



Key Performance Indicators

An Introductory Guide



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COMMON SENSE APPLIED

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Cover and page layout by:
www.TheBookProducer.com

Printed in Canada



*"If you don't know
where you are going,
any road will get you there"*

~ Lewis Carroll

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Introduction

Law firms of all sizes should calculate and track indicators of their performance and health. The most successful firms use these indicators to assist in making important business like decisions, in motivating and aligning behavior, and in adjusting to the new realities.

The challenge is to identify those specific indicators that are critical to the short, medium and long term success of your individual firm and then focus on them. Throughout this guide we will refer to this subset of critical indicators as key performance indicators (“KPI”).

A couple of important contextual points:

- ▶ It is unlikely that any firm will use all of the KPI identified in this guide; and
- ▶ The importance firms place on specific KPI will change over time as they move along their individual evolutionary track.

The list of KPI identified in the remaining pages is not intended to be exhaustive but rather as

collection of common and not so common KPI that firms are and will be using over time.

The KPI identified in this guide are broken down into the following three categories:

- Marketing
- Productivity
- Financial

A word of caution – KPI is simply a tool – they are no substitute for the use of common sense and good judgment when it comes to the management of your law firm.

Chapter 1

What Makes an Indicator a KPI?

Indicators should meet the following three criteria to qualify as a KPI for your firm:

1. It must reflect the firm's strategy and goals;
2. It must be key to the firm's success; and
3. It has to be quantifiable

Your firm's strategic focus will impact its selection of KPI. For example:

- Transaction-focused firms will undoubtedly have different KPI than relationship-focused firms;
- Billable hour driven firms have different KPI than tariff driven firms; and
- Firms at a growth stage in their lifecycle will have different KPI than firms at a succession or regrowth stage.

In this guide we have included KPI that apply to a range of “strategic focuses”.

The fact that in a tariff focused firm the billable hours per lawyer would not be as relevant as the number of matters per lawyer demonstrates the importance of the first two criteria in defining which indicators are KPI to it.

The author is not suggesting that all that counts in a law firm can be counted but rather what gets measured is what gets done. Therefore, if an indicator is not quantifiable, it is not likely that it will be incorporated into your firm’s decision making process which may in fact cause issues to go unaddressed.

Chapter 2

Marketing KPI

Typically KPI have focused predominately on the productivity and financial aspects of law firms. Firms are in the early stages of exploring marketing and business development KPI to understand what will work best for them.

The following list of possible KPI for marketing and business development in law firms are examples of various KPIs you might consider adopting / adapting for use in evaluating your firm's efforts.

- ***Client Growth Rate*** – the ratio of the number of clients that the firm handled its first matter for in the past 12 months to the total number of active clients (active can be defined as having handled a matter for in each of the past 2 of 3 or 3 of 5 years)
- ***Dormant Client Percentage*** – the ratio of the number of clients that firm has

not handled a matter for in 2 of the past 3 or 3 of the past 5 years to the number of total clients

- ***Average Fee per Client*** – the fee revenue for the year divided by the number of clients billed during the year
- ***Average Fee per New Client*** – the related fee revenue for the year divided by the new clients (of clients that the firm handled its first matter for in the past 12 months)
- ***Marketing Budget Ratio*** – the ratio of the total marketing spend (including salaries) to the total fees billed during the year
- ***Business Development Ratio*** – the ratio of the business development spend for the year to the total fees billed during the year
- ***Marketing Cost per Client*** – the ratio of the total marketing spend (including salaries) to the number of clients billed during the year

- ***Business Development Cost per Client*** – the ratio of the business development spend for the year to the number of clients billed during the year
- ***Average Fee per Matter*** – the fee revenue for the year divided by the number of matters billed during the year
- ***Average Fee per New Matter*** – the related fee revenue for the year divided by the number of matters billed for new clients (handled its first matter for in the past 12 months)
- ***Client Retention*** – the ratio of clients billed in the last 12 months to the total clients that had been billed in the 12 months prior to the last year
- ***Growth in Top Clients*** – the ratio of fees billed to top 100 clients (number can be adjusted to size of firm) in the past 12 months to the fees billed to the top 100 clients in the prior 12 months.
- ***Practice Areas per Client*** – the number of individual practice groups billed to clients on average

