

Time Recording & Time Costing

It is vital for the proper management of law practices that those who manage these practices should have the information to manage them effectively - each practice needs to know not only what it costs to run the practice but also what it costs to deal with each case, matter or transaction and the relationship of that cost to the chargeable fee. Practices also ought to know what non-fee earning work/time costs. Time recording and time costing are the best-known management tools to provide this information.

It is, however, important to be clear that time costing is different from fee charging, although the first can help the latter and with sophisticated time costing systems it is possible to build in figures which in many cases will produce a draft fee note. Fundamentally time costing is a system which endeavours to ascertain on some scientific basis what it costs a particular firm to do a specific job. It is basically a management tool.

Many solicitors have managed their firms - that is, taken certain policy decisions - on intuitive guesses; some people are good guessers or perhaps just lucky and some are not good guessers. It is much better to have some facts on which to make decisions about where the firm is going or how it should get there.

If it is known what a job has cost, it will be known whether the fee will produce a profit or a loss. If there is a loss it may be decided that the people doing the work have been inefficient, idle or so overworked that they are in a guddle; or that some of the work could be done just as well by an unqualified person at a lower salary and therefore at a lower cost; or it may be decided to try to expand work in one area or discourage it in another. Time costing will produce the factual framework for these decisions.

Work in progress is something which has in the past usually been ignored by those solicitors who accounted on a cash or fees rendered basis and was only calculated by those who had it in their accounts and then probably only so far as they needed to satisfy the Inland Revenue. The Finance Act 1998 changed the regulations for those firms operating on a cash basis and established that work in progress and debtors be brought into account for income tax purposes for the year commencing 1st October 1999. The Inland Revenue now requires work in progress to be valued on a "true and fair basis". These regulations will have far reaching consequences for firms who have never had to calculate work in progress for inclusion in their Profit and Loss Account.

Notwithstanding the introduction of the new regulations it has always been the case that without realistic work in progress figures from time to time as it is very difficult to know whether a firm is really growing or whether it may be contracting. A mere increase in fees rendered or cash received cannot of itself give a fair picture. For a full appreciation of a firm's financial position and of the parts of it, it is important to know the extent and value of the work in progress at least at the start and end of a financial year and preferably from month to month. Time costing can provide this information.

There may well be good reasons why some work should be done at a reduced fee or even at a loss - the firm may be spreading its bread on the waters! It is, however, important to know what the subsidy is. Time costing will tell this.

Before trying to define time costing it should be made clear that the handling of the time records and the time costing operation can be carried out manually or electronically - it is more laborious manually and because of labour costs it is unlikely that a manual system will be able to give the more sophisticated management information that will be available in a computerised system. With the cost of computers at an all time low and more time recording packages being available for lawyers, a computer system would be recommended. The time costing systems which are described do not require computers but the characteristics of what are described must be in any system that is installed.

Time recording

The basis of time costing is of course time recording. Without well kept and accurate records of the time spent on a matter the time cost cannot be fixed.

For time recording there are two basic essentials. The first is that there must be a means whereby the solicitor or other fee earner can record all the time spent on chargeable work for clients (although as mentioned later it is desirable for all time to be recorded). Normally he or she completes a form as he or she goes along, although there are on the market electronic methods of doing this. The form can be a daily time sheet or a weekly sheet. A daily time sheet is probably easier to keep and it is probably better to process solicitors' records on a daily basis.

The second essential is that the time recorded on the daily time sheet in respect of each matter should be transferred regularly to a time ledger for that matter so that at any point of time it can be ascertained how much time has been spent on that matter and by whom.

However, to make a time recording system work properly, there are a number of questions that have to be answered. For example:

1. What does one do with time that will not be chargeable?

All time, whether chargeable or not, should be recorded - basically because you are unlikely to record all your chargeable time properly unless you also record other time. It is also relevant to know how much time someone in an office is spending on administration, business development, that favourite charity, that Law Society committee, etc.

2. Who should keep time records?

All fee earners - that is, partners and members of the staff who perform legal work directly chargeable to specific clients - normally not typists, cashiers or receptionists, although a good secretary or personal assistant might well be operating in such a way that some of his or her time would be chargeable and therefore he or she should record his or her time.

3. What should be the unit of recorded time?

In other words, is time to be recorded in units of 1 minute, 6 minutes or half an hour? The nature of the lawyer's practice is such that he or she tends to deal with a large number of different items for different clients in the course of a day and therefore the shorter the minimum period is, the better. Six minutes is generally adopted. Experience has shown that if a letter has to be done by a fee earner the minimum time taken is probably about six minutes if there is included, for example, time spent reading the letter to be replied to, thinking time, dictating time and eventually reading and signing time.

