



5 Steps to Easy(ier) Legal Accounting

Measure your firm's worth

By Joshua Lenon

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Creating an accounting system for your firm has many benefits. For starters, knowing how much your firm makes is important leading up to tax season. But in general, knowing whether you're able to turn a profit month to month will determine the viability of your business. Having a better sense of your financials will also help you make improvements needed for more consistent, long-term success.

Despite the benefits of periodically reviewing your firm's accounting, many lawyers and their firms don't make the effort—and almost all lawyers can improve.

Whether you're looking to manage all of your firm's accounting yourself, or if you're looking to work with an accountant or outside consultant, this guide will help you better manage your money with confidence.

In this guide, we look at five steps lawyers can use to put an accounting system in place, and useful templates to get you started:

1. Create a chart of accounts
2. Pick an accounting tool
3. Determine profitability of your firm
4. Implement best practices for trust accounting
5. Schedule reviews of time entry, billing, and accounting



Step 1: Create a chart of accounts

A chart of accounts gives you a comprehensive listing of all accounts within your firm. Each account listed should include a detailed record for each type of asset, liability, equity, revenue, and expense. The chart of accounts consists of both balance sheet accounts (assets, liabilities, stockholders' equity) and income statement accounts (revenues, expenses, gains, losses).

Many law firms don't realize how many accounts need to be tracked to accurately reflect their firm's value. Here are some samples that can serve as guides for building your own chart of accounts. (We also provide examples below.)

- State Bar of Georgia's [Standard Chart of Accounts for Smaller Law Offices \(PDF\)](#)
- Law Society of British Columbia's [Online Learning Centre Chart of Accounts \(PDF\)](#)

You can't add too many valid accounts to your chart of accounts. Make sure you take an expansive view when building this chart to get everything necessary to track your firm's finances.



Step 2: Pick an accounting tool

Now that you have a chart of accounts, use software to track your firm's finances. When selecting your software, be sure to consider ease of use, integration with your practice management system, and ease of information sharing with your accountant.

You should also review whether your accounting software can handle cash basis accounting or accrual basis accounting. The main difference between the two systems has to do with when they recognize revenue. While many small firms can get by on cash basis accounting, which recognizes revenue only when it is received, larger firms should use accrual basis accounting. Accrual basis accounting recognizes revenue when it is earned and is a standard principle of accounting. If you want to work with an accountant, you will need to use accrual basis accounting.

Note, however, that firms using cash basis accounting may be required to shift to accrual basis accounting if [anticipated changes](#) are made to the United States tax code.

The most applicable solutions for lawyers include QuickBooks Online and Xero, both of which offer a detailed ledger system that integrates with Clio's billing features. Once you pick a tool, enter your chart of accounts and you'll be on your way to a better understanding of your firm's financial position.



Step 3: Determine profitability of your firm

The information from your chart of accounts will help determine many financial details about your firm going forward.

You should easily be able to create income statements and balance sheets for your firm within your accounting software. The income statement is also called the profit/loss report. It subtracts the expenses and losses from the revenues and gains over a measured period of time. Law firms want their income statement to end with positive numbers, which indicate that a firm is running profitably.

