

Cost cutting for
sustainability: 3 areas to target

Don't put payroll
management on autopilot

Making remote work ... work

Law firm planning in
a time of uncertainty

LAW FIRM MANAGEMENT

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Cost cutting for sustainability: 3 areas to target

U.S. law firms — of all sizes and practice areas — have had their financial foundations shaken as a result of the COVID-19 crisis. Firms that were flying high less than a year ago now find themselves scrambling to survive the economic fallout. One obvious place to begin is cost-cutting, and several areas make likely candidates.

1. STAFFING EXPENSES

The headlines in legal media have been plastered with news of firms reducing headcounts or compensation. With staffing traditionally one of a firm's biggest budget items, this tactic often is the first option.

It's important, though, to take a strategic approach when trimming positions and consider all levels of your firm, from staff to partners. Look at who's most productive, which practice areas are likely to see increased or reduced demand (and for how long) and similar factors, rather than focusing purely on salary. Determine, too, whether voluntary leaves or furloughs could work, as opposed to outright termination.

Now is a great time to re-evaluate past decisions about whether to rent or buy equipment — changed circumstances may call for a different option.

You also must take care to avoid the appearance of discrimination. One firm, for example, is now facing a lawsuit filed by a 62-year-old IT manager who alleges the firm fired him because of his age to reduce costs during the pandemic. (The firm claims he was fired for cause.)



IT, however, is one of several positions that may prove appropriate for outsourcing to freelancers and independent contractors who cost significantly less than full-time staff. Research and transcription work also are ripe for outsourcing.

Many firms seem to be making compensation cuts across-the-board of, say, 10%. You could reduce fixed salaries and add a variable pay component based on results. Or you might freeze salary increases.

This is a good opportunity to reassess your benefits package, too. Determine which benefits are most valued by employees and protect those, while cutting the benefits regarded as simply “nice to have.” Consider increasing employees’ out-of-pocket shares of health care costs and premiums.

2. SPACE NEEDS

Many firms have learned during the COVID-19 closures that remote work can be more effective

WATCH OUT FOR OCCUPATIONAL FRAUD

While cost-cutting and other survival strategies are important, law firms must not let their antifraud measures slip. The Association of Certified Fraud Examiners (ACFE) recently reported that the median loss from fraud schemes committed at professional services businesses such as law firms is \$150,000. This means that a single employee could dramatically hurt your firm's bottom line.

According to the ACFE, the presence of antifraud controls is associated with quicker detection and smaller losses. Such controls include a formal antifraud policy, fraud awareness training and fraud reporting mechanisms. Tips from employees, clients and vendors have long been a top method for uncovering fraud. Provide stakeholders with multiple reporting options (for example, email and an online form).

In addition, your firm's management should scrutinize expense reports to ensure claimed expenses are reasonable and related to business. Also, implement measures to prevent partners and managers from overriding internal controls — and segregate accounting duties.

than they previously thought. If you're one of them, you might be able to cut your space needs by increasing your remote work going forward. (See the article "Making remote work ... work" on page 5.)

Even if you don't want to — or can't — reduce your footprint, think about leasing out excess space you may have. However, be sure to check with your state's ethics rules first. Some states have specific rules on the sharing of office space between lawyers and nonlawyers.

3. VENDOR ARRANGEMENTS

This is a great time to re-evaluate past decisions about whether to rent or buy equipment. It might have been cheaper in the past to use a shredding service or rent office equipment, but now it might make more sense to own those machines.

Try to negotiate with the vendors with whom you have ongoing relationships. If portions of your staff are now working remotely, for example, you probably don't require as many desktop

computers, printers, copiers or phone lines. You might be able to consolidate services with a smaller number of vendors and obtain discounts for expanded or exclusive relationships.

When it comes to technology, remember that you don't always need the top of the line to reap efficiency benefits. So don't automatically upgrade or buy the latest models if your current hardware and software are working just fine. When computers or devices break, look for significant savings by replacing them with used or refurbished models.

LOOK BEYOND COSTS

In times of crisis, perspective is vital. As you look for ways to stabilize your financial standing for the long term, bear in mind that profitability is a function of both costs and revenues. Too many cost cuts can end up undermining your performance, making it more difficult to recover and seize opportunities. The better approach is to make your cuts strategically while also searching for avenues to increase revenue. •

Don't put payroll management on autopilot

The COVID-19 pandemic has thrown the economy for a loop. Many law firms have had to trim expenses and furlough employees. Laying off or decreasing pay for support staff, associates and partners can add payroll tasks to your workload. If your firm is reducing people on the payroll or outsourcing work to independent contractors, there are several issues management should review carefully.