4. Should a record be kept of what has been done in the time?

It is not essential for time costing as such but a record of what has been done in chargeable time is almost essential. This can be done simply by a series of activity codes such as L for letter, A for attendance at a meeting, IT for incoming telephone call, R for research, RD for revising or a drafts, etc. or a similar numeric code. It may also be desirable to record what was said or agreed on the telephone or at a meeting, but that will probably best be recorded separately and placed on the file - although there are systems which enable both to be done.

5. How do you identify matters?

It is probably best to have an integrated filing, time recording and financial accounting system so that each matter has a unique number used at every point. Provided there is a handy list of the numbers for the various client matters being dealt with it is easy to identify the client matter for the daily time sheet by its number which can be either alpha-numeric or simply numeric - if not, a description of the matter may be sufficient.

6. Is time spent on researching the law recorded?

Yes, provided it is necessary and relevant. It is of course a fallacy that solicitors know all the law, and anyway the purpose of the exercise is to find out the cost of carrying out a particular piece of work and if that involves time poring over books, etc., record it.

7. Does it take long to keep time records?

The answer must be "no" provided that a well-planned system has been set up which cuts to a minimum the extent of the entries which have to be made by the fee earners. Time recording requires discipline, and like all discipline it is initially painful, but a well-planned system makes the acquiring of the discipline easier. The real secret of keeping good time records is to record as one goes along but also to spend about two minutes four times a day at equally spaced intervals balancing the books so that, for example, at about 10.30 the time so far recorded is checked, any shortfall is remembered and the details are recorded. The same exercise should be done before lunch, in the middle of the afternoon and at the end of the day.

Experience shows that this is the only way to do it properly. In other words, if it is done as matters are dealt with throughout the day and these periodic checks are made, the time taken by a fee earner is minimal. The time recorded will of course have to be processed either manually or by being put into a computer, but this is not fee earner time.

8. How is time outside normal office hours dealt with?

It must all be recorded against specific client matters as the object is to record all the time spent on a matter whenever it may have been done. It may be desirable to have some method of recording that the work was done in unsocial hours, but work done over a weekend because a client specially required it should be differentiated from work done then because part of the previous week was spent sick in bed or on the golf course and there was a need to catch up or possibly because the fee earner is a workaholic. It is really only when the fee is being charged that it will be appropriate to reflect that certain work was done at the instigation of the client outside normal office hours and it is probably only such work that is done in "overtime".

There are of course other questions, but the important thing is for each firm to work out its own answers so that there is a consistency of approach and everyone within the firm records their time on the same basis.

Time costing

As has been indicated, time costing is the process which converts the time which has been recorded against a particular matter into pounds and pence so that when it is known that there has been spent, say, 6¼ hours on a court case or 14½ hours on a complicated transaction it is known that the cost of the court case is £631 and the cost of the complicated transaction is £1465.

Again there are a number of ways of going about this - one way is set out in the English Law Society booklet entitled "The Expense of Time". What should be aimed at is to arrive at an hourly cost rate (HCR) in pounds for each fee earner in the office which, if applied to the chargeable hours recorded over a year, will produce an annual gross income equivalent to the cost of running the practice.

Whatever formula is used there should be worked out on a realistic basis (1) an estimate of the firm's expenses in the coming year, i.e. the costs of books, cleaning, electricity, insurance, rates, rent, telephones, posts, photocopying, etc., and salaries and (2) how many hours are worked by each fee earner in the year, or more importantly the number of hours spent working for clients (i.e. chargeable or productive time).

The realistic assessment of the firm's expenditure is really the preparation of a careful budget taking into account expected increases in certain costs during the year ahead. If there is a good time recording system the number of hours spent by each of the fee earners on work for clients will be known, but if there is not such a system, as a guide 1,000 hours for a partner and 1,250 hours for a qualified assistant might be adopted - but a partner heavily involved in office administration will probably not be able to produce 1,000 chargeable hours.

If one looks at a three-partner firm with two qualified assistants, three unqualified assistants and one trainee and say that the budget expenditure for 2001 is £490,000 including fee earners' salaries of £87,000 but not any payment to partners. There is some argument about how partners' income should be dealt with in the formula. Some people say that as it is a costing exercise that is being done, partners should be given a notional salary equivalent to that of a well-paid assistant and add an appropriate amount to cover pension purchase and interest on working capital. Some differentiate between different categories of partner reflecting experience or expertise or speciality. Others say that the notional salary should be the minimum return the partner expects to receive at the end of the year. Some argue that in fixing budget figures the target income for partners should be taken but that in working out the formula a sum equivalent to an assistant's salary should be taken as a notional salary for a partner. Some of these approaches are not consistent with a costing operation and can lead to confusion.