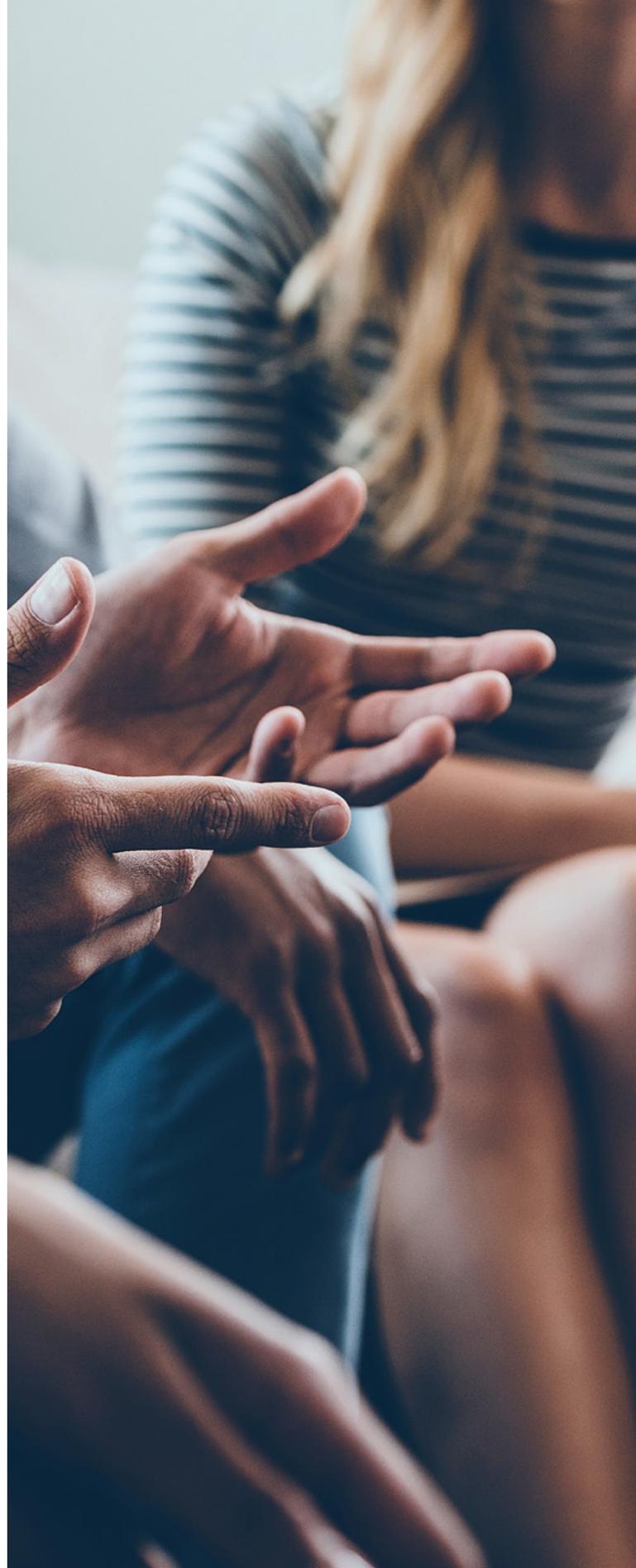
A positive outcome on an income statement does not mean that the firm is necessarily collecting the revenue, however. Collections would be measured in a statement of cash flows. Firms must monitor both income statements and cash flows to remain viable.

Step 4: Implement best practices for trust accounting

Client funds should be stored in a trust account until they are earned or distributed. Law firms should review their jurisdiction's [trust accounting rules](#) to make sure they set up their accounting procedures correctly.

Exact trust accounting requirements vary with the jurisdiction, but a good [practice management software](#) should help with assigning and tracking client funds by associating them with both a matter and a client. This should make it easier to maintain a ledger for clients and matters that tracks transfers, receipts, balances, and more.

Accounting software also helps with monthly reconciliations and file storage. One tip many law firms can benefit from is to scan and store bank statements, cancelled checks, and monthly reports as PDFs in their accounting system. For example, Clio can store files online, associating them with clients and matters. This makes them easily producible in the event of an audit or dispute.



Responsible trust accounting with Clio

Clio's trust accounting features let you easily handle trust funds in compliance with your jurisdiction's requirements. With Clio, you can keep a separate record of trust funds, which you can then associate to specific clients or matters.

With Clio's Trust Requests feature, you can send instant requests via email or Clio's client portal, **Clio Connect**, asking clients to deposit money into trust, while allowing them to make their deposit via secure electronic payment. New trust deposits will automatically be tracked as part of your law firm's trust accounting.

With Clio's Trust Ledger report, you can quickly generate reports on firm-wide or client-specific trust ledgers to fulfill monthly or annual reconciliations. Learn more about **Clio's Trust Accounting management**.

Learn more about Clio.

[Sign up for a free trial or schedule a demo today!](#)

Step 5: Schedule reviews of time entry, billing, and accounting

Law firms should not only set up an accounting system, they should also schedule periodic reviews of their accounting information.

The frequency of these reviews depends on your firm's needs. Here are some routines to consider:

- Daily—individual lawyers review their daily time entries for completeness and accuracy.
- Weekly—administrators review weekly summaries to make sure that firm billing standards are being met.
- Monthly—administrators and managing lawyers review trust account information and complete reconciliations as part of the firm's billing cycle.
- Quarterly—managing lawyers review their firm's profitability, running income statements, balance sheets, and statements of cash flow at least this frequently. (These reports will also help solos prepare their quarterly self-employment income tax payments.)
- Annually—managing lawyers review the annual period to determine profitability and to prepare for annual tax filings.