- ***Number of Lawyers per Client*** – the ratio of individual lawyers who generate working fee credits billed to clients on average
- ***Number of Matters per Client*** – the ratio of number of matters billed to the number of clients billed

Chapter 3

Productivity KPI

To ensure the most accurate measurement possible, productivity KPI utilize the concept of full time equivalent (“FTE”). FTE reflects how many actual timekeepers or staff your firm had for the period being measured. For example, a lawyer who was with your firm for six of the past twelve months would be treated as one-half of a FTE in determining your lawyer count.

The following list of possible KPI for measuring productivity in law firms are examples of various KPIs you might consider adopting / adapting for use in evaluating your firm’s efforts.

- ***Leverage*** – the ratio of Associates to Partners
- ***Percentage of Partners Hours*** – the ratio of Partners hours worked to the total hours worked by all timekeepers;

intended to measure whether Partners are working harder or smarter

- ***Billable Hours per FTE Timekeeper*** – the gross number of billable hours worked by Associates and Partners divided by the number of full time equivalents in each category
- ***Billings per FTE*** – the gross amount of fee billings by Associates and Partners divided by the number of full time equivalents in each category
- ***Average Worked Rate*** – the gross value of time worked for a timekeeping category as entered into work-in-progress divided by the related hours entered
- ***Average Billed Rate*** – the gross value of time billed for a timekeeping category as divided by the related hours billed
- ***Ratio of Averaged Billed to Average Worked Rate*** – the ratio of the average billed hourly rate for a timekeeping category to the average worked hourly rate. This can assist in extrapolating what the

likely impact will be on billed fees of potential rate increases

- ***Number of Matters Opened*** – number of new matters opened in the fiscal 12 month period; another measurement of workload
- ***Billable Hours per Legal Assistant*** – the ratio of the total billable hours for all timekeepers to the number of Legal Assistants
- ***Staffing Ratio*** – the ratio of total staff positions to the total number of timekeepers which includes Partners, Associates, Counsel, Paralegals, Staff Lawyers and Articled Students

Chapter 4

Financial KPI

Financial KPI are evolving as the fundamental economics of law firms change. This is resulting in a different view of what is critical to both tracking and measuring your firm's financial success.

One of the challenges to generating the following and other financial KPI is that many law firm accounting software packages don't lend themselves to readily generating the information on a timely or efficient manner.

- ***Unbilled Days*** – the ratio of the fee portion of unbilled work-in-progress to the average fee billings for the past 12 months; measures the length of time it takes you to bill the work you do.
- ***Uncollected Days*** – the ratio of the fee portion of accounts receivable to the average fee billings for the past 12 months or the length of time it takes to collect your accounts after they are rendered

- ***Cost Recovery Revenue per Matter*** – the total amount of internal costs billed to clients divided by the total number of matters billed
- ***Revenue per Square Foot*** – the gross amount of fees billed by all timekeepers divided by the total square footage of office space leased by the firm
- ***Revenue per Matter*** – the gross amount of fees billed by all timekeepers divided by the number of matters billed in the year
- ***Revenue per Employee*** – the ratio of the gross amount of fees billed by all timekeepers divided by the sum of all full time equivalents excluding partners
- ***Contingency in Work-in-Progress*** – the ratio of the work-in-progress that is being handled on a contingency fee arrangement to the total work-in-progress
- ***Charge Off Percentage*** – the ratio of the amount of billings written off as uncollectible as a percentage of the fees billed for the year

- ***Net Income Ratio*** – the ratio of the Firm’s net income (income prior to any distributions to partners) divided by the total fee billings of all time keepers
- ***Average Net Overhead*** – the net expenses (total expense minus billings of all non-partner timekeepers) divided by the number of Partner FTEs (Equity and Non-equity combined). This is the net cost that each Partner must cover before any profits are generated.

