Definitely Mabey

Measuring Key Performance Indicators

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This column will deal with some of the key results of the 2011 Canadian KPI Survey conducted by Law Firm KPI, a for-profit company (our intent anyways) co-founded by Karen MacKay of Phoenix Legal Inc., and me in 2010 to specifically undertake surveys of key performance indicators for law firms with up to 100 lawyers.

The purpose of the survey is to provide Canadian law firms with industry information in order to benchmark their own performance against the performance of other firms of reasonable comparative size.

More information on the annual survey can be found at LawFirmKPI.com.

What is KPI you may well ask?

Lots of firms use different subjective and objective indicators to track their performance and perceived fiscal health. So what makes an indicator become a KPI for a firm? When it:

- reflects the firm's strategy and goals;
- is key to the firm's success; and
- can be quantified.

During the course of discussions with law firms, both in Canada and the United States, it became clear that perhaps we had overestimated the body of knowledge that existed among firms on the topic of KPI. So we co-wrote a **mini-guide on KPI**, which, in addition to explaining what they are and their use, also provides definitions for a range of indicators broken down into the following three categories:

1. marketing
2. productivity
3. financial

A word of caution

Context is critical to the effective use of KPI as they are simply a tool and no substitution for the use of common sense and good judgment when it comes to the management of your law firm!

And now for the results

The data that will be discussed is based upon a survey size of 21 offices and 507 timekeepers, of which 183 were partners and 170 were associates.

As a result of the confidentiality of the survey and participating firms having paid to receive the full results, for the most part the information discussed will be of a general or generic nature. There are 25 KPI covered by the survey as well as 11 major expense categories shown as a percentage of revenue. The survey, in addition to providing participating firms their own KPI, also indicates the strongest, weakest, median, and average result for the group.

I would suggest that while there were no real surprises in the trends reflected by the survey results, there were a couple of surprises in the numbers including: the closing of the gap between firms on some KPI; and the steepness of the trend line.

The average leverage—the ratio of associates to partners—dropped from 1.97 in 2009 to 1.34 in 2010. Further confirmation that the ladder was rolled up in many firms during these tougher economic times can be seen in the increase in the ratio of partners' hours to the total of all timekeeper hours in 2010 which averaged 40.7 per cent up from an average of 37.7 per cent in 2009.

Again a penetrating glimpse into the obvious when I would point out that billable hours per full-time equivalent (FTE) on average were down for both associates—1,295 versus 1,384—and partners—1,307 versus 1,357.

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The double whammy with the drop in productivity is the increase in average uncollected days (receivables outstanding), which was up by six days in 2010 over 2009. Firms' average total "financial lock up" (unbilled work in progress plus accounts receivable) increased in total by 36 days due to a slowdown in the timely billing of clients.

The survey results suggest that firms did initiate rate increases with the average work rate for associates and partners up almost nine per cent and 12 per cent respectively in 2010.

Most of the increase in associates' hourly rates appears to have been written off at the point of billing with the ratio of average billed to work rate dropping 6.5 points to 88.2 per cent. However, the rate increases apparently met with resistance, likely both internally and externally. While the average hourly billed rate for associates remained flat, the same was not true for partners, which dropped by 9.5 per cent in 2010 from 2009.

While it may speak to both quality and nature of their client base, at the same time, this resistance was not across the board as the strongest billings per associate and partner increased by $68,000 and $81,000 respectively. This despite the average billings per associate and partner decreasing by $10,000 and $88,000 respectively.

If you listen closely you can still hear the non-believers in the permanency of the change in the economics of the practice of law speak of the days when it was common that 50 per cent of revenue went to the bottom line and that if today's leaders were worth their salt they would take whatever steps were necessary to return firms to the "good old days." Well I hate to be the bearer of bad news, but the average ratio of net income to revenue eroded again in 2010 to 35.2 per cent.

Lest you think the survey is stuck in the good old days of the billable hour, it generated some initial data on some new measures of a firm's revenue generation including:

- Revenue per matter billed: averaging $4,663;
- Revenue per square foot of office space: $328 to $724; and
- Revenue per employee (sum of billings for all timekeepers divided by all FTEs excluding partners), which averaged slightly more than $200,000.

While still relying on the billable hour, but approaching staffing from a slightly different perspective, the average billable hours per legal assistant (ratio of total billable hours for all timekeepers to the number of legal assistants) averaged close to 4,000 hours.

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The change in the "KPI average net overhead"—the cost that each partner must cover before any profits are generated by their billings (total expenses minus billings of all non-partner timekeepers divided by the number of partner FTEs)—always bears individual investigation as it can be affected by a drop in the billings of non-partner timekeepers; where a firm is in its capital equipment replacement cycle; new or renovated office space; severance costs; stepped-up marketing costs; partner attrition; etc. For example, in 2010 the average was approximately $225,600, a sizeable increase over the average for 2009.

At the risk of being repetitious, while KPI are a very valuable tool that can assist in making important businesslike decisions, motivating and aligning behaviour, and adjusting your firm to the new realities, they are no substitute for exercising common sense and good judgment when it comes to the management of your law firm.

Until the next column, remember,

"if you don't know where you are going, any road will get you somewhere."

Comments or Questions?

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