

# Simplified Bookkeeping for Lawyers

—

A White Paper



November 29, 2018

[eDataQuick.com](http://eDataQuick.com)

Beverly Hills, California USA

## Simplified Bookkeeping for Lawyers

Bookkeeping is a necessary part of any business, law firm practices included. Having up to date financial records is vital for analyzing, forecasting, and making crucial decisions that could take a law practice into a whole new level of sustainability and profitability.

But unlike traditional businesses that only require accounting of income, expenses and payroll, legal bookkeeping has additional requirements imposed by state government and/or bar association regulations that challenge a lawyer's basic knowledge of bookkeeping - remember, they don't teach bookkeeping in law school.

The following are among the challenges, not covered by traditional bookkeeping, that are unique to the legal profession:

### Client Trust Account Management

A Client Trust Account is a bank account that a lawyer establishes to hold funds owned by a client to pay current and future expenses, and/or to pay for the current or future services to be provided by the lawyer. Different states have different rules relating to the management of client trust funds. However, regardless of the jurisdiction, to avoid any appearance of impropriety and to survive an audit, a client trust account must be managed in such a way that:

1. It is never commingled with the law firm's operating funds.
2. If the trust account holds several client's funds, the balance on the account can be reconciled and broken down on a client-to client and date range basis.
3. All transactions related to a client, from the initial deposit to the last disbursement are tracked in a ledger.
4. Financial Reports are always readily available and accessible.
5. Unearned fees and costs at the end of the representation engagement must be returned to the client.
6. Records pertaining to client trust accounts should be retained for a minimum of 5 to 6 years after termination.

### Costs Advanced

It is common for lawyers to initially pay for expenses on a client's behalf. Examples include: deposition fees, experts' fees, witness fees, filing fees, photocopying and other clerical services. The tax treatment of these advanced client costs and how to properly enter them into the books are sometimes confusing. There are several court cases and IRS rulings *Canelo v. Commissioner*, 53 T.C. 217, 219 (1969), *aff'd* 447 F.2d 484 (9th Cir. 1971); *Herrick v. Commissioner*, 63 T.C. 562, 569 (1975)

(discussing *Burnett v. Commissioner*, 356 F.2d 755 (5th Cir. 1966)) that give guidance to the proper treatment of costs advanced. Noncompliance with the IRS rules can result in audits and penalties.

### **Billing and Invoicing**

Whether a lawyer charges a flat rate, bills by the hour, or works on a contingency, there are ethical rules relating to getting paid, that must be complied with. Also, costs incurred whether paid for by cash, check or by credit card need to be tracked and posted to the books correctly or risk not getting billed to the client.

The bottom line is documentation. It is important to remember that while a lawyer has secured an advanced fee that has been deposited in a client trust account, the funds may not be withdrawn from the trust account unless the amount earned or an expense incurred has been properly identified, entered into the books, communicated to and approved by the client.

Staying compliant is part of the formula for the success and survival of a law firm, and although absolutely necessary, bookkeeping is cumbersome, complicated and non-billable; it's not very hard to see why lawyers hate the bookkeeping aspect of a practice.

In our experience of handling bookkeeping for solo and small law firm practices, we've identified the following pain points that have caused lawyers who manage their own books, to struggle with accurate balances, fall behind on their books or both!

#### **The three-point reconciliation Process.**

Law practices that maintain trust accounts are required to perform a three-point reconciliation periodically – every thirty or sixty days depending on the rules of the state. To accomplish this feat, a do-it-yourself bookkeeper needs to maintain two separate sets of ledgers:

1. A check register, (book balance) which is the balance of the entire trust account, and
2. Individual Client ledgers, (client ledger balance) which are the balances of each of the client's funds within the trust account.

The sum of all client ledgers must equal the book balance, which must be equal to the actual balance in the bank statement (bank balance), at any given date range.

Blessed is the day when all three numbers match! Some of the common errors are in identifying transactions on the bank statement and entering the correct amounts on the correct ledgers. From time to time, book balance adjustments also have to be made for transactions like payments or deposits that have not yet cleared the bank.