However, for this example it would not be inappropriate to take a figure of £40,000 for each partner for both budget income and notional salary (including pension provision and interest on working capital) - a total of £120,000. This makes the minimum gross fee income required to cover expenditure (including partner income) £610,000.

The essential information is now available to put in the formula to calculate the hourly cost rate for each partner, qualified assistant, unqualified assistant and trainee ie. the estimated expenditure, the chargeable hours and the actual or notional salaries.

The simplest formula would simply be to divide the total expenditure, £610,000, by the sum of the chargeable hours for all the fee earners. If the total chargeable hours amount to 10,150 the hourly cost rate is £60.10 for each fee earner, but this does not reflect the different salaries paid to each fee earner and fixes the cost for the trainee at the same as the partner. It is therefore normal to calculate hourly cost rates taking into account the different actual or notional salaries. The formula can be structured to relate the total expenditure to each fee earner either according to his chargeable hours and actual or notional salary or partly on that basis and partly on a per capita basis. The latter probably produces more realistic figures.

The formula below calculates hourly cost rates partly per capita and partly according to salary (actual or notional). On this basis and using the above figures the partner rate rounded off is £101.00 per hour, the first qualified assistant is £54.00 etc. With its time recording system and these figures the three-partner firm can calculate what it has cost them to do any particular piece of work. They should also be able to ascertain at each stage how much the work has so far cost.

Calculation of hourly cost rates (HCR), 2001

Budgeted expenditure, 2001

Fee earners' salaries	£ 87,000	
Other expenditure	<u>403,000</u>	(x)(½ x = £201,500)
	£490,000	

Notional salaries, etc £120,000
 Total expenditure £610,000 Total salaries £207,000 (S)

Calculation

	Hrs HCR	Salary (s) (1)	Total $\frac{1}{2} \times \div 9$ (2)	$\frac{1}{2} \times \div S/s$ (3)	Cost (1)+(2)+(3)	£
Mr D	1,000	40,000	22,389	38,937	101,326	101
Mr B	1,000	40,000	22,389	38,937	101,326	101
Mr L	1,000	40,000	22,389	38,937	101,326	101
Q A 1	1,250	23,000	22,389	22,389	67,778	54
Q A 2	1,250	17,500	22,389	17,033	56,922	46
U A 1	1,250	13,500	22,389	13,144	49,033	39
U A 2	1,250	11,600	22,389	11,295	45,284	36
U A 3	1,250	11,400	22,389	11,096	44,885	36
<u>Tr</u>	<u>900</u>	<u>10,000</u>	<u>22,388</u>	<u>9,734</u>	<u>42,123</u>	<u>47</u>
<u>9</u>	<u>10,150</u>	<u>207,000</u>	<u>201,500</u>	<u>201,500</u>	<u>610,000</u>	

Inevitably there are a number of variations that can be introduced into the calculations - some arising from differences in philosophy and some being fine tuning to produce more accurate costs. It will be noted that the number of chargeable hours used is a major factor in the resultant HCR. If for example the trainee produced 1100 chargeable hours the HCR would be £38.

It should be remembered, however, that each firm's hourly cost rates are unique to it and indeed the hourly cost rate for each fee earner is unique to him or her. This does not mean, however, that one would not expect to find similarities in rates among firms similar in size, location and methods of operating.

As has been said the hourly cost rate if applied to the chargeable hours should produce a gross fee income equivalent to the budget costs/expenditure according to how this has been defined. But this may not be the result. There are certain premises underlying the theory.

The result will be attained only if:

1. There is sufficient volume of business.
2. The firm is able to charge and recover the full value of the chargeable hours.
3. The costs are contained within the budget figures.
4. The expected chargeable hours for fee earners are in fact worked.
5. The partners render fees promptly and are diligent in recovering them.

As the time cost is normally only part of a fee charged, the total gross fee income of a firm should be greater than the product of the total rates.

It is, however, a management function to monitor all these matters and a good time costing system will help a firm do this. Where appropriate a firm may have to adjust its figures to reflect changes in chargeable hours, expenditure, cash flow, etc. Indeed a firm should re-calculate its hourly cost rates if there is any significant change in any of the costs or other variables in the formula

Points to remember

- Time costing is a system to ascertain what it costs a particular firm to do a specific job.
- Time costing will almost certainly produce a different result in each firm. Do not assume that another firm's figures can be applied.
- Do not install a Rolls Royce system when a Ford one will do.
- Re-allocate work where costs incurred are excessive.
- Maintain a realistic valuation of work in progress.
- Maintain accurate records of all time spent by fee earning staff.
- Define who should keep time records and what the unit of time should be.
- Define the firm policy so as to ensure consistency in the recording of time by fee earners.
- Time costing and time recording are management tools but they do give guidance when calculating fees.