

## GERSTEIN LEGALTEC

# DRIVING BUSINESS PERFORMANCE WITH BUSINESS INTELLIGENCE

## A Finance Guide for Law Firms

A White Paper by Todd Gerstein

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### ***Introduction***

The term “Business Intelligence” (BI) was coined in the mid 1990’s and refers to the process of transforming raw data into useful actionable management information. Since data in its raw form is of fairly limited use, businesses are increasingly electing to use BI software to realize their data’s full potential. BI software allows you to easily aggregate, manipulate, and display data from multiple sources into actionable information, or information that can be acted upon to make informed decisions.

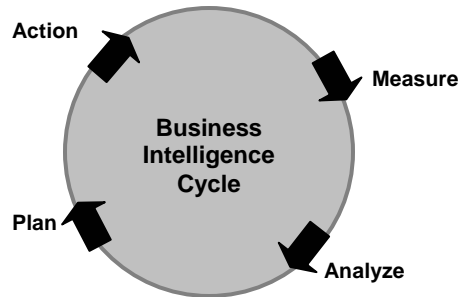
For example, let’s consider the data collected at a law firm. Tens of thousands or even hundreds of thousand of time transactions are billed and collected annually. Looking at this transactional data in its raw form, one could glean basic information such as how many hours were recorded for each client; what was the average rate; what was billed; and what was collected.

However, by implementing BI software, a law firm can turn its raw data into useful information to gain profound insight into its client base. Insights such as: which clients are profitable; which are not; what is causing the client to be unprofitable; and what can be done to rehabilitate the client’s profitability. By providing this type of window into vital information, BI enables law firms to drive performance.

*A law firm's most important decision-making metrics are called Key Performance Indicators (KPIs). These measures tell the firm the "what", i.e., "What is the status or health of the firm?"*

## **The Business Intelligence Cycle**

BI is a performance management framework, on ongoing cycle of four stages: Measure, Analyze, Plan, and Action.



### **Measure**

The hardest aspect of implementing BI is to define what information is useful and relevant to drive performance. BI solutions are charged with collecting and measuring a law firm's most important decision-making metrics called Key Performance Indicators (KPIs). These measures tell the firm the "what", i.e., "What is the status or health of the firm?"

KPIs become the building blocks for BI cubes. Not wanting to diverge in technical jargon let's call these cubes by their financial name, "Views." Views a law firm might include in a BI installation include:

- **Client Profitability:** How do you identify your most profitable clients? What is the most accurate method on an absolute dollar versus relative basis? What is the average profit margin for the firm and for each client? What caused the problem for clients outside the statistical norm?
- **Firm, Office and Department Profitability:** Which are your most profitable offices and departments on an absolute basis and relative basis? What can be done to improve performance?
- **Business Development:** Which practice areas and industry sectors are growing? Which are declining? What are the year-over-year trends? What is the average life cycle of a client? Which clients should we target for cross-selling and for what service?

*There is the old business adage, “What gets measured is what gets managed.” BI provides a mechanism to establish a culture of measurement.*

- **Working Timekeeper Performance:** What are working and billing hour/value trends by individual and by rank? Who are your most profitable timekeepers? How long does it take for an associate to become profitable? How has the timekeeper mix changed over time and how has it impacted profitability?
- **Cash Cycle Dynamics:** What is the inter-relationship between rate, billing and collection realization and profit measures? What is the relationship between days to bill and collect and profit measures? What is the relationship between leverage and profit measures? Which measures should the firm focus its attention to increase per partner profits?
- **Growth Factors:** What has been the year-over-year growth in hours, billings, and collections? How effectively has the firm been able to manage its rates? How long does it take for a new office to become profitable?

#### Sample KPIs for a Client Profitability View

Key Performance Indicator	Notes
Hours Booked	Over a defined period of time
Value of Hours Booked at Standard Rate	List price calculation
Value of Hours Booked at Negotiated Rate	Full retail price
Blended Rate Realization	This measures the firm's ability to secure its published rate
Total Value of Hours Billed	Actual amount billed
Billing Realization	This measures the firm's ability to bill what it books at the negotiated rate
Collected Amount	Dollars collected matched up to hours booked
Collection Realization	This measures the firm's ability to collect what it bills
Costs (Direct, Indirect, & Time Value of Money)	The value of costs associated with the hours booked
Net Profit	Absolute net dollar contribution to profit
Profit Margin	This measures the relative profitability of a client on a percentage basis
Average Days to Bill	How many days on average did it take to bill the time?
Average Days to Collect	How many days on average did it take to collect dollars billed?
Partner: Associate Leverage	This measures the firm's ability to leverage associate resources.