The three-point process is very difficult to manage by hand. A lawyer would probably be spending more of his billable time doing the bookkeeping than managing his case load. Using generic accounting software without proper bookkeeping training is also courting disaster. Legal accounting software is helpful, although using it also requires some training and could cost more than what a small law firm is willing, or able to spend.



## Case Cost Accounting

It is important to understand that all expenses incurred on behalf of a client, whether or not these are eventually billed to the client, are not always posted to the same account in bookkeeping. Costs advanced by a lawyer are categorized as either hard costs or soft costs, and are entered into the books differently. Also, generally, hard costs are not treated as tax deductible business expenses while soft costs are.

For example, direct expenses advanced by a lawyer such as deposition fees, expert and witness fees are considered loans to the client and as such, are not generally deductible as business expenses. These costs are usually reflected as assets on the balance sheet, as accounts receivable. In the event the amount is unrecovered, it can then be declared as a tax deductible business expense.

On the other hand, soft costs such as clerical services or photocopying fees are treated as tax deductible expenses. When reimbursed, these are posted as income.

No doubt, given enough time, a good accountant will be able to sort all these out. But if bookkeeping is done properly, the amount of time a tax preparer needs to look over the books will be minimal and almost effortless thus minimizing the higher paid tax preparer's billable time.

## Billing

To save on overhead expenses, solo and small law firm practices frequently use different basic systems for billing and bookkeeping. Often, the two systems are not compatible. Manual data entry has to be done twice, and accurately across both systems.

There are products available that integrate both billing and bookkeeping functions in a single software package. The downside is a higher monthly fee.

## Focus on your practice. Leave the bookkeeping to us, we'll simplify it for you!

Benefit from our experience in legal bookkeeping. We have identified all of the issues experienced by law firms and have addressed them using Generally Accepted Accounting Principles (GAAP). eDataQuick ensures:

- Compliant, Accurate, Audit-ready Client Trust Management.
- Timely Invoicing through QuickBooks or posting billing information from most attorney billing software into QuickBooks.
- Detailed expense information including archiving invoices and receipts linked to the bookkeeping entries for easy access.
- Full charge bookkeeping services from experienced CPAs at a fraction of the typical cost paid by law practices.
- We prepare complete information needed by your tax accountant and will work with the accountant to facilitate your tax return preparation at no extra cost.

Our bookkeepers also analyze your bills and invoices and post due dates extracted from them; post journal entries such as depreciation and prepaid expenses; make journal adjustments and do a myriad of other things. We will provide you with reports that will give you a more realistic idea of how much money you have coming in as well as projecting future income and expenses.

The first two months of our bookkeeping service is free! There is no setup costs and no ongoing commitment. Check out our website: [www.edataquick.com](http://www.edataquick.com) or, call us at 1(833) 463 3282 and speak with an account manager. We operate 24 hours a day, 7 days a week. You may also email us at [bookkeeping@edataquick.com](mailto:bookkeeping@edataquick.com).

### **About eDataQuick**

**eDataQuick is a subsidiary of [eData Services U.S., LLC](http://www.edataservices.com)**, an American owned and operated business. For almost 20 years eData Services has provided high value back-office business process outsourcing services for many industries, including medical, legal, engineering, and insurance professionals.

**We are customer focused and tailor our services** to meet our clients' needs. With more than 500 experts from over 20 professions, we deliver customized services to over 800+ clients in the United States. We are ISO 9001:2015 Certified, FTC and HIPAA compliant, and utilize state of the art technologies, including the Microsoft Azure Cloud, and Intuit technologies to protect all customer data.

**Our headquarters are in Beverly Hills, California.** All of the bookkeeping work is performed in our wholly owned facility in Makati, Philippines. We are in a unique position to deliver what our customers require. Benefit from the low cost labor arbitrage that your competitors are able to acquire while enjoying quality, security and reliability as if your work was performed in the United States.

**We employ highly skilled bookkeeping professionals**, whose minimum qualifications include a Bachelor's Degree in accounting, finance or similar fields. Most of them are Certified Public Accountants in the Philippines. All of our production staff are qualified to deliver GAAP compliant financial reports and have completed training as QuickBooks ProAdvisors.

