of operations.

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To project costs and net income during the first 12 to 24 months of operations, apply these factors and planning assumptions;

- Expect to collect roughly 90% of your billed fees (but always try for 100%).
- At the outset, office occupancy costs can consume almost all of your fee revenue. You should reduce this figure to well under 10% by starting operations in a serviced office space in a business center.
- Equipment costs, not counting initial acquisition, will consume about 5% to 10% of fee revenue.
- Staff costs will consume 12% to 20% of fee revenue, depending on whether you need highly trained paralegals or assistants. You can also reduce this expense substantially by using temporary, part-time staff, or by using clerical and administrative support in a business centre.
- Avoid the temptation to overspend on marketing. Try to limit marketing costs to 2% to 8% of revenue, depending on how aggressively you use print media, direct mailing, and community events to publicize your new firm.
- Allow 2% to 4% of your revenue for reference materials.
- Plan an operating contingency fund of 20% of revenue to cover expenses such as non-capitalized startup costs, professional services fees, licensure, indemnity insurance, and minor expenses. After your first year of operation, you should be able to reduce this contingency to 10%.

These estimates will produce cost projections that will consume between 51% and 62% of revenue.. Barring any unexpected revenue developments, this will produce a net income ranging from as high as 49% to as low as 38% -- not too bad for a first year! Your ability to manage costs and meet revenue goals will determine whether you can achieve these projections..

Compensation-based model

This model starts with the basic question, "How much money do you need to take home?" It applies the same general cost assumptions as does the revenue-based model, but works from the bottom line up to arrive at a level of fee billings needed to fund your compensation goals. The end question is "Can I realistically expect to generate sufficient fee billings to meet my remuneration needs?"

We recommend that you develop both models, as an internal check on your estimates.

How much start-up funding do I need?

An oft-quoted rule is that it takes most businesses three years to produce enough revenue to generate a steady profit. Most startup professional services firms can expect much faster results; but we recommend that you have enough cash available to carry you (and your partners) for at least six months, even if you would not receive any fees. You should be personally prepared to live on a sharply reduced income for at least one year; and it could take two years or more before your personal income returns to previous levels.

Most new practices require three months – and some as long as one year – to develop a steady cash flow adequate to meet expenses and to begin to provide compensation to the owners of the firm.

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Your funding requirements will depend primarily on three things:

How many and which of your current clients will likely move with you to the new firm? Despite what they tell you before you leave your old firm, not all clients will go with you. It might take months for some matters to transition from your previous firm. As a result, you should not count on full cash flow from these clients for at least two months and, for some clients, up to six months.

When will you start receiving fees from new clients? As a general rule, the earliest that you can expect to see non-retainer revenue from new clients is 90 days.

What opportunities do you have to minimize startup costs? For example, it will usually be much less expensive to occupy space in a serviced business centre than to lease and furnish commercial office space in a comparable location. Use of a business center can reduce your facilities costs to less than 5% of revenue.

When will my firm need a web site?

Day One! Your clients will expect it, and even a modest web site will be the most cost-effective way to project your new firm into the market.

What are the most effective cost-management strategies for new firms?

It sounds like a cliché, but each law firm really is different. Your practice specialty, your clients, and the competitive characteristics of your market will determine where the best cost-management opportunities can be found. Here are three cost-management strategies that usually produce the greatest results during the first year of law firm operations:

Contract for office space in a serviced business center. You and your colleagues can lease top-class furnished and fully serviced office space for a fraction of what it would cost with a traditional commercial lease and furnishing the office yourself. With their menu of services, charged only on an as-needed basis, you can also better control administrative and clerical costs.

Avoid hiring full-time, permanent employees until you are convinced that you need more people all day, every day. Consider contracting temporary staff for part-time work until workload makes it more economical to hire your own employee. Serviced business centers frequently offer highly-skilled clerical support for very competitive hourly rates. Before adding additional lawyers and paralegals on a permanent basis, try contracted temporary personnel.

As a general rule, lease, don't buy. It is true that, in most instances, purchasing equipment is more economical in the long term; but leasing is usually kinder on your cash flow during the first one or two years.

How substantial are the non-economic investments?

There is an old saying that "Every law firm is only 180 days from bankruptcy." Even with clairvoyant planning and mounds of money, this will be a stressful time, filled with long work days and uncertainty.

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One commentator discusses this investment as follows:

No matter what your area of practice is or the amount of support help you will be able to afford when opening your own firm, you will be making a substantial time commitment to your new firm. Consider whether this is the right time to make a move for you, your family, your lifestyle, and your finances. If you are taking on partners or shareholders, make sure all of you have made the same time commitment to the new practice. To avoid any misunderstandings that may arise in the future, you may wish to make your agreed-on time commitment part of your partnership/shareholder/PLC agreement. (note 1)

Is there a good checklist for Day One of my new law firm?

Actually, we know of three that are very good. Requirements vary among jurisdictions; but here are three very useful internet links to checklists and other resources that will be useful to new law firms anywhere.

Florida Bar Law Office Management Assistance Service, "New Law Practice/New Office Checklist," Available at <http://www.flabar.org>. *This is a detailed form that also includes space for deadlines, responsibilities, and one-time and recurring cost information.*

Felicia Folk, Opening Your Law Office, Law Society of British Columbia (2002). Available at [http://www.lawsociety.bc.ca/services/Practice/docs/OpeningLawOffice\(02-01\).pdf](http://www.lawsociety.bc.ca/services/Practice/docs/OpeningLawOffice(02-01).pdf) *This is a compact (35-page) guide which emphasizes the importance of getting organized before you open. It also contains an excellent bibliography of other resources.*

Opening a Law Practice, Institute of Continuing Legal Education (Ann Arbor, Michigan, 2001). Available at <http://www.icle.org/nlc/2001TK3803.htm>. *This is an on-line kit of materials, with forms which can be downloaded in Word or WordPerfect formats.*

Notes

1. Heidi L. Salter-Ferris, "Opening a Law Practice," [Michigan Basic Practice Handbook, Fifth Edition](#) (ICLE 2001).

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