Chapter 5

Presentation, Presentation, Presentation

In recent years the term *dashboard* has been introduced into the conversation dealing with indicators in general and KPI specifically. Many law firm accounting applications offering a module that attempts to provide a focal point that is readily accessible to management.

In its basic intent, the dashboard for a law firm is the same principal as the one in your car. Like cars, these law firm dashboards can run the gambit in sophistication and real value. Perhaps the more important analogy is that like your car's dashboard you can't drive your vehicle by solely watching your dashboard, rather it helps you know how you are progressing towards your destination.

Developing a dashboard for your firm will help your management team pull away from the

long grass and pay attention to what is important. For example, if your law firm develops a strategic focus on specific client relationships and supports that focus with client teams, measuring the breath of the relationship by tracking the number of matters per client, the number of practice areas that serve these clients and the number of lawyers with time on matters connected to this client are good indicators or KPI worth tracking. Matters is an indicator of growth in the client relationship; practice areas is an indicator of cross selling success and number of lawyers is a measure of breadth and depth of the relationships between your firm and the client. All of these measures are quantifiable and measure success towards the firm's goals.

But no matter what KPI you track providing management or the partners with reams and reams of paper or screens will normally serve to lessen the impact that the KPI can have on your firm's decision making. When developing a monthly report (5 - 6 pages maximum), attention needs to be paid to the preferred presentation style of the audience and a balance of words, numbers and pictures achieved so the report remains meaningful to all.

Chapter 6

Benchmarking

Benchmarking is defined as comparing your firm's KPI against the same KPI for other organizations.

Context is critical to the effective use of KPI. For many firms the only benchmark they have is their own past experience. Unfortunately, access to benchmarking data in the legal profession is limited.

There are very few formal and informal local sources for benchmarking that firms can avail themselves of, however users need to make sure that it is a comparable group (firm size, location, type of firm, etc.); that the KPI measured are consistently calculated; and that a third party conducts the process so the results are not skewed to the goals of the initiator of the benchmarking exercise.

Chapter 7

Exercise Judgment

A note of caution – no one KPI tells the full story, but rather they must be viewed collectively to achieve the best informed decision making results.

The following scenario perhaps best demonstrates the need to exercise judgment.

Your firm experiences a strong increase, year over year, in the average effective hourly rate (one of your KPI) which would be seen as a very positive indicator of how the firm is weathering the changes in the business environment or macro economic climate. However, when you dig deeper, you recognize that the increase exceeds the average hourly rate increase initiated by the firm.

What this KPI is really indicative of is that more partner time is being billed out at higher rates and less Associate time being billed out at lower rates which results in an immediate

increase in the effective hourly rate. This may be indicative of the partners having “rolled the ladder up” when it comes to allocating work to Associates.

In this scenario, the KPI is still acting as an important indicator of performance; however it is doing so by being too good and therefore acting as a red flag. Two other KPIs, Billed Hours per Partner FTE and Associate FTE, would help you provide the proper context for the initial KPI.

At the risk of repeating ourselves as valuable as they are, KPIs are simply metrics—they are no substitute for the use of common sense and good judgment when it comes to the management of your law firm.



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Types of past assignments have included; Inaugural partnership agreements; Compensation and retirement plans for partners; Strategic action planning and initiatives to achieve action plans; Succession / retirement planning for partners; Coaching of individual partners; Sounding board for Managing Partners; Re-capitalization of firms; Financial review of firms; Retreat facilitation and presentations; Leadership presentations and seminars

- Over 85 articles on law firm management published in legal periodicals in the US & Canada
- Presented at OBA, CBA, LMA, ALA, MPF, BCLMA, MPF conferences
- More than 29 years in a senior management role with 200+ lawyer multi-office law firm
- Fellow of the College of Law Practice Management (one of 16 Canadians)

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