Following these steps will help you get an accurate image of your firm's finances. Firms can easily run reports on successes and barriers in their cash flows.

Take the time to set up a proper accounting system and master your firm's finances.



Chart of accounts template

To get an accurate assessment of your firm's financials, you'll want to include as much information as possible. This section offers a list of relevant items to consider for each account. Be sure to review each item to ensure it is properly attributed in your accounting system.

For example, a line of credit should be counted as an asset if it hasn't been drawn upon, as it represents cash on hand. Once it's been withdrawn, however, the line of credit becomes a liability since it represents money owed. Real estate can also be both an asset and a

liability; ownership of a property is an asset, but if it is under mortgage it is also a liability.

Payroll tax liabilities are a key consideration for solo lawyers who don't give themselves a formal paycheck that includes tax deductions. In this case, money should be set aside on a quarterly basis to cover owed taxes at the end of the year.

The following tables offer a list of items to consider when creating a chart of accounts.

Assets

Type	Account	Description
Current assets	Operating bank account	
	Petty cash	
	Accounts receivable	
	Advanced client costs	
	Work in progress fees	
	Prepaid expenses	
Fixed and other assets	Real property	
	Furniture	
	Depreciation	

Liabilities

Type	Account	Description
Current liabilities	Bank loan / line of credit	
	Accounts payable	
	Business credit card	
	Payroll tax liabilities	
Long term liabilities	Capital loan	
	Equipment loan	

Segregated liabilities

Type	Account	Description
Trust bank accounts	IOLTA or pooled trust accounts	
	Separate interest bearing trust accounts	

Equity

Type	Account	Description
Firm investments	Capital	
	Retained earnings	
	Equity account: owner #1 (et al.)	
	Profit/income distributions for year	
	Drawings for the year: owner #1 (et al.)	

Revenue

Type	Account	Description
Cash flow	Fees earned	
	Disbursements recovered	
	Interest income	
	Other income	

Compensation

Type	Account	Description
Payroll	Secretarial	
	Word processing	
	Paralegals / clerks	
	Lawyers	
	Employee retirement benefits	
	Employee training and education	
	Other employee costs	
	Other non-owner employees	

Expenses

Type	Account	Description
Office	Office rent	
	Parking	
	Real estate taxes and insurance	
	Utilities	
Office operations	Telephones	
	Photocopies	
	Computer equipment	
	Practice management platform	
	Software subscriptions	
	Supplies	
Professional costs	Travel & related expenses	
	Professional dues	
	Continuing education	
	Conference fees	
	Professional liability insurance	
Promotion	Entertainment	
	Promotion & advertising	
Other expenses	Bad debt, fees	
	Bad debt, disbursements	
	Write-offs, unbilled disbursements	
	Recruitment cost	
	Other taxes and similar costs	
	Miscellaneous expenses	

Expenses

Type	Account	Description
Office	Office rent	
	Parking	
	Real estate taxes and insurance	
	Utilities	



About Joshua Lenon

Joshua Lenon is an attorney admitted to the New York Bar. He studied law at St. Louis University School of Law, obtaining a Juris Doctorate and a Certificate in International and Comparative Law, clerking for the Missouri Attorney General. Joshua also studied European Union Law at the University of Georgia School of Law's Brussels Legal Seminar.

Joshua currently serves as Lawyer-in-Residence for Clio, providing legal scholarship and research skills. He's been a guest lecturer for movements like legal hacking and legal technology at schools like MIT, Suffolk Law, and Vanderbilt, as well as before organizations like ReInventLaw and the ABA Law Practice Futures Initiative.

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About Clio

[Clio](#) is the most comprehensive cloud-based practice management platform for the legal industry. With the help of the cloud, Clio eases the process of time tracking, billing, administration, and collaboration for law firms of all sizes. Based in Vancouver, B.C., and with a European office in Dublin, Clio is used by legal professionals in over 50 countries. Clio has raised \$27 million from investors including Bessemer Venture Partners.

[Try it for free or schedule a demo today!](#)