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## **Analyze**

In the second stage of the BI Cycle, analysts and management review the measures to see if they can uncover hidden relationships that will help them answer “why,” i.e. “Why is this happening?”

For example, industry wisdom declares: the faster you bill, the faster you collect. Is this true? Is there a difference between 30 days and 60 days or is it most pronounced when time is over 90 days old? Take it one step further. Is there a relationship between days to bill and collection realization? Is there a greater tendency to write-off accounts receivable balances on quarterly bills versus monthly bills? These are the types of inter-relationships to examine in the Analyze stage. This type of analysis is called cross-tabulation.

In the following example, the days-to-bill measure is cross-tabulated against days-to-collect and collection realization.

### **Sample Cross Tabulation**

<b>Days to Bill</b>	<b>Days to Collect</b>	<b>Collection Realization</b>
30 – Monthly	45	97%
60 – Bi Monthly	47	96%
90 – Quarterly	64	90%

A firm viewing these results might conclude that there is a minor difference between monthly and bi-monthly billings, but that bills rendered quarterly take two more weeks to collect and the data shows a greater tendency to write-off accounts receivable balances. With this information, the firm might push to shift its quarterly clients to bi-monthly billings.

Obviously, this type of analysis does not guarantee a cause and effect relationship. So there are no guarantees that shifting from quarterly to bi-monthly will improve the days to collect and collection realization measures. Something else might be at play. But, it might be worth the time to take it to the next stage to see what the payout might be if there really is a causal relationship between the KPIs.

*In the plan stage, its time for the firm to quantify the impact of potential change. It is also the time to set goals for the future. Goals should be expressed in the language of KPIs.*

## **Plan**

Once you determine some of the possible reasons why things occur in the Analyze stage, its time to attempt to quantify the impact of potential change. This is the third stage of the BI cycle when you use BI tools to perform “What if” analysis with the data. This is also the time when the firm sets goals for going forward activities. Goals should be expressed in the language of the KPIs so that they can be measured for distribution to the plan stakeholders.

Let’s carry forward the example. In this stage the objective is to quantify the impact on revenue and collection realization, if quarterly billings are changed to bi-monthly. When completing the analysis, be sure to evaluate both the one time impact and the recurring impact.

So, if the law firm billed \$24 million per year in its quarterly cycle, what would happen if the work got billed bi-monthly? First, you would have to analyze what percent of the work could be shifted. Second, you need to calculate what would be the one time reduction in accounts receivable or pickup in revenue from accelerating the cycle. Third, what would be the increase in recurring revenue from the potential increase in collection realization and fourth what percent of the total pick-up do you anticipate?

Once you put all the numbers together, it is time for the law firm to decide if it ready to go to the next stage and take action. If the answer is yes, target KPIs for the change should be established for measurement against actual results.

## **Action**

The Plan Stage leads into the fourth stage in the BI cycle, the Action Stage. This stage is the “Call to Action.” This is the stage when the law firm implements the changes plotted in the previous stage.

Continuing our example, this is the time to execute the strategy. Clients must be notified and client bill cycles must be changed in the billing system. Next you might want to mark these clients in your accounting system, so you can measure the exact impact of the change. As you take action, the fourth stage is complete readying the firm for the next BI Cycle rotation.

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## **Conclusion**

There is the old business adage, “What gets measured is what gets managed.” BI provides a law firm the mechanism to establish a culture of measurement that creates a framework for Analysis, Planning and Action.

It is an extensive exercise to fully develop the KPIs and calculations for each View. The trick is to start with established BI best practices and adapt them to meet the firm’s unique requirements.

Keep in mind that the total amount of data that can be measured and analyzed can be over-whelming, so don’t attempt to do too much too fast. Pick two or three Views to work on first; learn to use the BI tools; and work through a complete BI Cycle before building out other components.

On the technical side, the law firm must: pick the right BI software to work with the accounting applications; implement the hardware and software; build data structures; populate the structures with data; program views, inquiries, reports, and cross tabulations; and user tools. Power users in finance need tools to manipulate the data whereas general users need tools to view and monitor performance.

Law firms that successfully adopt BI into their culture recognize the benefits and wonder how they ever functioned without it. It is the “best practices” framework to drive performance.

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