STAY CURRENT WITH RECORDKEEPING

The U.S. Department of Labor (DOL) requires every employer covered by the Fair Labor Standards Act (FLSA) to keep records for each nonexempt worker. (State requirements may vary.) The law doesn't specify the form of records, but they must include certain identifying information about the employee and data about the hours worked and wages earned. Unsurprisingly, the law requires this information to be accurate.

Generally, firms should retain payroll records for at least three years, and wage computation records for two years. The latter includes time-cards, wage rate tables, work and time schedules, and records of additions to or deductions from

wages. You may keep the records in your firm's office or a central records office.

AVOID EMPLOYEE MISCLASSIFICATION

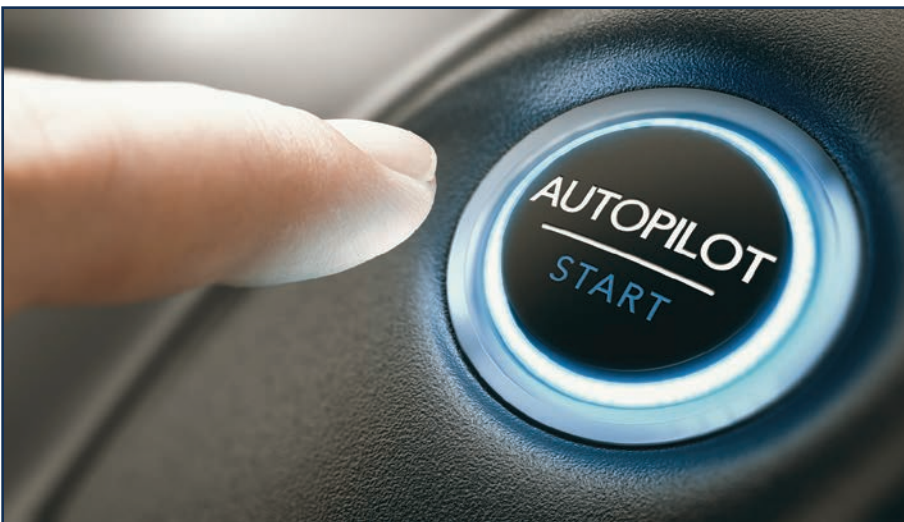
Employee misclassification is always a hot topic. In 2018, the DOL updated guidance on the appropriate standard for determining whether an employee is misclassified as an independent contractor under the federal FLSA. And in 2019 it issued an opinion letter covering the classification of independent contractors in today's gig economy. In recent years, the DOL has entered into agreements with many state agencies to cooperate in pursuing enforcement against misclassification of employees as contractors.

But contractor misclassification isn't the only type of misclassification on the enforcement radar. The FLSA also exempts certain employees from overtime pay. New rules went into effect on January 1, 2020, increasing the earnings threshold required to exempt many executive, administrative and professional employees from the FLSA minimum wage and overtime requirements. Firms can claim an exemption from overtime regulations for employees who are "bona

fide executive, administrative, professional and outside sales employees," if the employees meet certain conditions. Employers also must be aware of state tests, which may be more stringent.

MANAGE PAYROLL TAXES

Every employer must withhold Social Security, Medicare and income taxes from its employees' pay. Withheld Social



Security and Medicare taxes, along with the employer's Social Security tax contribution, generally are known as payroll (or FICA, for Federal Insurance Contributions Act) taxes.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act enables employers to delay payment of their share (6.2% of wages up to a wage base limit of \$137,700) of the Social Security payroll tax. They can pay the tax over the next two years, with the first half due by December 31, 2021, and the second half by December 31, 2022.

The Medicare tax rate is 1.45% each, with no wage base limit. Your firm also must withhold an additional 0.9% Medicare tax from employees whose wages are in excess of \$200,000 per calendar year. Only employees are subject to the additional Medicare tax, not employers. However, the Federal Unemployment Tax Act (FUTA) is your firm's responsibility. Employers must pay 6% of an employee's wages — up to the wage base limit

of \$7,000 — with a maximum credit of 5.4% for payments to state unemployment funds.

Failure to deposit any withheld taxes with the government on a timely basis can cause the IRS to hold your firm and other “responsible persons” personally liable for all outstanding amounts plus penalties and accrued interest. You must report FICA wages and withheld FICA and income taxes quarterly (using Form 941) and FUTA wages and taxes annually (using Form 940). State withholding and reporting obligations vary.

STAY INFORMED

While laws affecting payroll taxes and other employee compensation issues can change annually, the COVID-19 pandemic has resulted in even more legislation affecting payroll. Staying on top of the latest changes is more important than ever. Be sure to stay in touch with your financial advisor to ensure you're not missing anything. •

Making remote work ... work

This year has seen law firms temporarily shutter their offices and allow staff to work from home. Although many offices have reopened to some extent, some have shut down again due to COVID-19 infection rate surges. And more shutdowns could be needed, depending on what happens with the virus. Here are some issues that warrant attention.

TECHNOLOGICAL CAPABILITIES

As many firms learned the hard way when COVID-19 hit, it's one thing to work from home for a day or two on occasion, with professional co-workers and support staff available back in

the office. The situation is much more complicated when working remotely for a prolonged period, with your colleagues scattered about in their own homes.

It's essential that attorneys and support staff have sufficient equipment and technology to work efficiently away from the office. In addition to reliable devices with adequate capacity, they need communication tools (for example, Microsoft Teams, Slack and video-conferencing apps like Zoom), access to cloud storage and the ability to use digital signatures on vital documents. Of course, you also must ensure that strong cybersecurity measures that take ethical obligations into account are in place.



NEED FOR FLEXIBILITY

The right technology allows a firm operating remotely to be agile. But your firm also must be flexible enough to accommodate the unusual circumstances. Many remote workers won't be alone in their homes — they might have spouses, children and pets right there with them. Your management needs to accept that employees face competing pressures and may handle them in different ways.

Rather than focusing solely on the work to be done, consider ways to foster personal interactions.

Some experts suggest normalizing these new work environments to help colleagues better understand one another's circumstances. Participants on a video conference might, for example, give a quick virtual tour of their current working space and warn about potential distractions. It can help to know that someone is silent because he has muted his line to spare everyone the sound of his barking dog, not because he disagrees with a proposal.

TRAINING MATERIALS

You've probably noticed already that everyone adapts differently. Don't assume that brilliant legal minds will quickly or easily adapt to online meetings and messaging apps that they haven't customarily used on the job. You also don't want to learn about workers' struggles with certain applications or tools at the point when they need to use them.

Instead, provide easily accessible training materials, such as webinars, online tutorials and user

guides, in a centralized location. Consider making participation mandatory, with a way to "skip ahead" for those who are already proficient.

CULTURE MATTERS

While significant amounts of legal work can be done remotely, the practice of law still depends in some ways on a mentor and apprenticeship approach. Mentoring and face-to-face contact play an important role in nurturing talent at law firms.

Rather than focusing solely on the work to be done, consider ways to foster personal interactions. Don't count on impromptu contacts to do the trick. Instead, schedule regular video meetings that include the entire team. And slot in some time for personal updates (aka "water cooler talk").

KEEP AN EYE OUT

As the situation evolves, regularly review how remote work is working to identify gaps and potential problems that have cropped up. By making adjustments as you go along, you can continually improve the experience for attorneys, staff and clients. •

Law firm planning in a time of uncertainty

The COVID-19 pandemic and the resulting economic uncertainty, as well as social unrest, have created an economic tidal wave for which some law firms have found themselves unprepared. The resulting uncertainty makes it difficult, but not impossible, to plan.

TAKING ACTION

Here are some steps that can help.

Think tactically. During this tumultuous period, your long-term strategies might go out the window. You'll need to adopt tactics on the fly to deal with the shifting economy's effects on your clients and your own business. For example, you may be forced to decentralize planning, giving greater power farther down the ladder, particularly if some employees are let go. This way, practice groups, client teams and client relationship managers can respond promptly to client needs and unexpected opportunities for generating revenue.

Stay on top of the numbers. Arm yourself with up-to-date information on the firm's financial status, as well as the state of the legal market. This includes the firm's current cash position and budget performance year-to-date. You also need a strong grasp of the cash flow situation.

Track the market to identify practice areas and services in demand and those in decline, whether

just temporarily or likely for the long term. This information, along with your financial data, will empower you to make informed decisions.

Form a COVID-19 crisis management team.

If you haven't done so already, assign a dedicated crisis task force to monitor financials and other internal and external developments. The team should regularly meet to evaluate risks and opportunities. It also should monitor relevant government and health care guidance to ensure compliance. And it can seek out information from other geographic areas and industries to identify best practices for coping with the effects of this year's economic uncertainty on businesses.

If you haven't done so already, assign a dedicated crisis task force to stay on top of the financial numbers and other internal and external developments.

Update your business continuity plan. Another team can tackle your business continuity plan. It should review how your firm handled stay-at-home orders, school closures and other effects of the pandemic — in case they become necessary again.

Gather input from different firm levels and from clients about what worked and what didn't. As the team identifies gaps, it can formulate solutions that will allow you to improve future responses. (See the article "Making remote work ... work" on p. 5.)

SHORTEN YOUR TIME FRAMES

Planning typically is done in increments of one to five years. But the current environment calls for one- to three-month increments, with regular reviews and adjustments within those increments. •



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